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I. Introduction

Pakistan Tobacco Company Limited (PTC) is subsidiary of British American Tobacco. British American Tobacco Company owns 97% of the shares. PTC is the first came in 1947 making it one of the first foreign investments in Pakistan. British American Tobacco -the world's most international tobacco group - with brands sold in 180 markets around the world. PTC is one of the largest cigarette manufacturing company in Pakistan and has a market share of around 40% Pakistan. PTC the strongest distribution network in Pakistan. Pakistan Tobacco Company has instituted one of the largest afforestation efforts in South Asia in order to increase the natural forest cover in Pakistan, and ensure the environmental sustainability of operations. PTC run two state of the art factories and employ more than 1,700 people while indirectly providing livelihoods to more than a million people who are involved in various aspects of the business. PTC are market leaders and contribute more than Rs.30-billion in excise duties and taxes to the Government. PTC strategy reflects their vision, being the champions of growth, productivity, responsibility and a winning organization.

British American Tobacco is the world’s most international tobacco group with its brands sold in more than 180 international markets. With over 300 brands in the portfolio, the Group makes the cigarette chosen by one in eight of the world’s one billion adult smokers. The Group holds robust market positions in each of its regions and enjoys market leadership in more than 50 markets.

**Business model:**

PTC believes that Total Quality is more than just Product Quality; it is quality of everything they do in business. It means understanding Consumers, Customers, Stakeholders, and Suppliers. They are following the standards of professionalism according to parent company’s policy and procedures.

**The four Guiding Principles adopted from parent are:**

- **Strength from Diversity** reflects PTC’s cultural mix and a working environment that respects employees' individual differences. It also reflects their vision of harnessing diversity.
- **Open Minded** reflects openness to change, opportunities and new ideas, including ways of addressing regulatory issues and changing social expectations.
- **Freedom through Responsibility** describes decision making as close to the consumer as possible and affirmation to core belief.
- **Enterprising Spirit** reflects their ability to grow business and its value within challenging environments, with the confidence to seek opportunities for success, to strive for innovation and to accept considered risk taking as part of doing business

**Three Business Principles:**

- **Mutual Benefit**, The principle of Mutual Benefit is the basis on which stakeholder relationship are built.
- **Responsible Product Stewardship** basis on which PTC meet consumer demand for a legal product that is a cause of serious diseases. Therefore, PTC products and brands should be developed, manufactured and marketed in a responsible manner. PTC also aspire to develop tobacco products with critical mass appeal that will, over time, be recognized by scientific and regulatory authorities as posing substantially reduced risks to health.
- **Good Corporate Conduct**, the basis on which PTC business is managed. Business success brings with it an obligation for high standards of behavior and integrity in everything we do and wherever we operate. These standards cannot be compromised for the sake of results.
A number of Core Beliefs, which explain what the principle means in more detail, supports each of the principle. Both the Business Principles and Core Beliefs and their development are consistent with four Guiding Principles, which collectively express the culture of the Group and Pakistan Tobacco Company as part of it.

**Pakistan Tobacco Company Limited is part of the following trade and industrial associations:**

- Cigarette Manufacturers Association Of Pakistan (CMA)
- Management Association Of Pakistan (MAP)
- Overseas Investors Chamber Of Commerce & Industry (OICCI)
- Anti-Counterfeit and Infringement Forum (ACIF)

**Supplier Code of Conduct**

Supplier Code of Conduct complements Group Standards of Business Conduct by defining the minimum standards we expect our suppliers to adhere to in order to supply goods or services to BAT and any BAT Group company. This builds upon our long-standing commitment to operating to the highest standards of corporate conduct for both our own business operations and our wider supply chain. It also supports our continuing commitment to respect human rights and uphold international standards, including the United Nations Guiding Principles on Business and Human Rights and the Organization for Economic Cooperation and Development Guidelines for Multinational Enterprises.

**Strategic Focus**

**Principal business lines:**

The company produces high quality tobacco products to meet the diverse preferences of millions of consumers, and it works in all areas of the business - from seed to smoke. The company provides a number of reputed brands of cigarettes to consumers in Pakistan, including Benson and Hedges, Embassy, Gold Flake, Capstan and Gold Leaf. PTC portfolio catering to the different tastes and preferences of the entire tobacco market.

Pakistan Tobacco Company invests in trying to understand the consumers’ preferences and ensures that adult smokers make informed choices about different brands available in the market. Recently they have put in particular effort in promoting two Global Drive Brands, Dunhill and Pall Mall; and two of their great value for money brands, John Player Gold Leaf and Gold Flake.

**Product Range**

1. **Dunhill**

   Dunhill, a premium global brand, celebrated its centenary in 2007. 2008 was an exceptional year for Dunhill in Pakistan as the brand witnessed exponential growth; fuelled by its re-launch in July. Going forward, Dunhill is poised to strengthen its foothold in the premium segment. Dunhill was launched back in 2005 in the Pakistan as a quality offer for the top end market. It was freshly imported and launched targeting the super-premium segment at the price point of Rs.82/-. Dunhill’s was re-launch in 2008, which revolved around quality product, and new pricing keeping the premium cues intact. With the re-launch, the production was localized,
price repositioned to Rs.64/- and distribution expanded in addition to the introduction of the 10s packs in both Full Flavour and Lights variants.

2. Benson & Hedges
   In 1873, Richard Benson & William Hedges started a partnership in London. Benson & Hedges was launched in Pakistan in March 2003 and has since been able to build strong brand loyalty among its consumers showing excellent year on year growth.

3. John Player Gold Leaf
   The story of John Player Gold Leaf has to start from the story of its founder, John Player. An enterprising businessman, John Player started a small tobacco selling business in 1877 and turned it into a thriving cigarette company, John Player and Sons. John Player Gold Leaf has become an institution in itself, becoming one of the most recognizable cigarette brands in the country. John Player Gold Leaf has recently been declared the largest Urban Brand in Pakistan, beating out products across the FMCG spectrum.

4. Capstan by Pall Mall
   Capstan has a rich heritage, originating in Britain in the 19th century. The brand was created under the auspices of W.D. & H.O. WILLS at Bristol and London. Pall Mall looks at life from a positive perspective and understands that even a small change can make a huge difference. Pall Mall is about imagination in tobacco. Our way is simple and straight, imagining ways to deliver the unimaginable smoking experience. Pall Mall’s international appeal worked well with the exceptional taste of Capstan International. Pall Mall’s International image and appeal got Capstan the right exposure in the market. The migration has helped Capstan strengthen itself as an innovative brand.

5. Gold Flake
   Gold Flake, like many of BAT brands, also boasts its origins at W.D. & H.O. WILLS where it was a premium brand around the end of the 19th century. Launched in 1982, in 'soft cup' packaging, the brand took off when it was repositioned in the Value For Money (VFM) segment and later a 'hinge lid' variant was introduced in 2000. Gold Flake has grown tremendously as a brand since 2004, making it the largest volume brand in Pakistan, and the second largest brand in British American Tobacco's Asia Pacific region. The key to Gold Flake’s success has been its novel engagement schemes, which have fueled growth over the years. Through consumer relevant initiatives, Gold Flake has established itself as a fresh and modern offering in the VFM segment and is all set to consolidate its position as the major volume driver for Pakistan Tobacco Company. Gold Flake symbolizes for more, the determination to make things happen, and the optimism to change the future; it lives in an electrically charged environment that pulsates with energy.

6. Embassy
   Embassy, is a leading volume brand in Pakistan, and is most popular in Punjab where it enjoys a leading position. Having built its heritage over a number of years, Embassy thrives on its brand loyalty and locally tailored taste characteristics.

7. Davidoff Coffee
   The swizz manufacturer Zino Davidoff Group originally makes Davidoff coffee. PTC imports and sell it for additional profits. Globally speaking Zino Davidoff Group is a competitor of British American Tobacco. Therefore, this product is not shown in PTC website and we too came to know about this through Mr. Faheem. Pakistan Tobacco Company invests in trying to understand the consumers’ preferences and ensures that adult smokers make informed choices about different brands available in the market.
Financial overview:

The Company continued to be severely impacted by the massive consumer down trading to cheap duty evaded cigarettes. This is reflected in the business results of the 1st half ended in comparison to the same period last year (SPLY). Despite a series of efforts by the law enforcement agencies to curb illicit trade of cigarettes throughout the 1st half of the year, the illicit sector maintained its market share at 40.8% at June 30th 2017. In the face of these challenges, PTC continued its strategy of driving manufacturing excellence, effective cost management and addressing the affordability needs of its consumers to retain market leadership in the legitimate sector.
Key financial indicators of PTC for YTD H1 2017 are:

The Gross Turnover has declined vs. SPLY owing to the decline in sales volume primarily driven by the rise in market share of the illicit sector especially in the VFM segment. This decline was slightly netted off by the positive impact of excise led price increases taken during last year. Cost of sales was lower by 30% primarily due to lower volumes vs SPLY. PTC remains focused on maintaining a sustainable business model built on high productivity and effective cost management. PTC contributed PKR 34.3 Billion in H1’17 (down by PKR 23 Billion vs. SPLY) to the National Exchequer in the form of excise duty, sales tax, customs duties and income tax. The Company continues to stress the detrimental impact of growing sales of duty-evaded cigarettes on the sustainability of government revenues. In recognition of these negative factors, the government has initiated tax and policy reforms through the recent federal budget. The relevant authorities are urged to continue with the reforms and enforcement to create a level playing field to curb the growth of the duty-evaded segments of the industry and for the sustainability of government revenue.

