PAKISTAN TOBACCO COMPANY

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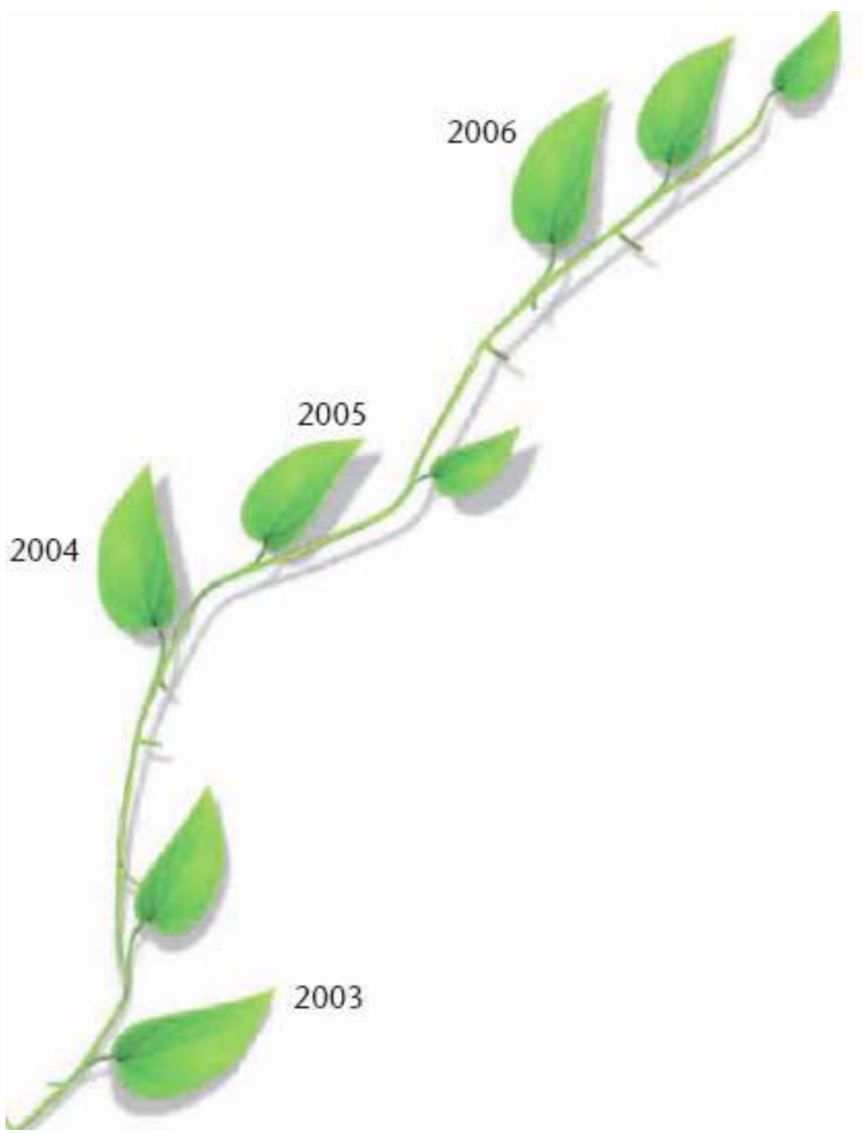
FINANCIAL ANALYSIS

FROM FY03-FY06



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Topic: Financial Analysis of Pakistan Tobacco Company

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PAKISTAN TOBACCO COMPANY

EXECUTIVE SUMMARY

Tobacco industry is a major contributor in the Pakistan economy. Although cultivation of tobacco is done on a small scale in Pakistan, it is a major source of revenue, employment and foreign exchange for the economy. Almost 80,000 people are employed in the cultivation of this crop.

Pakistan Tobacco Company is one of the key market players in this industry, and we hence decided to conduct our financial analysis on this company's liquidity and profitability, to know how and why. In order to do so, we started with the analysis of the industry as a whole and how this industry contributed to the Gross Domestic Product.

In order to analyze the company's internal health we first limited our analysis to FY03 till FY06, and made comparative financial statements of the balance sheet, profit and loss account and the income statement. We then carried out a Common Size Analysis, Trend Statement Analysis and Ratio Analysis of its Financial Statements. To gain a wider knowledge about the company in comparison with the industry, we chose another major company in the industry, namely, Lakson Tobacco Company comparing its profitability, short term liquidity and long term liquidity.

The analysis of the company is followed by a conclusion about the overall strength of the company and its position in the industry.

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CHAPTER#1

INDUSTRY OVERVIEW

"Usually we trust that nature has a master plan. But what was it she expected us to do with tobacco?"

- Bill Vaughan, Source: The penguin Dictionary of modern humorous quotes.

Smoking, though not good for health, is certainly good for numerous national economies around the world as source of employment and revenue, and Pakistan is no exception.

Tobacco industry, including growing, manufacturing, distribution and retailing, contributed 4.4% or over Rs.27.5 billion to the total GDP of Pakistan including Rs.15.17 billion and Rs.14.54 billion in excise duty and sales tax respectively, in 1997. It is the single biggest contributor of excise duty. 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.[1]

In FY05, PTC managed to become the market player, and widened this gap over their nearest competitor-namely, Lakson Tobacco Company-by 5.6%. The key drivers in this growth in volume were Gold Flake and Capstan.

In FY06, the overall tobacco industry grew by only 3%, while PTC grew by 13%, which is a great feat in itself to accomplish.

Recently, there has been a large anti-smoking campaign in Pakistan. Anti-tobacco campaigners accuse the government of being influenced by the tobacco industry. More than 90 per cent smokers are suffering from heart, lungs diseases, cancers and other diseases of serious nature and the ratio is rapidly increasing.

[1] http://www.pakistaneconomist.com/issue2000/issue31/i&e4.htm

The government of Pakistan has initiated many steps to decrease the ratio of smokers and protect youth from smoking, but in reality no steps have been taken. This is because the Pakistani government collects heavy taxes from the industry contributing a major portion to the government's income (approximately 27.5 billion rupees per year).[1]

Non duty paying cigarette manufacturers and the smuggled cigarettes result in loss for the government (tax revenue), cigarette manufacturing companies (sales revenue) and smokers (consuming sub standard cigarettes).

In 2006, the tobacco industry also faced many restrictions on advertisement and other regulatory issues. With the enforcement of FCTC(Framework Convention on Tobacco Control), more stringent regulations are being imposed.

HISTORY OF PAKISTAN TOBACCO COMPANY

Pakistan Tobacco Company Limited, a part of the British American Tobacco Group, took over the operations of the Imperial Tobacco Company of India in 1947, becoming the first multinational to establish itself in Pakistan. British American Tobacco, one of the world's most international business groups, has a position of market leader in more than 50 countries selling over 300 brands there.

It started its operations in Karachi near Karachi port and has come a long way. PTC is the largest excise tax generator in the private sector in the country. Over one million people are economically dependent on the industry in Pakistan.[2]

[1] http://www.yespakistan.com/people/tobacco.asp

[2]http://www.ptc.com.pk/OneWeb/sites/PAK_62VKZB.nsf/vwPagesWebLive/15C661D68814DD28C1256F070021D679?opendocument&SID=&DTC=

The share of the company in the excise duty of the country is 38 per cent of the total revenue of the country. Each cigarette manufactured by the company is taxed by 63 per cent of the total price. The company during financial year 2003-04 exported tobacco worth $7.2 billion.

Apart from being involved in cigarette production, PTC has greatly contributed towards the country's progress and development by introducing and using new and modern agricultural and industrial practices, thus benefiting the two sectors. The best farming practices of Pakistan Tobacco are now being applied to other crops such as sugarcane, wheat, cotton, rice, fruits and vegetables, thus improving productivity and economic growth at national level.

PTC has been supporting & contributing to various causes of national interest. Educating growers in the latest techniques and technology in agriculture, afforestation and free health care in designated areas are but a few examples.[1]

KEY ACTIVITIES

Pakistan Tobacco Company principal activities are to manufacture and market cigarettes and edible oils.[2]

COMPANY'S VISION

First choice for everyone

COMPANY'S MISSION

Transform PTC to perform with speed, flexibility and enterprising spirit of an innovative, consumer-based company.

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[1] http://www.ptc.com.pk/OneWeb/sites/PAK_62VKZB.nsf/vwPagesWebLive/FE1CB3D3BE7AD255C1256F0700247CB3?opendocument&SID=&DTC=

[2] http://www.business.com/directory/agriculture/horticulture_and_field_crops/tobacco/pakistan_tobacco_company_limited/

STRATEGIC OBJECTIVES

Higher operating margins, volume growth, level playing field and winning culture are defined at PTC as "must achieve objectives"

BRANDS IN PAKISTAN

The brands available in Pakistan are:

BENSON & HEDGES

JOHN PLAYER GOLD LEAF

PALL MALL

CAPSTAN

Embassy

GOLD FLAKE

DUNHILL

CHIEF BUSINESS

Cigarette manufacturing

COMPANY LISTINGS

The company is listed at Karachi, Lahore and Islamabad stock exchanges.

MAJOR COMPETITOR

Lakson Tobacco Company Ltd

AUDITORS

A.F. Ferguson & Co.

CORPORATE SOCIAL RESPONSIBILITY(CSR)

Pakistan Tobacco Company demonstrates responsible corporate conduct across all aspects of operations starting from marketing and consumer information to supporting sensible tobacco regulation; from respecting workplace employee rights and reducing environmental impacts as a consequence of their functional activities. In order to do so, it has recently started issuing its Social Report.

CHAPTER #2

The following figures are the Comparative **Balance Sheet**, Common Size **Balance Sheet** and the Trend Statement for FY03, FY04, FY05 and FY06.

	COMPARATIVE BALANCE SHEET			
	2006 000	2005 000	2004 000	2003 000
Current Assets				
Stocks	3,790,853	3,780,931	3,074,052	3,227,503
Stores and Spares	140,008	125,232	121,464	127,381
Trade debts	2,406	2,894	12,486	145,749
Loans and advances	12,205	32,676	32,273	62,826
Prepayments and other Receivables	164,595	136,778	155,129	243,875
Income tax refundable	-	-	-	4,050
Cash and bank balances	62,883	57,605	39,179	48,069
Total current assets	4,172,950	4,136,116	3,434,601	3,859,453
Non-current assets				
Property, Plant and Equipment	4,529,366	3,798,190	3,564,407	3,410,888
Long Term Investment in Subsidiary Company	5,000	5,000	5,000	5,000
Long Term Loans	18,660	17,782	16,324	16,481
Long Term Deposits and Payments	8,424	11,365	4,433	6,934
Total non-current assets	4,561,450	3,832,337	3,590,164	3,439,303
Total Assets	8,734,400	7,968,453	7,024,765	7,298,756
Less: Current Liabilities				
Trade and other payables	2,212,241	2,515,824	2,056,298	2272846
Interest accrued	11,115	10,911	5,041	11155
Short term finances	1,293,141	400,662	996,579	1,335,539
Income tax payable	233,712	676,969	79,549	-
Current portion of long term loans	-	-	-	200,000
Total Current Liabilities	3,750,209	3,604,366	3,137,467	3,819,540
Net Current Assets (Currents Assets - Current Liabilities)	422,741	531,750	297,134	39,913
Financed By:				
Share Capital				
Authorized Capital 300,000,000 ordinary shares of Rs.10 each	3,000,000	3,000,000	3,000,000	3,000,000
Issued Subscribed and Paid in Capital	2,554,938	2,554,938	2,554,938	2,554,938
Revenue Reserves	1,584,249	1,084,476	707,885	553,646
Shareholder's Equity	4,139,187	3,639,414	3,262,823	3,198,584
Deferred Taxation	845,004	724,673	624,475	370,623
Contingencies and Commitment				
	4,984,191	4,364,087	3,887,298	3,479,216

