

## ИССЛЕДОВАТЕЛЬСКИЕ ПРОЕКТЫ

# Examining the Informal Alcohol Market in Russia

**Dates:** May 2012 — December 2013.

**Research team of the National Research University — Higher School of Economics:** Prof. Vadim Radaev, First Vice-Rector of the HSE (head of research team); Dr. Irina Kratko, Associate Professor, responsible for new research based on national-level secondary data; Dr. Yana Roschina, Associate Professor, responsible for RLMS panel study; Zoya Kotelnikova, Senior Research Fellow; Elena Nazarbaeva, PhD student.

**International partners:** The International Center for Alcohol Policies (ICAP).

## Research Summary

The purpose of the proposed research is to examine the effects of policy measures on the production and consumption of commercial and noncommercial alcohol in the Russian Federation. In particular, the research is proposed to emphasize the impact of external factors on the size of the illicit and unrecorded markets in Russia. This relationship is proposed to be addressed both in the long run — through the analysis of secondary data, and in the short term — through the gathering of new data before and after two increases in excise tax that are to be implemented in Russia in 2012.

## Identified Problem

According to the latest report of the World Health Organization, nearly 30% of all alcohol consumed around the world is unrecorded and not taken into consideration in estimates<sup>1</sup>. Unrecorded alcohol is outside of the reach of government regulation. It is not subject to taxation and is significantly less expensive than legal commercial alcohol. In addition to being in direct competition with legal products, a market shift to unrecorded alcohol represents a significant loss to government revenue. The World Health Organization estimates that in 2005 unrecorded alcohol accounted for almost one third of all alcohol consumed in Russia (4.73 of 15.76L of pure alcohol per capita)<sup>2</sup>. Included in this category are home-produced alcohol (*samogon*), surrogate beverages, and illicitly produced alcohol beverages, which likely account for the largest proportion of this market segment. At the same time in accordance with the Russian Agency for Alcohol Regulation the unrecorded alcohol in Russia in 2011 accounted for 24% of all the alcohol market<sup>3</sup>.

The discussions are going around the problem of the taxation of beverage alcohol. Alcohol taxes can be used for various purposes, including producing government revenue, creating trade barriers, and encouraging the purchase of domestic products. The main debate is whether the taxation of beverage alcohol can be used as a public health and social tool for reducing alcohol consumption, abuse, and problems. The impact and effectiveness of taxation as a health policy tool remain the key issues of such debate.

Little is known about the impact of policy changes, such as the increase in pricing through excise tax and other restrictions on the unrecorded market and the production, consumption and sale of homeproduced, illicit, and surrogate alcohol.

<sup>1</sup> *Global Status Report on Alcohol and Health*. 2011. World Health Organization.

<sup>2</sup> *Global Information System on Alcohol and Health (GISAH)*. 2005. World Health Organization.

<sup>3</sup> See URL: <http://www.rg.ru/2012/02/17/alkogol-anons.html>

The existing research in this area has shown that high excise taxes can have a significant impact on the size of the illicit and unrecorded markets. For example, studies in different countries show that given the price elasticity of demand for alcohol, consumers are likely to switch to less expensive products when prices are increased. This means that there will be a shift in the type or quality of beverage being consumed, but no change in overall consumption<sup>4</sup>. Also where a disparity exists between the policies of neighboring jurisdictions, there is often significant cross-border trade of alcohol, both smuggled commercial and also illicit alcohol<sup>5</sup>. Stringent efforts to control the availability of beverage alcohol in the mid-1980s Soviet Union resulted in a sharp increase in illegal production and cross-border smuggling<sup>6</sup>.

A group of researchers examines substitutes. Substitution is also an outcome of high excise taxes, with a shift in demand to less expensive and often-harmful substitute products. This occurs in particular where resulting affordability of alcohol is low and affects primarily the poorer segments of society. For example, in Russia, untaxed homemade samogon is consumed at a rate of almost five times that of taxed vodka in some regions, due to its lower cost (from one-half to one-quarter that of vodka)<sup>7</sup>. Where home produced or other unrecorded alcohol is readily available, its consumption is likely to increase as a result of taxation changes<sup>8</sup>.

## Research Goals

**Short-term Goal:** examine the effects of excise tax increases in Russia in 2012 on the production and consumption of homeproduced, illicit and surrogate alcohol.

### Long-term Goals:

- examine the impact of external policy measures, particularly pricing and taxation, restrictions on sales and availability, on the affordability, production and consumption of illicit alcohol in Russia;
- develop and implement a successful model for examining of the illicit alcohol market and evaluating the size of the effect of governmental policy measures on the production and consumption of unrecorded alcohol that can be used for similar research in other countries and for comparative studies.

