

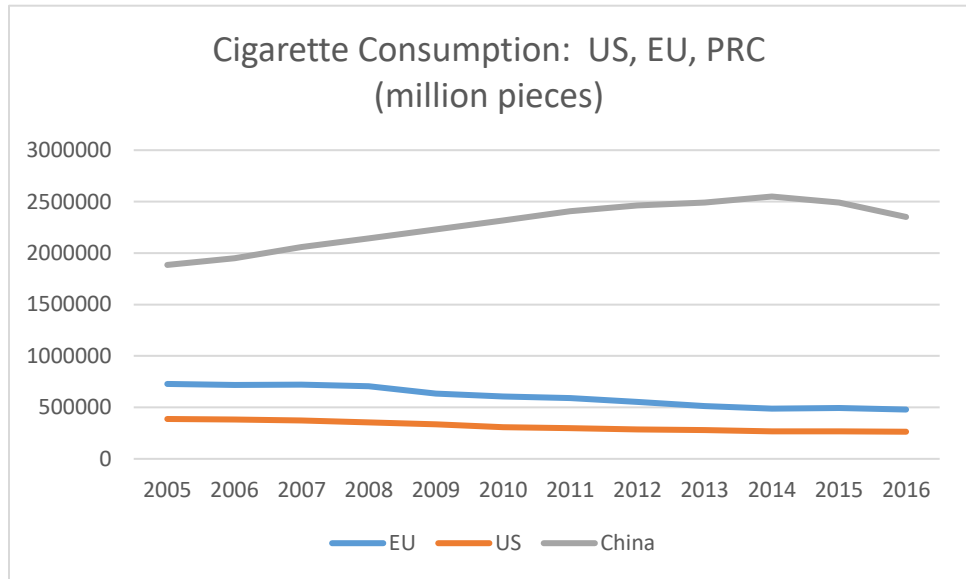
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**Cigarette Market**

Global cigarette consumption continued to decline due to lower smoking rates, not only in the EU and US, but also in China. However this trend will be partially or fully offset in some developing countries because of the growth in population of smoking age adults.

According to an IBISWorld Industry Report global revenue from tobacco products, including tax revenues, will continue to grow despite lower cigarette consumption. This is due to increased cigarette prices both in terms of before tax prices from cigarette manufacturers and increased cigarette taxes. Consequently, both tax revenues and industry profits are expected to continue to grow. IBISWorld expects global revenues from tobacco products to be \$662.9 billion in 2017.

