

SECTION OPERATIONS REPORT

**PHILIP
MORRIS**

SECTION MANAGER:

Barry M. Hopkins

HEADQUARTERS:

Detroit, MI

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PM USA
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I. MARKETING CONDITIONS**New PM Brand Introduction
Cambridge Full Flavor**

The initial sell-in on behalf of Cambridge Full Flavor is currently in process. The acceptance to date is well received and we anticipate no obstacles in obtaining respectable distribution levels. The field also reports that the sell-in and prebooking activities are going exceptionally well in management and retail accounts. Chains have been very receptive to the 2 for 1 promotion, which will be starting in July. We have implemented a preselling attempt on behalf of 2 for 1 at retail, which is meeting with great success.

Economic Conditions

An article in the Detroit Free Press quoted a spokesman from R. J. Reynolds, who revealed that they are in the process of eliminating 2800 jobs in their sales department over the next year. He stated that this would be accomplished via retirement and natural attrition and that no layoffs would occur. The R. J. Reynolds spokesman attributed this cutback to a shrinking cigarette market and heavy domestic competition. It is unclear, however, if this cutback will have an adverse affect on their field sales force, sales support or a combination of both. Locally, it is our understanding that only one R. J. Reynold's Division Manager has accepted this retirement package. Further more, we have found through a reliable source that R. J. Reynolds is offering two weeks salary for each year of service.

Kroger is embarking upon an \$80 million store expansion program which is projected to create up to 3000 new jobs in Michigan by the end of 1991 due. Over the projected five year program, Kroger will build 22 new combo-stores, which are the larger, state of the art, retail merchandising outlets. We will keep you apprised if additional information becomes available.

The new antismoking law that was put into effect January 1, 1987, in the state of Michigan, is becoming increasingly wide spread throughout the business community. The state law is having residual effects on industry, offices, plants, factories and the like. More and more businesses are adopting nonsmoking policies in the work place, i.e. The Steel Case Company has proposed removing vending machines from their plants; Superior Oil is banning smoking on company property. If this type of activity continues to grow at an alarming rate, it will obviously have adverse effects on overall consumption.

MARKETING CONDITIONS (cont'd)**Industry**

Wholesale Distributors anticipated the recent price increase and we have found that most warehouses have an abundance of inventory on hand. Many of the distributors have voiced their concerns about the price increase in lieu of probable doubling of the federal excise tax. All distributors are in receipt of their allocation printouts and we have found that they are taking full advantage of the additional buy-ins.

The Section sales year to date has realized a substantial improvement netting a 5.1% gain. This is largely attributed to the continued growth of the Marlboro, Merit and Virginia Slims franchises as well as the anticipation of the recent price increase. We are confident that our momentum in sales will continue on the positive side with the continued performance of the aforementioned brand families and the anticipation of the new product introduction throughout the balance of the year.

II. MAJOR COMPETITIVE DEVELOPMENTS**American Tobacco**

Major emphasis at retail is on behalf of the Malibu packing. Product is shipped from the manufacturer couponed at \$3.00 off per carton.

Sales Reps are aggressively attempting to place new grey, plastic value centers to house both Malibu and Lucky Strike Filters. Payment for these fixtures is based on store volume and number of shelves obtained. Top payment is \$35.00 per month or \$8.75 per shelf, per month (up to four shelves). Fixtures are six shelves high, four cartons wide and shelves are five high. An optional pack topper is also available and is used to display Malibu packs stickered at \$.30 off per pack. There has been limited reports of B1G1F displays of Malibu. Due to monthly payments, American has been successful in placing these value centers, however, brand movement has been very slow. As these value centers are lightweight and easily put together, American Reps are carrying several on their cars and are able to make placement immediately upon acceptance. Malibu has been displayed in 30-unit bins offering B3G3F in K-Mart stores only.

