

CAC XI : RIO DE JANEIRO

Item F : Tobacco

1. The consolidated Group forecast for 1989-1993 shows trading profits from Tobacco growing at 9% p.a. and levels of profitability which are sufficient for the activity to generate a substantial cash surplus which will be available for investment in other activities.
2. Key assumptions underlying these forecasts are that the total 'free-world' market for cigarettes will remain approximately constant at 2,850 billion p.a. and that the BAT Group will increase its share of the market from 19.3% in 1988 to 19.6% in 1993, reversing the slight decline experienced in 1987 and 1988. Also, that market conditions will be such that it will be feasible to continue the current trend of improving profitability.
3. Supporting assumptions about the market are that:-
 - (a) Anti-smoking pressures will continue but will be contained.
 - (b) Taxation will tend to increase but the increases will be moderated by the need to maintain the industry as a major source of revenue.
 - (c) The impact of the Single European Market will be significant.
 - (d) There will be improved access to monopoly markets both in Europe and the Far East.
 - (e) There will be increases in sales in Latin America, the Indian sub-continent, the Middle East and Africa, offsetting slow declines in the markets in North America, Europe and the Far East. This will maintain the total market at current levels, extending the trends which have been established over several years.
 - (f) For the product, there will be a continued fall in levels of delivery but at a slower rate than in the past. Full flavour products will continue to dominate with a continuing trend in consumer preference towards US type blends.
 - (g) There will be some increase in the polarisation of markets with International Brands increasing at one end of the price range but with emphasis also being given to value-for-money segments in many markets with competition increasingly using pricing or the postponement of price increases as a competitive tool.
 - (h) However, overall profit levels will also be influenced by the strategic need for Philip Morris and R.J. Reynolds to maintain the cash flow from their tobacco businesses.
 - (i) A key assumption for the US market is that the price of cigarettes will continue to rise significantly faster than inflation (enabling BATUS to continue increasing profits despite increasing the proportion of sales in the value-for-money segment).
4. A first issue for discussion will be the accuracy of these assumptions and the identification of key sensitivities likely to affect the relatively favourable industry environment which is projected, especially where these impact on the projections for the Group's own Tobacco businesses.

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5. Other issues for discussion will be:-
- (a) Likely developments in the competitive environment with particular reference to the extent to which the new financial pressures on R.J. Reynolds and Philip Morris and the comparatively poor showing of the other major Tobacco companies represents an opportunity for B.A.T Industries.
 - (b) Likely technological trends in products and processes within the industry and the adequacy of the current R&D programme as a means for enabling the Group to establish a competitive advantage through having a capability to build on the recent good record in launching innovative new products and in establishing facilities for lowest cost production.
 - (c) Opportunities for strengthening the current rather weak market position in Europe and the costs of doing this in relation to the potential benefits.
6. Delegates will also be asked to comment on the extent to which the recently expanded Tobacco Strategy Review Team meets the need for co-ordinating Group policies and strategies, to discuss whether further co-operation might be desirable and, if so, the optimum method for achieving this.
7. Taking the session as a whole, the aims will be to identify key sensitivities in the current projections for the Group's Tobacco activities and to identify new initiatives which might be taken to secure and if possible increase the contribution of the activity to the overall development of the Group. Implicit in this will be the question as to whether it is possible to identify specific opportunities for investment in Tobacco which are at least as attractive as opportunities within the Group's other major activities.

RS/DJA
23rd March 1989

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