The Beedi Industry of Sri Lanka

The Sri Lankan beedi industry has been a subject of concern due to its disproportionately low taxation compared to other tobacco products. Our ongoing research aims to shed light on the significant disparity in tax contributions between legal cigarettes and beedis in the tobacco market of Sri Lanka. The data from 2022 reveals an alarming tax gap, where the tax revenue generated from beedi falls far short of their substantial market volume. Furthermore, the rampant smuggling of tendu leaves, used for the majority of beedi production, exacerbates this issue, leading to a potential loss of billions in Government revenue.

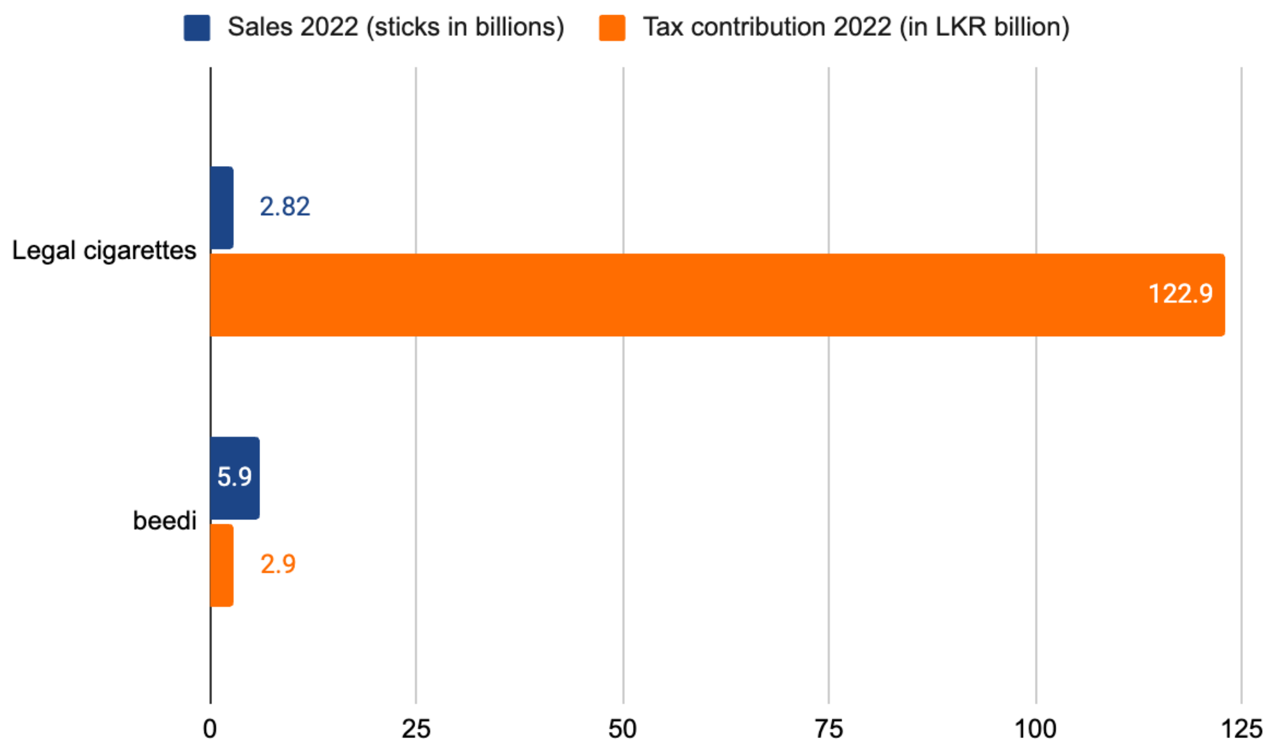
The beedi industry has emerged at a 6 year CAGR of 10% from 2017-2023

The Sri Lankan beedi industry has its roots dating back to 1956, nurtured by successive generations that have combined locally grown tobacco with imported tendu leaves to craft these products. According to the Excise Department of Sri Lanka, there are 590 registered beedi manufacturers. In 2023 alone, beedi consumption in Sri Lanka reached a staggering 6.51 billion sticks, commanding a substantial 67% share of the tobacco products market. Some estimates suggest that 62% of the beedi market in Sri Lanka relies on smuggled tendu leaves, amounting to approximately 4.1 billion sticks. Smugglers engage in a sophisticated operation by smuggling tendu leaves from India via sea routes and subsequently rolling the beedi within Sri Lanka's borders. This illicit trade undermines legal channels and contributes to the country's revenue loss.

Upward trend in beedi consumption emerging amidst an under-taxed environment

Based on the 2022 data, legal cigarette sales in Sri Lanka amounted to 2.82 billion sticks, contributing a tax revenue of LKR 122.9 billion. By stark contrast, the sales volume of beedi reached 5.9 billion sticks, more than twice the volume of legal cigarettes. However, the estimated Government tax revenue contribution from the beedi industry at a meager LKR 2.9 billion. When considering the entire tobacco market, the Government revenue from beedi accounts for a mere 2% of the total whilst 98% of total tax is from the legal cigarette industry, highlighting a significant taxation imbalance. Figure 1 exhibits the estimated disproportionate tax contribution existing in the tobacco market of Sri Lanka for the calendar year 2022.

