GCC Illicit Tobacco Indicator 2017

Prepared by Oxford Economics
November 2018



OXFORD ECONOMICS

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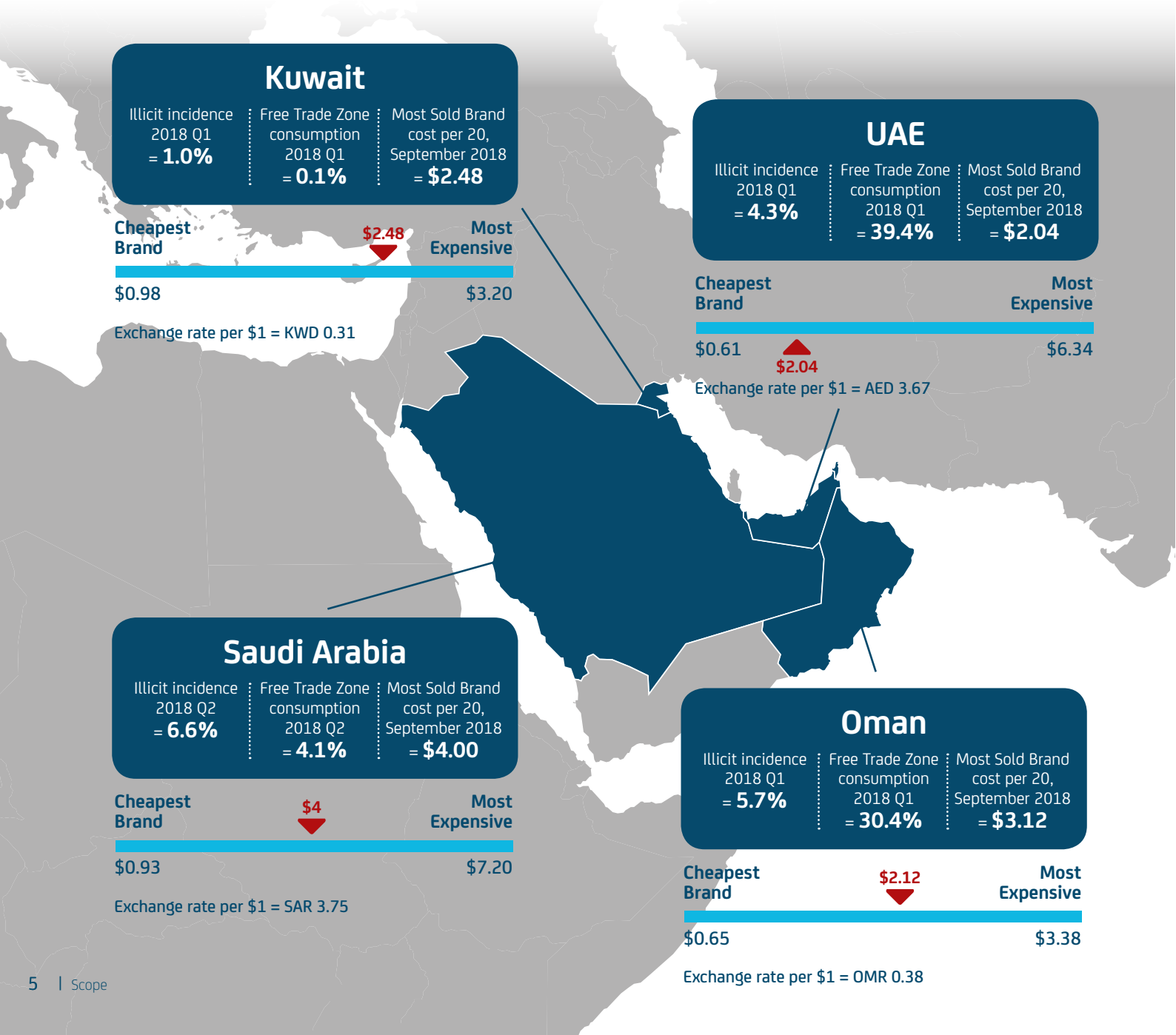
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Scope

This Report provides an overview of the nature of the illicit trade of cigarettes across four GCC economies, namely Saudi Arabia, the United Arab Emirates (UAE), Kuwait, and Oman. It establishes estimates of consumption of illicit cigarettes and the impact this has on tobacco tax revenue. To this end, the purpose of this Report is to:

- Validate Illicit Incidence levels, reviewing and refining estimates using available sources such as Empty Pack Surveys.
- Estimate the volume of Illicit Consumption, including where possible a breakdown by Market Variant.
- Estimate annual government Tax Loss from indirect taxes on cigarettes including Customs Duty, Excise Tax, and VAT as applicable.

Our study makes use of the latest available data, including full-year estimates for cigarette consumption and sales up to 2017, as well as Empty Pack Surveys up to 2018 Q2. We are therefore able to present full-year estimates up to and including 2017 for metrics such as Total Consumption, Legal Domestic Sales, Tax Revenues, and Tax Loss. We also provide an indication of how Illicit Consumption evolved in 2018 following changes to taxation on cigarettes in UAE and Saudi Arabia last year.



Glossary of Terms

BAT British American Tobacco.

bn Billion.

Bootlegging Small-scale Contraband.

CIF Cost, Insurance, and Freight.

Contraband (CB) Genuine product that has been bought in a low-tax market and which exceeds the legal border limits, or is acquired without payment of taxes for export purposes to be illegally re-sold (for financial profit) in a higher-priced market. There are generally two types of Contraband: Bootlegging and Wholesale Smuggling.

Counterfeit (CF) Cigarettes that are illegally manufactured and sold without permission of the trademark rights holder.

CPI Consumer Price Index.

Customs Duty Duty payable when a good enters a country from overseas.

Domestic Illicit Cigarettes that are legally produced by trademark rights holder to be illegally sold and consumed in the same market.

Duty-Free (DF) Purchases made outside the domestic market that have no state, local, or provincial taxes, import duties, or any other type of taxation added, and are subject to purchase volume restrictions.

Earmarked Tax Taxes whose revenues are reserved for a specific group or use.

EPS Empty Pack Surveys. Independent research agencies collect empty cigarette packs discarded by smokers in public places and record brands and Market Variants.

Excise Tax An indirect tax on the consumption of certain goods. Excise Taxes on cigarettes can be either specific, i.e. expressed as a monetary amount per quantity/weight of the product; ad-valorem, i.e. expressed as a proportion of the value of a product; or a combination of both. For the purpose of this Report, Earmarked Taxes levied on cigarettes are also considered as an Excise Tax.

FCTC The WHO Framework Convention on Tobacco Control.

Free-Trade Zone (FTZ) UAE FTZ such as Jebel Ali, Fujairah, Ajman and Ras al Khaimah where cigarettes can be legally produced. Cigarettes entering the UAE or any other GCC country from the FTZ are liable for all applicable taxes.

FOB Free on Board.

GCC Gulf Cooperation Council.

Illicit Consumption Consumption of Non-Domestic Illicit (Counterfeit, Contraband, and Non-Domestic with Unspecified Market Variant cigarettes) and Domestic Illicit cigarettes or loose tobacco. Typically, taxes applicable in the market where illicit cigarettes/tobacco are consumed are not paid.

Illicit Whites Cigarettes that are usually produced legally in one market, primarily for smuggling. While they may also be exported legally from some countries, they are smuggled across borders during their transit to the final market of sale where they have no legal distribution and are sold without payment of tax.

IMS In-Market Sales. Primary source of Legal Domestic Sales volumes.

Inflows/Outflows Inflows of Non-Domestic product into a market/Outflows of product from a market.

IT Illicit Trade Model developed for this Report to estimate Illicit Consumption in markets and trade flows between the 4 markets included in this Report.

JTI Japan Tobacco International.

JT Japan Tobacco.

LDC Legal Domestic Consumption is defined as Legal Domestic Sales net of Outflows.

LDS Legal Domestic Sales of genuine domestic tax-paid product through legitimate, domestic channels.

Market Variant Term used to designate the market in which a pack of cigarettes was initially intended to be sold. To be sold in a given market, a pack has to bear the required labelling (e.g., health warning) and potentially a tax stamp or a banderol. The EPS methodology (or, e.g., that of pack swap surveys) estimates the incidence of packs by Market Variant. As such, packs that do not bear the health warning and/or stamp required in the given market are considered Non-Domestic.

Most Sold Brand (MSB) Cigarette brand variant with the largest annual Legal Domestic Sales volume in a given market.

mn Million.

Non-Domestic Illicit Counterfeit, Contraband, and imports of other illicit cigarettes.

ND Non-Domestic – product that was not originally intended for the market in which it is consumed.

NDL Non-Domestic Legal – product that is brought into the market legally by consumers, such as during a cross-border trip.

OE Oxford Economics.

OE Tourism Model A comprehensive data set of tourism metrics covering 190 countries and 20 years of detailed historical data.

OECD The Organisation for Economic Co-operation and Development.

PM Philip Morris International.

pp Percentage points.

Smoking Prevalence The percentage of smokers in the total adult population.

Tax Loss Government revenues that are lost due to tobacco tax (Excise Tax, including Earmarked Taxes and VAT/GST/sales tax) that is not paid on illicit cigarettes. Import duties were not considered in the Tax Loss estimates.

Total Consumption Total Consumption of legal and illicit cigarettes in a market or Asia-16 markets.

UN The United Nations.

Unspecified Market Variant Unspecified Market Variant refers to cigarette packs that do not bear specific market labelling or Duty-Free labelling. The intended market is not known.

UNWTO The World Tourism Organisation.

VAT Value-Added Tax.

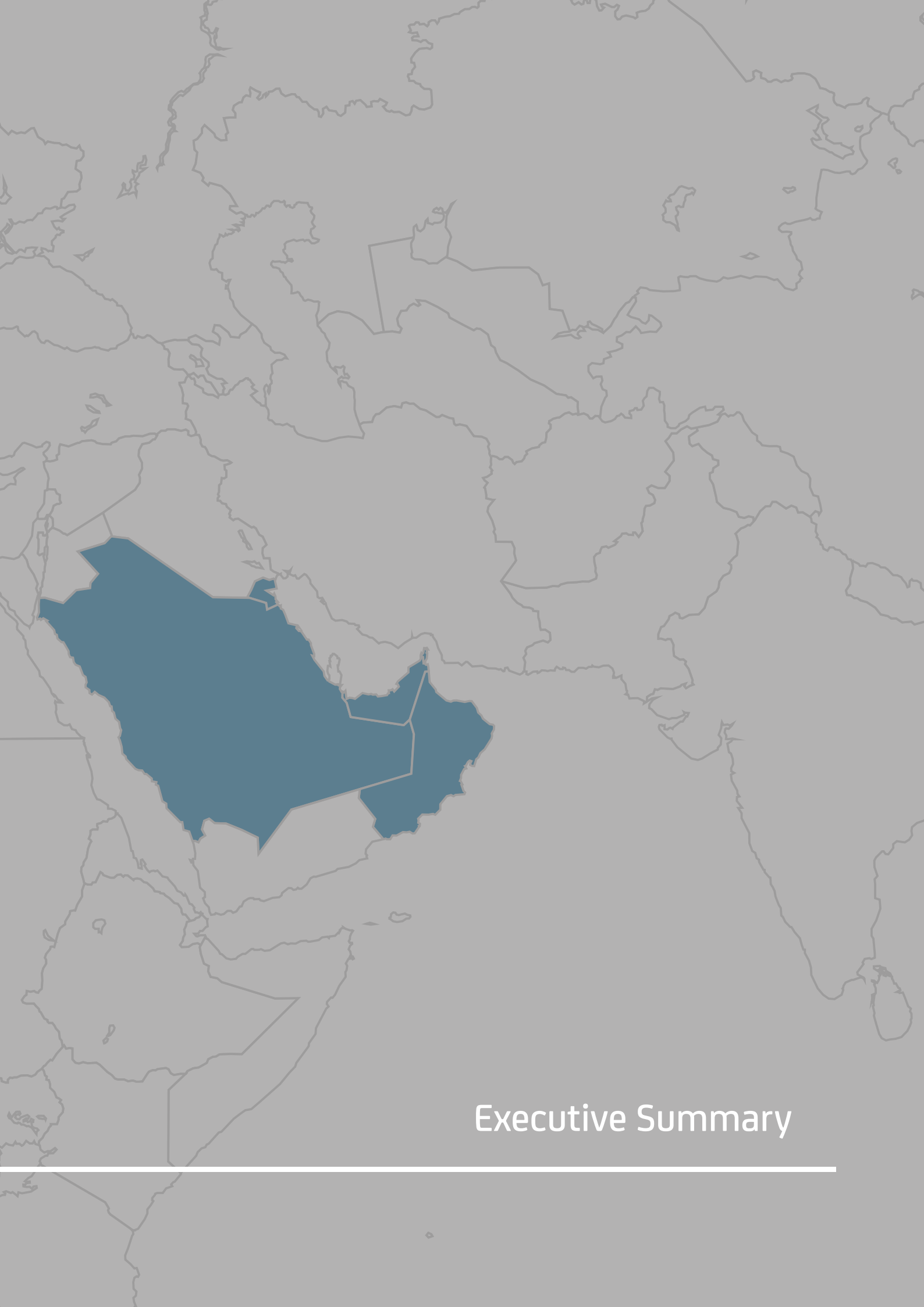
WHO World Health Organisation.

Methodology

Oxford Economics developed an Illicit Trade (IT) Flows Model to estimate the size of Illicit Consumption and trade flows in Kuwait, Oman, Saudi Arabia, and United Arab Emirates (UAE). A summary of the methodology is provided below[1]:

- Data on Legal Domestic Sales were provided to us by PMI for the purposes of analysis.
- Where necessary, background checks were made on manufacturers to assess whether they were located in Free Trade Zones in the UAE or outside of the GCC (and if so, in which country). This primarily consisted of internet-based research to identify the location of production facilities according to the manufacturers' own websites.
- Cigarettes manufactured in the UAE Free Trade Zones are considered as a separate category from Legal Domestic Sales or Illicit. Within the Legal Domestic Sales dataset, we have excluded brands manufactured in the UAE Free Trade Zones to avoid double-counting. This yields estimates of Legal Domestic Sales in line with other organisations.[2]
- We adjusted for Outflows of Legal Domestic Sales based on Empty Pack Surveys[3] to give a measure of Legal Domestic Consumption.
- A variety of sources, which included Empty Pack Surveys and additional corroboration by other studies, were combined to establish robust estimates of the incidence and size of Non-Domestic Inflows, to give a measure of Total Consumption.
- The Empty Pack Surveys provided a breakdown of the Inflows by Market Variant so that these could be matched against the Outflows data. The IT Flows Model was then "iterated" to ensure consistency between Inflows and Outflows by market, leading to refinement of the estimates of incidence and volume of Inflows. More details on the Empty Pack Survey methodology is provided in the country specific reports and the annex.
- Information from surveys and estimates of Non-Domestic Legal flows based on passenger data, average length of stay of inbound visitors, smoking prevalence, and average consumption per day by visiting smokers, were then used to identify illicit Inflows (i.e., Counterfeit, Contraband, and Non-Domestic Illicit with Unspecified Market Variant, also known as "Illicit Whites").
- Cigarette prices, duty and tax structures for cigarettes, and the actual rates applied in each applicable year were used to estimate the Tax Loss associated with the consumption of illicit cigarettes in each market for 2015-2017. No data on the value of revenues from tobacco tax or duties were publicly-available from official sources for this study, so data presented for historical years are estimated using Legal Domestic Sales and applicable taxes.
- Tax revenue has been calculated based on the Weighted Average Price (WAP) of cigarettes consumed in the market for each year, based on the calculated market share of certain price brackets in 2018. Tax yields have been adjusted to take into account any and all mid-year tax changes, weighting the annual yield accordingly.
- Throughout this Report, figures presented in tables and charts may not add up due to rounding.

[1]A more detailed methodology is available from our Asia Illicit Tobacco Indicator Methodological Overview Report, available via http://illicittobacco.oxfordeconomics.com/methodology/.
[2]See for example Tobacco in Saudi Arabia, Tobacco in Oman, Tobacco in UAE, Tobacco in Kuwait all by Euromonitor 2017.
[3]Conducted by independent research companies and commissioned by PM or jointly by several tobacco manufacturers.



Executive Summary

Executive Summary: Total Consumption

Aggregated Legal Domestic Sales (LDS) across the four markets in this study (Kuwait, Oman, Saudi Arabia and UAE) increased year-on-year between 2009 and 2015. However, since peaking in 2015, LDS declined year-on-year in both 2016 and 2017.

In 2016, GCC members agreed to implement 100% excise tax on tobacco products using the pre-tax change Retail Selling Price (RSP). This was implemented in Saudi Arabia in June 2017, UAE in October 2017 and Bahrain in December 2017. Preparations are underway in Kuwait and Oman, but there is no date for implementation as yet.

