

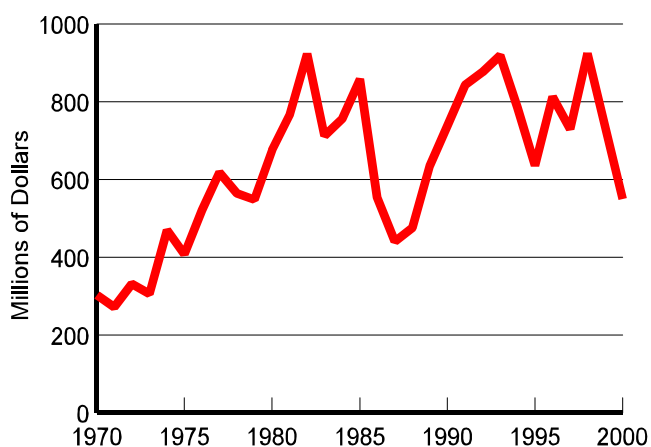


OVERVIEW OF KENTUCKY'S TOBACCO ECONOMY

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Tobacco has historically been a very important component of the Kentucky agricultural economy and culture. For generations, tobacco has played a key role in sustaining small family farms and enhancing many rural economies throughout the Commonwealth. However, as we enter the 21st century, the tobacco industry is in the midst of considerable change in response to political, economic, and legal challenges facing the tobacco sector. Current and anticipated changes in tobacco policy, marketing, and regulation will undoubtedly affect the future structure of the Kentucky tobacco economy. Nevertheless, tobacco is expected to remain a very important enterprise for many Kentucky farmers. This fact sheet provides an overview of the Kentucky tobacco economy and discusses the potential implications of the changing tobacco environment on the Kentucky agricultural economy.

Kentucky Tobacco Cash Receipts



- Kentucky tobacco cash receipts (sales) averaged over \$800 million during the decade of the 1990s, compared to \$680 million during the 1980s, and \$434 million during the 1970s. In 1998, Kentucky tobacco cash receipts reached a record high of more than \$900 million.

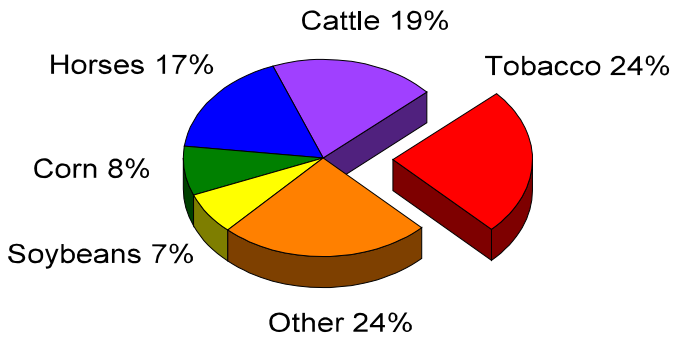
However, a multitude of adverse factors, including declining domestic cigarette sales, reduced leaf exports, movement of cigarette production overseas, and increasing imports have significantly reduced U.S. tobacco demand in recent years. Consequently, Kentucky tobacco cash receipts may be in the neighborhood of \$500 to \$600 million for the immediate future.

- Kentucky farmers grow three “types” of tobacco. Burley tobacco, comprising over 90% of total production, is grown in 117 of Kentucky’s 120 counties and is primarily used in cigarettes. Dark fire-cured and dark air-cured production is concentrated in 33 western Kentucky counties and is predominately used in smokeless tobacco products such as snuff, chewing, and pipe tobacco. While tobacco is grown in more than 100 nations, Kentucky’s burley and dark tobaccos are considered to be the world’s premium quality leaf.

- Kentucky is the nation’s largest producer of burley tobacco and dark fire and air-cured tobaccos. While North Carolina is the nation’s leading overall tobacco-producing state, Kentucky is the most tobacco-dependent state. According to the USDA, 17 of the United State's 20 most tobacco-dependent counties are in Kentucky. Many of these counties are located in regions with limited alternative farm and off-farm income opportunities.

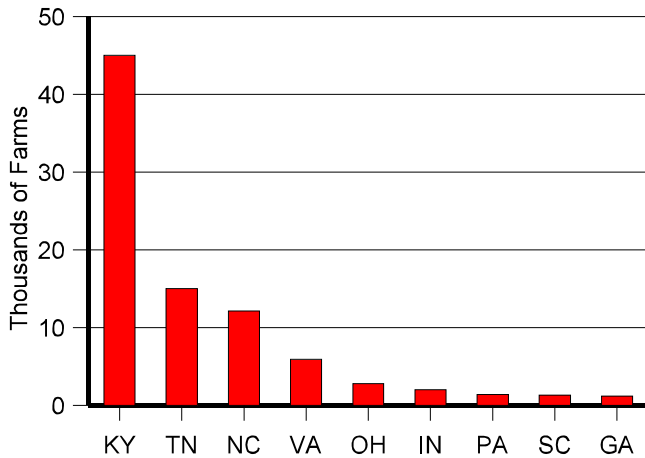
- Historically, tobacco has accounted for 40% to 50% of Kentucky’s annual crop receipts and 20% to 25% of Kentucky's total agricultural cash receipts, despite using only one percent of the farmland in Kentucky. The latest Census of Agriculture (1997) revealed that tobacco accounted for 36% of the net cash return from agricultural sales in Kentucky. Recently horses and cattle have surpassed tobacco as the leading farm enterprises.