American continues \$2.00 coupons on Lucky Strike. They are also placing \$2.00 coupons on selected cartons of Pall Mall Menthol, Tareyton and Silva Thins, which are soon to be outdated cartons.

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MAJOR COMPETITIVE DEVELOPMENTS (cont'd)**Brown & Williamson**

B&W is in the process of introducing their generic brand, Falcon, at retail. All carton stock is couponed at \$1.00 off and packs are stickered at \$.10 off. In pack outlets, 40 and 80-pack set/sells are being placed (\$.10 off per pack) with a \$2.00 and \$3.00 placement allowance. A limited number of floor displays have been reported in high-volume outlets. Movement to date has been slow.

Reps are placing 2 for 1 displays for all Richland packings and they are selling in unlimited quantities for dump bins. Both \$1.50 and \$2.00 coupons continue to be attached to cartons on the shelf. Up to 60 cartons of couponed product are placed in floor displays. Payment is unknown.

Reps also continue to attach \$2.00 coupons to all product on the shelf. In some carton outlets, 30 cartons are placed in floor bins paying \$5.00 to the retailer.

Last month, we reported on the \$2.00 promo product for Viceroy. Now we are seeing Belair and Raleigh coming in the same way. These cartons and packs have separate UPC codes from the regular product, which is still seen. Outside cartons are preprinted with \$2.00 off savings and packs inside these cartons have a \$.20 band attached. Apparently, Reps are placing this product in a floor display, paying the retailer from \$5.00 to \$7.00. In some pack outlets, Reps are placing the promo packs in a counter display, usually 40 units paying \$2.00 to the retailer.

B&W is placing heavy emphasis on shelf talkers.

A female Sales Rep in Grand Rapids Southwest territory has quit. She is being replaced by a female from Kalamazoo while a Rep will leave the Ypsilanti area to fill the Kalamazoo area. A vacancy in Benton Harbor, which was reported last month, has been filled by a new hire.

Liggett & Myers

Eves are being promoted in 30-carton floor displays offering a free Jordache cigarette case with a carton purchase. Placement allowance is \$5.00. In conjunction, free standing counter cards advertise a Jordache luggage offer, five piece set for \$99.95. Fair movement noted on Eve offer. It appears that L&M is attempting to upgrade Eve's image via association with a designer name.

MAJOR COMPETITIVE DEVELOPMENTS (cont'd)**Liggett & Myers (cont'd)**

Limited promotional activity has been noted on behalf of their new generic brand, Total. In select accounts, 40-unit 2 for 1 displays have been noted with a \$2.00 placement allowance. Retailers report slow movement.

Emphasis on maintaining distribution and inventory levels on generic products. Reps appear to be more aggressive at buying space on value racks. They will pay \$2.00 a row and want two shelves. An L&M Rep has told us that they will settle for less. Their requirement is that they be directly below the manufacturer or supplier of the rack. They are attempting to force American to purchase the bottom shelf or shelves at \$3.00 per row. It appears likely that both companies will buy space in either location if it is good for their business.

Reps are still attaching \$1.00 coupon to Quality Seal generics along with talkers advertising the savings. New Quality Seal generics "gift shop" brochures are being promoted in all outlets carrying the brand. Reps are also placing cards advertising the new look of packs and cartons of Quality Seal generics. Instead of a black and white pack, they will look more like a branded generic with a red and blue colored pack. Not too many of the new packs have been seen to date.

Lorillard

Sales Reps continue to promote Kent packings in 80-unit displays offering four AA batteries with a 2-pack purchase. Placement allowance is \$4.00.

Most brands continue to be couponed at \$2.00 off on an indiscriminate basis, depending on movement in each account. In all accounts, coupon emphasis is on Newport packings.

Lorillard Reps report that their consignment fund is currently \$3,700. It has been reported that Sales Reps are paying permanent counter display payments in cash, but this has not been confirmed.

The new True Silver packings are continuing to arrive in the field with little fanfare. To move out old style packing, Reps are attaching \$1.00 coupons.