**Market share:**

PTC is one of the largest cigarette manufacturing company in Pakistan and has a market share of around 40%. Both PTC and LTC control 72.3% of the market share together. Hence, fierce competition exist between the two. Share of illegal cigarettes is 28%

**Manufacturing:**

At the factory, the matured tobacco is checked for quality and then carefully blended with other ingredients which the brand recipe may call for, such as flavorings or pre-processed tobacco. Keeping track of the various types of tobacco and blend components is key and computers are increasingly used to track production runs.

Moisture content is crucial. Too dry and the tobacco leaf will crumble; too moist and it may spoil during storage. The blended tobacco is treated with just the right amount of steam and water to make it supple and then cut into the form in which it appears in the cigarette. Excess moisture is then removed so the cut tobacco can be given a final blending and quality check.

Cigarette making, is almost fully automated, with the cut tobacco, cigarette paper and filters continuously fed into cigarette-making machines. The technology has advanced dramatically over the years, but quality is not forgotten; each cigarette is automatically quality controlled to ensure that it meets every benchmark for its specification.

As packing machines put them into the familiar brand packs, wrap the packs in protective film, and group them into cartons and cases; further testing takes place at each stage to make sure the cigarettes are properly protected. The completed cases, time-dated to ensure the freshest product possible, are then ready for distribution. The two manufacturing sites are located at Jhelum, Punjab and Akora Khattak, NWFP.
Trade marketing and distribution:

Trade marketing is a large part of marketing activities, managing business-to-business relationships with the retailers and distributors from whom consumers buy products. PTC’s believe in ‘win-win-win’ approach sets them apart in the market place. Work to operate in the most efficient and effective way so that retailers can offer the products consumers want to buy, where and when they want to buy them, and at the right quality. Trade marketing field force provides value added services in complimenting the distribution effort, in select stores of the retail universe to enable mutually beneficial partnerships. PTC 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 our consumers. Around 250 exclusive distributors, employing a contingent of over 1,200 distribution representatives, provide direct store delivery services for finished products to the 500,000 plus retail stores throughout the country. PTC aim to optimize our finished goods supply chain efficiencies in delivering products of consistent quality on time, every time.

History:

From being just a single factory operation to a company that is now involved in every aspect of cigarette production, from crop to consumer, they have evolved and grown with Pakistan in the past 69 years. Starting from a single warehouse near Karachi port, the Company is now the largest cigarette manufacturer in Pakistan. By being instrumental in the campaign for modern agricultural and industrial practices, PTC has helped in the development and progress of the agricultural and industrial sector in the country. The history of the Pakistan Tobacco Company is closely linked with the development and history of the areas in which we operate. Be it corporate practices, social investments, advancements in agricultural techniques, or establishing new ways of marketing and distribution, we have always been instrumental in establishing the benchmarks against which others are measured.

Pakistan went from being a net importer of tobacco in 1948, which is when Pakistan Tobacco Company started operations, to becoming self-sufficient in tobacco production in 1969. Although tobacco is grown throughout the country, the primary source of this integral raw material is the NWFP where soil and climatic conditions suit tobacco cultivation the most. The province has been the focal point of our efforts in terms of tobacco-related activities in Pakistan, and as a result, produces around three-fourths of the tobacco leaf grown in the country. Pakistan Tobacco Company, as the largest cigarette manufacturer in Pakistan, has a special relationship with the land and people of the NWFP. The fruit of these activities is that in just 30 years Pakistan became the 5th largest tobacco producer in the world and 4th in highest yield.

In 1948, we pioneered the cultivation of Virginia tobacco in Pakistan with an average yield per hectare of 861 kg. Through our continuous efforts and the hard work put in by our contracted farmers, the yields have increased significantly to 2,400 kg/hectare. Prior to that native varieties like Jati & Motihari were cultivated mainly in the eastern part of Pakistan (Bangladesh). All the Virginia tobacco was imported from the USA & India. Flue Cured Virginia tobacco is now the most widely grown and widely used type of cigarette tobacco in Pakistan and the total production of this high value commodity has increased from 23.8 million kilograms in 1967-68 to 66 million kilograms in 2007. Pakistan is now the 7th largest producer of FCV in the world. As a result of PTC’s direct efforts, the current tobacco production in the country exceeds 100 million kilograms per year, although what is perhaps more important is the types of tobacco grown in the country. The share of higher value FCV, Burley and White Patta as opposed to lower priced filler tobacco has grown tremendously over the years, drastically increasing the returns for farmers and eliminating our reliance on imports for higher quality tobacco.
II. Research Design and Methodology

The research paper is based on analysis of annual report of PTC and its key competitors, published articles on Pakistan tobacco industry and interview of PTC Territory Executive Lahore Region Mr Raja Faheem. Due to time and resource constraints, the study has focused on tobacco cigarettes only. For both PTC and its competitors. Therefore, all the evaluations and results relate to tobacco cigarettes and other tobacco and no-tobacco products are not analysed of the company.

III. Company’s Vision and Mission Statement

Vision statement:
Satisfying Consumer Moments
We believe that by being the world’s best at satisfying consumer moments, we will become the leader in our industry. Consumers are at the core of everything we do and our success depends on addressing their evolving concerns, needs and behaviours.
Tobacco and Beyond
The second part of our vision – tobacco and beyond – recognizes the strength of our traditional tobacco business and the opportunities we see in next-generation tobacco and nicotine products. There is a great potential business opportunity because consumers are looking for choices and product categories in which we are uniquely placed to succeed.

Proposed Vision Statement:
“To achieve leadership of the global tobacco industry in both a quantitative and qualitative sense.”
Since it is more catchy and short and is more in line with the mission statement.
**Mission Statement:**
Transform PTC to perform responsibly with the speed, flexibility and enterprising spirit of an innovative, consumer focused company.

**Strategic Objective:**
Reflects vision of being the champions of Growth, Productivity, Responsibility and Winning Organization.

**Guiding Principles**

![Guiding Principles Diagram]

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**Business challenges and future outlook 2016:**
Illicit Trade is the biggest threat facing the sustainability of the legitimate tobacco industry. The duty-evaded cigarettes are sold at less than one third the price of the cheapest
brands in the legitimate sector. This deprives the government of very substantial revenue and is in sheer contravention of laws of the country. It is apparent that due to illicit sector depriving the legitimate industry of a level playing field, 2017 will be a challenging year, where we can expect volumes, profit and government revenues to be under severe pressure.

PTC strongly urges the relevant authorities to intensify law enforcement to curb the duty-evaded sector. If this is not addressed, it will lead to a permanent deterioration of the legitimate sector that will pose serious doubts to business sustainability and government revenue collection for the future.

Illicit Trade is the supply, distribution and sale of smuggled or counterfeit tobacco products, or tobacco products on which applicable duties and taxes in the country of consumption have not been paid. Illicit trade essentially takes three forms:
The first is importation for commercial use, also known as International Transient Brands (ITBs), of tobacco products on which payment of applicable taxes, such as duties, excise and sales tax is evaded in the country of consumption. These products may have had no taxes paid on them at all, or may have had lower taxes paid in another country.

The second is undeclared local production or Duty-Non-Paid (DNP) whereby products are produced and consumed within the same country but without payment of all local taxes. These products may be manufactured in approved factories but not declared to the authorities, or they may be manufactured in illegal covert operations.

The third is counterfeit products which are also an infringement of Intellectual Property Rights (IPR). These are products which are intended to be identical or near identical copies of a genuine branded product and its packaging so as to appear as the genuine product. By definition such products are illegal, as the manufacturer is not authorized by the brand owner to use the counterfeited brand assets. Counterfeits may be produced for the local market or exported.