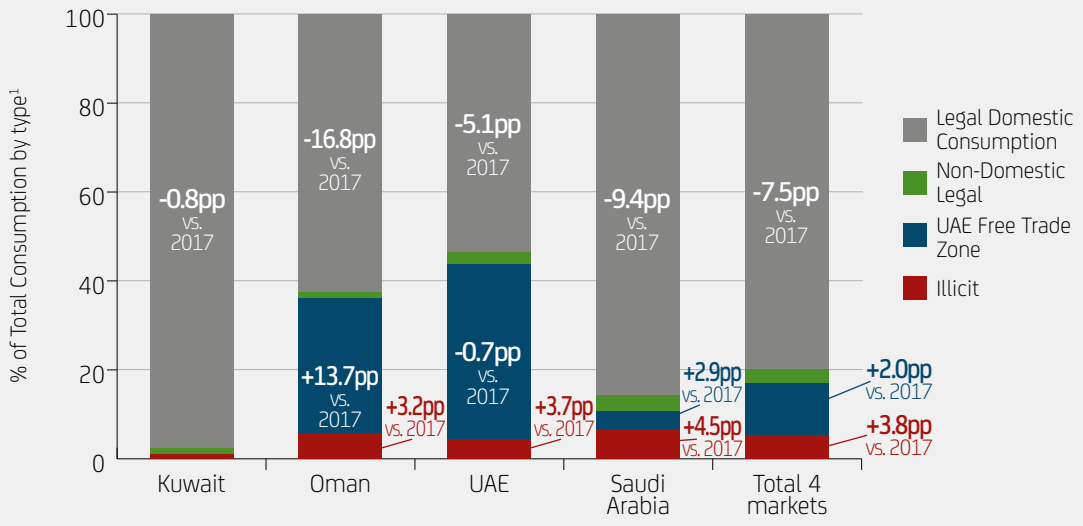
Illicit incidence across our four markets has increased in recent years – having been just 1.2% of Total Consumption in 2016, the Illicit Incidence rose to 1.6% of Total Consumption in 2017 and to 5.3% in the first half of 2018. Over the same period, cigarettes produced in the UAE Free Trade Zones rose from 8.9% of Total Consumption in 2016 to 11.8% of Total Consumption in the first half of 2018 (and was just below 40% in UAE).

Total Consumption (Legal and Illicit) across the four markets included in this report was an estimated 44.1 billion cigarettes in 2017. This is 10.2% lower than in 2016, when Total Consumption was estimated to be 49.1 billion. Total Consumption in 2017 consisted of:

- **Legal Domestic Consumption** – after adjusting the volume of Legal Domestic Sales for outflows of cigarettes to other markets included in this report, Legal Domestic Consumption amounted to an estimated **38.5 billion cigarettes** in 2017 or **87.3%** of Total Consumption.
- **Non-Domestic Legal** – Consumption of Non-Domestic Legal cigarettes amounted to **611 million cigarettes** (**1.4%** of Total Consumption). This was 275 million cigarettes higher than in 2016.
- **Cigarettes produced in UAE Free Trade Zones** – accounted for an estimated 11.8% of Total Consumption in 2018, an increase of 2 percentage points from 2017 when **4.3 billion cigarettes** or **9.8%** of Total Consumption were produced in the UAE Free Trade Zones. We classify these cigarettes separately from Legal Domestic Sales, Legal Domestic Consumption, Non Domestic Legal, and Illicit Consumption, because available evidence on retail selling prices suggests these cigarettes retail at or very close to the theoretical minimal tax level. Since these cigarettes must also have a cost of production and distribution, it is difficult to assess how these cigarettes are complying with all applicable taxes.
- **Illicit Consumption** – 5.3% of Total Consumption was estimated to have been illicit in the first half of 2018, up from **1.6%** of Total Consumption, or **695 million cigarettes**, in 2017. This is up from 568 million cigarettes and 1.2% of Total Consumption in 2016. Illicit Consumption consists entirely of Non-Domestic Illicit cigarettes.

Composition of Total Consumption, 2018

Percentage of Total Consumption by type[1]



Source: Oxford Economics

[1]For Total 4 markets the 2018 values have been obtained using the 2017 data for Total Consumption, as full year data for 2018 is unavailable.

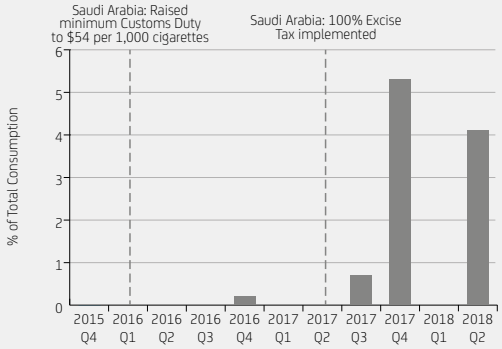
Executive Summary: Free Trade Zones

- The manufacture of cigarettes is not allowed in the GCC, with the exception of UAE Free Trade Zones such as those in Jebel Ali, Fujairah, Ajman, and Ras al Khaimah. If these cigarettes enter the UAE, customs duty (at a rate of 100% cost including insurance and freight, subject to a minimum $27 per 1000 cigarettes), excise duty (at a rate of 100% of the cost including customs duty), and VAT (as of 1 January 2018) should be levied.
- Minimum customs duty on cigarettes imported into UAE is $27/AED 100 per 1000 cigarettes or $0.54/AED 2 per pack of 20 cigarettes, and with 100% excise tax applied, the minimum theoretical tax burden rises to $1.08/AED 4 per pack of 20 cigarettes (excluding VAT). This excludes any cost of production or cost of goods. This is the same as the price charged for some cigarettes manufactured in the FTZ[1] and raises the question of whether all cigarettes produced in the FTZ have customs duty paid upon entering the UAE (and by extension, other GCC markets).
  Tax stamps are not affixed to packs of cigarettes in the GCC and therefore there is not an easy way to determine if applicable taxes have been paid.
- A detailed assessment of whether the cigarettes produced in the FTZ find their way into GCC countries by illicit means is beyond the scope of this study. However, research conducted by the International Chamber of Commerce group Business Action to Stop Counterfeiting and Piracy (BASCAP)[2] noted that in the global illicit trade in tobacco "almost all of the top starting and transit points host free trade zones". Meanwhile research from Passport[3] finds "The centres of illicit trade in [UAE] are the numerous free zones, and especially the Jebel Ali free zone in Dubai".
- Although Empty Pack Survey (EPS) data does not allow us to assess whether duty is paid on FTZ cigarettes when they enter the UAE or other markets (as none of the markets in this report operate a tax stamp system for cigarettes) it does enable us to track the presence of FTZ-manufactured brands in the markets in our study.
    - We find these brands accounted for 9.7% of total consumption in the four markets in 2017, up from 8.9% in 2016. Sales of these brands rose further to 11.8% of Total Consumption in 2018 so far (weighted using 2017 Total Consumption, and shares of FTZ cigarettes from EPS covering 2018 Q1 for Oman, UAE and Kuwait, 2018 Q2 for Saudi Arabia).
    - The share of these brands is highest in UAE, where according to the 2018 Q1 EPS FTZ cigarettes accounted for 39.4% of consumption in 2018 Q1. In Saudi Arabia, which alongside the UAE implemented the excise tax, the share of FTZ cigarettes in Total Consumption was 4.1% in 2018 Q2 having been 0.2% of the market in 2016.
    - Taken together, Illicit Consumption and UAE FTZ cigarettes account for 11.3% of the market in 2017, up from 10% in 2016.
- Timely data on government revenues from tobacco taxes are not publicly available for the markets covered in our report. Such data might provide additional useful evidence on the incidence of illicit tobacco. Given the uncertainty over what proportion of FTZ cigarettes are tax-paid, we presented expected tax revenues on FTZ cigarettes in each market. This is presented alongside expected tax revenues on Legal Domestic Sales, and estimated tax losses to Illicit Consumption.

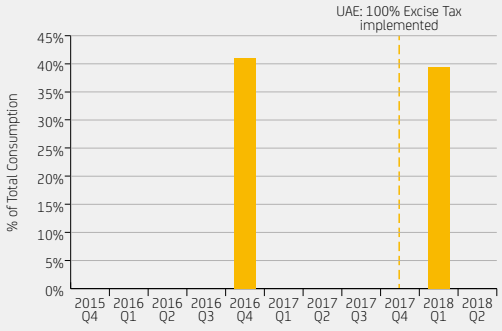
[1]See price list published at http://whatson.ae/dubai/2017/10/list-products-affected-excise-tax-leaked-huge/
[2]The Illicit Trade in Tobacco Products and How to Tackle It, BASCAP, 2012
[3]Illicit Trade in Tobacco Products, Passport International, February 2018

Executive Summary: Free Trade Zones

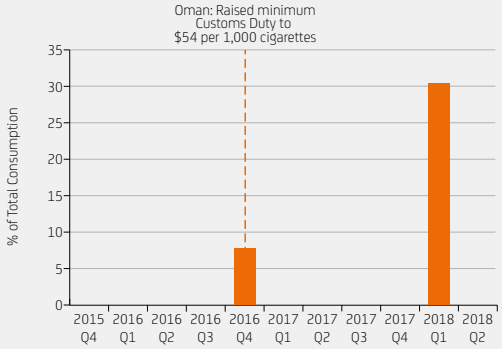
Saudi Arabia: FTZ share Total Consumption according to EPS by date[1]



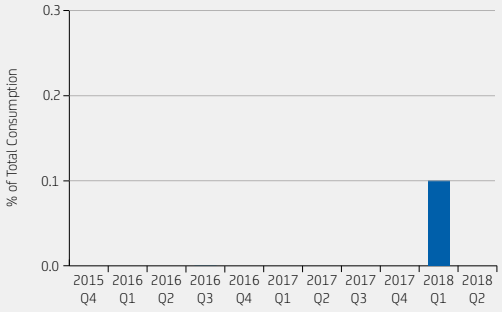
UAE: FTZ share Total Consumption according to EPS by date[1]



Oman: FTZ share Total Consumption according to EPS by date[1]



Kuwait: FTZ share Total Consumption according to EPS by date[1]



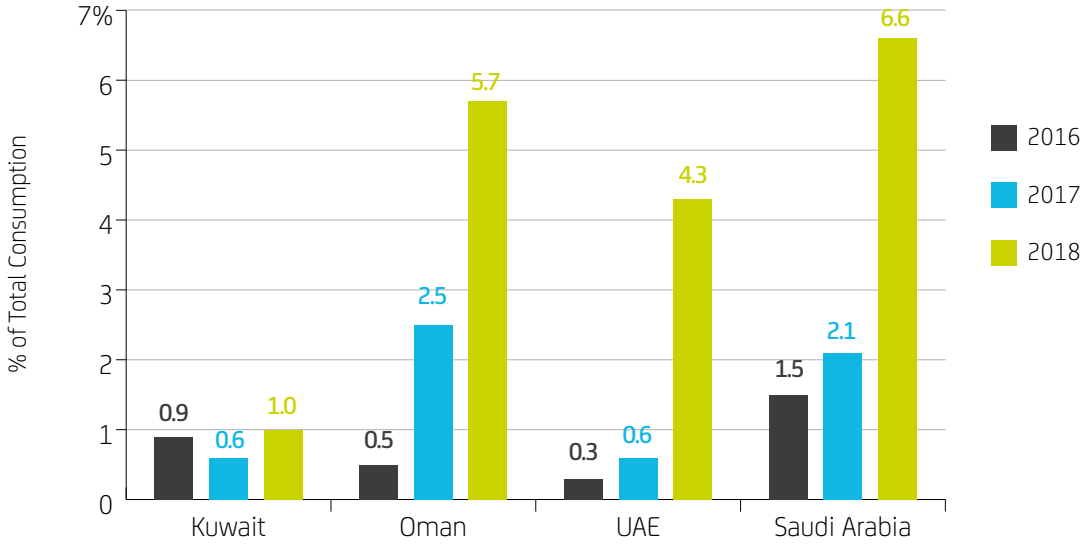
Source: Oxford Economics/Haver Analytics

[1]2018 data refers to 2018 Q1 for Kuwait, Oman and UAE, and 2018 Q2 for Saudi Arabia

Executive Summary:
Illicit share of Total Consumption

- Total Consumption of Illicit cigarettes in Kuwait, Oman, Saudi Arabia and UAE in 2017 is estimated at 695 million. This accounts for 1.6% of Total Consumption. Illicit Consumption has risen from 568 million (1.2% of Total Consumption) in 2016.
- A significant and rising share of Total Consumption across the GCC markets in this study are accounted for by FTZ-manufactured cigarettes. This category accounted for 9.7% of Total Consumption in the four markets in this report in 2017.
- As of 2018 H1, Illicit incidence ranges from a low of 1% in Kuwait (where the tax increase has been put before parliament but not yet approved) to a high of 6.6% in Saudi Arabia. This compares to a range of 0.6%-2.5% in 2017 and 0.3%-1.5% in 2016. The share of Illicit cigarettes in Total Consumption is estimated to have risen in 2018 Q1 in all four markets.
- In Saudi Arabia, where our estimate for 2018 suggests the Illicit share was highest amongst our four markets, cigarettes from Pakistan accounted for the greatest proportion of Illicit inflows, at 280 million cigarettes or 1% of Total Consumption in 2017. Pakistan was also the largest source of Illicit cigarettes across the four GCC markets in this study during 2017, accounting for 0.7% of Total Consumption.

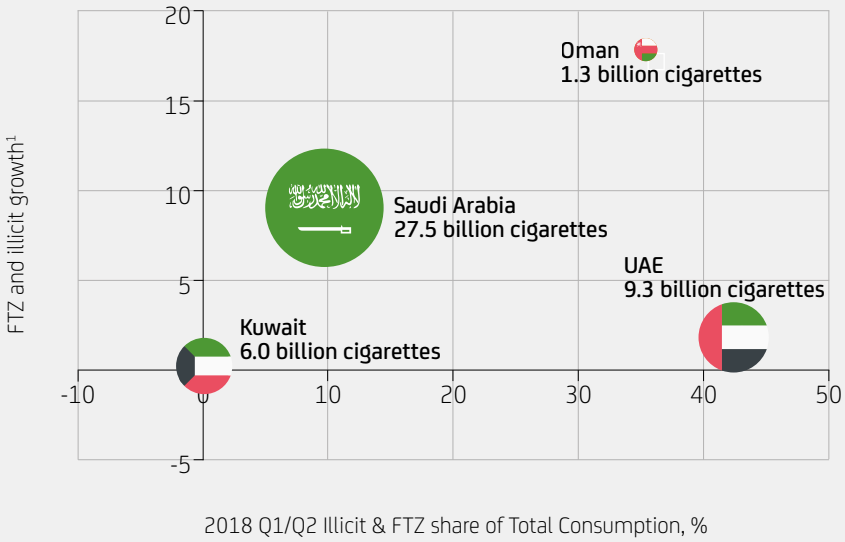
Illicit share of Total Consumption



Source: Oxford Economics
[1]2018 data refers to 2018 Q1 for Kuwait, Oman and UAE, and 2018 Q2 for Saudi Arabia

Market size and Illicit & FTZ share, 2018

Size of bubble indicates volume of Total Consumption in market in 2017



Source: Oxford Economics

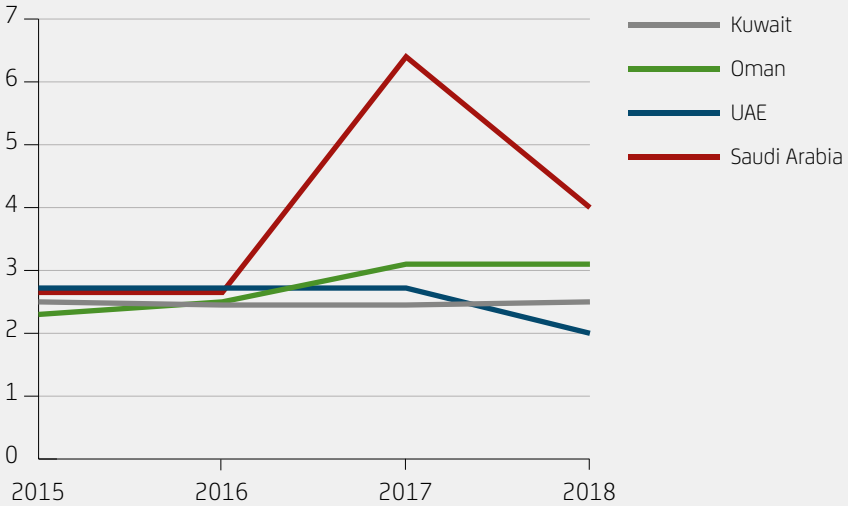
[1]Vertical axis refers to 20181Q1/Q2 P.P change vs. 2017 estimate

Executive Summary: Government Finances

- Tobacco taxation in the four GCC countries covered by this report is moving from a unified 100% CIF customs duty with a minimum specific duty at varying rates, to a more varied system incorporating per-cigarette customs duty at differing rates, ad-valorem tobacco-specific excise taxes, and Value-Added Tax (VAT) applicable to all goods and services (with exemptions).
- Key stages in the development of taxation on cigarettes are:
    - In 2002, GCC countries agreed to implement 100% customs duty on imported tobacco, with a minimum yield of $27 per 1000 cigarettes. This remained harmonized across GCC until 2015. However, each country has discretion to increase this minimum, and in 2016 Saudi Arabia and Oman raised it to $54 per 1000 cigarettes.
    - In 2016, GCC members agreed to implement 100% excise tax on tobacco products using the Retail Selling Price (RSP). This was implemented in Saudi Arabia in June 2017, and UAE in October. Preparations are underway in Kuwait and Oman, but there is no date for implementation as yet.
    - In 2017, GCC countries agreed to implement a 5% VAT on all goods and services (with national discretion over exemptions). The VAT was implemented in Saudi Arabia and UAE on 1 January 2018, with other GCC countries expected to follow suit in the years ahead.
- There is no publicly-available data for tobacco tax revenues in the four countries in our study. We have therefore estimated tax liabilities based on estimates of Legal Domestic Sales, sales of cigarettes produced in the UAE FTZ and the country-specific tax structure. Our estimate for total expected revenues from Legal Domestic Sales cigarettes in 2017 across the four countries in our study is USD 3.5 billion, up from USD 2.1 billion in 2016. Given that aggregate LDS fell 1.8% in 2017, the growth in expected revenues is entirely down to changes in tax structure.
- Our estimate for Tax Losses in 2017 to Illicit Consumption is USD 69.8 million, up from USD 27.7 million in 2016. This accounts for 1.8% of the potential revenues from taxation on cigarettes, up from 1.2% in 2016.
- The share of FTZ cigarettes in the four countries in our study is 9.7% in 2017, compared to 1.6% for Illicit Consumption.

