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A meeting of the Tobacco Strategy Review Team was held on 30th May 1991.

Present: Sir Patrick Sheehy, Mr. M.F. Broughton, Mr. B.D. Bramley,  
Mr. R.J. Pritchard, Mr. U. Herter, Mr. A. Monteiro de  
Castro, Mr. J-L. Mercier, Dr. R. Salter (Secretary)

In Attendance : Mr. T.J. Wylie, Mr. E. Kohnhorst

1. The Chairman welcomed Mr. de Castro as a member of the team in place of Mr. Rombaut, who is retiring as President of Souza Cruz.

Minutes of Previous Meeting/Matters Arising

2. The minutes of the meeting held on 27th February 1991 were agreed.

3. Matters arising from the minutes were:-

- (a) JTI : It was noted that there had been continuing monitoring of JTI as competitors. Although they continued to be active in Far Eastern markets, there was no evidence of dumping. There was also no evidence that they were competing actively for business in Eastern Europe or the USSR.
- (b) Overseas Travel : There had been no problems in implementing the proposed reduction in frequency of Technical Liaison meetings. The Chairman emphasised the need to keep a strict watch on travel overall, ensuring that the same rigorous criteria were applied in justifying overseas visits by individuals.
- (c) Export Training in Souza Cruz : It was noted that training in BATUKE was being arranged for the Brazilian Export manager. However, it had not been possible to provide a BATUKE manager to work in Brazil. The Chairman stressed the benefits in transferring expertise through secondments of staff and asked Mr. Bramley to consider further whether it would be possible to make someone available for secondment to Brazil.
- (d) R&D Funding Arrangements : Mr. Broughton reported that the details of the arrangements for charging out the costs of the centrally funded research in the most tax-efficient way had not yet been finalised. Mr. Mercier suggested that for Imperial Tobacco the most acceptable method for charging might be based on a fixed fee plus a percentage of turnover. It was also noted that following some relaxation of the Brazilian regulations relating to payments for technical assistance, Souza Cruz might be able to contribute to the costs of central research. Mr. de Castro was asked to investigate and to let Mr. Broughton know the current position on this.

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November Marketing Seminar

4. The progress report on the arrangements for the seminar due to be held in Orlando, Florida from 19th to 23rd November was noted.
5. It was also noted that the Chairman would send out invitations early in June and that Mr. Eckmann would then follow-up with delegates on the detailed arrangements for the seminar.
6. The managers to be invited would be as follows:-  
  
Brown & Williamson : Sandefur, Whitehair, Schoenbachler, Fitzmaurice  
  
Souza Cruz : Castro, Andrade  
  
Imperial Tobacco : Brown, Lee  
  
BATCF : Schweitzer, Tomat  
  
BATCo. : Brookes, Hazel, Watterton, Ross, Bruce-Miller, Grant, Tandrup, Viner, Wursser, Arnold, Laux, Edmunds, Chugh, Borloz, McDowell, Matamoros, Hahn, Dunt, Taylor, Adams, Rembiszewski.
7. Additions compared with the list agreed in February were Dunt, Taylor, Adams and Biszewski. Of these, Taylor replaces Freire and the last two are recent recruits to the BATCo. Board, who are due to join the company in the summer, from Pepsi-Cola and Suchard's respectively.
8. The Chairman, Mr. Broughton, Mr. Bramley, Mr. Pritchard and Mr. Herter will also attend the seminar and it will be made clear to everyone that this is an important event to which they are expected to give appropriate priority in ensuring attendance and in preparing for the meeting.
9. Reviewing the programme, it was agreed that Brand Goodwill, Excise Structures, Cost-Effectiveness of Promotion, Competitor Analysis and Distributor/Trade Relationships were the key issues which should be discussed. However, it was suggested that, subject to the availability of the outside speaker, the proposed order of the programme should be changed, starting with Brand Goodwill and Excise Structures on the first day and then going on to Cost-Effectiveness of Promotion on Day 2.

Smoking Quality

10. The Chairman proposed that improving the smoking quality of the Group's products should be a key strategic thrust for 1991-1992. He suggested that companies needed to develop improved measures of smoking quality which related more directly to consumer preferences. They then needed to have improved programmes, using these criteria both to evaluate new products and to monitor how existing products stood relative to competitors. It was important that there should be an increased consciousness throughout the Group of the importance of smoking quality and of the need to exchange experience on the best techniques for measuring this.