Lorillard is terminating low-volume Plan A accounts, i.e. Schmuckal Oil, Woodland Oil and Blodgett Oil.

MAJOR COMPETITIVE DEVELOPMENTS (cont'd)**R. J. Reynolds**

Continued promotional activity on behalf of Salem Light 100's in the custom case. Placing 40-unit 2 for 1 displays with a \$3.00 retail placement allowance. Retailers report fair to good movement.

Sales Reps continue to attach \$2.00 coupons to carton stock of Winston and Salem packings. In high-volume outlets, they are offering \$27.00 for a 120-carton floor display of same. There is a new slogan for the Salem family, "The Refreshest", which is seen on billboards. Also, please see attached Direct Account Fact Sheet for the new Winston Lights Box product.

Reps are beginning to make presentations on behalf of their new height-adjustable overhead package merchandiser. It has been reported that they are offering \$15.00 per month for placement of these fixtures. Apparently, this payment is for small basket type pack displays that are attached to the legs of the overhead. Thus far, we have been unable to obtain any written contract on this.

R. J. Reynolds has increased the coupons that they send out to people on a mailing list from \$2.00 coupons to \$2.50 coupons.

A company called Rapid Response in Dallas is sending out product preference surveys. In addition to the survey, which also asks questions on smokers in the family, they also have a flyer in the envelope telling the consumer that they will receive \$12.00 in cigarette savings by sending in the survey questionnaire form. Since R. J. Reynolds always advertises \$12.00 saving packets, we assume this might be their offer. We will report more on any further information as it becomes available.

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III. TRADE CLASSES**Wholesale Distributors**

On June 2, 1987, we attended the annual Michigan Candy and Tobacco Distributors and Vendors Association reception held at their headquarters in Lansing, MI. The reception followed their annual meeting of the board members. Representatives from most of the state's distributors were present. It is our understanding that among many topics, the issue of the proposed federal excise tax increase was discussed along with the Association's plans to unite in their efforts to oppose this. The mood at the reception was somewhat apprehensive due to increased competition and price cutting by distributors and pending litigation between several Association members. At last year's reception, PM was the only tobacco company present. This year, representatives from all five of our competitors were in attendance.

S. Abraham and Sons will be opening a new warehouse in Dexter, Michigan, within the next month. This facility will be used to supply product to stores they service in the Eastern portion of Michigan and Ohio. This warehouse was located in Dexter due to non-union labor. Fred Olert, Vice President of Sales, informed us that after the first 60 days in operation, he does not anticipate any slow down in volume at the Grand Rapids operation.

There has been no change with the problems that Gamby Candy is experiencing regarding minimal inventory on hand, partial shipments to their accounts and orders being filled late.

Wholesale Grocers

Nothing new to report.

Vending

ARA Vending of Steelcase, MI, may have to discontinue selling cigarettes in all Steelcase plants and offices. They apparently are concerned that by having cigarette machines on company property, they are encouraging smoking. The decision will be made sometime in June and if implemented, the machines will be removed in September. ARA has 55 machines on location and they sell 230 cartons of PM brands per week.

TRADE CLASSES (cont'd)**Vending (cont'd)**

During this reporting period, Special Activities Representative Larry Brown has been assisting Area Managers by conducting vending audits on a state wide basis. As a result of his efforts, we have identified both problems and opportunities within this trade class.

Sena Snacks Vending, a 43-machine account headquartered in Burton, MI, has informed us that they are converting from DataVend to TruCheck. They have sighted their reason being R.J. Reynold's claim that they will do all the administrative work for them, including making all brand changes in machines as they occur. We are developing a presentation to combat this impending change.

After reported DataVend presentations to HAV Vending, they have informed us that they are going to stay with TruCheck for now and will consider DataVend later in the year. They harbor ill feelings towards PM for being the last manufacturer to place them on direct. We are attempting to schedule a luncheon with their top management in an effort to smooth this out and build a rapport.