	COMMON-SIZE BALANCE SHEET			
	2006	2005	2004	2003
Current Assets				
Stocks	43.4	47.45	43.76	44.22
Stores and Spares	1.6	1.57	1.73	1.75
Trade debts	0.03	0.04	0.18	2
Loans and advances	0.14	0.41	0.46	0.86
Prepayments and other Receivables	1.88	1.72	2.21	3.34
Income tax refundable				0.06
Cash and bank balances	0.72	0.72	0.56	0.66
Total current assets	47.78	51.91	48.89	52.88
Non-current assets				
Property, Plant and Equipment	51.86	47.67	50.74	46.73
Long Term Investment in Subsidiary Company	0.06	0.06	0.07	0.07
Long Term Loans	0.21	0.22	0.23	0.23
Long Term Deposits and Payments	0.1	0.14	0.06	0.1
Total non-current assets	52.22	48.09	51.11	47.12
Total Assets	100	100	100	100
Less: Current Liabilities				
Trade and other payables	25.33	31.57	29.27	31.14
Interest accrued	0.13	0.14	0.07	0.15
Short term finances	14.81	5.03	14.19	18.3
Income tax payable	2.68	8.5	1.13	
Current portion of long term loans				2.74
Total Current Liabilities	42.94	45.23	44.66	52.33
Net Current Assets (Currents Assets - Current Liabilities)	4.84	6.67	4.23	0.55
Financed By:				
Share Capital				
Authorized Capital 300,000,000 ordinary shares of Rs 10 each	34.35	37.65	42.71	41.1
Issued Subscribed and Paid in Capital	29.25	32.06	36.37	35.01
Revenue Reserves	18.14	13.61	10.08	7.59
Shareholder's Equity	47.39	45.67	46.45	43.82
Deferred Taxation	9.67	9.09	8.89	5.08
Contingencies and Commitments				
	57.06	54.77	55.34	47.67

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	BALANCE SHEET TREND STATEMENT			
	2006	2005	2004	2003
Current Assets				
Stocks	117.45	117.15	95.25	100.00
Stores and Spares	109.91	98.31	95.35	100.00
Trade debts	1.65	1.99	8.57	100.00
Loans and advances	19.43	52.01	51.37	100.00
Prepayments and other Receivables	67.49	56.09	63.61	100.00
Income tax refundable				100.00
Cash and bank balances	130.82	119.84	81.51	100.00
Total current assets	108.12	107.17	88.99	100.00
Non-current assets				
Property, Plant and Equipment	132.79	111.35	104.50	100.00
Long Term Investment in Subsidiary Company	100.00	100.00	100.00	100.00
Long Term Loans	113.22	107.89	99.05	100.00
Long Term Deposits and Payments	121.49	163.90	63.93	100.00
Total non-current assets	132.63	111.43	104.39	100.00
Total Assets	119.67	109.18	96.25	100.00
Less: Current Liabilities				
Trade and other payables	97.33	110.69	90.47	100.00
Interest accrued	99.64	97.81	45.19	100.00
Short term finances	96.83	30.00	74.62	100.00
Income tax payable	-	-	-	100.00
Current portion of long term loans	-	-	-	100.00
Total Current Liabilities	98.18	94.37	82.14	100.00
Net Current Assets (Currents Assets - Current Liabilities)	1059.16	1332.27	744.45	100.00
Financed By:				
Share Capital				
Authorized Capital 300,000,000 ordinary shares of Rs 10 each	100.00	100.00	100.00	100.00
Issued Subscribed and Paid in Capital	100.00	100.00	100.00	100.00
Revenue Reserves	286.15	195.88	127.86	100.00
Shareholder's Equity	129.41	113.78	102.01	100.00
Deffered Taxation	228.00	195.53	168.49	100.00
	143.26	125.43	111.73	100.00

BALANCE SHEET

ASSETS:

Property Plant and Equipment: Property, plant and equipment form the major portion of the total assets at approximately 51%. PTC continues to invest heavily in fixed assets with the major investment in property, plant and equipment. The company spent Rs.1.2 billion (Rs.0.5 billion more than the last year) for acquiring latest machinery to facilitate up gradation in the technology footprint and to cater for increased demand.[1]

Another major change in plant is of net effect (inclusive of additions and deletions) Rs.343 million. The percentage that it forms of total assets is seen to fluctuate between 47%-50%.

Prepayments and Other Receivables: Other receivables have a declining trend throughout the four years from 2003-06. This is one of the reasons why PTC's cash receipts have increased in the same time period as mentioned above(could be seen in the cash flow statements).

Like Property, plant and equipment, there are slight variances in the amounts of the prepayments. Although they form a small share of the total assets, there significance is relevant to bring certainty in the continuing future operations of the corporation.

Stocks: The stocks as a percentage of totals assets have declined and in FY06 there has been a significant decrease of 39%. Conforming to this fact, the sales in the same year have increased considerably (income statement). The raw materials form the major part of the stocks which is good safety procedure to meet unsuspecting market situations.

Trade Debts: The Company has received major trade debts in the past years from its customers namely BAT Germany and BAT Singapore. In FY04 the trade debts decreased by 91% which is another major reason of increase in cash receipts. Another healthy sign is that t

[1] Pg.34 Directors Review Annual Report PTC 2006

PTC's doubtful accounts have remained constant meaning that the corporation did not incur any other bad debts.

Cash and Bank balances: There has been an upward trend in cash and bank balances in the last two years before which they were decreasing. A snapshot view of the notes indicates that PTC holds most of its cash in bank deposits which is common for most corporations.

Liabilities:

Trade and other Payables: There is a varying trend in this account. In FY06 PTC has cleared off 71% of its payable tobacco excise duty which has notably contributed in the 6% decrease in the trade and other payables account.

Short Term Finances: Short term finances are available under mark-up arrangements with the bank.[1] The important signal noticeable is that the mark-up rate is increasing every year by about 0.2-0.3% usually and in FY04 this rate has increased by 1%. But in FY05, short-term finances had declined considerably. Till it rose again to 4.25% in FY06.The good sign is that the company has reduced its short term finances.

Income Taxes Payable:

From FY04, income taxes payable rose to 9 times in FY05. The main reason is that the profit before tax has increased by 97% so accordingly a much higher income tax was charged.

Issued Subscribed and Paid in Capital:

Issued subscribed and paid up capital has remained the same throughout. This is because the number of common shares outstanding has remained the same, that is, 255,493,792.The total shareholder equity has increased due to an increase in retained earnings as a result of profitable operations.

[1] Note 24 PTC Annual Report 2006

We are now proceeding towards the financial analysis of the **Income Statement**. The following figures are the Comparative Statement, Common Size Statement and the Trend Statement.

	COMPARATIVE INCOME STATEMENT			
	2006 000	2005 000	2004 000	2003 000
Sales	35,715,451	30,615,062	25,452,634	
Sales Tax	4,833,285	4,103,324	3,413,146	
Turnover (net of sales tax)	30,882,166	26,511,738	22,039,488	22,572,247
Cost of Goods Sold	25,348,646	21,982,134	18,556,867	19,700,706
Gross Profit	5,533,520	4,529,604	3,482,621	2,871,541
Operating Expenses				
Marketing and distribution expense	1,824,048	1,578,656	1,442,356	1,466,095
Administrative expense	661,271	573,285	595,637	395,178
	2,485,319	2,151,941	2,037,993	1,861,273
Operating Profit	3,048,201	2,377,663	1,444,628	1,010,268
Other income	68,088	34,417	14,590	6,717
Other expenses	204,556	284,665	366,637	310,335
	2,911,733	2,127,415	1,092,581	706,650
Finance cost	51,060	45,351	36,542	91,955
Profit before taxation	2,860,673	2,082,064	1,056,039	614,695
Tax charge	955,685	760,145	390,812	293,614
Profit after taxation	1,904,988	1,321,919	665,227	321,081
Earning per share (Rupees)	7.46	5.17	2.60	1.26

	TREND STATEMENT OF INCOME STATEMENT			
	2006	2005	2004	2003
Turnover (net of sales tax)	136.81	117.45	97.64	100
Cost of Goods Sold	128.67	111.58	94.19	100
Gross Profit	192.70	157.74	121.28	100
Operating Expenses				
Marketing and distribution expense	124.42	107.68	98.38	100
Administrative expense	167.33	145.07	150.73	100
	133.53	115.62	109.49	100
Operating Profit	301.72	235.35	142.99	100
Other income	1013.67	512.39	217.21	100
Other expenses	65.91	91.73	118.14	100
	412.05	301.06	154.61	100
Finance cost	55.53	49.32	39.74	100
Profit before taxation	465.38	338.71	171.80	100
Tax charge	325.49	258.89	133.10	100
Profit after taxation	593.30	411.71	207.18	100

	COMMONSIZE INCOME STATEMENT			
	2006	2005	2004	2003
Turnover (net of sales tax)	100.00	100.00	100.00	100.00
Cost of Goods Sold	82.08	82.91	84.19	87.28
Gross Profit	17.92	17.09	15.80	12.72
Operating Expenses				
Marketing and distribution expense	5.91	5.95	6.54	6.50
Administrative expense	2.14	2.16	2.70	1.75
	8.05	8.12	9.41	8.25
Operating Profit	9.87	8.97	6.55	4.48
Other income	0.22	0.13	0.07	0.03
Other expenses	0.66	1.07	1.66	1.37
	9.43	8.02	4.96	3.13
Finance cost	0.17	0.17	0.17	0.40
Profit before taxation	9.26	7.85	4.79	2.72
Tax charge	3.09	2.87	1.77	1.30
Profit after taxation	6.17	4.99	3.02	1.42

INCOME STATEMENT

Turnover

In view of the sale performances during the past four years, the sales (net of sales tax) have increased with the exception of FY04 in which they witnessed a slight decline of 2.36%. However, even in this year the net profit saw an increase. In FY05 PTC benefited from a record sales volume of 30.6 billion sticks. This trend continued in to FY06 with 13% higher sales which resulted in the sale of 34.5 billion sticks. The major contributors of the sales are the brands Gold Flake, Capstan and Gold Leaf respectively.

Cost of Goods Sold

The cost of sales has an upward trend in value but it has decreased as a percentage of sales which is an encouraging sign. The increase is primarily due to economies of scale. For example in FY06, the nominal increase in per unit cost was 2% higher than the previous year. Furthermore, this minor increase was due to effective supply chain management. According to an international survey on supply chain carried out in FY06 by the Performance Management Group, PTC was rated as "Best in Class" in terms of total supply chain cost among its peer companies across the globe. [1]

Gross Profit

PTC is having an exceptional performance due to which it is experiencing a consistent increase in its Gross Profit and according to Director's Review the increase in Profits was due to increase in sales volume, improved margins and effective cost controls in all areas.[2]

Operating Expenses:

Despite the continuous increase in government restrictions on marketing and advertisement, PTC has never been shy to invest behind its brands and people. This can be seen from its marketing expenses which have grown steadily every year. PTC's marketing expense grew

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[1] Director's Review (Cost of Sales) PTC Annual Report FY06
[2] Director's Review Annual Report FY06

from Rs.1579 million in FY05 to Rs.1824 million in FY06, showing an increase of 16% against SPLY.[1]

The company's expenses have increased which can be seen from the trend statement. This is due to the increase in administrative expenses which is because of increased investment, expenses related to BPRs and bonuses given to employees. Nevertheless, in FY05, the administrative expenses were lowered by 4% as compared to FY04 which included SAP implementation costs which were offset by higher donations mainly for earthquake relief activities.[2]

Other Income

Other income follows an upward trend. The main reason is that the short term bank deposits have increased. This results in a higher interest income. There are other factors which affect other income such as gain of sale of assets but they only form a minor part of the total value of this head.

