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FROM: N. Granitz

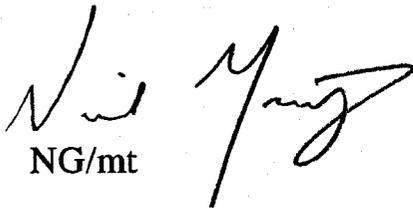
TO: MIG/MAG

April 22, 1994

RE: PROJECT X

Attached, please find the position paper for Project X.

Should you have any questions or comments, please feel free to see me.


NG/mt

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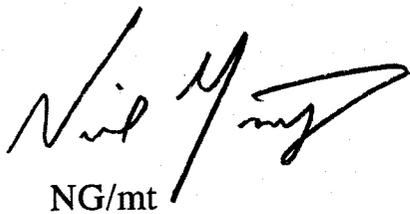
TO: R. Ackman
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P. Duhamel
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T. Lee
Y. Lessard

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NG/mt

Neil Granitz
MAG

PROJECT X

Introduction

The Federal Government and the Government of Ontario is currently considering the possible imposition of plain cigarette packaging. While this action has long been in the anti-smokers and (therefore) the governments' plans, the recent tax rollback has weighted the scales on the side of smokers and tobacco companies and legislating plain packaging may be seen as a way to appease the losers and bring it back into balance. Government review processes will begin with hearings in the next month with a recommendation expected to the Minister of Health by mid-June.

Packaging remains one of the last traditional tools to differentiate our brands and to reinforce our positionings. While the CTMC will be fighting the imposition of plain packs, we must prepare for the possibility by continuing to explore non-traditional means of communicating our positionings.

The objective of Project X is to yield a marketing strategy that allows Imperial Tobacco to competitively differentiate its trademarks on relevant attributes in a world of plain packaging. This paper will recommend the distinct areas that should be looked at and preparatory actions that should be taken in order to protect the integrity of our trademarks.

Before going any further, the **preventive strategies** currently in progress with the CTMC, Imasco, and Imperial Tobacco, will be discussed. While not part of Project X, they are included here to give the reader an appreciation of the complete picture.

The objective of the preventive strategies is to stop the government from legislating plain packaging. Preventative strategies are grouped into two areas:

- 1) Understand and alter the views of government on plain packs
- 2) Legal Challenges

1. **Understand and Alter the Views of Government on Plain Packs**

The key to success with this strategy is to understand what the government believes it will accomplish with the imposition of plain packaging and then to alter these views. There are two approaches to this. This can be achieved by showing the government that the means won't achieve the desired results or that the implementation has dire consequences. Each approach will be discussed separately.

Market research will be conducted to demonstrate that the imposition of plain packaging won't achieve the desired results. Past research will be reviewed and/or new research will be

undertaken, and then (if the results so indicate), the research will be strategically used to show them that plain packs will not achieve the desired objective. The CTMC is currently trying to get a better understanding of what the government hopes to accomplish. However, based on various sources (CTMC, Gervais Gagnon, Public Affairs), there are two objectives. The first is to lower the incidence of smoking, the second is to appease the health minister (who was a loser in the tax rollback). The first can be dealt with in research, the second cannot.

The government will likely support discussions regarding plain packaging with past research done on this issue. The most prominent piece of research will be the recently released research report by the Canadian Cancer Society entitled, "Effects of Plain Packaging on the Image of Tobacco Products among Youth." The research in this report arrives at the following conclusions (Please note how the conclusions build towards the effect of packaging on behaviour - smoking starting among teenagers):

Plain packaging can effectively break the link to other advertising and promotions

Plain packaging makes the package and therefore the product less interesting in its own right

Packaging has a greater influence on youth compared to adults

Packaging has a greater influence on youth contemplating smoking onset as compared to youth smoking regularly

Plain packaging is important as part of a comprehensive strategy to reduce smoking onset among youth but is insufficient on its own.

In reading through this comprehensive report, it becomes blatantly apparent that the research suffers from several major deficiencies. A critical assessment of the Canadian Cancer Society study was done by I.T.L. and R.B.H. Both points of view will be incorporated into a critical review done by Decima Research.

Additionally, primary research is currently being commissioned by the CTMC Research Council. The emphasis will be on understanding the link between packaging and smoking behaviour. As input to this process, a thorough search of all previous research, ITL and other, is currently under way. The objective is to determine if there is any research that supports or insubstantiates the link between branded packaging and smoking behaviour (starting, quitting). While the main emphasis is on packaging research, the closeness of this issue with the ad ban makes the abundance of research on cigarettes and advertising useful. The conclusions of several pieces of research will be briefly discussed.

