THE EFFECT OF THE IMPLEMETATION OF TOBACCO CONTROL ACT 2007 ON FINANCIAL PERFORMANCE OF CIGARETTES MANUFACTURING FIRMS IN KENYA: THE CASE OF BAT KENYA LTD

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A RESEARCH PROJECT SUBMITTED TO
THE SCHOOL OF HUMAN RESOURCE DEVELOPMENT,
IN PARTIAL FULFILLMENT OF THE REQUIREMENT FOR THE
AWARD OF DEGREE IN EXECUTIVE MASTERS IN BUSINESS
ADMINISTRATION OF JOMO KENYATTA UNIVERSITY OF
AGRICULTURE AND TECHNOLOGY

SEPTEMBER 2011

DECLARATION

This Research Project is my original work and has not been presented for award of a degree to any other university.

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DEDICATION

I dedicate this research to my daughter Lisa who challenged me in the year 2008 and gave me inspiration to attain an MBA degree.

ACKNOWLEDGEMENT

Special gratitude should go to my supervisors, Dr. C. Ombuki and Mr. W. Muturi for their advice and guidance during the preparation of this Research Project. I am also indebted to my wife Esther , our children Angela ,Lisa and Jerry for their patience and understanding during the long hours I spent on this research at the expense of providing the necessary fatherly companionship.

ABSTRACT

Tobacco Control Act 2007 which became effective in Kenya from July 2008 was meant among others to regulate the production, sale, advertising and promotion of tobacco products and ultimately control cigarettes smoking. When the tobacco regulations were implemented by the government, the cigarettes manufacturing companies were up in arms complaining that the Act would put them out of business. This study sought to determine whether the Act has affected the financial performance of BAT (K) Ltd. Thus, the study sought to find out whether the Act has affected the trend of profit before tax, marketing expenditure, sale revenue of cigarettes, and staff benefits costs. Study involved collecting secondary data from BAT (K) Ltd's Annual Financial Reports for the period 2006 to 2010. BAT was used as a case study as it controls 81% of the market share and company is therefore a good representative of the cigarettes manufacturers in Kenya. The study entailed a before-and-after implementation analysis and presentation of the financial data in form of time series graphs. The data analysis also involved use of tables, graphs and percentages that show trends that indicate the impact of the Act on the research variables. Descriptive research approach was used to interpret the data and draw conclusions. The study established that the Tobacco Control Act 2007 has affected the financial performance of BAT (K) Ltd as its annual profits before tax, marketing expenditure and staff-benefits costs have continued to reduce from 2009 after the Act was implemented. The study recommends that future Kenya government's policies and regulation on sale and consumption of tobacco products should focus on educating tobacco consumers on health risks of smoking cigarettes (control demand) rather than imposing regulations on sale of cigarettes (control supply) which has had adverse effect on the financial performance of cigarettes manufacturing companies as revealed by this study.

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ABBREVIATIONS

BAT : British American Tobacco Kenya Limited

ACT : Tobacco Control Act , 2007

IARC: International Agency for Research on Cancer

MDC : Marketing and Distribution Costs

PBT : Profit Before Tax

SBC : Staff Benefits Costs (salaries and wages)

SOG : Sale Revenue of Goods (cigarettes)

WHO : World Health Organization

DEFINITION OF OPERATIONAL TERMS

Tobacco Control: Measures that regulate the manufacture, sale, labelling, advertising and promotion of tobacco products and also the regulation of smoking to designated public places (Tobacco Control Act, 2007)

Financial Performance: Financial growth indicators of cigarette manufacturing firms in terms of sales revenue of cigarettes, marketing expenditure, staff benefits costs and profitability

Outcome: Performance or change of the dependent variables in this Research

Marketing Expenditure: Annual cost of marketing and distribution of Cigarettes

Profitability: Annual profit before tax

Staff Benefits Costs: Annual expenditure on staff salaries, wages and other benefits

Sales Revenue: Annual revenue from local sale of cigarettes in Kenya

CHAPTER ONE

INTRODUCTION

1.1 INTRODUCTION

This study attempts to find out the impact of the implementation of Tobacco Control Act 2007 on financial performance of BAT Kenya Ltd for the years 2006- 2008 and years 2009 - 2010 using a before and after implementation of Act analysis of data collected. According to Philip Kottler (2008) business regulations has four main purposes, which are; to protect companies from unfair competition, to protect consumers from unfair business activities, to protect the interests of the society from unbridled business behaviour and to charge businesses with the social costs created by their products or production process.

Pearce and Robinson (1997) reckon that the direction and stability of political factors are a major consideration for managers on formulating company strategies. Political constraints are placed on firms fair-trade decisions through; antitrust laws, tax programmes, control regulations, pollution and pricing policies by the government. Such laws and regulations are mostly restrictive and tend to reduce the profits of firms. One such law is the Tobacco Control Act of 2007 which became effective in Kenya from July 2008.

1.2 BACKGROUND OF THE STUDY

The tobacco industry contributes substantially to the economies of more than 150 countries, with more than 100 million people worldwide depending on it for employment. Tobacco taxes are a major source of revenue for most governments in the world. In Kenya and Brazil, the tobacco tax revenue is about six per cent of the total annual taxes collected (K'Obonyo P.O, 1998).

Tobacco is the world's most widely cultivated non-food crop. The farmers who choose to grow it, many of them in developing countries, do so because it is hardy, grows well in poorer soils and volatile weather, and is known for fetching stable prices.

Farmers can earn good yields from very small plots of tobacco, enabling them to put tobacco earnings into growing other food crops. The farming techniques used for growing tobacco also help to improve the yield of other food crops.

Most countries have tobacco manufacturing industry, and the industry usually forms an important component of the economic and social fabric of the economy. Even in countries that do not have tobacco manufacturing firms, tobacco marketing and distribution is an important source of national income and taxes.

1.3 THE TOBACCO INDUSTRY IN KENYA

Kenya's tobacco industry comprises of two key players, namely British American Tobacco (K) Ltd and Mastermind Tobacco (K) Ltd. British American Tobacco Kenya, Ltd. engages in the manufacture and sale of cigarettes in Kenya. It offers its products primarily under various brands, such as Dunhill, Benson & Hedges, Pall Mall, Embassy, Sportsman, Sweet Menthol, Crown Bird, Safari, Score, Rooster, and Crescent & Star. The company also undertakes contract manufacturing services for tobacco related products. British American Tobacco Kenya Ltd has it's headquarter in Nairobi, Kenya. British American Tobacco Kenya Ltd is part of the British American Tobacco Group. Mastermind Tobacco (K) Ltd also engages in the manufacture and sale of cigarettes in Kenya. It specializes in products such as Summit Lights, Supermatch Kings, Supermatch Menthol, Ralli Kings, Ralli Menthol, Rocket and Comet.

1.4 OVERVIEW OF TOBACCO CONTROL ACT 2007

The first attempt to control the tobacco industry was made in the 1980s by the then, Minister for Health. In a legal notice dated July 31st 1984, The Minister enforced the printing of the warning, "cigarette smoking can be harmful to your health", in English and Kiswahili; on all cigarette packets (The Mastermind Times, 2008). Under pressure from a growing anti-smoking lobby groups and international health agencies, Kenya's health authorities have toyed with the idea of enacting more stringent anti-tobacco legislation since 1995.The first Anti-tobacco Bill 1999 was drafted, and then shelved without explanation (The Mastermind Times, 2008).

In 2002, the Anti-tobacco Bill was tabled in parliament but was delayed until 2007 when it was passed into law. The Act came into force in July 2008.The Act sought to align Kenya's anti-tobacco legislation with laws in most of the developed countries, where strong anti-smoking lobbies have forced governments to impose strict controls on the sale and use of tobacco products. The purpose of the Tobacco Control Act 2007 was to provide a legislative response to national public health problem of substantial and pressing concern and, in particular, to protect the health of Kenyans in the light of conclusive evidence implicating tobacco use to incidences of numerous debilitating and fatal diseases. Protection of minors and other venerable people from inducements to use tobacco products and the consequent dependence on them and to enhance public awareness of the health hazards of using tobacco products. The Act substantially strengthens existing regulations by; enacting comprehensive bans on tobacco products advertising, promotion and sponsorship; explicitly prohibiting sales of cigarettes to minors and taking other measures to make it more difficult for people under 18 to buy cigarettes, such as banning single-stick and vending-machine sales. National Tobacco Control Board was created with strong powers to implement and enforce the legislation. The Board excludes cigarettes manufacturers' participation and is made up of 15 members from government and civil-society organizations.

Although tax increases are the most cost-effective approach to controlling tobacco consumption, this public health measure is grossly under utilized in Kenya. In many cases, the reasons for under utilization are complex, as demonstrated by Kenya government opting to establish tobacco control regulations. The Tobacco Control Act 2007 bans smoking in all public places in Kenya. It clearly defines public places, and ensures that owners and managers of indoor public places provide smokers with access to specifically designated smoking areas (DSA). Public places according to this law include all enclosed and partially enclosed places. It particularly bans smoking in open places such as stadium, bus termini and public recreation gardens and parks. This Act bans smoking in public transport vehicles and any other conveyance and also bans smoking in schools, hospitals and homes. The Act also expands protection against second-hand smoke by banning smoking in most public places and workplaces. Any person who smokes in a prohibited smoking area commits an offence and shall, on conviction, be liable to a fine not exceeding Kshs.50,000/= or to imprisonment for a term not exceeding six months, or to both.

1.5 STATEMENT OF THE PROBLEM

The role played by Cigarette manufacturing firms in terms of generating tax revenues for the government, foreign exchange generation, creation of direct employment of people working in the firms and others working in tobacco farms cannot be understated. Health concerns, however, have led the Kenya Government to make efforts to control cigarettes smoking. One such effort was the legislation of the Tobacco Control Act 2007. The intention of the Tobacco Control Act 2007 was inter alia, to regulate the production, sale, advertising and promotion of tobacco products and ultimately control cigarettes smoking. When the bill was introduced in 2002, there was an outcry from cigarette manufacturing companies that the move would affect their financial performance .When eventually, the Act was affected in 2008, the cigarettes manufacturing companies were up in arms complaining that the Act would put them out of business. It was not clear then, what impact the Act has had on financial performance. This is what this study undertook to find out.

