

Note for the TSG

PROJECT STEM: PROGRESS REPORT

As agreed at the last TSG meeting, the project Stem team will prepare progress reports and this one follows the recent meeting of the team.

P&L Formats

Attached as Appendix A is the suggested format for the report on cigarette operations which will be used at a TSG and Group level; it reflects the outline presented to the last TSG meeting. The Appendix also contains notes explaining certain of the items but, in addition, the following key points should be noted:-

- (a) The "TSG" (cigarette) data is allocated by market and brand.
- (b) The components of this data are split by production, brand owner and end market manager to separate out the relevant responsibilities. However Group profit for a market or brand will involve more than one of these columns e.g. the Group profit for a brand included in the TSG column would pick up the relevant brand profit from each of the three columns.
- (c) The legal entity column reflects the total profit of the relevant operation, whether company, Op. Group or Group. It includes the cigarette profit in the TSG column plus:-
 - other tobacco operations to give total tobacco profit; this includes leaf operations
 - non tobacco operations
 - central costs not allocated to cigarette, leaf or non tobacco operations.

The lines in this column need to be developed to reflect these non cigarette operations.

- (d) The definitions included in the Appendix are summarised and will need to cover more detail. This will be considered further at the next project team meeting; in particular, the split of conversion costs and the split/subsequent allocation of overheads will be addressed.
- (e) As noted in the last TSG report this exercise lends itself to a "network" solution with access to the same "data base" by companies, Op. Groups, brand owners, end market managers etc., who could access and aggregate information as required. To achieve this will require a major development and implementation of system and data changes, involving significant internal (and some external) resource.

1995/99 Plan

The Op. Groups will complete their plans as normal and provide information to enable the usual Group numbers to be consolidated. Also while it is not possible to implement any longer term reporting system for end market profitability within the time scale, the project team's initial suggestion is that Op. Groups do the following in their plan documents supplied to Windsor House:-

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- (a) The P&L statements will, as far as possible, follow the formats intended for use in the longer term project; the intention is to cover the main headings but not all the detail e.g. no split of conversion costs would be made.
- (b) While the plan document will be based on the Op. Group profit, it will also include a section showing Group figures for key end markets and key brands for which the Op. Group has responsibility. A suggested list is attached as Appendix B. Thus, the intention is to replace the overall "rough cut" of the budget year undertaken last time by a more detailed and rigorous analysis covering to key markets and brands for the plan years; this would cover the key lines in the suggested formats in Appendix A.

Op. Groups are exchanging information to enable the new management responsibilities to operate and so the 1995 QPR's will start to include supplementary information on end market profitability. However, for the next project team meeting, the members are following up the detailed implications of the points noted above on the plan, so that the detailed approach can be finalised; ongoing reporting for 1995 should be reviewed in the light of these subsequent discussions.

Market share/value share

The project team regard both market share and value share as useful components of regular management and financial reporting. However, it is considered that they may be better dealt with as part of a marketing data base (CIGMAR) rather than the proposed STEM financial data base. The feasibility of making CIGMAR part of an overall Group data base would need to be carefully investigated and would, in particular, have the following implications for CIGMAR:-

- (a) Extension of data collected, including formal projections.
- (b) Formalisation of input, both method and definitions; consistency with STEM financial data.
- (c) Access to data base to be equivalent to that decided for the STEM financial data base.

In the short term, Op. Groups may deal with value shares, as well as markets shares, in their 1995/99 Plans where this is considered relevant.

TRANSFER PRICING

This is obviously a much broader issue than the STEM financial reporting project involving taxation departments, the work on production capacity etc. and is not therefore part of this project team's intended work. However, the STEM project should at least provide the consistency of cost definitions to provide a firmer basis for discussions.

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ASSOCIATED COMPANIES

While these must be in the Group data base to provide complete results, there are practical difficulties in including associates as part of the data base which fully analyses results in detail between end markets and between brands; we certainly do not currently have the required information.

INTERNATIONAL DUTY FREE

The separate analysis of this market as required by the TSG relates to "genuine" duty free. This highlights the issue of other duty free trade; the basis for defining and reporting end markets will need to be agreed.

NEXT PROJECT TEAM MEETING

This will concentrate on the following:-

- (a) Feedback from the TSG on this note and from the marketing conference.
- (b) Review aims for 1995/99 Plan and 1995 QPR's.
- (c) Review list of end markets - potential problems
- (d) Further detailed development of definitions in Appendix A.
- (e) Review logic of Appendix A in detail.
- (f) Feedback from contact with other multinationals.
- (g) Implications of move to longer term system.

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