Most popular pricing point in each market[1]

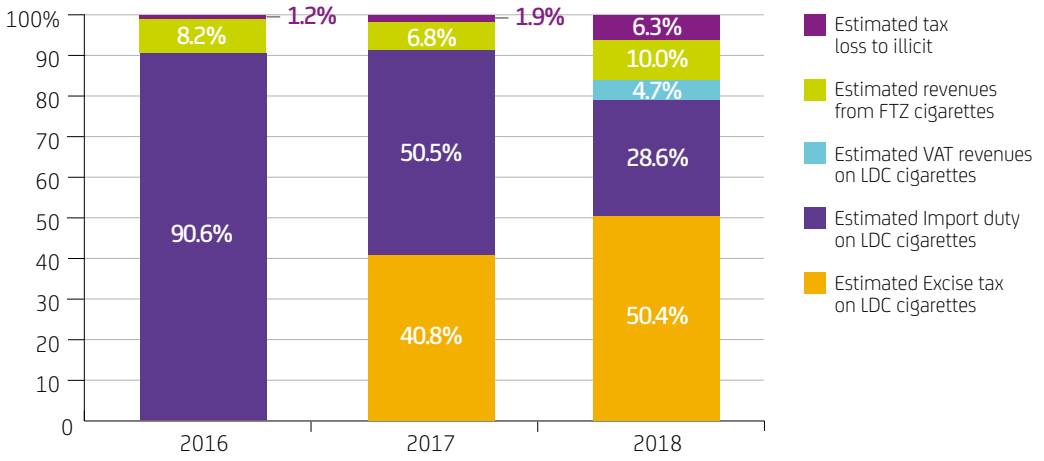
RSP $ per pack of 20



Source: Oxford Economics

[1]Price in January of each year, brand can change year-to-year

GCC: Composition of Total Potential Tobacco Tax Revenues[2]



Source: Oxford Economics

[2]Tax revenue has been estimated based on the Weighted Average Price (WAP) of cigarettes consumed in the market for each year, based on the calculated market share of certain price brackets in 2018. Tax yields have been adjusted to take into account any and all mid-year tax changes, weighting the annual yield accordingly.



Dashboard

Executive Summary: Dashboard

% Total Consumption unless otherwise stated	GCC 4 Markets	Saudi Arabia			United Arab Emirates			Oman			Kuwait		
	2017	2016	2017	2018 Q2	2016	2017	2018 Q1	2016	2017	2018 Q1	2016	2017	2018 Q1
Population (million, 2018 are full-year estimates)	50.9	32.2	32.8	33.4	9.3	9.4	9.6	4.4	4.6	4.8	4.0	4.1	4.2
Smoking prevalence (smokers as % of legal smoking age population)	40%	40%	41%	39%[1]	38%	39%	38%[1]	36%	36%	36%[1]	43%	43%	43%[1]
Legal Domestic Consumption (LDC)	87.3	97.5	95.0	85.6	58.7	58.5	53.4	90.3	79.3	62.5	98.2	98.4	97.6
UAE Free-Trade Zone (FTZ)	9.8	0.2	1.2	4.1	40.9	40.1	39.4	7.2	16.7	30.4	-	0.0	0.1
Total Non-Domestic Inflows (ND)	3.0	2.3	3.8	10.3	0.4	1.4	7.2	2.5	4.0	7.1	1.8	1.6	2.3
Non-Domestic Legal (NDL)	1.4	0.8	1.7	3.7	0.1	0.8	2.9	2.0	1.5	1.4	0.8	1.0	1.3
Non-Domestic Illicit	1.6	1.5	2.1	6.6	0.3	0.6	4.3	0.5	2.5	5.7	0.9	0.6	1.0
Total Consumption (cigarettes mn)	44,020	32,334	27,451	-	10,289	9,332	-	1,154	1,252	-	5,275	5,986	-
Tax losses (US$ mn)	69.8	24.4	63.8	-	1.2	3.2	-	0.2	1.6	-	1.8	1.2	-

Increasing trend from previous year

Declining trend from previous year

Source: Oxford Economics

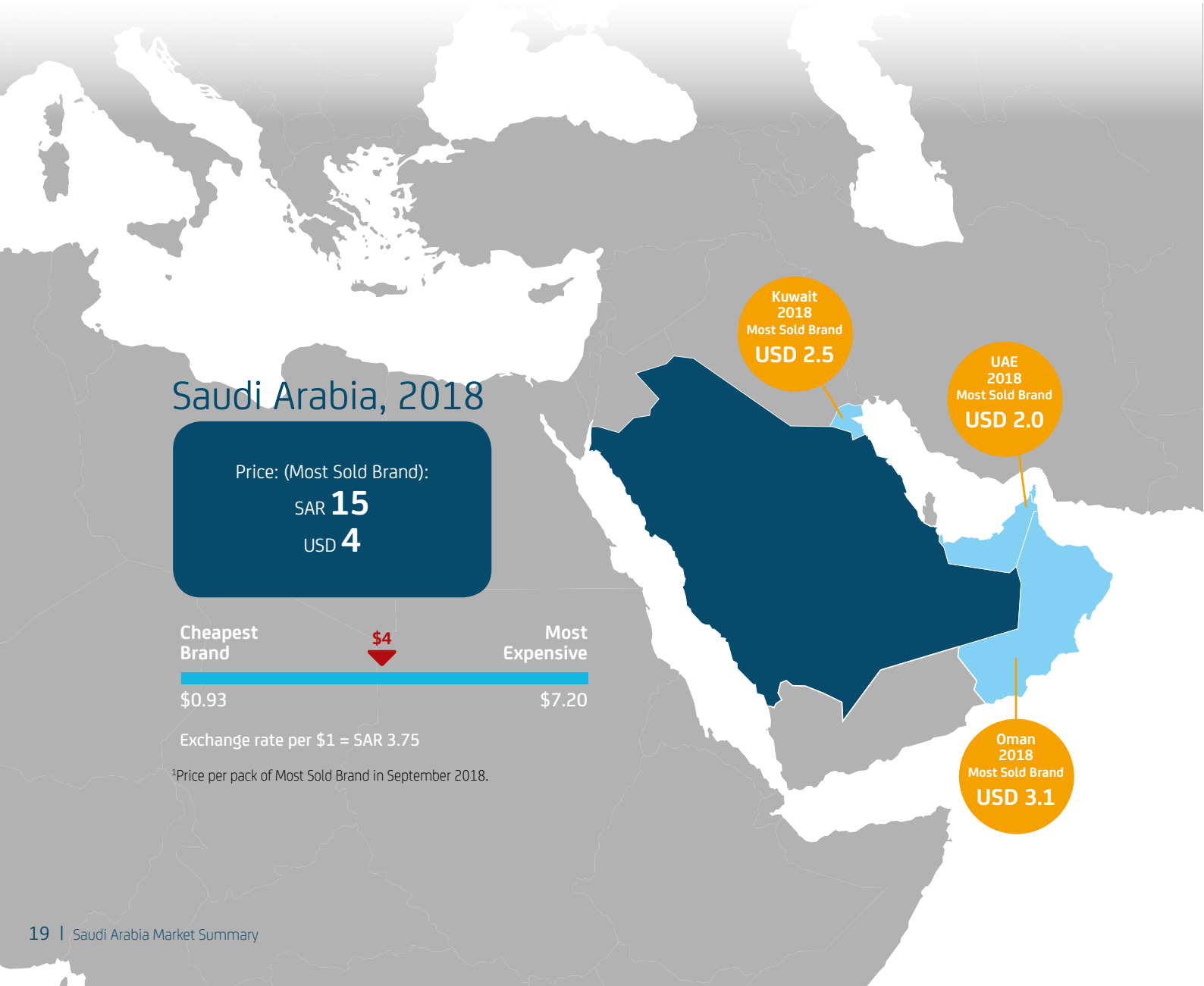
[1]September 2018



Market Summaries

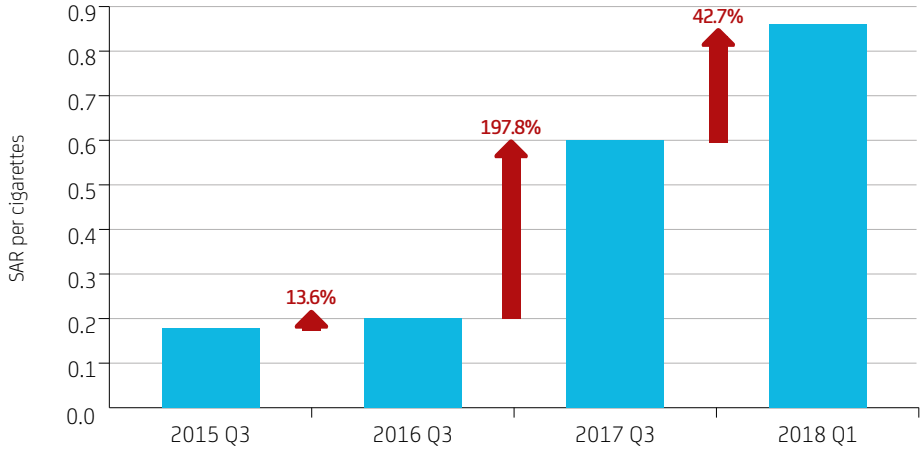
Saudi Arabia: Legal Domestic Sales

- In recent years the government has passed a number of measures aimed at curbing tobacco usage and deterring non-smokers from starting. A package of anti-smoking laws announced in 2015 by Royal Decree and implemented in 2016 banned smoking in public places and government offices, as well as outlawing promotional pricing or free samples of cigarettes.
- The government has also made substantial increases to taxes applied to cigarettes in recent years. The Customs Duty on imported cigarettes was increased from $27 per 1000 cigarettes in 2015 (the standard agreed amongst GCC countries) to $54 per 1000 cigarettes in March 2016. Additionally, a 100% Excise Tax was applied to the current retail selling price as of June 2017. Finally, VAT became applicable to cigarettes alongside a range of other goods on 1 January 2018, at a rate of 5% on top of the retail selling price incorporating both Customs Duty and Excise Tax.
- Following the introduction of new taxes in 2017, the price of the Most Sold Brand[1] in Saudi Arabia was SAR 24 per pack of 20 cigarettes. The retail selling price of the Most Sold Brand from 2015 has risen to SAR 24 in 2017 from a cost of SAR 10 in 2015.



[1]Price per pack of Most Sold Brand in September 2018.

Saudi Arabia: Tax yield applied to cigarettes[2]



Source: Oxford Economics

[2]Rate applied in July of each year to the Most Sold Brand in 2016 (Marlboro). This includes customs duty at the unit specific rate, excise tax and VAT, as applicable. Tax yield per cigarette will change due to changes in the tax structure, but also due to changes in the underlying cost of goods (since Excise is levied on an ad-valorem basis).

Saudi Arabia: Cigarette Consumption

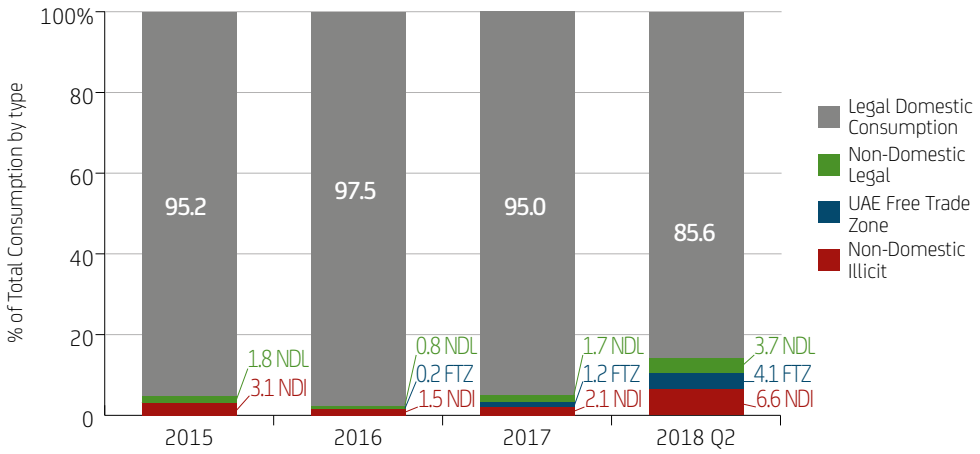
- Total Consumption (legal and illicit) is estimated to have fallen to 27.5 billion in 2017 from 34.0 billion in 2015, a decline of 19.4%. Around three-quarters of this decline occurred in 2017.
- In total, Illicit Incidence has risen from 1.5% in 2016 to 2.1% in 2017 and on to 6.6% in 2018 Q2.
- In volume terms, Illicit Consumption rose to 571 million cigarettes in 2017 from 484 Million cigarettes in 2016. This represents an increase of nearly 18%. The increase in 2018 is likely to be significantly higher based on evidence from the 2018 Q2 EPS.
- Between 2016 and 2017 the number of cigarettes originating in the UAE Free-trade zone increased from 58 million to 341 million, a five-fold increase. This has accelerated substantially since the introduction of excise tax. In 2018 Q2 cigarettes originating in the UAE Free-trade zone accounted for 4.1% of total consumption.
- Non-Domestic Illicit inflows accounted for all of the Illicit Consumption in 2018 Q2, as has been the case since 2015.

Saudi Arabia: Composition of cigarette consumption

	2015		2016		2017		2018 Q2	
Population (million, 2018 are full-year estimates)	-		50.9		32.2		32.8	
Smoking prevalence (smokers as % of legal smoking age population)	-		40%		41%		39%[1]	
	Cigarettes bn	%	Cigarettes bn	%	Cigarettes bn	%	%	% point change 2017-18
Legal Domestic Consumption (LDC)	**32.3**	**95.2**	**31.5**	**97.5**	**26.1**	**95.0**	**85.6**	**-9.4**
UAE Free-trade zone cigarettes	**0.0**	**0.0**	**0.1**	**0.2**	**0.3**	**1.2**	**4.1**	**2.9**
Total Non-Domestic Inflows (ND)	**1.6**	**4.8**	**0.7**	**2.3**	**1.0**	**3.8**	**10.3**	**6.5**
Non-Domestic Legal (NDL)	0.6	1.8	0.3	0.8	0.5	1.7	3.7	2.0
Non-Domestic Illicit	1.0	3.1	0.5	1.5	0.6	2.1	6.6	4.5
Domestic Illicit	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Total Consumption	**34.0**	**100.0**	**32.3**	**100.0**	**27.5**	**100.0**	**100.0**	**-**
Total Illicit Consumption	**1.0**	**3.1**	**0.5**	**1.5**	**0.6**	**2.1**	**6.6**	**4.5**
Total Illicit and Free-trade zone consumption	**1.0**	**3.1**	**0.5**	**1.7**	**0.9**	**3.3**	**10.7**	**7.4**

Source: Oxford Economics
[1]September 2018

Saudi Arabia: Composition of cigarette consumption (% of Total Consumption)



Source: Oxford Economics

Saudi Arabia: Free Trade Zones

- Cigarettes produced in UAE Free Trade Zones (FTZ) such as Jebel Ali, Fujairah, Ajman and Ras al Khaimah are not considered Illicit for this report. However, considerable uncertainty amongst industry sources exists as to whether the full tax liability on these cigarettes is met.
- In Saudi Arabia these cigarettes have a rapidly-growing market share. From a negligible presence in the market in 2015, and just 0.7% of Total Consumption in 2017 Q3, Empty Pack Surveys indicate that these cigarettes accounted for 5.3% of Total Consumption in 2017 Q4 and 4.1% in 2018 Q2.

Saudi Arabia: Government Finances

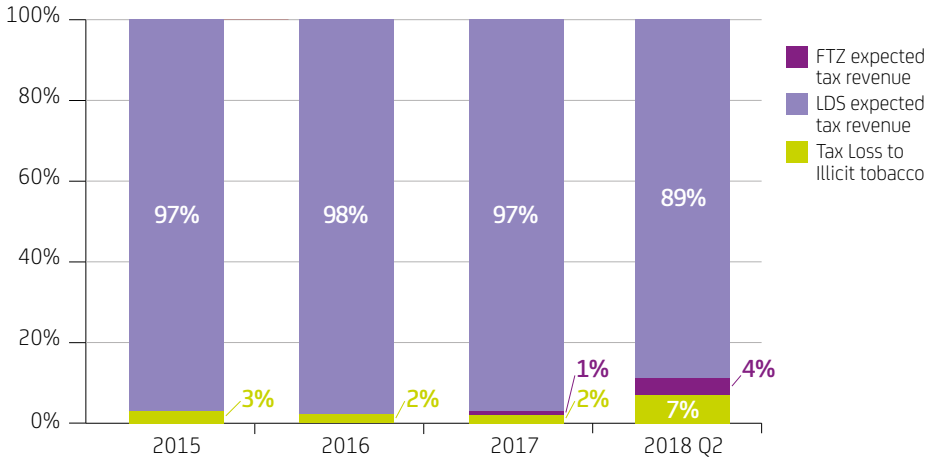
- Saudi Arabia operates a composite tax system on cigarettes combining customs duty, excise tax and value-added tax.
- An ad valorem customs duty on imported cigarettes (domestic production is banned) is levied at 100% of the CIF price, with a minimum specific duty of $54 per 1000 cigarettes. In practice, the vast majority of imported cigarettes are duty-paid at this unit specific rate. This was increased from the GCC-wide minimum of $27 per 1000 in March 2016.
- In June 2017, Saudi Arabia became the first GCC country to implement the 100% Excise Tax on tobacco products that was agreed by GCC governments in 2015. The tax is imposed on the previous retail price, incorporating both the CIF cost of goods plus the customs duty at the appropriate rate.
- Expected tax revenues from Legal Domestic Sales cigarettes were SAR 10.9 billion in 2017, up 83% from 2016.
- Our estimates indicate that the Tax Loss associated with the Illicit Consumption of cigarettes in 2017 amounted to SAR 239 million (USD 63.8 million). This represents an increase of 161% in comparison with 2016.
- With the illicit share of total consumption having risen from 2.1% in 2017 to 6.6% in 2018 Q2, and the average tax yield per cigarette having risen as a result of the rise in excise tax in June 2017, it is likely the Tax Loss from the consumption of Illicit cigarettes will rise substantially in 2018.
- Likewise, with UAE FTZ cigarettes accounting for 4.1% of Total Consumption in 2018 Q2 (1.2% for 2017 as a whole) the expected tax revenue from FTZ cigarettes will also have increased very substantially in 2018.