1.6 OBJECTIVES OF THE STUDY

The main objective of the study was to determine the effect of the implementation of the Tobacco Control Act of 2007 on the financial performance of BAT Kenya Limited using profit before tax , sales revenue of cigarettes, marketing expenditure on cigarettes and staff benefits costs as indicators of company's financial performance.

The specific objectives were:

1. To find out the effect of the Tobacco Control Act 2007 on the profit before tax of BAT Kenya Limited.
2. To determine the effect of Tobacco Control Act 2007 on the sales revenue of cigarettes for BAT Kenya Limited.
3. To determine the effect of Tobacco Control Act 2007 on marketing expenditure on cigarettes by BAT Kenya Limited.
4. To find out the effect of Tobacco Control Act 2007 on the staff benefits cost for employees of BAT Kenya Limited.

1.7 RESEARCH QUESTIONS

1. What is the effect of Tobacco Control Act 2007 on the profit before tax of BAT Kenya Limited?
2. How has the Tobacco Control Act 2007 affected the sales revenue of cigarettes for BAT Kenya Limited?
3. How has Tobacco Control Act 2007 affected the marketing expenditure on cigarettes by BAT Kenya Limited?
4. What is the effect of Tobacco Control Act 2007 on the staff benefits cost for employees of BAT Kenya Limited?

1.8 JUSTIFICATION OF THE STUDY

A study done by Mwangi (2002) to determine the effects of tobacco regulation on the marketing mix variables found out that the tobacco industry can no longer freely use the traditional marketing mix elements to promote sale of tobacco products.

Mwangi's research was based on the Tobacco Control Bill of 1999 which was later shelved by Kenya government after stiff opposition by cigarettes manufacturers. Since the passing into law of the Tobacco Control Act in 2007, no local research has been conducted in Kenya specifically to determine the effects of Tobacco Control Act 2007 on cigarettes manufacturing firms in Kenya. This study was therefore an attempt to find out the effect of the implementation of the Tobacco Control Act 2007 on the sales revenue of cigarettes, marketing expenditure, profit before tax and staff benefits cost of employees in the cigarette manufacturing industry in Kenya, using BAT Kenya Limited as a case study. The findings of this study will be important to the government of Kenya as cigarettes manufacturers are major tax payers and employers.

1.9 THE SCOPE OF THE STUDY

The case study was carried out on British American Tobacco Kenya Limited which has it's headquarter in Nairobi. BAT controls 81% market share in Kenya and its financial data gives a good representation of the financial performance of cigarettes manufacturers in Kenya. The study analysed data for the period 2006 to 2010 both years inclusive.

1.10 LIMITATION OF STUDY

The limitation of this study was the challenge of collecting research information from BAT Kenya. Getting published annual financial reports from BAT Kenya Ltd dating back to 2006 was a big challenge and author had to rely on contacts in Capital Markets Authority for assistance. Efforts to get clearance from BAT's Corporate Affairs office to have my research questionnaires filled by employees of BAT were unsuccessful. I was however lucky to get a manager from the marketing department who agreed to complete one questionnaire (Appendix II)

CHAPTER TWO

LITERATURE REVIEW

2.1 INTRODUCTION

This chapter reviews past studies in other parts of the world and even Kenya. The chapter is organized according to the conceptual framework in order to ensure relevance to the research problem of finding out the impact of Tobacco Regulations on financial performance of companies using profitability, sales revenue of cigarettes, marketing expenditure and staff benefits costs as performance indicators.

2.2 GLOBAL TOBACCO REGULATIONS

Tobacco Regulation refers to the laws which govern how the tobacco is grown, its manufacture, marketing and sale (BAT Training Manual, 2005). Regulation on tobacco worldwide is driven by World Health Organization (WHO) Framework Convention on Tobacco Control.

The WHO Framework Convention on Tobacco Control, which came into effect on 27 February 2005, requires that all of the 168 countries that agreed to the treaty, ban tobacco advertising unless their country's constitution forbade them (International Agency for Research on cancer, 2004). Some countries also imposed legal requirements on the packaging of tobacco products. For example, in the countries of the European Union, Turkey, Australia and South Africa, cigarette packs must be prominently labelled with the health risks associated with smoking. Canada, Australia, Thailand, Iceland and Brazil have also imposed that labels on cigarette packs must warn smokers of the effects, with graphic images of the potential health effects of smoking. In South Africa, the Tobacco Products Control Amendment Act was passed into law in 1999. This Act bans all advertising and promotion of tobacco products, including sponsorship and free distribution of tobacco products. Kenya effected the Tobacco Control Act 2007 in July 2008.

Despite a few 17th century restrictions, significant anti smoking legislation was not enacted until the second half of the 19th century, primarily in response to the fire hazard created by smoking (Jacobson, Wasserman, and Anderson, 1997). Two themes characterized this early legislation: one theme focused on the fire hazard created by smoking while the other concentrated on the morality of smoking. Eventually, opposition to smoking on moral grounds was swept aside by the economic benefits associated with tobacco production and consumption.

2.3 TOBACCO REGULATION IN KENYA

In Kenya, Tobacco Control Bill, originally planned for enactment in 2002, was finally passed by the Kenyan parliament on August 2007 and assented to by the President in November 2007. The Act took effect in July 2008, eight months after being made into law (Kenyan law cases, 2009).The Tobacco Control Act has had a groundbreaking effect on the tobacco industry, with several of its provisions requiring radical regulation to the production and consumption of tobacco products. The key areas of focus of the Tobacco Control Act 2007 are requirement of larger packaging of cigarettes with rotational health warnings, restrictions of smoking in closed public places, ban of any form of advertising and sales promotions, restrictions on brand sponsorships and sale of cigarette sticks. From 2008, the local authorities in major cities implemented the controls to outlaw smoking in public places. In the cities of Nairobi, Mombasa and Kisumu as well as other larger towns country wide measures were taken over the years to ban public smoking, with arrests and fines being imposed to enforce the law (Kenyan law cases, 2009)

2.4 LITERATURE REVIEW ON RESEARCH VARIABLES

2.4.1 Impact of Tobacco Regulation on Profitability

A study conducted by Deloitte and Touche (2004) for the National Restaurant Association in the United States found a significant negative impact of tobacco legislation on profits.

The study examined the impact of government imposed smoking bans on the sales and profits of individual table service restaurants. The analysis used data from national samples of restaurants collected during the period 1990 – 2000. The study included information on the features of the ordinances applicable to the restaurants and the economic and demographic characteristics of the communities where the restaurants were located.

The Deloitte study found that there was a temporary negative impact on restaurant gross profits in cases where 100 percent smoking bans were in effect. The decline in annual gross profits was roughly 49 percent at restaurants where such bans were enacted two years prior to the survey. Annual gross profits declines were estimated at 37 percent at restaurants where these bans were enacted four years earlier (Deloitte & Touche, 2004).

Obwino (2003) study on Consequences of Government Tobacco Control in Kenya concluded that 60% of respondents interviewed from select sample from cigarettes manufacturing companies indicated that government will loss tax revenue from Tobacco industries due to reduced profitability if tobacco control policies were implemented by the Kenya government. The study also found out that 31 % of the respondents indicated that tobacco companies will divest from Kenya if tobacco control policies were implemented.

2.4.2 Impact of Tobacco Regulation on Sales Revenue

The objective of a study by Lal .A, et al (2009) in Australia was to examine the impact of smoke-free policies on sales revenue in Tasmanian bars in Australia. Monthly sales revenue from January 2002 to March 2007, provided by the Australian Bureau of Statistics (ABS) was analysed. Time series analysis was used to assess the impact of the smoke-free policy.

The above study was the first to examine the effect of a totally smoke-free policy in bars in Australia.

Smoke-free in restaurant laws in Tasmania were implemented on 1 September 2001. Tasmania was the first state in Australia to introduce smoke-free laws in bars, pubs and licensed clubs on 1 January 2006 In 2001, Tasmania had a population of 472 000 people, about 2.5% of the total population of Australia. There were 521 pubs and licensed clubs in the state in the financial year 2007. The aim of this study was to assess the impact of the smoke-free law on sales revenue in Tasmanian bars. Source of data was from pub, bar, tavern and licensed club. Sales revenue data were obtained from the Retail Trade Survey undertaken by the Australian Bureau of Statistics (2007). This survey aimed to provide information about month-to-month movement of retail sales revenue across all retail sectors in states and territories of Australia as a whole. Revenue consisted retail and wholesale sales.

The sampling frame for the survey was the ABS Business Register, which sources its information about new businesses from those applying for group employer registration with the Australian Taxation Office. The sample size of the retail business survey in Tasmania was approximately 433 businesses. The scope of the survey for the category of pubs, bars, taverns and licensed clubs included businesses in Australia that generated income predominantly from the provision of alcoholic beverages for consumption on the premises, or in selling alcoholic beverages for consumption on or off the premises and hospitality club organizations that generated income predominantly from the provision of hospitality services (that is, drinking facilities, gambling, meals and other hospitality services) to members. Businesses mainly engaged in the provision of accommodation and retailing alcoholic beverages for consumption off the premises were excluded from these surveys. Licensed clubs are defined as hospitality club organizations that provide drinking facilities, gambling, meals and other hospitality services to members. This study used Time Series analysis to examine the effect of smoke-free legislation.

