

**“Marketing Strategy of Pakistan Tobacco Company  
after the implementation of International Marketing  
Standards”**

By

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## *Executive Summary*

Pakistan Tobacco Company Limited is part of British American Tobacco, the world's most international tobacco group, with brands sold in 180 markets around the world.

PTC produces high quality tobacco products to meet the diverse preferences of millions of consumers, and works in all areas of the business - 'from seed to smoke'.

PTC operations in Pakistan began in 1947, making them one of Pakistan's first foreign investments. PTC is committed to providing consumers with pleasure through excellent products, and to demonstrating that it meets the commercial goals in ways that are consistent with reasonable societal expectations of a responsible tobacco group in the 21st century.

The marketing standards worldwide in the tobacco industry have changed and the tobacco industry today is operating in an environment which can be called as a marketer's nightmare. It is governed by the International Marketing standards, or the "New world of marketing", where virtually all above the line marketing, advertising, promotions and mass media stuff is prohibited by law in almost all the countries in the world. PTC being a responsible company and as a part of a global initiative was the first to embrace the IMS and is actively pursuing the government and all the other stakeholders to move forward and implement the International Marketing standards in its full letter and intent.

While this has helped PTC to be recognized as a socially responsible company, on the other hand it has handcuffed almost all of its marketing efforts because now it is only restricted to below the line and a very targeted and a focused marketing strategy.

This thesis would encompass in detail the new face of marketing in Pakistan Tobacco Company in the new world of marketing as they call it, and would seek to find out the strategies and the actions that the company is working with to effectively and efficiently market its product to its consumers in the face of intense competition and heavy regulations. It would also discuss the current distribution and marketing structure of PTC with respect to trade marketing and how PTC is trying to reorganize in a market which is both competitive and challenging.

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# Introduction



British American Tobacco is the world's most famous international tobacco group, with brands sold in 180 markets around the world. They produce high quality tobacco products to meet the diverse preferences of millions of consumers, and work in all areas of the business – 'from seed to smoke'. BAT's operations began in 1902, and this year they are celebrating their centenary – 100 years of truly multinational operations. BAT's companies are committed to providing consumers with pleasure through excellent products, and to demonstrating that they are meeting their commercial goals in ways that are consistent with reasonable societal expectations of a responsible tobacco group in the 21st century.

British American Tobacco is operating in more countries than any other. It does business in 180 countries, with a global market share of 15.1 per cent. With over 300 brands in their portfolio, they make the cigarette chosen by one in seven of the world's one billion adult smokers. BAT's goals are not only to continue creating long term, sustainable shareholder value, but also to lead the tobacco industry in demonstrating corporate social responsibility and wider accountability. The products are risky and industry can be seen as controversial. The products are legal, no governments or serious campaigners seek prohibition, and about a billion adults choose to smoke worldwide.

Through 100 years of operations, they have built a strong international reputation for high quality tobacco brands to meet consumers' diverse preferences. BAT holds strong market positions in each of its regions and has leadership in more than 65 markets. The Group has over 80 factories in 64 countries, processing some 660 million kilos of leaf and producing over 800 billion cigarettes a year. Today, BAT is acknowledged as one of the world's leading Fast Moving Consumer Goods companies. They acknowledge the significant responsibilities that the business entails, and are working hard to demonstrate how they are carrying them out.

(Source: British American Tobacco, Globe House)

## 1.1 Tobacco Industry In Pakistan

Tobacco industry — growing, manufacturing, distribution and retailing — contributed 4.4 per cent or over Rs.27.5 billion to the total GDP of Pakistan including Rs 15.17 billion, including Rs.14.54 billion in excise duty and sales tax, in 1997. It is the single biggest contributor of excise duty, six-times than that from cotton yarn. Over 5 per cent of all taxes collected in the country come from the tobacco industry. It employs over one million people directly or indirectly which in terms of full-time equivalent jobs means 312,500 jobs supporting some 1.2 million persons.

The area under tobacco cultivation increased by 30 per cent during 1990-91 to 1998-99 — from 44,000 hectares to 57,000 hectares. The production has increased even more significantly during the same period — by 145 per cent from 75,000 tonnes to 109,000 tonnes. The value-added sector, the cigarette production, depicted a far more unproportionate increase of 72 per cent — from 29.8 billion sticks to 51.5 billion sticks during the same period.

Tobacco is the only crop grown in Pakistan whose yield is well above the world average and matches the per hectare yield in the US and other developed countries — an average yield of 1,900 kilograms per hectare. Tobacco industry — growing, manufacturing, distribution and retailing employs over one million persons directly or otherwise. This translates in the full time equivalent of 312,500 jobs supporting approximately 1.2 million persons. Manufacturing employs the highest number of persons — 35 per cent followed by 33 per cent by growing and 32 per cent in distribution and retail.

### **Smuggling**

It is easy to understand the threat of huge revenue loss that presence and easy availability of smuggled cigarettes pose to the economy of Pakistan. The government is losing a substantial revenue of Rs 3 billion from the smuggling of cigarettes into the country. According to Aslam Khaliq, the director Corporate and regulatory affairs of Pakistan Tobacco Company, the second top cigarette manufacturer after Lakson Tobacco, the government is losing at least Rs billion every year due to cigarette smuggling. He blamed the high taxation as the singular most important incentive for cigarette smuggling.



This is true if one looks at the global trends of taxation on cigarettes. Smokers in Pakistan pay the highest tax in the world second only to Denmark and the UK where 85 per cent and 82 per cent of the retail price respectively goes toward taxation. In Pakistan, 78 per cent of the retail price of premium brands ( all brands whose retail price is over Rs 10 per 20 sticks) and 58 per cent of the retail price of low segment brands go toward taxation.

### **Price war**

Defending the price war started by PTC by slashing the prices of a number of its middle-priced brands early this year, Aslam said that it brought numerous domestic manufacturers in the excise duty and sales tax net. For instance, slashing the prices on some of its brand by 50 per cent from Rs 19 to Rs 9 reduced the excise duty from 63 per cent to 43 per cent with sales tax remaining unchanged at 15 per cent. Despite price reduction, Aslam said, PTC was able to break even due to increased turnover and at the same time forced manufacturers who did not pay excise duty and sales tax in the net to create a level playing field.

Though worried about smuggling and high taxation, Aslam expressed that cigarette prices in Pakistan are on the much low side. He said that the manufacturers should be allowed to increase the prices of their products to better their revenues which are constantly threatened by massive smuggling. He also suggested that price increases would help discourage smoking in the country.

True. Experience in many countries show that each 10 per cent increase in cigarette prices results in a 5 per cent decrease in the numbers of smoking adults and much more in young adults — between 6 to 8 per cent — who have little surplus funds to spend on smoke. However, the argument that high prices discourage smoking is a bit flawed particularly in the context of Pakistan.

Number one, unlike all developed and many developing countries Pakistan choose not to spend even a negligible portion of tobacco taxes on healthcare, research, education, and anti-smoking activities. Such developing countries, not to mention the developed ones, as Nepal and Peru spend a share of cigarette taxes to support cancer research and treatment. Latvia allocates 30 per cent of the revenue which it earns from the tobacco tax on healthcare. Iran earmarks a portion of tobacco tax revenue on healthcare and education.

Secondly, if the manufacturers and policy makers are really serious about reducing smoking in Pakistan through price increases — and no one say that they are — they need to raise taxes on all brands of cigarettes be it locally manufactured — imported. Supporting the domestic tobacco industry against imports, as is the case with Pakistan, may be good for the local industry but negates the very argument that higher prices and taxation discourages smoking.<sup>1</sup>

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<sup>1</sup> <http://www.pakistaneconomist.com/issue2000/issue31/i&e4.htm>

## 1.2 Global Tobacco Industry:

### Introduction

Tobacco products are being chewed, snuffed, and (mostly) smoked all around the world. People have been consuming tobacco products for centuries. Tobacco is also grown in many places. Originally from the Americas, since 1492 it has spread far and wide. Today, tobacco is grown in over 100 countries.

No other product has stimulated demand for tobacco as much as the cigarette. Until the 1870s, cigarettes were mainly rolled by hand. Today, they are made by machines. Thanks to these machines, which can produce hundreds if not thousands of sticks per minute, cigarettes have become an article of mass consumption. In the process, cigarettes have become the main tobacco product (box 1). Today, over 80 per cent of tobacco grown is used for cigarettes. The world market for cigarettes is dominated by a low and steadily diminishing number of suppliers.

#### **Box 1. Tobacco usage**

It is useful to distinguish smoking from smokeless tobacco. Smokeless tobacco is tobacco that is consumed in an unburned form. The main types of smokeless tobacco are snuff and chewing tobacco. Snuff is powdered tobacco that can be inhaled through the nose or taken orally. It is popular in the United States and in Scandinavia. *Plug*, *loose-leaf* and *twist* are the main types of chewing tobacco used in Western Europe and North America but their use is in decline. *Pan* chewing (or *betel quid*) chewing is popular in South and South-East Asia. Cigarettes are the most popular type of smoking tobacco, as indeed of all tobacco. They can be without filter, but most are sold with filter-tips. They are machine made, but an important (sub-market) segment consists of Roll-Your-Own (RYO) cigarettes. *Bidis* are popular in India, where eight times as many *bidis* are sold as cigarettes (but sales of cigarettes are increasing more rapidly). *Bidis* consist of a small amount of tobacco wrapped in *temburni* leaf and tied with a small string. *Cheroots* are small cigars made of heavy-bodied tobacco; they have no wrapper and contain a single binder. *Kreteks* are indigenous cheroots containing tobacco, cloves and cocoa. *Kreteks* are very popular in Indonesia, where three times as many *kreteks* as cigarettes are being produced. Cigars come in many shapes and sizes from cigarette-sized cigarillos to 10 g. double coronas. Lastly, pipe smoking is one of the oldest methods of smoking tobacco. Pipes are smoked around the world but they differ in size, shape and material used. Certain water pipes allow a number of people to smoke simultaneously from the same pipe. Sources: Corrao et al., 2000; WHO, 1997.

The tobacco industry is no longer growing at the steady pace of the years prior to 1990 (Chapter 2). World cigarette demand was virtually flat in the 1990s. Demand is weak in the established markets of the OECD area. In North America it has been declining since the early 1980s (figure 1). US cigarette companies also face the problem of litigation (section 3.3); they are defendants in hundreds of lawsuits.

But the picture is not all bad for the large tobacco companies. Profits are good.<sup>1</sup> In the 1990s, the more internationally-oriented among them saw huge increases in sales volume. They “conquered” large shares of the East European and Russian markets when these countries liberalized their trade and investment regimes and privatized their former state monopolies. China, at one-third of the world market by volume, is the big prize that so far has escaped them. But in China their market share can only go up. The question is how far and how fast this will take place.

<sup>1</sup> Among the 150 largest US companies, Philip Morris was the only one to show average earnings growth per share of over 15 per cent per year for the period 1960-99 and for each of the subperiods (1960-80; 1970-90; and 1980-99) (FUW 25/4/01).

## 1.1. Tobacco and cigarettes

Tobacco is an essential ingredient for cigarettes, cigars, RYO (roll-your-own) tobacco, pipe tobacco, cigars, snuff and chewing tobacco. That is not to say that the *value* of tobacco in cigarettes and other tobacco products is necessarily high. In fact, in many OECD countries its share in total value is low compared to that of taxes, advertising and

Most tobacco is used for cigarettes. In the early 1990s, it was estimated that at least 80 per cent of tobacco leaf was used for cigarettes (FAO, 1990). Today, this might well be higher as demand for cigarettes is seen to outgrow that for other tobacco products.

Demand for tobacco is thus in large part determined by demand for cigarettes. The volume of tobacco sold in the world can be expected to closely follow increases (or

decreases) in the demand for cigarettes. That is not to say that demand for tobacco increases at the same pace as that for cigarettes. Historically, the amount of tobacco used per cigarette has decreased as a result of the increased use of filter tips; of the smaller diameter of cigarettes; and of reduced waste due to more efficient packing technologies. In addition, the proportion of leaf that can be used has increased through advanced processing technology (FAO, 1990).

### ***1.1.1. Different types of cigarettes use different types of tobacco*** <sup>3</sup>

Neither tobacco nor cigarettes are a homogeneous product. Due to the different conditions (type of soil, rainfall, irrigation, and climate) in the various tobacco growing regions, tobacco leaves vary in size, thickness, color, and flavour. Factors like the environment, the leaf's position on the stalk, harvesting, curing (i.e. drying), handling and processing, all influence the quality of the leaf and ultimately the smoking product. The sugar and nicotine ratios of the leaf account for the overall aroma and flavour of the tobacco leaf. The quality of the leaf is determined by its colour, texture, body, thickness, strength, flavour, aroma, rate of burn and processing qualities. Quality is expressed in grades. The US Department of Agriculture (USDA) recognizes 117 official grades of tobacco.

There are basically four types of cigarettes: Virginia ("flue-cured"); <sup>4</sup> "American" blend; dark; and oriental cigarettes. The latter two, dark (traditionally popular in French-, Spanish-, and Portuguese-speaking countries) and oriental (traditionally popular in the Eastern Mediterranean, Eastern Europe and the (former) USSR) have lost ground to the first two. Virginia (or "English") cigarettes are made almost entirely from flue-cured Virginia tobaccos. They are popular in the UK and in its former colonies. The American blend is currently the most popular type of cigarettes. Its world market share continues to grow. The main tobacco components of the American blend are flue-cured Virginia (approx. 50 per cent), Burley and Oriental (around 12 per cent). In addition, each cigarette brand uses a specific mix of tobaccos (and other ingredients such as sugar and aromatic substances) to give it its characteristic taste and to set it apart from its competitors.

The term “flue-cured” comes from the artificial curing (or drying) system by which metal pipes (“flues”) are used to distribute heat in curing barns as a means to remove all of the natural sap and moisture from tobacco leaves.

Virginia flue-cured is thus the main source of cigarette tobacco today. Its share in total unmanufactured tobacco has increased as a result of the popularity of Virginia and American Blend cigarettes (figure 2). Originally from the (US) state of Virginia, today it is grown in many countries. US leaf is considered to be the best ingredient for providing quality, flavour and aroma to cigarettes but it is expensive. Its high price (compared to non-US tobaccos) was once justified by its superior quality, but the quality of leaf from other countries has improved. Therefore it is no longer as important as it was for manufacturers of quality cigarettes to use a high proportion of US tobaccos in their blend. Nonetheless, demand for US tobaccos is still considerable. Manufacturers are reluctant to change the mixture of tobaccos in their blend for fear of altering the taste and losing loyal customers. For existing brands, changes in the sources of supply will thus occur gradually (providing a degree of stability to the world tobacco trade). A more rapid way of reducing the use of expensive leaf is by including less of it in new brands or new variations of the general brand (e.g. in “light” cigarettes).

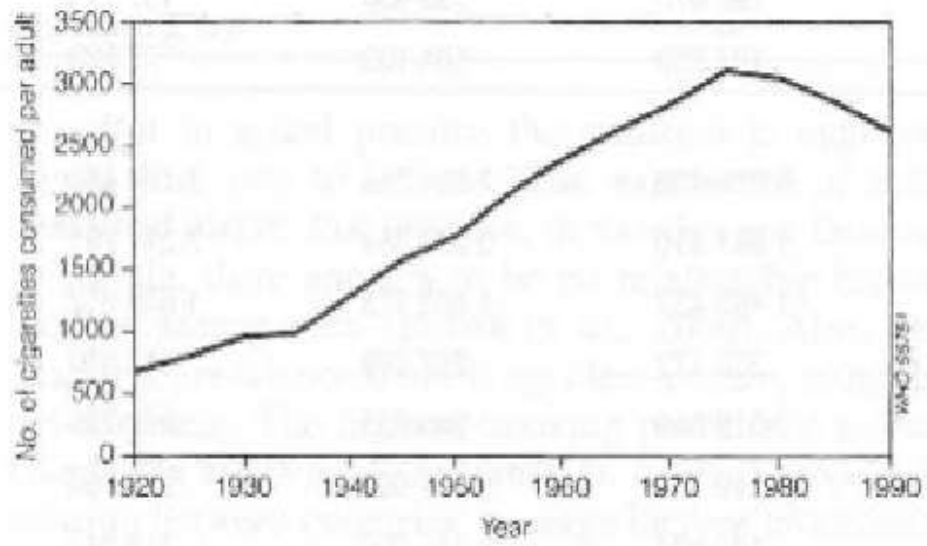
## **2. Consumption, production, and international trade**

In the world of tobacco and cigarettes many configurations co-exist. Malawi is an important producer of tobacco, but it exports 98 per cent of its crop. The Netherlands grows no tobacco of its own. Yet it is one of the world’s top exporters of cigarettes and cigars. The United States is a leading importer *and* exporter of tobacco as well as a leading exporter of cigarettes. And there is China, the world’s largest producer of raw tobacco, and the world’s largest consumer and producer of cigarettes whose participation in world trade of tobacco and cigarettes is very modest (see also box 2 on the China factor). We shall start with a discussion of demand and of demand trends. Data on world tobacco consumption and world cigarette production by country are available. But data on demand for cigarettes by country are more difficult to obtain. With the help of production and trade data “apparent demand” can be calculated. The second part of this chapter considers production and international trade.

## 2.1. Consumption

Worldwide, the production of tobacco and the consumption of tobacco products increased steadily until the early 1990s. Between the early 1970s and the early 1990s tobacco production increased by around 50 per cent in volume terms. Cigarette consumption and production increased at a slightly faster pace. Between 1990 and 1995, production of and demand for cigarettes grew at a more modest rate. Tobacco production reacted to this weakening of demand with a lag. After 1996, consumption appears to have declined. The Asian and the Russian crises dampened demand as did the drastic price increases in the US following the Master Settlement Agreement (section 3.3). On balance, according to the USDA, world tobacco consumption (at 6.5 million metric tons) and world cigarette production (at 5.5 million pieces) were no higher in 1999 than they were in 1991.

It should be kept in mind, however, that slow overall growth does not necessarily mean that demand growth for all countries or all categories of tobacco and cigarettes was slow. “American Blend” cigarettes have gained in market share. As a result, demand for the tobaccos that make up the American Blend has been above average (see also section 1.1.1). Per capita demand for cigarettes in the industrialized countries started to decline in the early 1980s (figure 3). After 1995, demand growth in the countries outside the OECD area slowed down and no longer compensated for declining demand in the industrialized countries.



1997

**Figure 3. Average annual cigarette consumption per adult in industrialized countries (1920-90)**

Source: WHO, 1997



**Table 1. World's leading unmanufactured tobacco producing, trading, and consuming countries (metric tons; dry weight; calendar years)**

	1995	1996	1997	1998	1999*
<b>Production</b>					
World total	5 541 142	6 563 927	7 720 562	6 438 201	5 926 859
China, People's Republic of	2 082 600	2 910 600	3 613 350	2 521 100	2 023 000
India	528 390	506 475	561 330	572 200	587 600
United States	513 247	619 432	729 139	626 504	571 526
Brazil	323 500	365 900	485 100	373 150	476 150
Turkey	170 070	190 391	250 836	217 570	215 640
Indonesia	145 650	150 450	148 775	175 825	185 005
<b>Exports</b>					
World total	1 759 091	1 981 981	2 004 521	1 907 289	1 949 663
Brazil	256 300	282 500	319 000	300 500	318 000
United States	209 482	222 316	221 512	211 917	230 000
Zimbabwe	174 289	195 958	159 941	168 804	205 500
Turkey	136 392	170 098	160 360	128 808	125 500
Malawi	99 057	95 555	111 449	135 300	107 600
Greece	133 000	130 250	103 000	97 179	100 000
<b>Imports</b>					
World total	1 778 246	1 949 282	1 960 464	1 858 915	1 712 450
Germany <sup>1</sup>	209 761	235 855	222 080	230 000	217 463
United States <sup>2</sup>	199 088	326 454	306 838	246 762	200 000
Russian Federation	148 110	148 000	184 900	200 830	165 000
United Kingdom	141 467	166 027	157 689	149 756	147 000
Japan	115 072	85 634	90 469	91 500	92 950
Netherlands	89 075	97 368	105 358	84 813	84 813
<b>Consumption</b>					
World total	6 305 704	6 453 712	6 374 201	6 287 785	6 282 163
China, People's Republic of	2 208 554	2 313 705	2 289 834	2 306 757	2 342 000
United States	699 200	706 688	673 927	634 412	662 488
India	463 920	472 326	476 850	483 360	478 310
Russian Federation	142 320	150 055	175 100	180 460	190 560

Indonesia	183 050	196 670	195 650	187 115	180 505
Japan	196 900	197 250	184 100	177 500	179 750
<b>Ending Stocks</b>					
World total	5 789 570	5 879 493	7 084 745	7 184 410	6 587 119
China, People's Republic of	1 390 866	1 941 310	3 079 364	3 211 291	2 807 691
United States	1 446 555	1 463 437	1 603 975	1 630 912	1 509 950
Turkey	320 595	268 172	292 898	313 010	334 150
Japan	370 251	318 049	280 235	252 735	221 681
Brazil	276 900	210 700	231 500	162 950	176 350
Italy	192 710	140 634	141 900	148 547	153 372
* Estimate; <sup>1</sup> Unified Germany; <sup>2</sup> General imports (actual arrivals). Source: USDA/FAS (Dec. 1999).					

On the whole, world demand and world production develop more or less in parallel. But this is clearer for cigarettes than it is for tobacco. Cigarettes are unsuitable for long-term stockholding. Their quality deteriorates rapidly and this is a powerful incentive for producers to adjust to changes in demand without too much delay. Other things being equal, trends in world cigarette production can act as a fair indicator of world cigarette demand.

That is not the case with tobacco. Tobacco stocks at year-end can be as high as the volume of production in that year (table 1). There are several reasons for this. First, tobacco can be stocked for a longer period than cigarettes before its quality starts to decline. Second, tobacco is an agricultural product. This makes it hard to predict with much precision the production volumes of different types and of different growing regions. Indeed, tobacco production volumes can vary considerably from one year to the next. Most manufacturers use a blend of different tobaccos in their product. Therefore they cannot risk having a shortage in a component part of their blend. They thus need sufficient stocks to tide them over from one harvest to the next. Lastly, stocks serve as a price-stabilization mechanism. Stocks do not just prevent supply shortages; they also prevent undue price increases following a poor harvest of a particular type of tobacco.

For individual countries and regions, demand for cigarettes is determined by a number of factors, including price, real incomes, macroeconomic developments, government efforts to discourage consumption (discussed in Chapter 4), as well as a range of structural and cultural factors. Retail price increases and a slowing economy have a negative effect on the demand for or the expenditure on tobacco products (but this sensitivity differs by each nation’s level of development and by socio-economic group). It may, but it need not lead to a reduction in the number of cigarettes consumed. People may simply buy cheaper cigarettes (“downtrading”). They buy local instead of imported cigarettes; popular instead of premium brands.

Structural and cultural factors also play a role. Why do people smoke, and why do they smoke the number of cigarettes that they do? On the whole, the average cigarette smoker is more likely to be male rather than female, with a low rather than a high income, and with fewer rather than more years of education. Far more smokers are found in less developed than in more developed countries (table 2).

**Table 2. Estimated number of smokers in the world (early 1990s) (in millions)**

<b>Countries</b>	<b>Males</b>	<b>Females</b>	<b>Total</b>
Developed countries	200	100	300
Developing countries	700	100	800
World	900	200	1100
Source: WHO, 1997.			

But in actual practice the situation is more complicated than these stylized facts would lead one to believe. The experience of many countries contradicts the picture described above. For instance, in Sweden and Denmark more women smoke than men do. In Russia, there appears to be no relationship between smoking and either education or income among men (Bobak et al., 2000). Also, among the countries with the highest smoking prevalence there is no clear pattern, either by geographical region or by level of development. The highest smoking prevalence is found in such low-income countries as Cambodia and Viet Nam (table 3). In the European Union, there appears to be no strong relation between countries’ average income levels and cigarette consumption (table 4).

Table 3. Estimated smoking prevalence among men (selected countries)

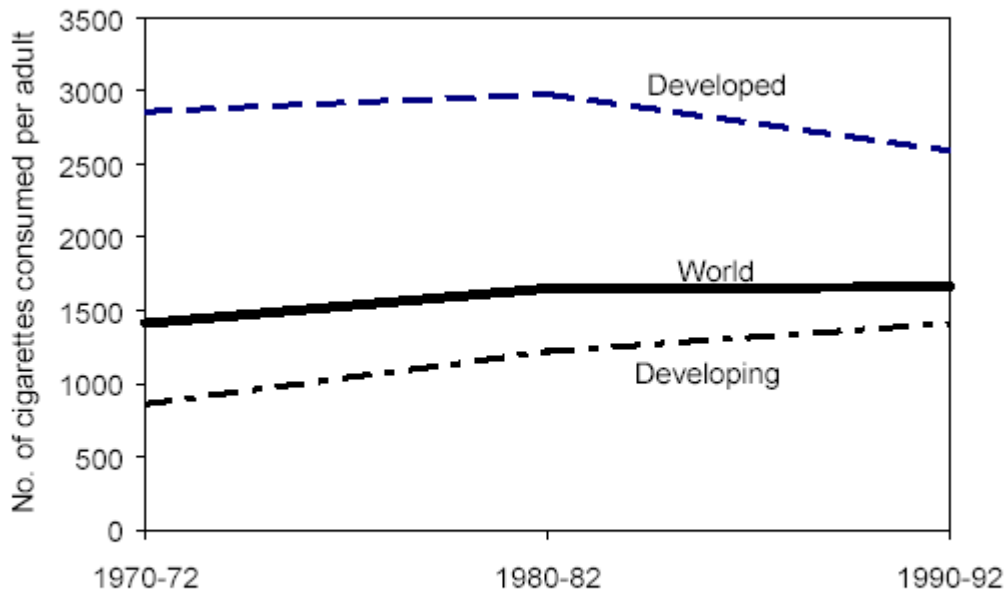
Income group	Country	Smoking prevalence
<b>Low income</b>	Cambodia	80
	Viet Nam	73
	China	63
	Bangladesh	60
	Sri Lanka	55
<b>Lower-middle income</b>	Latvia	67
	Russian Federation	67
	Dominican Republic	66
	Tonga	65
	Turkey	63
	Fiji	59
	Tunisia	58
	Panama	56
	Algeria	53
	Indonesia	53
	Samoa	53
	Estonia	52
	Lithuania	52
	Bolivia	50
<b>Upper-middle income</b>	Saudi Arabia	53
	South Africa	52
	Seychelles	51
	Poland	51
<b>High income</b>	Korea, Rep. of	68
	Japan	59
	Kuwait	52
Source: Bobak, 2000.		

**Table 4. EU cigarette consumption, 1996**

<b>Country</b>	<b>Average cigarette consumption per day by adults aged over 15</b>
Greece	9.3
Ireland	6.4
Spain	6.1
Germany	5.5
Austria	5.4
Portugal	5.4
France	5.2
Italy	5.0
Belgium	4.9
United Kingdom	4.8
Denmark	4.2
Netherlands	3.4
Sweden	3.2
Finland	3.0

Source: CGE, No. 452, July 2000 (based on INSEE).

Something similar can be said for trends. More men may be smoking cigarettes than women, but prevalence among women is on the increase. In the industrialized world, consumption per adult may be higher than in the developing world, but since the early 1980s it has been in decline (figure 3) and the gap between these two groups of countries is narrowing (figure 4). Between 1970 and 1990 per capita consumption grew particularly fast in the Far East (Annex table 1), but it levelled off in the 1990s in China and the Republic of Korea.



Source: WHO, 1997.

**Figure 4. Trends in annual per adult cigarette consumption in developed and developing countries (1970-92)**

What about demand in individual countries? In the absence of precise demand data we need to calculate “apparent demand” by deducting net exports (i.e. gross exports less imports) from domestic production. However, this figure may differ from real demand for two reasons. First, it takes no account of the variation in year-end stocks held by cigarette traders, wholesalers and retailers. Second, and more important, “apparent” demand takes no account of the share of demand that is satisfied by smuggling. Smuggled cigarettes take up a large share of the market in several countries.

Table 5 gives data on apparent demand for the world’s main markets. It shows that China is by far the largest market for cigarettes, followed by the United States, Japan,

Russia, Indonesia, Germany, Turkey, Brazil, India and the Republic of Korea. Demand in Indonesia and Turkey is increasing fast.

These data can be a poor indicator of value, though. Quality and prices differ from one tobacco and from one cigarette to another. US tobaccos, in particular, fetch high prices in the market. The quality of many Asian tobaccos, on the other hand, can be much lower. Their price may be one-half, or even one-third of US tobaccos. So in value terms, the share of the US is higher than the volume figures would seem to imply.

#### **Box 2. The China factor**

China plays a key role in the world tobacco industry. The country accounts for over 30 per cent of world consumption and production of cigarettes. Its share of tobacco production is around 36 per cent. Virtually self-sufficient in both tobacco and cigarettes, it is nonetheless a principal market for exporters of cigarette machines and cigarette paper. And because of the huge size of the Chinese market (between 300 and 350 million people smoke cigarettes), foreign tobacco companies are more than keen to sell their products there. The problem is that import barriers are high and joint ventures few (wholly owned production is excluded). Domestic demand growth is slow; more and more anti-smoking laws are being introduced. Production in 1998 was no higher than in 1993. Exports of tobacco or cigarettes have been few so far (but small amounts for China can be sizeable on a world scale).

Tobacco is also very important for China. Together, the production, processing and trade of tobacco and cigarettes provide employment to millions of people and a sizeable income to central, provincial and local governments alike. The tobacco trade and industry in China is controlled by a state monopoly run by the China National Tobacco Corporation (CNTC). The CNTC is highly profitable. Its profits amounted to the equivalent of more than US\$11,000 million in 1999. CNTC has been the State's top revenue generator for many years. It controls over 97 per cent of the Chinese market.

In anticipation of China's joining the World Trade Organization (and the resulting lowering of import barriers), the Chinese tobacco industry is undergoing a restructuring and modernization process. New, faster machines are being installed in an effort to raise productivity and quality. These also make more efficient use of raw material: in certain cases the amount of tobacco used per cigarette was found to have dropped by as much as one-third. Fewer machines are needed thanks to the higher levels of productivity attained. The number of production plants is also going down. From 180 in the early 1990s, the number of factories in operation had been reduced to 136 by 1999. Their number is expected to drop further, to around 100 in the early 2000s.

Source: Various.

**Table 5. World cigarette production volume, net exports (NE) and apparent consumption (AC). Selected countries and years (1,000 million pieces)**

Country	1985	1990	1995	1998	NE-98	AC-98
France	67	53	46	44	-40	84
Germany	165	164	221	178	40	138
Italy	78	65	50	52	-43	95
Netherlands	46	65	100	116	86	30
Spain	77	79	76	70	-12	82
United Kingdom	123	112	156	160	80	80
Switzerland	23	27	42	37	23	24
Bulgaria	92	82	74	46	15	31
Poland	90	81	101	95	3	91
USSR	381	350	141*	179*	-52	231
Egypt	47	41	42	47	1	46
Rep. of South Africa	28	32	37	36	–	36
Canada	63	46	51	50	1	49
Mexico	46	50	46	47	–	47
United States	665	670	746	716	197	519
Argentina	39	33	41	42	–	42
Brazil	146	160	173	178	73**	105
China	1178	1650	1735	1675	20	1655
India	80	85	95	106	1	105
Indonesia	106	155	186	214	17	197

Japan	303	268	262	250	-69	319
Rep. of Korea	75	86	87	96	-6	102
Pakistan	38	38	32	45	-3	48
Philippines	62	71	57	75	–	75
Turkey	61	62	99	114	8	105
Total	4860		5344		5598	
5608						

Note: \* Russia; \*\* No import data available.

Source: TJI/USDA and own calculations based on TJI/USDA.

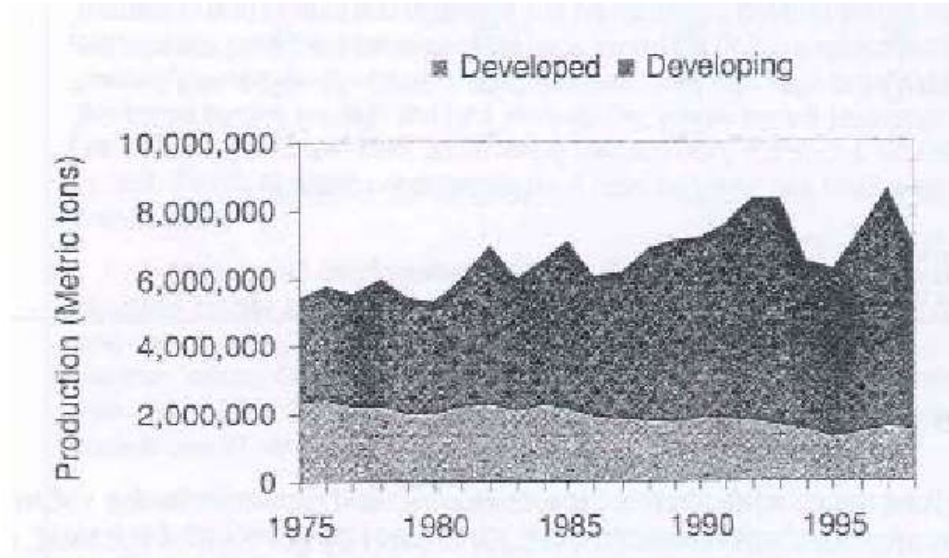


## 2.2. Production and international trade

Table 6 gives data on the share of major regions and countries in the volume of world production of unmanufactured *tobacco*. Asia, at around 60 per cent of the total, is the main tobacco producing region with China alone accounting for 36 per cent. China's share of world production, which had risen rapidly in the 1980s, was no higher in 1998 than it was in 1990. The shares of India, South America (mainly Brazil), and particularly Africa (Zimbabwe, Malawi) have not stopped increasing. The share of Europe (including Eastern Europe) declined (Italy's production dropped by one-third between 1990 and 1997) and that of the US remained more or less the same. By 1997, the developing countries accounted for 80 per cent of world production, compared to 53 per cent 30 years earlier (TJI, 5/97; and figure 5).