Several key projects look at why smokers start - and the conclusions are similar. In examining the results of Project Viking, based on comparative analysis between those that smoke and those that do not smoke, the main reasons for smoking were peer pressure, family pressure or family affinity to smoke. In another study conducted by the International Advertising Association, entitled, "Why do juveniles start smoking?", the key conclusion is that "factors other than tobacco advertising and its regulatory control have played a key role in juvenile

smoking initiation and incidence....Instead the decision to start smoking involves mostly a combination of personal, family and social factors." Project Plus/Minus , done by I.T.L. in 1982 points to the same conclusions - steering more in the direction of peer pressure. One respondent is directly quoted as saying, "You start smoking because of social pressure, to look older, to prove you're as man, to be part of a gang." Finally, a study conducted by the children's research unit in London, England entitled, "The Effect of Advertising on Juvenile Smoking Behaviour," arrived at the same conclusions. The main reasons derived for starting were curiosity, peer pressure and family influence. This study was replicated in Canada giving the same results.

Moving in more closely on packaging, a study conducted at the University of Otago in New Zealand talks about packaging as follows, " The phonetic style and visual presentation of brand names, colour schemes....will serve to communicate information influencing the attractiveness of a brand of cigarettes to an individual." Note how the emphasis is on branding and not on starting or quitting.

The search has turned up several studies that more credibility make the link between advertising and starting. The 1993 U.S. Surgeon General Report states that one of the factors that creates a disposition to smoke is the perceived pervasiveness of smoking - youth smoke because they believe that more youth smoke than actually do - and advertising perpetuates this pervasiveness. This point would not apply to pack design. The second link that the Surgeon General report tries to bring out is also analyzed in a University of Arizona study entitled, "Social Image Factors as Motivators of Smoking Initiation in Early and Middle Adolescence." Both studies establish that young adults are at a stage in their life where they are most likely to recognize a gap between their ideal self and their perceived self. By projecting independence, self confidence, class etc., cigarette brands offer to artificially fill this gap. Therefore, a young adult will be more susceptible to be initiated into smoking. This point could be applied to packaging and will be explored in research.

Additionally, the council is currently initiating an attitude tracker which, among other things, will measure the importance of the tobacco issue with the populace. Based on past research, the results will likely point out that there are many issues of greater importance than the tobacco issue, this research may be used by the CTMC in lobbying government.

In trying to alter the government's view by showing them that there are dire consequences to such an action - there are several arguments at the disposal of the tobacco industry:

- 1) Economic Arguments: What will be the economic impact on the tobacco industry and suppliers (retailers, printers etc.) to the tobacco industry? Peat Marwick will be looking at the economic arguments under the supervision of the CTMC.
- 2) Competitive arguments: Much the same as spillover advertising arguments, the imposition of plain packaging would put the Canadian tobacco industry at a competitive disadvantage to foreign manufacturers who have a greater ability to differentiate their product through spillover advertising. Related to this is the possibility that smuggling could restart with branded packs being brought back into Canada and smokers willing to bypass traditional domestic channels to get a branded (and possibly cheaper) pack. LAMB will be looking at the smuggling angle under the supervision of the CTMC.

- 3) Counterfeiting Threats: We have already witnessed the appearance of counterfeit packs in Canada. The plainer the packs are - the easier they are to imitate. A rise in counterfeiting will cut into the government's tax collection.

Depending on the argument, the total industry represents many stakeholders. These stakeholders are made up of manufacturers, retailers, printers, growers, packaging industry, unions, other suppliers etc. Depending on what form these arguments take, the various areas will be harnessed appropriately by the CTMC.



PROJECT X STRATEGIES: PREPARATION FOR A WORLD OF PLAIN PACKS

Background

While the preventive strategies are designed to stop the imposition of plain packaging, the preparatory strategies assume that plain packaging is an inevitability and therefore we must be ready. These strategies are competitive as their goal is to allow I.T.L. to differentiate its products. The remainder of this paper will examine strategies designed to achieve this.