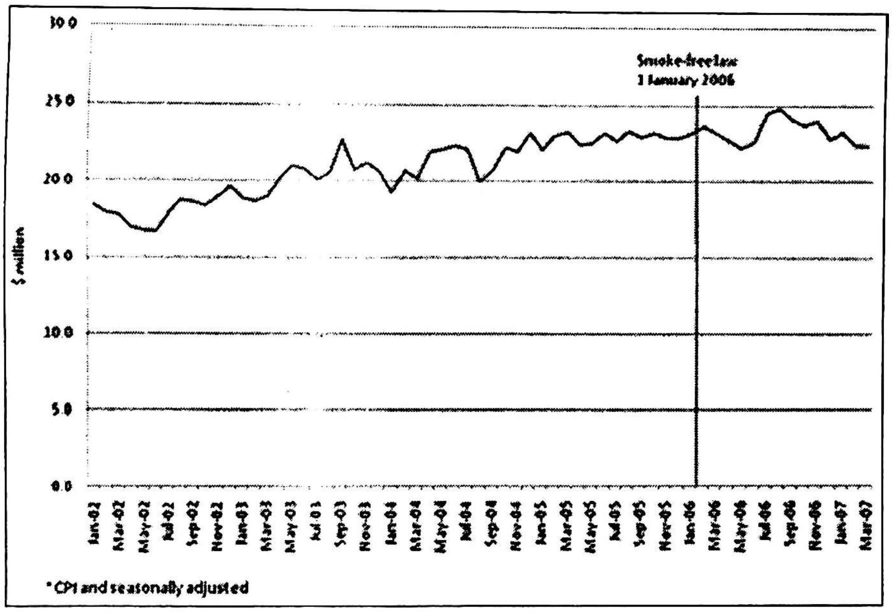

Figure 2.1: Sales Revenue for Tasmania bars
(January 2002 to June 2007)
Source: Australian Bureau of Statistics (2007)

The above graph shows the plots of the Consumer Price Index (CPI) and seasonally adjusted bar sales revenue in Tasmania, Australia from January 2002 to March 2007. The vertical line represents January 2006 when the smoke-free law (the intervention) came into effect. The average monthly sales revenue in the period before the introduction of the law was $A20.7million. The average monthly sales revenue increased to $A23.3 million in the period after the implementation of Smoke-free law. The results of this study suggest that the presence of a law prohibiting smoking in bars in Tasmania did not adversely affect bar sales revenue.

The findings from above study are consistent with other research done in United States of America and Canada using aggregate data on bars sales. Research in California showed there was an increase in bar sales following the smoke-free laws (Cowling DW, Bond P, 2005). The explanation is that while some smokers may avoid smoke-free bars, the percentage of smokers who do this is extremely small and is more than compensated for by increased patronage from non-smokers. The survey also found out that bar patrons in California were spending more time in bars, approves of the law and were observing higher compliance with the smoke-free bar law (Tang .H, Cowling DW, Lloyd JC, 2003).

These results indicates that bar owners and government policymakers should be reassured that they can adopt and maintain smoke-free legislation to protect workers and patrons from exposure to second-hand smoke in bars without fear of adverse effects on patronage and sales revenue.

2.4.3 Impact of Tobacco Regulation on Advertising

To say that tobacco advertising stimulates tobacco sales may seem a simple and moderate statement. In reality, tobacco control activists often meet serious opposition in defending this fact. Achieving the restriction or banning of tobacco advertising is one of the fiercest battles implementers face. Anti-tobacco control lobbyists usually assert that advertising does not increase the overall quantity of tobacco sold. Rather, the tobacco industry maintains that advertising merely enhances the market share of a particular brand, without recruiting new smokers. It is not possible to conduct a randomised controlled trial to study the effect of an advertising ban. Such a trial would require long-term exposure of one group of people to cigarette advertising, while ensuring that a control group would be completely unexposed. This is neither feasible nor ethical. Three main studies were therefore used to examine the relationship between tobacco advertising and consumption, they were; Econometric research on the link between expenditure on advertising and tobacco consumption; Research comparing tobacco consumption within a country before and after an advertising ban and International comparison of trends in tobacco consumption and anti-tobacco measures. Econometrics is defined as the application of mathematics and statistical inferences to the analysis of economic data.

Willemsen (1999) research on before and after an advertising ban compared tobacco consumption before and after a complete ban on advertising, controlling for other factors. Although such studies may be complicated by inadequate of data collection or poor implementation of the ban, they have yielded convincing data that a complete ban on advertising makes an important contribution towards reducing smoking prevalence. Selected studies are summarized in the table below;

Studies done by Willemsen (1999) in collaboration with the WHO on the effects of tobacco regulation on advertising:

Table 2.1: Willemsen Studies on the effects of Tobacco Regulations

Country, Year	Description of Anti-Smoking Measures	Effect
Norway, 1975	Complete ban on advertising and sponsoring, coupled with health warnings, public information and age limits on sales	Long-term reduction of smoking prevalence by 9%
Finland, 1977	Complete advertising ban, no smoking in public buildings, age limit on sales, strong public information, campaigns	Reduction of cigarette consumption of 6.7%
Canada, 1989	Complete ban on advertising and sponsoring, with higher tobacco prices	Corrected for price increases, a long-term reduction of smoking prevalence of 4%
New Zealand, 1990	Ban on advertising and sponsoring, higher tobacco prices	Reduction in tobacco sales of 7.5% of which 5.5% is attributed to advertising
France, 1991	Complete advertising ban, limiting smoking in public buildings, removal of tobacco from consumer price index	Reduction of smoking prevalence of 7% in 1991-1992.

Source: Willemsen, M.C (1999). Dutch Foundation on Smoking and Health.

International comparison of trends in tobacco consumption and anti-tobacco regulation study known as cross-sectional time-series analysis compares trends in tobacco advertising and consumption. A cross-sectional time series analysis in 22 countries for the period 1960-1986 concluded that increasingly strict regulation of advertising causes corresponding reductions in tobacco consumption (Laugesen. M and Meads.C, 1991). The degree of restriction on tobacco marketing was scored in each country: for example, Iceland, Finland and Norway, countries with a comprehensive advertising ban and strong warnings on tobacco products, scored 10 while others with less strict measures, such as a ban only on TV, radio or cinema advertising, had a lower score. On a scale of one to ten, an increase of 1 point was found to translate into a 1.5% reduction in tobacco consumption. Laugesen and Meads (1991) concluded that where a complete advertising ban is coupled with an intensive public information campaign on smoking,

a reduction in tobacco consumption of 6% can be achieved. A report by the World Bank supports this conclusion (Jha P, Chaloupka FJ, 1999).
Above studies demonstrates that tobacco advertising plays an important part in encouraging non-smokers to begin smoking. Advertising is a particularly important factor among young people. Comprehensive bans on tobacco advertising and promotion can result in a considerable reduction of tobacco consumption on a national level

2.4.4 Impact of Tobacco Regulation on Employment

Ireland was the world's first country to introduce a full workplace smoking ban. The Irish workplace ban was introduced with the intention of protecting workers from passive smoking (second-hand smoke) and to discourage smoking in a nation with a high percentage of smokers. Many pubs introduced outdoor arrangements (generally heated areas with shelters) despite speculation that the smoking ban would increase the amount of drinking and smoking at home. But later studies showed that this case not the case (The European Journal of Public Health, London, 2008). It has however been claimed that the smoking ban was a significant contributing factor to the closure of hundreds of small rural pubs, with almost 440 fewer licenses renewed in 2006 than in 2005 (Lister. D, 2007).

The objective of a study by Mark K Pyles, Donald J Mullineaux, Chizimuzo T C Okoli and Ellen J Hahn (2007) was to determine whether smoke-free law affected employment and business closures in restaurants and bars. The study used a fixed effects time series design to estimate the effect of the smoke-free law on employment and ordinary least squares to estimate the effect on business openings and closings. All restaurants and bars in Lexington-Fayette County, Kentucky and the six contiguous counties were considered. A positive and significant relationship was observed between the smoke-free legislation and restaurant employment, but no significant relationship was observed with bar employment. No relationship was observed between the Tobacco Control Law's implementation and employment neither in contiguous counties nor between the smoke-free law and business openings or closures in alcohol-serving and or non-alcohol-serving businesses.

Bartosch and Pope (1998) also used time-series framework to examine the effects of smoking restrictions in Massachusetts. They obtained employment data from the database produced by the Kentucky Workforce Cabinet, for the 64 months before and 14 months after the law took effect for each county in Kentucky. Population data were obtained from the Census Bureau and unemployment data from the Local Area Unemployment Statistics database maintained by the Bureau of Labour Statistics. The Study gathered data on monthly business openings and closings in food and drinking establishments in Lexington-Fayette County from the Lexington-Fayette County Health Department, Environmental Division, for the 46 months before and 19 months after the law took effect. The study examined whether average employment differed in the periods before and after the smoke-free law was implemented. Study found that mean employment was considerably higher in restaurants (at 3.4%) but employment was unchanged in bars.

2.5 REVIEW SUMMARY

Based on the above literature review, we note that most of the past studies have found that tobacco regulations reduced smoking in public places and tobacco bans in workplace reduced smoking among workers. Smoking bans in public places reduced general smoking through a combination of stigmatisation and reduction or lack of designated smoking areas. The economic effects of tobacco regulations was that they led to increase in employment in restaurants by 3.4 % in Massachusetts USA in 1998, bans on tobacco advertising on the other hand caused a reduction in tobacco consumption by average of 6% in countries covered by Willemsen Studies . Tobacco regulation had a positive effect on sales revenue and led to increase of 12 % in average sales revenue in bars in Australia after the implementation of smoke-free law in 2006. Annual gross profits declined by estimated 37 % in restaurants where bans were implemented four years prior to the study (Deloitte & Touche, 2004).

2.6 RESEARCH GAPS

The previous studies have concentrated on finding out the effect of tobacco regulations on the hospitality industry in developed countries. Hospitality industry is a major consumer of tobacco products and therefore poor financial performance of the hospitality industry will directly affect financial performance of cigarettes manufacturing firms as there will be reduced demand for tobacco products. The previous studies do not however reveal the real effect of tobacco regulations on the financial performance of cigarettes manufacturing companies.

This research therefore attempted to find out the real effect of the implementation of the Tobacco Control Act 2007 on the financial performance of the tobacco industry in Kenya using BAT Kenya Ltd as a case study. The study was based on a before and after analysis of data from 2006 to 2010 using 2008 as year of intervention when the Tobacco Control Act 2007 became effective from July 2008.

2.7 CONCEPTUAL FRAMEWORK

The conceptual framework for this study was based on key indicators of company's financial performance that is; profit before tax, sales revenue of cigarettes, marketing expenditure and the staff benefits costs for BAT Kenya Ltd. The study involved analysis of financial data from 2006 to 2010 to find out the financial performance of BAT Kenya Ltd before and after the implementation of the Tobacco Control Act 2007 in 2008.

