Czech University of Life Sciences Prague

Faculty of Economics and Management

Department of Trade and Finance

Master's Thesis

Financial Analysis and Assessment of the Companies Operating in the Tobacco Industry in the Russian Federation

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Faculty of Economics and Management

DIPLOMA THESIS ASSIGNMENT

Bc. Veronika Mazanik

Economics and Management

Thesis title

Assessment of the Financial Position and Performance of the Chosen Companies Operating in the Tobacco industry in the Russian Federation

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Objectives of thesis

The aim of this diploma thesis is to assess and compare the financial position and performance of the chosen companies operating in the tobacco industry in Russia by analyzing the companies´ financial statements with focus on the representation and changes of the reported assets, liabilities, expenses, revenues and cash-flow for a chosen period and to identify the potential financial problems and the most significant factors influencing the profit from the companies and the industry point of view.

Methodology

Methodology for the literature overview is based on data collection from the relevant legal framework, specialized publications and other written or online sources. The practical part of the thesis will be based on the information gained from the published annual reports of the chosen companies. Vertical and horizontal analysis and ratio analysis of the financial statements will be used to assess the financial position and performance of the companies and to prepare the practical part of the thesis. The methods of analysis, synthesis, comparison and deduction will be used to formulate the conclusions of the thesis.

The proposed extent of the thesis

70-80

Keywords

financial statements, financial position, balance sheet, assets, liabilities, equity, financial performance, income statement, expenses, revenues, profit, financial analysis, cash-flow, tobacco industry

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Declaration

I declare that I have worked on my diploma thesis titled "Financial Analysis and Assessment of the Companies Operating in the Tobacco Industry in the Russian Federation" by myself and I have used only the sources mentioned at the end of the thesis. As the author of the diploma thesis, I declare that the thesis does not break any copyrights.

In Prague on 31.03.2024 ____________________________

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I would like to thank Ing. Enikö Lorinczova, Ph.D. and all other persons, for their advice and support during my work on this thesis.

Financial Analysis and Assessment of the Companies Operating in the Tobacco Industry in the Russian Federation

Abstract

The diploma thesis is concerned with the financial analysis of three companies that represent the Russian tobacco industry – Japan Tobacco International, Philip Morris International and British American Tobacco. Additionally, it is evaluated of whether leaving the Russian market in 2023-2024 will potentially inflict a serious damage to companies' finances. The methodology of the thesis is represented by the literature review and empirical analysis, where techniques of financial analysis (horizontal, vertical and ratio analyses) are applied.

In the end, it is concluded that Japan Tobacco International has the best financial position, while the worst one is identified in the case of Philip Morris. When it comes to financial performance, the best situation is identified for the case of British American Tobacco. Additionally, it is suggested that leaving the Russian market today can become very dangerous for companies already suffering from static revenues.

Keywords: financial statements, financial position, balance sheet, assets, liabilities, equity, financial performance, income statement, expenses, revenues, profit, financial analysis, cash-flow, tobacco industry

Finanční analýza a hodnocení společností působících v tabákovém průmyslu v Ruské federaci

Abstrakt

Diplomová práce se zabývá finanční analýzou tří společností, které zastupují Ruský tabákový průmysl-Japan Tobacco International, Philip Morris International a British American Tobacco. Dále se hodnotí, zda odchod z ruského trhu v letech 2023-2024 potenciálně způsobí vážné poškození financí společností. Metodiku práce představuje literární rešerše a empirická analýza, kde jsou aplikovány techniky finanční analýzy (horizontální, vertikální a poměrové analýzy).

Nakonec se dospělo k závěru, že Japan Tobacco International má nejlepší finanční pozici, zatímco nejhorší je identifikována v případě Philip Morris. Pokud jde o finanční výkonnost, nejlepší situace je určena pro případ British American Tobacco. Kromě toho se navrhuje, že opuštění ruského trhu dnes může být velmi nebezpečné pro společnosti, které již trpí statickými příjmy.

Klíčová slova: finanční výkazy, finanční pozice, rozvaha, aktiva, pasiva, vlastní kapitál, finanční výkonnost, výkaz zisku a ztráty, výdaje, výnosy, zisk, finanční analýza, cash-flow, tabákový průmysl

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FDI	Foreign Direct Investment
EBT	Earnings before Taxes
EBIT	Earnings before Taxed and Interest
COGS	Costs of Goods Sold
USD	United States Dollar

WTO	World Trade Organization
JTI	Japan Tobacco International
EPS	Earnings per Share
PMI	Philip Morris International
BAT	British American Tobacco
RRP	Reduced-risk Products

1 Introduction

In light of the recent circumstances that effectively surround the Russian business environment, where the overwhelming majority of international companies leave the Russian market, it is downright essential to see how one crucial industry for the country performs. This industry is the tobacco industry, which is traditionally represented by the production and processing of tobacco-related items, which has for a very long time been regarded as a very important one for the Russian Federation and its predecessor – the Soviet Union.

