The Cost of Cigarette Tax Rate Freeze in Pakistan

POLICY BRIEF
June | 2025

- Excise tax rates on cigarettes have not increased since February 2023, which has profound negative implications for public health outcomes and government revenues.
- From March 2023 to May 2025:
  - The real tax rates have effectively decreased – e.g. from Rs 101 to Rs 84 per pack for low-priced brands,
  - The inflation-adjusted price of the most sold brand has declined from Rs 221 to Rs 200 per pack, and
  - The average share of the Federal Excise Duty in the retail price has fallen from 56% to 54%.
- Had the tax rates been adjusted to inflation in 2024-25 and 2025-26, it would have resulted in:
  - A 3% reduction in cigarette consumption,
  - 209,000 fewer smokers and over 215,000 lives saved, and
  - Additional revenue of Rs 97 billion.

Introduction

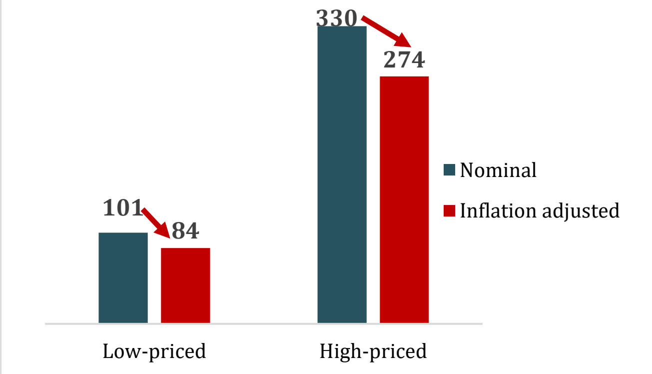
The government of Pakistan has been making consistent efforts to reduce the fiscal deficit over the past few years, with taxation playing a central role in its broader fiscal strategy. Resource mobilization through improved tax collection and policy reforms has been emphasized as a means to ensure sustainable public financing. However, the absence of progress on tobacco taxation stands out as a major shortcoming.

Despite its proven potential to generate significant revenue and reduce tobacco consumption—thereby improving public health—the rates of the Federal Excise Duty (FED) on cigarettes have remained unchanged since February 2023. Although public health advocates anticipated and strongly recommended a tax increase for the upcoming fiscal year (2025-26), the government ultimately decided to freeze the existing FED rates, missing a vital policy opportunity. This continued policy inaction has profound negative implications for tax revenue and health outcomes.

Tax rates have effectively decreased

The FED on cigarettes is structured around two pricing tiers: economy (low-priced) brands are taxed at Rs 101 per 20-stick pack, while premium (high-priced) brands are taxed at Rs 330 per pack. Since the excise tax rates are fixed amounts, their real value has decreased over the past two years due to inflation. As shown in Figure 1, the inflation-adjusted value of tax rates has declined from Rs 101 to Rs 84 for low-priced brands, and from Rs 330 to Rs 274 for high-priced brands. These values will be further reduced by 7.7% by the end of 2025-26, as per the inflation projected by the government.

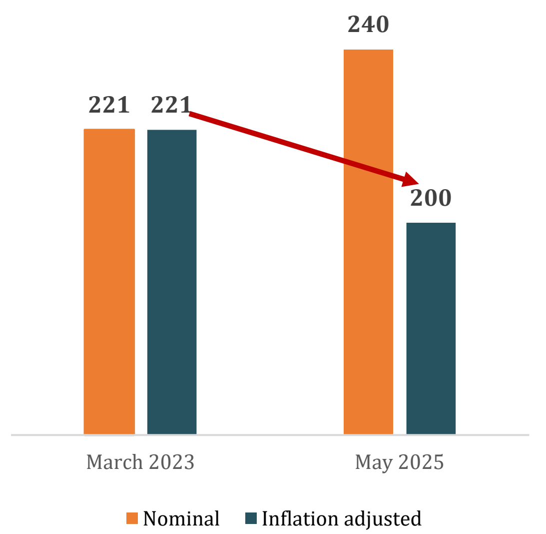
Figure 1: Nominal and real FED Rates, March 2023 - May 2025, Rs/pack



Real prices of cigarettes have declined

Cigarettes have effectively become cheaper and more affordable over the past two years due to stagnant excise tax rates and rising inflation. Although the nominal prices of cigarettes have increased between March 2023 and May 2025, this increase has not kept pace with the overall inflation rate. As a result, the real or inflation-adjusted price of cigarettes has fallen significantly. Figure 2 illustrates this trend clearly: while the nominal market price of the most sold cigarette brand rose from Rs 221 to Rs 240 per 20-stick pack, the real price, when adjusted for inflation, actually declined to Rs 200 per pack.