This study evaluated how the independent variables were affected by the implementation of the Tobacco Control Act of 2007.The independent variables for this research were the profit before tax, sales revenue of cigarettes, marketing expenditure and staff benefits costs of BAT Kenya Ltd. The dependent variables are the changes as a result of changes in the level or amount of the independent variables (Mutai, 2000).

The dependent variables are therefore the outcome or level of financial performance after the implementation of the Tobacco Control Act 2007. The relationships of the variables are shown in the Conceptual Framework diagram below:

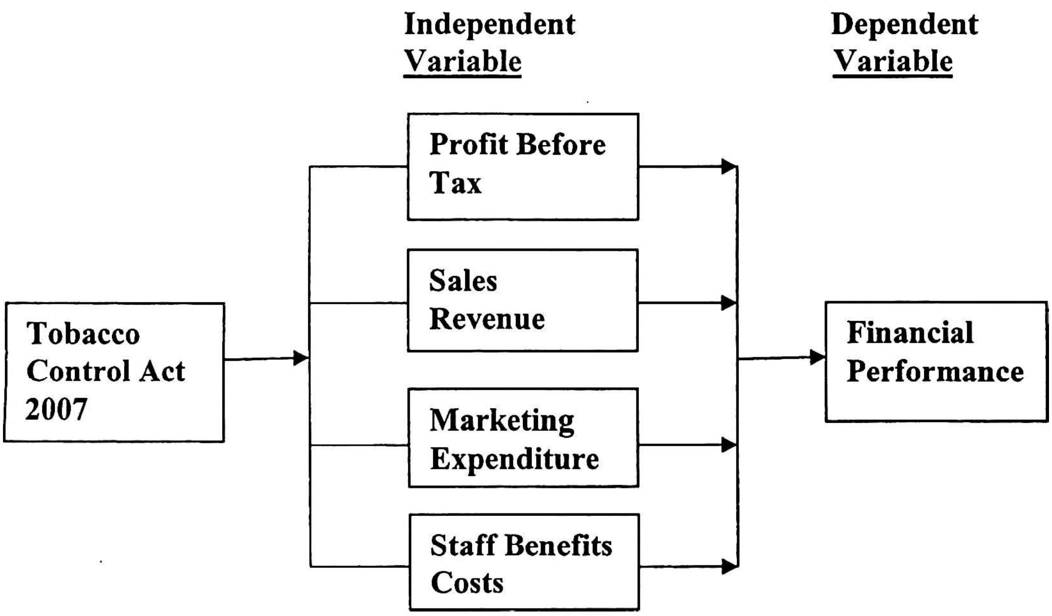

Figure 2.2: Conceptual Framework
Source: Author (2011)

2.7.1 Profit Before Tax - Government's legislation may affect the profitability of a company if law controls company's operational activities. This study will try to establish the effect of the Tobacco Control Act 2007 on the profitability of BAT Kenya Ltd.

2.7.2 Sales Revenue - Sales growth is dependant on the sales activities a company undertakes to avail its products to consumers. The study will find out how the Tobacco Control Act 2007 has affected the sales revenue of BAT.

2.7.3 Marketing Expenditure - The amount of money a company spends on advertising and promotion of its products contributes significantly to growth in sales volume. The study will find out how the Tobacco Control Act 2007 affected the expenditure on marketing and distribution activities.

2.7.4 Staff Benefits Costs - The amount of money a company spends annually on salaries and wages and other staff benefits is a good indicator of the level of employment or staff turnover during the year. The study will find how the Tobacco Control Act 2007 affected salaries and wages of BAT employees.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 INTRODUCTION

This chapter outlines the overall methodology used in the study. It includes research design, population of study, data collection method and data analysis approach used. The methodological approach for this study was secondary survey. This study sought to find out the impact of the Tobacco Control Act 2007 on the financial performance of the tobacco industry in Kenya, using BAT Kenya Ltd as a case study. The study was based on a before and after analysis of financial data from 2006 to 2010 using 2008 as year of intervention as the Tobacco Control Act 2007 became effective from July 2008.

3.2 RESEARCH DESIGN

This research took the form of descriptive design. According to (Cooper et al, 2003) a descriptive study is concerned with finding out who, what, which and how of a phenomenon, which was the main concern for this study. Mugenda (2003) notes that a research attempts to collect data and describe a phenomenon. The study focused on analysing the impact of Tobacco Control Act 2007 on financial performance of BAT Kenya Ltd.

The descriptive design was selected because it requires in-depth analysis in order to understand the effects of a new Act (Tobacco Control Act 2007) on BAT Kenya Ltd. Descriptive design is appropriate since the study requires insights to establish the real impact of Tobacco Control Act 2007 on marketing expenditure, sales revenue of cigarettes, staff benefits cost for employees as well as profit before tax for BAT Kenya Ltd.

3.3 TARGET POPULATION

The target of this study was BAT Kenya Ltd which controls 81% market share in Kenya (BAT Annual Financial Report, 2010) and therefore its financial performance is a good representation of the performance of the cigarettes manufacturing firms in Kenya. Financial performance indicators of profit before tax, marketing expenditure, sales revenue of cigarettes, and staff benefits costs for employees before and after implementation of the Tobacco Control Act 2007 in July 2008 were analysed using data obtained from BAT Kenya Ltd published Annual Financial Reports from 2006 to 2010.

3.4 DATA COLLECTION AND INSTRUMENTS

This research was based on secondary data availed by BAT Kenya Ltd through its published Annual Financial Reports. Research also involved interviewing a Marketing Representative in BAT using a questionnaire to verify the actual cause of changes in the financial performance of BAT as reflected in the BAT's Annual Financial Reports. The benefits of audited Annual Financial Reports over primary data is that, accuracy of audited reports for all public companies quoted at Nairobi Stock Exchange is verified by Capital Markets Authority before they are released to the public.

3.5 DATA PROCESSING AND ANALYSIS

Before the secondary information in BAT Annual Financial Reports was processed, financial data was first checked to ensure completeness, relevance and accuracy. The quantitative data collected was summarized and analyzed using Microsoft Excel application where numerical data was involved and interpretations presented in descriptive statistics. These were in form of tables and percentages, histograms and time series graphs.

CHAPTER FOUR

RESEARCH FINDINGS AND DISCUSSION

4.1 INTRODUCTION

This chapter presents results of the data collected for this study in order to make deductions and inferences. Secondary data was obtained from Capital Markets Authority for the period from 2006 to 2010. Using 2008 as the year when the Act was implemented, a before and after implementation data analysis was done to determine the impact of the Act on the financial performance of BAT. A questionnaire was used to interview a marketing representative in BAT in order to verify the interpretations from the analysis of the data extracted from BAT Annual Financial Reports. BAT was used as a case study as it controls 81% market share and is therefore a good representative of the cigarettes manufacturing industry in Kenya.

4.2 PRESENTATION OF RESULTS AND DISCUSSION

This study was guided by four specific objectives; to find out the effect of the implementation of the Tobacco Control Act 2007 on profit before tax, sales revenue of cigarettes, marketing expenditure on cigarettes and the staff benefits costs of BAT Kenya Ltd.The study therefore isolated four key independent variable for detailed analysis, that is; profit before tax, sales revenue of cigarettes, marketing expenditure and staff benefits costs. These independent variables are good indicators of companies' financial performance. The discussion have been organised in a way that all the four variables which are also outlined in the conceptual framework are addressed.

4.2.1 TOBACCO CONTROL ACT 2007 AND PROFIT BEFORE TAX

From 2006 to 2008, Profits before tax for BAT Kenya Ltd had been increasing annually by an average of 18 %. After the implementation of Tobacco Control Act in 2008, Profits before tax for BAT reduced by 13% in 2009 to Kshs. 2.1 million down from Kshs. 2.4 million in 2008. In 2010, the Profits before tax reduced by a further 6% to Kshs. 1.9 million.

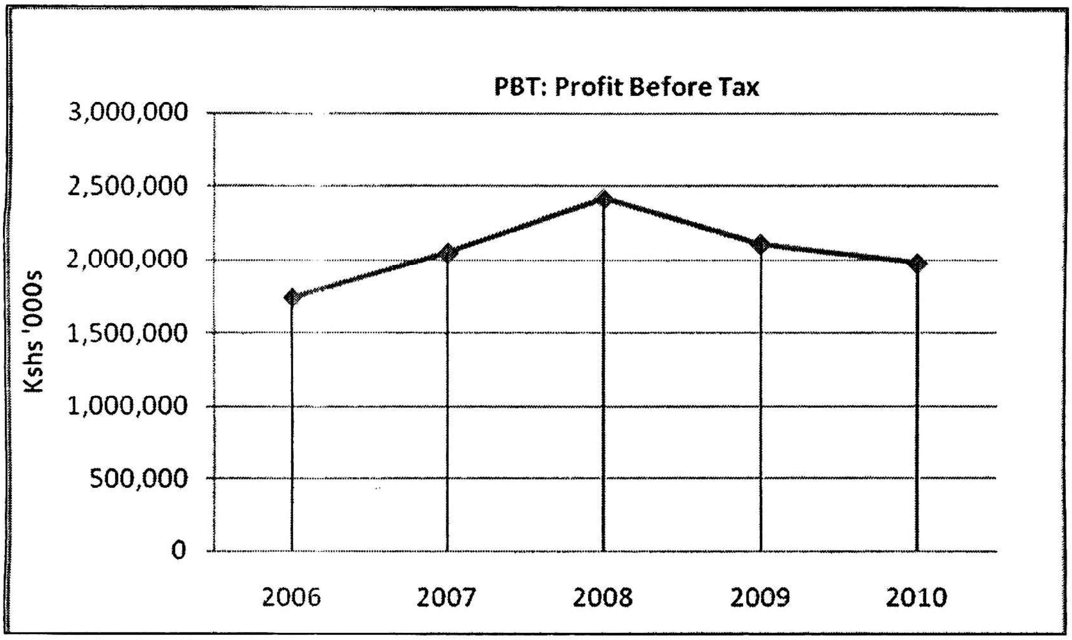

Figure 4.1: Annual Profit before Tax (2006 -2010)

The line graph shows that BAT Kenya Ltd started experiencing reduction of profit before tax from 2009; there was indeed an up-ward trend in growth of profits in the preceding years from 2006 to 2008. The impact of the Tobacco Control Act 2007 on the annual profits before tax for BAT Kenya Ltd is well captured by the sharp decrease of annual profits in years 2009 and 2010 (Figure 4.1).

