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**BRITISH-AMERICAN TOBACCO COMPANY LIMITED**

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**TO: ALL MARKETING DIRECTORS**

**CC: All Board Members  
All General Manager**

**FROM: J REMBISZEWSKI**

**DATE: 6th May 1993**

**SUBJECT: PHILIP MORRIS : MARLBORO PRICE CUTS IN THE U.S.A.**

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The purpose of this note is twofold:

- \* to inform you of the facts
- \* to advise you how we should prepare ourselves within BATCO.

I attach a summary of events, together with a few relevant statistics on Philip Morris in order to help you understand what is happening and why. In essence, Philip Morris has announced a fourpoint plan, the main element of which is the price promotion of Marlboro designed to regain lost market share. Reynolds appear to have followed with their premium brands but events during May will enable us to gain a clearer picture as implementation commences from early May.

While these announcements sound dramatic, they simply represent an escalation of the value for money and discount war that has been developing in the USA and hardly justifies the big bang PM made with their announcement. The reported \$2 billion fall in PM profits is unlikely to occur in practice although some decline is probable. Nevertheless, PM have reacted aggressively to mounting pressure upon Marlboro's share from the value for money and generic segments.

This reflects a situation where a recession had reduced disposable income, where the total market was declining and the industry, led by Philip Morris, had consistently implemented real price increases ahead of inflation. As a result, profit margins had become as high as 45% of net turnover, more than compensating for any volume declines.

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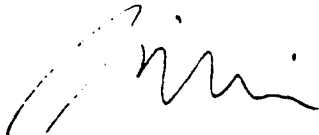
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We do not see a similar radical move in any other market but we do expect signs of more reluctance to price up Marlboro while in Europe, PM is actively developing the low price sector even at the expense of Marlboro. This all points to a higher risk of price wars started by PMI in markets where a recession promotes downtrading, tax/excise are either low or mainly ad valorem, there is overcapacity and a highly competitive climate.

To prepare ourselves, we are currently developing international low priced brands and consistent marketing strategies including product, packaging and, for some regions, low cost manufacturing. In addition, we will have to step up our efforts to improve productivity in all parts of the business. We must become a low cost manufacturer with lean organisations to be able to support our brands under increased price pressure scenarios.

Finally, you need to define clear pricing strategies for all your brands which should ideally define a key competitor. This can help to avoid price war spirals because it becomes a no win game if you execute this strategy fast. These strategies should be cleared with your Regional Management and in the case of international brands in doubt, you should also clear with the International Brand Group. You should also indicate where you see a need for a low price international brand introduction which should be regionally/globally orientated so that we avoid proliferation of brands, boosting our complexity and confusing the competition.

We must not act hastily especially in markets where there is no apparent risk since in most parts of the world we experience uptrading and the lack of strong enough international brands in those higher price segments to compete with PMI in this growing sector. The key challenge long term for BATCO remains to build brands and profitability via a healthy market-driven (product and advertising) growth.



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