Saudi Arabia: Expected Tax Revenue and estimated Tax Loss

	2015		2016		2017		% change in local currency 2016-2017
	SAR mn	USD mn	SAR mn	USD mn	SAR mn	USD mn	
Expected Tax Revenue on Legal Domestic Sales cigarettes	4,943.5	1,318.3	5,971.8	1,592.5	10,912.9	2,910.1	82.7
Expected Tax Revenue from UAE FTZ cigarettes	0.0	0.0	11.0	2.9	142.6	38.0	1200.8
Estimated number of illicit cigarettes purchased (cigarettes mn)	1,048.4		483.9		571.5		18.1
Estimated Tax Loss from Illicit Consumption	**160.3**	**42.8**	**91.6**	**24.4**	**239.1**	**63.8**	**161.0**
Lost excise tax revenue	160.3	42.8	91.6	24.4	239.1	63.8	161.0

Source: Oxford Economics, based on PMI data

Saudi Arabia: Total potential Tax Revenues by cigarette type, and estimated Tax Loss to Illicit Consumption

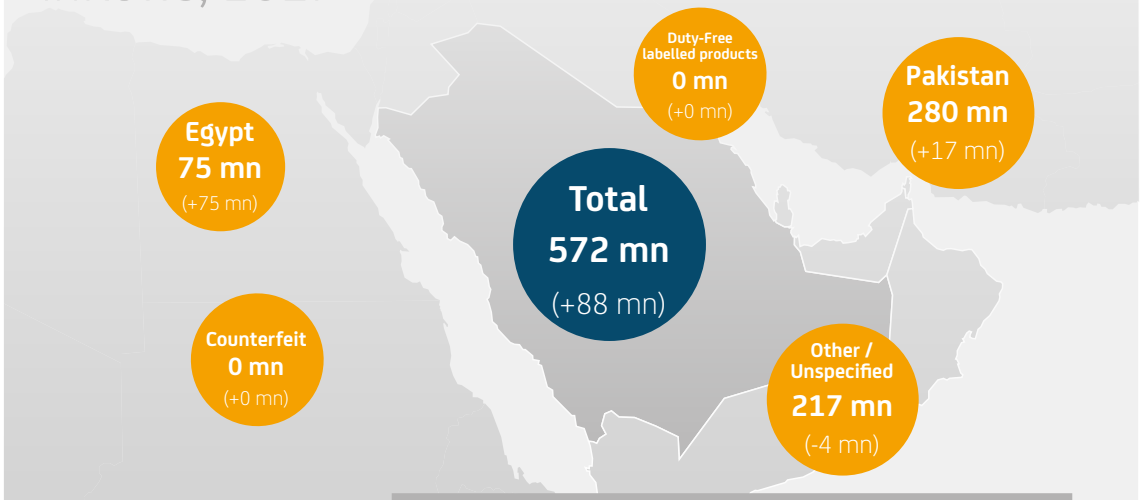


Source: Oxford Economics

Saudi Arabia: Trade Flows

- Over half of Non-Domestic cigarettes consumed in Saudi Arabia in 2017 were Non-Domestic Illicit - 571 million of a total 1,030 million. We estimate 459 million Non-Domestic Legal cigarettes[1] were consumed. No counterfeit cigarettes were identified in Saudi Arabia in 2017, although in 2018 Q2 our research indicated 0.02% of Total Consumption were counterfeit cigarettes.
- Within Non-Domestic Illicit, the largest single source remains Pakistan, which accounted for 280 million illicit cigarettes in Saudi Arabia in 2017, which corresponds to 1.0% of Total Consumption – broadly stable over the past couple of years. The volume of illicit cigarettes coming from Egypt is estimated to have increased from zero in 2016 to 75 million in 2017, but this remains less than half the volume estimated for 2015. Other/unspecified[2] markets accounted for 217 million cigarettes in 2017 – stable on 2016, but less than half of 2015.
- Saudi Arabia has implemented several measures to tackle illicit tobacco trade. A decree was passed in May 2017 to track transit shipments of cigarettes through Saudi Arabia via GPS. Containers holding cigarettes will be checked for quantity on arrival and departure from the country, to ensure against leakage into the local market. Meanwhile traders of cigarettes in transit will have to provide a bank guarantee to the value of the potential tax liability of the cigarettes if they were sold in the local market. At land borders, Saudi customs has introduced sniffer dogs and female search officers, in addition to the existing male search officers to improve detection of travellers bringing in excess tobacco. More broadly, Saudi Arabia has signed up to the Protocol to Eliminate Illicit Trade in Tobacco Products.

Saudi Arabia: Origin of total Non-Domestic Illicit Inflows, 2017



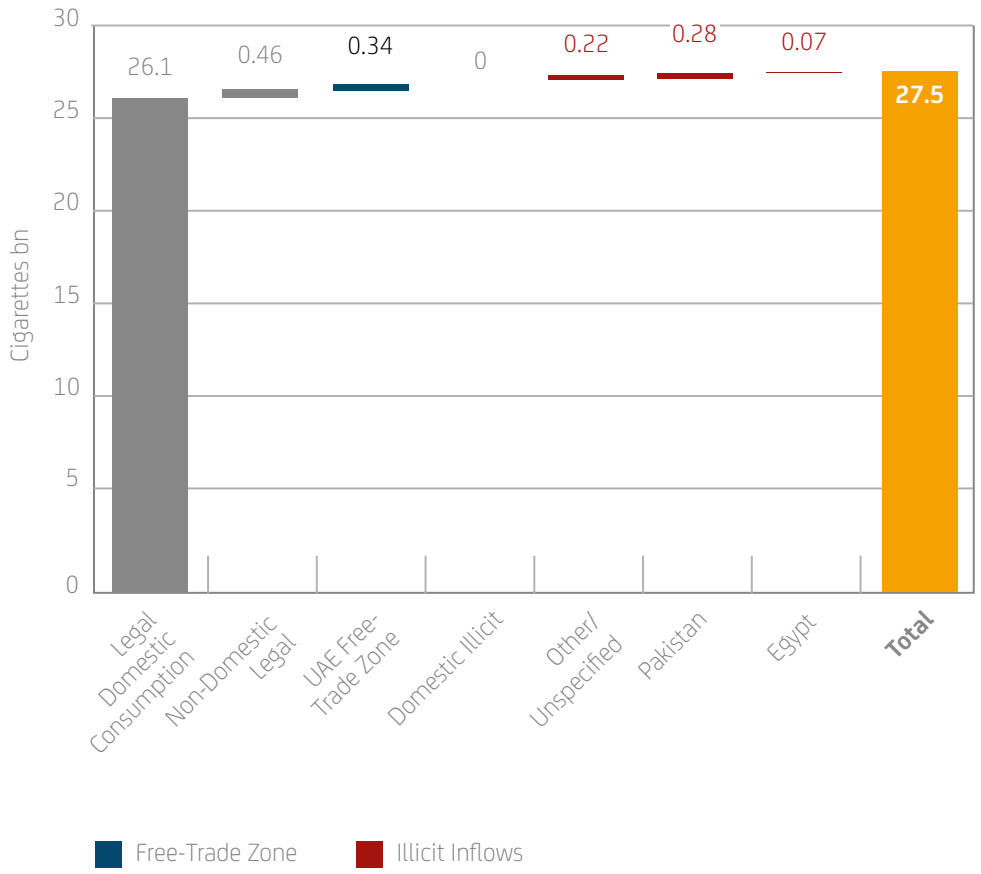
	Cigarettes mn		
	2015	2016	2017
Egypt	178.1	0.0	74.5
Pakistan	290.3	263.3	280.3
Duty-Free labelled products	54.9	0.0	0.0
Counterfeit	0.0	0.0	0.0
Other/Unspecified	525.1	220.6	216.7
Total	**1048.4**	**483.9**	**571.5**

Source: IT Flows Model and Oxford Economics

[1]Estimated using passenger data, Smoking Prevalence in tourists' country/market of origin, and the duty-free personal import allowance limit.

[2]Unspecified Market Variant refers to cigarette packs that do not bear specific market labelling or Duty-Free labelling. As such the intended market is not known.

Saudi Arabia: Consumption breakdown 2017



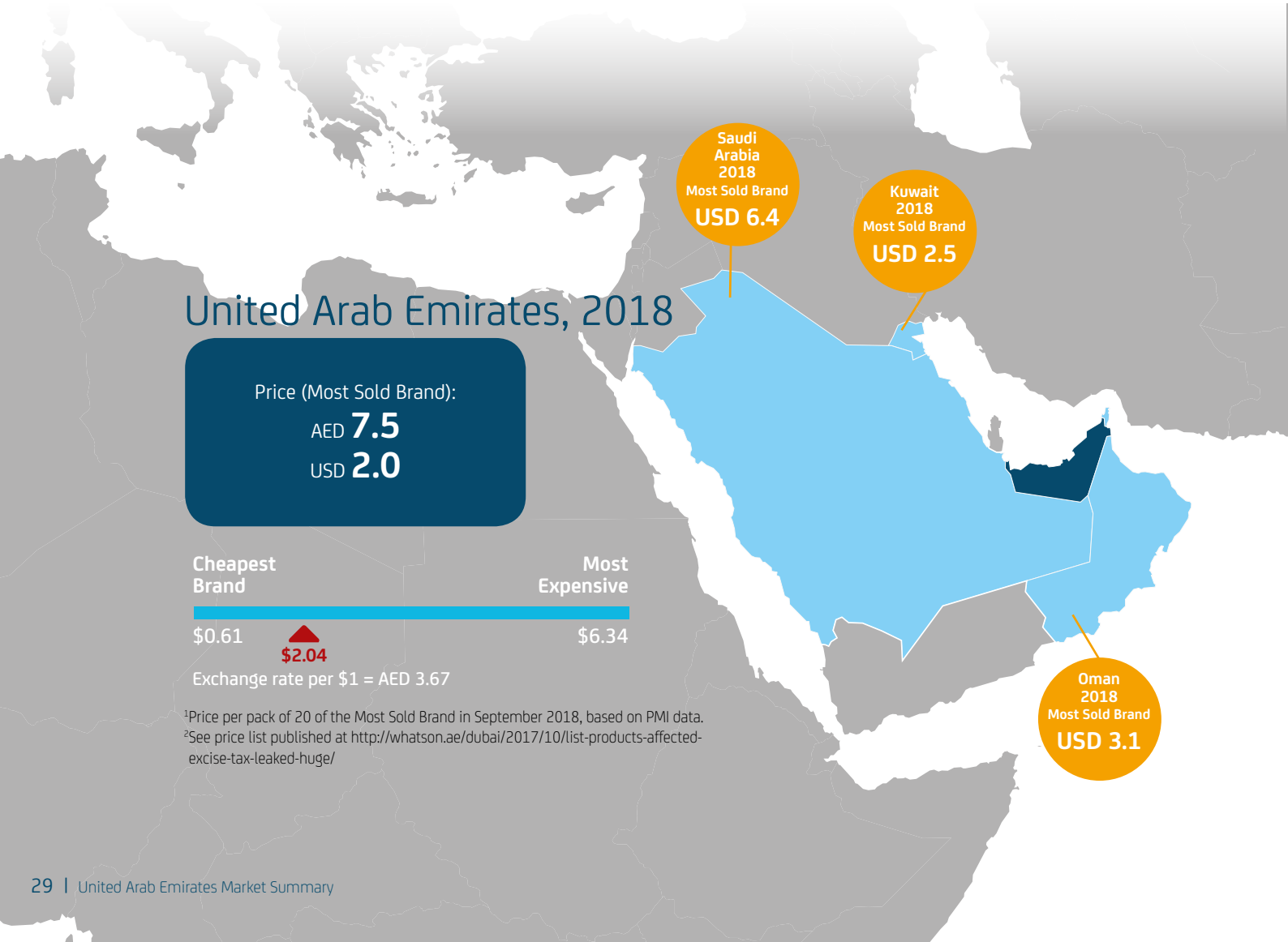
Source: Oxford Economics

Saudi Arabia: Data Sources

	Primary source	Calculation	Comments
Outflows of domestic duty-paid cigarettes	Empty Pack Survey data in other markets covered in this Report.	Empty Pack Survey data in other markets used to identify the presence of packs bearing Saudi Arabia market-specific labelling (e.g., health warnings, tax stamps, etc.).	Limited number of Saudi Market Variant cigarettes identified in other markets covered in this Report.
Legal Domestic Consumption (LDC)	—	Legal Domestic Sales minus Outflows of legal sales.	Limited Outflows of duty-paid cigarettes, so Legal Domestic Sales and Legal Domestic Consumption closely aligned.
UAE Free Trade Zone cigarettes	Empty Pack Surveys.	Estimated using Empty Pack Survey shares of total consumption accounted for by brands found to be producing in UAE FTZ.	Cigarettes produced in UAE FTZ should pay all applicable taxes when entering either the UAE from FTZ or another GCC from FTZ. However, in light of uncertainty as to whether this is the case, we choose to classify these cigarettes separately from NDL and NDI.
Total Non-Domestic Inflows (ND)	—	Sum of Non-Domestic Legal, Non-Domestic Illicit, and UAE Free Trade Zone (FTZ) cigarettes.	—
Non-Domestic Legal (NDL)	—	Estimated using passenger data, smoking rates, and passenger duty-free personal import allowance.	Maximum theoretical amount an individual can carry across a border. Passenger data from the UNWTO and OE Tourism Model.
Non-Domestic Illicit	Empty Pack Survey.	Based on Empty Pack Survey plus OE estimates.	Estimates derived from 2015 Q4, 2016 Q3, 2016 Q4, 2017 Q3, 2017 Q4 and 2018 Q1 Empty Pack Surveys. See Report methodology for more details.
Domestic Illicit	EPS and industry intelligence.	Based on augmentation of retail audit.	Empty Pack Surveys do not identify any domestic illicit cigarettes in Saudi Arabia. This is corroborated by industry anecdotal evidence.
Total Illicit Consumption	—	Sum of Non-Domestic Illicit and Domestic Illicit.	—
Total Consumption	—	Legal Domestic Sales minus Outflows of domestic duty-paid cigarettes, plus estimated Non-Domestic Legal consumption, plus consumption of UAE FTZ cigarettes, plus estimated Illicit Consumption.	The IT Flows Model estimate of consumption is 27.7 billion cigarettes for 2017.
Total Tax Loss	—	Total Illicit Consumption multiplied by the weighted average tax rates (Import Duty and Excise Tax).	See Report methodology for more details.

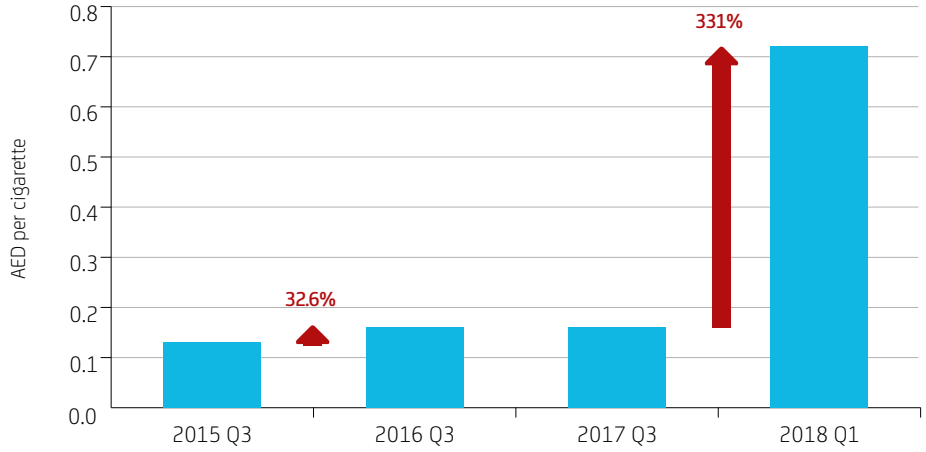
United Arab Emirates: Legal Domestic Sales

- Legal Domestic Sales fell in 2017, the first decline in Legal Domestic Sales since 2012. Nevertheless, over a four-year horizon (2014-2017) Legal Domestic Sales have been broadly stable.
- The UAE is the only GCC economy which permits the manufacture of cigarettes, but only in specified Free Trade Zones (FTZ). However, the government implemented a law in 2014 that the UAE would align with other GCC countries, giving cigarette producers a ten-year grace period before they have to cease production in the UAE. The government proposed a ban on smoking in public places in 2016, but it has yet to be implemented.
- Unlike Oman and Saudi Arabia, UAE did not increase the Customs Duty on cigarettes to USD 54 per 1000 cigarettes in 2016 from USD 27 per 1000 cigarettes. However, alongside Saudi Arabia, the UAE did implement a 100% Excise Tax on current retail selling prices (in October 2017). As of January 2018, VAT is also applied to the retail selling price including both these taxes.
- The retail selling price of the Most Sold Brand[1] in 2015 has risen to AED 21 (or USD 5.7) per pack of 20 cigarettes in 2018 Q1 from AED 10 (or USD 2.7) in January 2015. However, this brand is no longer the Most Sold Brand in 2018. The Most Sold Brand in 2018 Q1 is a lower-cost brand retailing at AED 7.5 or USD 2.0 per pack of 20 cigarettes.
- However, it is not clear all cigarettes sold in UAE have Customs Duty paid upon them. Price lists[2] showing prices "before" and "after" the introduction of Excise Tax in October 2017 contain brands manufactured in FTZ retailing at AED 4 per pack of 20 cigarettes after the Excise Tax increase. Since the sum of minimum Customs Duty (UAD 2) and Excise Tax (100% of previous retail selling price) is AED 4, this implies zero production cost if taxes are being paid in full.