4.2.2 TOBACCO CONTROL ACT 2007 AND SALES REVENUE

Though the annual local sales revenue of cigarettes for BAT have been increasing from year 2006 to 2010 (Figure 4.2), the annual growth in sales revenue after the implementation of the ACT in 2008 has been at a diminishing rate. The sale revenue increased by 12% in year 2007 and 2008. In year 2009 however, the annual sales revenue increased by a reduced margin of 9 % indicating that implementation of Tobacco Control Act 2007 had immediate negative impact on annual sales revenue.

In 2010, BAT came up with strategies to increase its sales revenue without contravening the Tobacco Control Act 2007; this resulted in 14% growth in sales revenue. This interpretation is supported by the Chairman of BAT who reported; "BAT's exceptional domestic sales was underpinned by tactical enforcement of anti illicit trade activities" (BAT Annual Financial Reports, 2010).

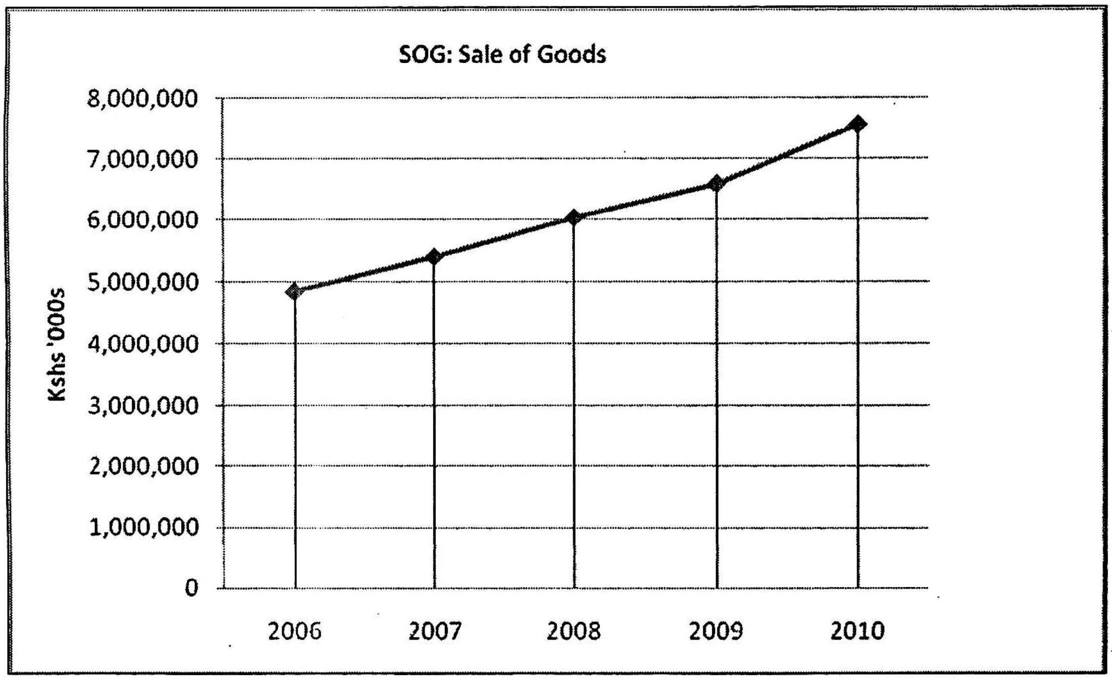

Figure 4.2: BAT Annual Sale Revenue of Cigarettes (2006-2010)

4.2.3 TOBACCO CONTROL ACT 2007 AND MARKETING EXPENDITURE

With the implementation of Tobacco Control Act 2007 in 2008, BAT was compelled to reduce its annual marketing activities. This phenomenon is well captured by Figure 4.3, which shows that annual marketing and distribution expenditure decreased by 8 % in year 2009 compared to 17% increase in year 2008. In 2010, there was further decrease of annual marketing expenditure by 18% compared to what BAT spent in year 2009.

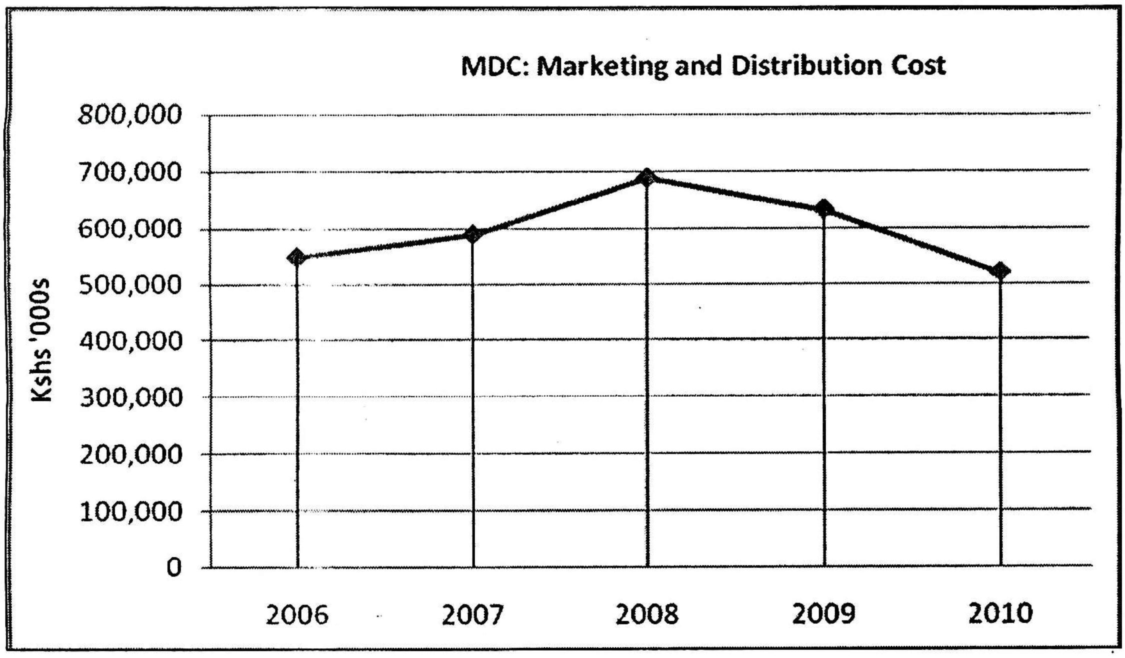

Figure 4.3: BAT Annual Marketing Expenditure (2006 - 2010)

The triangular shape of the graph in Figure 4.3 indicates that BAT was increasing its annual expenditure on marketing activities each year from 2006 to 2008.However, after the introduction of the Tobacco Control Act 2007 in 2008, BAT began to spend less money on marketing activities. This is well captured by the line graph which slopes downwards from 2009 due to reduced annual expenditure on marketing activities after implementation of Tobacco Control Act 2007.

4.2.4 TOBACCO CONTROL ACT 2007 AND STAFF BENEFITS COSTS

The annual Staff benefits costs for BAT increased by 16 % in year 2007 compared to year 2006 but increased by 15 % in year 2008 when the Tobacco Control Act 2007 was implemented. In year 2009 however, the staff benefits costs increased by a reduced margin of 9 % indicating that implementation of Act had immediate negative impact on annual staff benefits costs. In 2010, the annual expenditure on staff decreased by 2%, this is in spite of the fact that 45 new members of staff were employed during the year. The explanation for this phenomenon is that more staff lost their jobs in 2010 than those that were employed during the year. Kshs 223 million indicated in BAT's Annual Financial Report for 2010 (Appendix III) as 'restructuring costs', means that some employees were rendered redundant during the year.

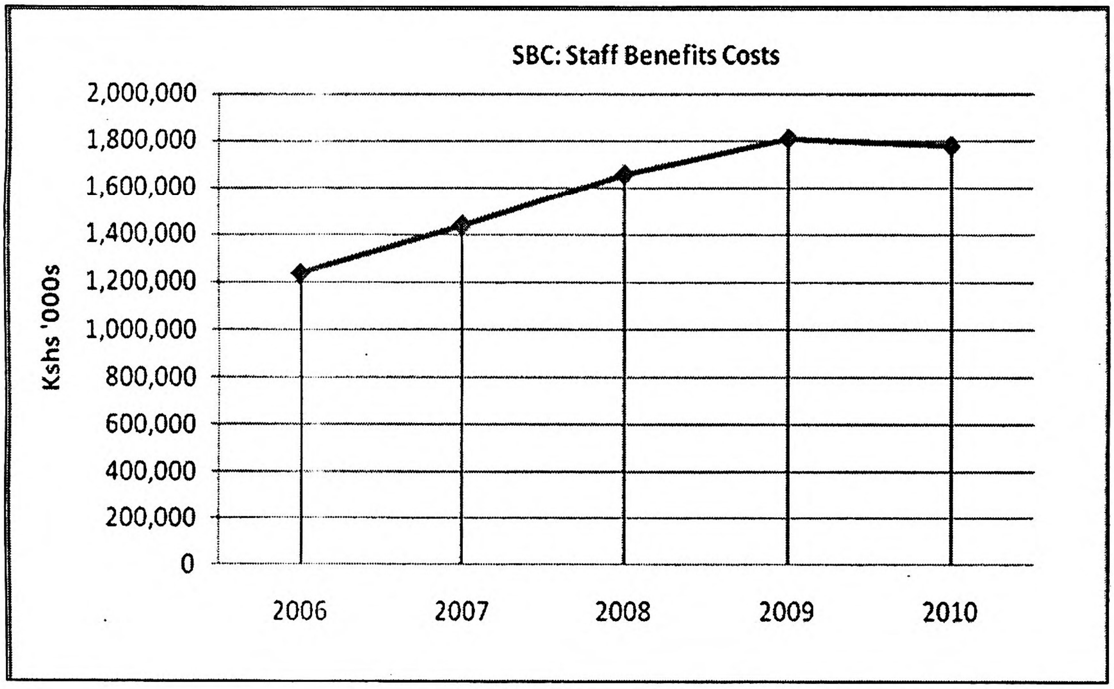

Figure 4.4: BAT Annual Staff Benefits Costs (2006 - 2010)

The trend of annual Staff benefits costs for employees of BAT Kenya Ltd is that there has been a gradual increment from 2006 to 2008 as illustrated by Figure 4.4. The continued upward trend in the amount of money spend on staff benefits costs in 2009 may be due to the fact that BAT was restricted in carrying out marketing activities to promote sales, and was compelled to hire more sales staff to do below-the-line sales promotion where its sales representative deal with the retail outlets directly as advertising of tobacco products to general public is prohibited.