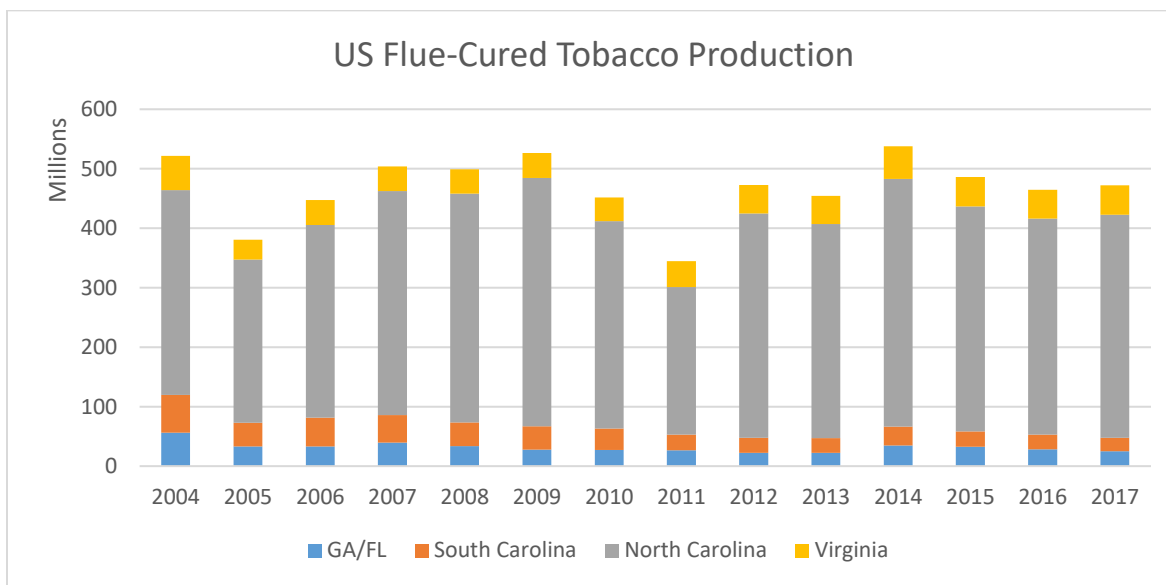
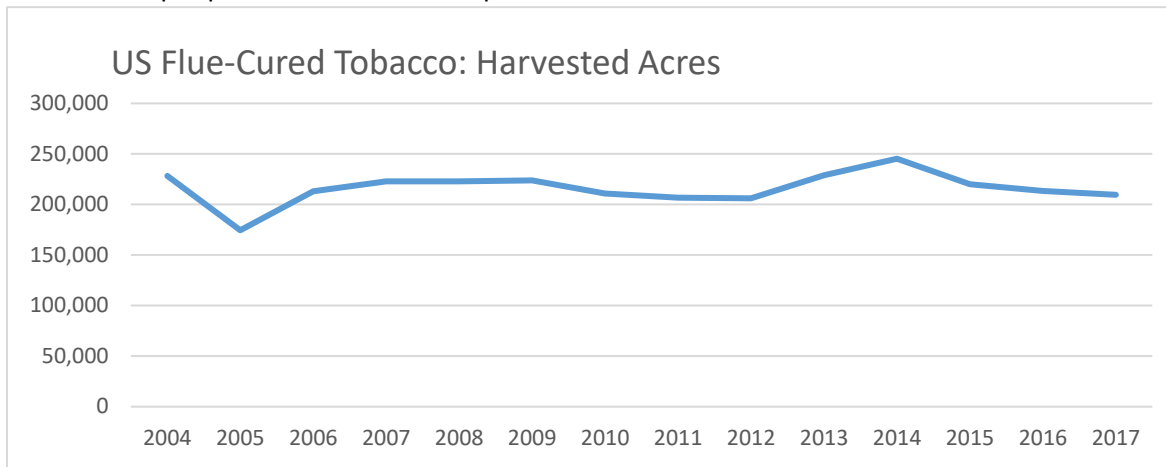


Global per capita income, particularly in developing countries with higher smoking rates, is expected to continue growth. Significantly for US tobacco producers, growing incomes means that more smokers will upgrade to premium brand cigarettes that contain more flavor style tobacco. This trend will partially offset declining demand for flavor style tobaccos in developed countries where smoking rates continue the long term trend of significant decline.

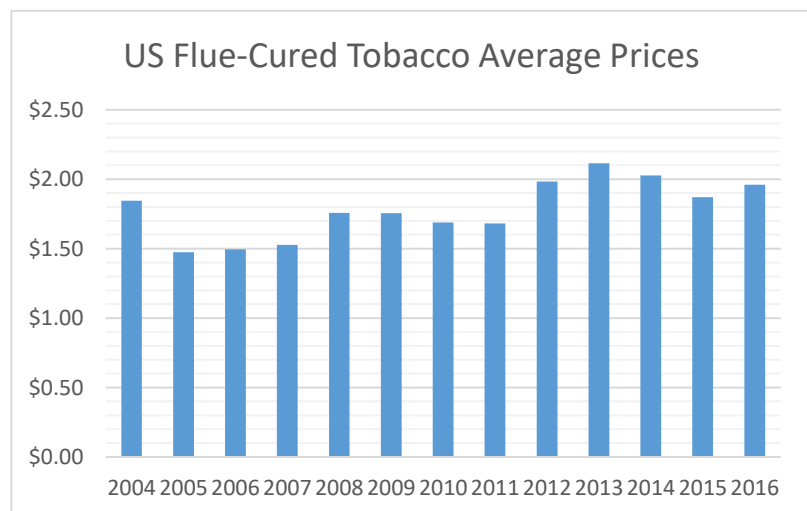
Sales of E-cigarettes and other tobacco vapor products continued to grow globally with sales of e-cigarettes and e-vapor products estimated to be over \$12 billion in 2016 according to Euromonitor International. While sales of e-cigarettes seems to be slowing with many analysts predicting limited growth, a new vapor product has emerged. Philip Morris International (PM) had introduced iQOS, a heat-not-burn (HNB) product, in test markets in Japan and Italy in 2014. The product has done very well growing to over 12% market share in the Japanese cigarette market in just two years. PM has indicated a major commitment and shift away from traditional combustible cigarettes to iQOS. British American Tobacco and Japan Tobacco have also introduced HNB products. PM hopes to have manufacturing capacity in place in Europe to produce 100 million Heets, the tobacco product used in the iQOS device, by the end of 2018. PM has submitted an application to FDA for approval of iQOS as a modified risk tobacco product in the US. HNB products could bring about the transformational change in the tobacco products market that has eluded e-cigarettes.

