Federal Trade Commission

Report to Congress

For 1996

PURSUANT TO THE FEDERAL CIGARETTE

LABELING AND ADVERTISING ACT

ISSUED: 1998

PURPOSE

This report is the latest in a series on cigarette sales, advertising and promotion that the Federal Trade Commission (the Commission) has submitted annually to Congress since 1967 pursuant to the Federal Cigarette Labeling and Advertising Act:[1]

> The Federal Trade Commission shall transmit a report to the Congress . . . concerning (1) the current practices and methods of cigarette advertising and promotion, and (2) such recommendations for legislation as it may deem appropriate.[2]

INTRODUCTION

The statistical tables appended to this report provide information on domestic sales and advertising and promotional activity for U.S. manufactured cigarettes for the years 1963 through 1996.[3] The tables were compiled from raw data contained in special reports submitted to the Commission pursuant to compulsory process by the five major cigarette manufacturers in the United States: Brown & Williamson Tobacco Corporation, Liggett Group, Inc., Lorillard Tobacco Company, Philip Morris Incorporated, and R.J. Reynolds Tobacco Company.

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[1] Pub. L. No. 89-92, 79 Stat. 282 (1965), as amended by Pub. L. No. 98-474, 98 Stat. 2204 (1984) and by Pub. L. No. 99-92, § 11, 99 Stat. 393, 402-04 (1985), current version at 15 U.S.C. § 1331 (1994).

[2] 15 U.S.C.A. § 1337(b).

[3] The information in Tables 6C and 12, however, is provided only through 1995 because final 1996 data are not yet available. These two tables will be updated in the Commission's next report.

COMMISSION ACTIVITY

On May 28, 1997, the Commission issued an administrative complaint against the R.J. Reynolds Tobacco Company, alleging that the company's use of the "Joe Camel" campaign to promote Camel brand cigarettes violated Section 5 of the FTC Act.

On September 9, 1997, the Commission issued a notice requesting public comment on proposed revisions to the testing method used to determine the tar, nicotine and carbon monoxide ratings of cigarettes. The proposed methodology would require that each cigarette variety be tested under two different sets of smoking conditions, rather than the single set used under the current system. The proposed revisions to the test method would produce tar, nicotine and carbon monoxide yields using both the current testing parameters and more intensive smoking conditions, thus producing a range of potential yields for each cigarette. The Commission also requested comment on: (1) the feasibility of generating the upper tier of ratings through mathematical formulas, rather than actual testing on a smoking machine; and (2) the usefulness and feasibility of two different legends that could be used in advertising to disclose the ratings.

Also in September 1997, staff members of the Bureaus of Economics, Competition and Consumer Protection submitted a report entitled "Competition and the Financial Impact of the Proposed Tobacco Industry Settlement" to the Congressional Task Force on Tobacco and Health. The report examined the likely effect on cigarette prices and cigarette company profits of the proposed global tobacco settlement agreement.

DISCUSSION OF THE DATA

Table 1 displays annual cigarette sales by manufacturers to wholesalers and retailers. In 1996, the major domestic cigarette manufacturers sold 484.1 billion cigarettes domestically, which is 1.9 billion more cigarettes than they sold in 1995. This 0.4 percent increase from the 1995 level contrasts with a 1.6 percent decrease in sales in 1995. Except for 1994 and 1996, cigarette sales have declined every year since 1985.

The Commission's two most recent reports to Congress noted that the volatility in cigarette sales by manufacturers in recent years reflected in Table 1 was not seen in the cigarette consumption series produced by the U.S. Department of Agriculture (USDA). Differences between the FTC and USDA series may reflect changes in inventory holdings by cigarette wholesalers and retailers. Shifts in inventories can influence the numbers of cigarettes sold annually by cigarette manufacturers to wholesalers and retailers, which is the statistic reported to the FTC and traditionally published in Table 1 of the annual cigarette report. In contrast, year-to-year changes in inventories are not reflected in the USDA data, which are based on an estimate of the number of cigarettes actually sold to consumers. To enable easy reference to both sets of figures, Table 1 has been revised this year by the addition of the U.S. Department of Agriculture's cigarette consumption estimates for the years 1963 through 1996.

Table 2 shows U.S. adult per capita cigarette sales per year, and is generated by dividing manufacturers' sales to wholesalers and retailers by the U.S. adult population. Based on the data reported to the Commission by the manufacturers, per capita sales declined from 2,482 in 1995 to

2,467 in 1996, a decrease of 0.6 percent, or 15 cigarettes per person. Per capita sales had decreased 2.5 percent, or 64 cigarettes, from 1994 to 1995.