Interestingly enough, the Russian tobacco market has quite recently become subject to the ongoing globalization and lowering borders for investment that happened in the 90s, when the majority of national industries were privatized and sold to private investors. The tobacco industry became one of industries, where there is almost no presence of purely Russian companies since the market is split just between three international holdings that own countless subsidiaries all over the world thus serving as parent companies – Japan International Tobacco, Philip Morrison and British American Tobacco. These are the companies that supply the whole entirety of different tobacco brands and varieties that are consumed by ordinary Russian residents and inhabitants (Lunze & Migliorini, 2013)

Due to this, the following diploma thesis is dedicated to the financial analysis, where the financial position and performance of the three companies will be assessed and compared with each other. Given the fact that the overwhelming majority of companies from various different segments announced their retreat from the Russian market, where some of the selected companies have already done so and initiated the talks for selling their business in Russia, it serves as a perfect foundation for carrying an analysis dedicated to the financial wellbeing of the companies. This can help to understand if the potential leave of the Russian market can deteriorate the situation with finances in those companies in a horrific way or the companies had been doing relatively great prior to the events of 2022-2023 and they are not likely to be hit at all by the decision to leave the market (Sonnerfeld et al., 2022).

The significance of the study is huge because it can serve as a potential basis of a future analysis where in a matter of years the effect of leaving the market once and for all will be evaluated with the help of an ex-post analysis.

2 Objectives and Methodology

2.1 Objectives

The main goal of the diploma thesis is to assess the financial position in terms of assets, liabilities and equity of the three selected companies – Japan International Tobacco, Philip Morris and British American Tobacco. Furthermore, the situation with the companies' cash-flows (operating, investing and financing) is addressed, as well as the financial performance with regard to revenue, expenses and profit of the top companies operating in the Russian tobacco industry.

Additionally, the thesis has subgoals that are mainly associated with the identification of factors influencing the profit of organizations, identification of potential risks and the evaluation of the effect of potentially leaving the Russian market once and for all performed by either of the companies.

2.2 Methodology

The diploma thesis relies heavily on the use of both induction and deduction. Both methods are made possible through an extensive process of data collection for the selected time period covering three fiscal years – 2020, 2021 and 2022, based on the available information as of Summer 2023. The main source of data are financial statements published publicly by all companies, which can be found on their websites, and parts of them are presented in the list of appendices to this diploma thesis.

Furthermore, the thesis uses the literature review and the document analysis techniques to form the basis for the empirical research carried in the practical part of the work, whereas the latter is represented mainly by three different techniques of financial analysis – the horizontal analysis (calculating percentual difference between given years and the base year), the vertical analysis (calculating shares of sub-elements from the selected parts of the financial statements) and ratio analysis (liquidity, solvency, profitability, efficiency and market valuation). The very last covered dimension of financial ratio analysis involves manipulations with stock market data, which is extracted from the Yahoo Finance. Overall, the methodology of the thesis is expected to help to achieve the objectives set earlier in the diploma thesis.

3 Literature Review

3.1 Tobacco Industry

The tobacco industry occupies a prominent position within the global economic sphere, exerting considerable influence on public health policies, economies, and societies worldwide. The sector has experienced significant changes over the course of several centuries, influenced by changing consumer preferences, developments in technology, and altering regulatory environments. This chapter provides an in-depth analysis of the historical evolution of the tobacco industry, with a specific focus on the rise of prominent tobacco companies, an examination of their market domination, and an exploration of the significant societal ramifications associated with tobacco smoking (Musk & De Klerk, 2003). The modern process of producing tobacco is presented in Figure 1.

Figure 1, the production process of tobacco

Source: Gretener & Magramo, 2022

The origins of tobacco can be traced back to the pre-Columbian Americas, during which indigenous tribes employed tobacco for spiritual, medical, and social functions. In the wake of the Columbian Exchange, tobacco was brought to Europe during the 16th century, experiencing swift and widespread acceptance throughout the continent. During the 17th century, tobacco emerged as a fundamental agricultural commodity in numerous European colonies, with a special emphasis on the American territories. The pivotal role of enslaved labor in the building of tobacco plantations significantly influenced the foundational development of the business. Effectively, the specific nature of the commodity significantly contributed to the fact that tobacco was seen as a luxury good back then, mainly due to problems with transportation and logistics (O'Connor et al., 2022).