Supermarkets

An article in the Detroit News on June, 2, 1987, reports a management struggle within the ailing Chatham Supermarket chain. Wendell Smith (the sole shareholder of Nu-Trax, the owner of Chatham Supermarkets since his purchase from the founding family in May 1985) has gone to court in an attempt to wrest control of the company from its chairman. Smith is trying to force the ouster of Alex Dandy with charges that he has been "transferring assets from Nu-Trax to himself and/or entities in which he is interested" and concealing, destroying and/or altering assets and records of the corporation. The chain has gone from 41 stores, at the time of Nu-Trax's purchase, to their present 5 locations. Dandy, also chairman of the 29 store Hamady Supermarkets of Flint, was brought in during March of 1986 in an effort to reverse the chains loss of \$400,000 per week.

A row gap analysis presentation was given to Dannys Foods buyer Ray Konieczny. He expressed strong interest in System 2000, particularly the low profile unit, and gave us authorization to install a 3' and 5' CMS II unit in one location. This was placed and we will follow-up on System 2000 during our appointment on June 15, 1987.

TRADE CLASSES (cont'd)**Supermarkets (cont'd)**

Due to a carton fixture upgrade, we have obtained a Plan A agreement in one of the three qualified, but unsigned, Hamady Supermarkets for 54 rows. This brings the number of Plan A's in Hamadys to 23. Region FVB Manager Dennis O'Neil, with AM Mark Barton, presented FVB and AG programs with its new payment schedule to Buyer Bob Evert. His decision is pending.

During the past month, Eberhard has moved three self-service racks. Apparently, L. V. Eberhard, the owner, is behind this move and we have been told that if he could, Eberhard would discontinue selling cigarettes completely.

Convenience Stores

Sunshine Foods will place R. J. Reynolds overheads in 35 locations as R. J. Reynolds has offered to pay an additional \$33.00 per month per store in these locations via overpayment on permanent counter displays and addition of Doral display. The Buyer has also committed to six locations for PM overheads.

Convenience/Gas Outlets

Clark Oil has accepted M-4 prime in 64 locations effective June 1, 1987. Initial placement has begun with our M-4's on-hand inventory. Back up quantities have been ordered. All stations are dropping the Lorillard display and going exclusively with PM and R. J. Reynolds. We have also upgraded B-2's and B-3's to low profile B-4's prime in two CMS locations. Buyer Jim Beard attended the Marlboro Country Music Concert and we will be golfing with him at the GMR Outing in Flint on June 9, 1987.

Four Star Service has been sold to Farview. No details are known regarding merchandising changes in this account.

Gerry Graham of Meijer Gas has authorized BV/BG displays for all stores. Placement of these displays has begun and is proceeding smoothly.

Gas Stations

Nothing new to report.

TRADE CLASSES (cont'd)**Drug Stores**

On June 5, 1987, we gained a test store placement of PM pack modules in one Arbor Drug location. Buyer Ken Wilk was very impressed with the fixtures appearance and particularly like the personalized logos that we had made (via printer) for the test location. Based on test results, Ken will make a decision between our fixture and R. J. Reynolds spring load pack fixture for all 72 locations. We developed a brand POG for store use and the fixture was labeled and stocked.

On Tuesday, June 2, 1987, Perry Drugs named David Schwartz its new President and Chief Operation Officer in an effort to turn around a six month decline in earnings. Schwartz was most recently Vice-president of Drug and General Merchandise for the Kroger Company. Buyer Jim Plate has requested a presentation on behalf of generic cigarettes to broaden his knowledge of this category and to explore merchandising avenues. We have scheduled an appointment for the week of June 15, 1987.

Mass Merchandisers

F&M Distributors has been given a Plan A proposal, however, no decision has been made at this time. The chain is currently looking at non-self service merchandising. Kathy Seager, who is handling this account, is holding off on any future negotiations until the account decides what they want to do.