## Research Activities and Outputs

### Conducting Primary Research and Nationwide Data Collection

The fieldwork consists of two stages:

**Stage 1:** A special nationwide survey was conducted by *GfK-Rus* in May–June 2012. The questionnaire was designed by HSE research team in cooperation with CAP. The idea was to take major questions from

<sup>4</sup> Doran C. M., Digiusto E. 2011. Using Taxes to Curb Drinking: A Report Card on the Australian Government's Alcopops Tax. *Drug and Alcohol Review*. 30 (6): 677–80 (published early online 15 March 2011); Gruenewald P. J. et al. 2006. Alcohol Prices, Beverage Quality, and the Demand for Alcohol: Quality Substitutions and Price Elasticities. *Alcoholism: Clinical and Experimental Research*. 30 (1): 96–105; Muller S., et al. 2010. Changes in Alcohol Consumption and Beverage Preference Among Adolescents after the Introduction of the Alcopops Tax in Germany. *Addiction*. 105 (7): 1205–1213.

<sup>5</sup> Nordlund S. 2007. The Influence of EU on Alcohol Policy in a Non-EU Country. *Journal of Substance Use*. 12: 405–418.

<sup>6</sup> Zaigraev G. 2004. The Russian Model of Noncommercial Alcohol Consumption. In: Haworth A., Simpson R. (eds). *Moonshine Markets: Issues in Unrecorded Alcohol Beverage Production and Consumption*. New York: Brunner-Routledge; 31–40.

<sup>7</sup> Stickley A. et al. 2007. Alcohol Poisoning in Russia and the Countries in the European Part of the Former Soviet Union, 1970–2002. *European Journal of Public Health*. 17: 444–449.

<sup>8</sup> Haworth A., Simpson R. (eds). 2004. *Moonshine Markets: Issues in Unrecorded Alcohol Beverage Production and Consumption*. New York: Brunner-Routledge.

the existing RLMS study (to make comparisons later) and add the following questions on production and consumption of non-commercial alcohol:

- questions on alcohol consumption of different types of alcohol;
- questions on the home production of:
  - Alcohol;
  - Home-brewed beer;
  - Home wine.

Up to 60 questions were put in the questionnaire (counted by the number of variables). These questions will be used later in the panel RLMS survey.

This special survey was conducted only once to get data before July 2012.

Sample size: 2,100 respondents.

**Stage 2:** An extended RLMS survey (Round 21) in October–November 2012 using the questions designed for Stage 1.

Sample size: 7000 households (both in urban and rural areas) and 16 thousand individuals.

Separate interviews with key informants will be added to the survey.

- Estimate the size of unrecorded and recorded alcohol markets in locales covered by the surveys. This could be done by assessing how much money consumers spend on different types of beverage alcohol over a period of time. Given the anticipated increase in excise tax in July 2012, an estimation of the size and characteristics of the legal and illegal sectors of the market before and after the tax increase becomes effective will allow to assess how such changes affect different segments of the population.

This survey would entail conducting in-person interviews with a sample of adults in three different waves. The measurements will be taken from the same individuals at each point in time. This technique will allow researchers to pinpoint changes in the total per capita pure alcohol consumption, variations in the types of beverages consumed as well as the reasons for those changes.

Survey data will be gathered before the implementation of the new excise tax (RLMS rounds prior to 2012 and special *GfK-Rus* survey) and after the tax increase (October–November 2012).

Longer-term effects should be also measured by using the data of extended RLMS panel survey (Round 22, October–November 2013). The data will be available by June 2014.

- Examine the dynamics of the market of unrecorded alcohol in selected locales.
- Examine the correlation between the production and consumption of legal, illicit and surrogate alcohol beverages and excise tax increases in every round of the tax increase in 2012 (using linear regression models).
- Carry out a comparative analysis of illegal alcohol markets between the locales and evaluate the impact of various factors on them.

- Examine the effect of the excise tax increases in 2012 on the consumption of legal and illicit alcohol in various demographic segments. Assess the size of that effect.
- Identify distribution channels of illicit alcohol in various regions.
- Create a portrait of a typical consumer, producer and seller of legal and illicit alcohol.

### **Initial Hypotheses:**

- 1) excise tax increase does not result in overall alcohol consumption decrease;
- 2) excise tax increase results in a shift of licit alcohol consumption towards lower price segments and lower quality products;
- 3) excise tax increase results in a growth of unrecorded alcohol market and a substitution of beverage alcohol types, namely:
  - a) increase in production and consumption of illicit alcohol;
  - b) increase in production and consumption of homeproduced alcohol;
  - c) increase in production and consumption of surrogate alcohol.