During the 19th century, there was a notable transformation in the tobacco industry as it underwent a process of industrialisation, leading to the emergence of important tobacco businesses. Philip Morris International, a company of significant historical importance, was established in the year 1847 in the city of London. It has since maintained its presence and influence over an extended period of time. Nevertheless, it was during the late 19th and early 20th centuries that tobacco corporations commenced the process of establishing a firm and widespread international foothold. British American Tobacco (BAT) established itself as a prominent entity within the business, resulting from the amalgamation of several British corporations in the year 1902. In a parallel manner, the American Tobacco Company undertook the process of merging with various smaller companies throughout the United States over the aforementioned timeframe. Further information about the biggest players of the industry will be provided in the analytical narrative of this diploma thesis (Slade, 1989).

The 20th century witnessed a notable era of growth and broadening of scope for tobacco corporations. The RJ Reynolds Tobacco Company, established during the latter part of the 19th century, implemented notable advancements such as the introduction of pre-packaged cigarettes and the popular Camel brand during the early 20th century. The aforementioned advancements resulted in the conversion of tobacco from a loose-leaf item into a consumer commodity that could be produced on a large scale. During the following decades, additional prominent entities, like Japan Tobacco International (JTI), Altria Group (formerly known as Philip Morris Companies), and Imperial Brands, made their entry into the market. The expansion of huge firms has engendered heightened levels of rivalry and innovation, hence yielding a diverse array of cigarette brands, flavors, and marketing tactics (Bero, 2005).

During the mid-20th century, a limited number of corporations had emerged as prominent entities within the tobacco sector. These corporations wielded substantial influence over worldwide markets, policy-making processes, and societal perspectives. The concentrated structure of the business facilitated these corporations in exerting significant influence on the formation of public narratives pertaining to tobacco consumption, frequently employing assertive promotional strategies. Tobacco corporations made substantial investments in advertising, utilizing strategies that specifically targeted diverse demographic groups and effectively capitalized on the dynamic shifts in cultural trends. The Marlboro Man emerged as a prominent advertising character, serving as a symbolic representation of masculinity and toughness, so playing a significant role in enhancing the popularity and desirability of Marlboro cigarettes. The industry's capacity to foster and sustain a devoted client base was assisted by the implementation of marketing methods, in conjunction with the addictive properties of nicotine (Yach & Bettcher, 2000). The Marlboro Man's caricature is presented in Figure 2.

Figure 2, Marlboro Man

Source: Ellis, 2021

The societal impact and controversies around a certain subject matter are of significant importance in academic discourse. These factors play a crucial role in shaping public opinion and influencing policy decisions. The influence exerted by the tobacco industry has been a subject of much discussion. The relationship between tobacco consumption and adverse health consequences, particularly the development of lung cancer and cardiovascular ailments, became progressively more apparent during the course of the 20th century. Concerns over the public health implications of extensive tobacco usage were raised by health advocates, medical experts, and governments. Consequently, regulatory measures were introduced, such as the inclusion of health warnings on cigarette packaging and the imposition of limitations on tobacco advertising (Palazzo & Richter, 2005).

The responses of tobacco firms to the increasing body of scientific information and growing public health concerns exhibited a range of divergent approaches. In many cases, there were attempts made to minimize the health hazards linked to tobacco consumption or to question the reliability of research results. These measures played a significant role in the development of a multifaceted network of legal disputes, public image management efforts, and policy discussions involving the business and diverse groups of individuals and organizations with vested interests (Chapman & Freeman, 2008).

3.2 Accounting Legislation in Russia

Accounting legislation in Russia is quite specific mainly due to the fact that the country was isolated for more than 70 years during the 20th century, which definitely influenced a numerous number of specificities and peculiarities within the Russian accounting legislation. The roots of the modern Russian accounting legislation can be traced back to the Soviet Union, whose basis was formed on the territory of modern Russia. The Russian Federation itself became a part of the Soviet Union under the name of the Russian Soviet Socialist Republic, becoming the center of the newly established state (Sokolov & Kovalev, 1996).