**Table 6. World unmanufactured tobacco: Production volume by main regions and countries (percentage; selected years)**

1985	1990		1995		1998*
<b>Asia</b>	<b>56.9</b>	<b>61.0</b>	<b>62.8</b>	<b>59.9</b>	
(China)	(31.6)	(37.2)	(36.5)	(36.1)**	
(India)	(6.9)	(8.0)	(8.9)	(9.1)**	
(Turkey)	(2.6)	(4.3)	(3.6)	(3.8)**	
<b>Africa</b>	<b>4.4</b>	<b>5.2</b>	<b>7.5</b>	<b>7.5</b>	
(Zimbabwe)	(1.6)	(1.9)	(3.3)	(3.0)	
(Malawi)	(1.1)	(1.4)	(2.1)	(2.0)	
<b>South America</b>	<b>7.7</b>	<b>8.2</b>	<b>8.8</b>	<b>9.2</b>	
(Brazil)	(5.7)	(6.2)	(6.3)	(6.2)	
<b>North America</b>	<b>13.5</b>	<b>13.1</b>	<b>12.4</b>	<b>14.1</b>	
(United States)	(10.0)	(10.4)	(9.0)	(10.4)	
<b>Europe</b>	<b>17.1</b>	<b>12.7</b>	<b>9</b>	<b>10</b>	
(including former USSR)					
<b>Total</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	
<b>Million tonnes</b>	<b>6.85</b>	<b>7.106</b>	<b>6.354</b>	<b>7.066</b>	
Note: * Provisional figures. ** 1997.					
Source: Own calculations based on TJI/USDA.					



**Figure 5. Tobacco production by developed and developing countries (1975-98)**

Source: Jacobs et al., (2000), based on FAO.

Cigarette producers make intensive use of domestic tobaccos. Nonetheless, around 30 per cent of world tobacco production (mainly high quality tobaccos) is traded internationally. There are several reasons for this. First, some large tobacco growing countries (Malawi, Zimbabwe, Tanzania) manufacture very few tobacco products of their own. Second, some important cigarette and cigar producing countries do not grow any tobacco domestically. The Netherlands (one of the world's top cigarette and cigar exporters) is a case in point. Others (Japan, Germany, Russia) do not produce enough to satisfy demand. A third reason is that most cigarettes sold today are blended cigarettes, i.e. they contain a mixture of different tobaccos. Few cigarette producing countries grow all of these tobaccos.

Most *cigarettes* are now consumed and produced in Asia. This is no surprise in view of that region's high share of world population. Within Asia, China alone produces 30 per cent of world total. The increasing share of Asia has taken place at the expense of

Europe and North America, which saw their share of the world total decline. The share of South America and Africa has remained stable since 1985 (table 7).

In China, domestic demand for cigarettes is largely satisfied by domestic production. Official figures indicate that the country trades very little. Exports and imports make up less than 2 per cent of national demand or production. India is in a similar situation (see also table 5).

In other countries, domestic demand is also mainly satisfied by domestic production but, in addition, they are sizeable exporters. The United States is a good example. It imports few cigarettes, but it exports one-third of its production (see also figure 1). It is the world's leading exporter, accounting for over 20 per cent of world exports. Exports became steadily more important for US producers in the 1980s when domestic demand started its long decline (see figure 1). In the late 1990s, however, US producers of cigarettes (and US farmers) came to face serious problems when cigarette exports weakened (following weak demand in East Asia and Russia and the relocation of some production to Europe) at a time when domestic demand was hit by the price hikes following the Master Settlement Agreement (see section 3.3).

**Table 7. World cigarette production volume by main region and main producing country  
(percentage; selected years)**

	1985	1990	1995	1998
<b>Asia</b>	43.5	49.8	50.4	50.9
(China)	(24.2)	(30.4)	(31)	(29.9)
<b>Europe</b>	29.8	25.6	24.7	24.9
(Including former USSR)				
<b>North America</b>	16.9	15.6	15.7	15.1
(United States)	(13.6)	(13.1)	(13.3)	(12.8)
<b>South America</b>	5.2	5	5.1	5.2
<b>Africa</b>	3.6	3.4	3.4	3.5
<b>Total</b>	100	100	100	100
Source: own calculations based on TJI.				

Certain countries export most of their production. In 1998, UK production was 160 billion pieces. It exported 125 billion pieces in that year. The Netherlands exported 103 billion pieces out of total production of 116 billion pieces.

A last category consists of countries that rely to a great extent on imports to satisfy domestic demand. Examples are Russia (in the 1990s), Japan (which also produces cigarettes domestically) and some countries in the Middle East (which do not have any production of their own).

International trade flows in cigarettes are explained by several factors. They can be the result of temporary supply mismatches: local producers may not produce the type or the quality of cigarettes that the market requires (more demand for the American blend, less for dark cigarettes). Or demand may be growing far away from where installed capacity is located (e.g. because a market hitherto closed to imports is opening up), with output only slowly reacting to the new situation. In Russia, the multinational tobacco companies installed much new capacity in the 1990s. Slowly, expanded domestic production came to replace imports. A worsened macroeconomic situation may lead to reduced volumes of demand for cigarettes, including demand for imported cigarettes. Sustained periods of prosperity may have the opposite effect. Official pressure may be another factor: pressure by the United States Trade Representative (USTR) is widely

seen as having contributed to the opening up of the Japanese, (Rep. of) Korean, and Taiwanese markets to imported cigarettes. Or it may simply be cheaper to produce in certain locations, either because local tobaccos are cheaper (an important factor given how many governments encourage manufacturers to use local tobaccos in their cigarettes), because local labour costs are lower, or because labour productivity is at a high level.

Increasingly, however, trade flows are explained by corporate strategies. Barriers to international and regional trade and investment flows have come down, and continue to come down nearly everywhere. This enables the large companies to concentrate production in fewer locations. In such circumstances, decisions by the large tobacco companies increasingly determine which market is being supplied from where. <sup>1</sup> It is to these company strategies that we now turn.

<sup>1</sup> Reemtsma, for example, internationalized its sales rapidly in the 1990s. From 35 per cent in 1991, international sales increased to 76 per cent of sales in 1999. Interestingly, in 1991 exports from Germany made up 64 per cent of those international sales. But by 1999, exports accounted for no more than 21 per cent of international sales, the balance being supplied from production at locations outside of Germany (Reemtsma AR, 1999).

### 3. The company response

The OECD-based tobacco companies have reacted to stagnating demand on their traditional markets in basically three ways: consolidation (the industry is increasingly dominated by a small number of relatively large players), diversification, and increasing productivity..

#### 3.1. Consolidation

Consolidation in the tobacco industry had been taking place for quite some time, but it accelerated in the late 1990s. Also, the size of the “deals” has become steadily bigger. Concentration can make a critical contribution to profitability through marketing (“global” brands), manufacturing and distribution. By producing high volumes at fewer locations, and by merging distribution activities, companies benefit from economies of scale. “The cigarette business needs volume to be profitable” <sup>1</sup>. Companies with large

sales in the quality brand segment (with high margins) are particularly attractive take-over targets as are those with a presence in fast-growing emerging markets.

Consolidation takes various forms. Smaller companies have been absorbed by their larger competitors. Austria Tabak took over the cigarette activities of Swedish Match, and was then taken over by Gallaher. Former state monopolies (such as Portugal's Tabacaria or those operating in Central and Eastern Europe and in Central Asia) have come under the control of the large multinationals. And, in an effort to broaden their market base, companies that previously were little active abroad have gone on a shopping spree outside of their national market (see also section 3.2). In the process, the degree of concentration of the industry has reached high levels, both at the national level (see table 8 for some examples) and worldwide. In 1999, three companies (CNTC at 30 per cent; Philip Morris at 17 per cent, and BAT at 16 per cent) controlled close to two-thirds of world cigarette production.

**Table 8. Concentration in the tobacco industry (market share of the dominant supplier; selected countries)**

Country	Percentage
Korea, Democratic Rep. of*	100
Iraq*	100
Algeria*	100
Madagascar*	100
Uganda	100
Zambia	100
Sri Lanka	99
Malawi	99
Mauritius	99
Sierra Leone	99

<sup>1</sup> According to Mr. Ulrich Herter, BAT's Managing Director in an interview with TJI (3/99, p. 56).

**Country Percentage**

Honduras	99
Nicaragua	98

Trinidad and Tobago	98
China*	97
Denmark	97
Korea, Republic of*	95
Ghana	92
Nigeria	92
Portugal	90
Thailand*	87
Kenya	87
Lithuania	85
Republic of South Africa	85
Egypt	85
Brazil	83
Venezuela	81
Czech Republic	81
* State-owned or state-controlled. Sources: TJI; Corrao, 2000.	

The tobacco industry is no stranger to high levels of concentration. In many countries the State monopoly was the exclusive producer and/or seller of tobacco products. In certain cases, this situation has barely changed (table 8). But in the worldwide privatization wave of the 1990s, many state tobacco companies were privatized either in whole or in part (the latter usually as a prelude to full privatization at a later date).

Many of these privatized companies were absorbed by multinationals or would-be multinationals. At first called in to supply farming advice, and manufacturing and marketing know-how, the multinationals would soon enter into joint ventures with or take an equity stake in the state-owned companies. They ended up taking over the whole company when it became clear that few local investors (including the State) had the resources available (or were willing to spend the ones that they had) for the much needed investments in new equipment to allow it to reach the levels of quality and productivity needed to compete in the more open trading environment (trade liberalization often accompanied privatization).

For the privatized companies, collaboration with the large tobacco companies was beneficial for a number of reasons. This collaboration helped them to modernize their production facilities; introduce modern distribution, management information and control systems; and provide training for their employees. The stronger financial position of the new parent company enabled them to invest in the replacement of assets, and in information technology. Lastly, the transfer of know-how helped them to reduce tobacco waste, achieve higher tobacco blend homogeneity, reduce cigarette weight variation and lower energy consumption.

At the national level, high levels of concentration make the dominant supplier a force to be reckoned with. Worldwide, concentration has placed considerable market share into the hands of a few players, enhancing their market power vis-à-vis their suppliers and subcontractors.

### ***Effects of consolidation on suppliers***<sup>2</sup>

Just like the cigarette manufacturers, their suppliers (the leaf dealers; the machinery and paper producers) must also cope with the consequences of slowing demand growth for tobacco products. But they have other problems too. Manufacturers need fewer machines as a result of a better use of capacity and the higher productivity levels achieved thanks to high-speed cigarette and packing machines. There is also more competition: China is developing its own machinery and cigarette paper industry.

In reaction, suppliers have felt obliged to rationalize production and raise productivity in an effort to maintain profitability. And they, too, have become involved in mergers and takeovers. Concentration has increased among leaf dealers<sup>3</sup> as well as in the cigarette paper<sup>4</sup> and machinery industry. Following similar moves by their customers, the suppliers to the tobacco processing industry also strive to become global players.

Such a development ties in neatly with the strategies of the tobacco multinationals. Similar to what is occurring in other industries,<sup>5</sup> the tobacco companies seek to do business with fewer suppliers but in the framework of long-term agreements. BAT has



set up regional supply chains to maximize efficiency gains and achieve synergy benefits. It is building alliances with strategic suppliers, with global agreements established for tow, board and film materials.

### 3.2. Diversification

In addition to taking over competitors, tobacco companies have tried to reduce their dependence on traditional, slow growing markets through diversification. This diversification has several dimensions: diversification (1) by market segment; (2) by target group; (3) by tobacco product; (4) by non-tobacco product; and (5) by geographical region. In part (and sometimes in large part) diversification has been achieved through mergers and acquisitions (see above, section 3.1)

*Diversification by market segment.* Cigarettes are sold in different categories, from the premium, highly-priced, high-margin category to the brandless (“generic”), low-margin type. The high margins of the premium cigarettes make them attractive to produce and sell. Companies with strong, well-established, international brand names have shown to be attractive take-over candidates. But by also offering cigarettes in the B- and C-category, companies reduce their vulnerability to demand slowdowns in times of crisis, when customers “trade down”, i.e. when they buy cheaper rather than more expensive cigarettes.

*Diversification by target group.*

Women and young people are prime target groups. The proportion of smokers among women is far lower than that among men. By successfully targeting women, a manufacturer can raise its overall market share. Many women see smoking as a symbol of women’s liberation. Manufacturers promote their cigarettes as a symbol of emancipation and independence. Some young women believe that smoking keeps them slim. Manufacturers produce (long, slim) cigarettes especially for their female customers. “Women are the tobacco industry’s prime target, especially in countries where they are experiencing improvements in their economic, social and educational status. Cigarettes are being promoted as both a “passport” to a better life and a symbol of emancipation, independence and success” (Corrao et al., 2000, p.32). In many

European countries, there is an overall trend towards girls smoking slightly more than boys (ibid.).

For obvious reasons, young people are the other promising category of (potential) smokers from the companies' point of view. Most people start smoking when they are young. Nonetheless, while targeting young people may make good commercial sense, it has become highly controversial in recent years. The smoking habits of young people have moved to the centre of the debate on smoking and health. Many of the actions aimed at discouraging demand for tobacco products (Chapter 4) target youth (no ads in youth magazines; no pictures of young people in ads; no TV ads early in the evening; retail access control and education programmes). The large tobacco multinationals have indicated that they are sensitive to the debate surrounding young smokers. In many countries tobacco companies no longer advertise their products to a young audience. It is uncertain, however, to what extent their more general adverts are picked up by young people.

*Diversification by tobacco product.*

Imperial Tobacco, for example, has targeted the roll-your-own (RYO) market for expansion. It dominates both the supply of tobacco and that of cigarette paper for this market. Through a string of acquisitions, Altadis became the world's leader in premium cigars.

*Diversification by non-tobacco product.*

Food products are a favourite for tobacco companies seeking to diversify. R.J. Reynolds bought Nabisco (which, in turn, was later acquired by Kraft). Philip Morris owns Kraft and Miller breweries. Japan Tobacco derives a (small) part of its sales from food. Logistics and wholesaling are another favourite. At Austria Tabak, wholesaling of tobacco and other products (and the operation of vending machines) make up a large share of turnover. Over 20 per cent of Altadis' earnings originate in its logistics division. Skandinavisk Tobakskompagni owns the largest wholesaler of consumer goods in

Denmark. BAT tried financial services (but, since 1998, is a pure tobacco company again).

Diversification into food and other activities makes the tobacco companies less dependent on (slow-growing) sales of tobacco products. But the profit margins in these industries are usually well below those attained in tobacco processing. Producing and marketing cigarettes remain the more profitable activities.

*Diversification by geographical market.*

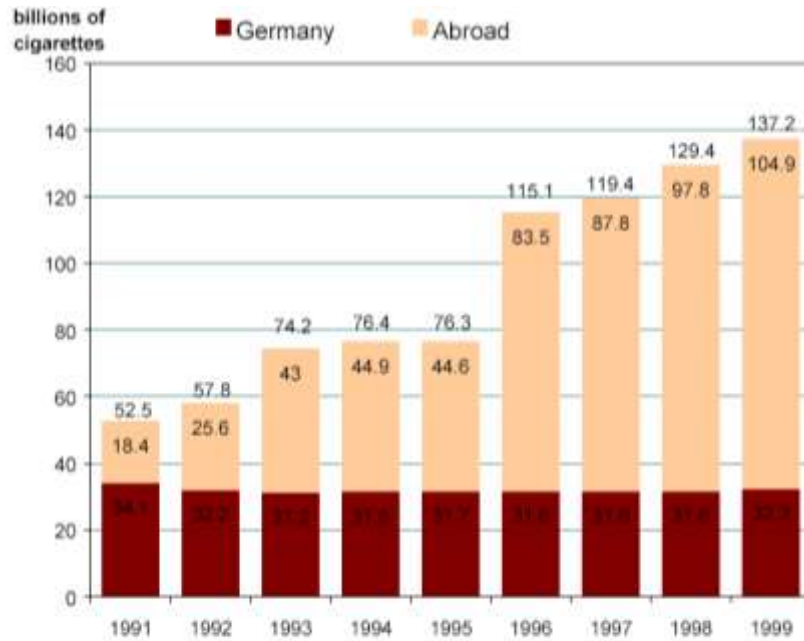
OECD-based tobacco companies are keen to reduce their dependence on their stagnant home markets and establish a presence in markets where growth is above average. After having “conquered” many markets in Latin America, Central and Eastern Europe, and the Central Asian republics in the 1990s, their focus is shifting to the Far East. All the major tobacco companies now have a presence in Poland, Russia and the Central Asian republics. Austria Tabak, which gained a presence in Estonia when it acquired the cigarette activities of Swedish Match, also has a 67 per cent market share in Guinea. The company was considering entering Asian markets when it was taken over by Gallaher in June 2001. Through this take-over and the acquisition in 2000 of Liggett-Ducat, the Moscow cigarette maker, Gallaher greatly reduced its dependence on the UK market. Similarly, Japan Tobacco became a world player when it acquired the international activities of R.J. Reynolds. Thanks to a relentless internationalization drive, Germany’s Reemtsma now sells less than one-third of its total in its home market (compared to over 60 per cent in 1991) (see also figure 6). It is now active in several Central and Eastern European countries and, in 1999, it acquired Cambodia’s Paradise Tobacco Company. BAT is building a cigarette company in Viet Nam and in the Republic of Korea.

<sup>2</sup>Sources TJI and BAT AR, 1999.

<sup>3</sup>For instance, Dimon, the world’s second largest leaf dealer (and itself the result of the 1995 merger of Dibrell Brothers and Monk-Austin Inc.) acquired Intabex in 1997.

<sup>4</sup>Production of cigarette paper has accumulated around three groups which together supply more than half the world market outside China (TJI, 3/99).

<sup>5</sup>See van Liemt, 1998.



**Figure 6. Reemtsma: Cigarette sales worldwide (1991-99)**

Source: Reemtsma/AR/99.

### 3.3. Litigation

The rationalization that follows consolidation, the various forms of diversification, and their strengthened hand vis-à-vis their suppliers should all help the remaining companies to maintain their profitability and, where possible, increase it. There is, however, one dark cloud on the horizon: litigation. Litigation means that the industry cannot do without the assistance of a sizeable number of legal experts. This is a cost factor. But in view of the sometimes enormous damages claimed by plaintiffs this would appear to be money well spent.

### **Box 3. Litigation: State of play**

“... Our tobacco business will continue to be a lightning rod for criticism and controversy, and will face significant legal, legislative and regulatory challenges, for many years to come.”<sup>1</sup>

Around the world, the tobacco industry is involved in hundreds of lawsuits. Most of these take place in US courts (but the number of lawsuits outside of the US is on the increase). Most of the defendants are the large US companies. The (compensation and punitive) damages sought involve many billions of US dollars. The vast majority of these cases have been dismissed. Some have been settled out of court. In very few cases the verdict has gone against the tobacco companies (these are being appealed). But when this does happen, it can be very costly. In the (collective) Engle case<sup>2</sup> in Florida, the verdict won amounted to over 144,000 million US dollars.

Plaintiffs can be any of three groups: (1) individuals or groups of individuals suffering from smoking-related illnesses; (2) relatives of people who have died from such illnesses; and (3) provincial and state governments and health care insurance companies attempting to recover the costs of the treatment of smoking-related illnesses.

The history of tobacco litigation has been summarized in three waves. The first (in the 1950s) and the second wave (that started in the 1980s) consisted of individual personal injury suits. The third wave of tobacco litigation that began in 1994 was different in that litigation was no longer limited to individual claims by individual smokers. For the first time, States and other third-party payers of medical costs sued the tobacco industry (Ciresi et al., 1999).

Most of the cases are brought in US courts and involve US citizens or entities on the one hand, and the US tobacco companies on the other. But the practice is spreading to other countries where local and internationally operating companies are being taken to court.<sup>3</sup> On the whole, courts outside of the US have been reluctant to hear this kind of case. “Class action” suits are not common in legal systems outside the US. Also, the damages that have been awarded are typically below US levels. In turn, this has tempted non-US parties to sue US tobacco companies in US courts.<sup>4</sup>

<sup>1</sup> Mr. Geoffrey Bible, Chairman and CEO of Philip Morris in his letter to shareholders in Philip Morris/AR/1998, p. 4.

<sup>2</sup> This was the first, collective, “class-action” lawsuit to go to trial in the US. The “class” consists of all Florida residents and citizens, and their survivors, who claim to have suffered, presently suffer, or have died from diseases and medical conditions caused by their addiction to cigarettes that contain nicotine (Philip Morris/AR/1998). In “collective” lawsuits, one plaintiff can institute proceedings on behalf of a group of people who have all suffered the same injury, without their having to prove their injuries individually. The bigger the group, the higher the claim (Reemstma/AR/ 1999).

<sup>3</sup> Philip Morris alone is involved in hundreds of smoking-related lawsuits. For an overview of the different types of suits, the arguments of the plaintiffs and the defence, as well as progress in the courts, see Philip Morris' Annual Reports/Notes to Consolidated Financial Settlements/Contingencies/Overviews of Tobacco-related Litigation.

<sup>4</sup> Whether the United States product liability system will spread to Europe or not is a question highly relevant to the tobacco industry. Bergkamp and Hunter (1996) think that the answer to this question is no. They give several reasons. For instance, in the United States, compensatory damages awarded can be many times higher than in Europe. Punitive damages are rarely awarded in Europe. This makes it much less attractive for European lawyers than for US lawyers to start a lawsuit (US lawyers typically receive some 30 per cent of the sum awarded). Also, the litigation threshold in product liability cases is much lower in the US, where winning defendants are not permitted to recoup their costs from the plaintiff, than in Europe, where they are.

The costs of the many lawsuits and the risk that sizeable damages may need to be paid have a depressing effect on the prices of Tobacco Company shares quoted in the stock market. Tobacco companies have comparatively low price/earnings (p/e) ratios. As long as companies operating or selling in the US market are more likely to be involved in lawsuits and more vulnerable to the high damages claimed by plaintiffs, they would appear to be at a competitive disadvantage vis-à-vis their competitors operating only in the rest of the world. This disadvantage may, however, be smaller than would appear at first sight. Through drastic price increases, the US tobacco companies were able to pass on to their customers the cost involved in the Master Settlement (box 4).

The large number of lawsuits is bad news for the tobacco companies. They are costly, require management attention and they depress the share price. They also give the industry a poor image, a serious matter for companies which rely so much on the "feel good" factor in the marketing of their products. The tobacco companies want to be seen as good corporate citizens. <sup>6</sup> Where appropriate they are keen to settle. There have been litigation settlements in the past. But nothing compares with the 1998 Master Settlement Agreement (MSA).

#### **Box 4. The US Master Settlement Agreement (MSA)**

In November 1998, the US cigarette manufacturers agreed to reimburse US states for smoking-related health costs, thereby ending the uncertainty of continuing lawsuits. They agreed to pay the remaining 46 states, the District of Columbia, and various territories<sup>1</sup> US\$206,000 million over 25 years to compensate them for the costs of treating smoking-related illnesses and to fund anti-smoking programmes. They agreed to pay, over a five-year period, a sum of US\$1,450 million earmarked for anti-smoking campaigns and US\$250 million over 10 years for setting up a national public health foundation, which will work towards deterring minors and youths from smoking. Manufacturers also agreed to limitations on advertising and to limits on sporting event sponsorship. As part of the MSA, they are committed to work cooperatively with the tobacco growers' community to address concerns about the potential impact of the MSA on that community. To that end, in January 1999, they agreed to participate in the establishment of a US\$5,150 million trust fund to be administered by the tobacco growing states.

<sup>1</sup>The manufacturers had previously settled similar claims brought by Mississippi, Florida, Texas and Minnesota. The US Federal Government is not a party to the Master Settlement. In September 1999, the Federal Government filed a lawsuit of its own against various cigarette manufacturers in an effort "to recover an unspecified amount of health costs for tobacco-related illnesses allegedly caused by defendants' fraudulent and tortious conduct and paid for by the government under various federal health care programs" (Philip Morris/AR/1999).

Source: Various.

<sup>6</sup> The industry has offered to lend support to the (UN) World Health Organization (WHO) in its fight to eradicate malaria and in AIDS prevention, and to finance (UN) International Labour Organization (ILO) projects to combat child labour.

## 4. Governments and tobacco

Governments face a dilemma. On the one hand, tobacco-growing and processing can make a considerable contribution to employment (the subject of the next chapter), tax revenue and foreign exchange receipts. In many developing and formerly centrally-planned economies, the tobacco companies have made sizeable and most welcome investments when other investors were reluctant to do so. On the other hand, governments have the obligation to protect the population's health. Smoking can be harmful to health. Treating people for smoking-related illnesses is expensive. This can lead to heated debates within the same government as each sector defends the interests it believes it should represent. How do governments cope with this dilemma?

#### 4.1. Tax income, foreign exchange earnings and direct foreign investment

The economic importance of tobacco-growing and processing differs from country to country. At the national level, cigarette (sales and import) tax can be a main source of government revenue. In Russia, cigarette tax revenue contributes around 8 per cent to the financing of the state budget (TJI 6/99).

When the government owns the industry, it receives profits in addition to tax. That is why, in so many countries, State monopolies continue to control cigarette trade and production (see also table 8). In China, profits from state-owned CNTC amounted to the equivalent of US\$11,000 million in 1999. CNTC has been the Chinese State's top revenue generator for years. Japan Tobacco earned more than US\$400 million for the Japanese State in the fiscal year ending March 2000 (BW, 28 May 2001). The monopolies can also play a social function. In Italy, several of the state monopoly's factories are placed in areas hit by high unemployment (TJI 3/98).

Then there are balance of payments issues to consider: many low-income countries rely on the export of cash crops such as tobacco to pay for the service of their foreign debt. Tobacco exports made up close to 10 per cent of Cuba's exports in 1997-98. In the case of Tanzania it was 15 per cent, In Zimbabwe over 25 per cent and in Malawi tobacco exports made up two-thirds of commodity exports (UNCTAD, 2000).

People smoke. But whether they smoke domestically produced cigarettes using home-grown tobacco or use imported cigarettes and tobaccos can make a world of difference when foreign exchange is scarce. That explains why so many countries try to limit the importation of cigarettes and encourage domestic producers to use local tobaccos, for instance, by providing a favourable tax treatment to companies that use a minimum percentage of home-grown tobaccos.

The cigarette companies have also been a prime source of investment in the formerly centrally-planned countries of Central and Eastern Europe, and Central Asia. When others were reluctant to invest, those companies saw the possibilities offered by a combination of pent-up consumer demand, outdated production facilities and the association with "freedom" and "western style" living that so appealed to the people in these countries after many years of central planning and little consumer choice. After having lobbied successfully for the "opening up" of Asian markets such as Japan and



the Republic of Korea, the large tobacco companies are eagerly waiting for the opening up of the other economies (notably China) that continue to restrict imports from and/or investments by foreign tobacco companies.

Tobacco growing, processing and exports can thus make a significant contribution to national employment and national income. Yet, however important tobacco growing and processing may be at the national level, its full economic and social significance is best grasped at the local or regional level. In some regions, tobacco is grown side by side with the crop which is the main source of income; its contribution to overall income is modest. But in many others, tobacco is a main source of income and employment (see also section 5.3).

#### 4.2. Public health

Tobacco growing and tobacco processing may bring considerable economic and social benefits, but the treatment of smoking-related illnesses is costly. Cigarette smoking causes cancer. It is addictive. The WHO estimates that tobacco products cause around 3 million deaths per year. Cigarette smoking is the major cause of preventable mortality in developed countries. In the mid-1990s, about 25 per cent of all male deaths in developed countries were due to smoking. Among men aged 35-69 years, more than one-third of all deaths were caused by smoking. The costs of treating all these people are clearly enormous (WHO, 1997).

So far, smoking has not had the same impact on mortality among women and among people from developing countries. There is an approximate 30-40 year time lag between the onset of persistent smoking and deaths from smoking. The effects of the greater incidence of smoking among these two groups will thus be felt with a lag, but it seems reasonable to believe that its impact on them will not differ fundamentally from that on developed country males.

It may be argued that smokers willingly take a certain health risk when enjoying their smoke. They like the taste and all the other things that they associate with smoking. But this does not apply to environmental tobacco smoke (ETS) or “second-hand smoke”. Smoke gets in your eyes. In your clothes. And in your lungs. Non-smokers cannot escape from smoke in badly ventilated areas. To be exposed to other people’s tobacco smoke can be a nuisance in addition to being a health risk for non-smokers.

### 4.3. The way out of the dilemma

Governments are thus faced with conflicting pressures. How do they cope? In practice, governments have opted for several strategies (which are often followed simultaneously). A recent strategy consists of seeking compensation for the costs of treating smoking-related illnesses. It has been followed with success in the United States, as we saw in section 3.4. Governments also set rules regarding the maximum content of hazardous substances in cigarettes. Most of all, however, governments try to discourage demand for what is, as the industry does not tire of telling us, essentially a legal product. This is done in a variety of ways, with some governments applying particular vigour and others taking a more relaxed approach. On the whole, however, the trend is clear: governments' rules on smoking are becoming ever more restrictive. The use of tobacco products is being discouraged in several ways.

*Limitation of the space where smoking is allowed.* This is done above all to protect non-smokers from involuntary exposure to tobacco smoke. Smoking is being prohibited in public places (particularly health care and educational facilities) and in mass transport. Legislation requires restaurants to reserve space for non-smokers.

*Limitation by age group.* It is prohibited to sell tobacco products to people under a certain age.

*Limitations on points of sale.* The use of vending machines is being restricted because these cannot discriminate against sales to young people.

*Health warnings* stating that tobacco is harmful to health have become obligatory. The warnings must be placed on packets and in ads, with the authorities prescribing the text and the minimum space allotted to the warning in the ad or on the packet.

*Education.* Governments sponsor education and public information programmes on smoking and health. <sup>1</sup>

*Advertising bans.* Restrictions concern the location of ads, the media used (no billboards, no ads in the printed media or in cinemas), the images presented (no young people, no cigarette packets), and the time when broadcasting is allowed (not during hours when children watch television).

The manufacturers are unhappy with these restrictions, and in particular with the ban on advertising. In their view, it is not proven that such a ban discourages demand for cigarettes (as its proponents claim). They are concerned about its effect on the value of their prime asset, the brand name (box 5).

**Box 5. The ban on advertising and the value of the brand name**

The authorities of many countries restrict advertising to discourage demand for cigarettes. If anything, they expect it to discourage young people from starting to smoke. In Italy, direct and indirect tobacco advertising have been banned for a long time. In France, the 1991 “Loi Evin” forbids all forms of tobacco advertising. The EU intends to ban virtually all tobacco advertising by 2006.

Tobacco companies contest such bans. To them, advertising is a key means for maintaining loyalty to the brand and for persuading existing smokers to switch brands. Advertising does not increase overall consumption or cause anybody to start smoking.

Advertising is the key to the image of glamour, sophistication, freedom, and healthy, outdoor living that the tobacco companies want their product to be associated with. It supports existing brands and is an essential tool for establishing new brands. The success of a tobacco company is driven by the power of its brand portfolio.<sup>1</sup> As in other consumer goods industries, brands are often the most valuable asset that companies have. BAT describes itself as “one of the world’s largest trade mark owners”. Philip Morris attributes its success to the power of its “global brand portfolio”.<sup>1</sup> The value of Marlboro, Philip Morris’ most valuable and the world’s leading cigarette brand, has been put at US\$21,000 million.

Advertising bans may have a negative effect on the value of existing brands, but their impact on potential new entrants (brands, companies) is even greater. It takes millions of US dollars to introduce a new tobacco product. Who wants to do so when you can’t even advertise its name?

In practice, the tobacco companies have proven to be quite resourceful in compensating for the effects of the advertising bans (even though it is becoming steadily more difficult to do so). Their strategies range from quickly introducing new cigarette brands before a ban comes into effect; to “brand stretching” or “trademark diversification”;<sup>2</sup> and “borrowing” an existing brand name that was not previously associated with cigarettes.<sup>3</sup> The sponsorship of sports and cultural events, particularly international sports events, has become popular. Formula One motor racing, which is followed by millions of people on television around the globe, is a very attractive tool for the marketing of existing and would-be worldwide brands.

<sup>1</sup> See the 1999 BAT and Philip Morris Annual Reports.

<sup>2</sup> Such as “Marlboro” country or “Camel Adventures”.

<sup>3</sup> Reemtsma sells BOSS and DAVIDOFF cigarettes (Reemtsma, 1999, AR) and Altadis “Omar Sharif” and “Alain Delon” cigarettes (Altadis, AR 2000).

Source: Various.

#### 4.4. Taxation

Raising the tax on tobacco products is a component of virtually every government's tobacco policy. On the surface, it is an attractive component because it raises the price of tobacco products (and thus discourages demand) *and* it raises government revenue (and keeps the treasurer happy). In actual practice, the situation can be more complicated. First, a flat tax per packet would act as a regressive tax as it weighs more heavily on people with

<sup>1</sup> In Thailand, the no-smoking campaign involves singers, actors and actresses as models for young people (TJI, 6/96). a low income. This effect is exacerbated by the fact that, in developed countries, this group of people uses tobacco more intensively than people with high incomes. Second, overall demand for cigarettes may decline so steeply that increased revenue through the higher tax per packet is outweighed by the lower sales volume.

However, the main constraining factor is that, as a result of the tax increases, prices become so high compared to those of surrounding countries that legally sold cigarettes are being substituted for smuggled ones. <sup>2</sup> In the mid-1990s, contraband goods made up 80 per cent of the Estonian market (TJI 5/99). In 1993, they made up 60 per cent of the Quebec market – a year later the Canadian Government was forced to cut back taxation. Worldwide, smuggled cigarettes were estimated to account for 5 per cent of global cigarette production and 30 per cent of international cigarette trade in 1994 (WHO, 1997) (see also box 6).

##### **Box 6. Smuggling**

“About 20 per cent of cigarettes and 80 per cent of hand-rolling tobacco now consumed in the UK is smuggled product... Within the past 4-5 years this trade has developed from “white van” cross-Channel black marketeering by small opportunists... It now involves organized criminal gangs who are finding it easier and more profitable than drug smuggling and are sourcing vast supplies in containers ...”. <sup>1</sup>

Smuggling, the illegal import of cigarettes, is a major headache for the governments of many countries. Smuggled cigarettes make up or have made up over a quarter of the local market in such diverse countries as Estonia, Latvia, the Philippines, Ukraine, and the UK.

Loss of tax revenue in the country of final destination is but one effect of the high incidence of smuggling. It also undermines government efforts to discourage the consumption of cigarettes through higher prices. It leads to the corruption of public officials and agencies, and paves the way for other,

more serious forms of smuggling (drugs, people). It is said to lead to criminal behaviour <sup>2</sup> and to help foment criminal and terrorist activities.