Pakistan Tobacco Company has always worked closely with the Government to implement laws and regulations (legislation) to ensure a 'level playing field' for all the companies in the tobacco sector. As a result, the share of the market held by the illicit sector has come down to 18.4% of total cigarette sales, which is still high given local market dynamics. The net loss to the national exchequer is estimated at Rs. 7.46 billion per annum assuming that all the illegitimate products sell at the minimum price determined by the Government for the purposes of tax collection. The loss to the legitimate industry amounts to over Rs. 2.0 billion per annum.

The measures taken by the Government to control illicit trade in cigarettes are as follows:

- Printing of manufacturer’s name and retail price
- Third party audits
- Destruction of machinery and confiscation of conveyance used for counterfeit products
- Disclosure of bank accounts
- Submission of audited bank accounts to FBR
- Sealing of excess capacity
- Installation of CCTV cameras
IV. External Analysis

**General environment:**

The tobacco industry is a source of revenues, employment and foreign exchange for the country. The industry has to pay very high excise and sales tax while complying with various strict rules and regulations of the government. The industry is facing high taxation. Along with taxation Anti-tobacco regulations and campaigns by NGO’s is increasing operational costs for these tobacco product manufacturers.

This year saw an unprecedented increase in the Illicit Trade in Cigarettes in Pakistan reaching the highest ever share of 40.6% as at December 2016. The legitimate tobacco industry declined by 10% by December 31st 2016 as a result of exponential growth of duty evaded segment. This was led largely by the excise driven price increases, the recent one being in Dec’16, and lack of effective enforcement by law enforcement agencies. Despite recovery in key economic indicators the consumer wallet remained under pressure. Hence excise led price increases had further stretched the consumer and widened the gap between the low price legitimate brands and duty evaded products. For example in Dec’16, the minimum total tax on a pack of 20 cigarettes was Rs. 43, yet the duty evaded segment was selling its products for prices lower than the minimum tax. All this contributed to an accelerated and significant down trading to duty evaded segment, resulting in a steep decline in the legitimate industry’s volume and consequently a loss in government’s revenue.

The bulk of the illegal cigarettes are local Duty Non Paid (DNP) which represents more than 85% of the illicit market. DNP cigarettes are produced in Pakistan on which duties and taxes have not been paid to the Government. Price range of the bulk of DNP packets of 20 cigarettes was from Rs. 20 to 35, whereas the legit Value for Money (VFM) segment pack price for the year (Dec’16) was Rs. 72. The non-payment of taxes on a Rs. 20 to 35 pack is evident from the fact that the minimum tax payable on a packet of 20 cigarettes is approximately Rs. 43 in December 2016. Continuous excise led price increases over the years have widened the gap between the legitimate and non-legitimate cigarettes hence making legal cigarettes very expensive for the consumer. The huge price differential has resulted in creating an uneven playing field for tax compliant legal industry and has consequently dealt heavy losses to both national exchequer and the tax paying industry. While multiple laws are in place to check tax evasion on cigarettes, effective enforcement remains a cause of concern. Robust action is required to cease the flow of illicit trade to wholesale and retail outlets. The unprecedented increase in illicit cigarettes requires active, effective and consistent enforcement.

**Main competitors:**

PTC faces direct competition with LTC only. The rest don’t have a significant power to threat PTC in any way. Presently there are seven listed tobacco companies in Pakistan which constitute as the organized sector of the industry:

Companies with foreign ownership
1. Pakistan Tobacco Company (PTC)
2. Lakson Tobacco Company (LTC)

Companies with local ownership
1. Souvenir Tobacco Company
2. Khyber Tobacco Company
3. Sarhad Tobacco Company
4. Tobacco International Ltd.

The unorganized sector mainly consists of the operations in NWFP and Azad Kashmir. This sector also includes foreign smuggled cigarettes. This unorganized sector constitutes of almost 13% of the total market in the country.
The main brands competing in their respective price segments are:

<table>
<thead>
<tr>
<th>Category</th>
<th>Price Range (Rs.)</th>
<th>Leading Brands</th>
<th>Market Share</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>23.75+</td>
<td>Gold Leaf</td>
<td>76%</td>
</tr>
<tr>
<td>B</td>
<td>17-16</td>
<td>Capstan</td>
<td>100%</td>
</tr>
<tr>
<td>C</td>
<td>15-6</td>
<td>Red &amp; White</td>
<td>47%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Wills Kings</td>
<td>10%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Gold Flake</td>
<td>15%</td>
</tr>
<tr>
<td>D</td>
<td>6</td>
<td>Embassy</td>
<td>54%</td>
</tr>
<tr>
<td>E</td>
<td>Below 6</td>
<td>Royals</td>
<td>20%</td>
</tr>
</tbody>
</table>

**Taxation:**

Cigarette industry has two-slab duty structure. The two slabs are:

1. A flat excise duty of Rs. 117,000 per million cigarette on brands costing less then Rs. 2.52 per pack of ten cigarettes (Categories D and E), exclusive of sales tax.
2. A 65% excise duty on brands costing more than Rs. 2.52 per pack of ten cigarettes, exclusive of sales tax.
3. Other than that, an 18% sales tax is also imposed on all the brands. The main burden on this industry is through indirect taxation that is applied on the revenues and not on profits. The direct tax is the normal corporate income tax @ 30%
Social, cultural and demographic Trends:

Smoking is getting increasingly popular in university and college students. According to the recent estimate the total market in the country is estimated at 56 billion sticks per annum, with a market growth rate of 11% per annum. The shortage in production is covered by either smuggled/imported cigarettes or by the unorganized sector with understated or unstated capacity and capacity utilization.

The imported brands have an important position in the upper category brands as there are very few brands that are manufactured locally (Gold Leaf, and recently Kenmore). Until a few months, back all the foreign brands were smuggled in to Pakistan. Recently American company R. J. Reynolds started importing its line of brands (Camel, Aspen, and More) to Pakistan followed by PTC’s import of Benson & Hedges. In future the market is expected to be filled with other imported brands such as 555 (by PTC), Marlboro (by LTC/Philip Morris), and Dunhill etc.

The issue of environmental pollution is not of critical nature in the industry as the industry is not responsible for any anti-environment activity. However it is heavily criticized for the health hazards that are caused by smoking. The tobacco companies try to improve their public image first through media advertising and secondly by engaging in other activities that improve their overall image. PTC started its plantation campaign in this regard few years back and also started the production of edible oil (Sun drop) for these reasons.

Industry Analysis:

The major product of this industry is cigarettes. Other than that, other products include cigars, ‘Bidi’, ‘Niswaar’, and tobacco for pipe and ‘Huqqua’. In Pakistan cigars and pipe tobacco are imported while the other products are locally manufactured. The production facilities for ‘Niswaar’, ‘Bidi’, and ‘Huqqua’ tobacco constitutes the unorganized sector and very little data is available. According to an estimate almost half of the tobacco consumption is through cigarettes while the rest through other means. As the prices of the products other than tobacco are very low, therefore the major source of revenue in the industry is cigarette manufacturing. Cigarette market can be divided into the following categories with the leading brand in each category and its market share. The categories are defined by the price range of each category.

As far as the import of raw materials is concerned, the paper roll and filters are imported while a part of the tobacco used in premium brands is also imported. Other than that, most of the raw materials are locally produced. The big companies, and among them the higher priced brands, use a larger proportion of imported raw materials. However there is a as such no international competition as the locally manufactures materials cannot compete their foreign counter parts in quality.

The pricing in this industry has a steady upward trend with an average rate of 5-8% per annum. This due to the sales tax and excise duties which the government imposes on the industry and which in turn are passed on to the consumers. The most significant feature of the pricing is the effect of taxes and duties. The industry does not increase the prices to improve its margins but it only attempts to maintain them. The two big companies (PTC, and LTC/PTI) usually set the prices in cohesion. The prices of their brands competing in the same category are exactly equal to each other. The smaller companies however try to undercut the prices of big ones to capture the market. It is easier for the small companies to undercut the prices as they constitute the tax evading sector of the economy.

Potter’s five forces model analysis:

Industry Attractiveness  Porter’s Five Force

1. Bargaining Power of Buyers (low to medium): Cigarette consumption in Pakistan is five times higher than in India with 620 cigarettes per adult per annum against 119 for India. This shows that the market for tobacco industry is very immense locally. According to
Pakistan Paediatric Association, 1,000 to 1,200 children between the ages of 6 and 16 years take up smoking every day.

2. **Threat of Completion (low to medium)** only two major companies compete with each other. These are Pakistan Tobacco Company and Lakson Tobacco Company.