## Flue-Cured Production and Market

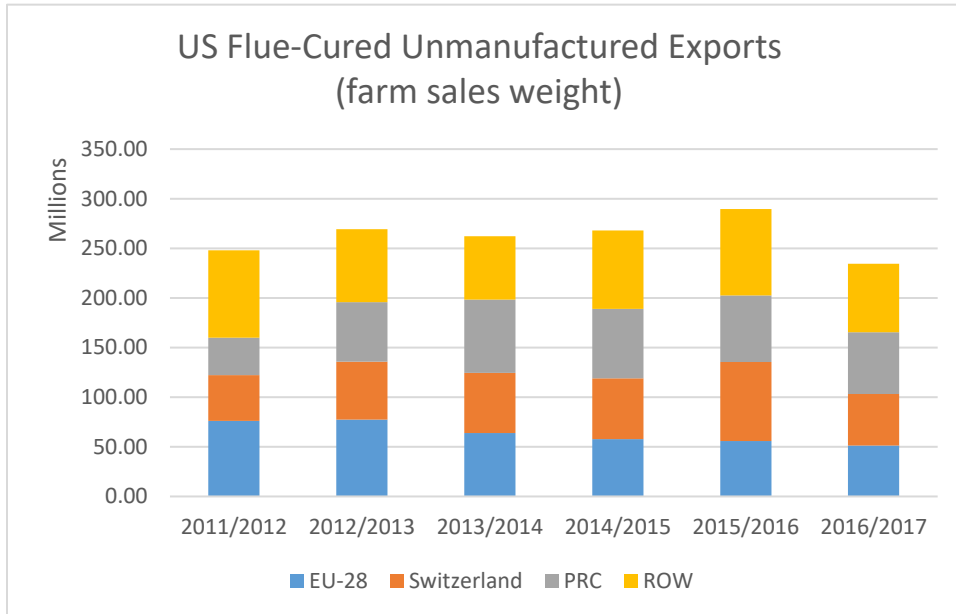
At 209,500 acres harvested acreage of U.S. flue-cured tobacco is forecast to be down slightly from 213,500 acres in 2016. Yield for 2017 was estimated at 2,254 pounds per acre over 200 pounds greater than the 2016 yield of 2,021. Consequently production for 2017 is forecast at 472,200 pounds up from 431,450 pounds in in 2016. Average price received in 2016 was \$1.96 per pound according to USDA, up from \$1.873 per pound for the 2015 crop.



Higher quality with a reasonable supply/demand balance led to higher prices in 2016 than in 2015. The 2017 Brazil crop was reported to be 1.37 billion pounds, according to Universal Leaf, up from a recent low of 1.01 billion pounds in 2016. Universal forecasts the 2018 Brazil crop to slightly lower at just under 1.3 billion pounds. The 2017 Zimbabwe crop was estimated to be 403 million pounds down from 442 million pounds in 2016. The 2017 average price per pound in



Zimbabwe was expected to be about \$1.34 per pound; about the same as in 2016.



Unmanufactured exports of US flue-cured tobacco fell from 290 million pounds for the 2015 crop to 235 million pounds for the 2016 crop. Exports declined despite strengthening of the Brazilian Real against the US dollar. This was likely due to lower US production in 2016. A stronger Brazilian Real and a larger 2017 crop should lead to higher exports for the 2017 crop.

Exports to the European Union (EU-28) declined for a second year from 55.7 million pounds to 51 million for the 2016 crop. Exports to Switzerland fell from 79 million pounds for the 2015 crop to 52 million pounds for 2016. Exports to Switzerland represent not only US tobacco bound for other European countries, but also tobacco bound for Asia. US exports to China continued to decline from 67 million pounds for the 2015 crop to 62 million for the 2016 crop. Use of US flue-cured by US cigarette manufacturers increased again from 160 million pounds for the 2015 crop to 262 million pounds for the 2016 crop.