Tables 3 through 3E show the amounts spent on cigarette advertising and promotion for the years 1970, and 1975 through 1996.[4] These tables break out the amounts spent on the different types of media advertising (e.g., newspapers and magazines) and sales promotion activities (e.g., distribution of cigarette samples and specialty gift items) and also give the percentage of the total amount spent for the various types of advertising and promotion.

Table 3E shows that overall, $5.1 billion was spent on cigarette advertising and promotion in 1996, an increase of 4.3 percent from the $4.9 billion spent in 1995. Spending has increased every year since 1987, except for a $1.2 billion decrease in 1994.

Newspaper advertising expenditures decreased 26.4 percent between 1995 and 1996, from $19.1 million to $14.1 million; this advertising category accounts for less than one-half of 1 percent of all expenditures. Although newspaper spending accounted for 23.1 percent of total expenditures in 1981, it has accounted for less than 1 percent of expenditures since 1992.

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[4] The reported figures include all advertising, merchandising, and promotional expenditures related to cigarettes, regardless of whether such advertising would constitute "commercial speech" or would be protected from law enforcement action under the First Amendment. The Commission began requiring tobacco companies to include expenditures for such protected speech in 1989.

A total of $243.0 million was spent on magazine advertising in 1996, a decrease of 2.3 percent from 1995. Magazine advertising represented 4.8 percent of total spending. Spending on magazine advertising peaked in 1984, when the cigarette companies reported spending $425.9 million (20.3 percent of total 1984 advertising and promotional expenditures).

Spending on outdoor advertising totaled $292.3 million in 1996, an increase of $18.6 million from 1995, when $273.7 million was spent. In 1996, outdoor advertising expenditures comprised 5.7 percent of total advertising and promotional spending, down from a high of 15.5 percent in 1983.

Spending on transit advertising rose from $22.5 million in 1995 to $28.9 million in 1996, an increase of 28.0 percent. This contrasts with a 23.1 percent decrease from 1994 to 1995. This category, like newspapers, accounts for only about one-half of 1 percent of all expenditures.

Spending on point of sale promotional materials declined by $6.4 million (2.5 percent) from 1995 ($259.0 million) to 1996 ($252.6 million). Point of sale advertising accounted for 4.9 percent of total advertising and promotion in 1996. These expenditures peaked in 1993 at $401 million.

Promotional allowances were $2.15 billion in 1996, up 15.3 percent from $1.87 billion in 1995. Since 1990, spending on promotional allowances has more than doubled. In 1996, these expenditures accounted for 42.1 percent of the total advertising and promotion expenditures. As in 1994 and 1995, this was the largest category of advertising and promotional expenditures.

Money spent giving cigarette samples to the public ("sampling distribution") rose from $13.8 million in 1995 to $15.9 million in 1996, an increase of 15.2 percent. Sampling expenditures remained well below their pre-1994 levels, however: slightly more than $100 million was spent in 1990 and just over $40 million in 1993. Cigarette sampling distribution accounted for only 0.3 percent of the total spent on advertising and promotion in 1996; these expenditures reached a high of 7.9 percent of the total spent on advertising and promotion in 1982.

In 1996, $544.3 million was spent on specialty item distribution through the mail, at promotional events, or by any means other than at the point-of-sale with the purchase of cigarettes.[5] (Specialty items distributed along with the purchase of cigarettes were redesignated as retail value added expenses beginning in 1988.) Specialty item distribution expenditures declined $120.8 million (18.2 percent) from 1995, and accounted for 10.7 percent of total advertising and promotional expenditures in 1996.

Spending on public entertainment increased by $60.5 million from 1995 to 1996 (54.7 percent). With expenditures reported at $171.2 million, public entertainment accounted for 3.4 percent of total advertising and promotion expenditures in 1996, the most it has been since 1983, when it accounted for 4.0 percent of the total.

[5] Specialty item advertising is the practice of branding items such as T-shirts, caps, sunglasses, key chains, calendars, lighters and sporting goods with a brand's logo, and then giving them away or selling them to consumers.

The cigarette companies reported a total of $38.7 million for direct mail advertising in 1996, an increase of $4.1 million (11.8 percent) from the $34.6 million reported in 1995. This category does not include direct mail containing coupons. Coupons sent via direct mail have been reported in the coupon and retail value added category since 1988.