### ***Conducting New Research Based on National-Level Secondary Data***

- Identify external factors (e.g., excise tax, import tariffs, restrictions on availability, etc.) that drive the production and consumption of illicit alcohol in Russia and examine the dynamics of both the factors and the market of unrecorded alcohol.
- Conduct retrospective analysis across several years to examine the correlation between changes in policy measures over time and production and consumption of legal and illicit alcohol beverages, including the following:
  - beverage alcohol consumption — total, legal commercial, illicit commercial, surrogate;
  - production of illicit alcohol;
  - indicators of harm — using mortality and morbidity data.
- Examine the dynamics of consumption of commercial and noncommercial alcohol in connection with price changes across several years, including the following:
  - economic analysis of price elasticity of demand for legal and illicit alcohol;
  - economic analysis of price elasticity among groups of consumers — light, moderate, heavy drinkers;
  - consumption shifts, and socioeconomic indicators (e.g., affordability).
- Analyze government revenue — short-term and long-term.

Available national and regional datasets from public sources (e.g., government) and from the industry include the following data:

- production of alcoholic beverages in Russia, nationally and regionally;
- wholesale trade of alcoholic beverages in Russia, nationally and regionally;
- retail trade of alcoholic beverages in Russia, nationally and regionally;
- import of alcoholic beverages in Russia;
- dynamics of sales of alcohol totally and per capita;

- structure of consumption of households, including consumption of alcohol;
- consumer price indices in Russia across several years totally and by region;
- production of illicit beverage alcohol in Russia across several years totally and by region;
- excise taxes on alcohol in Russia across several years;
- import tariffs on alcohol in Russia across several years;
- restrictions on sales of alcoholic beverages in Russia.

Datasets: RLMS previous rounds (2011 and before), Federal State Statistic Service (Rosstat) databases and regional databases on production and consumption of alcoholic beverages, analytical reports, overviews of state regulations and taxation issues, industry reports and reviews, alcohol industry expert evaluations.

## Methodology

The following methodology will be utilized during the data collection and processing:

- extensive literature review and examination of contextual issues— e.g., the prevalent patterns of alcohol production and consumption and the main laws relevant to legal and illicit alcohol;
- survey of households with emphasis on illicit and homemade alcohol production and consumption;
- interviews with key informants;
- desk research and the analysis of economic data;
- evaluation of the impact of external factors on illicit alcohol production and consumption using linear regression models;
- critical and action oriented research addressed to policy makers in the area of alcohol industry regulations.

In the data that is already available, the size of the unrecorded market refers to home produced beverages exclusively. The proposed indirect measures for assessing other segments of the informal alcohol market (e.g., illicit, surrogate, counterfeit) are as follows:

- the cost of alcohol that is below the current minimum price for vodka;
- the variance between the data related to the consumption and production of alcoholic beverages;
- the difference between the sales of alcoholic beverages and the distributed excise stamps on alcohol.

## Expected Outcomes

The new data generated would contribute considerably to the knowledge about the illicit alcohol market and its behavior.

- It would offer new insight into the impact of population-level policy measures, such as excise tax changes on consumption patterns. In particular, the research would provide robust information on the unintended outcomes of severe policies.

- Examining price elasticities and data on affordability would also allow better understanding of the impact of policy measures on different socio-economic populations.
- The data gathered from this work would allow a better understanding of the market segments in Russia, legal and illicit, their relative size, distribution, as well as the composition of consumers. It would offer a useful template for work that might be undertaken in other countries.

Specific outcomes of the research will include the publication of research papers in scientific peer review journals.

- It will provide the rigor and credibility needed for robust and compelling evidence. At the same time, it is important to allow the scientists to develop their own research agenda within the framework that we have laid out.
- Such an effort will be a vivid demonstration that it is possible for the scientific community and the industry to work together in a way that ensures scientific freedom and transparency and offers mutual benefit. This work will be conducted in accordance with ICAP's Dublin Principles.

Finally, the research outcomes have a clear relevance for the development of alcohol policies, both within the Russian context, and also internationally.

- Data from this research will help provide necessary information for the policy debates and the dialogue with policymakers, be it the Russian government, the European Union, or the World Health Organization.
- They can help form argumentation around the effectiveness of particular measures, for example, where fiscal policies are used to address public health issues.
- The inclusion of the analysis of the impact on revenue will provide important argumentation for the dialogue with government authorities.
- The data will provide some clear evidence on the impact of strong policy measures such as excise tax increases and the often-negative unintended outcomes that such measures can bring.

Finally, it will demonstrate that policies need to take into account national-level realities. Measures that may be applicable in high-income countries may not be appropriate in low- to middle-income countries. Indeed, the unintended outcomes may be more severe than the harm the policies are intended to address.