Governments naturally try to combat smuggling but the higher the price difference with the neighbours the more attractive the country becomes as a destination for smugglers. Smuggling cigarettes can be a hugely profitable business. <sup>3</sup> Governments must thus commit resources to additional surveillance of their borders, resources that many do not have. Making the use of tax banderoles obligatory can be another solution (but these are known to have been forged by the smugglers). In Brazil, where the treasury suffers from lost revenue due to the fact that many cigarettes exported to Paraguay are smuggled back into the country, the government introduced a 150 per cent *export tax* on cigarettes in 1999.

The position of the tobacco companies is ambivalent. The companies benefit from the sales of smuggled products originating in their factories just as they do from any other sales. Smuggling also helps establish their brand name in the country of destination, which can be very useful when the brand is not (yet) legally available there. But the position of those companies which sell through “normal” channels is different. They lose market share. As such, they become the government’s allies: both have an interest in combating illegal imports.

Whether smuggling takes place with the knowledge or the collaboration of the tobacco companies is a moot point. The companies claim that they neither control nor have any influence over smuggled products. However, certain governments have indicated that they are not convinced of their innocence.

<sup>4</sup>

<sup>1</sup> CGE, March 2000, p. 161.

<sup>2</sup> In Italy, the armoured-vehicle convoys of smugglers “show no hesitation in running police off the road” (CGE, Italy, February 2000, p. 135).

<sup>3</sup> Earnings are estimated to be in the range of US\$600,000 per truckload destined for the British Isles.

<sup>4</sup> The Canadian Government successfully sued one of the US tobacco companies, which it accused of aiding smugglers who redirected exported Canadian cigarettes back into Canada (TJI/1/99, p. 7; also TJI 1/00, p. 4). Following a two-year investigation by its anti-fraud unit, the European Union announced that it would sue US tobacco companies in an attempt to recover customs revenues lost through cigarette smuggling (TJI/5/00, p. 4).

<sup>2</sup> An extreme case is the situation in Latvia in 1995 when the excise tax was raised to a level 15 times that of Lithuania, its immediate neighbour (TJI 6/99).

## 5. Employment in the tobacco industry

Worldwide, the tobacco-processing industry employs hundreds of thousands of people. However, due to a combination of slow demand growth, consolidation, and higher productivity, this number is unlikely to increase by much in the near future. Fewer people are needed per unit of production. The industry is becoming less intensive in the use of labour. Tobacco *growing*, in contrast, gives work to millions of people. It continues to be a highly labour-intensive activity. The scope for productivity increases in tobacco growing would appear to be more limited than those in tobacco processing.

### 5.1. Employment: the figures

Over a million people are employed in the world tobacco industry (ISIC 314 or 16). But of this number a high percentage is employed in just three countries: China, India and Indonesia (table 9). The large number employed in China comes as no surprise in view of the large number of cigarettes (one-third of the world total) produced there. Still, the productivity gap with the United States is striking. China produces roughly three times as many cigarettes as the US, but it needs over nine times as many people to produce them. In the other two countries the scope for productivity improvements would appear to be even higher.

### 5.2. Employment trends

Table 10 gives employment data for selected OECD countries. Following considerable job losses in the 1980s, <sup>1</sup> these data show that, in the 1990s, employment in the tobacco industry declined in all cases (except for Poland which registered a small increase). In Australia, Germany, Hungary, the Republic of Korea and Turkey, employment declined by one-third or more in the seven-year period 1990-97. In most countries, the number of establishments in the industry also declined, in some cases quite substantially (Turkey, Denmark, Germany, Hungary, the Republic of Korea and the United Kingdom). The data given are for the tobacco industry as a whole, encompassing also other tobacco products than cigarettes (although the latter is usually its main component). Comparisons with cigarette production volumes are therefore not all that meaningful because they do not take account of changes in the volume of production in these other tobacco products. Nonetheless, it is noteworthy that in many cases cigarette

production decreased far less than employment in the tobacco industry. In some cases, employment went down when production increased.

<sup>1</sup>In the US and the UK alone, close to 40,000 jobs were lost in that decade, according to the OECD.

**Table 9. Employment in the tobacco industry (1990s\*)**

Albania	967 (c)		France	4 500 (0)		Nigeria	1 500 (u)
Algeria	–		Gabon	50 (c)		Norway	596 (c)
Argentina	2 700 (I)		Germany	12 000 (I)		Pakistan	40 000 (I)
Armenia	1 125 (c)		Ghana	1 121 (c)		Panama	180 (I)
Australia	1 600 (o)		Greece	2 800 (o)		Papua New Guinea	2 598 (c)
Austria	1 200 (o)		Grenada	17 (c)		Paraguay	–
Azerbaijan	1 497 (c)		Guatemala	500 (u)		Peru	400 (I)
Bangladesh	27 155 (c)		Haiti	–		Philippines	12 800 (I)
Belarus	–		Honduras	3 409 (c)		Poland	12 400 (o)
Belgium	3 000 (I)		Hungary	2 100 (o)		Portugal	1 200 (o)
Bolivia	205 (c)		India	415 000 (I)**		Romania	5 200 (I)
Bosnia Herzegovina	676 (c)		Indonesia	224 000 (u)***		Russian Federation	12 900 (c)
Brazil	18 000 (I)		Iran Islamic Rep.	10 500 (c)		Senegal	–
Bulgaria	13 100 (c)		Ireland	1 000 (o)		Serbia Montenegro	–
Burkina Faso	–		Israel	600 (c)		Sierra Leone	–
Burundi	181 (c)		Italy	14 100 (o)		Singapore	770 (c)
Cambodia	1 952 (c)		Jamaica	803 (c)		Slovak Republic	1 000 (I)
Cameroon	567 (c)		Japan	7 100 (o)		Slovenia	1 000 (I)
Canada	4 000 (o)		Jordan	1 000 (I)		South Africa	3 000 (c)
Cape Verde	40 (c)		Kazakhstan	–		Spain	9 300 (o)
Central African Republic	465 (c)		Kenya	916 (c)		Sri Lanka	3 500 (I)
Chad	–		Korea Rep.	4 300 (o)		Suriname	88 (c)
Chile	500 (u)		Kyrgyz Republic	1 110 (u)		Sweden	800 (o)
China	280 000 (I)		Lao PDR	–		Switzerland	–



Hong Kong, China	630 (I)		Latvia	358 (c)		Tajikistan	–
Colombia	1 100 (I)		Lebanon	–		Tanzania	5 000 (c)
Congo, Dem. Rep.	–		Lithuania	–		Thailand	31 708 (c)
Congo, Rep.	–		Macedonia FYR	6 000 (I)		Trinidad and Tobago	166 (c)
Costa Rica	600 (u)		Madagascar	–		Tunisia	2 669 (c)
Côte d'Ivoire	–		Malawi	6 000 (c)		Turkey	22 600 (o)
Croatia	2 680 (c)		Malaysia	5 200 (I)		Turkmenistan	–
Cuba	–	Mali	–		Uganda	–	
Cyprus	280 (I)		Mauritius	189 (c)		Ukraine	3 000 (c)
Czech Republic	1 000 (I)		Mexico	4 700 (o)		United Kingdom	8 000 (o)
Denmark	1 400 (I)		Moldova	2 293 (c)		United States	31 000 (o)
Dominican Republic	–		Morocco	2 500 (I)		Uruguay	468 (c)
Ecuador	380 (u)		Mozambique	389 (c)		Uzbekistan	–
Egypt, Arab Rep.	18 300 (u)		Myanmar	2 000 (u)		Venezuela RB	2 861 (c)
El Salvador	250 (c)		Nepal	4 660 (c)		Viet Nam	–
Estonia	–		Netherlands	5 400 (o)		Yemen	961 (c)
Ethiopia	950 (u)		New Zealand	500 (o)		Zambia	961 (c)
Finland	700 (o)		Nicaragua	–		Zimbabwe	5 600 (I)

Note: \* Figures are for the 1990s (i.e. 1990 or the most recent year in that decade). \*\* Only factory workers. \*\*\* Including *kretek* cigarettes.  
(–) Not available.  
Sources: OECD (o); ILO (I); UNIDO (u); TJI (I); Corrao (c).

**Table 10. Employment in the tobacco industry of selected OECD countries (1990 to latest; x 1,000 people)**

	Employment		Establishments		Annual cigarette production x 1,000 million
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	1990	1997	1990	1997	1990	1997
Australia	2.9 <sup>4</sup>	1.6 <sup>8</sup>	–	–	32.7	30.7
Austria	1.4	1.2	15	13	15	20
Denmark	1.55	1.4	17	12	11.4	12.3
France	5.2	4.5 <sup>7</sup>	–	–	55.5	46.9
Germany	19.3 <sup>1</sup>	13	57	33	221.1	182
Hungary	3.4	2.1	13	8	28.2	27.1
Ireland	1.31	1.0 <sup>7</sup>	6	6	6	7.97.9
Netherlands	5.9 <sup>3</sup>	5.4	15	11	81	116
New Zealand	0.62	0.5 <sup>8</sup>	4	7	7	6.36.3
Poland	11.0 <sup>3</sup>	12.4 <sup>7</sup>	–	–	86.6	95.2
Rep. of Korea	7.2	4.3	20	14	92	92.7
Spain	10.6 <sup>5</sup>	9.3	36	37	77.5	74.6
Sweden	1.1	0.86	9	8	9.8	7.2
Turkey	32.1	22.6	50	37	60.5	112
United Kingdom	9 <sup>5</sup>	8	43	25	126.5	170.2
United States	41	31.0	–	–	709.7	719

<sup>1</sup> 1991; <sup>2</sup> 1991-1992; <sup>3</sup> 1992; <sup>4</sup> 1992-93; <sup>5</sup> 1993 <sup>6</sup> 1995; <sup>7</sup> 1996; <sup>8</sup> 1996-1997.

Note: Only those countries were selected for which data for at least five consecutive years were available.

(–): not available.

Source: OECD, 1999; TJI/USDA

This downward trend in employment barely changed after 1997, the latest year for which OECD data are available. Demand in the OECD area has not grown (Chapter 2). If anything, consolidation of the industry appears to be accelerating (Chapter 3). More jobs have gone or are under threat. Consolidation intends to enhance the competitiveness of the merged companies and usually involves plant closures and redundancies. Production (but also research and development) is being concentrated in fewer sites. Overlap in distribution can lead to considerable job cuts. In December 2000, Altadis, the company formed out of SEITA of France and Tabacalera of Spain announced the closure of 8 of its 14 Spanish factories (and the construction of two new plants). Out of a total of 7,000, 2,000 jobs would be lost. On the French side, SEITA announced that 1,400 jobs, or one-third of its workforce, would be shed (FT, 21/12/00). In 1999, following its acquisition of Rothmans, BAT closed or announced the closure of factories in Singapore, Spain, Suriname, Papua New Guinea, Nicaragua,

Switzerland, Australia, Malaysia, South Africa and the UK (BAT AR, 1999). BAT plans to concentrate on fewer and bigger factories with greater manufacturing capacities.

Directly and indirectly, the combination of privatization and trade liberalization appears to accelerate this downward employment trend. In many countries, the tobacco companies are or were state-owned or state-controlled. Often they were monopolies (Chapter 4) with below average productivity due to high staffing levels, outdated equipment and/or idle capacity. When these companies are being privatized and prepared for operating in a more competitive environment, their employment levels tend to suffer. The Italian state monopoly ETI, which had already cut the number of its manufacturing plants from 21 to 17 in the mid 1990s, plans to reduce the number of production sites to 4 by 2003 and to lay off 3,300 employees to a planned level of 1700 by the end of 2003. These measures are designed to restore both the competitiveness and the financial performance of ETI prior to its privatization (IJI/2/00).

Jobs in OECD area plants look particularly vulnerable because demand is stagnating or declining. Exports, which make up a significant share of production in certain countries, suffer when previous export markets expand their own production (the case of US exports to Russia, for example). On the other hand, several of the OECD plants already produce at high levels of productivity.

But the effects of consolidation and productivity increases are not limited to the mature OECD markets. Privatization, together with trade and capital liberalization, are leading to a search for productivity increases everywhere, with potential negative effects for employment (although the cost advantages of productivity increases are smaller in low labour cost countries). In China, the number of production plants declined from 180 to 136 during the 1990s and their number is expected to drop to around 100 in the first decade of the 21st century (see box 2 on the China factor).

### **5.2.1. Productivity**

The cigarette industry has experienced spectacular productivity increases in the past century. The production capacity of the most modern cigarette machines increased from 250 cigarettes per minute (cpm) to 16,000 cpm in less than a century (box 7). But

such high-speed machines alone cannot ensure high productivity increases. Or, as Mr. Ulrich Herter, BAT's managing director put it: "... high speed is not an end in itself. It is important to get the right logistics around the machine..." (TJI 4/95 p.26). The layout of the plant needs to be adjusted to ensure that such high volumes are actually achieved. Production is being concentrated in fewer plants. Reemtsma's Berlin plant produced annually 3.65 billion cigarettes when it was inaugurated in 1959. Today, it produces ten times that volume (with a little over three times the number of employees) (Reemtsma AR 1999). Philip Morris' modern facility at Bergen op Zoom in the Netherlands produces 90 billion cigarettes annually with just 1,900 people. If such high levels of productivity were to become the norm, there would appear to be considerable further scope for downward adjustment of employment in the world tobacco processing industry.

**Box 7. Productivity in the tobacco processing industry**

Until the 1870s, all cigarettes were rolled by hand. Particularly dexterous (women) workers could roll four cigarettes per minute. The first cigarette machine, introduced in 1867, could produce 60 cigarettes a minute. It caused a sensation and had two effects. First, fewer people were needed to make the same number of cigarettes. Second, it enabled cigarettes to be produced on a large scale, thus paving the way for them to be marketed on a massive scale. In subsequent years these two effects (high productivity and mass marketing) continued to reinforce each other.

The capacity of cigarette machines did not stop increasing: 250 cigarettes per minute (cpm) in 1910; 1,000 cpm in 1921; 1,300 cpm by 1930; 1,500 cpm by 1955; 1,750 cpm by 1965. Then capacity started to accelerate with a handful of competitors producing ever faster machines. Production of cigarettes per minute increased to 4,000 by 1968; 5,000 in 1976; 7,200 in 1982; and 10,000 cpm in 1988. Still, there proved room for greater speed and by 1999 the fastest machines could produce 16,000 cigarettes per minute.

Clearly, few producers reach such high levels. But those that do have a competitive advantage. In an open market, producers who can afford them and can master the logistical problems involved in operating them efficiently will want to purchase the new machines to bridge the gap with their more efficient competitors. This can be expected to lead to further concentration and to production in fewer plants (it only makes economic sense to use high speed machines when production volumes are high). And it may well lead to greater concentration by company. Large companies are more likely to have the need to produce high volumes, the know-how to organize production efficiently, and the financial resources to invest in these machines (Source: based on TJI).

### 5.3. Some remarks on employment in tobacco growing

Tobacco is grown in over a hundred countries. It is a labour-intensive crop that provides work and income to millions of people. Over 80 per cent of world tobacco is produced in developing countries and regions (Chapter 2). The share of these countries in world production and exports is growing, but it is a slow process. There are limits to the possibilities of changing one tobacco for another in existing blends (see section 1.1.1).

Also, many governments consider tobacco growing a strategic activity. Governments support tobacco growing in various ways. Some subsidize production. Others oblige cigarette manufacturers to use a certain percentage of home-grown tobacco (or provide manufacturers with financial incentives to do so). Yet others oblige the state monopoly to buy up all (or all unsold) domestically grown tobacco (sometimes at high prices). In short, in many cases either the tax payer or the smokers are asked to subsidize domestic tobacco production.

As is the case with other types of agricultural activity, these governments support tobacco growing for economic (contribution to government revenue), social (it provides employment to many people), strategic (they don't want to depend on imports in times of war or crisis) and political (tobacco farmers may have a decisive vote in a decentralized political system) reasons. Not infrequently, a combination of these factors is at work.

The opportunities for productivity enhancement in tobacco growing would appear to be more limited than those in the tobacco industry. Tobacco growing will thus continue to occupy many people. But how their number will develop in the future is hard to say with precision. Stagnant demand for tobacco makes it likely that, worldwide, the number will go down. Just where this will occur depends on the circumstances of each country and region. People involved in the production of high quality tobaccos at competitive cost of the type for which demand prospects are good would appear to be in a more favourable position than others. But whatever changes do take place, they are bound to occur slowly.

Nonetheless, the authorities in many places are concerned about the effects that a drastic slow-down in demand for tobacco might entail. Often the question is raised whether tobacco can be replaced by

an alternative crop that matches its earnings per hectare or per person. Such questions must consider technical aspects (for instance, the sloping, rocky soils that are used for growing oriental tobaccos may be unsuitable for other crops); skill problems (farmers may have no experience in the growing of alternative crops) and “sunk costs” (farmers may have invested heavily in installations that are specific for tobacco). How easy or difficult is it to find alternative jobs for the people involved in tobacco growing? How are tobacco prices expected to develop compared to those of alternative crops? All these questions can only really be answered case by case, region by region, and country by country. Only detailed case-studies can be the basis of a meaningful discussion.

## 6. Conclusion

Demand for cigarettes and other tobacco products is influenced by two conflicting trends. On the one hand, the smoking prevalence of women is much lower than that of men; and that of developing country adults lower than people in industrialized countries. Even small increases in the percentage of women who smoke, and small increases in the proportion of smokers in developing countries would significantly raise world demand. On the other hand, more and more governments try to discourage demand for tobacco products. How these different pressures will affect the volume of demand in the near future is hard to predict. The current uncertain macroeconomic outlook is a further complicating factor. A return to the pre-1990 growth rates looks unlikely though.

In this uncertain situation, two scenarios are possible for the tobacco companies. In the best scenario, privatization and trade and investment liberalization continue as they did in the 1990s. The companies are allowed to enter hitherto closed markets where their superior manufacturing, distribution and marketing skills and deep pockets will lead them to conquer greater market shares. Litigation and demand discouragement remain within manageable proportions. High levels of concentration at the national level remain acceptable and increase internationally, enabling them to become ever more efficient and to lower costs. More Indonesian and Indian smokers switch to (white) cigarettes. The worst-case scenario would be radically different. Privatization, and trade and capital liberalization, come to a halt. Chinese exporters become important competitors in the Asian market. Litigation becomes an ever greater threat, with claims so high that they threaten the very existence of the companies concerned. Efforts to discourage cigarette smoking are highly successful. Indonesian smokers stick to their *kretek* cigarettes and Indian smokers to their *bidis*. This latter scenario is the less likely of the two. But it cannot be discarded.

The prospects for further employment growth in the tobacco processing industry look dim, however. Even if demand were to increase on a significant scale, this demand impulse would most likely be outweighed by the effects of consolidation and further productivity increases. High cost countries with stagnant demand; countries preparing for market opening; and countries on the verge of privatizing their state-owned companies look particularly vulnerable. <sup>2</sup>

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<sup>2</sup> (Source: International Labor Organization, International Labor Office, 2002)

## 1.3 Characteristics & Qualities

BAT has not sustained a significant global business presence for 100 years by accident. By 1912, just a decade after the business was founded, BAT had become one of the world's top dozen companies by market capitalization.

- They are committed to building value for their shareholders
- They believe there is real value embedded not only in how they run the business but also in how a company is put together
- In its ability to see the world as it really is
- In its ability to pick and retain talent
- To build relationships of trust with consumers, suppliers, distributors and partners
- To manage high quality brands.

The flexibility, new thinking, financial strength and long term vision that has given the employees 'sticking' power for a century will continue to drive BAT forward in search of continuing success.



## 1.2.1 GUIDING PRINCIPLES

Other guiding principles of the PTC culture include:

- **Enterprising Spirit: “Dare to be Different”** is the attitude that the company wants to sell to its employees, competitors and customers. PTC wants to project the image of being a creative and enterprising company that is continuously working towards new ways of improvement and enhancing the quality of the product being provided. **“Strength from diversity”** is its aim. By providing an assortment of product range, it aspires to acquire greater market share and stronger brand image. Like PTC have different brands in market like Benson & Hedges, John Player Gold Leaf, and Gold Flake etc.
- **Freedom through Responsibility:** Another catch phrase that is of considerable importance among the employees is freedom through responsibility. Every employee believes that the freedom and empowerment that PTC bestows upon its staff, is a responsibility that has to be carried out with complete sincerity and devotion. This freedom enhances the commitment of the people to their jobs.
- **Passion for Excellence:** Another value that PTC tries to inculcate in its employees is a passion for excellence. It wants to be the best in everything it does and for that every contributing member needs to strive towards continuous improvement and perfection. PTC give their employees proper training according to their skills. They see if an employee, in CORA or in any other department, can do well in marketing they give them marketing training and thus enhance their employee’s skill.

### 1.3.1 History and Introduction

**BRITISH AMERICAN TOBACCO“BAT”:** British American Tobacco came into existence on 29 September 1902 when the UK’s Imperial Tobacco Company and the American Tobacco Company of the United States form a joint venture under the leadership of Buck Duke (Founder Chairman). His strategy is to devise a superior product, hire the best people to make it, price it as low as possible, and mechanize, organize and merchandise.

By 1910, British American Tobacco’s sales are more than 10 billion cigarettes. Profits grow correspondingly quickly. British American Tobacco companies are manufacturing in 140 factories across 50 countries. Since July 2004, the business has been led by Paul Adams as Chief Executive.

### 1.2.3. Principles of Business Conduct:

**British American Tobacco is a commercial enterprise and our primary role is to build long term shareholder value by meeting consumers' preferences for high-quality tobacco products. However, we believe that by absorbing and balancing a wider range of expectations, we are best placed to continue building a sustainable tobacco business.**

Like other multinational enterprises benefiting from economic globalisation, we also face increasing demands to be more transparent and to demonstrate high standards of corporate conduct that might in the past have been taken on trust.

In today's rapidly changing world, large and successful businesses can be perceived as powerful and self-interested and can face barriers to trust. As a tobacco business, we can face more than others. In addressing these, a further challenge is that major enterprises like ours often encounter varying and at times conflicting stakeholder expectations in different countries and cultures.

To help meet these challenges, and following a commitment in the first British American Tobacco p.l.c. Social Report 2001/02, we have developed this Statement of Business Principles in consultation with managers from our businesses, as well as with external stakeholders.

The Business Principles and Core Beliefs cover the key issues that we believe underpin Corporate Social Responsibility (CSR) for a multinational business and, particularly, for the unique characteristics of a tobacco business.

There are three Business Principles, Mutual Benefit, Responsible Product Stewardship and Good Corporate Conduct, each of which is supported by a number of Core Beliefs, which explain what we think the Principle means in more detail. Together, these form the basis on which we expect our businesses to be run in terms of responsibility.

Both the Business Principles and Core Beliefs and the way they have been developed are consistent with our four Guiding Principles, which collectively express the culture of British American Tobacco: Strength from Diversity; Open Minded; Freedom through Responsibility; and Enterprising Spirit.

# THE PRINCIPLE OF MUTUAL BENEFIT

The principle of **Mutual Benefit** is the basis on which we build our relationships with our stakeholders. We are primarily in business to build long term shareholder value and we believe the best way to do this is to seek to understand and take account of the needs of all our stakeholders.

- We believe in creating long term shareholder value
- We believe in engaging constructively with our stakeholders
- We believe in creating inspiring working environments for our people
- We believe in adding value to the communities in which we operate
- We believe that suppliers and other business partners should have the opportunity to benefit from their relationship with us

# THE PRINCIPLE OF RESPONSIBLE PRODUCT STEWARDSHIP

The principle of **Responsible Product Stewardship** is the basis on which we meet consumer demand for a legal product that is a cause of serious diseases. Therefore, our products and brands should be developed, manufactured and marketed in a responsible manner. We aspire to develop tobacco products with critical mass appeal that will, over time, be recognised by scientific and regulatory authorities as posing substantially reduced risks to health.

- We believe in the provision of accurate, clear health messages about the risks of tobacco consumption
- We believe the health impact of tobacco consumption should be reduced whilst respecting the right of informed adults to choose the products they prefer
- We believe that relevant and meaningful information about our products should continue to be available
- We believe that under-age people should not consume tobacco products
- We believe that our brands and products should be marketed responsibly and directed at adult consumers
- We believe in the appropriate taxation of tobacco products and the elimination of illicit trade
- We believe in regulation that balances the interests of all sections of society, including tobacco consumers and the tobacco industry
- We believe that public smoking should be approached in a way that balances the interests of smokers and non-smokers

# THE PRINCIPLE OF GOOD CORPORATE CONDUCT

The principle of **Good Corporate Conduct** is the basis on which all our businesses should be managed. Business success brings with it an obligation for high standards of behaviour and integrity in everything we do and wherever we operate. These standards should not be compromised for the sake of results.

- We believe our businesses should uphold high standards of behaviour and integrity
- We believe that high standards of corporate social responsibility should be promoted within the tobacco industry
- We believe that universally recognised fundamental human rights should be respected
- We believe our industry should have a voice in the formation of government policies affecting it
- We believe in achieving world-class standards of environmental performance

#### 1.2.4. PAKISTAN TOBACCO COMPANY “PTC”:

Pakistan Tobacco Company Limited was incorporated in 1947 immediately after partition, when it took over the business of the Imperial Tobacco Company of India which had been operational in the subcontinent since 1905.

We are part of the trans-national British American Tobacco Group, which employs some 85,000 people worldwide at its operations in 180 countries. British American Tobacco has a position of market leader in more than 50 countries selling over 300 brands there. In 2004, the Group sold and produced a nearly 16% share of the global market of cigarettes.

PTC is the largest excise tax generator in the private sector in the country. In 2004 alone, PTC paid the government close to Rs.16 Billion in excise and sales taxes. This amounts to over Rs. 50 million per working day. Over one million people are economically dependent on the industry in Pakistan.

**VISION:** First choice for everyone

**MISSION:** Transform PTC to perform with the speed, flexibility enterprising spirit of an innovative consumer focused company

***“DARE TO BE DIFFERENT”***

# *Chapter 2*

## *Literature review*



## 2.1 Value Chain Analysis



### Value Chain Analysis

The value chain is a systematic approach to examining the development of competitive advantage. It was created by M. E. Porter in his book, *Competitive Advantage* (1980). The chain consists of a series of activities that create and build value. They culminate in the total value delivered by an organization. The 'margin' depicted in the diagram is the same as added value. The organization is split into 'primary activities' and 'support activities.'<sup>3</sup>

### Primary Activities

#### *Inbound Logistics*

Here goods are received from a company's suppliers. They are stored until they are needed on the production/assembly line. Goods are moved around the organization.<sup>4</sup>

#### *Operations*

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<sup>3</sup> THE MARKETING TEACHER FREE MARKETING RESOURCE 2002, *online Branding and Positioning lessons* [online], Available from: [http://www.marketingteacher.com/Lessons/lesson\\_value\\_chain.htm](http://www.marketingteacher.com/Lessons/lesson_value_chain.htm) [Accessed 27 July 2005].

<sup>4</sup> THE MARKETING TEACHER FREE MARKETING RESOURCE 2002, *online Branding and Positioning lessons* [online], Available from: [http://www.marketingteacher.com/Lessons/lesson\\_value\\_chain.htm](http://www.marketingteacher.com/Lessons/lesson_value_chain.htm) [Accessed 27 July 2005].

This is where goods are manufactured or assembled. Individual operations could include room service in an hotel, packing of books/videos/games by an online retailer, or the final tune for a new car's engine.<sup>5</sup>

#### *Outbound Logistics*

The goods are now finished, and they need to be sent along the supply chain to wholesalers, retailers or the final consumer.

#### *Marketing and Sales*

In true customer orientated fashion, at this stage the organization prepares the offering to meet the needs of targeted customers. This area focuses strongly upon marketing communications and the promotions mix.

#### *Service*

This includes all areas of service such as installation, after-sales service, complaints handling, training and so on.

### **Support Activities**

#### *Procurement*

This function is responsible for all purchasing of goods, services and materials. The aim is to secure the lowest possible price for purchases of the highest possible quality. They will be responsible for outsourcing (components or operations that would normally be done in-house are done by other organizations), and purchasing (using IT and web-based technologies to achieve procurement aims).

#### *Technology Development*

Technology is an important source of competitive advantage. Companies need to innovate to reduce costs and to protect and sustain competitive advantage. This could include production technology, Internet marketing activities, lean manufacturing, Customer Relationship Management (CRM), and many other technological developments.

### *Human Resource Management (HRM)*

Employees are an expensive and vital resource. An organization would manage recruitment and selection, training and development, and rewards and remuneration. The mission and objectives of the organization would be driving force behind the HRM strategy.

### *Firm Infrastructure*

This activity includes and is driven by corporate or strategic planning. It includes the Management Information System (MIS) and other mechanisms for planning and control such as the accounting department.<sup>6</sup>

## **2.2 Marketing Mix 7-Ps**

The 7-Ps or Extended Marketing Mix of Booms and Bitner is a Marketing Strategy tool that expands the number of controllable variables from the four in the original Marketing Mix Model to seven. The [traditional Marketing Mix model](#) was primarily directed and useful for tangible products. The 7-Ps model is more useful for services industries and arguably also for knowledge-intensive environments.

Booms and Bitner's expanded the marketing mix by adding the following 3 additional P's:

- 5. People:** All people directly or indirectly involved in the consumption of a service are an important part of the extended marketing mix. Knowledge Workers, Employees, Management and other Consumers often add significant value to the total product or service offering.
- 6. Process:** Procedure, mechanisms and flow of activities by which services are consumed (customer management processes) are an essential element of the marketing strategy.
- 7. Physical Evidence:** The ability and environment in which the service is delivered, both tangible goods that help to communicate and perform the service and intangible experience of existing customers and the ability of the business to relay that customer satisfaction to potential customers.

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<sup>6</sup> THE MARKETING TEACHER FREE MARKETING RESOURCE 2002, *online Branding and Positioning lessons* [online], Available from: [http://www.marketingteacher.com/Lessons/lesson\\_value\\_chain.htm](http://www.marketingteacher.com/Lessons/lesson_value_chain.htm) [Accessed 27 July 2005].

The first two additional Ps are explicit (People, Process) and the third one (Physical Evidence) is an implicit factor. Booms and Bitner also suggest that **Place** in a service-oriented company includes the accessibility of the service, and that **Promotion** in a service-oriented company includes the input of front-line service personnel. <sup>7</sup>

### 2.3 Life Cycle based Portfolio Management:

The **ADL matrix** from **Arthur D. Little** is a **portfolio management method** that is based on [product life cycle](#) thinking.

The ADL portfolio management approach uses the dimensions of environmental assessment and business strength assessment. The environmental measure is an identification of the industry's life cycle. The business strengths measure is a categorization of the corporation's SBU's into one of five (6) competitive positions: dominant, strong, favorable, tenable, weak (and non-viable). This yields a 5 (competitive positions) by 4 (life cycle stages) matrix. Positioning in the matrix identifies a general strategy.

In the ADL approach, the line of business or SBU is not especially defined by a product or organizational unit. The strategist must **identify discrete businesses** by finding commonalities among products and business lines using the following criteria as guidelines:

- Common rivals
- Prices
- Customers
- Quality/Style
- Substitutability
- Divestment or liquidation

This assessment of the **industry life cycle stage** of each business is made on the basis of:

- Business market share,
- Investment, and
- Profitability and cash flow.

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<sup>7</sup> THE MANAGEMENT PORTAL VALUE BASED MANAGEMENT.COM 2005, *Library services electronic resources* [online]. Available from: [http://www.valuebasedmanagement.net/methods\\_booms\\_bitner\\_7Ps.html](http://www.valuebasedmanagement.net/methods_booms_bitner_7Ps.html) [Accessed 18 July 2005].

The **competitive position** of a firm is based on an assessment of the following criteria:

- **Dominant:** Rare. Often results from a near monopoly or protected leadership.
- **Strong:** A strong business can usually follow a strategy without too much consideration of moves from rivals.
- **Favorable:** Industry is fragmented. No clear leader among stronger rivals.
- **Tenable:** Business has a niche, either geographical or defined by the product.
- **Weak:** Business is too small to be profitable or survive over the long term. Critical weaknesses.

Known **limitations of the ADL matrix** include:

- There is no standard length of life cycles,
- Determining the current industry life cycle phase is awkward,
- Competitors may influence the length of the life cycle.<sup>8</sup>

## 2.4 The BCG matrix

### Product portfolio method

The **BCG matrix method** is based on the [product life cycle](#) theory that can be used to determine what priorities should be given in the **product portfolio of a business unit**. To ensure long-term value creation, a company should have a portfolio of products that contains both high-growth products in need of cash inputs and low-growth products that generate a lot of cash. It has 2 dimensions: **market share** and **market growth**. The basic idea behind it is that the bigger the market share a product has or the faster the product's market grows the better it is for the company.

Placing products in the BCG matrix results in 4 categories in a portfolio of a company:

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<sup>8</sup> THE MANAGEMENT PORTAL VALUEBASEDMANAGEMENT.COM 2005, *Library services electronic resources* [online]. Available from: [http://www.valuebasedmanagement.net/methods\\_adl\\_matrix.html](http://www.valuebasedmanagement.net/methods_adl_matrix.html) [Accessed 18 July 2005].

**Stars** (=high growth, high market share)

- use large amounts of cash and are leaders in the business so they should also generate large amounts of cash.
- frequently roughly in balance on net cash flow. However if needed any attempt should be made to hold share, because the rewards will be a cash cow if market share is kept.

**2. Cash Cows** (=low growth, high market share)

- profits and cash generation should be high, and because of the low growth, investments needed should be low. Keep profits high
- Foundation of a company

**3. Dogs** (=low growth, low market share)

- avoid and minimize the number of dogs in a company.
- beware of expensive 'turn around plans'.
- deliver cash, otherwise liquidate

**4. Question Marks** (= high growth, low market share)

- have the worst cash characteristics of all, because high demands and low returns due to low market share
- if nothing is done to change the market share, question marks will simply absorb great amounts of cash and later, as the growth stops, a dog.
- either invest heavily or sell off or invest nothing and generate whatever cash it can. Increase market share or deliver cash

The **BCG Matrix method** can help understand a frequently made strategy mistake: having a one-size-fits-all-approach to strategy, such as a generic growth target (9 percent per year) or a generic return on capital of say 9,5% for an entire corporation.

In such a scenario:

A. Cash Cows Business Units will beat their profit target easily; their management have an easy job and are often praised anyhow. Even worse, they are often allowed to reinvest substantial cash amounts in their businesses which are mature and not growing anymore.