All reporting companies indicated that no money had been spent on endorsements and testimonials for cigarettes in 1996. No expenditures have been reported in this category since 1988.

Coupons and retail value added promotions expenditures fell slightly in 1996, declining from $1.35 billion to $1.31 billion, a decrease of 2.9 percent. Spending on coupons and retail value added had dropped sharply from 1993 to 1994, and then increased slightly in 1995. This category includes cents-off coupons, multiple pack promotions and retail value added offers.[6] The cigarette companies were first asked to report these expenses as a distinct category in 1988, when $874 million was spent.

In 1996, the Commission began collecting data from the major domestic cigarette manufacturers on expenditures related to cigarette advertising on the Internet. In 1996, the companies reported spending $432,000 on Internet advertising, which is less than 0.01 percent of all advertising and promotional expenditures for 1996. This category includes the Internet, World Wide Web, and commercial on-line services.

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[6] Multiple pack offers are additional packs of cigarettes that are given free with cigarette purchases, such as "buy one, get one free." Retail value added offers include non-cigarette items, such as key chains or lighters, given away at the point of sale with the purchase of cigarettes.

The Commission collects expenditure information in two categories that do not appear as line items on the charts because they may span several categories. In 1988, the Commission began requiring the cigarette companies to state separately the amount of money spent on sports and sporting events. For 1996, the major domestic cigarette companies reported that they spent $85 million on sports and sporting events,[7] an increase of $2 million from 1995.

In 1989, the Commission began requiring the cigarette companies to declare whether any money or other form of compensation had been paid to have any cigarette brand names or tobacco products appear in any motion pictures or television shows. This practice has been reported as unfunded since 1989.

The data on cigarette advertising and promotional expenditures reported in Tables 3 through 3E were not collected in their present form until 1975. Therefore, Tables 4 and 5, which report cigarette advertising expenditures from 1963 through 1974 and 1970 through 1974, respectively, have been retained in the report for comparative purposes.

Tables 6 through 6C give the domestic market share of, and the percentage of total cigarette advertising expenditures devoted to, cigarettes with tar ratings of 15 milligrams (mg.) or less for the

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[7] This includes expenditures for: (1) the sponsoring, advertising or promotion of sports or sporting events; support of an individual, group, or sports team; and purchase of or support for equipment, uniforms, sports facilities and/or training facilities; (2) all expenditures for advertising in the name of the cigarette company or any of its brands in a sports facility, on a scoreboard, or in conjunction with the reporting of sports results; and (3) all expenditures for functional promotional items (clothing, hats, etc.) connected with a sporting event.

years 1967 through 1995. The data are broken down into separate categories according to tar ratings of less than 3, 6, 9, 12, and 15 mg. (categories are presented cumulatively). As noted supra, 1996 data were not available when the Commission issued this report.

As shown in Table 7, filtered cigarettes have dominated the market since the Commission began collecting this information in 1963, rising from 58 percent at that time to 97 percent in 1992. The market share of filtered cigarettes remained constant in 1996 at 97 percent. Table 8 shows that the cigarette companies have reported a close correlation between advertising and promotion expenditures and domestic market share for filter cigarettes in recent years.

Table 9 provides the domestic market share of the various cigarette length categories. The King-size (79-88 mm) category continues to be the biggest seller, with 57 percent of the market. This category is followed by the Long (94-101 mm) group, which held 40 percent of the market in 1996. Regular (68-72 mm) and Ultra-Long (110-121 mm) cigarettes continued to account for 1 percent and 2 percent, respectively, of the market in 1996.

Tables 10 through 10B provide the domestic market share and percentage of total advertising and promotional expenditures devoted to Long and Ultra-Long cigarettes from 1967 through 1996. In 1996, the market share of longer cigarettes and the percentage of total advertising and promotional expenditures devoted to those cigarettes both remained constant at 42 percent.

Table 11 gives the market share of menthol and non-menthol cigarettes. In 1996, the market share of menthol cigarettes remained at 25 percent, while non-menthols held 75 percent of the market.

In 1994, the Commission began requiring the cigarette companies to indicate whether "tar" and nicotine ratings were displayed on cigarette packaging and advertising. Table 12 shows that cigarette varieties that printed tar and nicotine ratings on their packs represented only 6.1 percent of the overall market in both 1994 and 1995. Table 12 also shows: (1) the percentage of the overall cigarette market represented by varieties with different tar ratings, and (2) within each tar group, the market share of those varieties that disclose tar and nicotine ratings on their packs. As noted supra, 1996 data were not available when the Commission issued this report.