3. **Threat of New Entrants Rivalry (medium to high)** the market is a mix of free market structure and oligopoly.

4. **Substitutes (low to medium)** Substitutes are easily available in Pakistan so people have the option to switch to brands of other firms.

5. **Bargaining Power of Suppliers (low to medium)** Most of the tobacco used by the firms is produced in Pakistan, but still a considerable amount of tobacco is imported every year.

**Non-Pricing competition:**

1. **Product Styling:** In tobacco industry, the product styling plays a very important role, as the image of the brand is a crucial factor in the overall success of the brand. The company’s try to compete with each other through giving a distinct image to the product through various marketing activities. This image helps in the differentiating the brand from its competitors in the same price range.

2. **Advertising:** Advertising or “above the line promotion” activities help the brand to achieve its desired image among the consumers. However the competing companies try to consolidate their own image through advertising rather than try to undo the competitor’s brand. For example, Red & White and Wills Kings are two competing brands in the same category but their advertising campaigns are completely independent from each other. The reason being that their desired brand image and brand styling is different.

3. **Product Branding:** There are very strong brand names in this industry. In fact the brand name and image is of greater importance than the quality of the product.

4. **Dealer’s Discount:** The dealers play a major role in the industry as they can easily ‘make or break’ a brand in the market. But still the dealers’ discount in the business is very low and like the companies they earn their profits on sales volume rather than profit margin. Following are the profit margins for various types of dealers:

<table>
<thead>
<tr>
<th>Type</th>
<th>Margin</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retailer</td>
<td>2.8%</td>
</tr>
<tr>
<td>Wholesaler</td>
<td>0.5%</td>
</tr>
<tr>
<td>Distributor</td>
<td>1.3-1.8%</td>
</tr>
</tbody>
</table>

5. **Introduction of New Products:** Currently in Pakistan, there is a room for the tobacco products like cigars and pipe tobacco. However due to the low demand of these products and high costs of production no company is interested in launching these products either through local production or through imports.

**Competitor Analysis:**

**Philip Morris (Pakistan) Limited** is a major tobacco firm in Pakistan. The firm's principal activity is the manufacturing and sale of cigarettes and tobacco products. The firm is listed on the Pakistan Stock Exchange (PSX) under the moniker, PMPK. It is an affiliate of the Philip Morris International Inc. (PMI) company. PMPK ranks second in the market based on annual volume of cigarette sticks sold in the formal market. It has been a decade since the PMI formally made its entry into the Pakistani market, acquiring the local tobacco firm, Lakson Tobacco. And is the strongest Competitor of PTC.

In 2016, the Company's gross turnover remained flat while gross profit increased by 24.01% as compared to 2015. Other Expenses for the current year decreased, mainly due to higher restructuring costs charged in 2015 as well as operational efficiencies and improved cost management, allowing the Company to post a modest profit after tax of Rs. 575 million following five years of consecutive losses. However, volumes remained under pressure due to the exceptional growth in the low price non-tax paid tobacco products triggering an accelerated consumer down trading. The excise tax driven price increases further widened the price differential between the tax-paid and the low price nontax paid tobacco products, thus creating
an unfair playing field for the tax-paying tobacco industry. The Company is actively supporting all Government policies, actions to address the issue of smuggled, and non-tax paid cigarettes ("Illicit Trade"). The Company's earnings per share are Rs. 8.79 in 2016, as compared to a loss per share of Rs. 21.35 in 2015. The Company continued to review its operational capabilities and, as such, in 2016 invested in property, plant and equipment Rs. 1,452 million. The Company primarily made these investments under the umbrella of a comprehensive project of modernizing manufacturing facilities and equipment to achieve overall improvements in productivity and product quality. These investments reflect the Company's commitment towards the business and confidence in its future growth in anticipation that the prevalence of illicit Trade will be addressed by the Government on an urgent basis. The Company continues to make substantial contribution to the Federal Government's revenues. In 2016, the Company contributed Rs. 25.3 billion to the National Exchequer in the form of Federal Excise Duties, Custom Duties, Sales Tax and Income Tax, which represents a decrease of 2.31% compared to 2015.

**Competitive Profile Matrix:**

<table>
<thead>
<tr>
<th>Key Success Factors</th>
<th>Weight</th>
<th>Pakistan Tobacco Company</th>
<th>Lakson Tobacco Company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Rating</td>
<td>Weighted rating</td>
</tr>
<tr>
<td>Product Innovation</td>
<td>.12</td>
<td>4</td>
<td>.48</td>
</tr>
<tr>
<td>Manufacturing Technology &amp; Quality</td>
<td>.12</td>
<td>3</td>
<td>.36</td>
</tr>
<tr>
<td>Human Resource</td>
<td>.07</td>
<td>4</td>
<td>.28</td>
</tr>
<tr>
<td>Selling &amp; Distribution</td>
<td>.07</td>
<td>3</td>
<td>.21</td>
</tr>
<tr>
<td>Supply Chain Management</td>
<td>.1</td>
<td>3</td>
<td>.3</td>
</tr>
<tr>
<td>Financial Muscle</td>
<td>.1</td>
<td>3</td>
<td>.3</td>
</tr>
<tr>
<td>Patronage &amp; Support of an International Player</td>
<td>.2</td>
<td>4</td>
<td>.8</td>
</tr>
<tr>
<td>Government Lobbying</td>
<td>.05</td>
<td>3</td>
<td>.15</td>
</tr>
<tr>
<td>Brand Equity</td>
<td>.12</td>
<td>3</td>
<td>.36</td>
</tr>
<tr>
<td>CSR</td>
<td>.05</td>
<td>3</td>
<td>.15</td>
</tr>
<tr>
<td>Total Score</td>
<td>1</td>
<td>3.39</td>
<td></td>
</tr>
</tbody>
</table>

Due to inclination of consumers towards modified cigarettes and flavoured tobacco products innovation is vital for staying in lead in a youth dominated customer base. Since production is currently labour intensive and the worldwide tobacco industry is facing automation, balancing both is essential for success. Since PTC is semi-automated, labour force is very important for them as they have state of art production facility which needs to be complemented with their agrarian based input and brand ambassador based selling and distribution. Being forward and backward integrated SCM is very important for PTC as it provides them an edge over LTC. Being subsidiary of major global tobacco products manufactures finance is not an issue for them and both thrive on their brand and company image.

**Major Opportunities and Threats for Tobacco Cigarettes Industry**

**Opportunities**

1. Industry Growth
2. Young smokers
3. Promising mid Tar segment
Threats

1. **Illicit sector activities** The illicit sector continues to be the single biggest threat to long term commercial viability and sustainability of the legitimate sector along with its adverse impact on Government revenue.

2. **Law and Order Situation** The law and order situation has been precarious, culminating in the bombing at the Marriott hotel which led to collateral damage to our Head Office in Islamabad. The general security situation in the country continued to deteriorate in 2008 and it was especially difficult in the tobacco growing areas of NWFP.

3. **Technology** Changing Optimization techniques not only to ensure capacity enhancement but also to adhere to international Environment, Health and Safety standards.

4. **Available resources** Need of raw material for meeting rising demand of cigarette. Government intervention for decreasing the cultivation of tobacco.

5. **Social and economic trends** Increasing knowledge of cigarettes’ hazards. Anti-cigarette campaigns and litigations.