B. Dogs Business Units fight an impossible battle and, even worse, investments are made now and then in hopeless attempts to 'turn the business around'.

C. As a result (all) Question Marks and Stars Business Units get mediocre size investment funds. In this way they are unable to ever become cash cows. These inadequate invested sums of money are a waste of money. Either these SBUs should receive enough investment funds to enable them to achieve a real market dominance and become a cash cow (or star), or otherwise companies are advised to disinvest and try to get whatever possible cash out of the question marks that were not selected.

Some **limitations of the Boston Consulting Group Matrix** include:

- High market share is not the only success factor
- Market growth is not the only indicator for attractiveness of a market
- Sometimes Dogs can earn even more cash as Cash Cows<sup>9</sup>

## 2.5 BVA - Brand Asset Valuator

### Measuring Brand Value

The Brand Asset Valuator of advertising agency Young & Rubicam measures Brand Value by applying four broad factors:

1. Differentiation – Differentiation is the ability for a brand to stand apart from its competitors. A brand should be as unique as possible. Brand health is built and maintained by offering a set of differentiating promises to consumers and delivering those promises to leverage value.
2. Relevance – Relevance is the actual and perceived importance of the brand to a large consumer market segment. This gauges the personal appropriateness of a brand to consumers and is strongly tied to household penetration (the percentage of households that purchase the brand).
3. Esteem - Esteem is the perceived quality and consumer perceptions about the growing or declining popularity of a brand. Does the brand keep its promises? The consumer's response to a marketer's brand-building activity is driven by his perception of two factors: quality and

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<sup>9</sup> THE MANAGEMENT PORTAL VALUEBASEDMANAGEMENT.COM 2005, *Library services electronic resources* [online]. Available from: [http://www.valuebasedmanagement.net/methods\\_bcgmatrix.html](http://www.valuebasedmanagement.net/methods_bcgmatrix.html) [Accessed 18 July 2005].

popularity, both of which vary by country and culture.

4. Knowledge –Knowledge is the extent of the consumer's awareness of the brand and understanding of its identity. The awareness levels about the brand and what it stands for shows the intimacy that consumers share with the brand. True knowledge of the brand comes through brand-building. Differentiation and Relevance taken together say a lot about its growth potential ("Brand Vitality"), while Esteem and Knowledge determine the current power of a brand ("Brand Stature").

A Survey based on the Brand Asset Valuator is conducted annually containing data about 20.000 brands, based on the opinion of over 230.000 respondents in 44 countries. 10

## 2.6 Brand Personality Dimensions of Jennifer Aaker

The **Brand Personality Dimensions** of **Jennifer Aaker** is a framework to describe and measure the 'personality' of a brand in five core dimensions, each divided into a set of facets.

It is an easy to understand model to describe the profile of a brand using an analogy with a human being.

The **five core dimensions and their facets** are:

- **Sincerity** (down-to-earth, honest, wholesome, cheerful)
- **Excitement** (daring, spirited, imaginative, up-to-date)
- **Competence** (reliable, intelligent, successful)
- **Sophistication** (upper class, charming)
- **Ruggedness** (outdoorsy, tough)

Each facet is in turn measured by a set of traits. The trait measures are taken using a five-point scale (1= not at all descriptive, 5=extremely descriptive) rating the extent to which each trait describes the specific brand of interest. The **traits belonging to each of the facets** are:

- Down-to-earth (down-to-earth, family-oriented, small-town)
- Honest (honest, sincere, real)
- Wholesome (wholesome, original)
- Cheerful (cheerful, sentimental, friendly)
- Daring (daring, trendy, exciting)

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<sup>10</sup> THE MANAGEMENT PORTAL VALUEBASEDMANAGEMENT.COM 2005, *Library services electronic resources* [online]. Available from: [http://www.valuebasedmanagement.net/methods\\_brand\\_asset\\_valuator.html](http://www.valuebasedmanagement.net/methods_brand_asset_valuator.html) [Accessed 18 July 2005].



- Spirited (spirited, cool, young)
- Imaginative (imaginative, unique)
- Up-to-date (up-to-date, independent, contemporary)
- Reliable (reliable, hard working, secure)
- Intelligent (intelligent, technical, corporate)
- Successful (successful, leader, confident)
- Upper class (upper class, glamorous, good looking)
- Charming (charming, feminine, smooth)
- Outdoorsy (outdoorsy, masculine, Western)
- Tough (tough, rugged)

The **Brand Personality Dimensions Framework** of **Jennifer Aaker** can be used to investigate the current status (IST) of a brand and to describe the desired future status (SOLL) of it. <sup>11</sup>

## 2.6 Marketing Mix 4P's model 5P's:

The **Marketing Mix model** (also known as the 4 P's) can be used by marketers as a tool to assist in implementing the M. strategy. M. managers use this method to attempt to generate the optimal response in the target market by blending 4 (or 5, or 7) variables in an optimal way. It is important to understand that the **MM principles** are controllable variables. The MM can be adjusted on a frequent basis to meet the changing needs of the target group and the other dynamics of the M. environment.

<b>Product</b>	Historically, the thinking was: a good product will sell itself. However there are no bad products anymore in today's highly competitive markets. Plus there are many laws giving customers the right to return products that he perceives as bad. Therefore the question on product has become: does the organization create what its intended customers want? Define the characteristics of your	Functionality, Quality, Appearance, Packaging, Brand, Service, Support, Warranty
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<sup>11</sup> THE MANAGEMENT PORTAL VALUEBASEDMANAGEMENT.COM 2005, *Library services electronic resources* [online]. Available from: [http://www.valuebasedmanagement.net/methods\\_aaker\\_brand\\_personality\\_framework.html](http://www.valuebasedmanagement.net/methods_aaker_brand_personality_framework.html). [Accessed 18 July 2005].

	product or service that meets the needs of your customers.	
<b>Price</b>	How much are the intended customers willing to pay? Here we decide on a pricing strategy - do not let it just happen! Even if you decide not to charge for a service (a loss leader), you must realize that this is a conscious decision and forms part of the pricing strategy. Although competing on price is as old as mankind, the consumer is often still sensitive for price discounts and special offers. Price has also an irrational side: something that is expensive must be good. Permanently competing on price is for many companies not a very sensible approach.	List Price, Discounts, Financing, Leasing, Options, Allowances,
<b>Place</b>	Available at the right place, at the right time, in the right quantities? Some of the revolutions in business have come about by changing Place. Think of the internet and mobile telephones.	Locations, Logistics, Channel members, Channel Motivation, Market Coverage, Service Levels, Internet, Mobile
<b>Promotion</b>	(How) are the chosen target groups informed or educated about the organization and its products? This includes all the weapons in the marketing armory - advertising, selling, sales promotions, Public Relations, etc. While the other three P's have lost much of their meaning in today's markets, Promotion has become the most important P to focus on.	Advertising, Public Relations, Message, Direct Sales, Sales, Media, Budget

The **function of the MM** is to help develop a package (mix) that will not only satisfy the needs of the customers within the target markets, but simultaneously to maximize the performance of the organization. There have been many attempts to increase the number of P's from 4 to **5P's in the MM model**. The most frequently mentioned one being **People** or **Personnel**. Booms and Bitner have suggested a **7-Ps** approach for services-oriented companies.<sup>12</sup>

<sup>12</sup> THE MANAGEMENT PORTAL VALUEBASEDMANAGEMENT.COM 2005, *Library services electronic resources* [online]. Available from: [http://www.valuebasedmanagement.net/methods\\_marketing\\_mix.html](http://www.valuebasedmanagement.net/methods_marketing_mix.html) [Accessed 18 July 2005].



## 2.7 7-S framework of McKinsey

### Description of the 7-S framework of McKinsey

The **7-S framework** of McKinsey is a **Value Based Management (VBM) model** that describes how one can *holistically and effectively organize a company*. Together these factors determine the way in which a corporation operates.

### Shared Value

The interconnecting center of McKinsey's model is: Shared Values. What does the organization stand for and what it believes in or what can be said as the organization's Central beliefs and attitudes.

### Strategy

Strategies are the action Plans for the allocation of a firm's scarce resources, over time, to reach identified goals and to gain competitive advantage. These are the actions taken to assess the Environment, competition, customers.

### Structure

The way the organization's units relate to each other: centralized, functional divisions (top-down); decentralized (the trend in larger organizations); what kind of a reporting relationships people working in the organization have for example matrix, network, holding, etc.

### System

The procedures, processes and routines that characterize how important work is to be done: financial systems; hiring, promotion and performance appraisal systems; information systems. System is everything which transforms or helps transform inputs into outputs.

### Staff

Staff are the number of people working in the organization, or the human resource involved in transforming inputs to outputs and all the other core and value adding activities. Numbers and types of personnel within the organization is the staff.

### Style

It is the organizational way of doing things and working. Cultural style of the organization and how key managers behave in achieving the organization's goals or Management Styles.

### **Skill**

It is the human, managerial and technical knowledge and abilities that the staff possess. Distinctive capabilities of personnel or of the organization as a whole.. the skill set of the staff builds up the [Core Competences](#), which is the source of strength and competitive advantage.<sup>13</sup>

## **2.8 Value Chain framework of Michael Porter:**

The **Value Chain framework of Michael Porter** is a model that helps to analyze specific activities through which firms can create value and competitive advantage.

### **Inbound Logistics**

Includes receiving, storing, inventory control, transportation scheduling.

### **Operations**

Includes machining, packaging, assembly, equipment maintenance, testing and all other value-creating activities that transform the inputs into the final product.

### **Outbound Logistics**

The activities required to get the finished product to the customers: warehousing, order fulfillment, transportation, distribution management.

### **Value Chain model of Michael Porter: Marketing and Sales**

The activities associated with getting buyers to purchase the product including channel selection, advertising, promotion, selling, pricing, retail management, etc.

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<sup>13</sup> THE MANAGEMENT PORTAL VALUEBASEDMANAGEMENT.COM 2005, *Library services electronic resources* [online]. Available from: [http://www.valuebasedmanagement.net/methods\\_7S.html](http://www.valuebasedmanagement.net/methods_7S.html) [Accessed 18 July 2005].

## **Service**

The activities that maintain and enhance the product's value, including customer support, repair services, installation, training, spare parts management, upgrading, etc.

## **Procurement**

Procurement of raw materials, servicing, spare parts, buildings, machines, etc.

## **Technology Development**

Includes technology development to support the value chain activities, such as Research and Development, Process automation, design, redesign.

## **Value Chain model of Michael Porter: Human Resource Management**

The activities associated with recruiting, development (education), retention and compensation of employees and managers.

## **Firm Infrastructure**

Includes general management, planning management, legal, finance, accounting, public affairs, quality management, etc.

From a Value Based Management point of view, the Value Chain Framework helps to build a relative competitive advantage, together with Porter's [Competitive Advantage](#) thinking. The Value Chain Framework can be seen as one of two dimensions in maximizing corporate value creation. The other value creation dimension is the Market/Industry Attractiveness for which another model from Porter is often used: the [Competitive Forces](#) model.<sup>14</sup>

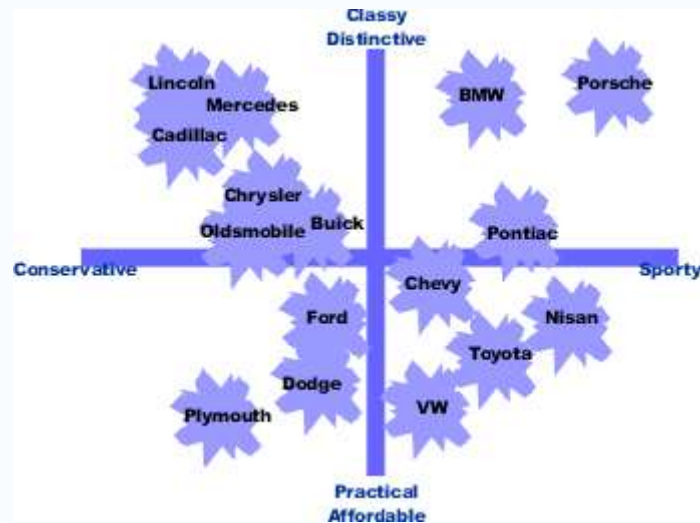
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<sup>14</sup> THE MANAGEMENT PORTAL VALUEBASEDMANAGEMENT.COM 2005, *Library services electronic resources* [online]. Available from: [http://www.valuebasedmanagement.net/methods\\_porter\\_value\\_chain.html](http://www.valuebasedmanagement.net/methods_porter_value_chain.html) [Accessed 18 July 2005].

## 2.9 Perceptual mapping

**Perceptual mapping** is a [graphics](#) technique used by [marketers](#) that attempts to visually display the perceptions of customers or potential customers. Typically the [position](#) of a [product](#), [product line](#), [brand](#), or company is displayed relative to their competition.<sup>15</sup>

Perceptual maps can have any number of dimensions but the most common is two dimensions. Any more is a challenge to draw and confusing to interpret. The first perceptual map below shows consumer perceptions of various [automobiles](#) on the two dimensions of sportiness/conservative and classy/affordable. This sample of consumers felt [Porsche](#) was the sportiest and classiest of the cars in the study (top right corner). They felt [Plymouth](#) was most practical and conservative (bottom left corner).<sup>16</sup>



*Perceptual Map of Competing Products*

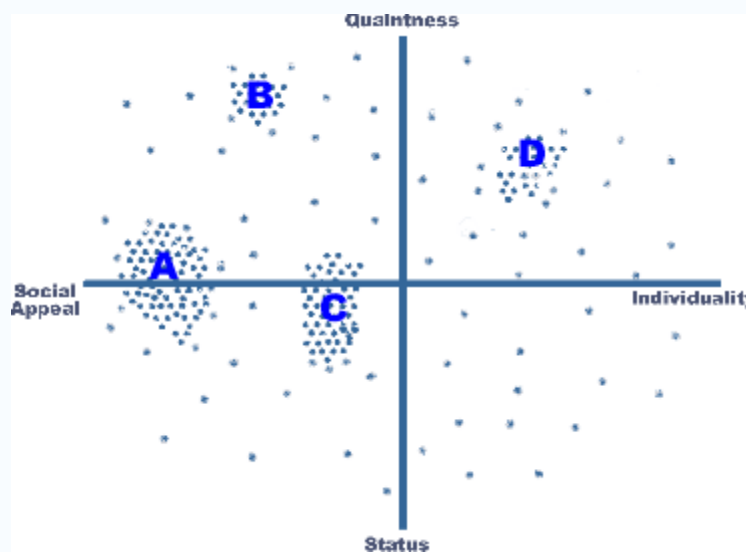
Cars that are positioned close to each other are seen as similar on the relevant dimensions by the consumer. For example consumers see Buick, Chrysler, and Oldsmobile as similar. They are close competitors and form a competitive grouping. A company considering the introduction of a new model will look for an area on the map free from competitors. Some

<sup>15</sup>

<sup>16</sup> Perceptual Mapping Analysis from Wikipedia, the free encyclopedia, Available at: [www.wikipedia.com](http://www.wikipedia.com), 24<sup>th</sup> August, 2005

perceptual maps use different size circles to indicate the sales volume or market share of the various competing products.

Displaying consumers' perceptions of related products is only half the story. Many perceptual maps also display consumers' ideal points. These points reflect ideal combinations of the two dimensions as seen by a consumer. The next diagram shows a study of consumers' ideal points in the alcohol/spirits product space. Each dot represents one respondents ideal combination of the two dimensions. Areas where there is a cluster of ideal points (such as A) indicates a [market segment](#). Areas without ideal points are sometimes referred to as demand voids.<sup>17</sup>



*Perceptual Map of Ideal Points and Clusters*

A company considering introducing a new product will look for areas with a high density of ideal points. They will also look for areas without competitive rivals. This is best done by placing both the ideal points and the competing products on the same map.<sup>18</sup>

Some maps plot ideal vectors instead of ideal points. The map below, displays various aspirin products as seen on the dimensions of effectiveness and gentleness. It also shows two ideal vectors. The slope of the ideal vector indicates the preferred ratio of the two dimensions by

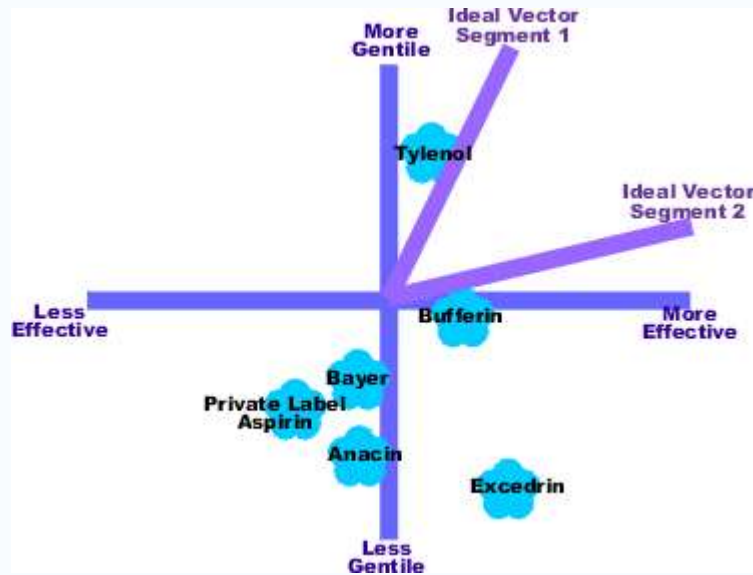
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<sup>17</sup> Perceptual Mapping Analysis from Wikipedia, the free encyclopedia, Available at: [www.wikipedia.com](http://www.wikipedia.com), 24<sup>th</sup> August, 2005

<sup>18</sup> Perceptual Mapping Analysis from Wikipedia, the free encyclopedia, Available at: [www.wikipedia.com](http://www.wikipedia.com), 24<sup>th</sup> August, 2005



those consumers within that segment. This study indicates there is one segment that is more concerned with effectiveness than harshness, and another segment that is more interested in gentleness than strength.<sup>19</sup>



*Perceptual Map of Competing Products with Ideal Vectors*

Perceptual maps need not come from a detailed study. There are also intuitive maps (also called judgmental maps or consensus maps) that are created by marketers based on their understanding of their industry. Management uses its best judgement. It is questionable how valuable this type of map is. Often they just give the appearance of credibility to management's preconceptions.

When detailed marketing research studies are done methodological problems can arise, but at least the information is coming directly from the consumer. There is an assortment of statistical procedures that can be used to convert the raw data collected in a survey into a perceptual map. [Preference regression](#) will produce ideal vectors. [Multi dimensional scaling](#) will produce either ideal points or competitor positions. [Factor analysis](#), [discriminant analysis](#), [cluster analysis](#), and [logit analysis](#) can also be used. Some techniques are constructed from perceived differences between products, others are constructed from perceived similarities.

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<sup>19</sup> Perceptual Mapping Analysis from Wikipedia, the free encyclopedia, Available at: [www.wikipedia.com](http://www.wikipedia.com), 24<sup>th</sup> August, 2005

Still others are constructed from [cross price elasticity of demand](#) data from electronic scanners.<sup>20</sup>

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<sup>20</sup>Perceptual Mapping Analysis from Wikipedia, the free encyclopedia, Available at: [www.wikipedia.com](http://www.wikipedia.com), 24<sup>th</sup> August, 2005

# *Chapter 3*

## Research Methodology

### **3.1. Introduction:**

Pakistan Tobacco Company is the first multinational investment in Pakistan, having a history and presence as old as the country itself. It is the largest taxpayer and revenue generator for the government of Pakistan outside the oil sector, which makes it a very valuable company for the Government of Pakistan.

This thesis would primarily discuss the marketing strategies of PTC, in general and how they have changed their strategies in the wake of restrictions on conventional ways of marketing for the tobacco companies worldwide.

Tobacco marketing has been under severe criticism worldwide for the last 10 to 15 years, and the allegations have been that it provokes young people to smoke because of attractive advertising, which connects performance, masculinity, athleticism, and adventure with smoking and is thought to have been instrumental in making young people smoke and generating smoking incidences.

Although there wasn't any kind of a major pressure on PTC to change the way they were doing advertising and marketing, they realized that very soon they could be facing the same problem, as the WHO and the world anti tobacco movements had become very active in pursuing a no tobacco and no advertising regime, and rather than finding solutions at that point, they decided to voluntarily adapt laws and regulations, that didn't even exist in Pakistan. The British American Tobacco along with PMI and JTI drafted a standard code of conduct for marketing and advertising of tobacco based products, which virtually restricts all kinds of advertisements in the electronic media. PTC fully implemented these standards in 2001, although it had unofficially embarked on a no advertising strategy since 1999.

The era after the full implementation and adoption of these standards is known as the "New World of Marketing" or NWOM, because nothing is the way it has used to be for the last 100 years and it's a whole new world and new methods of doing the same things.

This study encompasses the reasons, needs and effects of the International Marketing Standards and the NWOM, and how things have changed for PTC after that. It would also discuss how PTC can now use the same resources in marketing their products in an environment of stiffer competition, and gain the competitive advantage that it always had.

### **3.2 Significance of the Research:**

The study is important because general people have the perception that tobacco companies use negative and persuasive ways to attract young people in generating new smokers. This study would try to communicate PTC's strategy in this regard, and analyze what made them impose such restrictions on themselves, and how has it impacted them.

Cigarette is the fastest moving item, whose turnover is much higher and speedier than generally known FMCGs. This study is also significant because the analysis of the cigarette sector would give us insights about the movements of other FMCGs. The study's significance also increases because it delves into multiple core concepts of marketing such as trade marketing, brand management, channel management, merchandising, value chain, and research and consumer behavior.

### **3.3 The Thesis Plan:**

The thesis is planned in a sequence which is as follows:

- Introduction
- Literature Review
- Internal and External Environment (Environment Scanning). This includes SWOT analysis describing key Strengths, weaknesses, opportunities and threats.
- Competitive Environmental Analysis
- Findings and Analysis
- Conclusion& Recommendations
- Bibliography

### **3.4 Research Methodology**

The thesis has been completed employing different methodologies but primary research by the researcher has been a predominant one. Being attached with PTC for the last 2 months and training in Trade Marketing and Distribution, all the information has been acquired from experience and interviews with people associated with trade marketing and primary sales at a national and a regional level.

The information has been gathered from area managers, Trade marketing officers, Sales promoters and salesmen in the Central Punjab region. Additionally company wide information has been gathered from the head office. Apart from interviews, PTC's marketing documents and manuals have been referenced which are private and confidential documents. The researcher has spend around one month with the Central Punjab Trade Marketing and Distribution team in the markets of Lahore, Kasoor, Kahna and Raiwand, observing the marketing activities and questioning everybody involved from the salesman to the shopkeepers. The research has been very hands on and a through one where first hand market intelligence and response has been used rather than basing opinions using text or theories.

### **3.5 Limitations of the Thesis**

The thesis is mostly limited to the trade marketing and distribution aspects of PTC and its brands, and discusses what effect the new regime of International Marketing Standards would have on the trade marketing, which is the backbone of marketing in PTC. Although PTC has brands and marketing research departments, studying them would have made the study extremely lengthy and the time constraint would have to be removed. Since the International Marketing Standards have had direct implications on the Trade Marketing, it is justified to have more emphasis on trade aspect more than anyone else. Having said that, the brands aspect has not been totally ignored and is covered from time to time within the study as and where needed.

The study discusses the trade marketing and distribution strategy with respect to the whole company but would be focusing more on Central Punjab, being one of the largest markets in Pakistan, and because of dynamically changing and challenging circumstances in the specific

market, and would be discussing the Lahore market in the central Punjab Region being the largest market in the region.

### **3.6 Hypothesis**

This research study is based on the following hypothesis

- H1: Advertising does not have a huge impact on repeat sales of cigarettes, nor it changes smokers' choice drastically and hence below the line communications like personal selling, PR and relationship marketing is the most effective way of communicating with the target market for tobacco products.
- H2: Pricing of brands is the main determinant in establishing the personality and the perception of the brand. Positioning strategies in the tobacco industry plays an important role in the success of a new brand. Consumers stick to their known preferences and do not experiment a lot in their consumption patterns.
- H3: Value Chain model analysis and optimization is the cornerstone for marketing efficiencies in Fast Moving Consumer Good companies and by aligning and optimizing all the links in the value chain, synergies can be achieved which would cut costs and increase profits.

# *Chapter 4*

## *Company Analysis*



## **4.1 Pakistan Tobacco Company**

### 4.1.1 Aims and Objectives:

- Establish a focused, segmented and differentiated brand portfolio.
- Create a winning corporate culture, with focus on vision, mission and values.
- Drive consumer focused operational excellence i.e. Striving to meet stakeholders expectations
- Regaining volume and value leadership by positioning viable brands in all consumer relevant segments
- Driving world class standards in products processes and services through passionate, skilled and confident people
- Create a winning corporate culture with focus on Vision, Mission and Values
- Restructure PTC's cost base to become competitive locally and globally

### 4.1.2 Company Profile

Pakistan Tobacco Company (PTC) is a subsidiary of British American Tobacco (BAT), which is the largest international tobacco group in the world. PTC had been a top blue chip company until the mid 1990s when performance started to waver, market leadership was lost and rumors began spreading about factory closure and shareholders pulling out. A radical solution was needed, and the way forward was established in a 16-hour meeting of all managers and union officials, where concerns were raised and openly discussed, subsequent steps in the right direction changed all that and PTC regained its lost glory once again.

Pakistan Tobacco Company Limited (PTC) was incorporated in 1947 immediately after partition when it took over the business of the Imperial Tobacco Company of India. PTC is the first multinational company of Pakistan. It has come a long way from being just a small warehouse at Karachi port to one of the largest tobacco Company in Pakistan. The rapid expansion had transcended PTC into an institution that is proud of its endeavors for introducing innovations and breakthroughs in Pakistan. PTC is proud of its heritage and for being a company that derives its strength from its lone-term presence in Pakistan and from sharing learning's from BAT's global experiences. PTC is the first multinational to set up its business in Pakistan. It has been a leader in benchmarking innovative brands and marketing campaigns, which brought a whole new competitive edge to Pakistan's business world. PTC is proud of our reputation for manufacturing high quality cigarette brands.

The mission statement of PTC envisions itself as being the **'1<sup>st</sup> choice for everyone'**. It has continued to relentlessly pursue its medium-term Mission of ***“Transform PTC to perform with the speed, flexibility and enterprising spirit of an innovative, consumer-focused company.”***

The vision of PTC comprises of the following:

- Regaining volume and value leadership by positioning viable brands in all consumer relevant segments
- Driving world class standards in products processes and services through passionate, skilled and confident people
- Striving to meet stakeholders expectations
- To establish a focused, segmented and differentiated brand portfolio
- Create a winning corporate culture with focus on Vision, Mission and Values
- Restructure PTC's cost base to become competitive locally and globally
- Drive consumer-focused operational excellence

Throughout the BAT world, PTC is often mentioned and recognized as a leading company for its many successful initiatives.

## **4.2 BRAND PORTFOLIO**

PTC enjoys a strong consumer led portfolio of international, regional and national brands. Their goal is to fulfill the consumer needs for quality and satisfaction by providing brands to suit their preferences. PTC's brand portfolio is highly developed, has a high degree of brand awareness acceptability, and preference and loyalty.

<u>Category</u>	<u>Image</u>	<u>Brand</u>	<u>Price (Rs)</u>
<b>PREMIUM</b>	<b>International</b>	<b>Benson &amp; Hedges</b>	<b>60-65</b>
<b>HIGH</b>	International	John Players Gold Leaf	40
<b>MEDIUM</b>	Regional	Capstan	28
		Wills international	21
		Wills Navy Cut	13
		Wills Kings	25
<b>LOW</b>	Local	Gold Flake	15
		Embassy Filters	8
		Embassy Kings	14

### 4.3 Structure and Design of PTC

Since 96% of PTC is owned by B.A.T (British American Tobacco), the top management is regulated by B.A.T. Planning is done by the Board of Directors of PTC, jointly with B.A.T. Whether its product innovation, marketing campaigns or any other goals for the company, all are finalized by the Board of Directors. Mostly a period of 15 months or 2 years, pass before a new campaign is designed, finalized and launched.

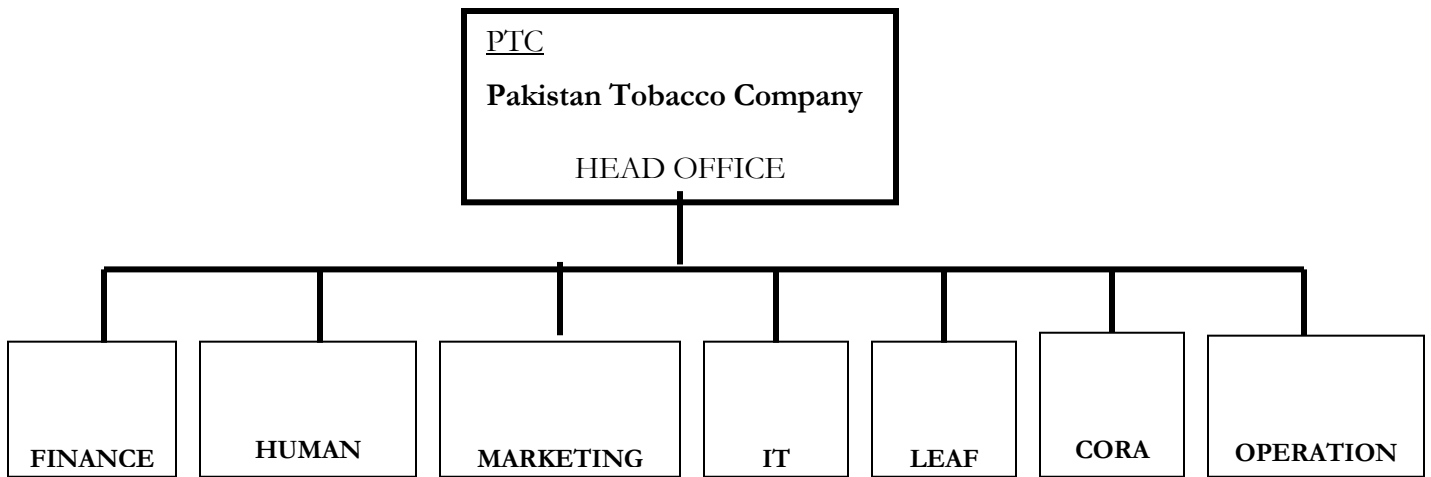
The Company consists of seven departments.

Authority given to the managers and directors of all the departments is the key to leading and directing in the organization.

The departments in the Pakistan Tobacco Company are as follows:

1. Human Resource
2. Marketing
3. Finance
4. Production
5. CORA (Corporate and Regulatory Affairs)

- 6. Legal
- 7. Leaf
- 8. Information Technology



## 4.4 Departments at PTC Head Office:

### 4.4.1 CORA (Corporate and regulatory Affairs):

This department deals with all the legal issues of the company. This department acts as a bridge for the organization, which connects it to its stakeholders.

Cora's strategy is designed to address the fundamental issues that influence public attitudes towards PTC.

- The primary issue is the risky nature of the product.
- It is recognized that along with the pleasures of smoking come real risks of serious diseases.
- It is recognized that, for many people, smoking is difficult to quit

### 4.4.2 Finance:

#### *Finance Vision*

“To be a pro-active value-adding business partner in delivery of the strategic imperatives and the management of shareholder value expectations”

This means that we must be seamlessly and actively embedded in the main business streams, adding challenge and innovation to the business processes whilst at the same time providing world-class cutting edge professionalism in Treasury, Tax, Audit and Corporate Accounting.

### 4.4.3 HR (Human Resource):

HR department deals with the following activities.

1. Measuring and aligning performance.
2. Managing organization learning
3. Resourcing
4. Managing Career Development
5. Managing Employee Relations

#### 4.4.4 IT Department:

IT provides all the infrastructure and support to the different functional departments. It also ensures that all the information required by the managers for decision making is available on time.

#### 4.4.5 Operations:

Operations are further subdivided into:

1. Leaf
2. Manufacturing
3. Supply Chain
4. Procurement

##### 1) *Leaf:*

###### **LEAF VISION**

"To maintain, develop and use our strong integrated position in Leaf world-wide to leverage the business to our advantage, vis-à-vis Security of Supply, Quality, Price and competitively to support BAT's growth to Number One."

##### 2) *Manufacturing:*

The way forward for manufacturing in PTC is being developed through the Manufacturing Strategy. In order to set a framework for manufacturing, which will enable PTC to respond to challenges in the future, the Strategy outlines the priorities which guide their marketing decisions.

PTC has six key departments within Manufacturing which develop, communicate and drive the implementation of the Strategy throughout the regions and operating companies in PTC:

1. Manufacturing Strategy & Sourcing
2. Strategic Machinery & Technology
3. Product Quality
4. Environmental, Health & Safety
5. Operations Technical Support
6. Manufacturing Performance

### **3) *Supply Chain:***

Supply Chain encompasses all processes, procedures and actions involved in planning, sourcing, producing and delivering our finished products.

#### *Supply Chain Vision:*

"To create a seamless end-to end supply chain from suppliers to customers, which provides excellent customer service at optimal overall cost?"

### **4) *Procurement:***

The aim is to ensure that PTC leverage their considerable global scale and in doing so act as one Company. Within this, their drive is to responsibly manage our global supply base in the short and long term. This is both in terms of the risks and the opportunities. It is further subdivided into direct and indirect procurement.



#### 4.4.6 Marketing:

Marketing is further subdivided into three functional areas which are:

1. Trade Marketing
2. Brand Marketing
3. Marketing Research

#### 4.4.7 Operation Finance

This section is placed in the production department as it only deals with the financial side of production. It can be considered as generally responsible for information management related to financial side of production, and scenario building for various other departments like marketing finance, one such case could be that of analyzing the change in the prices and import duties on various materials, or adjustment for changes in exchange rate, the final impact being the price of the stock keeping unit (SKU).

Following are the activities performed by this department:-

- Actual Costing - The calculation of the product cost is one of the major responsibilities of this department. The major components of the product cost are :
  1. Leaf
  2. Wrapping material
  3. Manufacturing cost
- Forecasting
- Regional Data Consolidation
- CAPEX – Actual consolidation and Forecasting
- Leaf buying/ Export
- Variance Analysis
- Scenario Analysis

#### 4.4.8 Internal Audit

Internal Audit department is mainly responsible for the audit of the strategic business objectives of the organization an audit directly reports its analysis to the international audit department at BAT headquarters.