[1]Price per pack of 20 of the Most Sold Brand in September 2018, based on PMI data.
[2]See price list published at http://whatson.ae/dubai/2017/10/list-products-affected-excise-tax-leaked-huge/

United Arab Emirates: Tax yield applied to cigarettes[3]



Source: Oxford Economics

[3]Rate applied in July of each year to the Most Sold Brand in 2016 (Marlboro). This includes customs duty at the unit specific rate, excise tax and VAT, as applicable.

United Arab Emirates: Cigarette Consumption

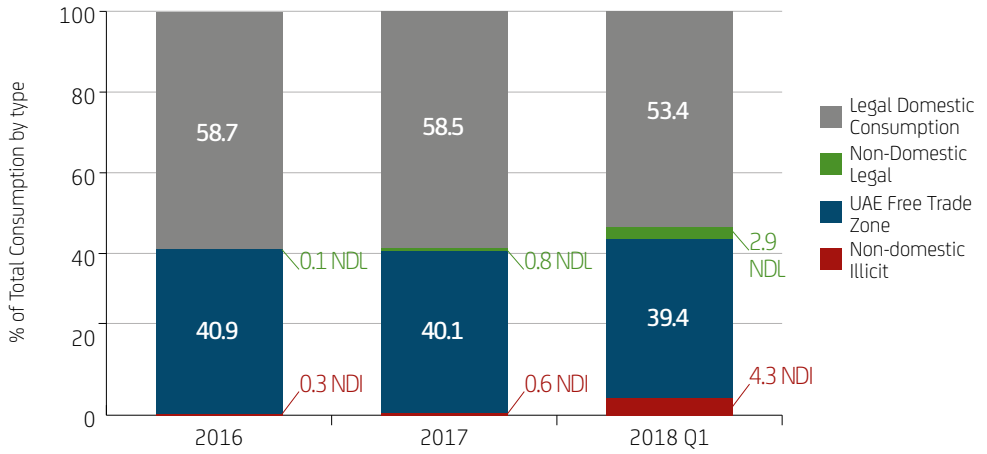
- The proportion of Total Consumption accounted for by Legal Domestic Consumption fell to just over 53% in 2018 Q1, from 59% in 2017.
- The Non-Domestic share of consumption has increased in recent quarters, rising to 7.2% of Total Consumption in 2018 Q1, up from 1.4% in 2017. Non-Domestic Legal accounted for 2.9% while Non-Domestic Illicit accounted for 4.3% of Total Consumption in 2018 Q1.
- Cigarettes from the UAE Free Trade Zones accounted for around 40% of the market for the three years covered in this study.
- Non-Domestic Legal and Non-Domestic Illicit both accounted for a relatively modest share of Total Consumption in 2016 and 2017.

United Arab Emirates: Composition of cigarette consumption

	2016		2017		2018 Q1	
Population (million, 2018 are full-year estimates)	9.3		9.4		9.6	
Smoking prevalence (smokers as % of legal smoking age population)	38%		39%		38%[1]	
	Cigarettes bn	%	Cigarettes bn	%	%	% point change 2017-18
Legal Domestic Consumption (LDC)	**6,036.2**	**58.7**	**5,460.1**	**58.5**	**53.4**	**-5.1**
UAE Free-trade zone cigarettes	**4,211.3**	**40.9**	**3,740.8**	**40.1**	**39.4**	**-0.7**
Total Non-Domestic Inflows (ND)	**41.5**	**0.4**	**130.8**	**1.4**	**7.2**	**5.8**
Non-Domestic Legal (NDL)	12.7	0.1	71.9	0.8	2.9	2.1
Non-Domestic Illicit	28.8	0.3	58.8	0.6	4.3	3.7
Domestic Illicit	**-**	**0.0**	**-**	**0.0**	**0.0**	**0.0**
Total Consumption	**10,289.0**	**100.0**	**9,331.6**	**100.0**	**100.0**	**-**
Total Illicit Consumption	**28.8**	**0.3**	**58.8**	**0.6**	**4.3**	**3.7**
Total Illicit and Free-trade zone consumption	**4,240.1**	**41.2**	**3,799.6**	**40.7**	**43.7**	**3.0**

Source: Oxford Economics
[1]September 2018

United Arab Emirates: Composition of cigarette consumption (% of Total Consumption)



Source: Oxford Economics

United Arab Emirates: Free Trade Zones

- Cigarettes produced in UAE Free Trade Zones (FTZ) such as Jebel Ali, Fujairah, Ajman and Ras al Khaimah are not considered Illicit for this report, and if they are sold in the UAE, they should pay both customs duty (at a rate of $27 per 1000), excise duty (at a rate of 100% of the cost including customs duty), and VAT (as of 1 January 2018).
- However, cigarette manufacturing in the FTZ is set to be phased out as part of the Anti-Tobacco Federal Law, which came into force on 21 January 2014. As part of this law the growing of tobacco and manufacturing of tobacco products was outlawed, although tobacco farms were given a two-year grace period before the ban came into place and cigarette factories in the FTZ were given a ten-year grace period.
- There is considerable uncertainty over whether all cigarettes produced in the FTZ have the applicable tax and duty paid upon them when sold in GCC markets. A price list released following the implementation of the excise tax in October 2017 showed several brands manufactured in the FTZ retailing at a price exactly equal to the minimum possible customs duty and excise tax (AED 4). Since these cigarettes must also have a cost of production and distribution, it is difficult to see how these cigarettes are complying with all applicable taxes.
- The share of FTZ cigarettes in Total Consumption in UAE has remained fairly stable over the past couple of years, but at around 40% this is a very significant portion of the market.

United Arab Emirates: Government Finances

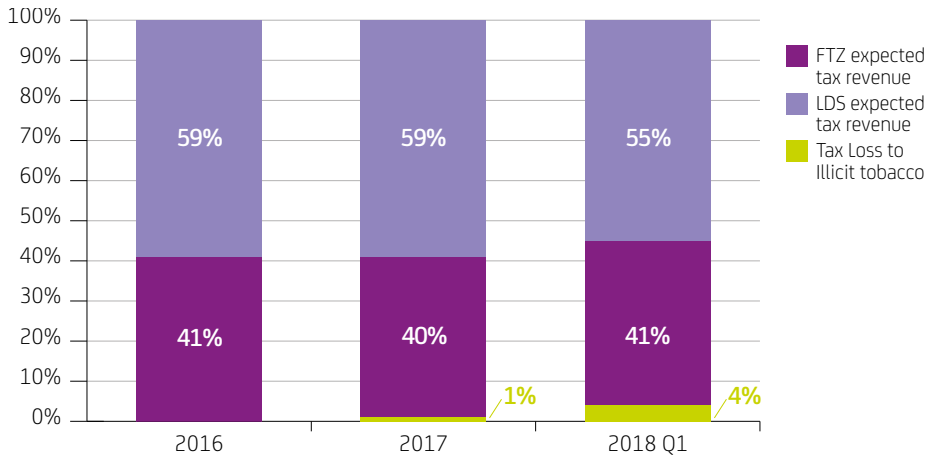
- The UAE operates a composite tax system on cigarettes combining customs duty, excise tax and value-added tax.
- An Ad-Valorem Customs Duty on imported cigarettes is levied at 100% of the CIF price. This applies to both cigarettes imported from outside the UAE and brought into the UAE from Free Trade Zones. The minimum yield for customs duty is set at $27/AED 100 per 1000 cigarettes.
- In October 2017, the UAE government implemented the Excise Tax on cigarettes agreed to in principle by all GCC governments in 2015. This is equivalent to 100% of the pre-excise tax retail selling price, i.e. the price of imported cigarettes on a CIF basis plus the Customs Duty.
- Further, in 2018 the UAE implemented a Value-Added Tax, at 5%. This is applicable to the retail selling price of cigarettes including both Customs Duty and Excise Tax.
- Our estimate is that expected tax revenues on Legal Domestic Sales cigarettes rose from AED 937 million in 2016 to AED 1,090 million in 2017 – an increase of just over 16%. We estimate the Tax Loss from the Illicit Consumption of cigarettes was AED 11.7 million in 2017, up from AED 4.5 million in 2016. A large portion of this rise was due to an increase in illicit consumption - using tax rates from 2016 on the 2017 illicit consumption data shows an expected Tax Loss of AED 9.1 million. Since FTZ-manufactured cigarettes accounted for just over 40% of Total Consumption in 2017 (falling to 39% in 2018 Q1), compared to 0.7% for Illicit Consumption in 2017 (rising to 6.0% in 2018 Q1), the actual losses from the consumption of Non-Duty Paid cigarettes could be substantially higher than this estimate, depending on what proportion of FTZ-manufactured cigarettes are tax-paid.

United Arab Emirates: Expected tax revenue and estimated Tax Losses

	2016		2017		% change in local currency 2016-2017
	AED mn	USD mn	AED mn	USD mn	
Expected Tax Revenue on Legal Domestic Sales cigarettes	936.6	255.0	1090.2	296.8	16.4
Expected Tax Revenue from UAE FTZ cigarettes	653.5	177.9	746.9	203.3	14.3
Estimated number of illicit cigarettes purchased (cigarettes mn)	28.8		58.8		104.2
Estimated Tax Loss from Illicit Consumption	**4.5**	**1.2**	**11.7**	**3.2**	**162.7**
Lost excise tax revenue	4.5	1.2	11.7	3.2	162.7

Source: Oxford Economics, based on PMI data

United Arab Emirates: Expected total potential Tax Revenues by cigarette type, and estimated Tax Loss to Illicit Consumption

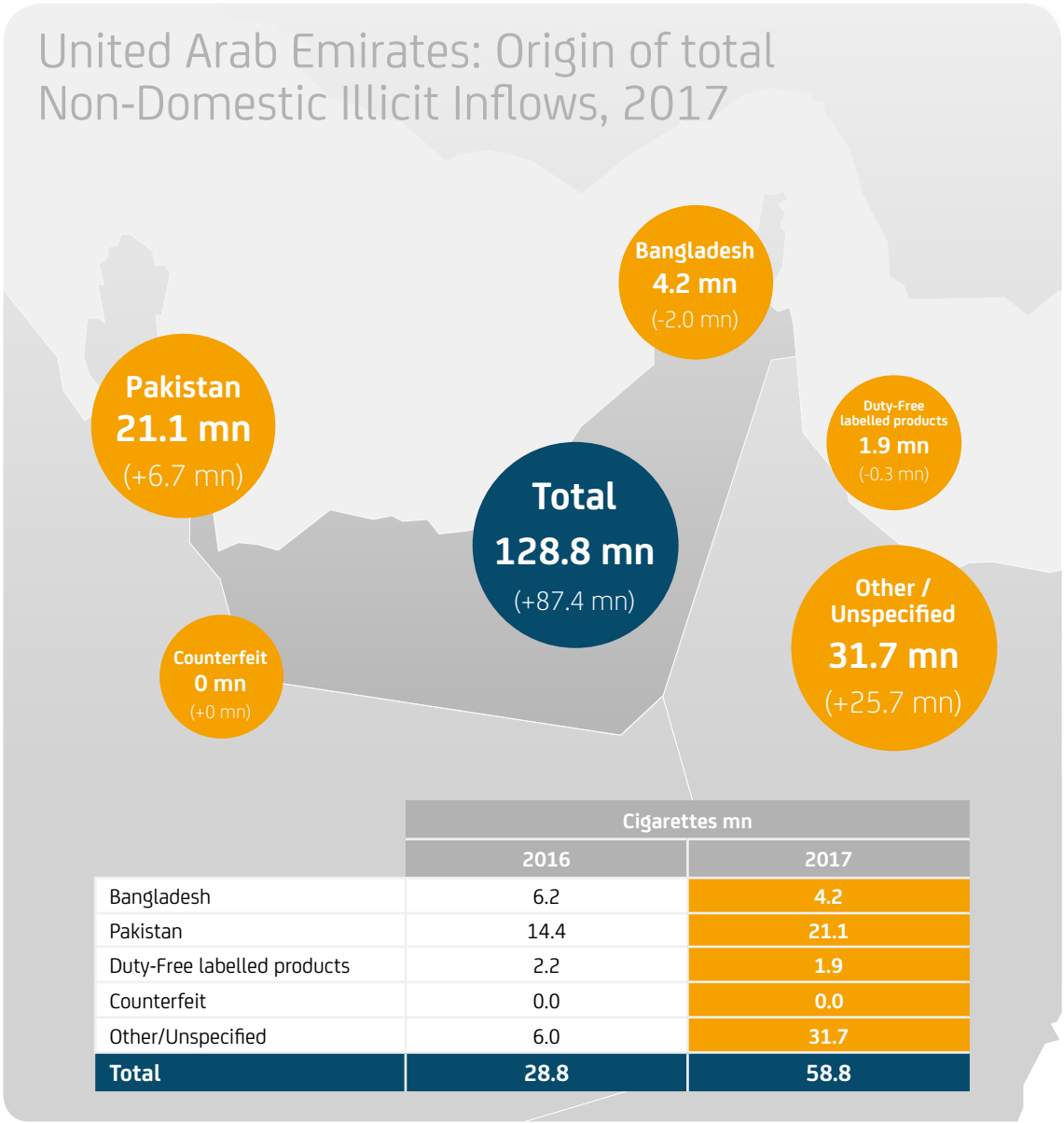


Source: Oxford Economics
Note: Our estimates suggest that tax revenues from Legal Domestic Sales were USD 297m in 2017

United Arab Emirates: Trade Flows

- Just 0.6% of Total Consumption was accounted for by Non-Domestic Illicit cigarettes in 2017, with Pakistan the largest single source. However, at just 21.1 million, this was a negligible share of total consumption. We estimate Non-Domestic Illicit Consumption of Other/Unspecified Market Variant[1] amounted to 31.7 million cigarettes.
- Inflows of Legal Non-Domestic cigarettes[2] rose almost five-fold in 2017, from just below 13 million in 2016 to just below 72 million in 2017. The share of Non-Domestic Legal cigarettes in UAE has risen further in 2018 Q1 according to the most recent EPS, from 0.8% of total in 2017 to 2.9% in 2018 Q1. UAE Free Trade Zone cigarettes are the primary source of outflows from UAE to other markets in our study, with 550 million cigarettes from the FTZ estimated to have found their way to Oman and Saudi Arabia in 2017. The presence of FTZ-manufactured cigarettes has risen in EPSs conducted so far in 2018 suggesting a further rise in outflows.

United Arab Emirates: Origin of total Non-Domestic Illicit Inflows, 2017



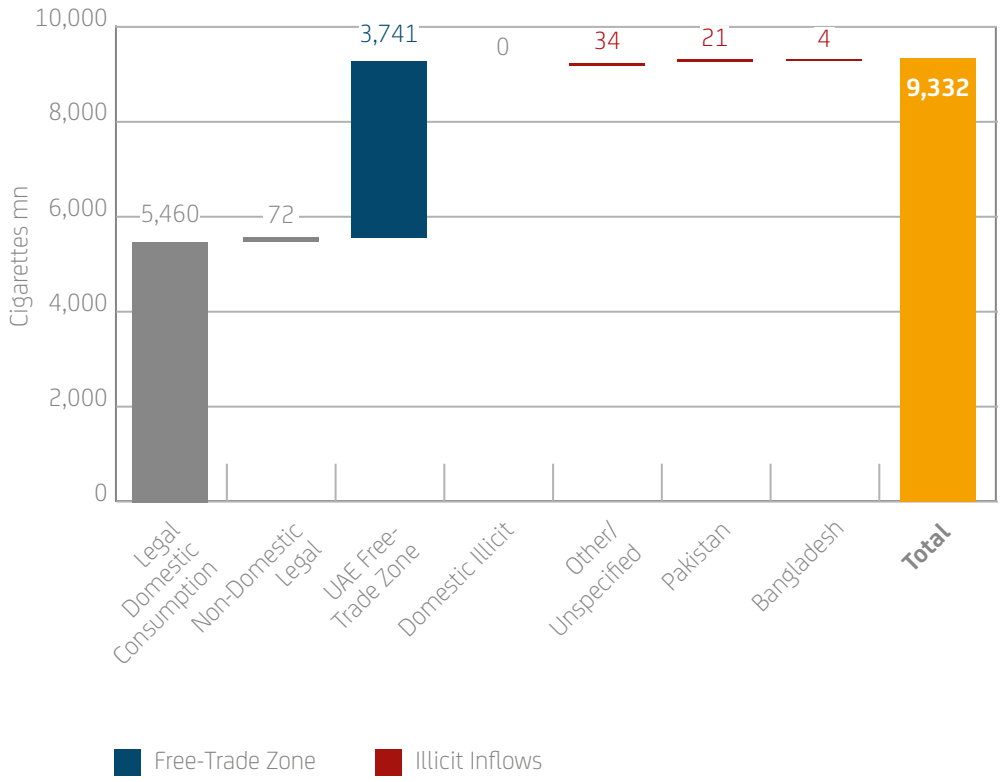
	Cigarettes mn	
	2016	2017
Bangladesh	6.2	4.2
Pakistan	14.4	21.1
Duty-Free labelled products	2.2	1.9
Counterfeit	0.0	0.0
Other/Unspecified	6.0	31.7
Total	**28.8**	**58.8**

Source: IT Flows Model and Oxford Economics

[1]Unspecified Market Variant refers to cigarette packs that do not bear specific market labelling or Duty-Free labelling. As such the intended market is not known.

[2]Estimated using passenger data, Smoking Prevalence in tourists' country/market of origin, and the duty-free personal import allowance limit.