6. Economic trends Rising taxes
   a. High inflation
   b. Rupee devaluation
   c. Rising commodity and oil prices
   d. Sharp increase in energy costs

7. Government action
   a. Cigarette use prohibition and awareness in people for hazards of smoking
   b. Ban on sales promotions
   c. Ban on product advertisements including sports sponsorships, TV, radio and outdoor hoarding.
   d. Changing Consumer needs
   e. Switching to Discount brands due to decreasing purchasing power of the consumers

8. Threat of rivalry and new entrants
**External Factor Evaluation Matrix:**

<table>
<thead>
<tr>
<th>Factor</th>
<th>Weight</th>
<th>Rate</th>
<th>Weighted rate</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Opportunities</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industry Growth</td>
<td>0.05</td>
<td>3</td>
<td>0.15</td>
</tr>
<tr>
<td>Young smokers</td>
<td>0.07</td>
<td>3</td>
<td>0.21</td>
</tr>
<tr>
<td>Promising mid Tar segment</td>
<td>0.05</td>
<td>3</td>
<td>0.15</td>
</tr>
<tr>
<td><strong>Threats</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Scarcity of raw material</td>
<td>0.07</td>
<td>3</td>
<td>0.21</td>
</tr>
<tr>
<td>Illicit cigarettes</td>
<td>0.07</td>
<td>4</td>
<td>0.28</td>
</tr>
<tr>
<td>Levy of heavy taxes and duties</td>
<td>0.06</td>
<td>3</td>
<td>0.18</td>
</tr>
<tr>
<td>New products like vape and e-cigarettes selling which can substitute</td>
<td>0.04</td>
<td>2</td>
<td>0.08</td>
</tr>
<tr>
<td>tobacco cigarettes</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>“Prohibition of Smoking and Protection of Non-Smokers Health Ordinance”</td>
<td>0.04</td>
<td>2</td>
<td>0.08</td>
</tr>
<tr>
<td>Controversy over Tobacco Support Price (Possible Hike)</td>
<td>0.06</td>
<td>2</td>
<td>0.12</td>
</tr>
<tr>
<td>Tax Evading Sector</td>
<td>0.05</td>
<td>3</td>
<td>0.15</td>
</tr>
<tr>
<td>Framework Convention on Tobacco Control (FCTC)</td>
<td>0.04</td>
<td>2</td>
<td>0.08</td>
</tr>
<tr>
<td>TV Ads Banned</td>
<td>0.02</td>
<td>2</td>
<td>0.04</td>
</tr>
<tr>
<td>Anti-Smoking Ordinance</td>
<td>0.06</td>
<td>2</td>
<td>0.12</td>
</tr>
<tr>
<td>Local Firms Gaining Share and Experience</td>
<td>0.06</td>
<td>3</td>
<td>0.18</td>
</tr>
<tr>
<td>Smuggling and low priced counterfeit</td>
<td>0.06</td>
<td>3</td>
<td>0.18</td>
</tr>
<tr>
<td>Tobacco Free Initiative in Pakistan</td>
<td>0.05</td>
<td>2</td>
<td>0.1</td>
</tr>
<tr>
<td>Increase cost to grow tobacco in northern areas</td>
<td>0.06</td>
<td>3</td>
<td>0.18</td>
</tr>
<tr>
<td>Increased operation cost in industry</td>
<td>0.05</td>
<td>2</td>
<td>0.1</td>
</tr>
<tr>
<td>Counterfeit products</td>
<td>0.05</td>
<td>2</td>
<td>0.1</td>
</tr>
<tr>
<td>Tobacco substitutes like e-cigarettes gaining popularity</td>
<td>0.05</td>
<td>3</td>
<td>0.15</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td>1</td>
<td>2.66</td>
</tr>
</tbody>
</table>

The company is responding at a reasonable pace to the changing environment considering their decision making process and bound to follow the practices of the parent company.

**Summary and Conclusion:**

Among the above mentioned CSF’s the threat from counterfeit and smuggled packets is the most ominous since it can seriously erode the brand’s sales potential. Retailers are naturally more willing to buy the counterfeit types since it allows them to earn huge margins from the sale of these cheaply bought packets. Furthermore, there are several restrictions that have been placed on the merchandising activities of brands. These include restrictions on merchandising any kind of material for schools / universities, hospitals and mosques. Hence, anything related to the brand, if caught anywhere near the above mentioned places, is immediately confiscated. This obviously translates into more careful (and subsequently more costly) merchandising activities for the brand. The new competitor by the name of Premier Classic is being marketed by Lakson Tobacco Company which is the licensee of the brand. This cigarette has been placed right into the premium category and, thus, poses a threat for the Gold Leaf as well as the Benson & Hedges brand. PTC must design an effective marketing campaign in order to counter the threat posed by this ambitious new comer.
V. Internal Analysis

### Revenue:

<table>
<thead>
<tr>
<th></th>
<th>2014 (PKR Million)</th>
<th>2015 (PKR Million)</th>
<th>2016 (PKR Million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue</td>
<td>36619</td>
<td>42907</td>
<td>44867</td>
</tr>
<tr>
<td>Growth % (yearly)</td>
<td>19.58</td>
<td>17.17</td>
<td>4.57</td>
</tr>
<tr>
<td>Growth % Average 3 Years</td>
<td>16.85</td>
<td>18.36</td>
<td>13.58</td>
</tr>
</tbody>
</table>

### Industry Growth:

<table>
<thead>
<tr>
<th></th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>Growth % (Yearly)</td>
<td>11.3</td>
<td>9.4</td>
<td>3.3</td>
</tr>
<tr>
<td>Growth % Average 3 Years</td>
<td>10.2</td>
<td>8.9</td>
<td>7.4</td>
</tr>
</tbody>
</table>

Pakistan Tobacco Company (PTC) is the market leader according to its market share. Its revenue has been increasing for the last 3 years. In 2016 the annual growth rate was 4.57% and average growth rate of 3 years was 13.58%. PTC has been doing great in the industry as both yearly and 3 year average growth rates are more than the industry. The overall market size has grown that has led to growth in revenues.

### Profitability Ratios:

<table>
<thead>
<tr>
<th>Ratios</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Margin %</td>
<td>37.8</td>
<td>43.2</td>
<td>50.8</td>
</tr>
<tr>
<td>Operating Margin %</td>
<td>19.4</td>
<td>24.1</td>
<td>33.4</td>
</tr>
<tr>
<td>Net Margin %</td>
<td>13.24</td>
<td>16.42</td>
<td>23.09</td>
</tr>
<tr>
<td>EPS %</td>
<td>9</td>
<td>18</td>
<td>32</td>
</tr>
<tr>
<td>ROA %</td>
<td>24.64</td>
<td>30.18</td>
<td>41.32</td>
</tr>
<tr>
<td>ROE %</td>
<td>72.26</td>
<td>76.69</td>
<td>88.78</td>
</tr>
<tr>
<td>ROIC %</td>
<td>57.12</td>
<td>64.03</td>
<td>80.97</td>
</tr>
<tr>
<td>Interest Coverage (Times)</td>
<td>73.56</td>
<td>148.21</td>
<td>336.64</td>
</tr>
</tbody>
</table>

The Gross Profit Margin, Operating Profit Margin and Net Margin has been increasing for the past three years. PTC has effectively controlled its costs that has led to increased margins along with increased revenues. The Earnings Per Share has increased 3.5 times from 9 in 2014 to 32 in 2016. The ROA of 41.32% is a measure that the company has used its assets effectively to generate revenues. The return on equity has also increased due to proportionally more increase in income than in capital. The interest coverage ratio of 336.64 indicate that PTC can pay 336 times the same interest from its net income.

### Liquidity Ratios:

<table>
<thead>
<tr>
<th>Ratios</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Ratio</td>
<td>1.06</td>
<td>1.20</td>
<td>1.52</td>
</tr>
<tr>
<td>Quick Ratio</td>
<td>0.05</td>
<td>0.05</td>
<td>0.21</td>
</tr>
<tr>
<td>Debt/Equity</td>
<td>0.05</td>
<td>0.04</td>
<td>0.02</td>
</tr>
</tbody>
</table>

The liquidity ratios indicate that the company’s financial position has improved over the time. The current ratio of 1.52 in 2016 indicates that for every 1rs of current liability the company has 1.52Rs of current Assets. The quick ratio is very low despite the current ratio being high is majorly due to a lot of investment in the inventories. The debt/equity ratio is 2% in 2016, this means that the debt is only a small proportion of the equity and company is very low geared.
### IFE Matrix:

