

**Tobacco Strategy Group
Thursday 9th February 1995
Agenda Item 6
Future Business Environment**

A paper entitled "Future Business Environment" will be presented to the Group Board in April and sent to the Operating Groups, incorporating the Group Board's comments, by the end of April.

The purpose of the paper is to review the likely trends in the Group's operating environment and to record the assumptions agreed by the Board for use in B.A.T Industries' planning. The main assumptions to be used and issues to be addressed in the Plans are set out in the paper. The main time periods covered are the short term, to the end of 1996, and the medium term to the end of 2000, corresponding to the periods covered by the next round of budgets and plans. The longer term prospects to 2000 and beyond are also taken into account where it is relevant to do so.

The paper will comprise three sections, the first containing a broad overview of the economic outlook, and the second and third containing the main assumptions and issues for Tobacco and Financial Services respectively. The CEC wishes the paper to continue to focus on the business implications from the economic and business environment forecasts. Therefore each section will be set out as an issue for BAT and an assessment of the position for discussion.

The purpose of the attached paper is to propose to the TSG a list of key issues or sensitivities facing the Tobacco business which should be addressed as part of the Future Business Environment paper.

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Environ
Tobacco

Future Business Environment 1996 - Key Issues facing the Tobacco Business

1. **Politics and Lobby Groups**

Tobacco is an easy target for increased **taxation**, which can reduce market size and distort competitive positions

However, there is now the precedent of **roll backs** which are an effective weapon against smuggling ?

One of the main threats in the US is from litigation and particularly **class actions**

Also in the US, the threat of **FDA regulation** has receded

Regulations continue to increase, including

- advertising restrictions
 - larger health warnings and plain packaging
 - smoking restrictions as a result of ETS concerns
- Philip Morris

2. **Consumers**

Half the world's smokers are in Asia-Pacific, and this proportion will increase. Hence the importance of the **emerging markets**, particularly China, India and Indonesia, to the future of the business

In markets where the economic recovery has not brought a "feel good" factor, consumers are **price sensitive** *Philip Morris*

In booming developing markets, there is **up-trading**, often to the benefit of Marlboro

In some markets, the decline in **smoking incidence** in some segments of the population appears to have bottomed out ?

Where consumers have the spending power, there is a shift to **International Brands**. Where spending power is limited, **local brands**, which appeal to local culture and heritage, are strong //

There is consumer demand for a **satisfying product** with fewer health concerns and less nuisance to non-smokers, hence the attempts to develop **smokeless** cigarettes, and the increase in the **Lights** segment

3. **Competitors**

Price wars are very damaging to the short and medium term profitability of markets

As developed markets decline, competitors have more **excess capacity** which may serve to keep prices down and increase competition in export markets

Philip Morris probably overtook BAT in volume terms outside the US in 1994. Are the steps we have taken through investing in new markets and agreeing market and brand strategies, sufficient to reverse this trend?

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