United Arab Emirates: Consumption breakdown 2017



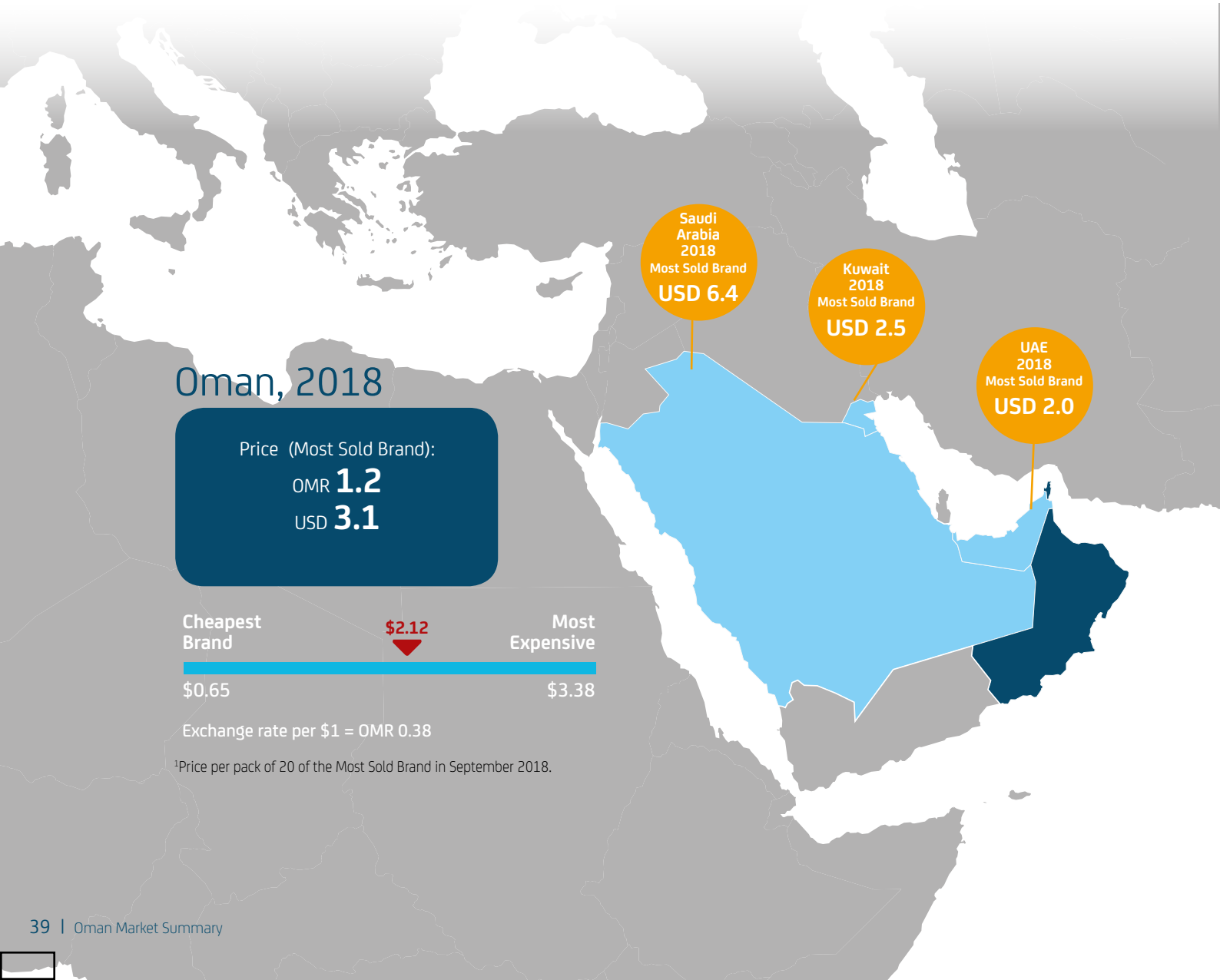
Source: Oxford Economics

United Arab Emirates: Data Sources

	Primary source	Calculation	Comments
Outflows of domestic duty-paid cigarettes	Empty Pack Survey data in other markets covered in this Report.	Empty Pack Survey data in other markets used to identify the presence of packs bearing United Arab Emiratesi market-specific labelling (e.g., health warnings, tax stamps, etc.).	UAE FTZ Market Variant cigarettes identified in other markets covered in this Report.
Legal Domestic Consumption (LDC)	—	Legal Domestic Sales minus Outflows of legal sales.	Limited Outflows of duty-paid cigarettes, so Legal Domestic Sales and Legal Domestic Consumption closely aligned.
UAE Free Trade Zone cigarettes	Empty Pack Surveys, OE estimates.	Estimated using Empty Pack Survey shares of total consumption accounted for by brands found to be producing in UAE FTZ.	Cigarettes produced in UAE FTZ should pay all applicable taxes when entering either the UAE from FTZ or another GCC from FTZ. However, in light of uncertainty as to whether this is the case, we choose to classify these cigarettes separately from NDL and NDI.
Total Non-Domestic Inflows (ND)	—	Sum of Non-Domestic Legal, Non-Domestic Illicit, and UAE Free Trade Zone (FTZ) cigarettes.	—
Non-Domestic Legal (NDL)	—	Estimated using passenger data, smoking rates, and passenger duty-free personal import allowance.	Maximum theoretical amount an individual can carry across a border. Passenger data from the UNWTO and OE Tourism Model.
Non-Domestic Illicit	Empty Pack Survey.	Based on Empty Pack Survey plus OE estimates.	Estimates derived from 2016 Q4 and 2018 Q1 Empty Pack Surveys. See Report methodology for more details.
Domestic Illicit	EPS and industry intelligence.	Based on augmentation of retail audit.	Empty Pack Surveys do not identify any domestic illicit cigarettes in United Arab Emirates. This is corroborated by industry anecdotal evidence.
Total Illicit Consumption	—	Sum of Non-Domestic Illicit and Domestic Illicit.	—
Total Consumption	—	Legal Domestic Sales minus Outflows of domestic duty-paid cigarettes, plus estimated Non-Domestic Legal consumption, plus consumption of UAE FTZ cigarettes, plus estimated Illicit Consumption.	The IT Flows Model estimate of consumption is 7.8 billion cigarettes for 2017.

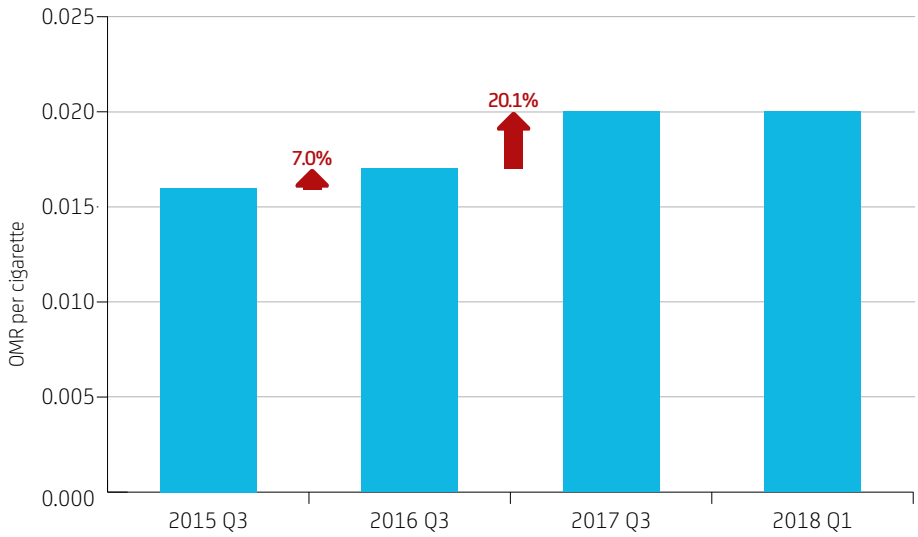
Oman: Legal Domestic Sales

- Growth in Legal Domestic Sales eased markedly from 2014-2015 into 2016, and Legal Domestic Sales actually fell in 2017.
- The government announced measures to reduce smoking in February 2018, as part of a broader strategy for combatting non-communicable diseases. Specifically, new limitations on smoking in enclosed places will be introduced, alongside increased promotion of the health impacts of tobacco. Moreover, in-store advertising will be banned, building on the 2016 ban on tobacco advertising in TV, radio, press and online.
- Oman is also planning to increase tax on tobacco products. Alongside Saudi Arabia, Oman's government chose to increase the Customs Duty on imported cigarettes from USD 27 per 1000 cigarettes in 2015 to USD 54 per 1000 cigarettes in October 2016. The government plans to introduce a 100% Excise Duty on current retail selling prices (although the timing of this rise has not been announced at the time of writing).
- Cigarette prices in Oman are OMR 1.2 (or USD 3.1) per pack of 20 cigarettes for the Most Sold Brand[1] in Q1 2018. This is unchanged on a like-for-like basis versus Q1 2017, and OMR 0.2 (USD 0.5) higher versus 2016. Cigarette prices in Oman in Q1 2018 were around half of those prevailing in Saudi Arabia, which implemented a 100% Excise Tax in 2017.



[1]Price per pack of 20 of the Most Sold Brand in September 2018.

Oman: Tax yield applied to cigarettes[2]



Source: Oxford Economics

[2]Rate applied in July of each year to the Most Sold Brand in 2016 (Marlboro). This includes customs duty at the unit specific rate, excise tax and VAT, as applicable. Tax yield per cigarette will change due to changes in the tax structure, but also due to changes in the underlying cost of goods (since Excise is levied on an ad-valorem basis).

Oman: Cigarette Consumption

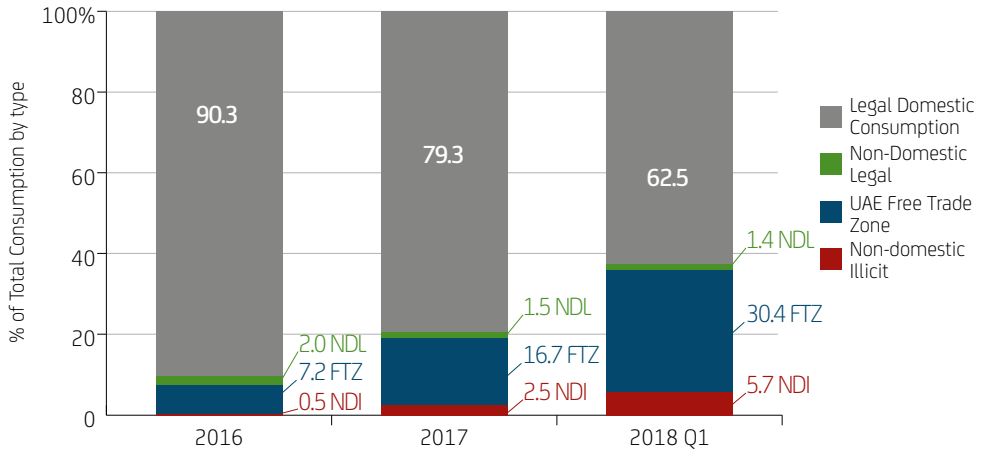
- Total Consumption (Legal, Illicit and cigarettes from the UAE Free Trade Zones) is estimated to have risen to 1.3 billion cigarettes in 2017 from 1.2 billion cigarettes in 2016 – an increase of 8.5%.
- Within this, we estimate that Legal Domestic Consumption edged down by 5.0% to just under 990 million cigarettes in 2017. However, evidence from the 2018 Q1 EPS suggests that the proportion of Total Consumption accounted for by Legal Domestic Consumption has fallen sharply since 2017. In our the EPS for 2018 Q1, 62.5% of cigarettes were identified as Legal Domestic Consumption, down nearly 17pp versus 2017.
- The bulk of the decrease in Legal Domestic Consumption has been driven by a large rise in the presence of cigarettes from the UAE Free Trade Zones in Oman. These accounted for just 7.2% of cigarettes in Oman in 2016, but this share has more than quadrupled to 30.4% in the 2018 Q1 EPS.
- Consumption of Non-Domestic Illicit cigarettes has also increased substantially. We estimate this category to have risen to 5.7% of Total Consumption in the 2018 Q1 EPS, up from just 0.5% in 2016.
- Non-Domestic Legal inflows are also estimated to have fallen (modestly) between 2016 and 2018. These cigarettes accounted for 1.4% of Total Consumption in the 2018 Q1 EPS, down from 2.0% in 2016.

Oman: Composition of cigarette consumption

	2016		2017		2018 Q1	
Population (million, 2018 are full-year estimates)	4.4		4.6		4.8	
Smoking prevalence (smokers as % of legal smoking age population)	36%		36%		36%[1]	
	Cigarettes bn	%	Cigarettes bn	%	%	% point change 2017-18
Legal Domestic Consumption (LDC)	**1,041.5**	**90.3**	**992.1**	**79.3**	**62.5**	**-16.8**
UAE Free-trade zone cigarettes	**83.5**	**7.2**	**208.9**	**16.7**	**30.4**	**13.7**
Total Non-Domestic Inflows (ND)	**28.6**	**2.5**	**50.6**	**4.0**	**7.1**	**3.1**
Non-Domestic Legal (NDL)	23.3	2.0	19.3	1.5	1.4	-0.1
Non-Domestic Illicit	5.3	0.5	31.2	2.5	5.7	3.2
Domestic Illicit	-	-	-	-	-	-
Total Consumption	**1,153.7**	**100.0**	**1,251.6**	**100.0**	**100.0**	-
Total Illicit Consumption	**5.3**	**0.5**	**31.2**	**2.5**	**5.7**	**3.2**
Total Illicit and Free-trade zone consumption	**88.8**	**7.7**	**240.2**	**19.2**	**36.2**	**17.0**

Source: Oxford Economics
[1]September 2018

Oman: Composition of cigarette consumption (% of Total Consumption)



Source: Oxford Economics

Oman: Free Trade Zones

- Cigarettes produced in UAE Free Trade Zones (FTZ) such as Jebel Ali, Fujairah, Ajman and Ras al Khaimah are not considered Illicit for this report. However, considerable uncertainty exists as to whether the full tax liability is met.
- Oman has a high and rising incidence of these cigarettes. The estimated share of UAE FTZ cigarettes in Total Consumption in Oman in 2016 was 7.2% and this rose to 30.4% in the 2018 Q1 EPS.
- The prevalence of cigarettes produced in UAE Free Trade Zones (FTZ) could be partly a result of Oman's location at the strategically-positioned Straits of Hormuz, where the distance between the Arabian Peninsula and Iran is shortest. News reports suggest smugglers take cigarettes into Oman in order to smuggle them across the Straits into Iran.[1] It may well be the case that a portion of FTZ cigarettes destined for consumption in Iran leak out into domestic Omani markets.

[1]See https://roadsandkingdoms.com/2014/how-iran-smuggles-its-smokes/ for example for an examination of the illicit trade routes between tobacco manufacturers in the UAE Free Trade zones and consumers in Iran, via Oman, and https://www.maritime-executive.com/editorials/omans-smugglers-await-the-return-of-iranian-sanctions for a broader discussion of the Oman-Iran route for illicit trade.

Oman: Government Finances

- As part of the GCC, Oman operates an ad-valorem Custom Duty on imported cigarettes and tobacco goods, at 100% of CIF, with a minimum specific tariff of $54 per 1000 cigarettes. This was increased from $27 per 1000 cigarettes in October 2016. Oman is also due to implement both a 100% Excise Tax on cigarettes (the National Tobacco Control Committee had indicated this would happen in June 2018[1], but this tax has not been implemented at the time of writing) and VAT at 5%, as part of GCC-wide agreements, but there is no explicit date for the introduction of either measure.
- Expected tax revenue from Legal Domestic Sales cigarettes rose by 12.8% in 2017, from OMR 17.7 million in 2016 to OMR 19.9 million in 2017. However, with the volume of Illicit Consumption rising to 31.2 million cigarettes in 2017 from 5.3 million in 2016, we estimate the Tax Loss associated with the Illicit Consumption of cigarettes rose to OMR 0.6 million in 2017 from OMR 0.1 million in 2016.
- With the illicit share of Total Consumption estimated to have risen further in 2018 Q1, it seems likely that the Tax Loss will rise substantially again in 2018.
- Cigarettes from UAE FTZ accounted for 7.2% of Total Consumption in 2016, but this rose to 30.4% in 2018 Q1. The expected tax revenues from UAE FTZ cigarettes is therefore likely to increase in 2018 versus 2017, given the increase in the share of these cigarettes of Total Consumption.