Other Expenses

Other Expenses only increased in FY04 as the company laid off 270 of its employees. This can be seen from the notes and the director's review. In the notes these lay-offs are termed staff separation costs. The staff separation costs decreased in FY05 as the workforce was further reduced by 70 employees in the year. The staff separation costs are finally reduced to a nil value in FY06 as PTC did not lay off any employees in this year.

Tax Charges

PTC's consistently enhanced sales and financial performance has resulted in a significant increase in the government's revenue. The tax charge has gone up by 225% from FY03 to FY06. As in FY06, PTC contributed Rs.23 billion to the national exchequer in terms of excise duty, sales tax, income tax etc.

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[1] Director's Review Annual Report FY06
[2] Director's Review Annual Report FY05

Years	Industry Contribution		PTC Contribution	
	Rs in Billion	Growth	Rs in Billion	Growth
2000	18	12%	10	13%
2002	21	17%	13	30%
2004	25	19%	16	23%
2006	31	24%	22	38%

(Contribution by PTC and the Industry to the Governtment Exchequer)

Figure taken from annual report FY06.

Net Income:

Net income has grown much faster than sales. This is because the company has benefited from operative and administrative efficiencies and in reducing their cost of production which resulted in lower cost and expenses per-rupee of sales. This can be observed from the Common Size Statement.

Figure taken from annual report FY06

PAKISTAN TOBACCO COMPANY

The following figures are the Comparative, Common Size and Trend Statements of the

COMPARATIVE CASH FLOW STATEMENT

	2006.00	2005.00	2004.00	2003.00
Cash Flow from Operating Activities				
Cash receipts from costomer	35715939.00	30624654.00	25585897.00	22519584.00
Cash paid to the Government for Federal Excise Duty, Sales Tax and other Levies	(22134488.00)	(19126208.00)	(16021304.00)	(14309453.00)
Cash paid to suppliers	(8850492.00)	(7795529.00)	(6450403.00)	(5534395.00)
Cash paid to employees and retirement funds	(1750686.00)	(1400619.00)	(1465490.00)	(1266329.00)
Income tax paid	(1278610.00)	(62527.00)	(53370.00)	(46299.00)
Other cash receipts / (payments)	9646.00	(1070.00)	42369.00	(28693.00)
Net cash outflow from operating activities	1711309.00	2238701.00	1637699.00	1334415.00
Cash Flow from Investing Activities				
Purchase of property, plant and equipment	(1238014.00)	(716852.00)	(597702.00)	(854107.00)
Proceeds from sale of property, plant and equipment	37755.00	42815.00	38027.00	23585.00
Cash paid to subsidiary company	(420.00)	(476.00)	(620.00)	(539.00)
Net cash outflow from investing activities	(1200679.00)	(674513.00)	(560295.00)	(831061.00)
Cash Flow from Financing Activities				
Repayment of long term loans	-	-	(200000.00)	(370000.00)
Dividend paid	(1402017.00)	(943649.00)	(507318.00)	(203960.00)
Financial charges paid	(43216.00)	(32531.00)	(42656.00)	(120863.00)
Long term loans, deposits and prepayments	-	-	2658.00	1479.00
Interest received	47402.00	26317.00	-	-
Net cash outflow from financing activities	(1397831.00)	(949863.00)	(747316.00)	(693344.00)
Net (Decrease)/ Increase in Cash and Cash Equivalents	(887201.00)	614325.00	330088.00	(189990.00)
Cash and Cash Equivalents at January 1	(343057.00)	(957382.00)	(1287470.00)	(1097480.00)
Cash and Cash Equivalents at December 31	(1230258.00)	(343057.00)	(957382.00)	(1287470.00)
Cash and Cash Equivalents Comprise:				
Cash and bank balances	62883.00	57605.00	39197.00	48069.00
Short term finances	(1293141.00)	(400662.00)	(996579.00)	(1335539.00)
	(1230258.00)	(343057.00)	(957382.00)	(1287470.00)

	Common Size Cash Flow Statement			
	2006.00	**2005.00**	**2004.00**	**2003.00**
Cash Flow from Operating Activities				
Cash receipts from costomer	115.65	115.51	116.09	99.77
Cash paid to the Government for Federal Excise Duty,	(71.67)	(72.14)	(72.69)	(63.39)
Sales Tax and other Levies				
Cash paid to suppliers	(28.66)	(29.40)	(29.27)	(24.52)
Cash paid to employees and retirement funds	(5.67)	(5.28)	(6.65)	(5.61)
Income tax paid	(4.14)	(0.24)	(0.24)	(0.21)
Other cash receipts / (payments)	0.03	(0.00)	0.19	(0.13)
Net cash outflow from operating activities	5.54	8.44	7.43	5.91
Cash Flow from Investing Activities				
Purchase of property, plant and equipment	(4.01)	(2.70)	(2.71)	(3.78)
Proceeds from sale of property, plant and equipment	0.12	0.16	0.17	0.10
Cash paid to subsidiary company	(0.00)	(0.00)	(0.00)	(0.00)
Net cash outflow from investing activities	(3.89)	(2.54)	(2.54)	(3.68)
Cash Flow from Financing Activities				
Repayment of long term loans	-	-	(0.91)	(1.64)
Dividend paid	(4.54)	(3.56)	(2.30)	(0.90)
Financial charges paid	(0.14)	(0.12)	(0.19)	(0.54)
Long term loans, deposits and prepayments	-	-	0.01	0.01
Interest received	-	-	-	-
Net cash outflow from financing activities	(4.53)	(3.58)	(3.39)	(3.07)
Net (Decrease)/ Increase in Cash and Cash Equivalents	(2.87)	2.32	1.50	(0.84)
Cash and Cash Equivalents at January 1	(1.11)	(3.61)	(5.84)	(4.86)
Cash and Cash Equivalents at December 31	(3.98)	(1.29)	(4.34)	(5.70)
Cash and Cash Equivalents Comprise:				
Cash and bank balances	0.20	0.22	0.18	0.21
Short term finances	(4.19)	(1.51)	(4.52)	(5.92)

TREND STATEMENT CASH FLOW				
	2006	2005	2004	2003
Cash Flow from Operating Activities				
Cash receipts from costomer	158.59	135.99	113.62	100
Cash paid to the Government for Federal Excise Duty,	154.68	133.66	111.96	100
Sales Tax and other Levies				
Cash paid to suppliers	159.92	140.86	116.55	100
Cash paid to employees and retirement funds	138.25	110.6	115.73	100
Income tax paid	2761.64	135.05	115.27	100
Other cash receipts / (payments)	133.62	-3.73	247.66	100
Net cash outflow from operating activities	128.24	167.77	122.73	100
Cash Flow from Investing Activities				
Purchase of property, plant and equipment	144.95	83.93	69.98	100
Proceeds from sale of property, plant and equipment	160.08	181.53	161.23	100
Cash paid to subsidiary company	77.92	88.31	115.03	100
Net cash outflow from investing activities	144.48	81.16	67.42	100
Cash Flow from Financing Activities				
Repayment of long term loans	-	-	54.05	100
Dividend paid	687.39	462.66	248.73	100
Financial charges paid	35.75	26.92	35.29	100
Long term loans, deposits and prepayments	-	-	179.72	100
Interest received	180.12	100	-	-
Net cash outflow from financing activities	201.61	136.99	107.78	100
Net (Decrease)/ Increase in Cash and Cash Equivalents	466.97	423.35	273.74	100
Cash and Cash Equivalents at January 1	31.26	87.23	117.31	100
Cash and Cash Equivalents at December 31	95.56	26.65	74.36	100
Cash and Cash Equivalents Comprise:				
Cash and bank balances	130.82	119.84	81.54	100
Short term finances	96.83	30	74.62	100
	95.56	26.65	74.36	100

CASH FLOW

Cash Flow from Operating Activities:

Net cash outflow from Operating Activities was highest in FY05 amounting to Rs.223 million following a decline of 23.557% in FY06 w.r.t. FY05, mainly due to higher income tax, dividends payment and capital expenditure.

Cash receipts from customers increased by 58.59% in FY06 from FY03. The total increase in cash receipts is due to an increased turnover, visible from the trend statement of the profit and loss account showing an increase in of 36.81% in FY06 w.r.t. FY03. Another reason accounting for this increase was the collection of most of its trade debts in FY05 following a slight decrease in FY06. (Note 19 Annual Report 2006) In the tobacco industry, the sales are done on a cash basis; rather than on account from customers. Loans and other receivables seldom occur.

PTC is in favor of paying complete taxes and has always been emphasizing in restricting the laws on the collection of taxes to tackle the tax evaded sector. There has always been an upward trend in the income taxes paid by the company but in FY06 PTC paid the highest income tax of its history of worth 1.28 billion, 21.44% more than the previous year mainly due to strict government regulations and also due to increased turnover.

Cash Flow from Investing Activities:

Net cash outflow from Investing Activities was increased in FY06 which can be seen from the trend statement. This is due to purchases in property, plant and equipment. The company spent 1.2 billion for acquiring latest machinery. So this year the company has invested more to modernize its plant, possibly relying more on technology because it laid off many of its employees in the previous year. The upward trend is seen from the following values starting from FY04 of Rs.271 million following into FY05 of Rs.586 million and finally to Rs.1.2 billion in FY06[1] mainly due to the company's decision to modernize its plant and equipment every year.

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[1] Director's Review of respective years.

Cash Flow from Financing Activities:

Net cash flow from Financing Activities has decreased by 101.61% from FY03 to FY06. A major contributor in this decrease was the increase in dividends paid. The company announced dividends in FY04, FY05 and FY06 with the exception of FY03. In the Comparative Cash flow we see that dividends paid amounted to Rs.203 million which were the dividends payable of previous years.

Another reason accounting for the increase in net cash flow from financing activities was because the company's long term loans, deposits and prepayments were extinguished, hence reducing prospect cash inflow in both FY05 and FY06.