<table>
<thead>
<tr>
<th>Factor</th>
<th>Weight</th>
<th>Rate</th>
<th>Weighted Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strength</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Strong Distribution Network</td>
<td>0.05</td>
<td>4</td>
<td>0.2</td>
</tr>
<tr>
<td>1st MNC to start tobacco processing in the area</td>
<td>0.07</td>
<td>3</td>
<td>0.21</td>
</tr>
<tr>
<td>Efficient time delivery (within 3 days from Production)</td>
<td>0.07</td>
<td>4</td>
<td>0.28</td>
</tr>
<tr>
<td>Market Leader</td>
<td>0.05</td>
<td>3</td>
<td>0.15</td>
</tr>
<tr>
<td>Strong Brand Name and image in customers mind</td>
<td>0.06</td>
<td>3</td>
<td>0.18</td>
</tr>
<tr>
<td>Consistent quality management</td>
<td>0.05</td>
<td>2</td>
<td>0.1</td>
</tr>
<tr>
<td>Environmental Standards achieved</td>
<td>0.06</td>
<td>3</td>
<td>0.18</td>
</tr>
<tr>
<td>Focus on health and safety on the company premises</td>
<td>0.05</td>
<td>2</td>
<td>0.1</td>
</tr>
<tr>
<td>Training and development of the employees</td>
<td>0.05</td>
<td>3</td>
<td>0.15</td>
</tr>
<tr>
<td>Influence on Government</td>
<td>0.04</td>
<td>2</td>
<td>0.08</td>
</tr>
<tr>
<td>Technology</td>
<td>0.06</td>
<td>3</td>
<td>0.18</td>
</tr>
<tr>
<td>Weaknesses</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Price gap is large between average and premium products (no in-between products)</td>
<td>0.07</td>
<td>3</td>
<td>0.21</td>
</tr>
<tr>
<td>Low profit margin, highly dependent on volume for profit realization</td>
<td>0.06</td>
<td>4</td>
<td>0.24</td>
</tr>
<tr>
<td>Other than its three main brands Dunhill, Captain and Gold-leaf other don’t have a significant demand</td>
<td>0.05</td>
<td>3</td>
<td>0.15</td>
</tr>
<tr>
<td>Innovate new flavors and products like electric cigarettes</td>
<td>0.06</td>
<td>3</td>
<td>0.18</td>
</tr>
<tr>
<td>Fear of losing jobs in employees due to downsizing</td>
<td>0.04</td>
<td>2</td>
<td>0.08</td>
</tr>
<tr>
<td>Minimum marketing compared to its competitors</td>
<td>0.05</td>
<td>2</td>
<td>0.1</td>
</tr>
<tr>
<td>Centralized system</td>
<td>0.06</td>
<td>3</td>
<td>0.18</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td></td>
<td>2.95</td>
</tr>
</tbody>
</table>

### Porter’s Five Generic Strategies:

**Cost Leadership Strategy:**
A primary reason for pursuing forward, backward and horizontal integration strategies is to gain low-cost leadership benefits. This strategy helps in achieving economies of scale, achieve maximum capacity utilization and linkages with suppliers and distributors. The basic idea is to under-price competitors and thereby gain market share and sales, entirely driving some competitors out of the market.
Supply Chain Model:
The model followed by the Pakistan Tobacco Company in Supply Chain activities is as follows: and they call it “from crop to consumer”.

Harvesting

Curing

Processing

Manufacturing

Trade Marketing & Distribution

Harvesting:
Since Virginia tobacco was non-native to this region of Pakistan, it was a tough task to initiate this crop across NWFP. The endeavour involved proper extension services in crop related cultural practices, consistent efforts in making tobacco a viable crop for the farmer community, and introducing mechanisms so that yield and quality can be improved. As a result of PTC activities Pakistan has become the 5th largest tobacco producer in the world and 4th highest in yield. It was only through consistent, farmer focused initiatives and developing closer relationships with their farmers that Pakistan Tobacco Company was able to achieve such feats.

The best practices in the tobacco production process introduced with the assistance of Pakistan Tobacco Company have had a national impact as these were later transferred to other crops. The benefits for the wider farming community due to these initiatives include:
- Research and introduction of high yielding, disease resistant, varieties of tobacco, and the free distribution of their seeds to growers.
- Polyethylene covers: Initially used for tobacco seed protection they are now being widely used for growing vegetables in all parts of the NWFP.
- Introduction of compound fertilizers NPK: This contributed to higher yield and quality improvements.
- Introduction of diesel water pumps: as a low cost alternative to supplement irrigation in the rain fed area of Buner, NWFP.
- Introduction of mechanical ploughing for tobacco cultivation in some areas in the NWFP.

Curing:
Curing is a carefully controlled process used to achieve the texture, colour and overall quality of a specific tobacco type. During the process, 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. Curing is done by the farmer after cultivation. The three curing processes commonly used in Pakistan are:
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 a central heating system. This controlled heat allows the leaves to turn yellow/orange, at which point the process is complete. 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 cures the leaves to a yellow to orange colour with high sugar content. Oriental tobacco is the most prominent among the sun cured 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 brings his bales to PTC leaf buying depots for sale from where it is sent to PTC’s Green Leaf Threshing Plant for further processing.

Processing and manufacturing:
After harvesting and curing, a Green Leaf Threshing plant processes the cured leaf. The main purpose of this processing is to:

- remove sand, dust, scraps and foreign matter;
- separate the lamina from the stem (threshing); and
- Drive down the moisture content to safe storage levels.

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

Manufacturing:
At the factory, the matured tobacco is checked for quality and then carefully blended with other ingredients which the brand recipe may call for, such as flavourings or pre-processed tobacco. Keeping track of the various types of tobacco and blend components is key and computers are increasingly used to track production runs. Moisture content is crucial. Too dry and the tobacco leaf will crumble; too moist and it may spoil during storage. The blended tobacco is treated with just the right amount of steam and water to make it supple and then cut into the form in which it appears in the cigarette. Excess moisture is then removed so the cut tobacco can be given a final blending and quality check.

Cigarette making, once done entirely by hand, is today almost fully automated, with the cut tobacco, cigarette paper and filters continuously fed into cigarette-making machines. The technology has advanced dramatically over the years, but quality is not forgotten; each cigarette is automatically quality controlled to ensure that it meets every benchmark for its specification. As packing machines put them into the familiar brand packs, wrap the packs in protective film, and group them into cartons and cases; further testing takes place at each stage to make sure the cigarettes are properly protected. The completed cases, time-dated to ensure the freshest product possible, are then ready for distribution.

PTC’s two manufacturing sites are located at Jhelum, Punjab and Akora Khattak, NWFP.

PTC’s aim is to build on our excellent Trade Marketing & Distribution capability, which bears all the hallmarks of a world-class field force for effective retailer and consumer contact.
Trade marketing is a large part of their marketing activities, managing business-to-business relationships with the retailers and distributors from whom their consumers buy products. They believe that their ‘win-win-win’ approach sets them apart in the market place. They don’t just focus on achieving their own goals, but aim to create benefits for their trade customers as well as their consumers. They work to operate in the most efficient and effective way so that retailers can offer the products their consumers want to buy, where and when they want to buy them, and at the right quality.

Their trade marketing field force provides value added services in complimenting the distribution effort, in select stores of the retail universe to enable mutually beneficial partnerships. They make substantial investment in retail, through quality in-store and on-store furniture and fittings to stock and display their products for the convenience of their consumers.

Around 250 exclusive distributors, employing a contingent of over 1,200 distribution representatives, provide direct store delivery services for their finished products to the 500,000 plus retail stores throughout the country. In doing so, they aim to optimize finished goods supply chain efficiencies in delivering products of consistent quality on-time, every time. The strong performance of their brands suggests that they are getting it right. Over recent years they have grown their brands, while remaining well within strict national laws regulating tobacco marketing, and voluntarily adopting their own International Marketing Standards.

**Trade marketing and distribution:**

Trade marketing is a large part of PTC marketing activities, managing business-to-business relationships with the retailers and distributors from whom customers buy products. PTC trade marketing field force provides value added services in complimenting the distribution effort, in select stores of the retail universe to enable mutually beneficial partnerships.

**Summary:**

Pakistan Tobacco Company in the last three years have experienced double digit growth and has controlled its costs effectively. The profitability ratios shows that company is in great position. The liquidity ratios indicate that the company has invested greatly in inventories and that can cause liquidity problems in the short term. There is a need to effectively manage inventories to overcome these possibilities. The second issue that PTC could incur is due to its centralized systems. PTC needs to decentralize some divisions such as Human resource, Marketing, Sales and Production. Decentralization of these divisions could help in more affective decision making.
VI. Strategy Formulation

SWOT Analysis

Strength
- Strong distribution network
- 1st MNC to start tobacco processing in the area
- Biggest FMCG
- Efficient time delivery (within 3 days from production)
- Consistent quality management of whole product range
- Strong brand name and image in customers mind
- Market leader

Weakness
- Price gap is large between average and premium products (no in-between products)
- Low profit margin, highly dependent on volume for profit realization
- Other than its three main brands Dunhill, Captain and Gold-leaf other don’t have a significant demand
- Decrease in prices of almost half the product range
- Decreased prices to capture more market share and reposition prices in the minds of the consumers.
- Considering its vision statement they can plan business ventures beyond tobacco products
- Introduce products between the extreme ends products
- Innovate new flavours and products like electric cigarettes

Opportunities
- Industry Growth
- Young smokers
- Promising mid Tar segment

Threats
- Illicit cigarettes
- Levy of heavy taxes and duties
- New products like vape and e-cigarettes are selling which can substitute tobacco cigarettes.
### Space Matrix