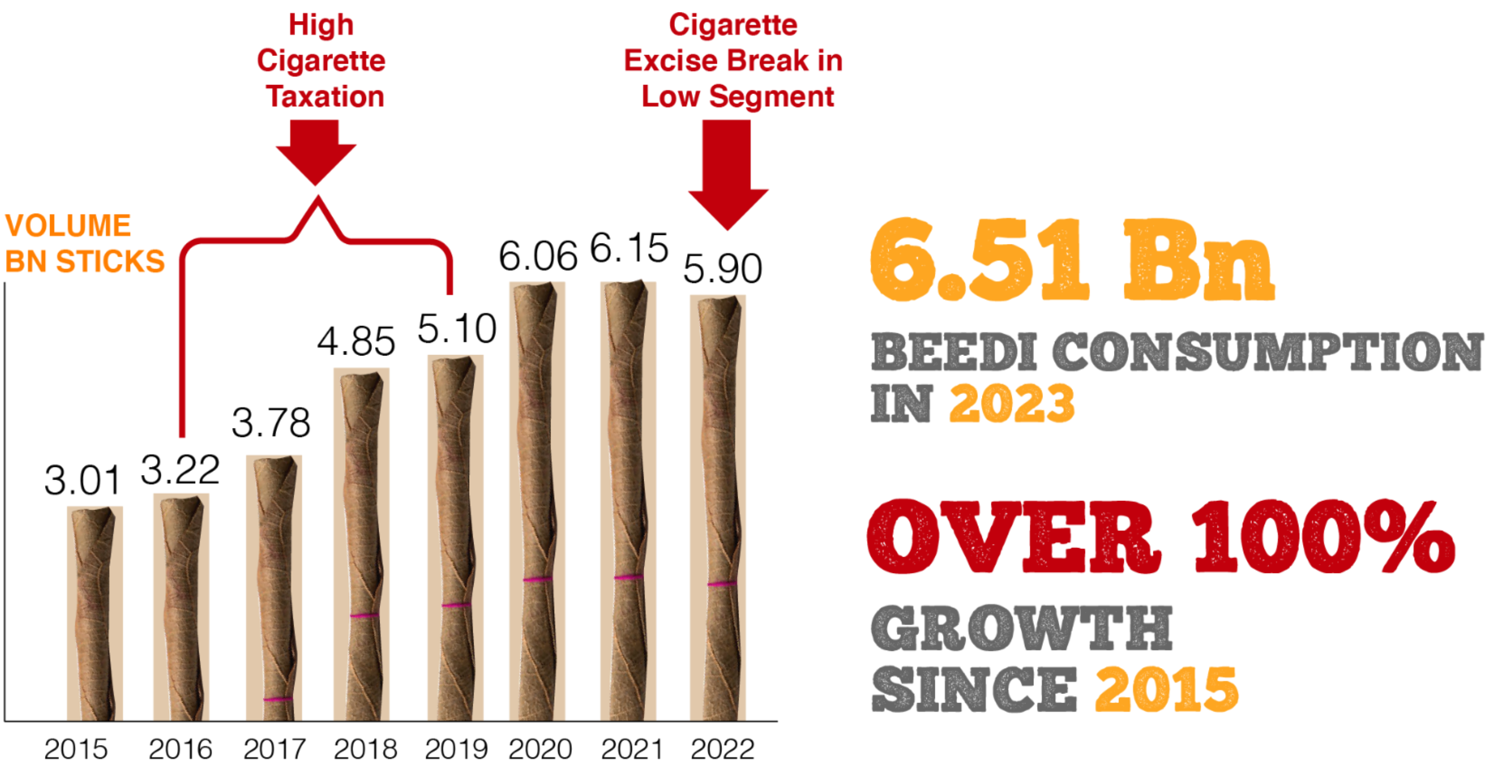
Figure 1: Sales and Government tax revenue contribution in the tobacco industry (2022)



Source: RIUNIT calculations

The below infographic (figure 2) perfectly captures the landscape of the beedi industry. From 2016-2019, the industry has grown at an annual average rate of 16.57%. The underlying reason was attributed to the excise tax hikes which came into effect in the 4th quarter of 2016. The growth in consumption of beedi was mainly due to the shift from the 59mm legal cigarette, Capstan, where the excise tax share per stick rose by 67.38% in 2016 following the tax revision. Thereafter an exponential growth was visible in the beedi industry. The tax revision which came to effect from the 1st January 2023, increased excise on the 59mm tier by 98%. As a result, the beedi consumption will further aggravate.

Figure 2: The beedi industry at a glance



According to our understanding of how the tobacco market behaves, and the substitution impact of beedi on cigarette consumption, we expect a hike in beedi consumption this year

According to an ongoing research by RIUNIT, beedi sales are expected to grow by over 10.36% in the year 2023. If this projection holds true, it will further exacerbate the existing tax gap and widen the revenue loss for the Government.

State revenue to lose approximately 19Bn in 2023 due to beedi smuggling

The growth of the illicit beedi market in Sri Lanka has resulted in substantial revenue loss for the Government. The fiscal losses to the Government could be as high as a staggering LKR19 bn in 2023 as a direct consequence of smuggling of tendu leaves. This untapped revenue source holds the key to managing the country's fiscal deficit and is vital for ensuring optimal fiscal outcomes and the provision of high-quality services to its citizens. This ongoing study by the Research Intelligence Unit (RIUNIT) is expected to be completed in Q3 2023 and the final report is to be released in Q3 2023.

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