DIVIDENDS APPROPRIATED (Rs MILLION)

FY06	FY05	FY04	FY03
766	639	307	-

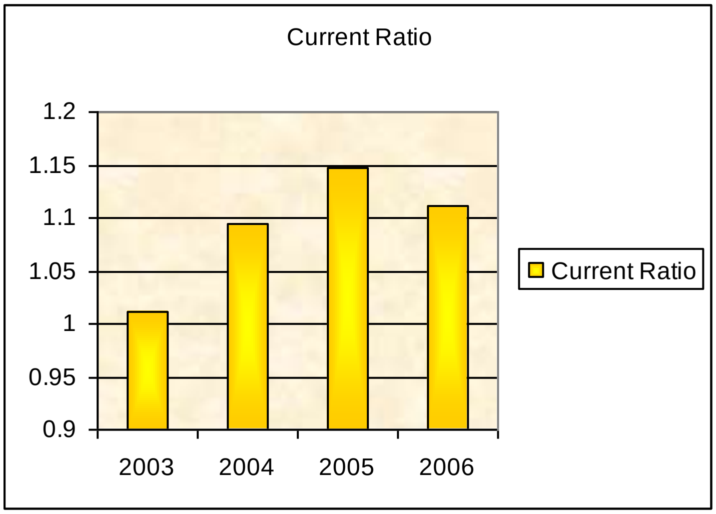
CHAPTER # 3

		2006	2005	2004	2003

MEASURES OF SHORT-TERM LIQUIDITY					
Current Ratio		1.11	1.14	1.09	1.01
Quick Ratio		0.045	0.055	0.065	0.121
Working Capital		422741	531750	297134	39913
Net cash provided from operating activities		1,711,309	2,238,701	1,637,699	1,334,415
Cash flows from operations to current liabilities		46.00	62.00	52.00	35.00
Inventory turnover rate		6.50	6.20	5.70	
Days to sell the average inventory		56	58	64	
Free cash flow		(255,370)	925,188	1,292,371	
MEASURES OF LONG-TERM CREDIT RISK					
Debt ratio		0.42	0.452	0.44	0.52
Interest coverage ratio		110.00	93.04	68.00	12.90
MEASURES OF PROFITABILITY					
Gross profit rate		17.91	17.09	15.80	12.72
Operating expense ratio		9.29	7.55	7.70	10.68
Earnings per share		7.46	5.17	2.60	1.26
Return on Assets		36.49	31.71	20.17	
Operating Profit Margin		9.87	8.97	6.55	
Asset Turnover		3.69	3.54	3.08	
Return on Equity		48.98	38.30	30.35	

Measures of short term liquidity

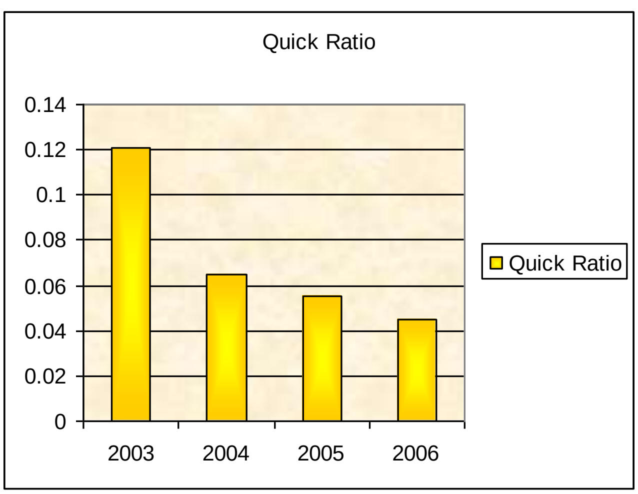
Current Ratio



Current ratio is current assets divided by current liabilities. Current ratio of the company increased from 1.0(FY03) to 1.09(FY04). It has then increased in FY05 and then declined again in FY06. This means that for every 1 rupee of current liabilities the company has 1.1 rupees of current assets, i.e. the company's current assets are 1.1 times larger than its current liabilities. Though this ratio is not high but still the company's debt-paying ability is good as it is in a strong financial position and thus qualifies as a good credit risk.

Quick Ratio

Quick ratio also called the acid-test ratio; another measure of short-term liquidity is often preferred to the current ratio as it compares only the most liquid current assets called quick assets with current liabilities.

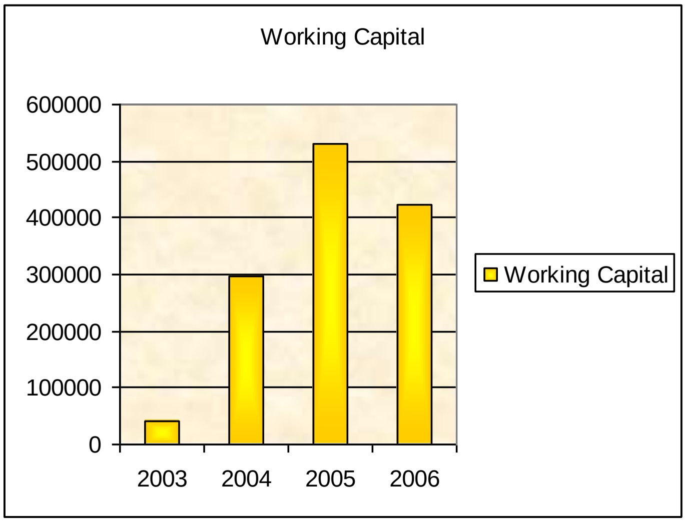


Quick assets, the assets that can be readily converted into cash include cash, accounts receivable and marketable securities.

The quick ratio of the company decreased from 0.12(FY03) to 0.06(FY04) and to 0.05(FY05). In FY06 it then declined to 0.045. The quick ratio of the company declined because the company is continuously investing in its plant and equipments which is increasing the balance of the current liabilities as not all payments are paid up immediately in cash. In FY04 there was a major decline in the ratio. it was further decreased in FY05. This change has been due to the reason that from 2003 to 2005 the accounts receivables and trade debts have decreased, thereby reducing the quick ratio.

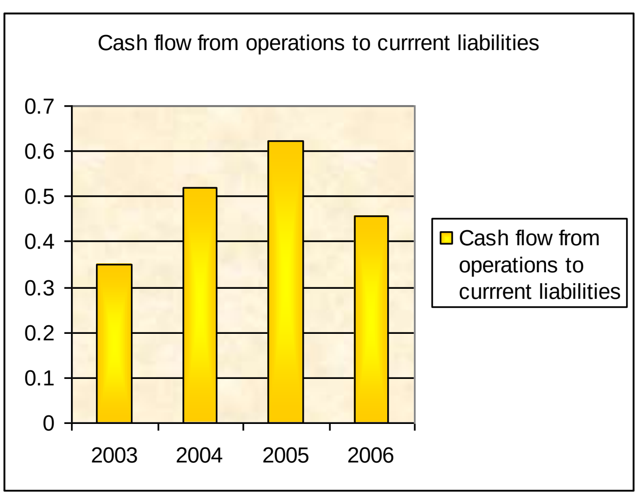
Working Capital

Working capital is current assets minus current liabilities. The working capital has increased from FY03-05. In FY03 it was Rs.39913, in FY04 it was Rs.297134 and then Rs.531750 in FY05. The reason working capital increased in FY04 was due to the increase in sales while the increase in FY05 was due to increase in current assets, mainly the stocks. In FY06 the working capital again decreased. In FY06 the working capital decreased because of the increase in current liabilities. The decrease in FY06 is not such a worrying sign even for short term creditors since the current ratio provides a better measure for short term liquidity which is still more than 1.



Cash flow from operations to current liabilities

Cash flow from operations to current liabilities has shown an increasing trend from FY03 to FY05. It increased from 35% to 52% and then to 62% in all these years. In FY06 it decreased to 46%. This means that the ability of the company to generate cash from its operating activities to fulfill its current liabilities was strong and kept increasing



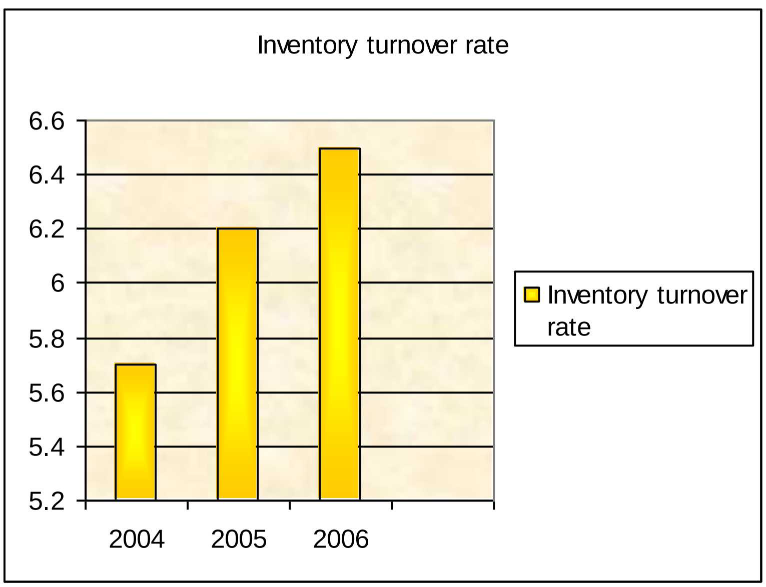
from FY03 to FY05 but has decreased in FY06 due to the decline in net cash outflow from operating activities in FY06.

Net cash outflow from operating activities

Net cash outflow from operating activities increased from FY03 to FY05 from Rs. 1334415 to Rs. 2238701. This is because the cash receipts from customer increased during these years. In FY06, however, this amount decreased to Rs. 1711309 because cash paid to government for Federal excise duty and the amount of income tax was much greater in FY06 than the previous years.

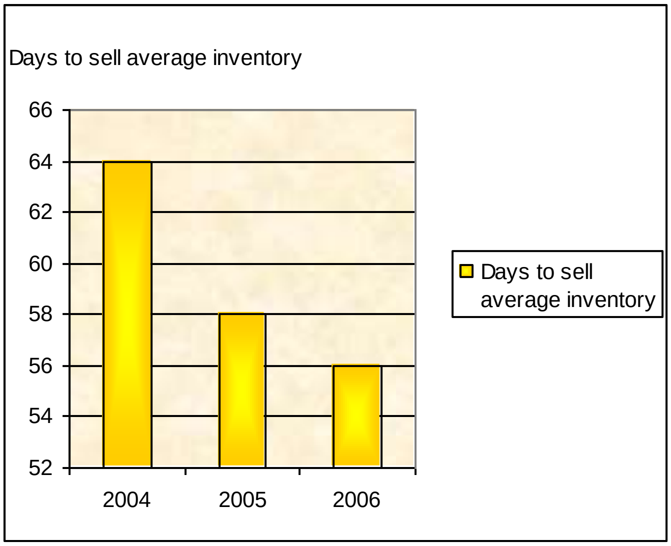
Inventory Turnover Rate

The inventory turnover rate tells how many times during the year the company is able to sell a quantity of goods equal to its average inventory.



This rate increased from 5.7 in FY04 to 6.2 in FY05 to 6.5 in FY06 which is an encouraging sign since it shows how quickly PTC is selling its inventories, specifically 6.5 times.

Days to sell average inventory

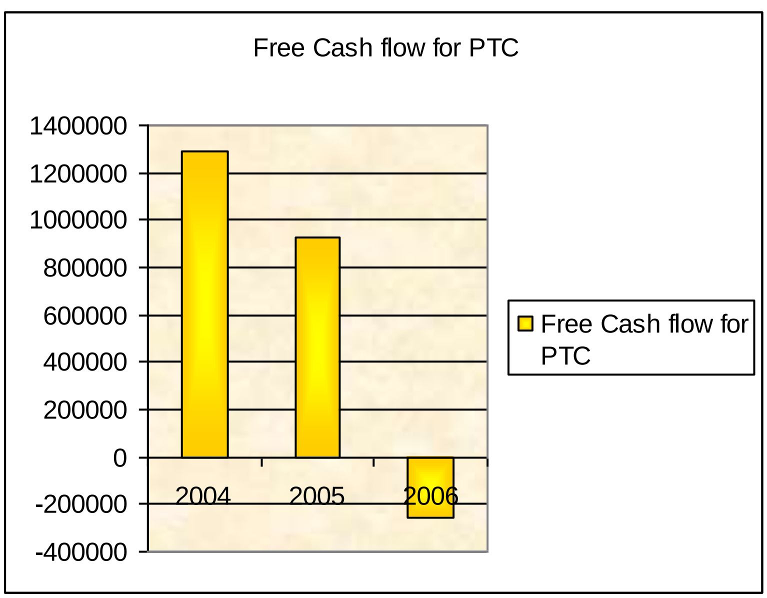


While looking at this ratio it can be said that PTC is improving its inventory management as the figures are showing that with every year there is a decrease in this ratio which is a good sign.

