

D R A F T

Guidelines for Souza Cruz : July 1987

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General

1. The overall strategy for Souza Cruz is to maintain the growth and profitability of the Tobacco business and to use this activity to generate a flow of funds which, after payment of an appropriate dividend, can be invested in a limited number of other businesses of substantial size which can achieve leadership in their markets and which are capable of providing growth sustainable over the longer term future.
2. The current priorities for Souza Cruz are:-
 - (a) To negotiate with Government to maintain cigarette prices and profitability at levels where it is possible to earn profits sufficient to pay dividends and to provide funds for investment in other activities.
 - (b) To integrate Tabasa into an overall Souza Cruz plan for leaf exports.
 - (c) To formulate action plans and strategies resolving the uncertainties regarding:-
 - (i) Pulp and Paper.
 - (ii) Fruit Juice.
 - (iii) Bioplanta.
 - (iv) Options for developing Downstream Agribusiness activities.
 - (v) Polo.

Financial Guidelines

The following Financial Guidelines are provisional and will need to be reviewed when the economic and inflationary prospects for Brazil become clearer.

3. Returns on Investment : Souza Cruz should aim to achieve an overall return on investment of 16% (based on local management accounting conventions and including investment income), with Tobacco providing a higher return than the diversified businesses.
4. Dividends : Dividends expected from CONTAB (gross of 25% Withholding Tax) are:-

	<u>1987</u>	<u>1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>	<u>1992</u>
US\$m	28	31	35	39	44	49

These assume that the dividends paid to the UK by CONTAB should be the maximum allowed under the Foreign Registered Capital (FRC) regulations but that they will be restricted by limits to the availability of cash resources and distributable profits. It is also assumed that Souza Cruz will distribute a minimum of 60% of attributable profits as measured on a Brazilian accounting basis. In view of the current high level of inflation and devaluation, the latest estimate of the dividend for 1987 is US\$28m, which is significantly lower than the maximum which would be allowed under the FRC regulations. The remaining years represent a 12% p.a. increase (8% p.a. real + 4% p.a. inflation) but the aim should be to restore dividends to the full amounts allowed under the FRC regulations.

5. Debt/Equity : Souza Cruz should aim to have no borrowing at the year end, other than that resulting from the use of small subsidised short-term borrowings.

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Specific Priorities

6. For Tobacco, there should be a continuing aim to maintain a dominant position in the Brazilian Cigarette market in terms both of market share and of the strength of distribution. However, the immediate priority must be to negotiate with Government for an increase in the profitability of the market.
7. There should be continuing emphasis on applying resources to product quality, ahead of any increases in the media spend.
8. Plans for a new factory should be prepared in good time to enable the company to react quickly if a favourable sales trend should become established.
9. *Embassy?* Leaf Exports should continue to be given a high priority and a strategy developed for the integration of Tabasa.
10. For Paper, the existing plant should be upgraded from 60,000 tons p.a. to 100,000 tons p.a. capacity subject to reasonable assurances on pulp supplies. Opportunities should be sought to introduce Carbonless and possibilities for purchasing additional facilities to provide the necessary production facilities should be kept under review.
11. For Pulp, the first priority should be to negotiate a revised shareholders' agreement allowing Souza Cruz to continue to influence key decisions in Aracruz. Subject to reasonable assurances on this, Souza Cruz should give favourable consideration to the plan to increase the capacity of Aracruz.
12. While accepting that, under current conditions, there are unlikely to be immediate opportunities to acquire new Paper/Pulp activities at acceptable prices, it is still important to build up in-depth knowledge of the sector and its component companies so that if an opportunity does arise to make an acquisition or to acquire specific facilities from another company, Souza Cruz is in a position to prepare a proposal from a good base of knowledge.
13. For Fruit Juice, the immediate priority should be to improve the performance of Maguary and to establish a firm base for considering the potential for expansion.
14. For Polo, the ultimate aim should be divestment, once multiple sources of supply for polypropylene film have been developed in Brazil. Souza Cruz should aim to maintain the positive cash flow planned for this business even if, as a result, the proportion of the equity shareholding held by Souza Cruz is reduced.
15. For Bioplanta, there should be a continuing aim for the business to achieve a positive cash flow by 1989. However, it is also important that the company should operate at a level where it is possible to assess the opportunities for Souza Cruz to set up a profitable activity 'downstream' in Agribusiness. If NPI ~~is~~ not wish to subscribe ~~their~~ share of the investment required for the expansion of Bioplanta, it should be suggested to them that they should either let the proportion of equity held by them be reduced or should consider a complete dissolution of the joint venture arrangement.
16. Financial Services should continue to be considered as a possible new activity in which to invest and Souza Cruz should be prepared to move rapidly if there is any relaxation of the current limitations on foreign participation in the sector.

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