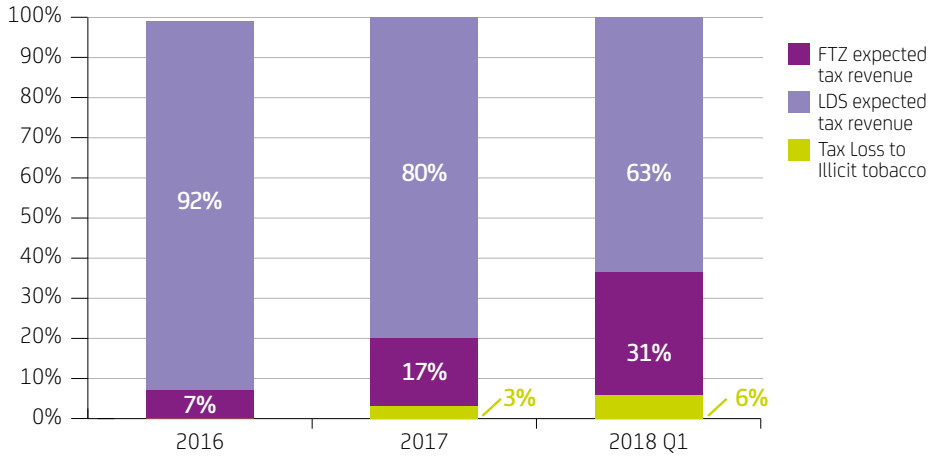
Oman: Expected Tax Revenue and estimated Tax Loss

	2016		2017		% change in local currency 2016-2017
	OMR mn	USD mn	OMR mn	USD mn	
Expected Tax Revenue on Legal Domestic Sales cigarettes	17.7	45.9	19.9	51.8	12.8
Expected Tax Revenue from UAE FTZ cigarettes	1.4	3.7	4.2	10.9	195.0
Estimated number of illicit cigarettes purchased (cigarettes mn)	5.3		31.2		488.6
Estimated Tax Loss from Illicit Consumption	**0.1**	**0.2**	**0.6**	**1.6**	**594.2**
Lost excise tax revenue	0.1	0.2	0.6	1.6	594.2

Source: Oxford Economics, based on PMI data

[1]http://www.muscatdaily.com/Archive/Oman/100-excise-tax-on-tobacco-energy-drinks-from-June-576l

Oman: Total potential Tax Revenues by cigarette type, and estimated Tax Loss to Illicit Consumption

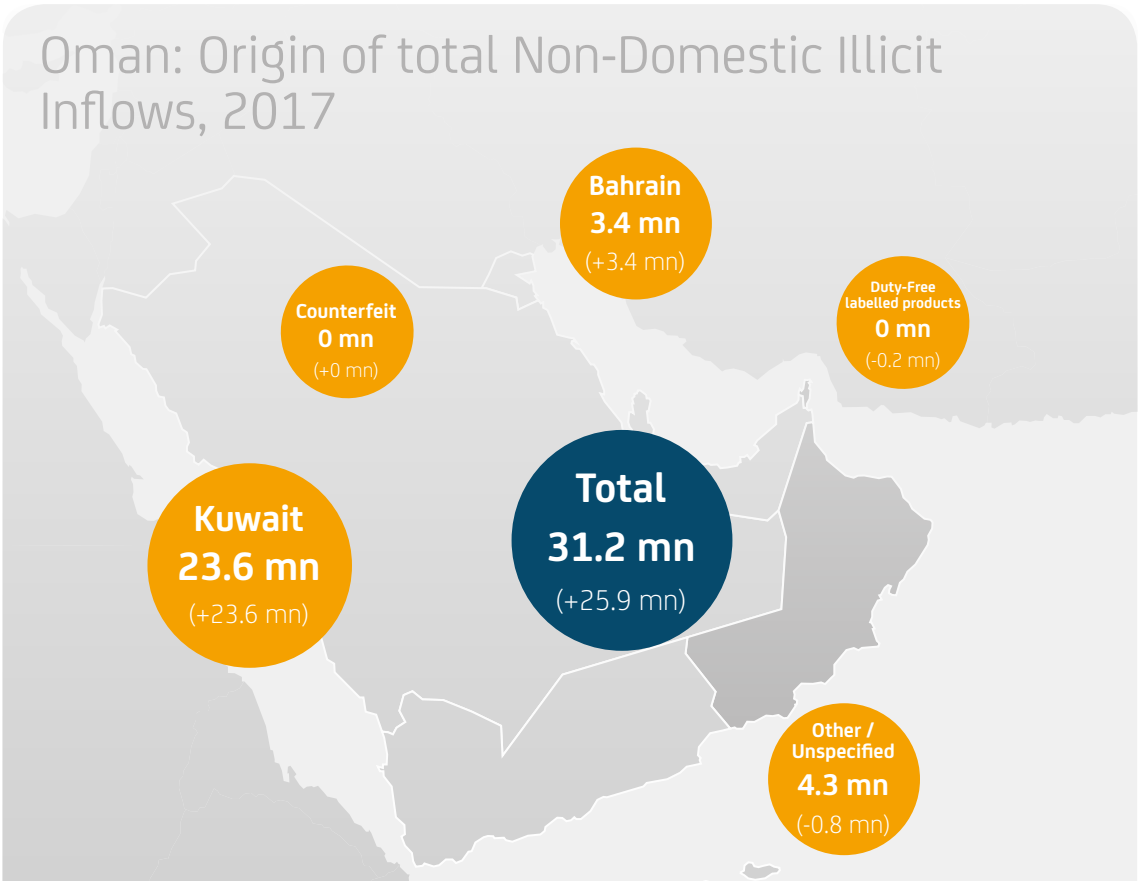


Source: Oxford Economics
Note: Our estimates suggest that tax revenues from Legal Domestic Sales were USD 297m in 2017

Oman: Trade Flows

- Our estimates suggest that the volume of Non-Domestic cigarettes in Oman nearly doubled in 2017. At 50.6 million cigarettes, Non-Domestic accounted for 4.0% of Total Consumption in 2017, up from 2.5% in 2016 (28.6 million in volume terms). Of this, 19.3 million were Non-Domestic Legal in 2017, and 31.2 million were Non-Domestic Illicit.
- In 2017, there was a significant increase in the volume of Non-Domestic cigarettes from Kuwait, rising from a negligible presence in 2016 to nearly 24 million in 2017.
- There were very modest inflows from Bahrain and Other/Unspecified[2] sources in 2017, although both remain negligible shares of Total Consumption. There were no counterfeit products identified in 2016 or 2017.

Oman: Origin of total Non-Domestic Illicit Inflows, 2017



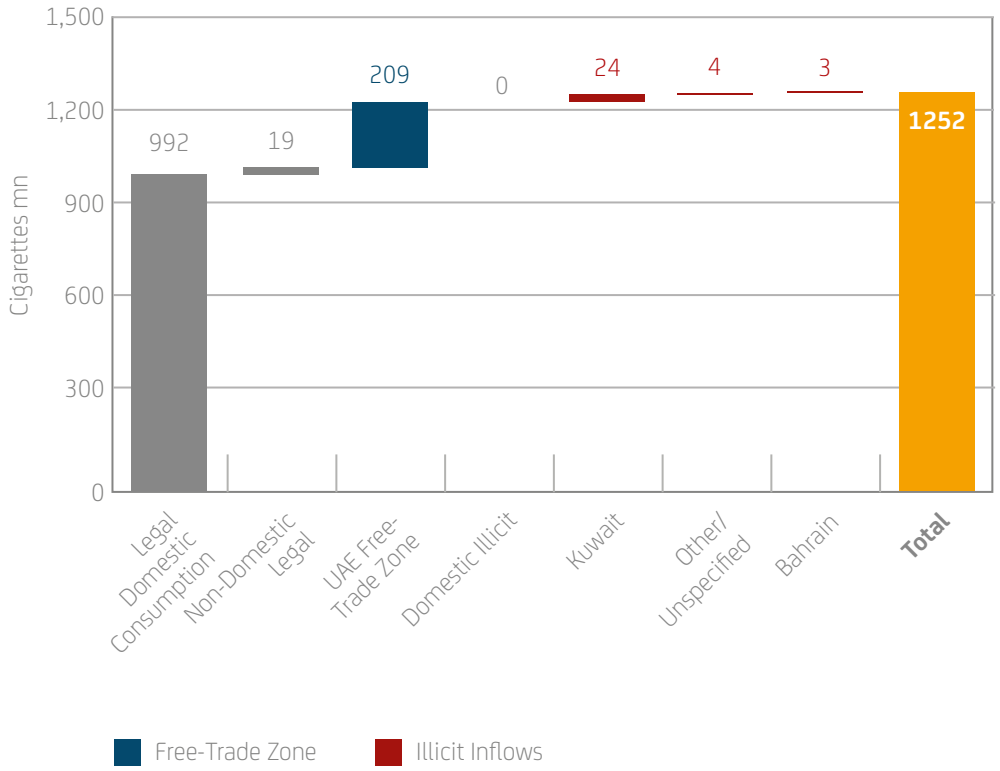
	Cigarettes mn	
	2016	2017
Bahrain	0.0	3.4
Kuwait	0.0	23.6
Duty-Free labelled products	0.2	0.0
Counterfeit	0.0	0.0
Other/Unspecified	5.1	4.3
Total	**5.3**	**31.2**

Source: IT Flows Model and Oxford Economics

[1]Estimated using passenger data, Smoking Prevalence in tourists' country/market of origin, and the duty-free personal import allowance limit.

[2]Unspecified Market Variant refers to cigarette packs that do not bear specific market labelling or Duty-Free labelling. As such the intended market is not known.

Oman: Consumption breakdown 2017



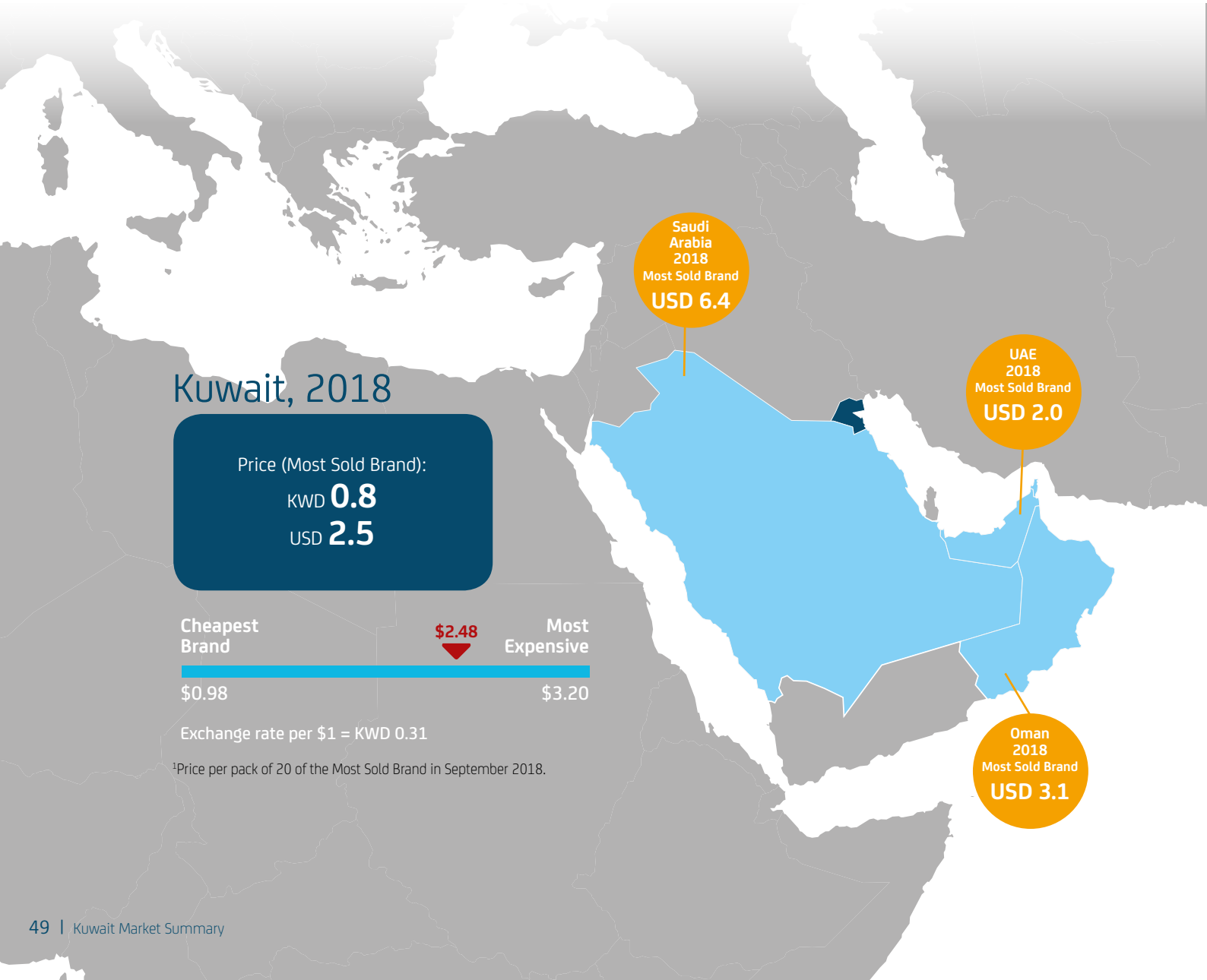
Source: Oxford Economics

Oman: Data Sources

	Primary source	Calculation	Comments
Outflows of domestic duty-paid cigarettes	Empty Pack Survey data in other markets covered in this Report.	Empty Pack Survey data in other markets used to identify the presence of packs bearing Oman market-specific labelling (e.g., health warnings, tax stamps, etc.).	Limited number of Oman Market Variant cigarettes identified in other markets covered in this Report.
Legal Domestic Consumption (LDC)	—	Legal Domestic Sales minus Outflows of legal sales.	Limited Outflows of duty-paid cigarettes, so Legal Domestic Sales and Legal Domestic Consumption closely aligned.
UAE Free Trade Zone cigarettes	Empty Pack Surveys, OE estimates.	Estimated using Empty Pack Survey shares of total consumption accounted for by brands found to be producing in UAE FTZ.	Cigarettes produced in UAE FTZ should pay all applicable taxes when entering either the UAE from FTZ or another GCC from FTZ. However, in light of uncertainty as to whether this is the case, we choose to classify these cigarettes separately from NDL and NDI.
Total Non-Domestic Inflows (ND)	—	Sum of Non-Domestic Legal, Non-Domestic Illicit, and UAE Free Trade Zone (FTZ) cigarettes.	—
Non-Domestic Legal (NDL)	—	Estimated using passenger data, smoking rates, and passenger duty-free personal import allowance.	Maximum theoretical amount an individual can carry across a border. Passenger data from the UNWTO and OE Tourism Model.
Non-Domestic Illicit	Empty Pack Survey.	Based on Empty Pack Survey plus OE estimates.	Estimates derived from 2016 Q4 and 2018 Q1 Empty Pack Surveys. See Report methodology for more details.
Domestic Illicit	EPS and industry intelligence.	Based on augmentation of retail audit.	Empty Pack Surveys do not identify any domestic illicit cigarettes in Oman. This is corroborated by industry anecdotal evidence.
Total Illicit Consumption	—	Sum of Non-Domestic Illicit and Domestic Illicit.	—
Total Consumption	—	Legal Domestic Sales minus Outflows of domestic duty-paid cigarettes, plus estimated Non-Domestic Legal consumption, plus consumption of UAE FTZ cigarettes, plus estimated Illicit Consumption.	The IT Flows Model estimate of consumption is 1.3 billion cigarettes for 2017.

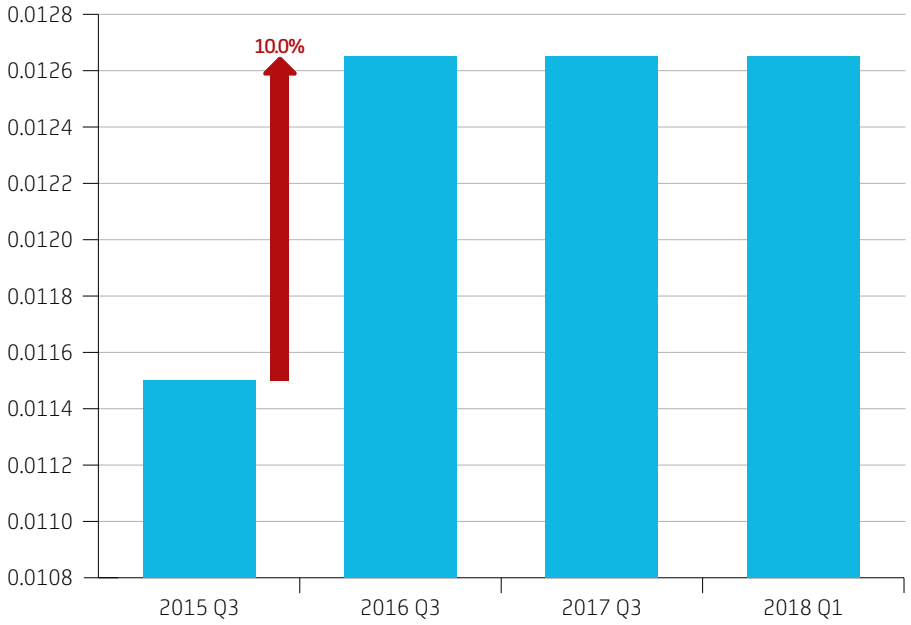
Kuwait: Legal Domestic Sales

- Legal Domestic Sales increased in 2017 and have risen every year since 2011.
- Kuwait was one of the first countries in the world to introduce a ban on smoking in public places, doing so in 1995. But "due to the lack of tobacco law enforcement, tobacco consumers were not deterred", according to the World Health Organisation. Enforcement was stepped up in 2016 though, with increased resources for monitoring, higher fines, and an additional ban on smoking in vehicles. All tobacco advertising is banned.
- Unlike Saudi Arabia and the UAE, Kuwait has not yet implemented the 100% Excise Tax on cigarettes. It does, however, apply the GCC-standard import duty of USD 27 per 1000 cigarettes (choosing not to increase this to USD 54 per 1000 as in Saudi Arabia and Oman in 2016). The Selective Tax Bill, which would implement 100% Excise Tax on tobacco products has been put before Parliament, but not yet approved.
- Cigarettes in Kuwait are the cheapest of the four countries covered in the GCC Illicit Tobacco Indicator report.[1] As of 2018 Q1, the Most-Sold Brand cost KWD 0.8 or USD 2.5 per pack of 20 cigarettes in Kuwait, with the same brand costing USD 3.1 in Oman, USD 5.7 in UAE, and USD 6.7 in Saudi Arabia.



[1]Price per pack of 20 of the Most Sold Brand in September 2018.

Kuwait: Tax yield applied to cigarettes[2]



Source: Oxford Economics

[2]Rate applied in July of each year to the Most Sold Brand in 2016 (Marlboro). This includes customs duty at the unit specific rate, excise tax and VAT, as applicable.