Liquor Stores

Nothing new to report.

Other Retail Outlets

Nothing new to report.

Returned Goods

Nothing new to report.

IV. SSM KEY ACCOUNT CONTACTS

No key account contacts were made during this reporting period.

V. MERCHANDISING**Plan A/Compact Impact**

We are currently in the process of setting the racks in the Speedway Chain to POG's. We anticipate that all 72 stores will be set by the end of this month. This will have a positive impact on the current level of penetration bringing it up from 75% to 80%.

We are embarking on a psychological ploy. We have put the rumor on the streets of our new Plan A and have been telling retailers that there may be changes in our area of choice thinking. This information has been relayed to the other tobacco companies, which has resulted in a phone call from the B&W District Manager. He is quite concerned about his primary shelf in most major chain accounts located in the Michigan market. He has been told that PM will no longer accept space unless it is directly below the manufacturers of the rack. A B&W Rep has advised us that, if this is our new policy, he will be happy to accept the fourth shelf in all major accounts. Although we may have no changes in our area of choice concept, and B&W occupies 80% of the third shelf space in our market, we may be able to reposition our product due to this concession by B&W. Upon the arrival of our new Plan A contract, we will develop a Plan A presentation geared towards primary shelves. We will then monitor our success and make adjustments as necessary. B&W has told us that they will be talking to all major chains giving the approval of adjusting from third shelf to fourth.

Plan A-1

We are in receipt of all information pertaining to the August Marlboro A-1 promotion. Area Managers have begun presenting this program to chain accounts and to date, acceptance has been excellent. We are receiving many favorable responses from the field pertaining to cash payments in noncontracted A-1 accounts. Due to this program, we anticipate 100% acceptance.

MERCHANDISING (cont'd)**Plan A-1 (cont'd)**

The Marlboro Lighter promotion is meeting with tremendous success, and right now, it is even more timely because it is running concurrent with the Detroit Grand Prix activities. With an event as major as the Grand Prix, it might be wise in the future to run a Marlboro carton and pack promotion simultaneously with this event as it really lends itself to heightening brand awareness and bringing additional attention to the Grand Prix event.

Plan AG/AV

Despite Reynolds aggressive campaign to dominate this category advocating their exclusivity of racks and high payments, we have still managed to realize a 10% increase in penetration of AG/AV's now totalling 485 on location. We are confident that with our increased payments, in contract terms, we will expand upon our recent achievements and realize approximately 650 AG/Av placements by year end.

Plan B/Plan R

We continue to increase our penetration of B displays throughout the operation. Year to date, we have increased our units by 112 on location for a 3.5% gain. Moreover, we have improved counter positions and upgrading prime locations by 35%.

With the arrival of the BV/BG displays during the past month, we have realized 18% increase in penetration of this unit. We currently have 2,298 on location for a total of 5,587 permanent counter displays on location. We anxiously await additional allocations of BV displays that would be placed during the introduction of Cambridge Full Flavor at retail.

Vending Programs

The Section total number of vending placement for 1987 is as follows: B&H Family-127, Marlboro Family-360, Merit Family-245, Parliament-0, Virginia Slims Family-60, Others-0.

MERCHANDISING (cont'd)**DataVend**

We have completed DataVend transaction forms on Canteen Vending of Detroit, which has been submitted to DataVend during this reporting period. At this time, Canteen is waiting for their preliminary run and adjustments will be made after reviewing these reports. This account has responded to DataVend in a very positive manner.

Ride-Withs

Nothing new to report.

RDA

Nothing new to report.

PM Fixtures

During a recent appointment with Jack Ronan of A&P Supermarkets, we received a favorable response toward the System 2000 test in the Detroit market. Jack has informed us that he will be rendering a decision on behalf of the test by the week of June 22, 1987. We will advise you of any developments.