4.3 SUMMARY OF FINDINGS

This study revealed that the implementation of Tobacco control act 2007 has negatively affected the financial performance of BAT (K) Ltd as the annual profit before tax, marketing expenditure of cigarettes and staff benefits costs have been decreasing from year 2009 after the ACT became effective in 2008 as illustrated in Table 4.1. However, from September 2010, BAT commenced contract manufacture of semi-processed tobacco (cut rag) for export which contributed to increase in gross sales revenue of Kshs.3.1 billion (BAT Half-Year Report to June 2011). The profit before tax of Kshs.1,978,572 in Table 4.1 was therefore arrived at after proportionate adjustment to remove the profit attributable to export sale of semi-processed tobacco for the period September 2010 to December 2010.

Table 4.1 BAT (K) Ltd Annual Financial Reports (Extracts)

Year	Profit before Tax (Kshs'000s)	Sales Revenue (local) (Kshs'000s)	Marketing & Distribution Costs (Kshs'000s)	Staff Benefits Costs (Kshs'000s)
2006	1,746,526	4,842,155	547,885	1,238,748
2007	2,049,596	5,412,984	588,748	1,440,870
2008	2,416,913	6,050,517	688,703	1,655,617
2009	2,108,964	6,595,964	632,009	1,807,866
2010	1,978,572	7,567,850	518,249	1,776,436

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATION

5. 1 INTRODUCTION

This chapter summarizes the research findings and compares them with similar previous studies highlighted in Chapter 2 to draw some conclusions. Researcher also gives recommendations and suggestions for further studies.

5.2 SUMMARY OF FINDINGS

This case study objective was to establish the effect of the Tobacco Control Act 2007 on the financial performance of BAT (K) Ltd. Thus, the study sought to find out whether the Act has affected the trend of profit before tax, marketing expenditure, sale revenue of cigarettes, and staff benefits costs. Study involved collecting secondary data from BAT (K) Ltd's Annual Financial Reports for the period 2006 to 2010. BAT was used as a case study as it controls 81% of the market share and company is therefore a good representative of the cigarettes manufacturers in Kenya. The study entailed a before-and-after implementation analysis and presentation of the financial data in form of time series graphs. This study sought to answer the following Research Questions:

1. What is the effect of Tobacco Control Act 2007 on the profit before tax of BAT Kenya Limited?
2. How has the Tobacco Control Act 2007 affected the sales revenue of cigarettes for BAT Kenya Limited?
3. How has Tobacco Control Act 2007 affected the marketing expenditure on cigarettes by BAT Kenya Limited?
4. What is the effect of Tobacco Control Act 2007 on the staff benefits cost for employees of BAT Kenya Limited?

5.2.1 Profit before Tax for BAT Kenya Ltd

After the implementation of Tobacco Control Act2007 in 2008, Profits before tax for BAT (K) Ltd reduced by 13% in 2009 to Kshs. 2.1 million down from Kshs. 2.4 million in 2008. In 2010, the Profits before tax reduced by a further 6% to Kshs. 1.9 million. These findings clearly indicate that Tobacco Control Act 2007 has negatively affected the Profit before tax for BAT from 2009.

This study's findings are consistent with a past study by Obwino (2003) on the Consequences of Government Tobacco Control in Kenya that concluded that Government will loss tax revenue from Tobacco industries due to reduced profitability if Tobacco Control Bill of 1999 was implemented by the Kenya government at that time.

5.2.2 Sales Revenue for BAT Kenya Ltd

Though the annual local sales revenue of cigarettes for BAT have been increasing from year 2006 to 2010 (Figure 4.2), the annual growth in sales revenue after the implementation of the ACT in 2008 has been at a diminishing rate, that is ; 12% in year 2008 and 9% in year 2009. In 2010 however, the sales revenue grew by 14% , the explanation for this is that BAT has come up with strategies to increase its sales revenue without contravening the Tobacco Control Act 2007.The conclusion we can draw from this findings is that sales revenue for BAT were affected by the Tobacco Control Act 2007 and the high sales revenue realized in 2010 was due to enforcement of anti-dumping of imported cigarettes into the local Kenya market.

These findings are consistent with similar study done by Lal .A, et al (2009) to examine the impact of smoke-free policies on sales revenue in Tasmanian bars in Australia that concluded that the average monthly sales revenue in bars decreased in the period immediately after the implementation of smoke-free laws. Monthly sales revenue then picked up in subsequent months and increased beyond prior implementation levels.

5.2.3 Marketing Expenditure for BAT Kenya Ltd

With the implementation of Tobacco Control Act 2007 in 2008, BAT was compelled to reduce its annual marketing activities. Annual Marketing and distribution expenditure therefore decreased by 8 % in year 2009. In 2010, there was further decrease of annual marketing expenditure by 18% compared to what BAT spent in year 2009.This clearly demonstrates that the Tobacco Control Act 2007 adversely affected the amount of money BAT spends annually for marketing activities to promote sale of cigarettes.

The above findings are consistent with results from past studies conducted by Willemsen (1999) and Laugesen and Meads (1991) on tobacco consumption before and after an advertising ban that concluded that comprehensive bans on tobacco advertising and promotion can result in a considerable reduction of tobacco consumption on a national level.

5.2.4 Staff Benefits Costs for BAT Kenya Ltd

In year 2009 the annual staff benefits costs increased by a reduced margin of 9 % compared to 15% increment in 2008, indicating that implementation of Tobacco Control Act 2007 had immediate negative impact on staff benefits costs for employees of BAT. In 2010, the annual expenditure on staff benefits decreased by 2%. The big decrease in the amount of money BAT spent for staff benefits of salaries and wages in 2010 clearly indicates that the Tobacco Control Act 2007 has negatively affected the staff benefits for employees of BAT.

This findings contradicts a study done by Bartosch and Pope (1998) in Massachusetts, USA that examined whether average employment differed in the periods before and after the smoke-free in public law was implemented and concluded that mean employment was considerably higher in restaurants (at 3.4%) but employment was unchanged in bars. One may however argue this study is different and should not be compared as Bartosch and Pope Study dwelt on employment in bars and restaurants.

5.3 CONCLUSIONS

The study concludes that the implementation of the tobacco control Act 2007 from 2008 has had a negative impact on the financial performance of the cigarettes manufacturing firms in Kenya in terms of reduced profitability, marketing activities and number of employees. Using the case of BAT (K) Ltd which has a market share of 81 % (BAT Annual Financial Report, 2010) and is therefore a good representative of the tobacco industry in Kenya. We have established that annual profits before tax for BAT increased by 18% in 2008 but decreased by 6% in 2010.

Annual marketing expenditure increased by 17% in 2008 but decreased by 18% in 2010 due to reduced marketing activities after the implementation of the Tobacco Control Act 2007. Annual staff benefits costs (salaries & wages) increased by 15 % in 2008 but decreased by 2% in 2010 when the implementation of Tobacco Control Act 2007 took toll on the employees of BAT as more staff lost their jobs in 2010 than those that were employed during the year.The implementation of the Tobacco Control Act 2007 did not however, inflict prolonged reduced margins in growth of annual sales revenue for BAT as the company responded quickly and came up with strategies to increase its sales revenue without contravening the Tobacco Control Act 2007 which realized 14% growth in sales revenue in year 2010, up from a low of 9% in year 2009.

The above conclusions are supported by answers given by a BAT Marketing Representative in an interview conducted through a Questionnaire for this study (Appendix II).

5. 4 RECOMMENDATION

The study recommends that future Kenya government's policies and regulation on sale and consumption of tobacco products should focus on controlling consumer demand for tobacco products through educating tobacco consumers on health risks of smoking cigarettes rather than imposing controls on supply of tobacco products from cigarettes manufacturing firms which has brought negative effects of reduction in profitability, employment and government's tax revenue.

5.5 SUGGESTION FOR FURTHER RESEARCH

This study analysed the effect of the implementation of Tobacco Control Act 2007 using secondary data from BAT (K) Ltd for the period 2006 to 2010. Further research needs to be undertaken to determine the impact of the ACT on cigarettes consumption and lifestyle preferences of cigarettes smokers.

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APPENDIX I: INTRODUCTION LETTER

Date: July 27, 2010

Ref: JKU/SHRD/KIM/EMBA- PROJECT /2010

TO WHOM IT MAY CONCERN

Dear Sir / Madam,

RE: RESEARCH PROJECT

This is to introduce to you: **Bernard Gathu Mwaniki - HD334-033-0780/2009**, who is a student pursuing Executive Masters in Business Administration Degree program at Jomo Kenyatta University of Agriculture & Technology.

The student is currently undertaking a research project entitled: **"The effect of the implementation of Tobacco Control Act 2007 on financial performance of cigarette manufacturing firms in Kenya : The case of BAT Kenya Ltd ".** In partial fulfilment of the requirement for the award of Degree in Executive Masters in Business Administration.

The purpose of this letter is to request you to give the student the necessary support and assistance, to enable him obtains the data and statistics that are necessary for the project. Please note that the information given is purely for academic purposes and will be treated with strict confidence.

Thank you.

Yours faithfully,

SCHOOL FOR HUMAN RESOURCE DEVELOPMENT

Dr. M. Kavoi
DIRECTOR

APPENDIX II: RESEARCH QUESTIONNAIRE

The aim of this Questionnaire is to assess the impact of the implementation of Tobacco Control Act, 2007 on the profitability, marketing expenditure, sale of cigarettes and staff cost of employees in cigarettes manufacturing firms in Kenya. BAT Kenya has been selected as a case study since BAT Kenya is a public quoted company and has necessary secondary data and information on the impact of the implementation of the Tobacco Control Act 2007. Availed information will help us know the real impact of the Act on financial performance of BAT Kenya which is a major source of employment and huge tax payer to the government of Kenya.