Free Cash Flow

Free Cash flow is the excess of operating cash flow over basic needs. Company's free cash flow had a downward trend from FY04 to FY06. It is mainly due to the following reasons:

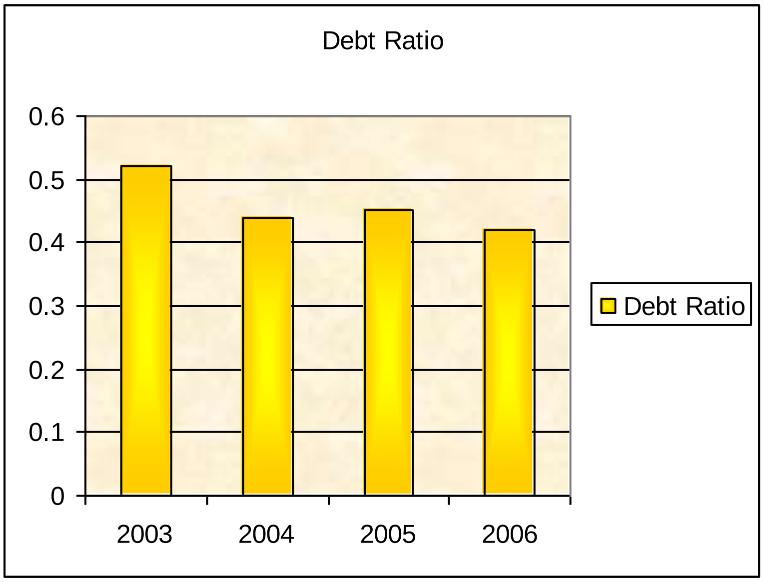
1. The Company is continuously paying its dividends
2. PTC is carrying on with its enormous investments in its plants and equipments.
3. PTC continues to pay rapidly increasing tax amounts.



Measures of Long Term Credit Risk

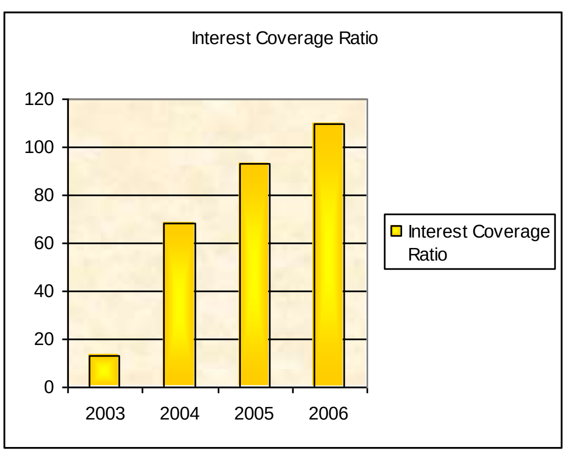
Debt Ratio

Debt ratio expresses what part of the firm's resources is obtained by borrowing and what part is invested by owners.

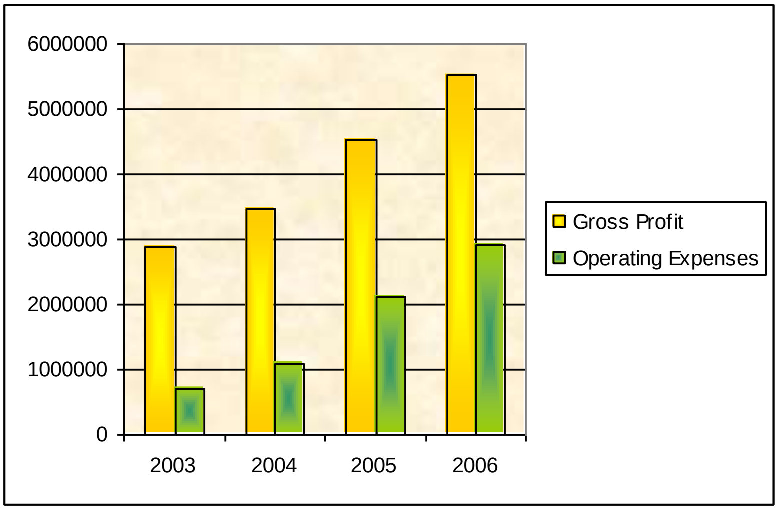


The debt ratio or the percentage of assets financed by debt decreased in FY04 in comparison to FY03, then increased slightly in FY05 and again decreased in FY06. This is a positive sign as it indicates falling amounts of liabilities.

Interest coverage ratio



Interest coverage ratio has increased significantly throughout the years from 12.9 in FY03 to 110 in FY06. The major increase in this ratio occurred in FY04 when interest coverage ratio increased from 12.9 to 68 because the annual interest expense decreased from Rs. 78366 to Rs. 21265, a decrease of 73%.

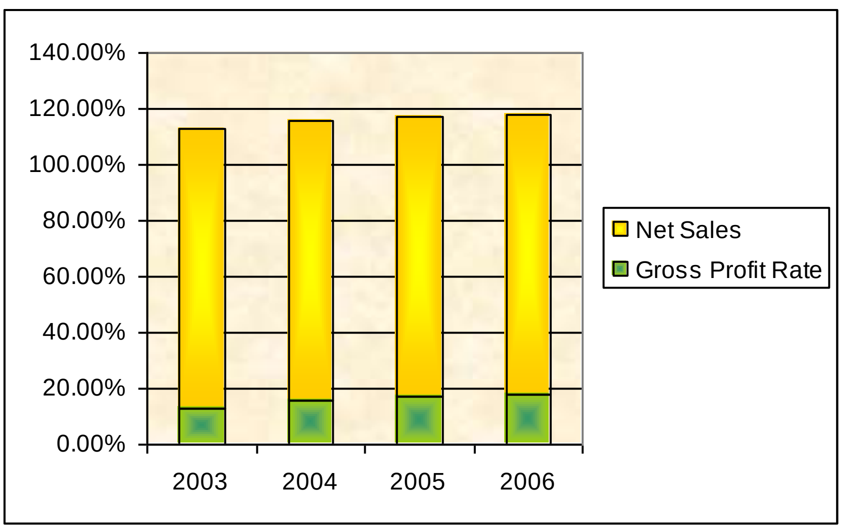


The reason for the increase in the ratio for the remaining years was the increase in operating income that occurred because of a continuous greater increase in gross profit. PTC has improved its ability to meet its interest payment obligations. An interest coverage ratio of 110 indicates for every one rupee obligation of interest, PTC has Rs. 110 available. PTC provides a strong credit risk position for long term creditors.

Measures of Profitability

Gross Profit Rate

Gross Profit is a measure of the profitability of a company's product.



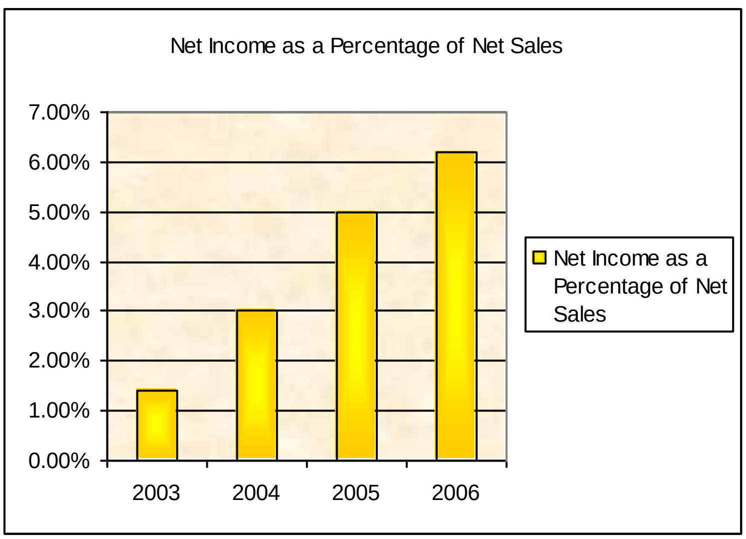
The gross profit rate has been increasing in all the years presented by means of the graph, from 12.7 in FY03 to 17.9 in FY06. This is because the company's sales have been increasing and the cost of goods sold has been decreasing as a percentage of net sales which can be seen from the common size income statement.

Operating Expense Ratio:

Operating expense ratio shows the ability of management to control expenses. The lower the operating expense ratio the better it is for PTC. This ratio increased from 8.2% to 9.2% from FY03-04. It then decreased to 8.1% and then to 8% in FY05 and FY06 respectively. The increase in FY04 was due to the increase in marketing expense. For other years, net sales increased significantly thus decreasing the operating expense ratio which is a positive indicator for PTC.

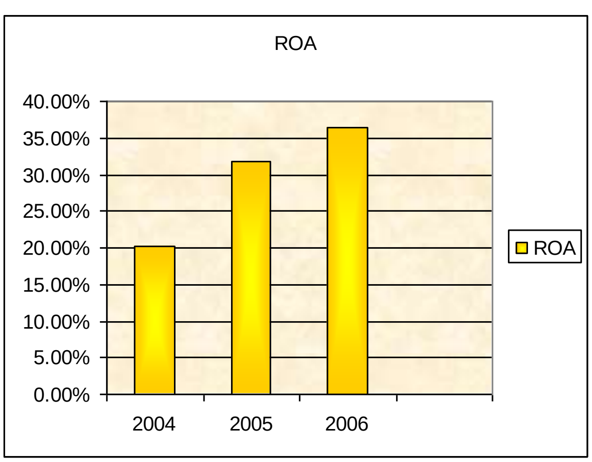
Net income as a percentage of net sales:

This ratio is an indicator of management's ability to control costs. Net income as a percentage of net sales increased throughout the last four years from 1.4% in FY03 to 6.2% in FY06 showing the growing ability of PTC to better control its cost.



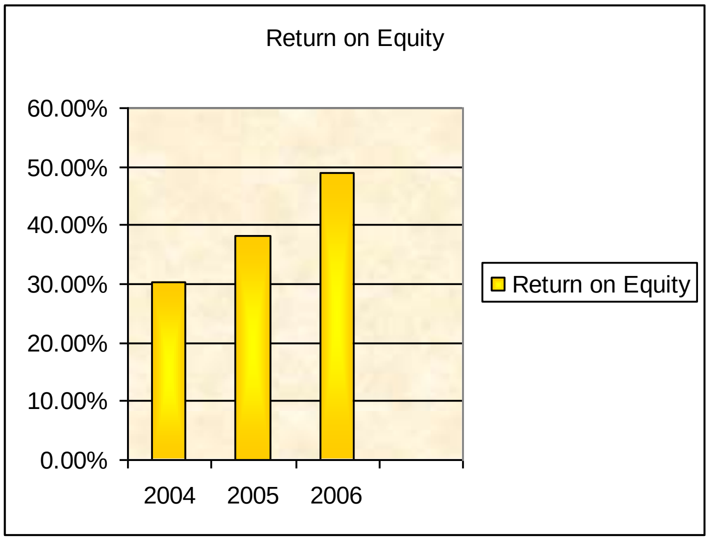
Return on assets:

ROA is the measure of the productivity of assets, regardless of how the assets are financed. Returns on funds supplied from all sources, has been increasing from 20.2% in FY04 to 31.8% in FY05 and to 36.5% in FY06. This is because operating income and average



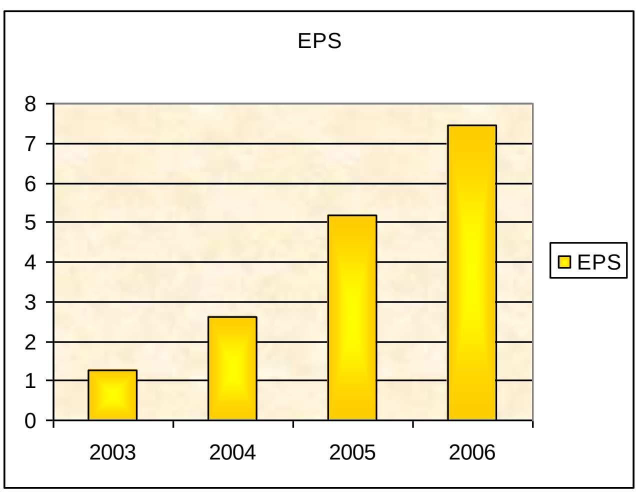
total assets have both been increasing all these years.

