GUIDELINES 1981 : IMPLICATIONS FOR B.A.T INDUSTRIES

The purpose of this paper is to summarise the Group Objectives and Investment Strategies agreed by the Board at the meeting on 29th September 1981 and to show the implications for B.A.T Industries of the Operating Groups achieving dividends and debt:equity ratios in accordance with the Guidelines.

1. Growth Objectives: The Group's overall financial objective is to increase attributable profits and dividends by at least 3% p.a. in real terms.

   In addition, there should be a minimum dividend cover of 1.5 on CCA attributable earnings less "unavailable retained earnings".

2. Dividends: The table shows the implications for B.A.T Industries of the Operating Groups declaring dividends in accordance with the Guidelines.

Dividend Declarations £m	1982	1983	1984	1985	1986
B.A.T. Co.	75	75	80	90	100
BATUS (at US $1.82 rate)	62	67	80	86	96
Interversa (at DM4.42 rate)	13	14	17	17	19
Wiggins Teape	4	10	20	25	30
MPI	7	7	8	9	10
B.A.T Stores	6	8	10	10	10
B.A.C.	4	4	5	6	7
Amatil (at A$2.03 rate)	2	3	3	3	4
Imasco (at C$2.86 rate)	5	6	7	8	8
TOTAL	178	194	230	254	284
B.A.T Industries' Requirement	158	180	200	224	250
Surplus	20	14	30	30	34

The dividends shown for BATUS, Interversa, Amatil and Imasco are net receipts, after allowing for withholding taxes.

It should be understood that all Guidelines agreed for Operating Groups should be minimums and, in particular, it is expected that, where earnings growth increases, there should be a comparable increase in dividends to B.A.T Industries.

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3. Risk Profile: The Group should achieve and maintain a reasonable 'risk profile', particularly as measured by the industrial and geographical distribution of earnings and assets and by the debt:equity ratio (where the policy is to limit this to a maximum of 50% overall and 60% in transferrable currency areas). However, no really valuable and justifiable investment opportunity should be lost as a result of an inflexible constraint on resources. In exceptional circumstances, the debt:equity ratio could be allowed to rise above the limit stated provided there is assurance that the proportion of debt to equity will return to a ratio inside the limit within 3 years.

4. Debt:Equity : The year end debt:equity requirements included in the Guidelines to the Operating Groups are summarised below.

Ratio %	1982	1983	1984	1985	1986
B.A.T. Co.	11	10	8	7	7
BATUS (UK Basis)	60	59	56	56	56
Interversa	50	50	50	50	50
Wiggins Teape	90	80	70	65	65
MPI	60	60	60	60	60
B.A.T Stores	25	25	25	25	25
B.A.C.	50	50	50	50	50

If the Operating Groups stay within their Guidelines, the resulting debt:equity ratio for B.A.T Industries will be at or below 40%.

The sensitivity to variations from these Guideline figures is indicated in the following table, which shows the approximate change in percentage points in each Operating Group ratio which would result in a change of one percentage point in the ratio for the Group as a whole.

B.A.T. Co.	3
BATUS (UK Basis)	4
Interversa	7
Wiggins Teape	15
MPI	15
B.A.T Stores	20
B.A.C.	35

It should be noted that the debt:equity requirements for B.A.T Stores and the resulting debt:equity ratios for B.A.T Industries exclude the effects of the £40m payment for Mac Markets, due in 1983. If this is funded by borrowings, the B.A.T Industries debt:equity ratio will be increased by about 2 percentage points, equivalent to 40 percentage points for B.A.T Stores Holdings.

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5. Performance Objectives: The Group Objective is that the return on assets should be a minimum of 25% in historic accounting terms. (At an inflation rate of 10%, this equates to a CCA return of approximately 15%).

The targets agreed for the Operating Groups clearly must reflect the situation in which they find themselves but it will become increasingly important to ensure that, where they are making new investments, these can be reasonably expected to meet the Group's objective for returns on assets.

The return targets for the medium term included in the Guidelines to Operating Groups are as follows:-

Return on Assets

	CCA	Historic
B.A.T. Co.	15	28
BATUS	14	25
Interversa	15	20
WT	11	24
MPI	10	20
B.A.T Stores	10	20
B.A.C.	15	26

6. ACT: The ACT issue is one of considerable concern and highlights yet again the importance of UK performance. However, radical ways of reducing the impact should also be considered or re-considered.

7. Growth Opportunities: Operating Groups should be asked in their Plans to assess the real growth opportunities available to them in the medium and longer term, with a realistic evaluation of the investment required and returns to be achieved. The consequences of these assessments should then be reviewed by BAT Industries in the light of its growth and other objectives.

8. Leadership: Each business within the Group should be established in a leadership position in its chosen market through having a defined competitive advantage. This could occur in a number of ways (e.g. through a superior product, through lower production costs, through market position, etc.) and it is left to each business to define their competitive advantages. This objective is believed to be particularly important since it is on the competitive strengths of its component businesses that the ability of the Group to achieve its financial objectives ultimately depends.

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9. Investment Strategies agreed by the Board were as follows:-

(a) The first priority in investment should be the maintenance and, where possible, the improvement of the competitive position of the Group's Tobacco businesses.

(b) However, it is still the Group's long term aim to reduce its dependence on Tobacco by achieving a rate of growth in non-Tobacco profits such that by 1990 these are contributing at least 50% of total Group profits.

(c) Non-Tobacco investments should centre on activities which can be undertaken within the framework of existing businesses.

(d) Additional opportunities should be sought to build on existing Group strengths. Opportunities for improving the use of existing assets (e.g. property) should also be given special consideration.

(e) Emphasis should continue to be placed on the need for each element of the business to be capable of achieving self sufficiency in funding and there should be a continuing requirement for a rigorous attitude to be taken to activities with low performance which cannot be improved within an acceptable time scale.

(f) Particular emphasis should be given to improving the results for UK based businesses without increasing the proportion of Group assets employed in these businesses.

(g) Further consideration should be given to ways of accelerating profits growth in BATUS by investment within the limits of their debt:equity guideline and without dilution of B.A.T Industries' shareholding.

(h) Elsewhere, particular emphasis should be given to accelerating the rate of development of non-Tobacco activities in selected countries overseas, particularly in SE Asia and Latin America. Priority should be given to countries where the Group has an existing business and where funds are available, but the possibility of additional net investment should not be ruled out.

(i) Preference should be given to maintaining or establishing successful businesses rather than merely selling technology. Although majority shareholdings are preferred, it is accepted that minority positions, with a sufficient degree of management control, may be the optimum achievable in certain countries.

RS/PS
28th October, 1981

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