



# ERS *Report Summary*

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## Policy Reform in the Tobacco Industry: Producers Adapt to a Changing Market

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### *What Is the Issue?*

Prior to the 2004 tobacco buyout, burley and flue-cured tobacco producers operated under a system of quotas and price supports that kept tobacco prices artificially high by limiting tobacco production. The Fair and Equitable Tobacco Reform Act of 2004 (or tobacco buyout) changed the tobacco policy in the United States by eliminating quotas and price supports, while providing buyout payments to quota owners and growers. Without tobacco quotas, producers were freed from tobacco planting restrictions that limited the amounts and types of tobacco that could be marketed in a geographic region. While changes in tobacco policy gave producers the freedom to plant as much tobacco as they wished, they were also exposed to increased market and price risks, ultimately impacting their ability to adapt to current market conditions.

### *What Did the Study Find?*

- Flue-cured tobacco producers made greater changes in their tobacco operations than burley tobacco producers in the first 4 years after the buyout by increasing their tobacco acreage more and investing more in their tobacco operations.
- Producers who continued to grow tobacco after the buyout farmed more tobacco acreage per farm in 2008 than they did in 2004. Flue-cured tobacco producers increased their tobacco acreage per farm by 30 acres, or 50 percent, between 2004 and 2008, while burley tobacco producers increased their tobacco acreage per farm by 3.6 acres, or 26 percent.
- Tobacco acreage per farm is expected to rise through 2013. Producers who intend to plant flue-cured tobacco in 2013 plan to plant 115 acres of tobacco per farm while burley producers expect to plant 20 acres of tobacco per farm. Much of the expected rise in tobacco acreage per farm is attributed to the exit of smaller scale tobacco producers prior to 2013 since the total tobacco acreage for burley and flue-cured tobacco is anticipated to remain roughly the same in 2013 as in 2008.
- Flue-cured tobacco producers were more likely than burley tobacco producers to make capital investments in their tobacco operations. The principal reasons for investing were to improve production efficiency, handle the expansion in tobacco acres, and replace machinery, equipment, and buildings.
- As producers increased their tobacco acreage per farm, they became more sensitive to fluctuations in the availability and cost of hired labor. Tobacco producers reported that it takes an average of 72 labor hours per acre to produce flue-cured tobacco for market and 151

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labor hours per acre for burley. Hired labor accounts for the majority of tobacco labor, with flue-cured tobacco producers more dependent on migrant labor than burley producers due to the larger size of flue-cured operations.

- Tobacco producers are using marketing contracts to manage the increased marketing risk. Without auction houses or guaranteed buyers, most tobacco producers are now marketing their tobacco under a marketing contract. However, producers are exposed to market risk if buyers should choose not to renew contracts, as most contracts last for 1 year.

### ***How Was the Study Conducted?***

The authors of this report used data collected from the tobacco version of the 2008 Agricultural Resource Management Survey (ARMS). The ARMS is a detailed, annual survey of farm businesses and associated households conducted jointly by the U.S. Department of Agriculture's Economic Research Service (ERS) and National Agricultural Statistics Service (NASS). The tobacco version of the survey focused only on producers of either burley or flue-cured tobacco in 2008. To track the adjustments made by the 2008 tobacco producers, growers were asked to report on their tobacco operations in 2000, 2004, and 2008. Therefore, the ARMS data presented in this paper for 2000 and 2004 are not representative of all tobacco producers in those years, since those who exited tobacco farming before 2008 were not included in the survey. Tobacco producers in Kentucky, Tennessee, and North Carolina, where the majority of burley and flue-cured tobacco production occurs, were included in the survey.