Kentucky Ag Cash Receipts (1990-1999)



- Kentucky agriculture is noted for its small family farms. Kentucky currently possesses the fourth largest number of farms in the United States. According to the latest (1997) Census of Agriculture, nearly 45,000 of Kentucky's 82,000 farms grow tobacco. This represents almost 50% of the total number of farms growing tobacco in the United States. Tobacco accounts for more than 50% of the total ag sales for 34,000 of Kentucky's 45,000 tobacco farms.

U.S. Tobacco Farms by State

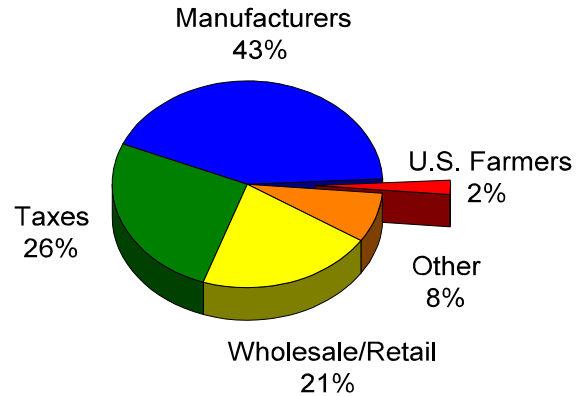


- U.S. Census data reveal that the average farm in Kentucky consists of 162 acres, with 5.7 acres of tobacco planted. Over 45% of Kentucky tobacco farms have agricultural sales totaling less than \$10,000.

- On average, an acre of tobacco generates around \$4,000 in gross returns and around \$1,500 in net returns at the farm level. In comparison, an acre of tobacco produces over \$50,000 in federal, state, and local tax

revenue as a result of excise and sales taxes on tobacco products. U.S. tobacco farmers receive approximately 2 cents of the domestic retail tobacco dollar or about 5 to 6 cents per pack of cigarettes sold in the United States.

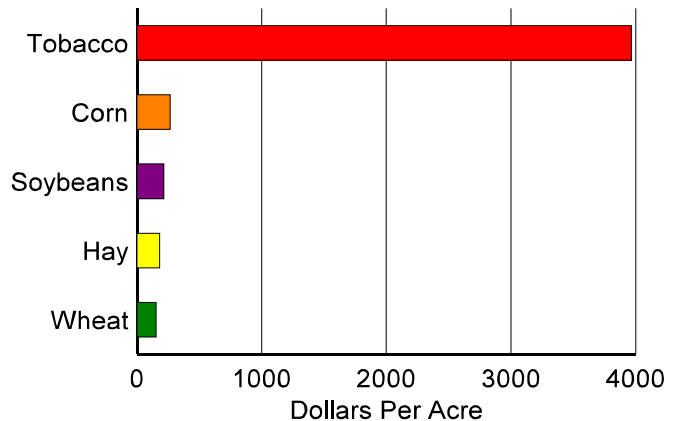
Distribution of the Retail Tobacco Dollar



- The federal tobacco program, dating back to the 1930s, has been a major factor in sustaining a large number of small family farms in Kentucky. The tobacco program, consisting of mandatory production controls, minimum price levels, and non-recourse federal loans, operates at zero cost to U.S. taxpayers. Tobacco not purchased by U.S. tobacco companies is taken under loan by farmer-controlled cooperatives who process, store, and later resell the tobacco. The program requires that the cooperatives repay the federal government all principle and interest on these loans. Only in rare situations, resulting from disaster conditions, has the federal government excused the repayment of these loans.

- Kentucky farms produce a host of different commodities that vary across the state. Most individual

Kentucky Crop Values Per Acre (1990-1999 Average)



farms report several agricultural income sources -- and these supplemental enterprises continue to mount. However, 75% of the farms growing tobacco in Kentucky reported that tobacco accounted for at least 50% of their agricultural sales in 1997 -- up from 61% of the farms reported in the 1987 Census.

- Research conducted at the Tobacco Health and Research Institute at the University of Kentucky may provide additional opportunities for Kentucky tobacco farmers via genetic engineering of the tobacco plant to produce pharmaceuticals and other beneficial consumer products.

- The 2000 Kentucky General Assembly designated 50% of Kentucky's national tobacco settlement (Phase I) funds to assist in diversifying the Kentucky Ag economy during the post tobacco settlement era. In addition, Kentucky tobacco farmers are scheduled to receive \$1.5 billion over the 1999-2010 period as part of the national tobacco grower settlement agreement (Phase II).

- Changes in tobacco policy and marketing will likely result in tobacco dollars affecting fewer farmers and rural communities in the future. Nevertheless, tobacco is expected to remain a viable, important, yet smaller part of the agricultural economy in this state for the foreseeable future.

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