Kuwait: Cigarette Consumption

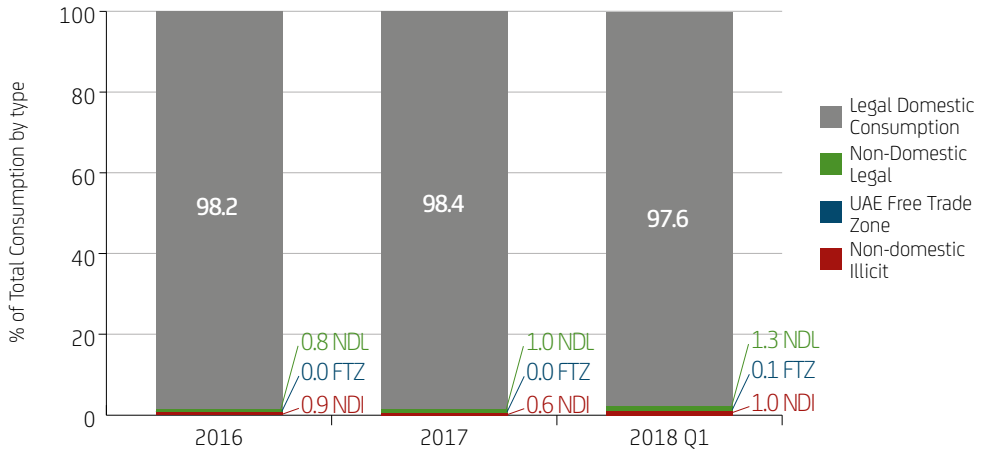
- Total Consumption (Legal, FTZ, and Illicit) is estimated to have risen to 6.0 billion in 2017 from 5.3 billion in 2016, an increase of 14.3%. Within this, just over 98% was accounted for by Legal Domestic Consumption. There has been a modest decline in the share of Legal Domestic Consumption in 2018 Q1, but at 97.6% the vast majority of Total Consumption is of legal domestic cigarettes and this share is higher than any other market in our study.
- Non-Domestic Legal accounts for around half of the remainder of Total Consumption. The consumption of Non-Domestic Legal cigarettes as a proportion of Total Consumption was estimated at 1.0% in 2017, 0.2pp higher than 2016. In 2018 Q1 the proportion of Non-Domestic Legal cigarettes increased to 1.3% of Total Consumption.
- We estimate that Illicit Incidence fell to 0.6% in 2017 from 0.9% in 2016, before increasing in 2018 Q1 to 1%. In volume terms, Illicit Consumption dropped to 33.2 million cigarettes in 2017 from 50 million cigarettes in 2016 - a fall of 6.3%.
- Non-Domestic Illicit inflows accounted for all of the Illicit Consumption in 2017, with no Domestic Illicit reported.
- In comparison to the other countries covered in this report, Kuwait consumes a far smaller proportion of UAE Free-Trade zone cigarettes. In both 2016 and 2017, there were effectively zero UAE Free-Trade zone cigarettes, while in the 2018 Q1 EPS this had increased to just 0.1% of Total Consumption.

Kuwait: Composition of cigarette consumption

	2016		2017		2018 Q1	
Population (million, 2018 are full-year estimates)	4.0		4.1		4.2	
Smoking prevalence (smokers as % of legal smoking age population)	43%		43%		43%[1]	
	Cigarettes bn	%	Cigarettes bn	%	%	% point change 2017-18
Legal Domestic Consumption (LDC)	**5,181.5**	**98.2**	**5,889.4**	**98.4**	**97.6**	**-0.8**
UAE Free-trade zone cigarettes	**-**	**-**	**2.2**	**0.0**	**0.1**	**0.1**
Total Non-Domestic Inflows (ND)	**94.0**	**1.8**	**94.0**	**1.6**	**2.3**	**0.8**
Non-Domestic Legal (NDL)	44.0	0.8	60.8	1.0	1.3	0.3
Non-Domestic Illicit	50.0	0.9	33.2	0.6	1.0	0.4
Domestic Illicit	**-**	**-**	**-**	**-**	**-**	**-**
Total Consumption	**5,275.5**	**100.0**	**5,985.6**	**100.0**	**100.0**	**-**
Total Illicit Consumption	**50.0**	**0.9**	**33.2**	**0.6**	**1.0**	**0.4**
Total Illicit and Free-trade zone consumption	**50.0**	**0.9**	**35.4**	**0.6**	**1.1**	**0.5**

Source: Oxford Economics
[1]September 2018

Kuwait: Composition of cigarette consumption (% of Total Consumption)



Source: Oxford Economics

Kuwait: Government Finances

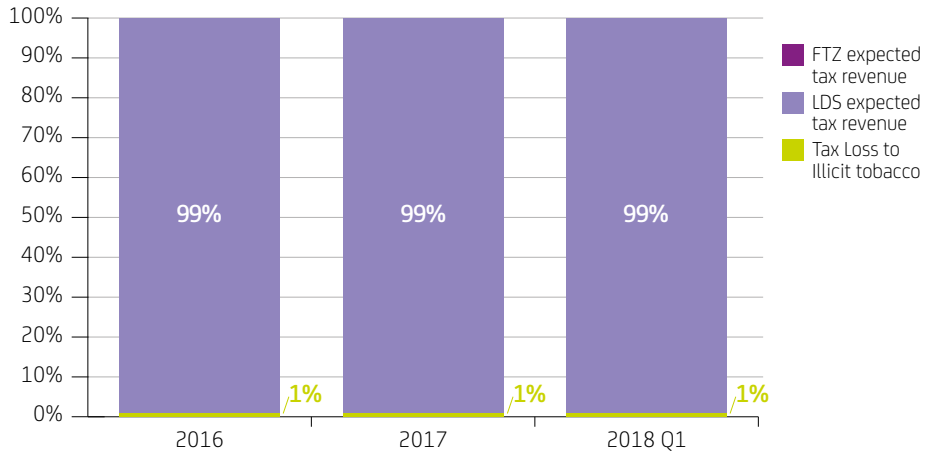
- As part of the GCC Kuwait operates a single tax system on cigarettes levying customs duty at 100% of the CIF price, with a minimum specific duty of $27 per 1000 cigarettes.
- Following agreement between the finance ministers of the GCC in 2015, the decision was taken in May 2017 by the General Secretariat of the GCC to impose 100% tax on cigarettes throughout the union. So far this tax has been implemented in the UAE, Saudi Arabia and Bahrain, with Oman and Kuwait expected to do so imminently, although no date has yet been set.
- Our estimates indicate that the Tax Loss associated with the Illicit Consumption of cigarettes in 2017 amounted to KWD 0.4 million (USD 1.2 million). This represents a decrease of 34.1% in comparison with 2016.
- With the illicit share of Total Consumption having risen to 1% in 2018 Q1 from an estimated 0.6% in 2017, it is likely both the nominal value the Tax Loss and Tax Loss as a proportion of total potential tobacco tax revenues will rise modestly in 2018 as a whole.

Kuwait: Expected tax revenue and estimated Tax Losses

	2016		2017		% change in local currency 2016-2017
	KWD mn	USD mn	KWD mn	USD mn	
Expected Tax Revenue on Legal Domestic Sales cigarettes	57.0	189.0	64.9	215.2	13.9
Expected Tax Revenue from UAE FTZ cigarettes	0.0	0.0	0.0	0.0	—
Estimated number of illicit cigarettes purchased (cigarettes mn)	50.0		33.2		-33.5
Estimated Tax Liabilities from UAE FTZ cigarettes	0.0	0.0	0.0	0.1	—
Estimated Tax Loss from Illicit Consumption	**0.5**	**1.8**	**0.4**	**1.2**	**-34.1**
Lost excise tax revenue	0.5	1.8	0.4	1.2	-34.1

Source: Oxford Economics, based on PMI data

Kuwait: Total Potential Tax Revenues by cigarette type, and estimated Tax Loss to Illicit Consumption

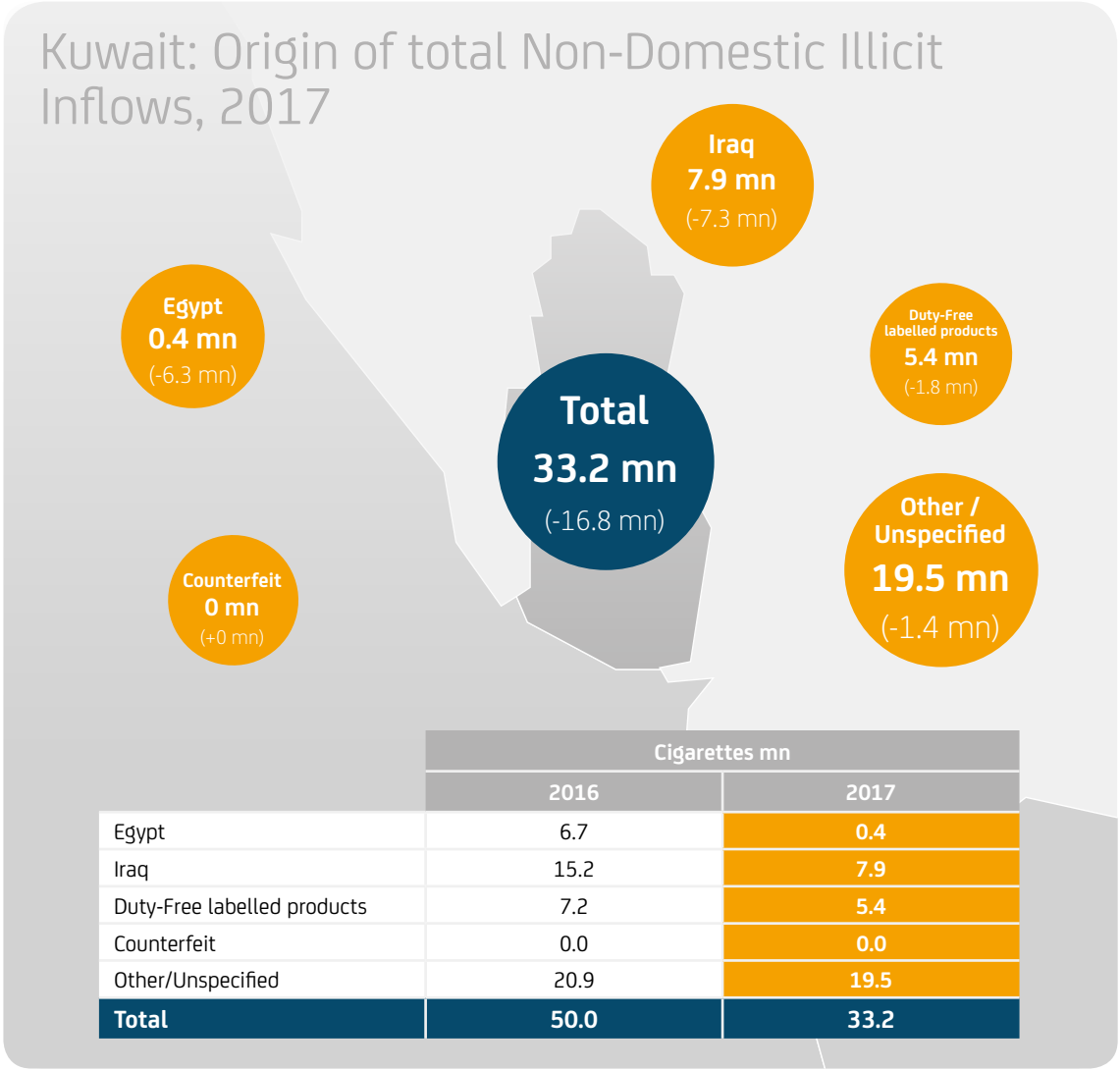


Source: Oxford Economics

Kuwait: Trade Flows

- Our estimates suggest that two-thirds of Non-Domestic cigarettes consumed in Kuwait in 2017 were Non-Domestic Illicit (61 million, out of a total of 94 million). We estimate just over 33 million Non-Domestic Illicit[1] cigarettes were consumed.
- Within this total, two-thirds of Non-Domestic Illicit are classified as Other/Unspecified[2] – although we estimate that there was a modest fall in volume in this category in 2017. The total volume of Non-Domestic Illicit cigarettes decreased by 33% in 2017, falling to 33 million from 50 million.
- Cigarettes from Iraq (7.9 million) and Egypt (0.4 million) are estimated as the highest country-specific sources of Contraband in 2017. As in other markets in this region, no counterfeit cigarettes were identified in Kuwait for any period covered in this study.
- As indicated by the presence of Kuwaiti designated cigarettes in the EPS surveys from the three other countries within this report, an increasing proportion of Kuwaiti Legal Domestic Sales are flowing out of the country. There were an estimated 68 million Kuwaiti variant cigarettes identified in Oman, Saudi Arabia and the UAE in 2017, up from a negligible volume in 2016. This was equivalent to 1.1% of Legal Domestic Sales in 2017.

Kuwait: Origin of total Non-Domestic Illicit Inflows, 2017



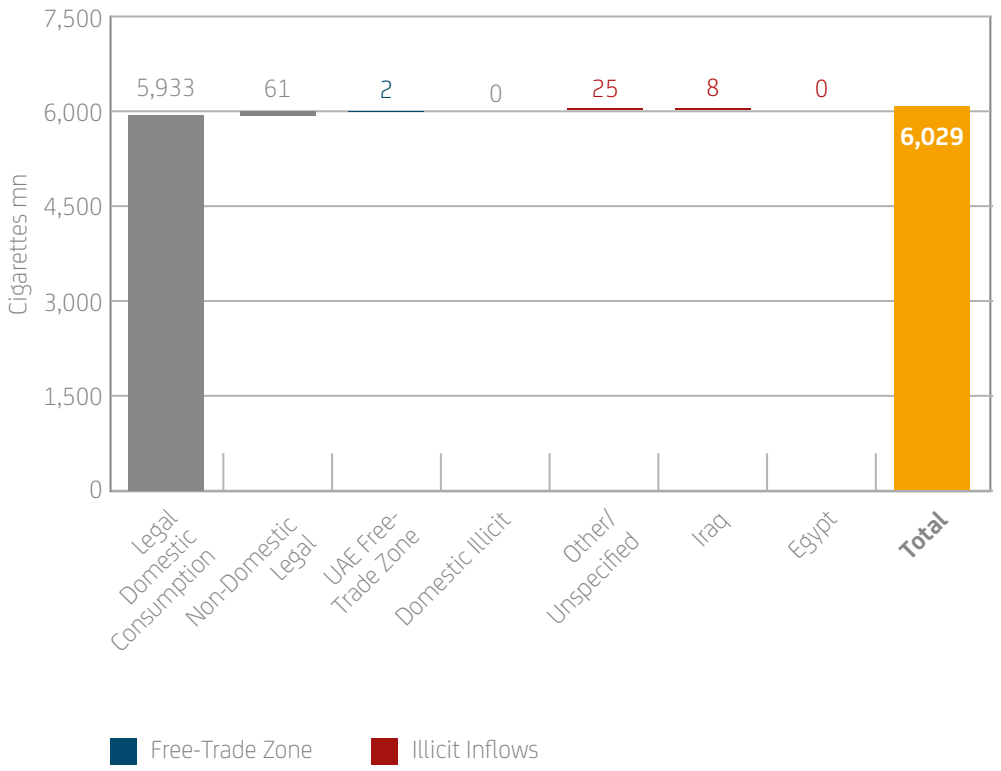
	Cigarettes mn	
	2016	2017
Egypt	6.7	0.4
Iraq	15.2	7.9
Duty-Free labelled products	7.2	5.4
Counterfeit	0.0	0.0
Other/Unspecified	20.9	19.5
Total	**50.0**	**33.2**

Source: IT Flows Model and Oxford Economics

[1]Estimated using passenger data, Smoking Prevalence in tourists' country/market of origin, and the duty-free personal import allowance limit.

[2]Unspecified Market Variant refers to cigarette packs that do not bear specific market labelling or Duty-Free labelling. As such the intended market is not known.

Kuwait: Consumption breakdown 2017



Source: Oxford Economics

Kuwait: Data Sources

	Primary source	Calculation	Comments
Outflows of domestic duty-paid cigarettes	Empty Pack Survey data in other markets covered in this Report.	Empty Pack Survey data in other markets used to identify the presence of packs bearing Kuwaiti market-specific labelling (e.g., health warnings, tax stamps, etc.).	Limited number of Kuwait Market Variant cigarettes identified in other markets covered in this Report.
Legal Domestic Consumption (LDC)	—	Legal Domestic Sales minus Outflows of legal sales.	Limited Outflows of duty-paid cigarettes, so Legal Domestic Sales and Legal Domestic Consumption closely aligned.
UAE Free Trade Zone cigarettes	Empty Pack Surveys, OE estimates.	Estimated using Empty Pack Survey shares of total consumption accounted for by brands found to be producing in UAE FTZ.	Cigarettes produced in UAE FTZ should pay all applicable taxes when entering either the UAE from FTZ or another GCC from FTZ. However, in light of uncertainty as to whether this is the case, we choose to classify these cigarettes separately from NDL and NDI.
Total Non-Domestic Inflows (ND)	—	Sum of Non-Domestic Legal, Non-Domestic Illicit, and UAE Free Trade Zone (FTZ) cigarettes.	—
Non-Domestic Legal (NDL)	—	Estimated using passenger data, smoking rates, and passenger duty-free personal import allowance.	Maximum theoretical amount an individual can carry across a border. Passenger data from the UNWTO and OE Tourism Model.
Non-Domestic Illicit	Empty Pack Survey.	Based on Empty Pack Survey plus OE estimates.	Estimate derived from the 2016 Q3 and 2018 Q1 Empty Pack Survey. See Report methodology for more details.
Domestic Illicit	EPS and industry intelligence.	Based on augmentation of retail audit.	Empty Pack Surveys do not identify any domestic illicit cigarettes in Kuwait. This is corroborated by industry anecdotal evidence.
Total Illicit Consumption	—	Sum of Non-Domestic Illicit and Domestic Illicit.	—
Total Consumption	—	Legal Domestic Sales minus Outflows of domestic duty-paid cigarettes, plus estimated Non-Domestic Legal consumption, plus consumption of UAE FTZ cigarettes, plus estimated Illicit Consumption.	The IT Flows Model estimate of consumption is 6.0 billion cigarettes for 2017.
Total Tax Loss	—	Total Illicit Consumption multiplied by the weighted average tax rates (Import Duty and Excise Tax).	See Report methodology for more details.

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