## 4.2 The concept of “From Seed to Smoke”:

The tobacco plant is a member of the same botanical family as tomatoes, potatoes, peppers or eggplants. An adaptive species, it can be grown economically from 50° Northern to 40° Southern latitude.

More than 100 countries grow tobacco. China is the largest producer, followed by the United States, Brazil, India, Zimbabwe and Turkey. Tobacco thrives in poorer soils, providing farmers with a welcome alternative crop. In many cases, it provides a higher income than any other smallholder crop. As a crop, it integrates well into environmentally friendly rotations, and its inclusion benefits subsequent crops like maize.

A typical farmer in rural Uganda, for example, with two to three hectares of land can earn a good income from only a small part of that land being planted with tobacco. British American Tobacco can help the farmer by providing seeds and fertiliser and by giving advice on planting, growing, harvesting and curing tobacco and other crops.

There are some 13,000 tobacco seeds in a gram - looking rather like powdery instant coffee. The seeds are so small that they must be nurtured in specially prepared and protected seedbeds for 60 days before transplanting to the field.

After a couple of weeks, soil is banked up around the seedlings to protect them and to allow them to develop a good root system. Two months later, the plants' flowers and some of the upper leaves are 'topped' to concentrate growth in the remaining leaves (in the same way that tomato is 'pinched out').

Throughout the growing period, the farmer needs to provide the appropriate nutrition for the plant and watch out for pests as the crop grows towards the harvesting stage.<sup>21</sup>

### 4.2.1 Harvesting:

With the exception of some countries such as the United States, where the crop is

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<sup>21</sup> ([www.PTC.com.pk](http://www.PTC.com.pk), August 2005)

mechanically harvested, the farmer will typically harvest by hand, sequentially taking off 2-4 leaves per plant as the leaves ripen from bottom to top, which stretches the harvesting period from over 2 to 4 months. The typical Ugandan farmer will harvest about 15,000 plants, each with 22 leaves.<sup>22</sup>

Virginia tobacco is named after the US state where it was first cultivated. It is also called "bright tobacco" because of its yellow to orange colour, achieved during the flue-cure. This type grows particularly well in subtropical regions with light rainfall, such as Georgia (USA), southern Brazil and Zimbabwe. Classic English brands like Benson & Hedges and Dunhill use exclusively Virginia tobacco.

Burley is a slightly lighter shade of green than Virginia. After being air-cured, the tobacco turns brown with virtually no sugar, giving it an almost cigar-like taste. It requires heavier soils and more fertiliser than Virginia. The best Burley is grown in the USA, Central America, Malawi and Uganda. Together with Virginia and Oriental tobacco, it makes up an American Blend, as used in brands like Lucky Strike or Pall Mall.

Oriental is the smallest and hardiest of all tobacco types, grown into the hot summer of the Balkans, Turkey and the Middle East. These conditions and a high planting density create an aromatic flavour, enhanced by sun-curing, as in a traditional Turkish cigarette.<sup>23</sup>

#### 4.2.3 Curing:

Curing is a carefully controlled process used to achieve the texture, colour and overall quality of a specific tobacco type. During the cure, leaf starch is converted into sugar, the green colour vanishes and the tobacco goes through colour changes from lemon to yellow to orange to brown like tree leaves in autumn. There are four main curing methods.

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<sup>22</sup> ([www.PTC.com.pk](http://www.PTC.com.pk), August 2005)

<sup>23</sup> ([www.PTC.com.pk](http://www.PTC.com.pk), August 2005)

### Air-Curing

Air cured tobacco, for example Burley, is hung in unheated, ventilated barns to dry naturally until the leaf reaches a light to medium brown colour. At this point, there are virtually no sugars left in the leaf.

### Flue-Curing

Heat is introduced into a barn via pipes from an exterior furnace like radiators connected to the central heating system. This controlled heat allows the leaves to turn yellow/orange, at which point they are fixed. These leaves now contain a high amount of sugar. Virginia tobacco is flue-cured.

### Sun-Curing

Leaves are strung out on racks and exposed to the sun. The whole process takes from 12 to 30 days. The sun's direct heat fixes the leaves at a yellow to orange colour with a high sugar content. Oriental is the most prominent among the sun cured tobaccos.

### Fire-Curing

Fire-curing follows the same principle as producing smoked meats. Brushwood is burnt under the tobacco leaves, which dries the tobacco and produces a smokey fragrance. This type is principally used in some pipe tobaccos.

After curing, the farmer grades the leaves into different leaf positions, qualities and colours and packs his grades into what is known as a farmer bale of 30-50kg. He then takes his bales to a buying centre for auction or sale.

## 4.2.4 Processing:

The cured leaf is then processed through a Green Leaf Threshing Plant. The main purpose of the processing is to:

- Remove sand, dust, scraps and foreign matter
- Separate the lamina from the stem (threshing)
- Drive down the tobacco to a safe 'keeping moisture' content.

Processed tobacco is packed into 200kg cardboard boxes for shipping to manufacturing sites. Pakistan Tobacco Company's Green Leaf threshing plant is located at Akora Khattak, NWFP.

#### 4.2.5 Trade Marketing and distribution:

The aim of TM&D is to build an excellent Trade Marketing & Distribution capability which bears the hallmark of a world class field force for effective retailer and consumer contact.

375 exclusive Distributors employing a contingent of over 1200 distribution representatives provide direct store delivery service of our finished products to the 400,000 plus retail stores throughout the country. In doing so TM&D aims to optimise the finished goods Supply Chain efficiencies in delivering products of consistent quality on-time, every time.

The retail universe is classified into Supermarkets, Groceries, Convenience stores and recreation or leisure outlets such as hotels, cafes and restaurants.

The company's Trade marketing field force provides value added services in complimenting the distribution effort, in select stores of the universe to enable mutually beneficial partnerships. it makes substantial investment in Retail, through quality in-store and on-store furniture and fittings to stock and display our products for the convenience of the consumers<sup>24</sup>

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<sup>24</sup> British American Tobacco website on production, From Seed to Smoke, available at: ([www.bat.com](http://www.bat.com))



### 4.3 FCTC -10 Key issues for global tobacco control and the FCTC

*The Framework Convention Alliance (FCA) is an alliance of over 160 non-governmental organisations from around the world that are working to support the development of a strong Framework Convention on Tobacco Control, and related protocols. A strong, credible FCTC will require proper funding, reporting, surveillance, research and co-ordination to form the foundations of the Treaty. The 10 commitments we believe demand the most urgent attention of delegates are the following:*

- 1. Advertising.** The FCTC should ban all forms of direct and indirect tobacco advertising, promotion, and sponsorship - but with accommodation for those parties where existing, genuine constitutional barriers prevent a complete ban. Each party would prohibit all forms of advertising unless it faced constitutional constraints, in which case it would restrict advertising as far as possible within the tested limits of its constitution.
- 2. Smuggling.** One in three internationally traded cigarettes enters the black market, and it is now essential to stop this by introducing effective security measures in the distribution system. Customs authorities must be able to trace the movement of tobacco products retrospectively to identify where diversion to the black market occurred. There are about 10,000 wholesale traders in the world, and these could be built into a licensed system in which they would record movements of tobacco products by scanning pack markings. Technology is available to do this at less than US\$0.02 per pack.
- 3. Pack markings.** Produce a clear pack-marking regime - the language is currently confusing. There are up to seven markings requirements to be specified in G1.
- Rotated health warnings (not merely a bland general warning) - these must cover at least 50% of the pack in line with world best practice.

- Use of pictures for at least some warnings to provide powerful visual communication of risk.
- Information on ingredients and/or smoke emissions, but only if these provide useful information about the product to consumers. There should be no requirement for listing of tar, nicotine etc. yields on packages (see 6).
- “For sale only in [market]” marking. This shortens the distribution chain and will help to tackle diversion to the black market.
- “Not for sale to under-18s” label. The FCA opposes this because it makes tobacco seem more adult - and hence more attractive to kids.
- Security markings required for tracing - essential for a meaningful counter-smuggling strategy.
- Plain packaging required for parts of package other than where mandatory messages appear.

For all markings, the FCTC should establish a framework of minimum standards for size, positioning, and, as appropriate, the use of pictures and rotation. National authorities should specify culturally relevant messages and content for warnings and consumer information, in local languages.

4. **Health before trade.** Change the guiding principles to give higher priority to human life than to commercial interests. The FCTC should be the prime treaty on tobacco and not be subject to challenge under the WTO agreements. The guiding principles must be changed to reflect FCTC supremacy in treaty conflicts relating to tobacco and to take a precautionary approach to evaluating measures intended to protect life. Nothing in the FCTC should prevent parties going further.
5. **Prohibit misleading claims and descriptors.** Ban clearly misleading brand names using words like ‘light’, ‘mild’, and ‘ultra low’ or similarly misleading expressions and symbols. These implied health claims have no scientific basis, and mislead consumers and confuse regulators. The FCTC should also ban any health claim on tobacco products unless approved by the authorities in the country where they are placed on the market.



- 6. Abandon the ISO methodology.** The system of measuring tar and nicotine ‘yields’ with a smoking machine does not give useful information about the impact of smoking on health. These machine readings are not, therefore, a useful basis for regulation or comparison of products. The ISO is dominated by the tobacco industry, and should have no more than a strictly subordinate role to the WHO, which must lead in the definition of standards for public health.
- 7. Increase taxes.** Tobacco taxes are effective in reducing demand and raising revenue. It will be impossible and undesirable to develop a common tax regime in the FCTC, but each party should commit to raise its tobacco taxes so that tobacco does not become more affordable. This means increasing tobacco taxes at least at the rate of growth of incomes - considerably ahead of inflation. Some fraction of tobacco tax revenue should be dedicated to funding tobacco control and cessation programs.
- 8. Close down duty free.** Duty free is an unjustified tax break to travellers, and opens a back door route to the black market by allowing retail access to tobacco products on which the full duties have not been paid.
- 9. The right to smoke-free life.** The FCTC should recognize the right not to breathe second-hand smoke - a toxic and carcinogenic pollutant. The aim of the FCTC must be to eliminate involuntary exposure to tobacco smoke. There is no need to specify vulnerable groups in the text: everyone deserves protection.
- 10. End all forms of subsidy to tobacco.** There is no justification for subsidizing any part of the production of tobacco. If there are social needs for subsidizing communities based on tobacco farming, any support should be for diversification, infrastructure development or activities that produce public goods.

## *Chapter 5*

### *Industry and environmental analysis*

## 5.1 Industry Structure:

### 5.1.1 Porter's Five Forces Analysis:

#### 5.1.1.1 The power of buyers:

Pakistan Tobacco Company is responsible for primary sales only, that is its first buyers are the distributors, who buy the cigarettes from PTC, the distributors are then responsible for the secondary sales that is selling to the retailers. Therefore by buyers we mean the distributors, with the responsibility of selling PTC's products. PTC has a total number of 334 distributors all over Pakistan, who are fairly scattered. Although the number of distributors is not that much as compared to the competition, the terms and conditions and the mode of business with PTC is so attractive and the profits margins and sales turnover are so lucrative that each and every distributor in Pakistan wants to be a distributor of PTC, therefore PTC enjoys a good power as compared to their buyers and buyer power is low.

#### 5.1.1.2 The Power of Suppliers:

The supplier for PTC are suppliers of leaf and wrapping material, which includes everything in the cigarette such as filter, paper, tipping paper, etc. leaf is grown by farmers who own their fields in NWFP province. As the same farmers sell leaf to all the companies, the competition to get the superior quality of leaf at a low price is very high in the buying season. Therefore the leaf suppliers have a fair deal of power and they enjoy and use it.

For other suppliers PTC is mostly importing from Japan, Korea and Europe, where they have their suppliers at the BAT level. Since all the OpCos are buying from the same suppliers, and the order quantities are huge, these suppliers can not afford to lose PTC and hence do not have a great power which they could use to their benefit. Therefore the power of supplier can be said as moderate, because of high power in the leaf area and low power in wrapping material and others.

Supplier power for the big brands like PTC and Lakson are low because both of them are mostly backward integrated, and whatever raw material they acquire, they have their own loyal

band of suppliers, the brand of the suppliers is not well known and popular as well, and they are content enough to be associated with PTC

#### **5.1.1.3 Threat of new entrants:**

Threats of new entrants in the high end of the market, or the high positioned brands, producing quality products is low, but a party or group who wants to set up a low investment small cigarette producing, there are possibilities to enter the market with comparatively lesser investment, there fore we can say that the threat of entry is moderate .Reasons for that are:

- **Economies of scale:**  
Manufacturers like PTC and Lakson have acquired and achieved economies of scale and production efficiencies, therefore the new entrants will also have to compete on the same level, which would mean higher costs and low chances of surviving for longer periods of time.
- **High capital intensive entry requirement:**  
For a company to come in the market and setting up a manufacturing plant at par with PTC is almost impossible by any normal vendor or manufacturer. Although some local companies have started producing using local machinery, but they can never meet the standards, quality and the volumes being produced by the two big companies.
- **Access to distribution channels:**  
The distribution efficiencies that PTC and Lakson have achieved are also a barrier to entry for a new entrant, because it would have to compete at the same level to formulate such a pervasive and penetrating distribution channel. It can start working and cater to a very small area, but to play at the same level and come closer to competing, it would have to spend the same amount of time and resources to get access to the distribution channels.
- **Expected retaliation:**  
Existing manufacturers can exert pressure on the government because they are one of the highest tax payers, additionally they can lower down their prices and create problems, for a

period of time, which might not matter much to them but for a new entrant that short period is crucial and decisive.

#### **5.1.1.4 The Threat of substitutes:**

Substitutes for cigarettes can be snuff, Hukka, pipe, bididi, or cigar. Although a smoker of a cigarette would not even settle for another brand other than his own, all these products can be substitutes because all have tobacco. As far as tobacco is concerned, research has showed that nicotine is addictive, therefore a person who starts smoking frequently will be addicted to it, so there can be no substitute for tobacco. Nicotine pills are available in the market for people who want to quit smoking but 90 percent of the smokers say that it doesn't give them the same boost and is not effective. Therefore the substitution for smoking a cigarette would be either quitting smoking altogether or nothing else, hence making the threat of substitutes is weak and not important.

#### **5.1.1.5 Competitive Rivalry:**

The competitive scenario in the Pakistan tobacco industry didn't use to be that tough even a decade ago, but it is very competitive these days, where PTC can never be complacent and just sit there. The constantly have to be on their toes, because Lakson is trying all it can to revive its dead brands and increase the sale of its milker brand Morven Gold. With Phillip Morris's entry in the market, PTC is constantly chalking out new plans to counter Marlboro if launched in Pakistan. The competitive scenario is tough and rivalry is high because although other brands are all in low and ultra low category, there are around 300 brands available in the market, and with such a wide choice for consumer, the company can't just relax. PTC refrains from all negative tactics such as negative competition and IMS compliance but all the other companies do not follow them very often. The illicit trade also takes the advantage away from PTC and hence disallows it a level playing field, increasing the competitive rivalry many times.

## **5.2 Environmental Analysis:**

### ***5.2.1 SWOT Analysis:***

#### *5.2.1.1 Strengths:*

##### **Experience in the industry:**

Pakistan Tobacco Company has been in the business for the last 58 years, infact since the inception of the new country, and has the privilege of being the first multinational investment of the country. Not only that the company has been in the same industry even before Pakistan was founded and has been in the subcontinent for over a hundred years, with the name of Imperial Tobacco and then British American Tobacco.

Its experience in the industry and the ups and downs that it has seen within it, has made it a force to reckon with, because nobody knows the tobacco industry better than PTC. Additionally it has helped it to develop long lasting and time tested relationships with its distributors and other stakeholders which are a source of strength for the company, and adds to its competitive advantage.

##### **Variety of Product Offerings/Brand Offerings:**

PTC offers a brand in every category of the market starting from the premium to the low and ultra low categories, and has a brand for the choice of every consumer, catering to a broad strata of socio economic population. The competition doesn't enjoy this kind of a diversity and lacks far behind PTC as far as quality brands in the premium and high segments of the smoker market is concerned.

Additionally this means that PTC has its risk diversified, because it is not depending solely upon one brand or couple of brands, which it relies upon to generate revenues and earn profits, instead it has a balanced mixed of brands in its portfolio so that the risk is diversified without exposure to it.

**International group:**

PTC is a subsidiary of BAT, the largest and the most international group in the world. It is said that one in every seven smokers in the world smokes BAT brands. Although PMI is said to be the largest company in the world due to its volumes, but if only the US is taken out of its share pie, it would not remain even in the top five. This magnitude and globalism gives PTC the competitive advantage that no other company has in this region. Wherever needed it can fall back on its parent group for advice, and resources. Besides global synergies are also achieved, and cross market data and information is shared across all the OpCos, giving it the power of information needed to make its decisions.

**Structure and Culture:**

PTC has a corporate culture which is second to none in many aspects. It wants itself to be the first choice for everyone, and that remains for the employees as well. It used to be a very beauraucratic company some 5 or 6 years ago, but that has changed dramatically and now the company is literally one with a very open minded culture and the open door policy, where innovation and creativity are encouraged. PTC takes strength from its four guiding principles which are:

- Freedom through responsibility
- Enterprising spirit
- Strength from diversity
- Open mindedness

PTC has been successful in creating and maintaining a quality human resource pool, and a system in place which results in a system, which can not be imitated by any other company, and unmatched strength.

Some other strength that PTC possesses are:

- PTC has a differentiated segmented market.
- PTC has competitive pricing and positioning.
- They have World Class accreditation such as MRP-II and ISO 9001.

### *5.2.1.2 Weaknesses:*

#### **Constrained in advertising and using media:**

Although the international marketing standards and the decision to go off air was PTC's own, and on which they must have a lot of debate, but whatever was the thought process and intention, it is a weakness which has left it handcuffed as it cannot advertise about anything in the electronic media, specially television and radio. Now even if it wants to publicize about its CSR initiative it cannot because of these restrictions.

#### **Distribution and reach in villages and far flung areas**

One of the weaknesses where the competition is doing good is the reach and marketing efforts in villages and far flung areas. Out of almost 47000 villages in Pakistan, PTC is only reaching around 14000, which is not a very high number. Lakson Tobacco Company's rural distribution is superior, the reason might be the profile of consumers they are targeting, yet PTC needs to improve its efforts in rural distribution to maximize its market share and earn more out of the untapped rural market.

### *5.2.1.3 Opportunities:*

#### **New product development:**

PTC is currently only into manufacturing and marketing cigarettes, and no other tobacco product like pipe tobacco or cigars. Although the market for these products is very small and it's a niche segment, but as the market is maturing, people would be requiring new products fairly soon. Additionally PTC is the only company in the premium segment and soon would have to be present in the market with these products, before PMI enters the market. It also has the opportunity to export these products in markets abroad, where they have significant markets.

#### **Rural Coverage:**

Although PTC has an efficient distribution system, yet it lacks in village sales both in retail sales or village direct distribution and wholesale. This is because there are a lot of villages and rural areas all over Pakistan where it is not feasible for it to set up distribution. In some cases PTC even pays VSA village sales allowance for the distributors to send their salesman to the



areas which are out of route just to have the presence of the brands there.

Improving the coverage in villages would not only improve the sales but also would make PTC more competitive with regards to Lakson's Morven Gold, which has excellent distribution in rural Sindh and Punjab.

#### **Innovative marketing strategies:**

With all the above the line marketing closed for tobacco companies, the need for innovative strategies for below the line is all the more. But with all the previous budgets that went in advertising, are now free to be used in below the line and other innovative ways of communication.

#### **Trade communications and relationships:**

PTC has the benefit of excellent relationships with its trade partners, but this is an area where nothing can be said enough. The trade partners include the distributors, contracts and retailers. After the self imposed restriction on advertising, PTC has further tried to strengthen its ties with its trade partners, by investing in them and having a line of communication through retail excellence programs and retail partnership programs, also they have incentive for top traders based on their targets.

#### **Corporate social responsibility Initiative:**

PTC is one of the very few companies in Pakistan who are pursuing corporate social responsibility very seriously, and don't just mean words from it, but the actions are very much evident. Its CSR initiatives of learning resource centers, afforestation, clean drinking water, and mobile dispensaries in rural areas are some of their actions that they have taken in this regard, yet it needs to put in more in order to be known as a truly vanguard company, which although is in a controversial industry, yet is doing business with responsibility and with full knowledge of the problems that prevail within the society, and using its resources to give back to the society and the stakeholders involved. This is a great opportunity which if fully exploited in its true letter and intent and with a true spirit would gain a very positive and a favorable influence of the general public and the society.

#### **Government relationship and lobbying**

#### *5.2.1.4 Threats:*

##### **Government regulations:**

PTC faces major threats from government regulations which can be imposed by the ministry of health. The Pakistani government has traditionally been very lenient with PTC and other tobacco groups, and didn't have any ideas as such to make laws which would make life tough for tobacco companies, but as the international scenario is getting tougher and tougher every day and the UN and WHO are pursuing anti smoking very seriously, the government has to comply and show to the international community that it is doing its best to reduce the harm caused by smoking. The ministry of health these days is the major source of concern for PTC and new regulations like no smoking in public places and transportation, health warning, and information are some of the regulations that have been imposed. Although these regulations are not that tough comparative to the other countries in the world, we can anticipate stricter ones to come in the near future.

##### **Anti Smoking Activists/NGOs:**

Anti smoking activist bodies and NGOs all over the world and in Pakistan as well are very active these days in persuading governments to increase regulations on the tobacco industry. These groups have a public support as well on the basis of which they exploit the government. These parties are also a threat to the business of PTC because they have been successful previously in creating public favorability, pressurizing governments and helping out people to litigate against the companies therefore it has to constantly formulate strategies to defend itself in the face of growing opposition towards the business it runs.

##### **Competitors:**

The local competitors such as Lakson Tobacco are a threat for PTC. Although all other players are very small in terms of value share and other resources, these can be a source of threat in the times to come. Lakosn tobacco company has been the volume leader for 8 consecutive years, but they could never be the value share holders, but this tells us that a local company can lead the market in terms of volume and can be a threat for PTC.

**Entry of PMI:**

Philip Morris, the world's largest tobacco company has acquired major share in LTC and although has not started working, it is being anticipated that they are watching the market closely and would come up big and dangerous anytime. Therefore PMI coupled with LTC, with the image that it has can be a serious threat, as it can damage the market share PTC enjoys.

**Illicit Trade:**

Illicit trade can be subdivided into three categories:

- Smuggling
- Counterfeit
- Tax evasion

A whole lot of smuggled cigarettes called the International Transit Brands are seeping in through different channels in the country. These smuggled brands are available in the premium, high and medium segments at almost the same price, posing a serious threat to the sales of PTC's premium brands like B&H and Gold Leaf, additionally brands like Pine and Business Class threat the growth of Capstan.

Some local manufacturers are also manufacturing counterfeit cigarettes and selling them in the market, causing a great threat to PTC, because not only people react and the company image is disturbed, the smoker retaliates and quits smoking the brand in dissatisfaction.

PTC is the highest tax payer in the country after the oil sector, but a great number of manufacturers selling low category cigarettes in the price category of under 10 rupees, are in the market who are evading taxes and transferring the price benefit to the consumer. This also makes PTC vulnerable because it pays almost 63 percent of its income as taxes to the government and competitive edge is lost when somebody else doesn't pay taxes in the same market.

## 5.2.2 PEST Analysis:

### 5.2.2.1 Political factors:

Tobacco industry in general and PTC in particular are subject to a great intensity of government regulations and interference. There are a lot of political stakeholders involved at all levels of the business. The Pakistan Tobacco Board controls the buying of tobacco by all companies and fixed quotas for the quantity that a company can buy, additionally it serves as a direct monitoring agency for tobacco growth, manufacturing and sales in Pakistan. The ministries of Health, Trade and commerce and the Central Board of Revenue are also major parties involved from the government side, all of whom play a major role in making the policies that affect the business of PTC and implementing them.

Tobacco industry is a highly taxed industry and the CBR in that aspect works very closely with it to see if all the policies and procedures are being followed. Similarly Ministry of Health also works as a watchdog to ensure that the sales of tobacco are directed to individuals who meet the criteria and all the regulations laid down by the WHO and the international standards are being followed.

The political and military governments have throughout history relied on PTC because it has been one of the highest revenue generators in the country. This also gives PTC some extent of power because they can use pressure to have policies chalked out which work to their advantage.

The NWFP government housing the tobacco growing areas has also had a role to play in getting jobs for people from the frontier province in the company.

### 5.2.2.2 Economic Factors:

The growth in the economy has been a great catalyst for the growth of sales for PTC in the past couple of years. The volumes for PTC have grown at a very rapid speed in the few years that have passed, and no obvious reason could be found out by the analysts as to what can be a

single factor which has fueled such a rapid growth. In the end it was found out that since the macro economic indicators have all been on a rise since 4 or 5 years, and the economy has shown growth which has trickled down to people in all segments and social classes, and their buying power and spending capacity has increased, which meant that not only their consumption of cigarettes has increased, they have switched their brands and have moved up in the brand categories.

PTC as already mentioned is one of the largest contributors towards the national economy, to an extent that when the government needs money for finalizing its budgets, it asks the company to submit their taxes in advance and get rebate, because of the sheer magnitude of the revenues paid. The approximate taxes that PTC pays to the government are Rs.6 Crore every working day.

### **5.2.2.3 Social Factors:**

As with any other consumer product, the social factors in the society and the country play a major role in deciding the consumption of that good. As with the tobacco industry, everybody knows that it is a controversial industry, with the high health risks that it poses to the people who consume it. This makes it a product which is socially not likeable by the masses and majority of the people don't like to be associated with smoke and smokers because of health risks that it poses. In a society like ours this becomes all the more negative because it is embedded in training from our elders from childhood not to smoke and people do it without the consent and willingness of their family members or parents. On the other hand there are a lot of individuals who smoke, just to be known as socially advanced people, and because people in their circle do so. With the high social disowning that it has, it is a fact that people start smoking because of peer pressure or to conform to or look like someone they know or they like, or just because everybody around them is, so if there is no social life or if a person doesn't have a social circle who smoke, his chances of starting smoking are very low.

Where there are factors that socially restrict or discourage people to start or continue smoking, there are also factors which encourage people to start smoking or continue doing it because of their social life. People want to be seen as modern and trendy and think that smoking gives them a macho image, which is partly due to the advertisements that have been aired by companies. People who have a social life and a lot of other people in their social circle smoke

to socialize and be known as someone who conforms to group norms. Therefore the decision to smoke or not to smoke both are heavily dependant upon ones social circumstances, and it can largely influence a decision in this aspect, based on the significance it has in that person's individual life.

#### **5.2.2.4 Technological Factors:**

The advancement in technology has enabled tobacco companies to speed up their processes and achieve efficiencies that help them produce more and more in the same time. Technology basically helps companies like PTC to increase their production capacities and produce effectively and efficiently. PTC is constantly upgrading its production technology and has recently acquired top of the line machinery for stick manufacture and packing which can produce 6000 sticks in a minute and can pack 500 boxes in a minute.

Investment in information systems has also given PTC the much needed competitive advantage, because with the state of the art information system at their fingertips they can makes decisions in real time based on information from all markets, which would otherwise taken days.

The information systems being used in PTC are SAP, SIS, RCS-6 etc. PTC also helps their distributors set up information systems to help them speed up the whole distribution process.

# *Chapter 6*

## Analysis

## **6.1 DISTRIBUTION CHANNEL & THIER RELATIVE IMPORTANCE:**

### **6.1.1 CHANNEL:**

PTC has its production facility at two different points. One is in JEHLUM and the other is in Akhora Khattok. The stocks are delivered to company warehouses at 14 different locations. These warehouses serve 18 different areas all over Pakistan. PTC has different distributors in these areas. One area is served by more then one distributor. For example to serve the area of Lahore, PTC has 3 distributors namely; Allied Marketing, Shahbaz Brother Limited and SM Riaz Brothers. These distributors are served by the warehouse in their relevant area. In some cases an area is directly served by factory. For example for the area of Lahore, Jehlum factory directly dispatches stocks. In some cases one warehouse is serving more than one area. For example, the ware house in Faisalabad is serving Faisalabad as well as the area of Jhung and the areas of Rawalpindi and Islamabad are also served by one warehouse. Every distributor has its unique territory in a particular area in which it serves the market through

1. Wholesale (buy product from distributor, bulk buyer, sells product to retailer)
2. Retail (buy product from distributor / wholesaler, sells product to consumer)
3. Shop Selling (the distributor sales at its own door step)

**6.1.2 PRIMARY SALES:** “The total stocks dispatched from warehouse or directly from the factory to a particular area are known as PRIMARY SALES of that area”. The primary sales can be calculated by the monthly dispatches to an area.

**6.1.3 SECONDARY SALES:** “The total stock sold by the distributors of an area to retail and wholesale market is known as SECONDARY SALES”. Secondary sales are given by distributor of an area. It can be calculated by a simple equation

$$\text{SEC SALES} = \text{Opening stock} + \text{Monthly Purchase} - \text{Closing Stock} \pm \text{Claim Adjustment}$$

**6.1.4 CONSUMER OFF-TAKE:** “The consumer off-take is the sales being done by retailer to end consumer” the consumer off-take is being calculated by AC Neilson by surveyors. AC



Neilson conducts **Retail Audit** on monthly basis and submits report to regional offices and head office on monthly basis.

#### **6.1.5 RELETIVE IMPORTANCE OF DIIFERENT CHANNELS:**

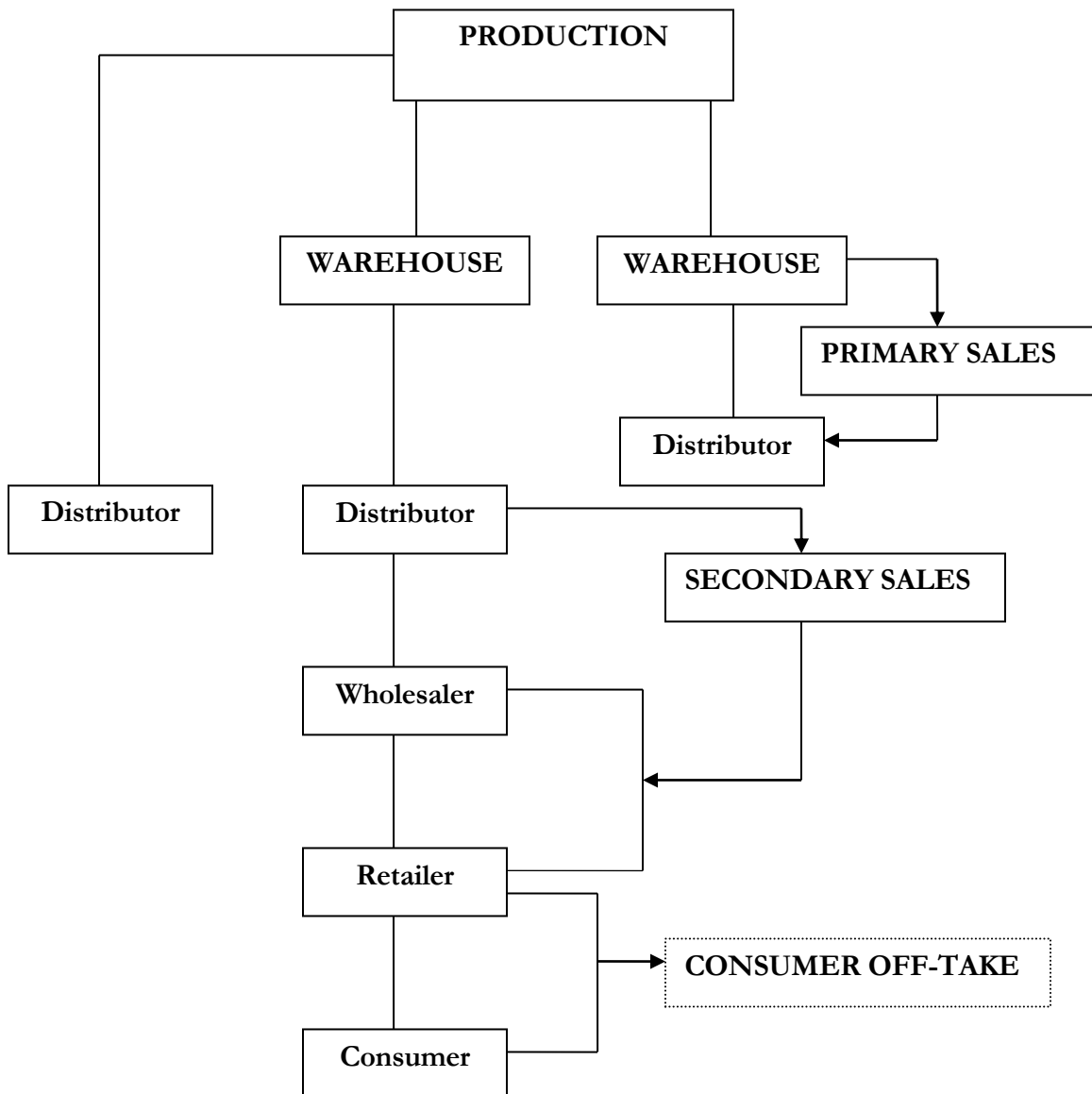
##### **Whole sale:**

- Drives volume
- Bulk purchaser
- Passive distribution channel

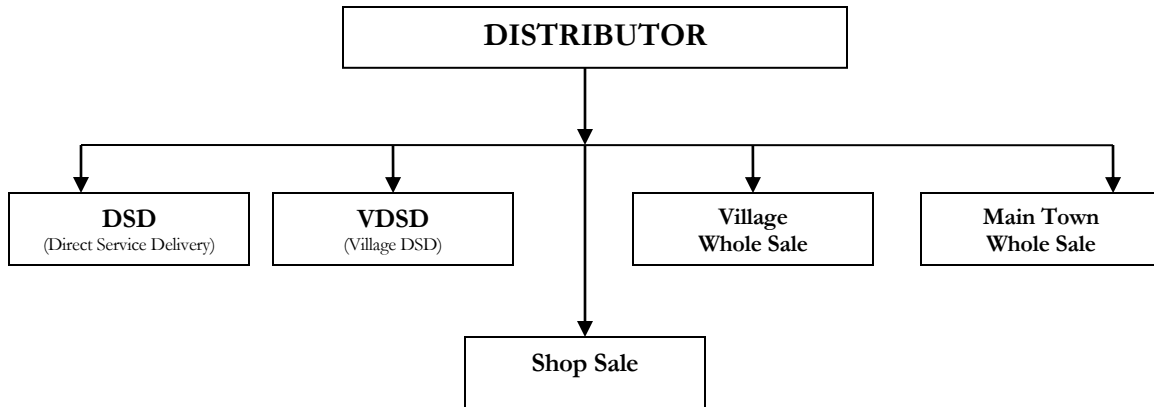
##### **Retail:**

- 100% Supply chain control
- consumer touch point

## 6.2 DISTRIBUTION CHANNELS



## DISTRIBUTOR'S CHANNEL



**6.2.1 IDEAL EQUATION FOR DISTRIBUTION CHANNEL:** Different channels have several relative advantages. Some areas are not feasible for retail distribution and in those particular areas, wholesaler plays important role. But in main town company always discourages sales through wholesaler. The ideal equation for a company's sales is:

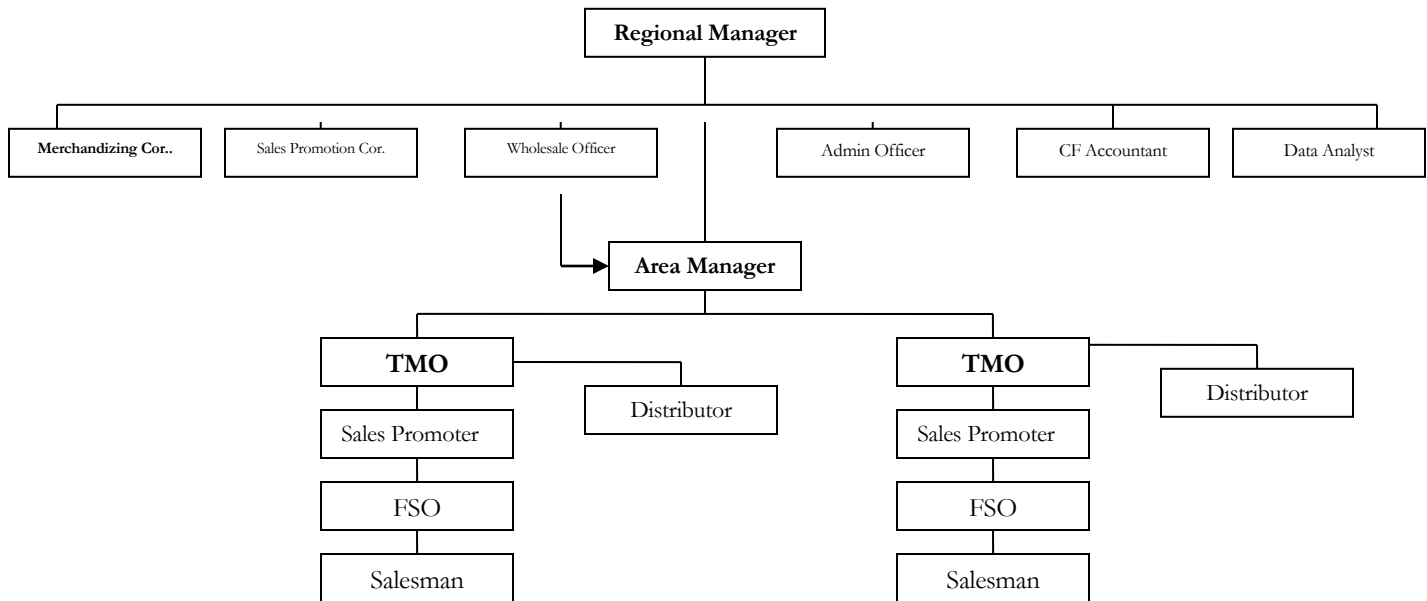
$$\text{TOTAL SALES} = 30\% \text{ WHOLESAL}E + 70\% \text{ RETAIL}$$

It is acceptable if the 60% of the company's sales derives from wholesale. Currently 50% of the PTC sales of Lahore derive from wholesale and 50% from retail sales. It also depends upon the area geographic and infrastructure. For example 70% of the total sales of Karachi derive from wholesale.