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11. Mr. Kohnhorst described the evaluation techniques used in Brown & Williamson. He stressed the importance of bridging the gap between internal tests and the commitment to a test market in a way that gave added confidence that the test market would be successful, without involving the need for extended periods of intermediate testing. This had been achieved through the use of an external (Dupont) panel whose characteristics had been recorded in a way which enabled markets to be simulated on a small scale. This had enabled Brown & Williamson to cut down significantly on the cycle-time and cost for testing new products.
12. Mr. Mercier stressed the importance of differentiating qualities required by different consumer groups. In Canada, certain qualities which were a plus for Players smokers would be a substantial negative for du Maurier smokers and vice-versa. JPS, which in theory was the best cigarette Imperial made, appeared not to appeal strongly to any group and had a very low market share.
13. When Imperial made changes to the composition of du Maurier (e.g. to reduce tar levels), care was taken to have each new variant tested by the established du Maurier panel of smokers.
14. It was noted that BATCF place a high priority on both the physical characteristics of their products and also smoking quality, which is monitored against competitors on a regular annual basis. In cases where BATCF products are found to be inferior, appropriate development programmes are initiated.
15. Although Marlboro has shown a steady improvement year by year, Lucky Strike is still thought to be superior on BATCF's criteria. HB is judged to be inferior but some apparently 'bad' qualities may make the cigarette more attractive to older smokers.
16. BATCF will consider whether the Dupont techniques might be adopted in developing improved tests.
17. It was noted that smoking quality was still a problem in Souza Cruz and improving this would be given a high priority in 1991-1992.
18. Within BATCo., OMEGA testing panels were being established and were in place in most companies. However, it was recognised that smoking quality still needed to be given a higher priority. Current initiatives included improved training programmes. Consideration was also being given to the need to upgrade the function of quality controllers so that this became more of a job in its own right rather than a staging post for developing managers.
19. It was suggested that further consideration should be given throughout the Group to reducing the numbers of blenders and to increasing the status of the few really expert blenders that a company required in order to be able to develop and maintain product quality.
20. It was noted that another key element in achieving and maintaining quality was the way in which the tobacco was processed. In Brown & Williamson, a change in the re-drying process for burley had been identified as the cause of a sharp fall in smoking quality in repeat tests on a product whose composition had apparently been unchanged. The quality of Marlboro was also thought to depend more on their process than on the quality of the Tobacco used in their products.

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21. It was agreed that the Chairman would organise a meeting with Mr. Kohnhorst, Mr. Andrade and representatives from BATCo. and BATCF to consider what should be done:-
  - (a) To establish a better interchange of experience on quality testing within the Group.
  - (b) To improve the effectiveness with which smoking quality is measured and monitored.
22. It was agreed that smoking quality should be given a higher priority and that each company should be asked to include in their plans a section on improving the measurement and upgrading of smoking quality.

Marketing Issues

23. **Marketing Information System** : Mr. Bramley reported that the work to develop a common information base of marketing data, accessible by all Operating Groups, was almost complete. However, there were still a few issues to be resolved on the type of data to be collected (e.g. shipments or end market sales), on the arrangements for access and on the costs of setting up and maintaining the system. Mr. Bramley will set up a meeting to resolve these issues and will make recommendations to the next meeting of the team.
24. **Sponsorship** : It was noted that the Lucky Strike sponsorship of Motor Cycle racing appeared to be fulfilling its objectives. However, the cost-effectiveness of sponsorship associated with the Group's other international brands needed further review:-
  - (a) The programme for Benson & Hedges will be reviewed by the new marketing director for BATCo.
  - (b) The programme for SE555 needs better definition and a more effective use of sales of peripheral products closely associated with the main sponsorship.
  - (c) The Kent programme is thought to be too fragmented and to lack a strong central theme.

Mr. Bramley and Mr. Pritchard will report back to the next meeting on the results of these reviews.