<table>
<thead>
<tr>
<th>Financial Position</th>
<th>Score</th>
<th>SP</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Return on investment</td>
<td>6</td>
<td>Technology changes</td>
<td>-5</td>
</tr>
<tr>
<td>Leverage</td>
<td>4</td>
<td>Role of inflation</td>
<td>-5</td>
</tr>
<tr>
<td>Liquidity</td>
<td>5</td>
<td>Demand variability</td>
<td>-5</td>
</tr>
<tr>
<td>Working capital</td>
<td>6</td>
<td>Price range of competing products</td>
<td>-3</td>
</tr>
<tr>
<td>Cash flow</td>
<td>6</td>
<td>Barriers to entry into market</td>
<td>-2</td>
</tr>
<tr>
<td>Inventory turnover</td>
<td>6</td>
<td>Competitive pressure</td>
<td>-3</td>
</tr>
<tr>
<td>Earnings per share</td>
<td>6</td>
<td>Ease of exit</td>
<td>-5</td>
</tr>
<tr>
<td>Price earnings ratio</td>
<td>5</td>
<td>Price elasticity of demand</td>
<td>-2</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Risk involved</td>
<td>-3</td>
</tr>
<tr>
<td>Average</td>
<td>5.5</td>
<td>Average</td>
<td>-3.67</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>CP</th>
<th>IP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market share</td>
<td>-2</td>
</tr>
<tr>
<td>Product quality</td>
<td>-2</td>
</tr>
<tr>
<td>Product life cycle</td>
<td>-3</td>
</tr>
<tr>
<td>Customer loyalty</td>
<td>-3</td>
</tr>
<tr>
<td>Capacity utilization</td>
<td>-4</td>
</tr>
<tr>
<td>Technology know how</td>
<td>-3</td>
</tr>
<tr>
<td>Control over suppliers and distributors</td>
<td>-4</td>
</tr>
<tr>
<td>Average</td>
<td>-3</td>
</tr>
</tbody>
</table>

X-axis: -3 + (+5.14) = 2.14
Y-axis: -3.67 + (5.5) = 1.83

#### Aggressive (PTC)
- Backward, forward, horizontal integration
- Market penetration
- Market development
- Product development
- Diversification

#### Competitive
- Backward, forward, horizontal integration
- Market penetration
- Market development
- Product development

#### Conservative
- Market penetration
- Market development
- Product development
- Related diversification

#### Defensive
- Retrenchment
- Divestiture
- Liquidation

#### Competitive
- Backward, forward, horizontal integration
- Market penetration
- Market development
- Product development
BCG Matrix

Market Growth Rate

High

Low

Relative Market Share

High

Low

- Dunhill
- Benson STAR
- Gold leaf
- Capstan
- Embassy

COW

DOG

IE Matrix

EFE

IFE

<table>
<thead>
<tr>
<th></th>
<th>4.0</th>
<th>3.0</th>
<th>2.0</th>
<th>1.0</th>
</tr>
</thead>
<tbody>
<tr>
<td>3.0</td>
<td></td>
<td></td>
<td>2.95, 2.66</td>
<td></td>
</tr>
<tr>
<td>2.0</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1.0</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Grand Matrix

**Quadrant II**
1. Market development
2. Market penetration
3. Product development
4. Horizontal integration
5. Divestiture
6. Liquidation

Rapid Market Growth

**Quadrant I (PTC)**
1. Market development
2. Market penetration
3. Product development
4. Forward integration
5. Backward integration
6. Horizontal integration
7. Related diversification

**Quadrant III**
1. Retrenchment
2. Related diversification
3. Unrelated diversification
4. Divestiture
5. Liquidation

**Quadrant IV**
1. Related diversification
2. Unrelated diversification
3. Joint ventures

Slow Market Growth

Weak Competitive Advantage

Strong Competitive Advantage
## Quantitative Strategic Planning Matrix (QSPM)

<table>
<thead>
<tr>
<th></th>
<th>Strategy 1</th>
<th>Strategy 2</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Backward Integration</td>
<td>Brand love/loyalty</td>
</tr>
<tr>
<td><strong>Strengths</strong></td>
<td>Weight</td>
<td>AS</td>
</tr>
<tr>
<td>Strong Distribution Network</td>
<td>0.05</td>
<td>3</td>
</tr>
<tr>
<td>1st MNC to start tobacco processing in the area</td>
<td>0.07</td>
<td>3</td>
</tr>
<tr>
<td>Efficient time delivery (within 3 days from Production)</td>
<td>0.07</td>
<td>3</td>
</tr>
<tr>
<td>Market Leader</td>
<td>0.05</td>
<td>4</td>
</tr>
<tr>
<td>Strong Brand Name and image in customers mind</td>
<td>0.06</td>
<td>3</td>
</tr>
<tr>
<td>Consistent quality management</td>
<td>0.05</td>
<td>3</td>
</tr>
<tr>
<td>Environmental Standards achieved</td>
<td>0.06</td>
<td>3</td>
</tr>
<tr>
<td>Focus on health and safety on the company premises</td>
<td>0.05</td>
<td>2</td>
</tr>
<tr>
<td>Training and development of the employees</td>
<td>0.05</td>
<td>4</td>
</tr>
<tr>
<td>Influence on Government</td>
<td>0.04</td>
<td>3</td>
</tr>
<tr>
<td>Technology</td>
<td>0.06</td>
<td>3</td>
</tr>
<tr>
<td><strong>Weaknesses</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Price gap is large between average and premium products (no in-between products)</td>
<td>0.07</td>
<td>2</td>
</tr>
<tr>
<td>Low profit margin, highly dependent on volume for profit realization</td>
<td>0.06</td>
<td></td>
</tr>
<tr>
<td>Other than its three main brands Dunhill, Captain and Gold-leaf other don’t have a significant demand</td>
<td>0.05</td>
<td></td>
</tr>
<tr>
<td>Innovate new flavours and products like electric cigarettes</td>
<td>0.06</td>
<td>3</td>
</tr>
<tr>
<td>Fear of losing jobs in employees due to downsizing</td>
<td>0.04</td>
<td></td>
</tr>
<tr>
<td>Minimum marketing compared to its competitors</td>
<td>0.05</td>
<td>1</td>
</tr>
<tr>
<td>Centralized system</td>
<td>0.06</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>1.00</td>
<td></td>
</tr>
<tr>
<td><strong>Opportunities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industry Growth</td>
<td>0.05</td>
<td>4</td>
</tr>
<tr>
<td>Young smokers</td>
<td>0.07</td>
<td>4</td>
</tr>
<tr>
<td>Promising mid Tar segment</td>
<td>0.05</td>
<td>2</td>
</tr>
<tr>
<td><strong>Threats</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Scarcity of raw material</td>
<td>0.07</td>
<td>4</td>
</tr>
<tr>
<td>Illicit cigarettes</td>
<td>0.07</td>
<td>2</td>
</tr>
<tr>
<td>Levy of heavy taxes and duties</td>
<td>0.06</td>
<td>2</td>
</tr>
<tr>
<td>New products like vape and e-cigarettes are selling which can substitute tobacco cigarettes</td>
<td>0.04</td>
<td>3</td>
</tr>
<tr>
<td>“Prohibition of Smoking and Protection of Non-Smokers Health” Ordinance 2002</td>
<td>0.04</td>
<td></td>
</tr>
<tr>
<td>Controversy over Tobacco Support Price (Possible Hike)</td>
<td>0.06</td>
<td>3</td>
</tr>
<tr>
<td>Tax Evading Sector</td>
<td>0.05</td>
<td>3</td>
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<tr>
<td>Framework Convention on Tobacco Control (FCTC)</td>
<td>0.04</td>
<td></td>
</tr>
<tr>
<td>TV Ads Banned</td>
<td>0.02</td>
<td>3</td>
</tr>
<tr>
<td>Anti-Smoking Ordinance</td>
<td>0.06</td>
<td></td>
</tr>
<tr>
<td>Local Firms Gaining Share and Experience</td>
<td>0.06</td>
<td>4</td>
</tr>
<tr>
<td>Smuggling and low priced counterfeit</td>
<td>0.06</td>
<td>1</td>
</tr>
<tr>
<td>Tobacco Free Initiative in Pakistan</td>
<td>0.05</td>
<td></td>
</tr>
</tbody>
</table>
Summary:
According to the space matrix, PTC should take an aggressive approach to the market, which involves:
  - Backward, forward, horizontal integration
  - Market penetration
  - Market development
  - Product development
  - Diversification

Backward integration can be carried out since PTC has no formal agreement with their suppliers. The farmers who grow the tobacco on the fields sell the tobacco to PTC. Either an agreement or an establishment of their own tobacco fields would be a wiser decision. They need to penetrate in the market by developing a market for middle class smokers as PTC either has really expensive cigarettes or really cheap cigarettes. Product development and diversification can be carried out by either introducing vapes or introducing new flavors to their cigarettes. The QSPM also supports the idea of backward integration with scores directing clearly towards this strategy. The rest of the matrices shows how PTC has a huge brand name in the market and just needs to utilize its brand name efficiently to boost sales and to increase the market share.