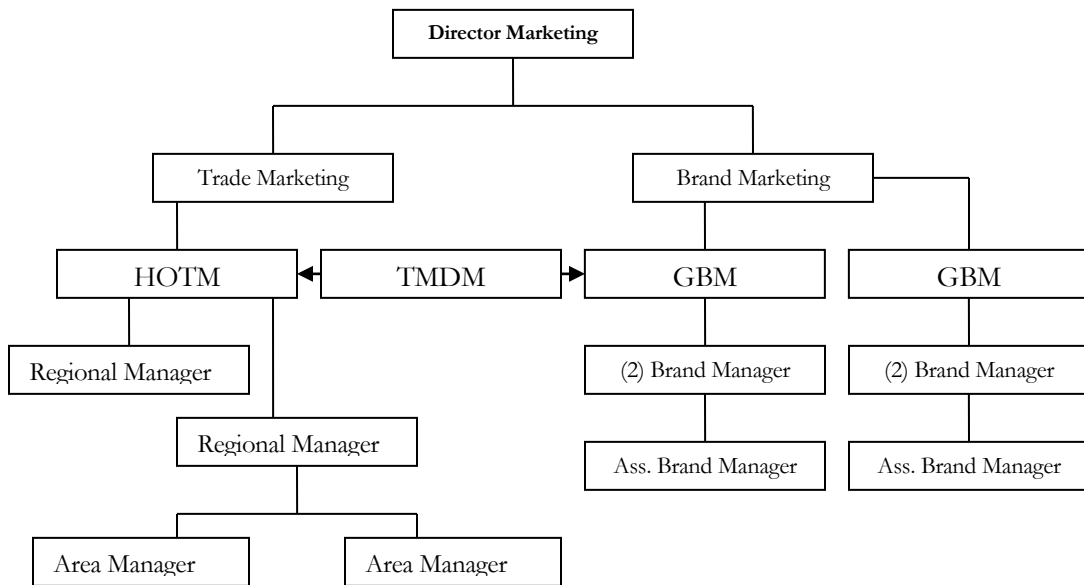
### 6.2.3 TRADE MARKETING AND DISTRIBUTION ORGANIZATIONAL STRUCTURE OF PTC

**Regional Office Structure:** PTC has five regional offices in Pakistan headed by 5 regional managers. There are 18 Area Managers working in Pakistan for different areas. The regional office structure is as follows:

## REGIONAL OFFICE STRUCTURE



## MARKETING DEPARTMENT STRUCTURE



Currently the area office Lahore is handling 7 distributors. Out of 7 distributors 3 are serving Lahore market. There are total 8 TMOs working in that region. 3 of them are under the process of training. There are also 26 SPs and 110 salesmen serving this area.

**6.2.4 SALES PROMOTER:** sales promoter are the trade marketing staff who are working directly with the front line sales team. Their core responsibilities includes

- Merchandizing
- Availability
- Market intelligence
- Consumer contacts
- Supervision of sales team
- Sales promotion communication
- Competitors brand analysis & sales comparison
- Direct sales
- D&D collection from the market

The SPs who cover main town have company owned motorbike and all the VSP (Village Sales Promoters) have company owned car (Bolan). On an average every SP cover 50 shops per day which is called “*Load Factor*” and he also contact 10 consumers as well. Every SP has different BEATS. The frequency of each BEAT is twice or thrice per week it means that every shop in an area is covered twice or thrice a week. Every VSP (Village Sales Promoter) cover 4-5 villages per day and contact 50-60 retail outlets. Every VSP is supervising almost 40-45 villages and has 10-12 different beats. SP covers only those shops which drive the 80% of total sales volume. VSPs work 24 days consistently and then take 4 days of at the end of each month. The first 2 days of every month are for office work.

**SP Importance:** SP playing an important role in the success of PTC. SPs are the front line team of PTC as they are directly dealing with the retailers, wholesalers and consumers. The SP team of PTC is experienced, trained and groomed so that they can perform tier duties more efficiently. PTC frequently arranges different training programs for SP’s. SP’s are the communication source between PTC and market. Most of the market decisions rely on their feedback taken frequently from the market.

### 6.3 Critical Success Factors

In our company there are six key areas - called Critical Success Factors (CSFs) - within the Trade Marketing and Distribution function in which Best Practice must be achieved to enable end markets to meet the TM&D Mission.

The CSFs are:

Strategy and Planning

Supply Chain Management

Resource Management

POP (Retail Marketing) Management

Account Management

Information Management

To effectively manage these CSFs we have also identified the following 21 activities:

CSF's help to develop and drive annual/other periodic strategies and plans for all Trade Marketing and Distribution activities within a specific country, channel or territory. All aspects must be cascaded down through the overall Trade Marketing and Distribution organisation to provide consistent and impactful direction for the activities of all Trade Marketing and Distribution personnel.

Strategy & Planning

TM&D Planning

A concise statement of key strategies and implementation plans for TM&D activities within each country. The plan must clearly identify priority brands, channels, territories, retailers and how these priorities will be supported through promotion, merchandising, availability and trade programs. These priorities will be communicated to every level of the TM&D organisation.

### Cycle Planning and Sales Operational Planning

A cycle plan is an operational execution plan specifying in detail the objectives, focus and timing of brand-driven TM&D activities in each channel/territory/account across a rolling 18 month time frame.

Sales Operations Planning (SOP) meetings take place each month, and they give the end market an opportunity to assess current vs planned performance, take corrective action as necessary and deliver more accurate and balanced plans for the remainder of the plan period.

### Coverage Planning

Trade Coverage planning is to decide which outlets need to be visited, who should call on them and how often these outlets should be visited.

### Supply Chain Management

The management of the Supply Chain and through this the management of the product flow, (replenishment quantities and inventories of product) throughout the entire chain from the factory to the consumer. This is achieved by building efficient partnerships (including 3rd parties, such as suppliers, distributors, wholesalers and retailers) with the ultimate aim of quality, availability and inventory management at the optimum unit cost for the entire supply chain.

### Supply Chain Strategy and Management

The efficient and cost effective design and management of the product, information and cash flows in the entire Supply chain in co-operation with our partners to achieve the sustained competitive edge.

### Order Management

Order Management is the procuring, communicating, and tracking of replenishment requirements in a timely and accurate manner using the most efficient and cost effective methods.

### Order Fulfillment

The process of filling product demands throughout the supply chain to ensure fresh product is always available at the targeted point of purchase by optimising product handling and minimising damages and costs.

### Trading Terms

Accurate, efficient and consistent application of trading term policies, procedures and conditions to maximise cash flow and minimise debt exposure and cost. These include invoicing, payment process, and quantity allocation, along with delivery and/or payment adjustments.

### Inventory Management

Monitoring and management of stocks throughout the supply chain in order to ensure availability, quality and freshness of our brands at the targeted outlets, while minimising working capital and maximising efficiency and cost effectiveness.

### Resource Management

The effective management of financial, human and other resources to ensure that the TM&D organisation and capabilities reflect the needs of the changing trade environment and ensuring that its objectives are met.

### Financial Planning and Management

Creation and management of a consistent financial investment plan compatible with the TM&D strategy and financial goals of the company.



### Manpower Planning

Provide a manpower plan that defines the level of manpower required to fulfil the sales plan, and to provide a pool for the long-term development of the company. This will include budget, manpower planning, basic deployment strategies, career and succession plans.

### Organization Development

The organisation structure and development plan to support the implementation of Best Practices. It also covers the design, planning and delivery of training programs aimed at developing and maintaining our people at the highest level of skills and capabilities required for our business goals.

### POP Management (Retail Marketing) Management

POP management is a strategic process for satisfying the in-store needs and wants of today's demanding consumer and the in-store business requirements of the trade. It involves providing marketing support activities on a planned basis within the store to generate consumer loyalty, attention and purchase (and is subject to IMS and local market legislation).

Implementation of in-store consumer focused activities in order to drive performance of BAT brands at the point of retail and to create opportunities to expose our target consumers to the brand world.

### Product Availability

To ensure presence of the optimal product range

- At any time the consumer wants.
- In sufficient quantity.
- At a price in line with the company pricing policy.
- With the right quality.

- To ensure the visibility of the product range to the consumer through Best Practice display methods (e.g. eye level) and standard planograms.

#### Trade Marketing in-store communication and promotions

To implement tailored in-store communications and promotions aimed at improving consumer off-take (stimulating trial, impulse sales) and reinforcing brand image, positioning, and awareness through:

Semi-permanent and permanent POS materials.

Cycle based in-store trade and consumer promotions that leverage sales or a defined marketing objective to the target consumer.

Sampling activities.

Tailored planograms i.e. planograms adapted to individual retailers' needs.

All these activities are subject to local and legal permissibility.

#### Retail Media (\*) in-store communication and activities

To implement in-store communications and activities aiming at building the brand world by using retail media that have the ability to change our target consumers' perception of our strategic brands via:

Retail Media in-store marketing solutions, such as

Tailored brand image communications.

Activities that improve consumers' shopping experience ("Retailtainment").

#### Tailored events

- Exclusive events/consumer programs.
- Brand switching activities
- Through retailer (Trade Ambassadorship).
- Direct Marketing.
- Consumer Networking.

- Exclusive Trade Support Programs.
- Retail Investments.
- Retail Training Programs.

It also includes the controlled distribution i.e. displaying products with the objective of communicating the brand image.

#### Account Management

The management of all retail, wholesale and Horeca chains to achieve effective implementation of our TM&D activities.

#### Account Planning

Creating a periodic plan for a specific account which details trading terms, investment in and timing of TM&D activities and contacts, brand focus and service levels. It will establish clear account objectives in terms of volume, profit, availability, product range and market share. If completed in conjunction with the account, a business plan can create a strong bond, which drives towards a 'partnership' vs 'adversarial' approach.

#### Account Profitability

Understanding the profitability of an account in terms of both:

BAT profit from the account.

Account's profit from BAT products.

A good understanding of the financial implications of the category leads to better quality business recommendations and decisions, and can improve the overall focus on the tobacco category in store.

### Category Management

In our strategic customers we may wish to become the Category Captain. This involves managing the whole category on behalf of the retailer and is designed to grow the category by delivering a win-win-win result - a win for the consumer, the retailer and BAT.

### Business Development

Identifying and entering new retailers and channels based on a clear understanding of long-term market trends, and with the potential for a positive return on investment.

### Information Management

The gathering and analysing of data and distribution of relevant information, in a timely and consistent manner in a format which supports better and faster decision making.

### Market Intelligence

Carrying out trade and consumer research on trade structure, consumer behaviour, competitor performance and long term channel trends. It includes Retail Audit, Customer Satisfaction Measurement, competitor analysis, and consumer awareness measurement e.g. General Consumer Survey (GCS).

### Internal Monitoring

Monitoring and the measurement of financial, sales and human resources performance. It includes TM&D financial performance, Dashboards, Sales Effectiveness and Employee Satisfaction.

### Information Technology

Developing tools to enable the appropriate gathering, analysis, communication and distribution of all relevant information in a flexible manner

## 6.4 Classification of Cigarettes & their Strategies:

### *6.4.1 Premium Category:*

Pakistan became the first market in the BAT group to launch the 'Gold Standard' pack, which not only appeals to consumer aesthetics but also served to distinguish the brand from illicit versions available in the market. This is high quality brand that was launched to cut down the illicit versions available in the market and to give consumers a choice with the freshest quality and great blend. This brand is produced by best available tobacco for upper class of the society. This brand prices above Rs.40 and till Rs.75 and is a premium brand e.g. Benson & Hedges & Benson & Hedges Lights. Therefore the strategy used for this brand is "Focus Differentiation".

### *6.4.2 High Category:*

John Player Gold Leaf is considered to be the high quality benchmark of PTC. This brand prices between Rs.30 to Rs.40 is high category brand. Therefore the strategy used for this brand is "Differentiation". This is a flagship brand of PTC, which has been giving the company greater and greater heights and unprecedented profits year after year. The margin on this brand for the retailer is not very high, but its tremendous sales and quick turnover makes it a very fast consuming and a favorite brands for retailers all over Pakistan. The brand Gold Leaf has gained and acquired a brand muscle and equity which makes it a household name for every person in Pakistan, whether smoker or not.

### *6.4.3 Medium Category:*

The brands in this category belong to the medium segment. The brands are concentrated in specific pockets. These brands price between Rs. 20 to Rs. 30 e.g. Capstan, Wills. Tobacco of these cigarettes is a little hard. Therefore the strategy used for this brand is some where between "Low Cost Leadership & Differentiation". Basically Capstan is there to provide a

choice to the smoker who doesn't want to consume a low image cheap cigarette and also cannot afford a high priced cigarette like Gold Leaf or Benson, so this brand gives him a value for money, and good quality and blend at a reasonable price and image.

#### ***6.4.4 Low Medium Category:***

Gold Flake is PTC's drive brand in the low category by virtue of opt singular potential for growth in a market where 80% of the business resides at and below Gold Flake's price point. This brand prices between Rs. 15 to Rs. 20 and is of low medium category. Therefore the strategy used for this brand is "Low Cost Leadership". This brand is competing Lakson's Morven Gold , which is the highest selling brand in the market.

#### ***6.4.5 Low Category:***

Embassy, amid stiff competition form ultra- low category brands, maintained its position as the third largest volume brand in Pakistan. This brand prices below Rs 15 and is low category. These cigarettes are for lower income groups and tobacco of these cigarettes is very hard. Therefore the strategy used for this brand is "Low Cost Leadership".

### **6.5 Core Competences:**

The core competence of PTC is the Production of premium quality cigarettes, and to have the right people in the right working environment.

#### **6.5.1 Innovation:**

In the wake of the new millennium, Pakistan Tobacco Company is constantly changing and reinventing itself so as to keep ahead of the rapidly changing environment of the commercial world. The employees are encouraged to have an out of the box thinking. Therefore, it is following the prospector strategy.

#### **6.5.2 Business Partners:**

Pakistan Tobacco Company has a large number of business partners. Furthermore PTC equips these business partners with skills and expertise, which they use, for developing their own business as well. Their partners are:

- **Farmers:-** the farmers receive free seeds from PTC as well as free advice on planting, growing and harvesting.
- **Distributors:-** they are fully integrated into PTC's business, continuously improving on performance standards.
- **Local Suppliers:-** they benefit from skill transfer of modern, cost effective working practices, resulting in increased velocity and efficiency of their own internal process.

### **6.5.3 Virtual Organization:**

In the field of information technology (IT), Pakistan Tobacco Company has taken a leading role placing IT at the core of their business strategy has allowed them to harness the power of leading edge technology solutions to create a “Virtual Organization” across the length and breadth of Pakistan. Using one of the largest data networks in Pakistan, staff located throughout the country has access to all our key information sources and state of the art business systems to make rapid and accurate decisions.

### **6.6 Strategies to Enlarge Organizational Domain:**

At different point of time PTC uses different strategies according to the need or requirement.

**1- Market Penetration:** PTC is constantly pursuing this strategy to increase its share of the resources in its existing domain. It is doing this by advertising and marketing. The complete detail of this is given in the market strategies, which will be described shortly.

**2- Product Development:** To protect and enlarge its existing domain PTC constantly comes up with new and improved along with their new one. For example it recently came up with capstan for the medium class who like style. Benson & Hedges Lights for the upper class, who require some thing less intense.

**3- Market Development Strategy:** PTC has decided to take its products to new domains of the country. For example Mardan and all the other tribal areas of NWFP, were not in the market before.

## Logistics and Area Offices:



Under the department of LEAF, the company has :



## Marketing Strategies

PTC has divided its Brand portfolios into four types:

- Premium
- High
- Medium
- Low-segment

**Premium** brand consists of Benson & Hedges (B&H) and high has John Player Gold Leaf (JPGL)

**Medium category** brands consists of Capstan

**Low-Segment** includes Wills, Embassy and Gold Flake



## *BRAND PORTFOLIO STRATEGY*

PTC has a Brand portfolio strategy, which states “if a tobacco consumer switches from a high quality/high priced tobacco product to a more in-expensive one, they should switch to the tobacco products offered by PTC in that category”

### **Marketing by Brand Portfolio:**

Marketing campaigns are based on brand portfolios, meaning that advertisement for every product is designed keeping in view, the target market/consumer. Keeping this in mind the promotional strategies for Premium brands like B&H are created keeping in mind the elite group of tobacco consumers. Promotional strategies in Pakistan are strongly based on price as opposed to the product features or taste.

The category that comprise of brands like Capstan, Gold flake and embassy, frequently offer promotional campaign like free key chains, gifts and lottery schemes.

### **Situation of two brands of PTC and their strategies in the market:**

#### **Benson & Hedges:**

##### ***2000 & BEYOND***

A premier brand. A premium image. A feeling of “impassioned spirit”.

Benson & Hedges continues to be the No. 1 choice among international brands.

To support the brand’s cosmopolitan image, Above-The-Line communication continued to express the distinctive “impassioned spirit” campaign in Print and Television. Sponsored Television programs such as “*Movie Nite*” and “*Global Beat*” also played an important role in enhancing brand image early on, but after the implementation of IMS, the below the line activities are targeted towards upward and trendy, ASU 30 smokers through activities such as

concerts, musical nights, parties at HoReCas and key accounts. A database of around 3000 smokers who have willingly shared their information and want to be contacted is maintained and used from time to time for promotional activities.

#### HUSTLE & BUSTLE

From 2000 onwards, building brand relevance through direct contact activities remained a cornerstone of our Below-The-Line program. Sponsored music programs were held on special occasions, while on the merchandizing front, innovative retail media concepts were introduced in new environments. Brand presence was enhanced through outdoor merchandizing executions. The coming months will witness a flurry of new exciting activities that will firmly establish Benson & Hedges as the brand of choice for premium smokers.

#### CAPSTAN:

##### ***Men Still Demand CAPSTAN the World Over***

Year 2000 was a defining year for Capstan early in the year, PTC made the decision to position *CAPSTAN as our main Medium category offer. Following a price repositioning from Rs.24 to Rs.20 to bring the brand into the Medium category, support was also revived after over a decade. The brand responded strongly, with monthly sales at year-end over four times previous levels and vying for leadership of the category.*

##### Price Repositioning

Full support was extended to Capstan through innovative use of TV, Radio, Print and Point of Purchase materials to create awareness for the new price. It was ensured that the price is communicated effectively without compromising the high image profile of the brand.

##### Thematic Campaign

A new advertising campaign featuring a new generation of the “Capstan Man” was launched in October 2000 with the famous copy line of “Men Demand Capstan the World Over”. This

has been a driving force in establishing the brand as a true image leader in the Medium Segment. Hence, despite price cuts of key competitive brand, Capstan has continued to grow significantly and improve its profit margins.

#### Sponsorships

A number of events and exhibitions were sponsored by Capstan. This was part of On-ground initiatives to generate awareness and trial for the brand. “Capstan and Shandur” was the leading event that caught everyone’s attention. Moreover, various sponsorship and stall activities were conducted in Karachi and Lahore.

#### The Years Ahead

In the year 2001, we intend similar and continuous support to the brand and emphasis to consumers the high quality and image of capstan to drive leadership in the Medium Segment.

#### GOLD FLAKE:

### **SUCCESS STORY**

#### Record-Breaking Of GOLD FLAKE

Following its price repositioning from the Medium Category to the Low Category (Rs.18.04 to Rs.9.55), the dramatic success of Gold Flake energized the system, arresting the alarming trend of volume decline in 2<sup>nd</sup> half of 1999. PTC were quick to seize the opportunity, reviving brand support after a gap of five years, and continuing to grow volume despite major competitive brand *MORVEN GOLD* responding similarly with a similar reduction. The repositioning followed by sustained activity behind the brand resulted in volume growth of +700% in 2000 vs. 1999 alone. The brand now occupies an important position in our portfolio addressing a strategic vital consumer franchise.

#### BIG Volume Drivers

The introduction of pack variants – Gold Flake 20s Hinge Lid Pack and Gold Flake 50s Hinge Lid Pack – contributed to the increase in volumes and helped to improve brand image. Whereas the Gold Flake Soft Cup is a high seller in rural areas of Punjab and Sindh.

Gold Flake was brought down from Medium category brand to low-segment brand with a major price repositioning from Rs.20 to Rs.10. The marketing strategy was to double the sales by decreasing price by half. The brand sold less than 1 billion cigarettes in 1999, but only in the short time span of 15 months, sales have grown to 6.7 billion in 2000, hence increasing sales more than 6 fold.

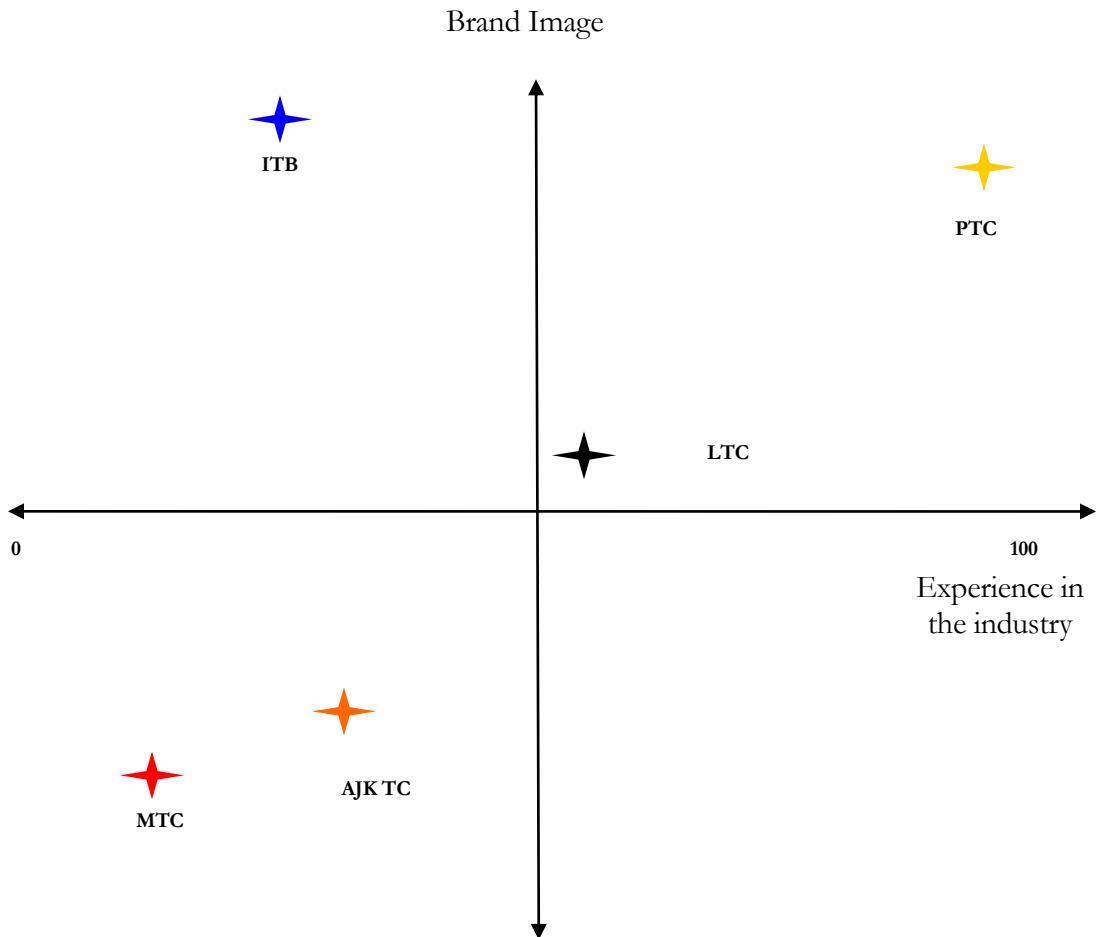
## 6.7 Positioning Analysis

Dimensions for Perceptual Map Analysis:

The following attributes have been taken to analyze the market position of PTC with respect to its competitors and to judge the perception in the minds of the consumers.

- Brand image
- Experience in the industry
  
- Marketing activities
- Recognition (Pakistani Market)
  
- Availability (Pakistani Market)
- Distribution and coverage
  
- Price
- Variety
  
- Quality
- New product development/launch

6.7.1 Perceptual Map Analysis No.1:  
Brand Image vs. Industry experience

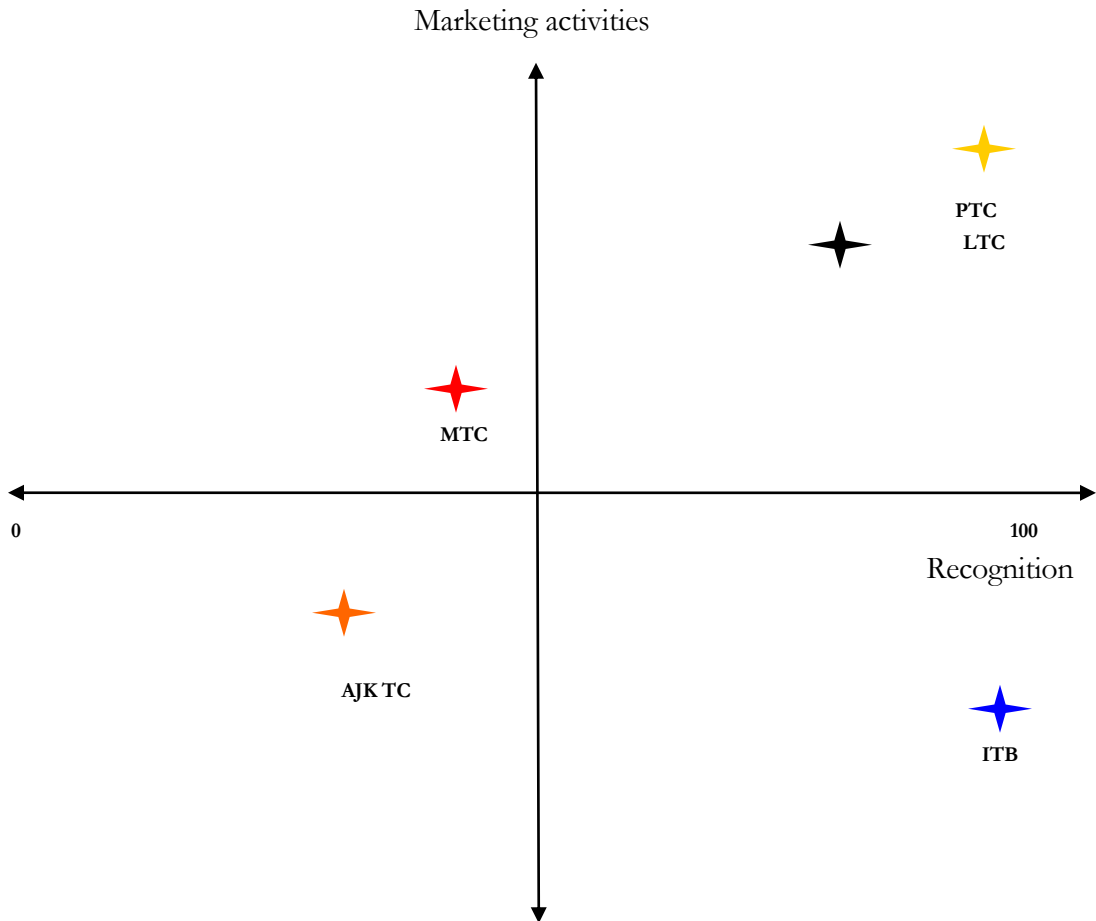


Analysis:

This perceptual map takes two attributes of Brand Image and Industry experience and plots 5 major companies on the map. PTC ranks on top as far as experience in the industry is concerned but the ITBs or the international transit brands top the image because foreign items are perceived as having better quality and image otherwise as far as experience in the market is concerned it's a new phenomena.

Lakson products are not perceived as having good quality because they don't have any product offering in the high or premium category, and also lacks behind PTC in industry experience.

6.7.2 Perceptual Map Analysis No.2:  
Marketing Activities vs Brand Recognition

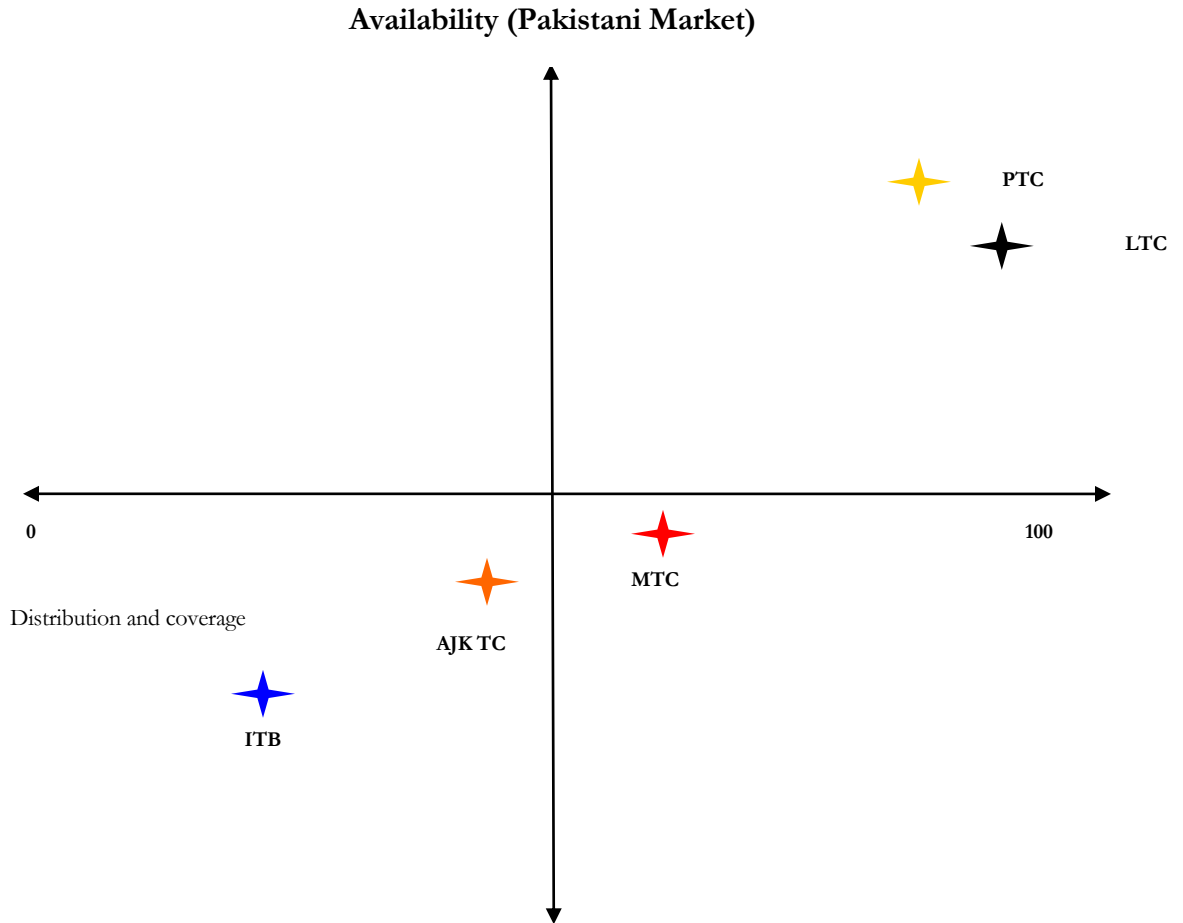




In the second perceptual map we analyze the attributes of marketing activities and brand recognition. PTC is ahead of all other brands in both these dimensions, because of the quality of marketing activities. But LTC doesn't lag behind by a great margin and is gaining recognition as well as increased marketing activities, imitating PTC. The ITBs are recognized equal to PTC's brands as they are mega international brands with great prestige associated to them like Marlboro and Dunhill. The Mardanwala brands are better in their marketing activities and brands like Melburn are recognized in the market in Punjab. Gold Street by AJK Tobacco Company has been doing reasonably well, but they lack the recognition as well as marketing intensity that is required.