Return on equity:



ROE is the rate of return earned on the stockholder's equity in the business. It has increased from 30.35% in FY04 to 38.30% in FY05 to 48.98% in FY06. Although average total equity increased slightly, it was the large increase in net income that brought about the increase in ROE. Since ROE is increasing and in FY06 it has reached to 48.98% it is a very good sign for shareholders.

Earnings per share:

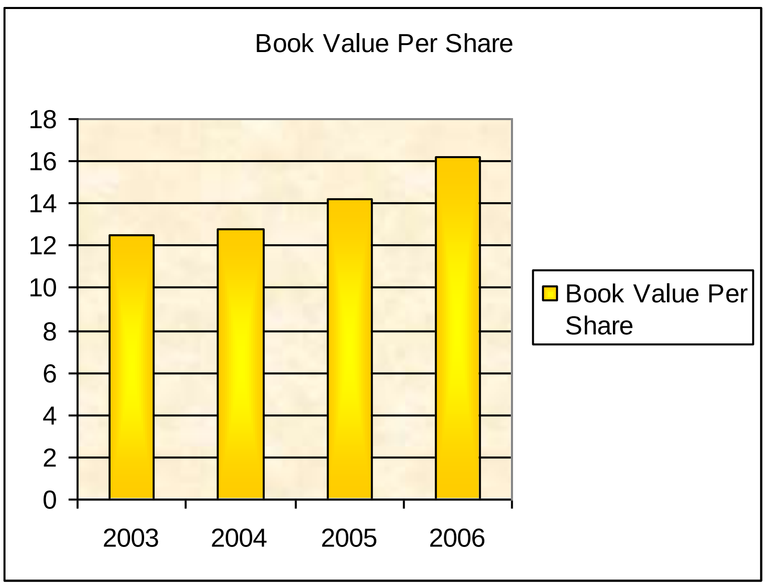


EPS is net income expressed on a per-share basis. EPS has increased significantly from 1.26 to 2.60 then to 5.17 and then finally to 7.46 from FY03-06. Although the number of shares outstanding has remained constant it is the increase in net income that is responsible for the increasing EPS.

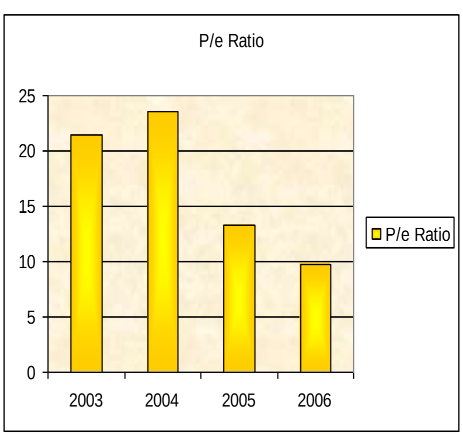
Measures to evaluate the market price of common stock:

Book value per-share:

It is the recorded value of net assets underlying each share of common stock. Book value per-share has increased from 12.5 to 12.8 and then to 14.2 from FY03 to FY05. In FY06 it increased to 16.2. This means that for every one share PTC's book value for it is 16.2 in FY06 which is a positive indication since the value of net assets for each share is increasing.



Price Earnings Ratio



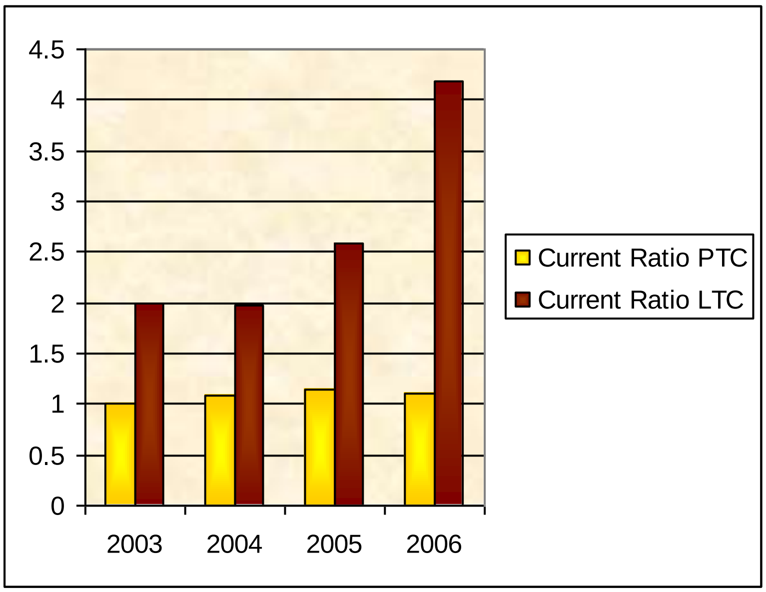
The price earnings ratio is determined by dividing the market price per share by the annual earnings per share. The p/e ratio increased from FY03 when it was 21.4 to 23.6 in FY04. it then decreased to 13.3 in FY05 and then to 9.7 in FY06.

CHAPTER #4

We now compare the various ratios of PTC with its competitor, LTC.

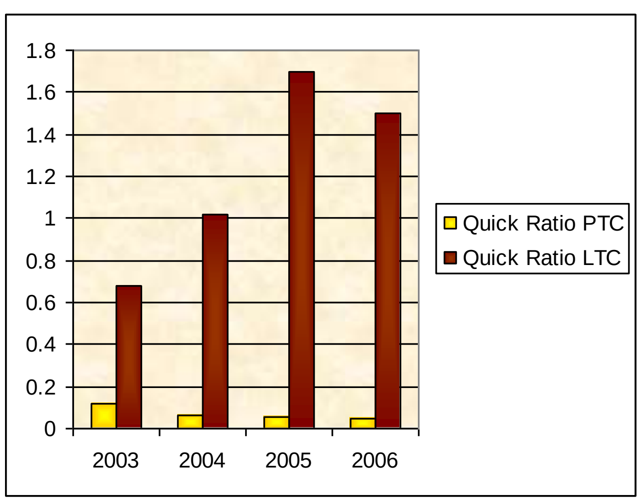
Current Ratio

Current Ratio of LTC is about four times higher than PTC in the current year. This is mainly due to the fact that although the current assets of PTC are increasing but on the other hand its current liabilities have always remained higher than LTC. In FY06 for example, the current liabilities of PTC were about 350% higher compared to LTC. As for every 1 rupee of current liabilities LTC has 4 rupees of current assets available while PTC has just 1.1.



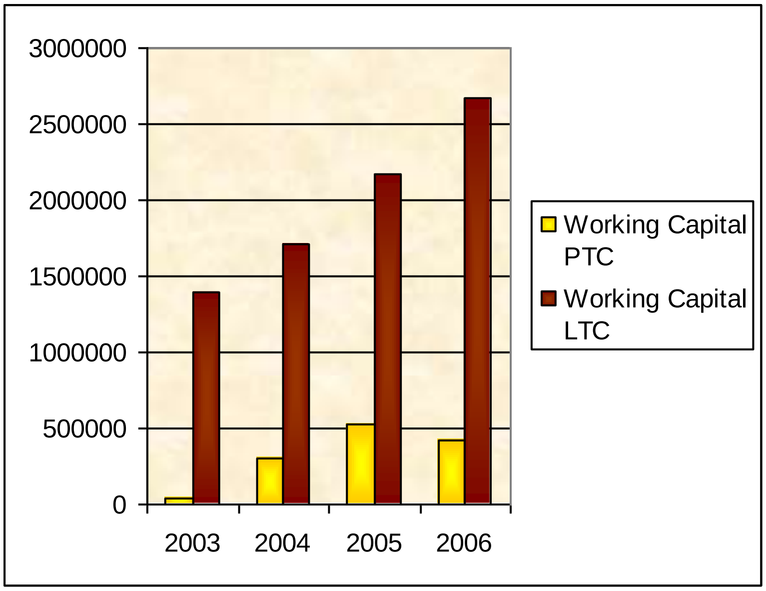
Quick Ratio

Quick Ratio of LTC has always remained higher than that of PTC. The reason is not due do a major difference in current assets, but, as also given in the explanation earlier in the current ratio, PTC's current



liabilities are a great deal higher than LTC.

Working Capital

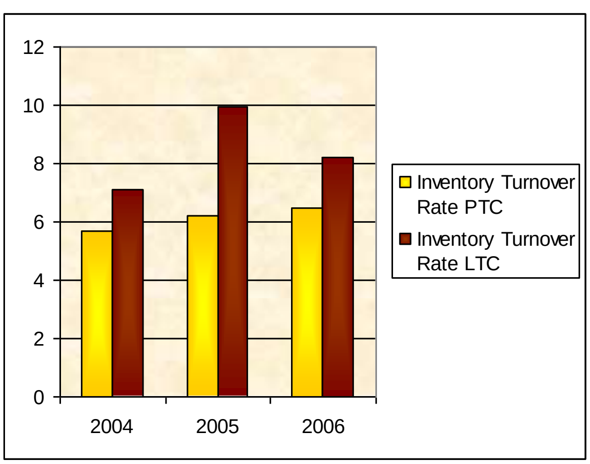


The working capital of LTC is much higher than PTC. This simply gives another view of picture provided by the current ratio.

Days to collect average account receivables

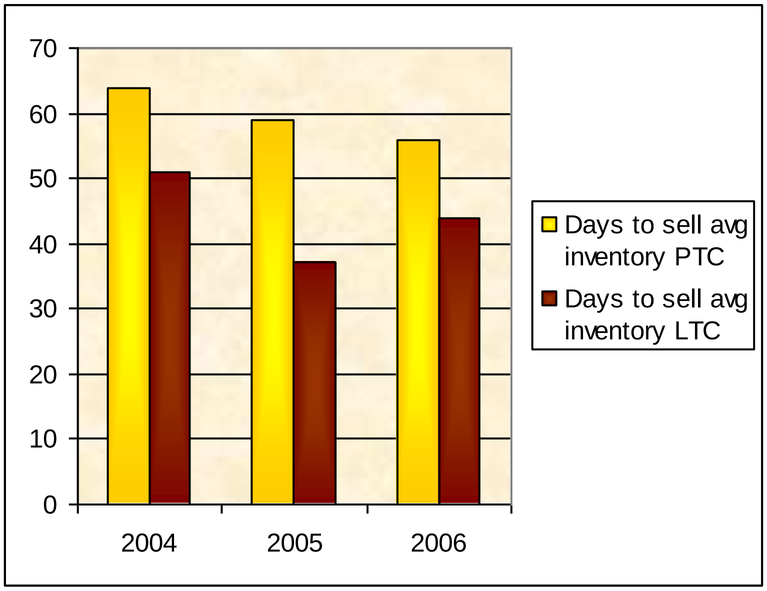
This ratio is not significant or relevant enough due to the nature of the tobacco business as the payments of cigarette packs are made on a cash basis.