VII. Objectives, Strategy Recommendations and Action Plan

Objectives and Action Plan:
Since PTC’s market share has seen a decline this year because of various factors. Following are the strategic and financial objectives

Financial objectives:
  - To increase and maintain the market share of the company to 44-45% for the next 3 years
  - To increase the annual sales by 8%
  - To reduce the cost of sales by 12%
  - To increase the debt to equity ratio to at least 1:2

Strategic Objectives:
  - To make the production and supply chain more efficient by integrating backwards
  - Reduce product prices
  - To reduce tax expenses
  - To diversify products and target new segments

Business and organizational strategies:
PTC’s market share was 42% in 2016 which decreased by the end of the year to 40% because of various reasons but mostly because of the fact that the illicit trade of the cigarettes is on the rise and it is taking a huge chunk of the market share. PTC is relying completely on the government to make strict policies to stop the illicit trade. The company should instead take some measures itself to tackle this situation because the politics of Pakistan is very volatile and the policies change with every new government. PTC should reduce the prices of all of their products.
cigarette brands leaf to an extent where it seems attractive to the customer so that even if the policies are not favourable, the company can boost its sales to some extent. When the sales will improve the cost of sales will also drop which is necessary considering the difference between sales and cost of sales is very low. In addition to that the debt of the company has also increased since last year and the debt to equity ratio is 0.84 which is falling below the idle situation. So it is very important for the company to increase its sales so that it can pay its debts easily.

PTC should follow a backward integration strategy and buy its own land to grow tobacco itself. Because PTC does not have a lot of formal contracts with farmers for longer durations it depends more on the third party suppliers to deliver. If PTC buys lands that are closer to its production units not only will it improve the supply chain it will also reduce the unnecessary costs which come while bargaining with the suppliers. The operations will also improve as the company will produce depending on the demand of the product in the market so there won’t be an excess of product. In addition to that the company can create job opportunities for farmers and educate them with the modern technology used in agriculture industry.

Another strategy PTC can implement is to invest in its R&D department, basically hire some experts in taxation who can collaborate with the finance department and figure out possible ways to reduce tax expenses. This will not only increase the income but it will also give the company the opportunity to invest in other places like buying lands and machinery as already mentioned above.

One possible strategy for PTC can be to diversify its products. For instance it can introduce flavoured cigarettes under the cheap brand like “Gold flake”. This product can be targeted at the people especially younger people who are fond of “sheesha”.

VIII. Interview Transcript

Q1. Please explain the efficiency of PTC’s business model and strategic model.
PTC manufactures and delivers products that includes Tobacco and beyond. PTC’s business model includes running operations at the right pace and speed scale. Any particular cigarette that PTC produces will be available in the market within 3 days. The operations process of PTC is from “Seed to Smoke”. They manufacture from the beginning. Third party farmers with whom PTC does not have a formal contract are helped to grow the right kind of high quality tobacco, which the company then buys. They have a trademark supply chain to deliver to the consumer.

Tobacco Auction
The tobacco is bought from annual auctions. Only Green leaf tobacco (GLT) is harvested. The tobacco bales are sent to Jehlum factory for processing

Manufacturing
One machine can produce 10,000 cigarettes per minute. There are 8 such machines in Jhelum factory.

Storage
Factories are managed by the supply chain function. Their ware houses are called Depos. In Lahore the Mohlan-wall depo can store 1 billion sticks. Sticks is a unit of measurements for cigarettes in BATC.

Distribution
BATC calls its distributors valued business partners and they transport packed cigarettes from PTC to the retailers and eventually to the end consumers. Allied Marketing is the biggest distributor of PTC cigarettes.

Retail landscape
The retail side PTC has three types of retail shops.
1. Pay & Go
2. Shop & Browse
3. Entertainment

**Pay & Go**
In pay & go customers, know what they want. They just come, ask for the product and pay for it. Pay and go includes shops with small cigarette counters at cashier desks.

**Shop & Browse**
Opened sometime exploring the aisles they spend at least 5 minutes in the shop.

**Entertainment**
This segment includes selling cigarettes in cafes or other places, which have some form of entertainment like, snooker club, Shisha Cafes.

**Value for money Segments**
This includes the road side eateries (Khokas) PTC delivers their products to tobacco handlers which are its customers there then delivered them to consumers in flexible quantities and prices by altering the PTC made packages.

**Q2. What is the most important success factor for PTC?**
Consistency is the most important factor for PTC's success the quality is never compromised because any change in taste or quality of the product will lead to dissatisfied customers it is difficult to maintain consistent because the company has to ensure that different types of tobacco leaves and machines provided the desired results through varying combination.

**Trade marketing**
PTC operates according to trade marketing and distribution. PTC has a national strategy for a country. Distribution standards of PTC are top notch. In fact many FMCG’s find PTC’s distributors to distribute their own products because of their high standards.

**Q3. Main opportunities and threats for PTC.**
PTC produces 80 billion sticks per year approximately external threats include elicit cigarettes, which evade taxes, and the legit cigarette. Since the company is not allowed to do any above the line or below the line advertising for its consumers, it is a major hindrance to promote their products. Company can only do direct one to one initiative to convince consumers and for that, they have brand representatives. The illicit cigarettes are a major threat as they do not pay any duly small brands generally undersell or underquote.
The international smuggled cigarettes are also a major threat, as the company does not make much money on them. They are produced to be sold to a different market with different dynamics. When they are sold in the country, they take away shares from locally produced PTC cigarettes.

If international smuggled cigarettes are of another brand other than the British American Tobacco company, which is the parent company of PTC, then again PTC loses money and loses market share.

In the legit sector, PTC is the market leader. Due to low cost illicit cigarettes, share of capstan decreases

**External Opportunities** includes down trading. Recently PTC lowered prices of some of its cigarettes to combat illicit market.

A main internal threat is that PTC does not have a cigarette priced for middle group between the high end and low-end priced cigarettes.

**Q4. Alternative company strategy**
The company wants to expand and that is why it has an alternative strategy. It includes the beyond covering non-tobacco based offerings. There are non-combustible products like snuff, currently it is not popular in Pakistan and is known as Tara. The coffee beans based product line is also launched under this motto and is known as Davidoff. Another alternative strategy is to launch a Pakistan only cigarette to counter Marlboro.
Q5. What is PTC’s value proposition and is it being clearly communicated?
The value proposition of PTC is to provide high quality products of tobacco and beyond with consistency in quality, taste etc. The next step for the company would be brand love. The company would work on increasing the brand love of the company to make it even more successful. It is inspired by brand love of Coca-Cola.

Q6. When developing and implementing strategy, does the organization effectively balance short and long term priorities?
The long and short term strategies of the company are very well connected. The repositioning of prices is a long term strategy which would benefit the company immensely. The prices of some cigarettes like Capstan by Paul Mal were decreased. The company’s short and long term strategies are well connected to each other like a well-oiled machine.

Q7. How much ease and expense is required for PTC consumers to switch to a competitor’s offering?
It is hard to switch products in the tobacco category. There are two categories here:
1. The adult under 30: the adult under 30 are more prone to change their cigarette brand so company policy is to target this segment to make sure that they smoke PTC products.
2. The adults over 30: the consumers in this category rarely change brand. The goal is to make sure that adults under 30 change their brand to PTC cigarettes and then become a long term customer over 30.

PTC employee’s goods on one on one marketing strategies to get more customers to switch to their brand.

Q8. How frequently does PTC deliver new value adding ideas to its customers to keep them engaged?
PTC launches new products after they check market demand in a particular segment. Then their brand ambassadors actively work to engage new and potential customers.

Q9. Considering factors such as competition and timing of discounts, does PTC provide the right amount of discounts and at the right price
PTC offers a window to operate and gives discount to its retailers at certain times but no direct discounts are given to consumers.

Q10. How often does PTC covert leads for potential sales into actual sales in the long run
There is no set conversion rate according to timeframe as direct human interaction is involved. People who switched to other brands are coming back to use PTC products after prices were reduced. This repositioning is a strategy which will show results in 2020.

Q11. To what extent could substitute products or services be a threat to competitors in this industry?
Substitute products like low cost illegal cigarettes are a major threat as their increase in market share is a loss for the legitimate cigarette companies and a major loss of revenue for the government as well.