### 6.7.3 Perceptual Map 3

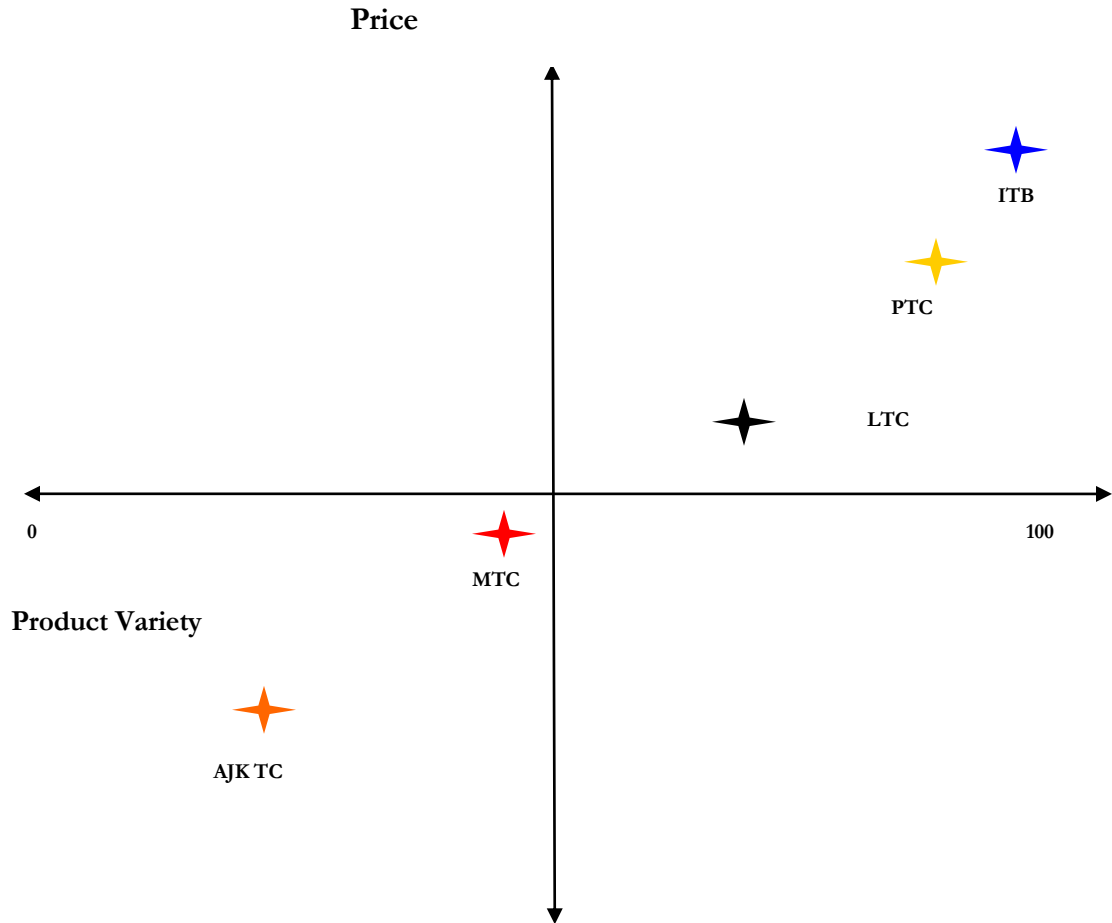
Availability Vs Distribution and Coverage



Analysis:

The third perceptual map analyzes the companies on the dimensions of availability and distribution coverage. Here Lakson is ahead of PTC as far as distribution coverage is concerned because they have presence in more rural areas and villages than PTC, but wherever cigarettes are available PTC is there, although they might not be supplying themselves but Out of stock position would be lower if PTC brands are available and the availability would be better than LTC, but Lakson does well as far as distribution is concerned due to their strong rural coverage. Mardanwala has got a fairly well developed distribution network and is managing good supply to its retailers both in urban and rural although not as elaborate as PTC and LTC.

6.7.4 Perceptual Map 4  
Price Vs Product Variety



### Analysis:

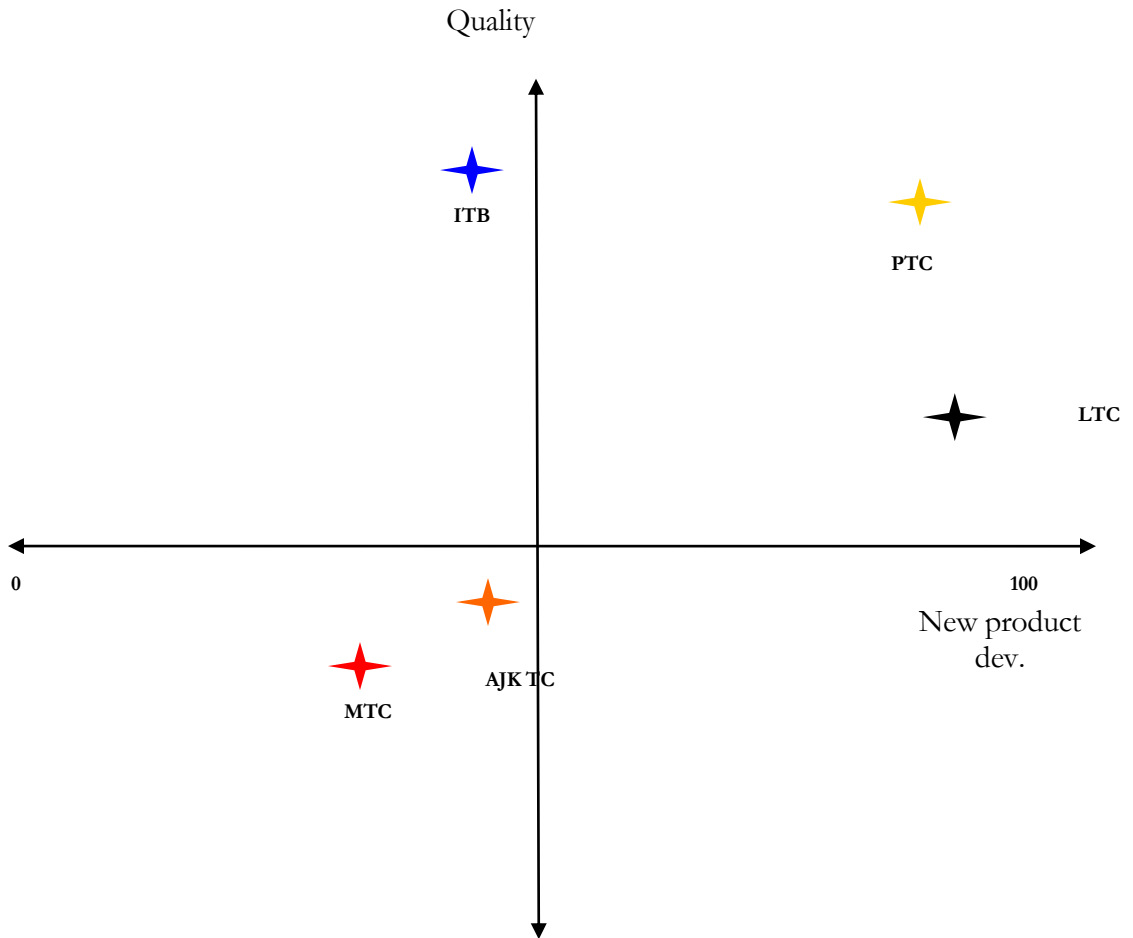
This perceptual map analyzes the companies on the dimensions of price and product variety. The ITBs have the highest prices and almost all of them are in the premium segment, with the highest variety in brands, from premium to medium. This can be understood by the example that only the smuggled Dunhill has around 10 varieties available in market of Karachi, followed by PTC and LTC in the high price ranges. The mardanwalas and the AJK tobacco are both in the low and ultra low category.

As far as the product variety is concerned PTC is ahead of LTC because it is offering a cigarette in every price range starting from Premium to ultra low, whereas LTC starts from medium low and down.

6.7.5 Perceptual Map Analysis No.5:

Quality

New Product development/Launch



## 6.8 BRAND PERSONALITY DIMENSION INDEX

Brand personality dimension index quantitatively analyses the personality of a brand on five major product attributes; *sincerity, excitement, competence, sophistication and ruggedness*. Each attribute is further defined by various sub-attributes that describes which attribute is the best. The weights are based on industrial level; how it contributes to the overall personality of any brand within that industry. Scale is based particularly on the brand, whose index we are trying to find out. We have calculated the personality dimension index of Pakistan Tobacco Company as a corporate brand.



SINCERITY	WEIGHT	SCALE (1-5)	
Down-to-earth	0.250	3	0.750
Honest	0.350	5	1.750
Wholesome	0.10	2	0.200
Cheerful	0.30	4	1.200
<b>Total</b>	<b>1.0</b>		<b>3.800</b>

EXCITEMENT	WEIGHT	SCALE (1-5)	
Daring	0.250	5	1.25
Spirited	0.250	4	1
Imaginative	0.150	4	0.6
Up-to-Date	0.350	4	1.4
<b>Total</b>	<b>1.0</b>		<b>4.25</b>

<b>COMPETENCE</b>	<b>WEIGHT</b>	<b>SCALE (1-5)</b>	
Reliable	0.350	5	1.750
Intelligent	0.300	4	1.200
Successful	0.350	4	1.400
<b>Total</b>	<b>1.0</b>		<b>4.35</b>

<b>SOPHISTICATION</b>	<b>WEIGHT</b>	<b>SCALE</b>	
Upper Class	0.40	3	1.600
Charming	0.60	4	1.800
<b>Total</b>	<b>1.0</b>		<b>3.400</b>

<b>RUGGEDNESS</b>	<b>WEIGHTAGE</b>	<b>SCALE</b>	
Outdoorsy	0.300	4	1.200
Tough	0.700	3	2.100
<b>Total</b>	<b>1.000</b>		<b>3.300</b>

Brand Personality Dimension Index:

$$3.8+4.25+4.35+3.4+3.3= 19.10$$

*(Analysis on next page)*



### **6.8.1 Analysis of Brand Personality Dimension Index:**

PTC is not perceived as a down to earth brand because of its extravagant campaigns which has showed it as something above the ordinary, but it is believed to be an honest brand, much of which has to do with its efforts in corporate social responsibility.

Everybody knows that smoking is dangerous for health and is therefore not considered as wholesome but is perceived as cheerful because of the colorful and gaudy colors in the ads and packs. Its overall score on the sincerity attribute is 3.8 out of 5.

Because PTC has always attached itself with adventure like sailing and cricked it is considered an exciting brand, scoring high on all attributes of daring, spirited, imaginative and up to date getting a total score of 4.25 on excitement attribute.

As far as the competence attribute is concerned, PTC scores highly by getting 4.35 out of 5, which is exceptional. It manages to get a high score because smokers know that brands like Gold Leaf and Benson are reliable brands. The corporate logo and the image that has been formed in the minds of the consumers make them feel that it is an intelligent company, formulating intelligent and innovative campaigns and strategies. And on the basis of all these PTC is perceived as a successful company.

It scores a 3.4 on sophistication because it has got all kinds of brands in its portfolio touching lower middle and upper segments therefore an average score is what it gets because of not being totally upper class, but this score should be considered a positive attribute because of evenly balanced brands. On the ruggedness attributes it gets a 3.3 because most of its brands like Benson and Gold Leaf are considered as high class and sophisticated not rough and rugged. These brands are images of fine quality and delicacy and years of experience in the field of the art of blending.

## 6.9 Brand Perception Index:

Brand Perception Index = Visual + Verbal + Experiential

### 6.9.1 PTC



Attributes	Weights	Rating (1-5)	Total
<b><u>Visuals</u></b>			
Packaging	0.3	4	<b>1.2</b>
Colors	0.2	4	<b>0.8</b>
Logo	0.3	4	<b>1.2</b>
Design	0.2	3	<b>0.6</b>
<b>Total</b>	<b>1</b>		
<b><u>Verbal (based on Advert)</u></b>			
Clarity of Message	0.3	4	<b>1.2</b>
Product	0.1	3.5	<b>0.35</b>
Demonstration/Sampling			
Music	0.3	4	<b>1.2</b>
Content	0.3	3	<b>0.9</b>
<b>Total</b>	<b>1</b>		
<b><u>Experiential</u></b>			
Quality	0.4	4	<b>1.6</b>
Reliability	0.3	5	<b>1.5</b>
Favorability	0.3	5	<b>1.5</b>
<b>Total</b>	<b>1</b>		<b>12.05</b>

## 6.9.2 Lakson Tobacco Company



<b>Attributes</b>	<b>Weights</b>	<b>Rating (1-5)</b>	<b>Total</b>
<b><u>Visuals</u></b>			
Packaging	0.3	3	<b>0.9</b>
Colors	0.2	3.5	<b>0.7</b>
Logo	0.3	3	<b>0.9</b>
Design	0.2	3.5	<b>0.7</b>
<b>Total</b>	<b>1</b>		
<b><u>Verbal (based on Advert)</u></b>			
Clarity of Message	0.3	4	<b>1.2</b>
Product Demonstration	0.1	4.5	<b>0.45</b>
Music	0.3	4	<b>1.2</b>
Content	0.3	4	<b>1.2</b>
<b>Total</b>	<b>1</b>		
<b><u>Experiential</u></b>			
Quality	0.4	3	<b>1.2</b>
Reliability	0.3	3.5	<b>1.05</b>
Favorability	0.3	3	<b>0.9</b>
<b>Total</b>	<b>1</b>		

### 6.9.3 Mardanwala Cigarettes

<b>Attributes</b>	<b>Weights</b>	<b>Rating (1-5)</b>	<b>Total</b>
<b><u>Visuals</u></b>			
Packaging	0.3	3.5	<b>1.05</b>
Colors	0.2	3	<b>0.6</b>
Logo	0.3	4	<b>1.2</b>
Design	0.2	3	<b>0.6</b>
<b>Total</b>	<b>1</b>		
<b><u>Verbal (based on Advert)</u></b>			
Clarity of Message	0.3	2.5	<b>0.75</b>
Product Demonstration	0.1	3	<b>0.3</b>
Music	0.3	3.5	<b>1.05</b>
Content	0.3	3	<b>0.9</b>
<b>Total</b>	<b>1</b>		
<b><u>Experiential</u></b>			
Quality	0.4	3.5	<b>1.4</b>
Reliability	0.3	2.5	<b>0.75</b>
Favorability	0.3	3	<b>0.9</b>
<b>Total</b>	<b>1</b>		<b>9.5</b>

## 6.10 Market Share Calculation

In the following tables the market share of the big players of the tobacco industry has been calculated. These calculations will help us put the companies in the concerned quadrants in the BCG matrix.

### PTC



Market Share  
**PTC**

Attribute	Weight	Rating (1-5)	Value
Brand Awareness	0.25	4	1
Availability	0.2	4	0.8
Quality	0.2	4.5	0.9
Experience	0.1	5	0.5
Marketing & Distribution	0.25	4	1
<b>Total</b>	<b>1</b>		<b>4.2</b>

### Lakson Tobacco Company



Market Share  
**LTC**

Attribute	Weight	Rating (1-5)	Value
Brand Awareness	0.25	3	0.75
Availability	0.2	3.5	0.7
Quality	0.2	3	0.6
Experience	0.1	2.5	0.25
Marketing & Distribution	0.25	3.5	0.8
<b>Total</b>	<b>1</b>		<b>3.1</b>

## Mardanwala

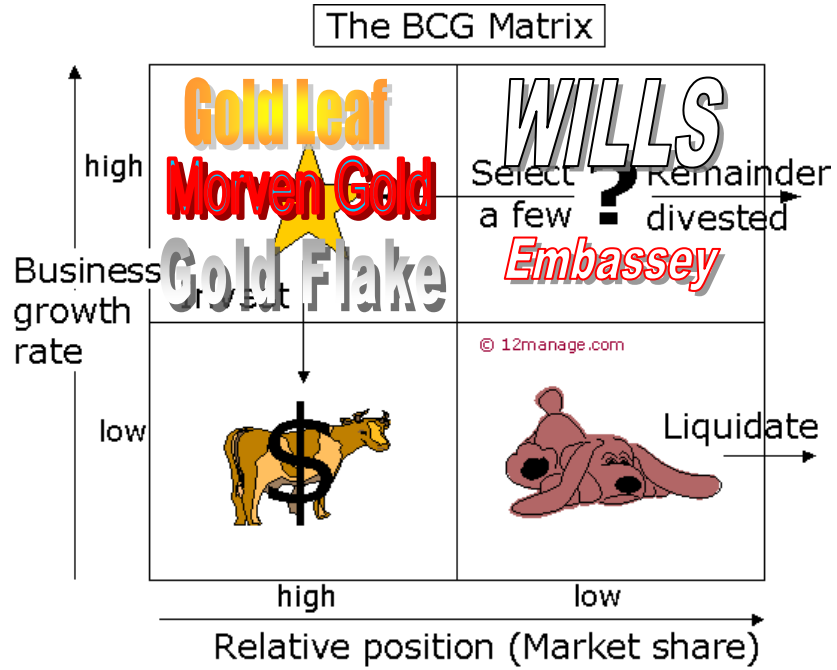
Market Share  
**MDW**

<b>Attribute</b>	<b>Weight</b>	<b>Rating (1-5)</b>	<b>Value</b>
Brand Awareness	0.25	2	0.5
Availability	0.2	2.5	0.5
Quality	0.2	2	0.4
Experience	0.1	2	0.2
Marketing & Distribution	0.25	2	0.5
<b>Total</b>	<b>1</b>		<b>2.1</b>

### 6.10.1 Market growth rate:

The market growth rate for the international market has normally been downwards for the last many years, but in case of Pakistani market it used to be around 3 percent growth annually up to a couple of years back. The recent improvement in the economy in the last 2 years has seen remarkable growth in business in many sectors and tobacco is one of them. According to experts the growth rate in the market is around 7 percent.

## 6.11 BCG Matrix Analysis:



## **6.12 Marketing before the International Marketing Standards implementation:**

Before year 2000 Pakistan Tobacco Company was one of the highest advertisers in the national media, both electronic and print. Huge advertising budgets were allocated and spent on advertising and promotion. A sizeable amount of the marketing budgets went towards above the line activities such as mega sponsorships of sports, and cricket was a greatly favored game sponsored by PTC for about 15 years, where it was the official sponsor of the Wills World Cup 1996, played in India, Pakistan and SriLanka.

The television was used generously for advertising PTC's brands, and the quality of the adverts used to be such, which required a lot of money to be spent, like the Voyage of Discovery by Gold Leaf, or Gold Flake. The last mega activity which PTC carried out was the launch of Abrar's Album, and his videos, which were all sponsored by PTC. In short all the resources were targeted towards advertising, sales promotions, sponsorships, PR activities etc, with no or very minimal attention towards trade promotions, trade offers and relationship building with the trade partners.

The advertisements in the electronic media were all typical cigarette ads with emphasis on adventure and fun, without taking into account what type and profile of audience is watching these advertisements. The government of Pakistan didn't have any objections to it, as well, despite the growing restrictions on tobacco manufacturers all over the western world. It was smooth sailing in Pakistan, but the BAT top management at the Globe House was facing the music because of problems with its OpCos operating in countries where the restrictions had been applied on tobacco marketing and advertising.

The top management realized and predicted that such regulations would be coming to all the countries in the world sooner or later because of growing pressure from international bodies such as WHO and anti smoking lobby. Seeing the inevitable , BAT along with two other giants in the global tobacco industry, Phillip Morris and Japan Tobacco drafted an agreement which would place restrictions on themselves to market the products in a responsible way, so as to go



for a one to one, permission based advertising and promotion rather than going at it with all guns blazing and broadcasting indiscriminately at every body without the care for the age, gender and preference. This agreement is known as “International Tobacco Products Marketing Standards” and its main clauses are as follows:

## **6.13 INTERNATIONAL TOBACCO PRODUCTS MARKETING STANDARDS**

- The parties subscribing to these Standards (the "Participants") wish to record their belief that tobacco products should be marketed in a responsible manner and that reasonable measures should be taken to ensure that the promotion and distribution of tobacco products is:
  - directed at adult smokers and not at youth, and
  - with the principle of informed adult choice.
- These Standards should be observed in both their letter and intent.
- In subscribing to these Standards, the Participants wish to encourage:
  - all others who manufacture or market tobacco products to join them as Participants; and
  - all others who are associated with the manufacture, sale, distribution or marketing of tobacco products to embrace the principles of these Standards.
- The practices of the Participants should not be less restrictive than these Standards unless required by law, but any more restrictive legal requirement or voluntary undertaking shall take precedence over these Standards.
- The Participants should incorporate these Standards into their own internal codes.

- The Participants intend to support the comprehensive incorporation of these Standards into national laws.
- These Standards do not apply to the relationship between Participants and their suppliers, distributors or other trade partners, although those parties are encouraged to comply with the Standards in any dealings they have with consumers.
- The Participants shall take reasonable measures to prevent third parties from using their tobacco product brand names or logos in a manner which violates these Standards.
- These Standards are not intended to prohibit the use of any trademarks as brand names or on packaging.
- A Participant shall comply with these Standards as quickly as possible, and in any event no later than 12 months from the date that it subscribes to the Standards or, where existing contractual provisions prevent earlier compliance, in any event by December 31, 2002, provided in all cases compliance is not in breach of relevant laws. The timetable for compliance with the Sponsorship Standards is set out in paragraphs 17 and 19.

## **Definitions**

The following definitions are provided to assist in the interpretation of these Standards.

Term used in this Standards Explanation:

**Adult:** A person who is at least 18 years old, except where legal requirements or voluntary undertakings entered into by the Participants specify a higher minimum age for the lawful sale, purchase, possession or consumption of tobacco products, in which case the term “adult” means a person of at least that minimum age.

**Advertisement:**

Any communication by or on behalf of a Participant to consumers which has the aim of encouraging them to select one brand of tobacco products over another.

**Promotional event :**

An event or activity organised by or on behalf of a Participant with the aim of promoting a brand of tobacco product, which event or activity would not occur but for the support given to it by or on behalf of the Participant.

**Sponsorship:**

Any public or private contribution to a third party in relation to an event, team or activity made with the aim of promoting a brand of tobacco product, which event, team or activity would still exist or occur without such contribution.

**Tobacco products:**

Manufactured cigarettes, cigars, cigarillos, pipe tobacco, fine cut tobacco, and pre-formed tobacco rolls.

**Youth:**

Any person who is not an adult. The term also includes the plural.

***Content Standards:***

1. The following Content Standards are intended to cover all communications by or on behalf of a Participant to consumers which have the aim of encouraging them to select one brand of tobacco products over another. Certain communications associated with sponsorship activities are subject to separate requirements set out in paragraph 19.

2. No advertisement shall:

- be aimed at or particularly appeal to youth
- feature a celebrity or contain an endorsement, implied or express, by a celebrity
- depict any person under or appearing to be under 25 years of age
- suggest that any of the following is enhanced by smoking:

- sporting or athletic success,
- popularity,
- professional success, or
- sexual success, or
- Suggest that most people are smokers.

3. All new advertisements published or disseminated after subscription to these Standards, including renewals and replacements of existing advertisements, shall contain a clearly visible health warning except those which:

- appear on point of sale material the advertising display area of which is smaller than 250 square centimetres,
- are, either individually or in deliberate combination with other advertisements
- smaller than 25 square centimetres and are placed on promotional merchandise, or
- until December 1, 2006 are used at and connected with sponsored activities

#### Media Usage Standards

##### 4. *Print:*

4.1 No advertisement shall be placed in any printed publication unless there is a reasonable basis upon which to believe that

- (a) at least 75% of the readers of such publication are adults, and
- (b) the number of youth who read it constitute less than 10% of all youth in the country of circulation.

4.2 No advertisement shall be placed on the packaging or outside cover of a magazine, newspaper or similar printed publication intended to be read by consumers.

4.3 Reasonable measures shall be taken to ensure that no advertisement is placed in printed publications adjacent to material that particularly appeals to youth.

##### 5. *Outdoor and Billboard:*

5.1 No advertisements shall be placed on any billboard, wall mural or transport stop or station which is located closer than 100 metres from any point of the perimeter of a school attended predominantly by youth, or ,either individually, or in deliberate combination with other such advertisements, exceeds 35 square metres in total size.

6. *Cinema*: No advertisement shall be displayed in a cinema unless there is a reasonable basis upon which to believe that at least 75% of the audience are adults.

7. *Television or Radio*: No advertisement shall be placed on television or radio unless and until:

(a) Each person seeking access to the channel or program on which such advertisement is placed provides verification that he or she is an adult, and

(b) The broadcast is restricted to countries where such advertisements are not prohibited by law.

8. *Internet*: No advertisement shall be placed on the Internet unless and until:

(a) Each person seeking access to the Internet site on which such advertisement is placed provides verification that he or she is an adult, and

(b) Access is restricted to those countries where such advertisements are not prohibited by law.

9. *Video, Audio and Computer*:

No electronic advertisement shall be incorporated within any video or audio cassette, compact disk, digital video disk or similar medium unless reasonable measures have been taken to ensure that the intended recipients of the item are adults.

For the avoidance of doubt, Participants may distribute video or audio cassettes, compact disks, digital video disks and similar media provided that the contents, cover, packaging and means of distribution comply with these Standards.

10. *Product Placement*: There shall be no direct or indirect payment or contribution for the placement of tobacco products, advertisements or items bearing tobacco brand names, within the body of any:

- motion picture,
- television programme,
- theatrical production or other live performance,
- live or recorded performance of music,
- commercial film or video,
- video game, or

- any similar medium where such medium is intended for the general public.

#### Promotion and Event Standards

#### 11. All activities and communications concerned with

- promotional offers
- promotional events
- promotional items, or
- sampling shall comply with the Content Standards.

#### 12. *Promotional Offers*

12.1 Promotional offers and programs for specific brands which appear on the package, at the point of retail sale, by mail or through other communications shall be directed only to adults and, unless prohibited by law, only to smokers.

12.2 Reasonable measures shall be taken to ensure that youth and (unless prohibited by law) non-smokers are excluded from direct mailing lists.

12.3 Participation in promotional offers by the general public will be conditional upon evidence of age eligibility and (unless prohibited by law) confirmation of smoker status.

12.4 Where promotional offers permit an adult smoker to be accompanied by other persons at a third party event or in an activity, such other persons shall be adults.

13. *Promotional Events:* Each Participant shall ensure that only adults are allowed access to promotional events.

#### 14. *Promotional Items:*

14.1 No advertisements shall be placed on:

- items where those particular items are marketed to, or intended to be used Predominantly by, youth, or shopping bags.

14.2 No advertisement larger than 25 square centimetres - either on its own or in deliberate combination with other advertisements - shall be placed on any items (other than on items

with a smoking-related function) which are to be sold, distributed or offered to the general public.

14.3 Any item of clothing which is offered for sale or distribution by or on behalf of a Participant shall only be offered in adult sizes.

15. *Sampling*: Reasonable measures shall be taken to ensure that:

- (a) sample tobacco products are not offered to youth or to non-smokers
- (b) samples are only offered in a segregated area access to which is restricted to adults
- (c) personnel employed directly or indirectly by Participants to offer sample tobacco products or to conduct promotional activities
  - (i) are at least 21 years of age, and
  - (ii) verify the age and (unless prohibited by law) smoker status of those to whom the samples and promotions are offered, and
- (d) unsolicited tobacco product samples are not distributed, either directly or through a third party, by mail.

## Sponsorship Standards

### *Sponsored Events*

16. No sponsorship shall be provided for:

- an event or activity which bears a tobacco product brand name, unless there is a reasonable basis upon which to believe that all persons who compete, or who otherwise take an active part, in the sponsored events or activities are adults, or
- a team or an individual which bears a tobacco product brand name, unless all persons sponsored by Participants are adults.

17. As from December 1, 2006, no sponsorship shall be provided unless:

- (a) there is a reasonable basis upon which to believe that attendance at the sponsored event or activity will comprise no less than 75% adults, and
- (b) There is a reasonable basis upon which to believe that the sponsored event or activity will not be of particular appeal to youth, and

(c) the Participant does not anticipate that the sponsored event or activity will receive exposure, other than as a news item, on television or radio or the Internet, unless such exposure complies with these Standards, and

(d) Success in the principal activity associated with the sponsorship does not require above-average physical fitness for someone of the age group of those taking part.

### *Sponsorship Advertising*

18. All individuals authorized to bear tobacco product advertisements, logos or brand names at sponsored events or activities shall be adults.

19. All forms of advertising associated with or ancillary to sponsorship shall comply with the provisions of these Standards. The following are excluded from these Standards until December 1, 2006:

- on-site signage at sponsored events
- incidental television and radio broadcasts of sponsored events
- Applications of trade marks or logos to people or equipment participating in sponsored events.
- Packaging, Sales and Distribution Standards

20. Cigarettes shall not be sold or distributed to consumers in packages containing fewer than ten sticks.

21. Fine cut tobacco shall not be sold or distributed to consumers in pouches smaller than 10 grams.

22. No incentive or materials shall be provided to support the sale of cigarettes in single sticks.

23. All cigarette packs and all primary packaging for other tobacco products shall carry a clearly visible health warning.

24. All cartons and bundles offered for sale duty-free shall carry a clearly visible health warning.

25. Reasonable measures shall be taken to prevent youth having access to cigarettes in vending machines.



Youth access and minimum age restrictions

26. *Youth Access:* The Participants shall make sustained efforts, in co-operation with governments and other regulatory agencies, customers and others to prevent youth having access to tobacco products. They shall also seek ways in which to reinforce and give effect to measures that will prevent youth having access to tobacco products.

27. *Minimum Age Restrictions:* The Participants are committed to the enactment and enforcement of minimum age restrictions for the lawful sale or purchase of tobacco products in every country in which their tobacco products are sold. The Participants support efforts by appropriate authorities, manufacturers of tobacco products, distributors and retailers to ensure the effective enforcement of such restrictions.

**(Pakistan Tobacco Company Website, [www.PTC.com.pk](http://www.PTC.com.pk), August 2005, *IMS*)**

## 6.14 The need for the implementation of the marketing standards:

If we go through the clauses of these marketing standards, it looks like a marketer's nightmare, and shows that the world after these marketing standards would be a jail for the marketer, with their hands cuffed not enabling them to use the communication media of any sort for any purpose. But the PTC sensed and was realizing that in the wake of the international pressure on tobacco companies all over the world, Pakistan government which had been very cooperative till that time, would also change and strictly implement these standards, because the world anti tobacco movements and the WHO were working seriously to bring some sense to the tobacco marketing.

PTC by that time had seriously embarked on a Corporate Social Responsibility initiative, in line with their international standards, and portrayed themselves as a responsible company, which although is in a controversial industry, still believed in working towards the betterment of the society in being a good corporate citizen. Therefore it wanted to prove to the world and the antis that it can go off the air and stop advertising for the betterment of the society.

The move was also important and had to be taken because PTC because of its advertising and marketing activities had been successful in making powerful and sustainable equity of their key brands, and they knew that even without advertisement they would do well, but they also knew that Lakson was comparatively new in the market, and had not done enough to create recognition for its brands and desperately needed advertisement for its image enhancement, therefore PTC wanted to show the government a way to block all the ads on the television, which would inflict more pain on Lakson than it would on PTC.

The need was also amplified because the management was feeling that it was moving away from being a consumer focused company, and lacked the knowledge that it needed from the market, also the relationships with the trade partners had over a period of years become very cold. The retailers and distributors worked and cooperated because it was their necessity and there was demand in the market, but for a company in such a business, it was imperative to have remarkable trade relationships with its partners – the retailers and the distributors. With emphasis low on above the line communication, more effort and resources would go into the below the line, one to one , relationship building marketing.

The move to go off the air and regulate the industry by accepting a self imposed ban on itself, was supposed to have a beneficial effect on PTC, bringing them cost savings, and establishing them as a socially responsible company.

#### **6.14.1 Effects of the implementation of the IMS:**

The initial result that it had was that the sales force got a bit demotivated, because they thought that there only way of communicating with their consumers is being taken away from them, and it would leave them dumb, and ineffective, but the top management knew that it would have a very little impact, if at all, and they needed to bring confidence in the people and make them understand the rationale behind the self imposed ban on advertising and media.

The huge budgets of millions of Rupees which went into advertising and sponsorships were now being used in below the line activities such as Retail Excellence programs, Retail Partnership Programs, consumer promotions, trade promotions, incentives and bonuses for top performing salesman and retailers, distributor competitions and distribution excellence programs.

The company has since that time slowly moved away from an advertisement based company towards a company focused on supply chain and efficiencies in the trade marketing and distribution. Trade marketing and distribution is at the heart of marketing efforts of PTC and the whole marketing department revolves around the activities and the outcomes of the TM&D.

With lots of extra resources freed from advertisement and sponsorships, the company has started to gather more information about its trade channels, distribution inefficiencies, shortcomings in the current ways of marketing in an effort to know more and more about its customers and consumers, so that they get the best quality product, with superior efficiency and effectiveness, while keeping the costs low.