Inventory Turn-over rate:



While analyzing the trend of this ratio it can be inferred that PTC is progressing in terms of its inventory turn-over as it is coming closer to that of LTC's in FY06 due to higher sales compared to LTC.

Days to sell average inventory

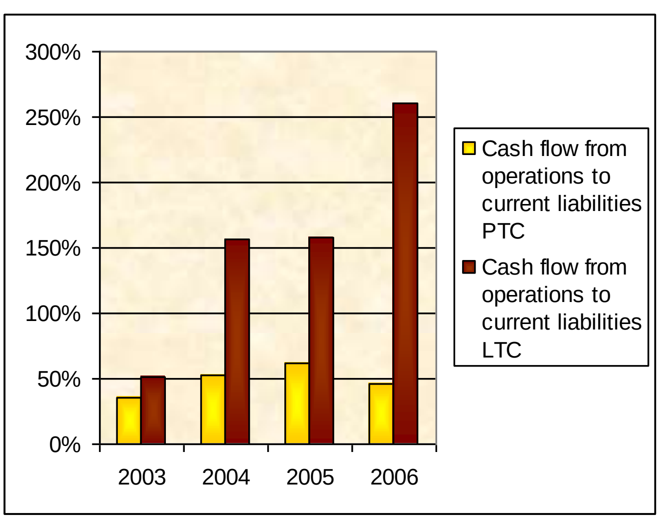


It is evident from the graph that there is a downward trend in the days to sell average inventory for PTC and compared to this the same sum for LTC has increased in FY06. However LTC still has an edge since it still takes fewer days to sell off its inventory. This is not such a worrying sign since the trend shows PTC's improving ability of better inventory management.

Operating Cycle

The operating cycle for both companies is basically the number of days it takes to sell their average inventories because the days to collect accounts receivable is almost negligible due to the nature of the business.

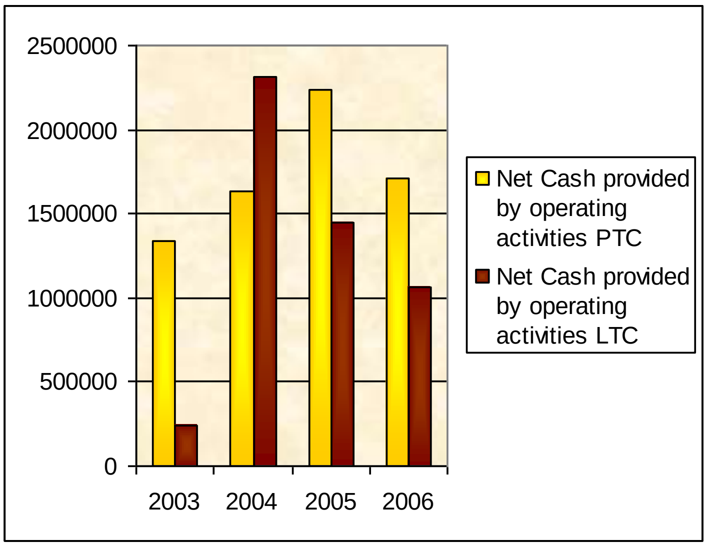
Cash flow from operations to current liabilities



Cash flow from operations to current liabilities is less than of LTC as compared to PTC mainly due to the reason that the current liabilities of PTC are higher than of LTC in all years but this ratio has declined in FY06 due to the reason that company has paid much more income taxes as compared to the previous years which has declined its operating cash flow. Nonetheless, it is pretty obvious, that LTC's condition is exceptional with respect to the ability to pay off its current liabilities. LTC's 260% of operating cash flows to current liabilities shows that for every one rupee of current liability, LTC has Rs.260 available.

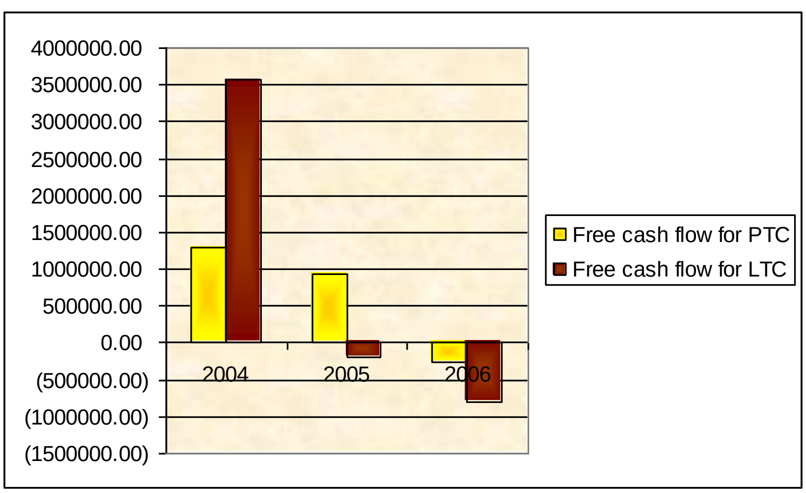
Net Cash provided by operating activities

The net cash flow provided by operating activities has witnessed the greatest increase in 2005.



Net cash provided by operating activities of both companies has declined because of paying higher taxes but in FY05 there was a significant increase in case of PTC due to the reason that there was a major increase in cash receipts from customers and same was the reason for a significant increase in case of LTC for FY04.

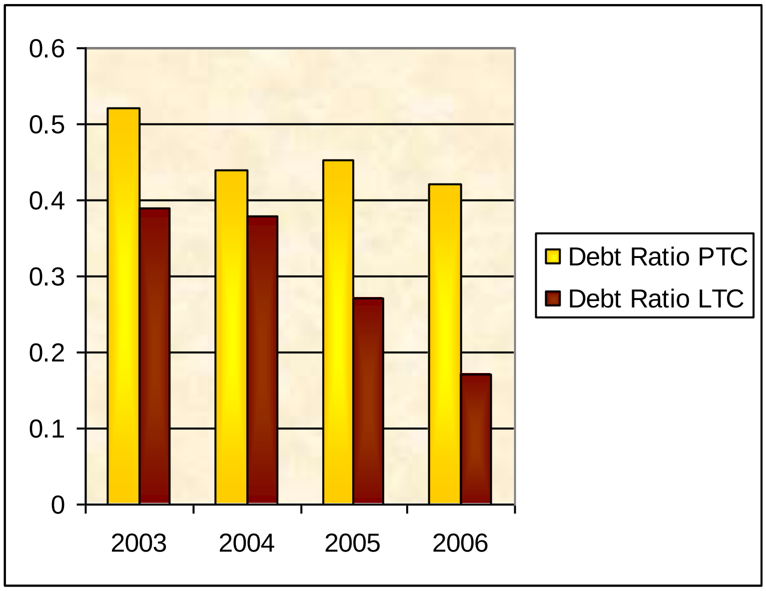
Free Cash Flow



In terms of this ratio PTC is better than LTC as it can be seen that although PTC's free cash flow has declined but it is still greater than the free cash flow of LTC. The reason for a high decline in LTC's free cash flow in FY05 was due to lesser cash generated from operations and higher fixed capital expenditures.

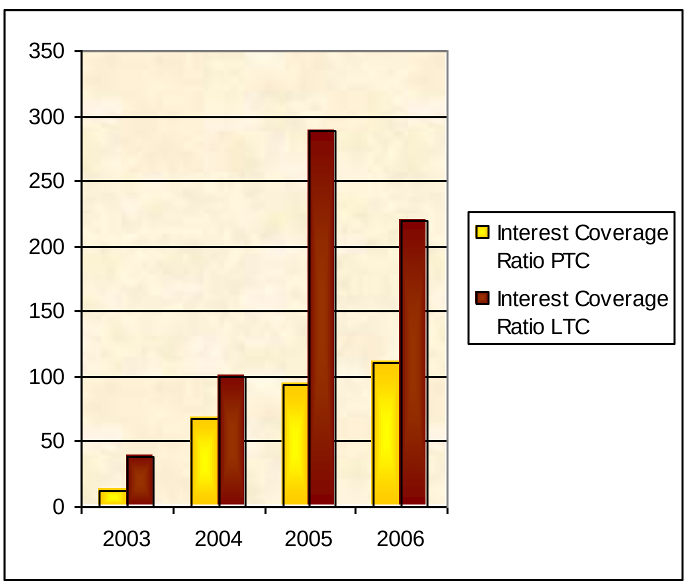
Measures of Long Term Credit Risk

Debt Ratio



The debt ratio of both tobacco corporations has decreased from 2003 which is favorable for both of them. However, LTC gains advantage because its debt ratio is decreasing at an increasing rate. In FY05 the debt ratio of PTC was higher than the debt ratio of LTC due to the reason that PTC has done short term financing. LTC has not done any short term financing in FY05.

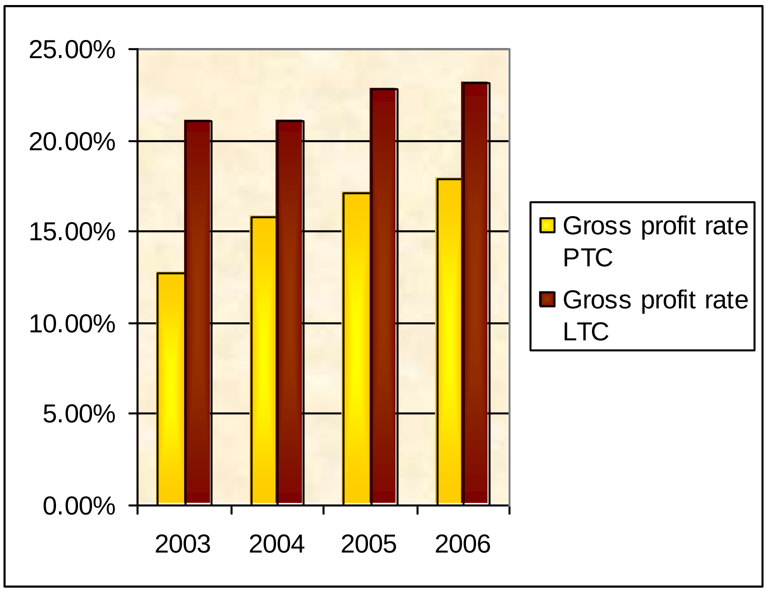
Interest Coverage Ratio



The interest covering ratio of PTC is less than that of LTC .Due to the reason that it has lesser interest expenses as compared to PTC. But on the other side both companies are in good condition as they have more than 50 rupees for one rupee of interest. Although the interest coverage ratio of PTC is less but still it is not in a weak position as in FY06, PTC has 110 rupees for each one rupee of interest. But relatively PTC has lesser credit risk as compared to LTC which in the same year has 220 rupees for every one rupee of interest.