SECTION ACTIVITIES

Our Merit Special Merchandising Program met with good success. At the close of the program, we realized a total of 750 cartons sold in 2100 stores averaging approximately 33 cartons per store. Once again, this program has provided an excellent vehicle for a much needed inventory on behalf of the Merit Merchandising Program. I would encourage the continuation of this and similar programs in the future as they prove effective in selling depth of inventory.

Our Management and Retail meeting, in support of the Cambridge Full Flavor introduction and ICR revisions, was most successful. Our thanks to the training department for providing quality overheads to present this material as well as explicit instructions.

SECTION ACTIVITIES (cont'd)

We continue to work on our POS warehouse consolidation program. In the Detroit market, Divisions 41-05 and 41-06 will consolidate to one location. We can also incorporate the three local Retail Merchandisers into this warehouse. We are still negotiating in the Grand Rapids area with several warehouses to complete our consolidation program. Our project date of completion is July 1, 1987.

All arrangements have been made for another successful Detroit Grand Prix. We have had excellent response from customers to attend this function and all sampling personnel will be in place during the weekend. Our thanks to Kathy Hookana's department for working closely with us and keeping us apprised of all developments. We will report on its success next month.

During this reporting period, a congressional meeting was held with Senator Vanderjack of Muskegon. The Senator is very much opposed to federal excise tax increases and is supporting our efforts 100%. We continue to receive favorable responses from the trade for our efforts in this area and it was discussed at great length during the MTCDDVA meeting that Philip Morris' aggressive campaign could have a definite impact on taxation.

Arrangements have been made for our June Management Meeting concerning our new Plan A program. All field personnel are anxiously awaiting this information. We have established objectives for Plan A in our operation that will result in improved merchandising through increased rows, improved rack positioning and increased inventory.

VII. SALES SERVICES

We currently have two new Merchandising Assistants in the office. It is recommended that an additional training class be conducted to render training in support of the PC and MIDAS System. I would recommend that a class be held in Richmond or in our Section to accommodate these two new individuals to get them off on the right foot in their new assignments.

SALES SERVICES (cont'd)

We have greatly enhanced our communications network throughout the operation with the introduction of beepers. We have found that this program has been most successful in providing excellent contact to improve merchandising and handle problems as they arise. We are currently considering the addition of three beepers that would be assigned to key personnel strategically located outside of the Detroit market for improved communications in these areas.

IX. MEDIA DEVELOPMENTS

The Grand Prix, obviously, draws a very large amount of attention and excitement prior to the actual race. There are a lot of radio and television advertisements announcing the event and pre-race activities, i.e. free tickets, local bar promotions from sponsors, etc. I feel it would be to our advantage if we look into increasing the awareness of Marlboro's participation in this event from a two dimensional aspect. First, billboards in high traffic areas with the Marlboro car appearing on the advertisement. Second, local promotional activities where we would have the opportunity to sample, give away incentives and free tickets to this event. In my estimation, I feel this would lend greatly to Marlboro's participation in this event.

X. ASSOCIATIONS/CONVENTIONS

All information pertaining to the Michigan Coin Machine Operators Association convention has been forwarded to New York. Mr. Joe Cook, President, would like us to sponsor a Saturday Night Cocktail party during this convention with a country music theme. He feels that Marlboro would be an excellent tie-in with his planned activities. During the convention last year, we sponsored a Hawaiian luau, which was a great success and we feel a country music theme would enhance our exposure at this meeting. Final details and cost factors will be presented once they are obtained.

We have participated in four golf outings during the past month, which has been conducive towards building much needed rapport with several accounts. Additionally, we are able to ascertain information relative to high level management.

We will also be participating in the Fontana Brothers and King Group trade shows next month. All arrangements will be completed and New York has been advised with all pertinent information.

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XI. MISCELLANEOUS COMMENTS

Our thanks to Don Jennings and Jim Medina for their prompt follow-up towards our suggestion of last month regarding POS backorders. We feel with the expansion of an additional 30 days, we can better monitor this activity.

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