PART A: GENERAL INFORMATION

1. Please indicate your department in BAT Kenya?

   Department: Marketing

2. Please indicate your Title?

   Title/ Position: Marketing Manager

PART A

3. Are you aware of the Tobacco Control Act 2007?
   Yes (X)
   No ( )

4. In your opinion, has the Tobacco Control Act 2007 affected cigarette manufacturers (BAT Kenya) in any way?
   Yes (X)
   No ( )

5. In what ways has the Tobacco Control Act 2007 affected BAT Kenya?

A. Act has affected BAT Kenya (please explain) :	The Act outlawed advertising of cigarettes in public media
B. Act has not affected BAT (please explain) :	

PART B

6. A) Please indicate how the implementation of the Act has affected BAT Kenya's Labor force?

(Please tick one)

Some employees have been laid off	X
The number of employees has remained the same	
Company has increased no. of employees	

6. B) Can you attribute the above staff redundancy as due to Tobacco Control Act 2007?

Yes (X)   No ( )

7. A) Has cigarettes advertising activities been affected by the implementation of the Tobacco Control Act 2007?

Yes (X)   No ( )

7. B) Please explain how cigarettes marketing expenditure has been affected by the Tobacco Control Act 2007?

From 2008 , BAT Kenya has been spending less money annually on marketing and distribution of cigarettes in Kenya

7. C) Can you attribute the above change as due to Tobacco Control Act 2007 ?

Yes (X)   No ( )

8. A) Which of the following statements best explain how the Tobacco Control Act 2007 has affected BAT Kenya's cigarettes marketing activities ?

(Please tick one)

BAT Kenya spends more annually on marketing activities since the introduction of the Tobacco control Act 2007	
BAT Kenya spends less annually on marketing activities since the introduction of the Tobacco control Act 2007	X
The amount that BAT Kenya spends annually on marketing activities has not changed since the introduction of the Tobacco control Act 2007	

8. B) Can you attribute the above change as due to Tobacco Control Act 2007?

Yes (X) No ( )

9. A) Please indicate how the implementation of Act has affected the annual sales of cigarettes by BAT Kenya? (Please tick one)

Sales of Cigarettes per year have reduced ( )
Sales of Cigarettes per year have increased ( )
Sales of Cigarettes per year have remained same ( )
Other (please specify) : BAT compelled to increase retail prices (X)

9. B) Can you attribute the price changes as due to Tobacco Control Act 2007?

Yes (X) No ( )

10.A) Which of the following statements best explain how the Tobacco Control Act 2007 has affected BAT Kenya's profitability?

(Please tick one)

BAT Kenya posts lower annual profit before tax since the introduction of the Act in 2008	X
The annual profit before tax of BAT Kenya has not been affected by the introduction of Tobacco Act in 2008	
The annual profit before tax of BAT Kenya has increased since the introduction of the Act in 2008	

10.B) Can you attribute the above change as due to Tobacco control Act 2007?

Yes (X) No ( )

Thank you for taking your time to complete this questionnaire.

APPENDIX III: BAT (K) Ltd Annual Financial Reports (2006 - 2010 Extracts)

Consolidated

	Notes	For the year ended 31 December 2007 Shs'000	2006 Shs'000
Gross turnover		15,770,234	12,859,171
Excise duty and value added tax		(6,351,328)	(5,045,016)
Revenue	6	9,418,906	7,814,155
Other operating income		359,246	44,383
Cost of operations	7	(7,670,148)	(6,049,576)
Operating profit	8	2,108,004	1,808,962
Net finance cost	10	(58,408)	(62,436)
Profit before income tax		2,049,596	1,746,526
Income tax expense	11	(663,949)	(545,104)
Profit for the year (of which Shs 1,385,647,000 has been dealt with in the accounts of the company)		1,385,647	1,201,422
Earnings per share			
Basic and diluted earnings per share (Shs)	13	13.86	12.01
Dividends			
Interim dividends – paid in the year	12	650,000	450,000
Proposed final dividend for the year	12	1,050,000	750,000
Total dividends		**1,700,000**	**1,200,000**

Consolidated profit and loss account

	Notes	For the year ended 31 December 2008 Shs '000	2007 Shs '000
Gross turnover		17,435,970	15,770,234
Excise duty and value added tax		(7,152,601)	(6,351,328)
Revenue	5	10,283,369	9,418,906
Other income		136,776	365,912
Cost of operations	6	(7,858,216)	(7,670,148)
Finance costs	7	(145,016)	(65,074)
Profit before income tax	8	2,416,913	2,049,596
Income tax expense	10	(716,518)	(663,949)
Profit for the year (of which Shs 1,700,395,000 has been dealt with in the accounts of the Company)		1,700,395	1,385,697
Earnings per share			
Basic and diluted (Shs per share)	11	17.00	13.86
Dividends:			
Interim dividends paid in the year	12	450,000	650,000
Proposed final dividend for the year	12	1,250,000	1,050,000
		1,700,000	1,700,000

Consolidated statement of comprehensive income

	Notes	Year ended 31 December 2009 Shs'000	2008 Shs'000
Gross turnover		18,719,542	17,435,970
Excise duty and value added tax		(7,625,146)	(7,152,601)
Revenue	5	11,094,396	10,283,369
Other income		220,306	136,776
Cost of operations	6	(8,779,231)	(7,858,216)
Restructuring costs		(314,252)	-
Finance costs	7	(112,255)	(145,016)
Profit before income tax	8	2,108,964	2,416,913
Income tax expense	10	(630,533)	(716,518)
Profit for the year (of which Shs 1,478,431 has been dealt with in the accounts of the Company)		1,478,431	1,700,395
Other comprehensive income			
Total comprehensive income for the year		1,478,431	1,700,395
Earnings per share			
Basic and diluted (Shs per share)	11	14.78	17.00
Dividends:			
Interim dividend – paid in the year	12	450,000	450,000
Proposed final dividend for the year	12	1,025,000	1,250,000
		1,475,000	1,700,000

The notes on pages 45 to 67 are an integral part of these consolidated financial statements.

Consolidated statement of comprehensive income

	Notes	Year ended 31 December 2010 Shs'000	2009 Shs'000
Revenue	5	13,539,233	11,094,396
Other income		200,266	220,306
Cost of operations	6	(10,576,979)	(8,779,231)
Restructuring costs		(223,001)	(314,252)
Finance costs	7	(216,947)	(112,255)
Profit before income tax	8	2,722,572	2,108,964
Income tax expense	10	(955,336)	(630,533)
Profit for the year (all of which has been dealt with in the accounts of the Company)		1,767,236	1,478,431
Other comprehensive income			
Total comprehensive income for the year		1,767,236	1,478,431
Earnings per share			
Basic and diluted (Shs per share)	11	17.67	14.78

The notes on pages 72 to 99 are an integral part of these consolidated financial statements.

BRITISH AMERICAN TOBACCO

HALF YEAR RESULTS FOR THE SIX MONTHS ENDED 30TH JUNE 2011

The Directors of British American Tobacco Kenya Limited are pleased to announce the unaudited group results for the six months ended 30 June 2011 as shown below:

Key highlights:

• Revenue	Up by Shs 3.1b
• Profit before tax	Up by 14%
• Contribution to government revenues	Up by 6%
• Interim dividend	Shs 3.50 per share

The extracts of the financial statements are as follows:

Condensed Income Statement for the six months ended 30 June:

	2011 Shs' m	2010 Shs' m
Revenue	9,096	6,006
Operating profit	1,715	1,525
Finance costs	(52)	(64)
Profit before tax	1,663	1,461
Income tax expense	(498)	(438)
Profit after tax	1,165	1,023
Dividend	350	-
Basic and diluted earnings per share (Shs)	11.65	10.23

Condensed Balance Sheet as at 30 June:

	2011 Shs' m	2010 Shs' m
Capital and reserves		
Share capital	1,000	1,000
Revaluation surplus	1,108	1,153
Retained earnings	2,721	2,517
Shareholders' funds	4,829	4,670
Non-current liabilities	924	1,271
	5,753	5,941
Assets		
Non-current assets	6,372	6,192
Working capital		
Current assets	7,416	5,911
Current liabilities	(8,035)	(6,162)
Net working capital	(619)	(251)
	5,753	5,941

Condensed Cash Flow Statement for the six months ended 30 June:

	2011 Shs' m	2010 Shs' m
Cash generated from operations	470	434
Net interest paid	(52)	(85)
Tax paid	(674)	(379)
Net cash from operating activities	(256)	(30)
Net cash used in investing activities	(313)	(164)
Net cash used in financing activities	(1,362)	(1,025)
Decrease in cash & cash equivalents	(1,931)	(1,219)
At start of period	(415)	(1,122)
At end of period	(2,346)	(2,341)

Condensed Statement of Changes in Equity for the six months ended 30 June 2011

	Share capital Shs' m	Revaluation Shs' m	Retained earnings Shs' m	Total Shs' m
At 1 January 2010	1,000	1,153	2,519	4,672
Net profit	-	-	1,023	1,023
Final dividend for 2009	-	-	(1,025)	(1,025)
At 30 June 2010	1,000	1,153	2,517	4,670
At 1 January 2011	1,000	1,108	3,006	5,114
Net profit			1,165	1,165
Final dividend for 2010			(1,450)	(1,450)
At 30 June 2011	1,000	1,108	2,721	4,829

Overview:

Notwithstanding a challenging operating environment, underlying revenue on domestic and export cigarettes grew 15% reflecting higher total volumes coupled with an exchange rate benefit on exports revenue. Total revenue also benefited from the commencement in September 2010 of the contract manufacture business stream for cut rag (Semi-processed leaf) contributing to the total increase in revenues of Shs 3.1b. Contribution to government revenue from excise, VAT and corporation tax was Shs 4.6b, an increase of 6% compared to the same period last year driven by higher corporation tax payments.

Profit before tax improved by 14% reflecting higher domestic and export volumes, the impact of cut rag exports offset by lower domestic pricing and resultant margins arising from the need to protect our competitive position.

(vi) Capital risk management

The Group's objective when managing capital is to safeguard it's ability to continue as a going concern in order to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital.

4 Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including experience of future events that are believed to be reasonable under the circumstances.