25. It was noted that German TV may refuse to televise Motor Sports on the grounds that they are sponsored by Tobacco companies. It was agreed that Mr. Herter would check on this and find out whether the Motor Sports themselves were opposing this ban. In the meantime, the possibility of a ban should be taken into account when signing any contracts.
26. **Trade Mark Diversification** : It was agreed that companies should keep within the spirit as well as the letter of the law in any promotions of non-Tobacco products carrying Tobacco trademarks.

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International Brands

27. **US International Brands** : Mr. Pritchard reported that US export and contract sales were 2 billion below budget for the first quarter. However, after reviewing the situation with regional managers, it had been agreed that the budget was still achievable and might be exceeded by up to 2 billion.
28. For **Kent**, it was noted that while shipments were below budget, in-market data suggested that final sales to consumers were holding up well. Deviations from the standard specifications for the brand were being eliminated progressively but it was noted that there was a continuing problem in South Africa. It was agreed that if Kent could not be produced to the US specification, the brand should be withdrawn from the market.
29. **Lucky Strike** continued progressive but there was still a need to improve distribution in Spain. A problem in some markets was that the brand had been introduced before ammonia treatment was specified as an essential part of the manufacturing process. Companies without stainless steel equipment in their primary departments were still unable to introduce this treatment as a standard part of the process. Elsewhere, there had been progress in upgrading quality, including further reductions in the use of local leaf in Spain.
30. **Pricing** : Lucky Strike was designed to compete directly with Marlboro and it was agreed that the basis for this should be to achieve parity in quality while offering the consumer an incentive to buy by positioning the brand up to one price point below the Philip Morris brand. As an alternative, it might be possible to compete at an equivalent price on the basis of better smoking quality. What should be avoided is positioning the brand two price points below Marlboro. This degraded the image and might actually be inhibiting sales in some markets (e.g. Malaysia). In cases where Lucky Strike was positioned more than one price point below Marlboro, there should be an aim to increase the price to the target level by end-1992 at the latest. Mr. Pritchard was asked to monitor progress towards this target.
31. **Barclay** : It was noted that the agreed strategy for Barclay was to launch the 2mg (Ultra) version as soon as possible in all markets, allowing this to become established for at least 2 months in distribution before the standard version reverted to a 5mg rating. The timing for the subsequent introduction of the 1mg (Ultra) version is less critical.
32. Because of the (Borgward) testing regime in Benelux, the Ultra product will only achieve a 3mg rating in these countries. However, it was agreed that it should still be launched in the same way and to the same timetable as for the 2mg product in other markets.
33. **UKIB** : Mr. Bramley reviewed progress in UK International Brands and it was noted that there was a plan to upgrade the blend for Players Gold Leaf (PGL). It was suggested that there was a need to revitalise SE555 and PGL, both of which were felt to have a greater potential than was being realised at present. There was continuing concern that SE555 should be targeted at a younger market and that the promotional spend might be too low. The target market for PGL was also thought to be too 'highbrow' in relation to the brand's image.

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34. **France** : The Chairman was disappointed that no paper had been put forward discussing options for acquiring the rights to Lucky Strike in France. Mr. Broughton was asked to follow-up on this. The Chairman also asked Mr. Pritchard to give further consideration to the possibility of licencing Barclay to SEITA.

Eastern Europe/USSR

35. Mr. Herter reported that, excluding the special sales to the USSR and even after allowing for the change in status of the East German market, the sales increase in the Eastern European markets had slowed considerably as a result of the difficult and volatile economic situation in these territories. He also noted that although sales in Yugoslavia were holding up well, there was a switch from exports to licenced sales with a consequent reduction in profits.
36. Mr. Pritchard and Mr. de Castro reported that Brown & Williamson and Souza Cruz were also experiencing difficulties in selling to the USSR and Poland but were continuing to seek opportunities where these arose.
37. **Hungary** : Mr. Bramley reported that negotiations were continuing with the SPA on the possibility of moving to a majority holding in the company in Pecs.
38. **Poland** : Mr. Herter reported that talks were continuing with the ministries of privatisation and agriculture in Poland regarding the factory at Augersdorf and auditors were currently valuing the company. A draft letter of intent would be discussed with the Chairman within the next few days prior to submission for approval by the CPC.
39. **USSR** : Mr. Herter reported that an office had been set up in Moscow and that the recruitment of staff was in hand. It was noted that the Chairman would visit the USSR in September for a meeting of the Anglo-Soviet Round Table.
40. The Czechoslovakian market had been researched and a report would be available for the next meeting.
41. **Romania** had also been researched but Mr. Pritchard reported that the market was in a state of disorder. A further study of the industry structure and potential opportunities for investment would be put in hand. Mr. Herter had also provided the name of a potential candidate to provide representation in the market.
42. Mr. Herter also reported that a representative had been appointed in Bulgaria and that it was intended to replace the representative in Yugoslavia.