In developing future strategy an important step will be the pursuit of an understanding of how the government defines plain packaging. What elements of the pack remain and what elements of the pack are banished? For example, if the materials of the pack and the shape of the pack are defined in government legislation, then there is no reason in trying to develop packs of different shapes and sizes. At the moment, all we have to go on are the mock-ups used in the plain packaging research project done by the Canadian Cancer Society. In this study, plain packages were buff colour with black printing in standard font. Only the brand names, qualifier, health warning label and U.P.C. code appeared on the packages. Although it will be evolving over time, further clarification of how plain packaging is defined will be sought by the I.T.L. Public Affairs department.

At this point in time, it is difficult to predict what exactly will be the case. Imperial Tobacco must be prepared for everything. **The only valid assumption we can make is that we are going to lose all or part of packaging and the unique elements that it brings to the marketing mix in allowing us to communicate. Imperial Tobacco must be prepared and able to communicate product information and brand imagery in order to reflect the desired positioning and maintain brand differentiation with the target consumer.**

The Issues

What exactly could we be losing with the coming of plain packaging? Based on results from Project Project, packaging is a major communicator of information about the brand (brand name, strength, length, etc.). It is also a communicator of imagery. Within the imagery components, which image attributes is the pack strongest at establishing and reinforcing? Image results from several pack redesigns (Export, Omega, Ruby) were examined. The chart below shows the net imagery movement on key attributes. The scores below represent the gaps that result when comparing the ratings before the re-design to the ratings after the re-design among the targets.

	Omega	Export	Ruby
Strength	- .4	- .2	- .3
Masculinity	- .1	- .6	-
Quality	+ .3	+ .2	+ .1
Up-to-date	+ .8	+ .5	+ .1
Popularity	- .1	- .1	- .1
Youthfulness	+ .2	+ .4	- .1
Tradition	- .2	- .4	-

While the results are subject to the objectives of the project and the success of its execution, several generalities can be derived. Firstly, these results, as well as results from qualitative research have shown us that pack design is a powerful communicator of strength. It has the ability to uniquely position a brand versus its competition. As they are highly correlated to strength, aftertaste and irritation (not shown above) also can be positioned through the pack design - Project Trident showed that the pack design could even separate strength from irritation. Also related to this is masculinity - which the pack design can be a strong indicator of. Secondly, the scores above indicate that the pack is a great communicator of modernity (up-to-date). The pack redesigns have created considerable imagery movement on this attribute. Similarly, the pack also appears to be effective at communicating youthfulness and quality. Thirdly, for the attribute of tradition, a pack redesign appears to reduce tradition. We can assume that completely plain packs would impact negatively on tradition. Finally, the pack does not appear to be effective in conveying popularity.

Assuming a loss of these abilities through the loss of packaging, what tools could achieve the same job? Project Project tells us that in-store merchandising, product, public relations, sponsorship, sponsorship advertising, and unconventional communications (database marketing) can fulfill these roles. Additionally, all the characteristics of packaging should not be discounted - there are still the elements of shape and material which have been proven to be effective and strong communicators in past research (Lexus, Tomahawk, Trident). In essence, all four P's of marketing are still viable. At this point, the learning from Project Project needs to be positioned and understood in a world of plain packaging. The ability and depth to which other tools can replace what packaging was communicating needs to be better understood.

In the context of required speed of reaction, will there be imagery erosion over time and if so, how

long will it take? In Project Image, smokers are shown plain white card with trademark names written on them in black letters. Based on the results, it is apparent that smokers have no problem attributing image characteristics to the "plain" cards. Therefore, if plain packs are implemented, there would be no immediate liability. But if no reinforcement was done, it is a likely conclusion that, over time, there would imagery erosion with current smokers - and a lack of imagery differentiation for future smokers. While research may be able to tell us how long we can coast, there is no reason to search out that answer. Firstly, we should constantly be reinforcing our imagery and never allow a lapse. Secondly, our trademarks are not fully positioned as desired and there are currently projects on the books (Omega, Lexus, Tron) to reinforce these trademarks on the deficiencies. Finally, and most important, if we move swiftly and smoothly in the transition, there is a potential competitive advantage to be gained if we are able to strongly position our brands and our competitors are not.

