

FILE NOTE

B.A.T Industries Diversification

1. For an activity to be of interest to B.A.T Industries:
 - (a) It must be profitable and have growth potential (consistent with Group objectives).
 - (b) We must be able to take a leadership position in the relevant market segment and this leadership position must be based on a durable competitive advantage.
 - (c) We must have knowledge and experience of the industry/market at Board level.
 - (d) It must be of sufficient size to justify Board time and to avoid a dissipation of management resources.
 - (e) It should add strength to and take strength from other Group activities (i.e. there must be a positive advantage to be gained from membership of the Group).

2. To meet the basic criteria:

- (a) It will be helpful if the activity is related to existing Group activities and can draw strength from these.

Also, if there is an identified existing Board member who has the necessary knowledge and experience of the industry/market.
- (b) Failing this, the new activity will need to be headed by a person who is of Board calibre and who can identify fully with the Group.
- (c) Perhaps the greatest strength of B.A.T Industries is its wide geographical spread and activities which have unrealised potential for overseas expansion would be particularly suitable as investments.

3. A major issue is the extent to which diversification should be centralised at B.A.T Industries level or at Operating Group level.

Perhaps the main determinant of this is the degree to which B.A.T Industries is prepared to trust the judgement of the Operating Group or Company Board.

Even if diversification is delegated to a subsidiary level, there is an obvious advantage to having a limited range of activities within the Group so that some judgement can be applied at the centre (who might wish to employ analysts with specialist knowledge).

As a broad generalisation, it might be expected that responsibilities for diversification would be delegated to BATUS, Interversa, BATCo. and to a more limited extent to certain major companies within BATCo. In addition, the Associated Companies will also have their own diversification strategies.

The other major non-Tobacco businesses will be managed by B.A.T Industries and the same criteria will be applied to them as to other diversified activities. The key question here will be the degree of diversity that can be managed directly by the B.A.T Industries Board (i.e. if they cannot be grouped together, do we need to have fewer activities?).

RS/DJA

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