Other European Markets

43. It was noted that Brown & Williamson's representative in Greece had moved into the BATUKE office, that the representative in Portugal had moved into the BATCF office and that the representative in Sweden had moved into the Tiederman's building in Stockholm.
44. In Turkey, it was hoped that the distribution of cigarettes would be privatised but importation would still be subject to restrictive legislation. It was intended to open a liaison office in Istanbul.

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Latin America/Caribbean

45. **Mexico** : Mr. Pritchard reported that the US Congress had agreed to extend the 'fast track' authority to the negotiations for the extension to Mexico of the North American Free Trade Area. Brown & Williamson will press to have tobacco products included in any agreement. Although the Group would prefer to wait until it is known what the new trade regime will be, formal applications to be allowed to import cigarettes will continue to be pursued and opportunities to manufacture will also be evaluated. Mr. Pritchard will also confirm that the FTA would not open the Mexican market to exports of Kent from Lorillard.
46. **Colombia** : It was noted that a meeting had been held to co-ordinate the efforts to exploit the opportunities arising from the opening of the Colombian market.
47. **South Cone** : Mr. Bramley was asked to set up a working party to report back on the implications for the Group of the projected 'South Cone' common market.
48. **Caribbean Representation** : The Chairman asked Mr. Bramley and Mr. Pritchard to give further consideration to the possibilities for rationalising the Group's representation in the Caribbean, in order to improve the cost-effectiveness of selling in the region.

The Far East

49. It was noted that efforts were continuing to penetrate the market in Thailand and De La Rue were printing Tax Stamps for use there. However, the authorities were still placing barriers in the way of imports. Negotiations were continuing in Burma and Vietnam.
50. **China** : It was noted that following a meeting on 29th April of the people directly concerned, Mr. Bramley was proceeding with the recruitment of the key personnel required to head up the companies which it had been decided to form in order to provide a more effective thrust in the China market. The Chairman asked for a note to be prepared for the CPC as soon as possible, confirming what is proposed. It was also suggested that setting up the new companies could pre-date the appointment of the respective CEOs.

Manufacturing

51. Mr. Kohnhorst presented a review of the Group's manufacturing facilities. It was noted that this showed a reasonable level of cover for expected sales up to 1993 but possible shortages of capacity towards the middle of the decade. Mr. Kohnhorst was asked to extend the study and to identify where additional machinery orders needed to be placed to provide a capacity 15% greater than the sales forecast to 1995.
52. Other conclusions from the review were that:-
  - (a) The capacity increases should be concentrated in Brown & Williamson, BATUKE and BATCF rather than in the smaller companies.

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- (b) The ability to produce high quality International Brands remains paramount and there should be an aim to increase the ability to transfer production from one factory to another.
  - (c) Upgrading the standard of the production facilities in Brazil remains a key requirement and further consideration should be given to the feasibility of importing second-hand machinery from the USA. //
53. Mr. Broughton presented a paper comparing the contributions from different markets and from brands produced in different locations. It was agreed that this had been a useful exercise but it was felt that it was better to carry out studies of this type ad-hoc rather than setting up a system to collect this data on a continuing basis.
54. It was agreed that Mr. Kohnhorst should be asked to recommend a consistent scheme for measuring and comparing production costs, groupwide. M
55. It was also suggested that further thought should be given to possible transfers of production in order to improve net profitability (i.e. after taking into account the effect of taxation and the ownership of the company producing the cigarettes). Transferring contract manufacture to Southampton would appear to be particularly advantageous from this point of view.
56. **BATCF** : It was noted that Mr. Berter had produced a paper for the CPC outlining the options for expanding capacity in Germany. This was presented to the team for information. It was noted that capacity in Germany could be expanded to 50 billion p.a. without major structural additions or changes to the existing facilities.