Figure 2: Market price of the most sold brand, Rs/pack

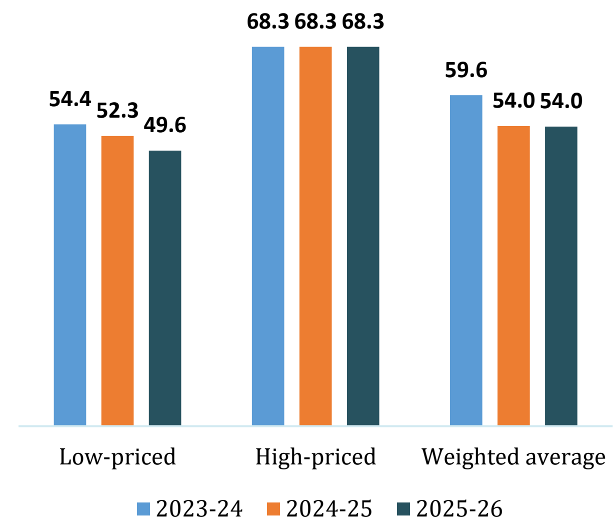


The FED share in retail prices has fallen

The share of excise tax in retail price continues to remain below the widely accepted international benchmark of 70%, particularly for economy brands, and has actually declined since 2023-24.

As shown in Figure 3, the FED share in the average retail price of economy brands has fallen from 54.4% in 2023-24 to 52.3% in 2024-25, and is projected to decline further to 49.6% in 2025-26. The share in the case of premium brands is almost stagnant. The weighted average of both brand categories reflects that the FED share would fall from 59.6% in 2023-24 to 54% in 2025-26.

Figure 3: Share of FED in retail prices (%)



The health and revenue implications of the tax freeze are significant

Figure 4 illustrates the estimated health and revenue consequences of maintaining the current cigarette excise tax rates, based on a tax simulation model developed by the Social Policy and Development Centre (SPDC). Taking a conservative approach, the simulations assume a minimum increase in tax rates and explore the potential outcomes if the FED rates for 2024-25 and 2025-26 had been adjusted in line with actual or projected inflation during those years.

Figure 4: Cost of tax rate freeze since 2023-24
Simulation: If the FED rates were adjusted to inflation in 2024-25 and 2025-26.

	Cumulative Effect
Consumption and health effects	
Change in:	
Total consumption (million sticks)	-3,189
The number of adult smokers	-208,944
The number of future smokers	-285,173
The number smoking-attributable deaths	-215,717
Revenue effect (Rs in million)	
Change in:	
FED revenue	84,009
GST revenue	13,112
Total revenue	97,121

The estimates show a significant decline in cigarette consumption and the number of adult smokers if inflation-adjusted tax increases had been implemented. Specifically, cigarette consumption would have decreased by 3.19 billion sticks over two years, approximately equivalent to a 3% reduction in total consumption. In terms of public health impact, there would have been about 209,000 fewer smokers and over 215,000 lives saved (through a reduction in premature smoking-attributable deaths). In addition, the government could have generated additional revenue of Rs 97 billion, including Rs 84 billion from the FED and Rs 13 billion from sales tax.

Recommendations

Regularly adjusting the Federal Excise Duty (FED) rate for inflation would support the government's efforts to curb tobacco consumption and reduce tobacco-related illness, death, and economic burden. Such adjustments represent the minimum necessary to preserve the real value of tax rates over time. Increasing cigarette taxes would also help Pakistan fulfil its commitments under the WHO Framework Convention on Tobacco Control (FCTC), while simultaneously boosting government revenue—an important step toward addressing the fiscal deficit.

This research is funded by the Economics for Health team (formerly Tobacconomics) at Johns Hopkins University (JHU). JHU is a partner of the Bloomberg Philanthropies' Initiative to Reduce Tobacco Use. The views expressed in this document cannot be attributed to, nor can they be considered to represent, the views of JHU or Bloomberg Philanthropies.

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