Competitive Response

Possible competitive reaction must be understood. With the possibility of less packaging differentiation, the imposition of plain packaging may be seen as an opportunity for current generic/store brand producers to get deeper into the game. Although not an exact parallel, the experience in the U.S. tells an interesting story. When generic products and store brands were first introduced, they had low acceptance except among people who had no particular brand loyalty and made their decisions based on price. This changed in the late 80's, early 90's. Store brands underwent significant upgrades in packaging designs/logos that gave these brands a similar appearance to the name brands, allowing consumers to accept these products as a legitimate alternative to name brands. In Canada, the gap may be closing from the opposite direction. Instead of generic/store brands coming closer to major trademark brands, major trademark brands are coming closer to store/generic brands. In the absence of continued communication impetus, they could represent a threat. This increases the importance of significantly differentiating our brands not only from the major trademark competition, but also from the generic competition (generic/store/indian brands). The share and activities of these brands must be closely monitored and responded to. Any positioning research must include comparisons to these brands.

What will be the competitive reaction of our CTMC competitors? We can at least assume that they are doing everything we are in terms of planning differentiation strategies for their trademarks. We can also at least assume that they are not doing everything we are when it comes to applying ethics and complying with and interpreting the law. Historically, I.T.L. has always been law-abiding and ethical. The same has not been true of our competitors. Whether its re-entering smuggling, stickering their products or pushing sponsorship advertising to the limit - our competitors have been less cautious and less conscientious when it comes to a code of law and ethics. And they have used it as a competitive tool. We can assume no less this time around. While our actions will be guided by our own interpretation, in planning how we will react to their actions, the only view we can take is a wait and see approach. We must see what they do and then determine if it requires reaction. The only stipulation here is that the reaction must be fast. There is one special case that requires discussion and that is the case of a smuggling revival. Consumers may show a preference for branded packs and be willing to buy them through illicit channels. Product produced outside of Canada will certainly maintain full packaging integrity. Therefore, Canadian manufacturers could produce elsewhere and move their products through smuggling channels. As well as increasing share through distribution, this tactic would allow brand differentiation to continue as the smuggled packs would always be

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around mixed in with the plain packs. This tactic is not limited to Canadian producers - American and other producers could use this tactic. Our competitors have access to out of country production and we must prepare for it.

A PREEMPTIVE APPROACH

The starting point of Project X strategies is the assumption that plain packaging is a given and then the strategies deal with responding to what the government legislates. If plain packaging is a given outcome - then is there opportunity to participate in this outcome? Strategically, there is a competitive advantage for us to negotiate the governments definition of plain packaging. We should be prepared to recommend what parts of the package design would be most advantageous for ITL to keep.

PROJECT X ACTIVITIES

Based on the above, the project activities for Project X will be as follows:

- Gain a better understanding of consumer reaction to plain packs. What is their imagery? Which design elements are the strongest communicators for ITL? How do the brands compare?
- Revisit the Project Project understanding of communication tool strengths and abilities. We need to better understand what cues smokers will be looking for in a world of plain packaging. Additionally, there are many tools and properties of tools that we still don't fully understand.
- Based on an understanding of what packaging properties need to be replaced, explore new and innovative ways to communicate the trademark positionings (emphasis on strength, masculinity, quality, modernity, and youthfulness) and product information
- Reexamine the priorities of currently defined projects that have significant implications on trademark positioning objectives.

The first three will be tested in research. The fourth activity will be assessed during the prioritization of the marketing plans.

Development

Given the uncertainty of what form plain packaging will take, further understanding and development must encompass all possible losses of different pack messages. This can be divided into three categories:

- 1/ **Brand name and qualifier:** Although it is not expected that we will lose the brand name, the possibility cannot be ruled out. Development should concentrate on ways to communicate the actual name and qualifier, i.e. Player's Light, du Maurier Special Mild etc.
- 2/ **Other Information:** The pack also carries other information about the product such as quantity and type, i.e. "25 virginia cigarettes" or descriptive information such as "same strength, less irritation." We may have to find new ways to convey this information.
- 3/ **Image Information:** The logo, graphics, colour, lettering etc. are key image communicators. Development must focus on replacing this ability. The attributes that should be concentrated on are strength, masculinity, modernity, tradition, quality and youthfulness.

Each division in marketing will be assessing the ability of their area to effectively compensate for the loss of any of the above messages - and develop concepts to express this ability. A new brand launch poses different communication challenges than ongoing imagery reinforcement. Therefore, divisions should be looking at the two cases. Testing of concepts in the initial wave of research will allow us to better understand what is and what is not feasible.

As Project X unfolds, it may become evident that there are immediate actions I.T.L. can take to fulfill the "X" objectives and more long term actions that will be required. Given this assumption, an action plan will prioritize key activities.