Leaf

57. **Leaf Rationalisation** : Mr. Pritchard reported that the classification scheme introduced last year was working satisfactorily. The Chairman asked for a further review of the impact of the scheme in rationalising buying (e.g. had it resulted in a reduction in the number of trips to buy tobacco in Brazil) and in reducing stocks. Mr. Pritchard will report on this at the next meeting.
58. **Supply Situation** : It was noted that Burley tobacco could be in short supply in 1991-1992, especially if RJR and Philip Morris, who have been running down stocks, again become major buyers. It was again emphasised that companies must ensure that they have security of supply for the types of tobacco they require. J. Hunt
59. **Exports** : It was also suggested that Leaf exports could represent a significant opportunity for the Group. BATCo. and Souza Cruz were asked to give increased emphasis in their plans to building up a 10-year plan for expanding exports.
60. **Leaf Co-ordination Meeting** : It was agreed that since the Leaf specialists within the Group meet at least once a year, there was little justification for organising an extra co-ordination meeting of the type which had been suggested by Souza Cruz.
61. However, it was noted that Leaf processing was a key element of the manufacturing process which was not understood sufficiently well and where it might be advantageous to exchange expertise. Mr. Pritchard was asked to outline a proposal for setting up a meeting to discuss this topic.

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Management Development

62. **Training and Development Review** : Mr. Broughton reported progress on Mr. Ross' project to consider possible improvements to the training and development of managers in the Tobacco businesses. He also confirmed that the project was on track for completion by end-July.
63. Discussing the progress report, it was suggested that the final report should be related to a single population of managers and that it should be assumed that the expatriate pool would be phased out.
64. It was also suggested that although movements between functions could be advantageous later in a manager's career, the first priority in training and development should be to improve managers' effectiveness within their functional specialisations.
65. It was noted that the Chairman and Mr. Broughton would agree with Mr. Ross, the headings for his final report.
66. **Inter-Company Transfers** : Mr. Bramley reported that there had been continuing progress in arranging inter-company transfers. A review meeting would be held in June and he would present a formal report, reviewing progress over the year, at the meeting arranged for September.
67. **Recruitment** : Mr. Herter reported that the team set up to consider possible problems in recruiting staff to support the projected expansion in Eastern Europe had met and had made significant progress in manning the teams.
68. It was noted that the project team for Poland was largely drawn from BATCF while the team for Hungary was largely from BATCo. While it was appreciated that this was a historical accident, it was suggested that there should be a positive effort to make future teams international in composition.

Trading Results

69. It was noted that a key feature of the results for the first quarter had been the 5% increase in volume relative to last year. However, the full year forecast was for a volume increase of only 3½%.
70. It was noted that the current forecast for the Group shows profits slightly lower than 1990 at the half year. It is important, therefore, that results equal to the budget are achieved in the second quarter. Mr. Broughton will be in touch with individual Operating Groups on this in the near future.

Regulatory Issues

71. **Environmental Charter** : It was noted that none of the Tobacco companies wished to sign the charter proposed by the ICC. However, there may need to be further discussion on this before and during the environmental policy review by the B.A.T Industries Board, due in October.
72. **Smoking Compendium** : Mr. Bramley reported that a revised version of the Smoking Compendium would be available for distribution shortly.

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73. **Environmental Tobacco Smoke** : Mr. Pritchard reported that discussions on the EPA report were continuing.
74. **Fire Safety** : He also reported that there had been no further progress on the proposal to develop tests for a 'fire-safe' cigarette.
75. **Additives Register** : Mr. Bramley reported that the Additives Register would be available for distribution later in the year.

Production/Process Development

76. It was agreed that the discussions of **Sidestream Smoke**, **Y-1 Tobacco**, **Decomposition Products of Ammoniated Tobacco** and the use of **Reconstituted Stem** should be held over the next meeting.

Next Meeting

77. The next meeting will be held on Friday, 6th September. Key subjects for discussion at this meeting will be the competitive position in technology (the Chairman's letter dated 1st May refers) and the Research priorities for incorporation in the R&D programme.

RS/DJA  
6th June 1991

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