Measures of profitability

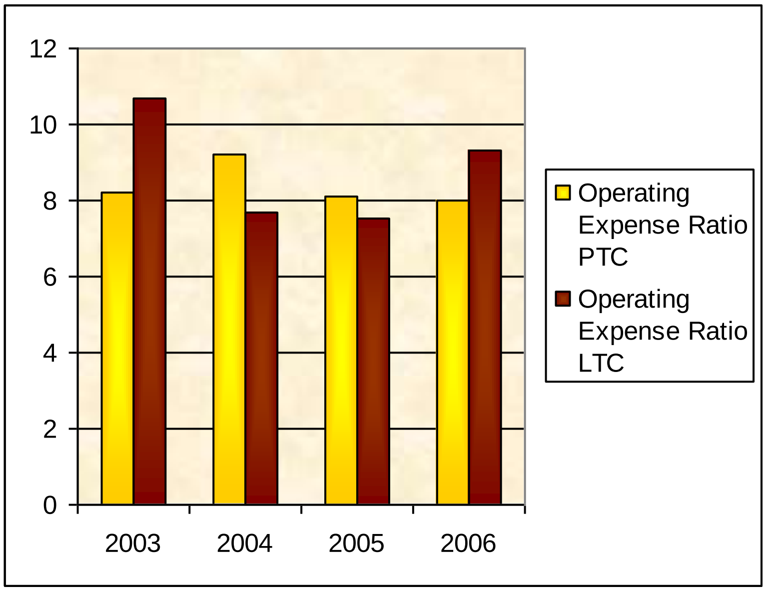
Gross profit rate



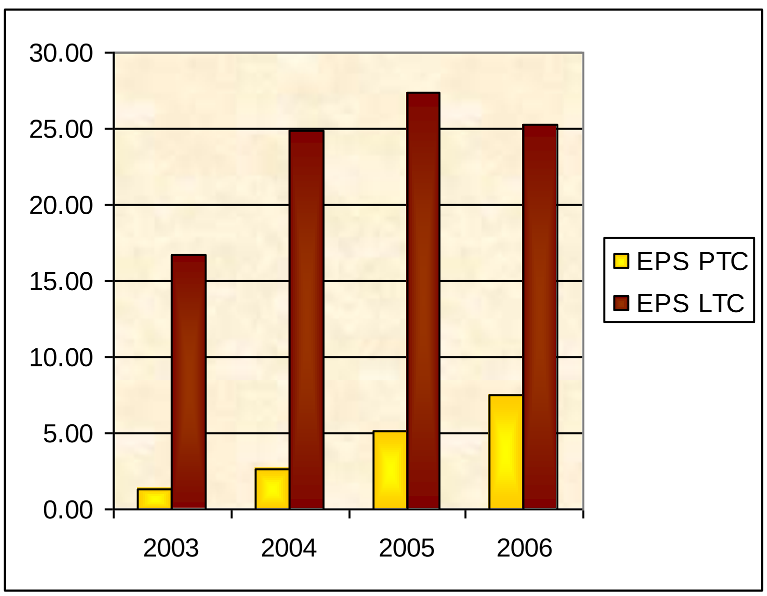
PTC's sales are more than LTC in the last two years. Still the Gross Profit Rate of LTC is higher than that of PTC showing reductions in their cost of sales due to better efficiency. As it can be seen that in FY06 cost of good sold are 82% of total net sales in case of LTC but they are 76% of net sales this is the reason of difference in gross profit rate.

Operating Expenses Ratio

Operating Expense Ratio of PTC has declined in FY05 and FY06 due to increase in its turnover. On the other hand, LTC's ratio has increased due to the increase in operating expenses mainly administration expenses. Not only this, its sales are also lesser compared to PTC so it results in an overall higher operating expenses ratio.

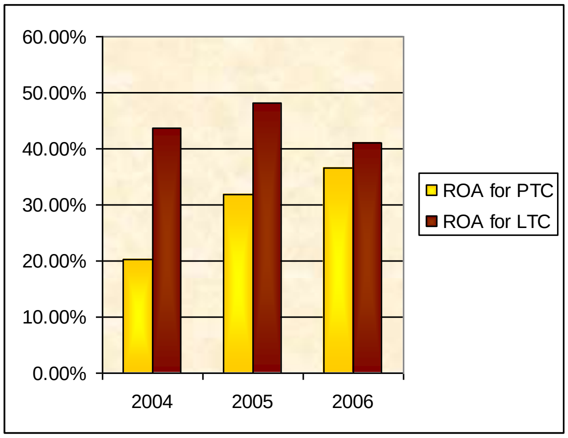


Earning per share



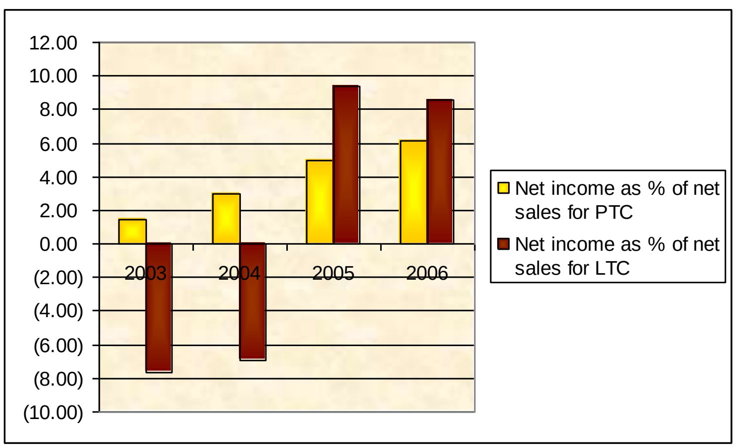
The EPS of LTC has remained excessively high when compared to PTC. The earning per share of LTC has grown faster due owing to the fact that its net income as a percentage of net sales is higher when compared with PTC. In FY 05 EPS of LTC has increased because its number of shares has remained the same but in FY06, since more shares were issued so the EPS was reduced. Nonetheless, it is still ahead of its rival in terms of this ratio.

Return on Assets



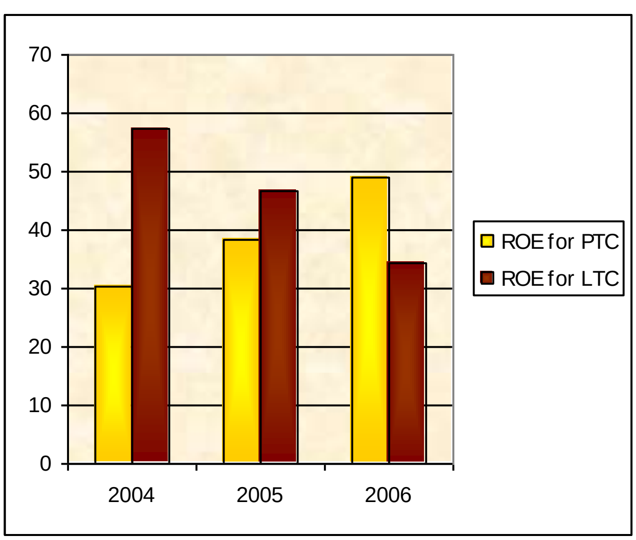
The Return on Assets for PTC increased more in 2005 than in 2006. The reason for this is that although the net income continued to increase in FY06, it was accompanied by an increase in total assets. However, the ROA of LTC is still higher than that of PTC primarily because PTC has 47% more of total assets.

Net income as a percentage of net sales



While looking at this ratio it can be said that PTC has improved its efficiency by reducing its cost but on the other side LTC has performed an excellent job by reducing its cost in a way that it has brought its ratio from a negative to a handsome amount of above 8.

Return on Equity



This is one of the very few ratios in which PTC has excelled more than LTC owing to the fact that LTC has issued more shares in FY06. Moreover, the net income of PTC was more than that of

LTC in FY06 while the number of common shares outstanding remained constant.

a) MEASURES OF SHORT TERM LIQUIDITY

Ratio	PTC	LTC	Preferred company
Current ratio	1.1	2.59	LTC
Quick Ratio	0.045	1.13	LTC
Working Capital	Rs 422741000	Rs 2665295000	LTC
Inventory Turnover Ratio	6.5	8.926	LTC
Days to sell average inventory	56	44	LTC
Cash flow from operations to current liabilities	60%	260%	LTC
Net cash provided by operating activities	Rs1700,000	Rs 1100,803	PTC
Free cash flow	Rs (255370)	Rs (794380)	PTC

b) MEASURES OF LONG TERM CREDIT RISK

Ratio	PTC	LAKSON	Preferred company
Debt ratio	42%	17%	LTC
Interest coverage ratio	110	220	LTC

MEASURES OF PROFITABILITY

Ratio	PTC	LTC	Favorable Company
Gross profit rate	17.91%	23.11%	LTC
Operating expense ratio	8.02%	9.29%	PTC
Net income as a % of net sales	6.2%	8.6%	LTC
Earning per share	7.46	25.25	LTC
Return on Assets(ROA)	36.49%	40.95%	LTC
Return on equity(ROE)	48.98%	34.17%	PTC

Conclusion

PTC's performance has been exceptional, especially in the last two years, since FY05 when it re-gained market leadership. PTC is in a stable condition and has been improving with regularity which can be observed from the improving trends in the ratios. However, its performance should be evaluated by comparing its ratios with its nearest competitor, namely, LTC. LTC outperforms PTC in almost all ratios of liquidity, both long and short term. PTC's net income as a percentage of net sales is also less than that of LTC making it less attractive for external stakeholders.

However, we should not analyze PTC's performance on the basis of just these accounting ratios. PTC despite having weaker ratios has considerably improved in the last few years. This is the same company which was incurring a net loss in 1999. Its credit limit was almost over and done with. It has picked up since then, when BAT injected a huge amount of equity to the failing company.

	Years		Growth
	2006	1999	
Volume (Billion Sticks)	34.5	18.7	84%
Operating Profit (Rs in Million)	3,048	344	786%
Profit After Tax (Rs in Million)	1,905	(136)	1500%

Figure taken from Director's Review 2006 1

PTC's success story is such that not only has PTC captured the market leadership in FY05, it also increased the gap from LTC by 5.6 ppt (AC Nielson Retail Audit research data)[1]. While the tobacco industry grew by 3%, PTC's overall growth in FY06 was an impressive 15%.

PTC also faces some challenges which it has to overcome to gain a competitive advantage over LTC. While LTC targets the masses, i.e. the low income group, PTC has only one brand for these consumers- Embassy. Embassy's sales have been disappointing in comparison to previous years so PTC needs to work on forming a strategy to target the low-income group segment of the market.

Moreover, government restrictions on advertisements have made the marketing process more difficult. Along with this is the fact that NGO's are becoming more active in their campaign's against the use of tobacco. Tobacco business has always been looked upon with a cautious and negative eye due to its adverse affect on human health. It is encouraging that PTC is playing a role for the environment by planting trees. The reality exists, that tobacco will always be injurious for health so it would continue to remain a challenge.

Another troubling factor is the tax evading sector which is providing lower prices for similar products. Smuggling is also common in the tobacco industry and it is believed to have around 15-20% of the market share. PTC is one of the highest tax paying entity in Pakistan. It should therefore, continue to exert pressure on the government to reduce the illicit trade of tobacco related products.

Future Outlook

While looking at the overall performance of the company we can say that PTC with its vision of "The First Choice for Everyone" will make further progress. The company has already gained market leadership and has widened the gap in FY06. Along with this, PTC continues to invest heavily in its plants and equipments. Furthermore, the company is attaining new heights in many areas including leaf purchases, production volume, sales volume and profitability. It can be recommended that if PTC progresses with this similar tendency and increasing sales

[1] Director's Report Annual Report PTC FY06

volume, it could become the most attractive company in the tobacco industry for both external and internal stakeholders.