In the process of applying the Group's accounting policies, management has made judgements in determining:
-the classification of financial assets and liabilities
-whether assets are impaired
-provisions and contingent liabilities.

5 Segment reporting

There is only one business segment (manufacture and sale of cigarettes and tobacco) and one geographical segment based on the location of the manufacturing site (Kenya) hence no segment information is presented.

The Group's revenues by destination are as follows:	2007 Shs'000	2006 Shs'000
Local sales	5,412,984	4,842,155
Exports and contract manufacture sales	4,005,922	2,972,000
	9,418,906	7,814,155

6 Revenue

The Group's revenues by type are as follows:	2007 Shs'000	2006 Shs'000
Goods	9,039,857	7,575,813
Services	379,049	238,342
	9,418,906	7,814,155

In 2006, direct costs attributable to the provision of services amounting to Shs 189,682,000 were netted off against the gross revenue in arriving at the reported revenue from services of Shs 48,660,000. These have now been reported as part of raw materials and consumables in Note 7. This reclassification has no impact on the reported profit for 2006.

7 Cost of operations

	2007 Shs'000	2006 Shs'000
Raw materials and consumables	4,793,877	3,900,144
Marketing and distribution costs	588,748	547,885
Administrative and other operating expenses	1,860,015	1,283,894
Depreciation of property, plant and equipment (Note 18)	366,769	312,589
Amortisation of intangible asset (Note 19)	60,736	5,061
Amortisation of prepaid operating lease rentals (Note 20)	3	3
	7,670,148	6,049,576

Notes

4 **Financial risk management (continued)**

vi) Capital management

The group's objectives when managing capital are to safeguard the group's ability to continue as a going concern in order to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital. In order to maintain or adjust the capital structure, the group may adjust the amount of dividends paid to shareholders, issue new capital or sell assets to reduce debt.

5 **Segment information**

The group operates in one business segment - manufacture and sale of cigarettes and tobacco and one geographic segment based on the location of the manufacturing site in Kenya hence no segmental information is presented.

The group's revenues by destination are as follows:

	2008 Shs '000	2007 Shs '000
Local sales	6,050,517	5,412,984
Export and contract manufacture sales	4,232,852	4,005,922
	10,283,369	9,418,906
Analysis of revenue by category		
Sale of goods	9,977,485	9,039,857
Sale of services	305,884	379,049
	10,283,369	9,418,906

6 **Cost of operations**

	2008 Shs '000	2007 Shs '000
Raw materials and consumables	5,142,870	4,793,877
Marketing and distribution costs	688,703	588,748
Administrative and other operating expenses	1,559,970	1,860,015
Depreciation of property, plant and equipment	405,653	366,769
Amortisation of intangible assets	61,017	60,736
Amortisation of prepaid operating lease rentals	3	3
	7,858,216	7,670,148

Notes (continued)

5 Segment information

The group operates in one business segment - manufacture and sale of cigarettes and tobacco and one geographic segment based on the location of the manufacturing site in Kenya; hence no segmental information is presented.

The group's revenues by destination are as follows:

	2009 Shs '000	2008 Shs '000
Local sales	6,595,964	6,050,517
Exports	4,498,432	4,232,852
	11,094,396	10,283,369
Analysis of revenue by category:		
Sale of goods	10,840,897	9,977,485
Sale of services	253,499	305,884
	11,094,396	10,283,369

None of our customers have sales in excess of 10% of the total revenue.

6 Cost of operations

	2009 Shs'000	2008 Shs'000
Raw materials and consumables	5,676,057	5,142,870
Marketing and distribution costs	632,009	688,703
Administrative and other operating expenses	1,941,961	1,559,970
Depreciation of property, plant and equipment (Note 17)	467,512	405,653
Amortisation of intangible assets (Note 18)	61,689	61,017
Amortisation of prepaid operating lease rentals (Note 20)	3	3
	8,779,231	7,858,216

7 Finance costs

	2009 Shs'000	2008 Shs'000
Interest income	(162)	(175)
Interest expense - bank borrowings and related party loans	165,777	105,792
Net foreign exchange (gains) / losses	(53,360)	39,399
Net finance costs	112,255	145,016

Notes (continued)

5 Segment information

The group operates in one business segment - manufacture and sale of cigarettes and tobacco and one geographic segment based on the location of the manufacturing site in Kenya, hence no segmental information is presented.

The group's revenues by destination are as follows:

	2010 Shs'000	2009 Shs'000
Local sales	7,567,850	[illegible]
Exports	5,971,383	[illegible]
	13,539,233	[illegible]

Analysis of revenue by category:

	2010 Shs'000	2009 Shs'000
Sale of goods	13,091,616	[illegible]
Sale of services	447,617	[illegible]
	13,539,233	[illegible]

No customers have sales in excess of 10% of the total revenue.

6 Cost of operations

	2010 Shs'000	2009 Shs'000
Raw materials and consumables	7,512,977	[illegible]
Marketing and distribution costs	1,448,860	[illegible]
Administrative and other operating expenses	1,011,350	[illegible]
Depreciation of property, plant and equipment (Note 17)	547,456	[illegible]
Amortisation of intangible assets (Note 18)	56,336	[illegible]
	10,576,979	[illegible]

7 Finance costs

	2010 Shs'000	2009 Shs'000
Interest income	(245)	[illegible]
Interest expense - bank borrowings and related party loans	186,860	[illegible]
Net foreign exchange losses /(gains)	30,332	[illegible]
Net finance costs	216,947	[illegible]

7 Cost of operations (continued)

In order to reflect the total cost attributable to the manufactured product, manufacturing process and support related costs incurred in 2006 amounting to Shs 847,954,000 have been reclassified from administrative and other expenses, previously Shs 2,131,848,000, to raw materials and consumables, previously Shs 2,862,508,000.

In addition, leaf processing costs of Shs 189,682,000 relating to 2006 have been reclassified from revenues to raw materials and consumables as explained in Note 6 above.

These reclassifications have no impact on the reported profit for 2006.

8 Operating profit

The following items have been charged in arriving at operating profit:

	2007 Shs'000	2006 Shs'000
Employee benefits expense (Note 9)	1,440,870	1,238,748
Auditor's remuneration	6,500	7,000

9 Employee benefits expense

	2007 Shs'000	2006 Shs'000
The following items are included within employee retirement benefits expense / (reversal):		
- Defined contribution scheme	50,263	44,703
- Unfunded retirement benefits obligation (Note 16)	(6,629)	697
- National Social Security Fund	1,567	2,241

Contributions to the National Social Security Fund are determined by local statute.

10 Finance costs

	2007 Shs'000	2006 Shs'000
Interest income	6,666	1,076
Interest expense	(24,416)	(39,379)
Net foreign exchange losses	(40,658)	(24,133)
Net finance cost	(58,408)	(62,436)

11 Income tax expense

	2007 Shs'000	2006 Shs'000
Current income tax	548,266	438,383
Deferred income tax (Note 17)	115,683	106,721
Income tax expense	663,949	545,104

Notes

7 Finance costs

	2008 Shs '000	2007 Shs '000
Interest expense - bank borrowings	105,617	24,416
Net foreign exchange losses	39,399	40,658
Net finance costs	145,016	65,074

8 Profit before income tax

The following items have been charged in arriving at the profit before income tax:

	2008 Shs '000	2007 Shs '000
Employee benefits expense (Note 9)	1,723,145	1,440,870
Redundancy cost	142,129	184,039
Auditor's remuneration	7,350	6,500

9 Employee benefits expense

The following items are included within employee benefits expense:

	2008 Shs '000	2007 Shs '000
Retirement benefits costs:		
- Defined contribution scheme	62,768	50,263
- Defined benefit scheme (Note 16)	-	(6,629)
- National Social Security Funds	4,760	1,567

10 Income tax expense

	2008 Shs '000	2007 Shs '000
Current income tax	714,178	548,266
Deferred income tax (Note 15)	2,340	115,683
	716,518	663,949

Notes (continued)

	Group	
8 Profit before income tax	**2009**	**2008**
	Shs'000	**Shs'000**
The following items have been charged in arriving at the profit before income tax:		
Employee benefits expense (Note 9)	1,899,978	1,723,145
Auditor's remuneration	7,819	7,350

9 . Employee benefits expense	**2009**	**2008**
	2009	**2008**
	Shs'000	**Shs'000**
The following items are included within employee benefits expense:		
Salaries and wages	1,807,866	1,655,617
Retirement benefits costs:		
- Defined contribution scheme	90,197	62,768
- National Social Security Fund	1,915	4,760

10 Income tax expense	**2009**	**2008**
	Shs'000	**Shs'000**
Current income tax	697,065	714,178
Deferred income tax (Note 15)	(66,532)	2,340
Income tax expense	630,533	716,518

The tax on the group's profit before income tax differs from the theoretical amount that would arise using the statutory income tax rate as follows:

	2009	**2008**
	Shs'000	**Shs'000**
Profit before income tax	2,108,964	2,416,913
Tax calculated at domestic rate applicable to profit -30% (2008:30%)	632,689	725,074
Tax effect of:		
Income not subject to tax	(11,452)	-
Expenses not deductible for tax purposes	25,750	13,322
Over-provision of deferred tax in prior years	(16,454)	(21,878)
Income tax expense	630,533	716,518

Notes (continued)

8 *Profit before income tax*

The following items have been charged in arriving at the profit before income tax.

	Group	
	2010 Shs'000	[illegible]
Employee benefits expense (Note 9)	1,859,486	[illegible]
Auditor's remuneration	7,424	[illegible]
9 Employee benefits expense		
Salaries and wages	1,776,436	[illegible]
Retirement benefits costs:		
- Defined contribution scheme	80,336	[illegible]
- National Social Security Fund	2,714	[illegible]
	1,859,486	[illegible]
10 Income tax expense		
Current income tax		
- Current tax on profits for the year	929,652	[illegible]
- Adjustments in respect of prior years	41,068	[illegible]
Total current tax	970,720	[illegible]
Deferred income tax (Note 15)		
- Current deferred income tax credit	(57,532)	[illegible]
- Adjustments in respect of prior years	42,148	[illegible]
Total deferred income tax	(15,384)	[illegible]
Income tax expense	955,336	[illegible]