Research

A wave of qualitative research exploring the above issues will be conducted. It should start with an exploration of what elements of the pack are most effective and valuable in communicating our positioning and then move in to the realm of plain packs. More specifically, what needs to be understood is the starting point for plain packs - how do consumers perceive them and how do they differentiate them versus the competition (CTMC and others). Research must also begin to explore the ability and depth of new tools to position the brands. Initial concepts aimed at filling the packaging gap will be tested. The timing of the research will be dependent upon the generation and availability of concepts by other departments in marketing.

Additionally, market research should assess the impact that plain packaging may have on information collection tools - and develop a plan to fill the gap.

Strategy

There are currently some key projects underway that have significant packaging implications. There may be net imagery gains to be enjoyed by executing faster or it may come to pass that the launch cannot occur before the implementation of plain packaging. Looking at different possible timing

scenarios for plain packaging, the prioritization of Omega follow-up, Tron, and Lexus will be reviewed and communicated.

Anticipating the further loss of traditional communication tools, Projects Alpha, Beta and Gamma were developed specifically to facilitate ITL's continued expression of its positionings. The implications of plain packaging on the project objectives and the timing of these projects will be reviewed.

As pricing could become a major cue for differentiation, the communication value of different pricing scenarios will be explored.

Packaging

Until proven otherwise, the packaging department should investigate all possibilities to develop communicative packaging that will establish and reinforce the desired positionings for each of our major trademarks. An exploration of materials and shapes should be undertaken. Previous research has proven that these are potent tools. For example, in Project Lexus, we saw that the shape of the package could communicate modernity, femininity and class. Another example is the tin. The actual tin and the materials used to manufacture the tin communicated quality and modernity. Once the proposed specifications are known, unrestricted opportunities to use the pack (such as graphics on the inside) should be investigated.

Product

If the results of Project ABC tell us that smokers can tell a difference, then we must analyze if these differences are reinforcing the positioning. If these differences are not reinforcing the positioning, it should be investigated if differences can be created that reinforce the current positionings. Regarding the components of the cigarette, past research has shown that these components - paper, filter, tobacco - are powerful communicators of many of the desired positioning attributes. For example, in recent Lexus research, the length and width were shown to be able to communicate masculinity/femininity. The tipping was shown to be able to communicate modernity and quality. The colour of the filter can communicate strength, and masculinity. In fine cut research, we have learnt that the colour and cut of the tobacco is a strong indicator of quality and strength. Use of these resources should be further examined and developed.

Trademarks

The legal ramifications of a trademark on a pack should be understood - is legislation possible that can deny a trademark appearing on the pack?. Depending on the answer, we should begin to explore the process of **descriptive trademarking**. Descriptive trademarking here is defined as the use of trademarks to differentiate or to describe a product benefit. An example of this would be to trademark a descriptor such as Superroll 200. Another effective use of this may be in trademarking names that

describe consumer needs. For example, anticipating price segmentation, we could trademark a brand, "Peter Jackson Value Price". It is clearly a tactic that is currently being used by R.B.H.

Communications

The resource allocation of sponsorship advertising should be examined. Should we be planning to spend more resources in this area given the dissolution of packaging? Prioritization should be scrutinized on the development of effective sponsorship advertising that clearly communicates the desired positionings of all our trademarks Companies.

Although it is not undertaken today, the use of company (trademark) spokespersons should be examined. Project Project taught us that public relations spokespersons can be valuable information and imagery reinforcing tools.

From a legal point of view, communications can examine the opportunities that will develop if brand graphics no longer appear on the packs. What are the ramifications for sponsorship and sponsorship advertising. For example, if they do not appear on the pack, can the branded graphics, letterings, etc. return to the advertising. The entire program of merchandising takes on an increased communication emphasis if the above is possible. Finally, communications should also be investigating unconventional means of communication for example, database marketing.

In-store merchandising should be researched to understand what is possible in-store to differentiate our brands. Similar to packaging, can the material and structure of displays be used to reinforce the positionings.

Field

The sales force will be assessing the effect that plain packs will have on merchandising. For example, will the Imperial Look still be viable? Is there still opportunity to use colour on the shelves? The difficulty of new product launches should also be evaluated.



Next Steps

In order to discuss direction and determine the timing and priority of this project, a project team will be assembled with representatives from each area of marketing.