The efforts are now going into strengthening and realigning the supply chain in a seamless manner so that it can supplement and add value to the marketing and distribution.

PTC went off the air with its advertisements in 2001, but even before that since 1999 it wasn't showing any ads showing the products or a person smoking. Only corporate ads showing what PTC is and reporting some of its CSR achievements were aired, but Lakson didn't stop and intensified its efforts for both media and sponsorships. But Lakson were finally stopped by the government in 2003, because of efforts by PTC to persuade the government to stop all companies in Pakistan showing tobacco ads on the television.

The results of these efforts have been exceptionally positive. The sales have shown a steady growth and the company has been profitable for 4 consecutive years after 7 continuous years of losses. The volumes and the value share have been rising and in the month of July 2005, PTC even beat Lakson who had been a volume leader for 6 years. The volume growth in brands like Gold Leaf and Gold Flake have been all on the positive side and the forecasts show even more growth of these brands.

The time after the ban on advertisements and media has been named as "the new world of marketing" by PTC. The new world of marketing is challenging because it needs everybody in the company to better understand the customer and the consumer. This is a one to one permission based way of communication, rather than speaking to everybody at the same time, in the process communicating with people who are not supposed or suited for that information, causing a loss in the form of ineffective communication and low productivity.

Some of the programs that Trade Marketing has started now to build goodwill of the company in the minds of the customers in the new world of marketing are:

#### **6.14.2 Retail Partnership Programs:**

The RPP is scheduled twice a year in every area and major markets. The intention of RPP is to take into confidence all the retailers, giving them information about the company, product knowledge and ways to improve their sales and revenues. This session is usually held at a 5 star hotel in metros and 3 or 4 star in small towns, and almost 200-300 major retailers are called to spend a couple of hours, which is followed by a lunch and certificate distribution. The local team also gets to listen to the retailer's concerns in all areas and tries to resolve their problems.

### **6.14.3 Top Trader Programs:**

The top trader programs are for the retailers who have high sales of PTC's brands. The top traders are given Gold or Silver status and a target is assigned to them based on their sales records. They can earn a maximum of 1200 points every month and can redeem those points in the form of electrical appliances with point scores associated with them. This is done to give the retailers an additional incentive to sell more of PTC's brands. The duration of such activities is usually six months.

### **6.14.4 RCS-6:**

RCS-6 is a database, which is used by the trade marketing team, to collect and update information about high selling outlets and all the relevant information about them. The Trade marketing officer, has to visit 200 shops in a month to check if the trade activities are all being conducted there or not. During this visit he takes all the information about the shop, location, merchandising, own and competitor sales, brands sold, personal information etc, and updated it in the RCS database in his laptop. This database is maintained by all the TMOs in market or area and every month after updating , it is replicated on the main database, in the region, to be used by the Regional Manager, the Area Manager or the Head Office. This database is a repository of all the information about outlets in a territory and a market, and serves as a reference point in sales trends, merchandising, and promotion programs.

### **6.14.5 Trade promotions:**

In the new world of marketing the efforts and the emphasis on trade offers have been increased. The cycle activities in one year for the trade promotions and offers have increases, to gain loyalty from the retailers and giving them incentives to sell more to earn more. These trade promotions can be , trade offers, redemption, a certain amount of free percentage free, etc.

### **6.14.6 Key Accounts:**

The shops or the outlets which sell high volumes of Benson & Hedges, Gold Leaf and Capstan are categorized into Key accounts. Key accounts are looked after by a Key Accounts Officer, and not a TMO who is responsible for visiting every outlet at least twice a month to

see all the trade marketing activities are running smoothly and the distribution is up to the mark. Key accounts are offered special incentives, and merchandising and special offers are formulated for them because of the profile of the consumers they serve. Fuelled & Energized is a promotion that is going on Benson&Hedges on petro marts, these days, which are key accounts.

## **6.15 The New shape of Sales and marketing in PTC after the new world of marketing standards.**

### ***Transformation of Sales to Trade Marketing and Distribution (TM&D):***

After the shift in the marketing standards from an organization mass marketing products, to one which is now putting all its efforts to move towards relationship based marketing and strengthening of the trade and distribution channels, the marketing department has undergone many changes. Some have been quick and rapid while some have been gradual. In the following some of those changes would be discussed:

#### **Trade marketing and distribution:**

The aspect of the company which was previously dealing with sale of products at all levels, and was known as sales is now known as Trade Marketing Distribution (TM&D). The National Sales Manager is called as the Head of Trade Marketing, similarly new positions such as Trade Marketing Development Manager, and Trade marketing officers which were formerly known as Sales Officers have arisen.

The whole TM&D function is dealt as an organization, and is responsible for the overall development of new goals and targets and then means to achieve them by facilitating each and every step in the value chain from the seed to smoke, hence the TM&D organization can truly be called as the backbone of PTC.

### **6.15.1 Trade Market and Distribution**

#### **Vision:**

First Choice For Everyone

#### **Mission:**

Reach our target consumers in a most efficient and effective way by becoming benchmark supplier to trade within strategic channels in every market place where we do business.

### **6.15.2 TMO Role**

- Planning
- Distribution
- Trade Relation
- In store Marketing
- Managing People
- Administration

### **6.15.3 Critical Success factors**

- Strategy & Planning
- Supply Chain Management
- Recourse Management
- POP Management
- Accounts Management
- Information Managemen

## 6.16 Linkage Between CSF & Responsibilities

<b>Critical Success Factor</b>	<b>Your Six Responsibilities</b>	<b>You are Contributing through</b>
Supply Chain Management	<ul style="list-style-type: none"> <li>• Distribution</li> </ul>	<ul style="list-style-type: none"> <li>• Maximising successful calls</li> <li>• Achieving call frequency objectives</li> <li>• Ensuring optimal stock levels and product quality</li> <li>• Ensuring that consumer price is in line with the brand strategy</li> </ul>
POP Retail Marketing Management	<ul style="list-style-type: none"> <li>• In-Store Marketing</li> </ul>	<ul style="list-style-type: none"> <li>• Implementing trade and consumer promotions.</li> <li>• Placement of branded materials</li> <li>• Preparation, implementation and checking of planogram.</li> </ul>
Account Management	<ul style="list-style-type: none"> <li>• In-Store Marketing &amp; Trade Relations</li> </ul>	<ul style="list-style-type: none"> <li>• Implementing and following up of account plans for merchandising and promotions.</li> </ul>
Resource Management	<ul style="list-style-type: none"> <li>• People Management</li> <li>• Administration</li> </ul>	<ul style="list-style-type: none"> <li>• Recruiting, supervising, training and coaching SPs and part timers</li> <li>• Managing all assigned funds, materials and equipments in the most secure and economical manner.</li> </ul>



<b>Critical Success Factor</b>	<b>Your Six Responsibilities</b>	<b>You are Contributing through</b> 
<b>Information Management</b>	<ul style="list-style-type: none"> <li>• Trade Relations</li> <li>• Administration</li> </ul>	<ul style="list-style-type: none"> <li>• Providing market information and reports to the relevant people on time.</li> <li>• Maintaining accurate and relevant records and outlet information.</li> </ul>
<b>Strategy &amp; Planning</b>	<ul style="list-style-type: none"> <li>• Planning</li> </ul>	<ul style="list-style-type: none"> <li>• Giving input in the cycle planning process.</li> <li>• Maximising productivity in trade coverage, call rate and call preparation.</li> </ul>

#### **6.16.1 4 Guiding Principles**

- Strength from Diversity
- Open Minded
- Freedom through Responsibility
- Enterprising Spirit

#### **6.16.2 Business Focus**

- Market Leadership or Premium Positions
- Productivity ( Supply Chain – In directs )
- International Brands, Lights, Premium and ASU 30

## **6.17 7 Strategic Imperatives**

1. Focused brand portfolios communicated through state-of-the-art adult smoker engagement programs.
2. Industry leading product portfolio, designed to address consumer needs and social expectation.
3. Optimum product availability through world-class customer service.
4. Leading position in priority markets.
5. Recognition as a responsible company in an industry seen as controversial.
6. Wired for # 1
7. A winning environment, inspiring passion for the business, talented people, and personal fulfillment.

### **Volume Classification**

<b>Volume</b>	<b>Annual Volume</b>	<b>Monthly Volume</b>	<b>Daily Volume</b>
1	20000+	1667+	56+
2	10000 – 19999	833 - 1667	28 – 56
3	5000 – 9999	417 - 833	14 – 28
4	20000 – 49999	167 - 417	6 – 14
5	1000 – 1999	83 - 167	3 – 6
6	500 – 999	42 - 83	2 - 3
7	200 – 499	17 - 42	1 – 2
8	100 – 199	8 – 17	3 – 1
9	0 – 99	0 – 08	0 - 0.3

## **Trade Marketing & Distribution**

### **6.17.1 The 9 Steps of the Call**

It is important for each Trade Marketing Rep to understand and value the 9 steps of the call as one of the critical tools to accomplish their roles. These steps provide a logical sequence to the functions a Rep must perform during every outlet visit to ensure that they meet their requirements and the call time is optimised.

### Step 1. Preparation

Our company constructs long term and short term plans, which cascade through the organisation and form the basis of the territory's yearly, monthly, weekly and daily plans. This topic focuses on the specific daily call plans:-

- Establish your objectives

What do you want to achieve from the call, from both a company and personal perspective?

- Define the present situation

Identify what is likely to aid or hinder you from reaching your goals

- Develop actions

Develop a set of actions to reach your goals (it may be necessary at any Time during the call to re-assess the situation and re-plan). The day before the call Using information collected on previous calls, set objectives for the next days call. Ensure you fulfil any obligations made to your customer during previous calls.

- Prior to the call

Review the objectives you have set for yourself and remember key details, so you can personalise the visit. Ensure you have the right resources in place to conduct the activities needed.

### Step 2. Approach

The approach is the time spent between arrival at the outlet and the point at which you make your opening remarks.

Observation outside the outlet

You should gather information which helps you tailor your call. Adopt the consumer's viewpoint to see what is likely to attract their attention, and the environment in which they are

shopping. Studying the outlets consumers provides a better understanding of what will appeal to them.

Observation inside the outlet

Observe the situation from the consumer's perspective, as well as your own. This includes reviewing the:-

Tobacco display area

Having products correctly displayed, visible and in accord with any merchandising agreements is of vital importance in achieving our TM&D strategy. The tobacco category space should be reviewed vs other categories.

Pricing

Correct pricing is paramount to ensure consumer and customer satisfaction. You should compare store prices vs other outlets in the area. store format .This can help you achieve the most prominent positions for our merchandising

New merchandising opportunities

This can improve brand visibility and assist the sell-through of our products discussion with the customer. This can help identify customer need. Asking open-ended questions will help draw out information.

Your opening remarks

Before the formal presentation, you must introduce yourself (and highlight which brands you represent) and make your opening remarks, which should generate interest and favourable attention from the retailer.

### Step 3. Stock Check

From the stock check, you can learn a lot about the Stock must be checked at every call, to ensure the right product is delivered, and is in the best possible condition (it is important to do a product age and quality check to ensure rotation of stock). You must be familiar with the outlet's portfolio – both of BAT brands and competitors, and know how much stock is held,

customer's overall tobacco business (i.e. which are the best sellers etc). In any out-of-stock situation, you should identify the reasons and consider a possible solution (which may form part of the main discussion).

#### Step 4. Presentation

You must introduce the objectives of the call. These could be:-

Product availability

In-store marketing

Promotion

During the discussion you offer advice, assistance and information based on the issues you have seen/discussed/identified. You should also endeavour to satisfy the customer's needs as well as meeting your own call objectives (ask open-ended questions and listen carefully to retailer responses).

To successfully meet your objectives, you need to be familiar with the features and benefits of your proposal. You need to focus on the objectives of selling in and selling out.

There is a 5 stage selling format:-

- I. Summarise the situation
- II. State the idea
- III. Explain how it works
- IV. Reinforce the key benefits
- V. Close the deal

#### Step 5. Closing

Following the introduction of your ideas, features and benefits, you reach a point where a decision has to be made. Negotiate and reach agreement on the proposition.

You must be able to handle any objections raised before you can close.

The close must prepare the ground for the next visit. You are building a long-term relationship, where every call is a link in the chain. Do not forfeit long term benefits for short term success.

Closing steps may be as follows:-

- assume agreement has been reached
- summarise the key points
- offer alternative choices
- offer a special deal, if available
- offer a trial quantity of the product
- ask for the order

#### Step 6. In-store marketing and Merchandising

During each call the TMR must carry out the in-store activities based on the agreement gained during closing. Merchandising and consumer contact provide an opportunity to help the customer sell out the product, and reach a wider potential audience. To guarantee maximum effect, you must use the right material in the right place to convey the right message.

Points to remember:-

If the material is channel specific, use it in the right channel check the size of the material for the retail space ensure brand image and outlet image are compatible ensure the investment in materials is in line with the outlet importance position the material close to the product and the point of purchase place material in a prominent position (eye level, no obstructions etc)

In a number of countries there are strict legal guidelines relating to tobacco merchandising. These must be adhered to – and approved by local Legal/CORA.

### Step 7. Consumer Contact

The role of the TMR is to create a favourable impression of our company (responsible company with high quality brands to meet consumer tastes) with both customers and consumers. Consumer information can help the customer improve their category offering.

The best place to talk with consumers is when they purchase cigarettes, and always introduce yourself in a clear, understandable way. Talk only with smokers who are aged 18 or over who are willing to engage in conversation, and if permitted under local legislation.

- Introduce yourself and company, and mention the best known products
- Ask if they have time/are willing to talk with you
- Find out if they purchase for self-consumption or for others
- Find out why they choose a particular brand and how long they have smoked it
- If they previously smoked any other brand, what was it and why they changed
- If not a BAT brand, this is an opportunity to introduce brands from our portfolio with similar characteristics

### Step 8. Administration

Administration is the TMR's way of keeping track of activities and forms the basis for future planning.

Admin consists of 2 elements:-

Recording data on consumer record card/TM&D solution hand held devices which can be sent to the office

Filling out official documentation i.e. invoices or order forms related to the actions arising from the call

Every transaction must be recorded according to local legal requirements, and when products are sold, an invoice must be issued.

## Step 9. Evaluation

Evaluation of performance leads to improved performance and the basis for more stretching future planning with SMART objectives.

At the end of the call, the TMR must review what happened against the call objectives. All the elements which contributed to achieving or failing to achieve objectives should be summarised and documented. This can help the TMR improve performance through learning by experience.



## **6.18 Trade marketing channels of distribution:**

The channels through which secondary sales are done are:

### *6.18.1 Grocery:*

These are the Kiriyana stores normally found in every bazaar in cities and downs. Their sizes can vary from a very small kiriyana store to a large super market like Al-Fatah in Lahore or Agha's in Karachi.

### *6.18.2 Convenience:*

This is the second channel of distribution and covers small outlets such as Paan Shops, Khokas, Kiosks and petromarts. PTC has agreements with all the petromarts of Shell, PSO and Caltex, by virtue of which these outlets would exclusively sell PTC brands and are key accounts, which have special offers running for them from time to time. Although this is not a big channel, but still has a lot of potential for selling high and premium brands, and by getting exclusivity in them, PTC has blocked the way for PMI and other entrants to gain access to these outlets.

### *6.18.3 HoReCa:*

HoReCa stands for Hotels, Restaurants and cafés. Although this is very new concept which is to gain access to all the major hotels in the metropolitans which have a good name and a repute such as Café Zouk, Nandos, Area 51, Evolution, Cinnamon, Pappassalis etc. these are the areas which are used to promote and sell Benson & Hedges because of a high turnout of ASU 30 smokers at these places. Additionally the brand team from time to time initiates promotional activities like concerts or musical programs at these places and exclusively invites B&H smokers from the database which it maintains for these smokers.

### *6.18.4 Concept of Key Accounts:*

Out of the universe of all the outlets in metropolitans like Karachi, Lahore, Pindi /Islamabad, some 1650 outlets have been selected as the key accounts. A key account is an outlet which is a high selling outlet of Benson &Hedges, Gold Lead and Capstan. The key accounts have a separate Key Accounts Executive and a Key Accounts officer looking after them, just to give them special attention and priority. The key accounts have special promotions and trade

programs and incentives by giving them more targets than the other retailers. Most of the large grocery stores and petrolmarts are key accounts.

#### 6.18.5 Cycle Activities:

The cycle activities are started as the year begins and keep going on throughout the year for some brand or another or sometimes simultaneously on multiple brands. The cycle activities may include trade promotions, trade offers, redemption offers, national or local consumer promotions etc. a cycle calendar is designed at the beginning of every year which schedules tentatively all the cycle activities that would go on throughout the year. Cycle plans are developed on the basis of the dates in the calendar which is followed by a cycle brief, for each local market and cycle instructions, which serve as the instructions for each and every action that is to be performed in the campaign.

The cycle activities can include both the consumer and the trade promotions or both at a time, for example a national consumer promotion with the name of “first choice” is running on Gold Flake these days, and with that a trade offer on B&H of 1 percent free is running for the retailers, with a redemption scheme for 5:1 free pack. Previously a consumer promotion with the name of “winning drive” was run for 2 months on Capstan, in the month of July and August.

#### 6.18.6 Distributor's competition:

Distributor's statistics on each and every aspect are taken for every six months and at the end the average of all these factors are taken to assess the distributor's efficiency in distribution, coverage, resources and cost saving measures. Financial indicators like net margin, ROI and operating profit are also assessed for competition. Based on the results prizes of 200,000 and 100,000 are given to first and second distributors all over Pakistan.

## *6.19 Conclusion and Recommendations:*

Pakistan Tobacco Company has moved from conventional marketing to a very new, daring and a strategically important method of marketing, which is based on merely selling and distributing the product like any other company, but the emphasis is on building long lasting and strong relationship with trade partners at every level.

If we look at the effects, the ban on tobacco advertising has been a blessing in disguise for PTC. It has enabled them to look at things that they had been doing for ages, from an altogether different perspective and critically evaluate the way they had been doing things.

The International Marketing Standards was an initiative by PTC and not something that was imposed from outside. The reason for the self imposed ban was also based on a very far reaching vision. The management in PTC saw that international regulations on the sale of tobacco products were becoming stricter by the day, and although Pakistan government was indifferent in this situation, a time would come when the government because of international pressure would have to ban the advertising of tobacco products and impose stricter bans on selling of tobacco products. PTC knew that it had invested so much in its brands to an extent of creating household names of brands like Gold Lead, Gold Flake and embassy in their relevant markets. On the other hand, Lakson had just started to realize the power of advertising and started out making catchy advertisements for their products. In this situation PTC could afford to stop advertising all together and still do good, whereas for Lakson it could mean curtains, considering their position in the market because they had just started to work on their brands.

Therefore PTC achieved at least three objectives from the implementation of the IMS. The first was compliance with internationally agreed marketing principles for tobacco products and aligning themselves with BAT centrally. The second was saving huge costs spent on advertising and massive promotions aimed at broadcast audience, and the third was to block Lakson's efforts by persuading the government to impose total ban on advertising of cigarettes on television and radio.

The IMS and the ban on advertisements presented PTC an opportunity to rethink of the ways of doing business in an environment where modes of communication were limited but more focused, so instead of talking to masses and reducing the efficiency of communication, the new approach was to talk to only the audience who was supposed to be communicated to, increasing the efficiency of communication and reducing cost drastically.

The marketing strategy now is focused more towards achieving efficiencies in distribution and supply chain, and providing the best services to customers and stakeholders in each and every channel be it primary, secondary, retail, or wholesale. The finances that are no longer being used for advertising are used for trade offers and promotions at much bigger levels. The efforts are to establish and develop good working relationship with the retailers so that they feel valued by being a partner of PTC.

Distributors are now being given more importance and PTC is helping them streamline their operations to give the best possible service while keeping their costs low and to push for higher levels of coverage and productivity.

People both inside and outside the company used to feel that the ban on advertising and these IMS would handcuff their hands and sales would decline, but since that time sales are on a all time high and growing every year, which means that the recipe has worked for PTC.

A lot still needs to be covered. Out of around 48000 villages in Pakistan, only 13000 to 14000 are being covered, so there is a lot of gap which has to be bridged. Out of stock problems in metropolitans and large cities has always been a source of concern for management and solid steps needs to be taken to minimize the out of stock situation for all brands. To sum things up, the decision to “off the air” and bring sense to marketing in the tobacco industry has been a radicle step that has been taken by PTC, and as always it has been pioneer in doing new things in the country. All other have followed suit but their attempts have been half hearted because they had more at stake. Contrary to people’s perceptions and apprehensions that smoking would end all together and tobacco companies would be forced out of business, the situation has been totally in contrast, and PTC has been doing record business since that time. At the same time it has satisfied all the people from the government to the general public who were unsatisfied with the norms of tobacco advertising, by reaffirming that they are a socially

responsible company which believes in doing business in a responsible and an ethical way, and which is committed towards the betterment and the uplift of the society in which it operates, taking along all the stakeholders and fostering a culture of open communication with all the stakeholders at all levels.

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## Annexure 1

# LIST OF ARTICLES

### **‘It’s not about how you spend but how you earn your money’**

#### **On Corporate Social Responsibility (CSR)**

There are actually two terms that need to be understood in this context. One is CSR (Corporate Social Responsibility) and the other is CSI (Corporate Social Investment). People generally confuse the two. Most businesses in Pakistan are involved primarily with just CSI, which is spending on socially responsible initiatives such as giving donations, managing healthcare facilities, preserving the environment etc. In fact, CSR goes far beyond CSI and CSI is just one part of the overall CSR Philosophy. For us at PTC, its not about how you spend (CSI) but how you earn your money (CSR). That is the crux. Each and every organization that does CSI, also needs to make sure that the way they are making their money is ethical, meets the reasonable expectations of the society and that the organization doesn’t behave in a irresponsible manner.

#### *ON CSR at PTC*

Pakistan Tobacco Company we aim to demonstrate responsible corporate conduct across all aspects of our operations. We abide by this philosophy each step of the way: from appropriate marketing and consumer information to supporting sensible tobacco regulation; from respecting workplace human rights and reducing our environmental impacts to contributing to local communities. We seek to work continuously to engage with our stakeholders, to balance their views and to align our business decision-making with reasonable societal expectations of a modern tobacco group.

We recognize that CSR presents particular challenges for a tobacco company. Tobacco products pose real risks to health and raise important questions about how best to define responsible product stewardship. We therefore believe that for our business, the only meaningful approach to CSR is one based squarely on our products, on the issues surround

them and on ways of responding to sometimes strongly held views of our stakeholders.

## On the benefits of CSR

To see the long term benefits of CSR to our society, let me share with you a few dimensions, such as counterfeiting, tax evasion, environmental degradation etc. Now these kind of menaces are there in the society because generally the businesses are not adhering to CSR but only to CSI. In our society most companies think that by giving donations they have become socially responsible. It doesn't work this way! It may wash off some of your sins but it doesn't make you responsible. To be socially responsible you need to ensure that you are following all the laws, not polluting the environment, not evading taxes so on and so forth; For example if you are in the food business CSR means that you are using only food grade colour that is not unhealthy, you are not using low quality ingredients but are conforming to the highest standards of health and hygiene in your production. This is CSR and this way not only companies become socially responsible but the whole society benefits.

## On the critics of CSR

The management of a business is a trust given to the managers by the shareholders and part of that trust includes ensuring long term business sustainability. In today's corporate world, the businesses can't just survive on day to day adhocism, rather a long term sustainability strategy is a must. If we don't have CSR and the society disagrees with your business conduct, in the long term consumers are going to react. People here have this misconception that this CSR is a western phenomenon and it can't happen in Pakistan. I feel that consumers anywhere have a great power to influence and regulate businesses. It is going to happen sooner or later but it is going to happen, if not happening already. I can quote many recent examples in Pakistan where business had to abandon projects because the local communities forced them to do so. Therefore the businesses need to be very careful on how they earn their money - focus should not be just on spending it, because the spending process comes much later. To give an example, if all business in Pakistan behave ethically and pay all taxes, than we can all imagine the very favorable impact on our economy as Government revenue will go up many fold.

On responsible communication

We had taken the decision to voluntarily stop cigarette advertising on TV, as of Jan 1<sup>st</sup> 2003, whereas the Government regulation came much later in 2003. We were the only cigarette company to have done so. On the outdoor also there is a fundamental change in our policy and now you don't see huge billboards of cigarette brands. Previously whole buildings were branded and now the maximum size is not more than 35 sq meters in total.

**(Raza Zulfiqar, Corporate Affairs Manager PTC.)**

## **27 per cent young smokers inspired by cigarette advertising**

ISLAMABAD: Advertising increases the desirability of tobacco use. This assertion has once again been substantiated in a survey revealing that 27 per cent of young smokers in Pakistan were motivated to do so by media and outdoor advertisements, and that another 6 per cent intended to take up smoking in future.

Shared with journalists at a press conference here Monday, the survey has been conducted by TheNetwork for Consumer Protection to assess the impact of tobacco advertising on youth and was presented by Ayyaz Kiani, Dr. Ehsan Latif and Kaneez Zehra. Its findings have been derived from interviews of young people aged between 15 and 25 years.

The survey has reported the incidence of smoking amongst the respondents as being 36 per cent. Forty per cent of the male respondents and 13 per cent of the female respondents were smokers. Ninety-four per cent said they had seen or heard tobacco advertisements, largely on the electronic media, followed by billboards and cigarette sale outlets. Forty-two per cent said tobacco advertisements portray smoking as an exciting activity.

The tobacco industry's claim to the effect that its advertisements are aimed at brand-switching and target those who have already chosen to smoke rather than those who are yet to initiate smoking have also been rejected by the survey. Twenty-seven per cent of the youth said they who took up smoking after seeing advertisements as against just 12 per cent who opted for brand-switching.

Most smokers begin smoking in their teenage—in most cases between 14 to 20 years. According to the survey, the mean age of smokers was 21 years while 22.5 per cent had been smoking for more than five years, meaning that a large proportion of the target initiated smoking at the age of 17.

On the question of under-age sale, 57 per cent of the respondents said such restrictions do not work whereas 48 per cent said underage ban implies that it is appropriate to smoke after the age of 18. The survey also points to an increase in the number of female smokers.

An estimated 0.1 million people in Pakistan die due to tobacco-related illnesses each year. According to The Network, 1200 youth in their teens take up this habit daily. At a global level, the annual death toll attributable to tobacco is expected to rise from its current estimates of 5 million per year to 10 million by 2025, with 70 per cent of these deaths projected to be occurring in the developing countries.

Having shared the findings of the survey, the team presenting the report emphasised that partial bans will never make a difference in terms of affecting a decline in youth smoking, and that the government must give a serious thought to imposition of comprehensive bans on tobacco promotion.

*(Shahina Maqbool)*

## Annexure 2: Statistics

### Standard grading system for flue-cured and Burley tobacco

Standard grading system for flue-cured tobacco										
Colour symbols										
L	Lemon	KR	variegated red or scorched				KV	variegated greenish		
LL	whitish-lemon	V	greenish				KM	variegated mixed		
F	Orange	KL	variegated lemon				G	green		
FR	orange red	KF	variegated orange				GR	green red		
R	Red	KD	variegated dark red				GK	green variegated		
K	Variegated					GG	grey green			
Groups					Qualities					
B	Leaf	P	primings		1	choice		4	fair	
H	Smoking leaf	M	Mixed-group			2 fine			5 low	
C	Cutters	N	nondescript		3	good		6	poor	
X	Lugs	S	scrap							

Source: Dimon, 1999 (based on USDA).

Standard grading system for Burley tobacco										
Colour symbols										
L	buff	D	dark red				VR	greenish red		
F	tan	K	variegated				G	green		
FL	tannish buff	M	mixed				GF	green tan		
FR	tannish red	V	greenish				GR	green red		
R	red	VF	greenish tan							
Groups					Qualities					
X	flyings	T	tips		1	choice		4	fair	
C	lugs of cutters	M	mixed		2	fine		5	low	
B	leaf	N	nondescript		3	good				
		S	scrap							

Source: Dimon, 1999 (based on USDA).

**Annex table 1. Estimated annual per capita consumption of cigarettes per adult 15 years of age and over, selected countries, 1970-72 to 1990-92, ranked according to consumption in 1990-92**

Country	1970-72 Per capita consumption	Rank 1980-	82 Per capita consumption	Rank	1990-92 Per capita consumption	Rank
Poland	3 010	11	3 400	6	3 620	1
Greece	2 640	16	3 440	4	3 590	2
Hungary	2 940	13	3 320	7	3 260	3
Japan	2 950	12	3 430	5	3 240	4
Republic of Korea	2 370	20	2 750	15	3 010	5
Switzerland	3 700	2	3 060	10	2 910	6
Iceland	2 940	14	3 230	9	2 860	7
Netherlands	3 150	6	3 290	8	2 820	8
Yugoslavia	2 330	21	3 030	12	2 800	9
Australia	3 410	4	3 440	3	2 710	10
United States	3 700	3	3 560	2	2 670	11
Spain	2 190	22	2 440	21	2 670	12
Canada	3 910	1	3 800	1	2 540	13
New Zealand	3 060	9	2 890	13	2 510	14
Ireland	3 050	10	3 030	11	2 420	15
Germany	2 430	18	2 420	22	2 360	16
Belgium	3 090	7	2 880	14	2 310	17
Israel	2 060	23	2 400	23	2 290	18
Cuba	2 690	15	2 630	17	2 280	19
Bulgaria	1 770	35	1 880	36	2 240	20
United Kingdom	3 250	5	2 740	16	2 210	21
Austria	2 390	19	2 620	18	2 210	22
Saudi Arabia	1 220	52	1 940	35	2 130	23
France	1 860	31	2 080	29	2 120	24
Turkey	1 950	29	2 250	25	2 100	25



Luxembourg	3 090	8	2 580	19	2 080	26
Portugal	1 440	40	1 800	41	2 010	27
Syrian Arab Republic	950	63	1 730	45	2 000	28
Italy	1 800	34	2 310	24	1 920	29
Venezuela	2 060	24	2 210	26	1 920	30
Denmark	2 050	25	2 050	31	1 910	31
China	730	72	1 290	56	1 900	32
Suriname	1 160	56	1 870	37	1 870	33
Norway	2 030	26	1 950	33	1 830	34
Mauritius	1 310	48	1 940	34	1 830	35
Trinidad and Tobago	1 440	41	1 960	32	1 780	36
Philippines	2 010	27	2 190	27	1 760	37

32 SECTOR WP 179-2002.doc/v2 **Country 1970-72 Per capita consumption Rank 1980-82 Per capita consumption Rank**

**1990-92 Per capita consumption Rank**

Colombia	1 880	30	1 790	42	1 750	38
Tunisia	1 380	44	1 590	49	1 750	39
Finland	2 000	28	1 800	40	1 740	40
South Africa	1 340	46	1 600	48	1 720	41
Uruguay	1 630	38	1 720	46	1 700	42
Jordan	1 020	61	1 840	39	1 680	43
Malaysia	1 400	42	2 040	30	1 630	44
Singapore	2 510	17	2 550	20	1 610	45
Argentina	1 810	33	1 770	43	1 610	46
Algeria	950	64	1 580	50	1 600	47
Fiji	1 150	57	1 650	47	1 590	48
Romania	1 740	36	2 130	28	1 550	49
Sweden	1 700	37	1 840	38	1 550	50
Brazil	1 330	47	1 750	44	1 500	51
Nicaragua	1 380	45	1 440	52	1 460	52
India	1 010	62	1 310	55	1 370	53
Costa Rica	1 850	32	1 520	51	1 340	54
Iraq	1 250	51	1 090	64	1 280	55
Cambodia	940	65	1 260	58	1 220	56
Albania	1 220	54	1 230	59	1 220	57
Egypt	730	73	1 180	61	1 210	58

Indonesia	500	83	950	72	1 18059	
Chile	1 310	49	1 380	53	1 130	60
Guyana	1 220	53	1 280	57	1 130	61
Paraguay	1 190	55	1 030	68	1 100	62
Thailand	810	69	1 080	66	1 050	63
Senegal	430	88	760	79	1 05064	
El Salvador	1 260	50	1 030	67	1 010	65
Dominican Republic	910	66	1 010	69	1 010	66
Bangladesh	510	81	680	82	990	67
Mexico	1 600	39	1 370	54	970	68
Democratic People's Republic of Korea	1 050	60	1 210	60	960	69
Panama	1 15058950			71	960	70
Iran (Islamic Republic of)	900	67	1 160	62	930	71
Morocco	680	75	1 12063920			72
Congo	880	68	890	73	900	73
Ecuador	650	77	830	74	870	74
Jamaica	1 40043990			70	860	75
Honduras	1 090	59	1 080	65	850	76

SECTOR WP 179-2002.doc/v2 33 Country 1970-72 Per capita consumption Rank 1980-82 Per capita consumption

Rank 1990-92 Per capita consumption Rank

Sierra Leone	460	86	810	76	810	77
Yemen	470	85	570	88	810	78
Viet Nam	N/A	111	790	77	790	79
Angola	740	71	740	80	740	80
Cameroon	270	98	590	87	740	81
Côte d'Ivoire	800	70	810	75	710	82
Benin	640	78	770	78	650	83
Pakistan	630	79	720	81	640	84
Lao People's Democratic Republic	510	82	600	86	600	85
Haiti	170	104	630	85	580	86

Nepal	170	105	290	103	580	87
Kenya	420	89	560	89	500	88
Togo	560	80	480	92	490	89
Madagascar	270	99	470	93	460	90
Mozambique	370	95	460	94	460	91
Zimbabwe	700	74	660	83	430	92
Bolivia	400	92	560	90	430	93
Sri Lanka	460	87	520	91	430	94
Zambia	500	84	430	96	430	95
Liberia	390	93	420	97	420	96
United Republic of Tanzania	380	94	370	99	370	97
Nigeria	290	97	350	100	370	98
Peru	410	90	390	98	350	99
Guatemala	660	76	640	84	340	100
Malawi	200	102	330	101	330	101
Uganda	300	96	300	102	300	102
Zaire	220	101	240	105	270	103
Ghana	410	91	440	95	250	104
Niger	110	108	100	110	170	105
Sudan	170	106	150	108	150	106
Myanmar	90	109	140	109	150	107
Solomon Islands	250	100	250	104	140	108
Afghanistan	150	107	160	107	140	109
Ethiopia	60	110	70	111	90	110
Cape Verde	200	103	220	106	N/A	111
Source: WHO.						