Quite unique external policy and the status of one of the first socialist countries in the world led to the creation of a unique system of accounting. The accounting system of the Soviet Union was largely associated with the centralized planning that was exercised by the economy of the newly established state, thus contributing to meticulous audit procedures that were associated with business transactions. Consequently, the dual accounting system was established that involved ordinary transaction procedures and then the track of the current business progress. Furthermore, there was an evident lack of the true cost and financial decisions because there was no functioning market and decisions were made usually by the party (Richard, 1995).

Once the Union dissolved in 1991, there was an evident need to change the system that could not function in the new environment at all. With the first wave of liberal reforms, a particular number of those reforms touched the accounting legislation and got rid of the majority of planning and audit mechanisms used in the Soviet Union. Furthermore, a huge number of newly privatized companies required a new piece of legislation that will be suitable for privately owned companies since in the past, the companies were state-owned and the central planning was suitable for those companies (Truhachev et al., 2017).

With the establishment of the new Constitution of Russia in the end of 1993 and the reworked Civil Code of the country, the latter made the first efforts to create a legal basis for accounting practices in Russia by introducing the concepts such as civil relations, contracts, property and obligations. Notably, this was explicitly states in the second part of the new Civil Code dedicated to business law and provisions for accounting and financial reporting. As the time went on and the process of privatization continued, the new Russian government made a huge effort to ensure that the Federal Law "On Accounting" will be finally published and become valid from 1996. This piece of law established the main principles of Russian accounting, trying to make the Russian legislation closer to the international one. One of the main principles introduced in the law was the concept of the double-entry bookkeeping, which became the foundation for ensuring a further harmonization of Russian accounting (Sarikas & Djatej, 2005).

Alternatively, the accounting law was not the only one introduced in 1996. Alongside the earlier mentioned legislation, there was the first official legislation introduced associated with audit activities. The Federal Law "On Auditing Activity" from 1996 establishes the main foundation and legal framework for auditing practices in Russia. It helps companies to better understand the requirements for auditing firms and describes the process of conducting auditing procedures (Enthoven, 1999).

In 2001, there was a new wave of accounting legislation published in the Russian Federation. The Federal Law "On Consolidated Financial Statements" from 2001 for the first time introduced a clear guideline on how to prepare, process and present consolidated financial statements. In addition to that, explicit instructions were given on how to prepare specific financial statements – what should be included, and which elements should explicitly be stated. This was another huge step forward towards the harmonization of Russian accounting and approaching the international standards. Furthermore, this specific law ensured that foreign companies would have to perform more or less similar accounting procedures as in the rest of developed world, thus increasing the investment attractiveness of the country. In addition to that, the Federal Law "On Joint Stock Companies" published in 2001 addressed that kind of companies in more detail, especially in terms of the advised management and process of reporting financial statements. In 2008, there was a similar effort done by the Russian Federation to significantly improve the process of managing limited liabilities companies by introducing a unique legislation for those companies (Aletkin, 2014).

When it comes to the main authorities regulating Russian accounting, it is important to specify that the main regulatory body is The Ministry of Finance of the Russian Federation with its seat in Moscow (the office is presented in Figure 3), just like any other big ministry. Concentration of ministries and institutions in Moscow helps the Russian Federation to achieve a higher degree of cooperation between different institutions and ensures a better cohesion. Apart from the Ministry of Finance, it is still important to stress out the role that both The Federal Tax Service (the office is presented in Figure 4) and the Central Bank of Russia (the office is presented in Figure 5) play in the accounting world of the country (Kim, 2013).

Figure 3, the Ministry of Finance of the Russian Federation

Source: Saeedy & Wirz, 2022

At last, it is important to stress the most important information about the Russian Federation’s accounting system and its peculiarities. The country demands that all firms will be reporting the information in the Russian rubles, which is pretty logical given that it is the only national currency in the country. Furthermore, the information should be disclosed in Russian, which is also pretty common everywhere in the world. The fiscal year in Russia starts on the 1st of January and lasts until the 31st of December, which is also once again pretty common in the world (Combs et al., 2013).

Figure 4, the Federal Tax Service of the Russian Federation

Source: The Moscow Times, 2023

Finally, the taxation of the country made the country quite attractive in the past due to its relatively eased taxation. The value of the corporate tax in Russia accounts for 20%, where 3% go directly to the country's federal budget and the rest is distributed within the region where the company is based. For this purpose, there are significant problems with regional disparities in the country due to the fact that the overwhelming majority of the country's business entities are based in Moscow or its vicinity. In total, tax rates in the country vary between 15.5% and 20%, which is lower than in the majority of developed countries that significantly contributed to the country's attractiveness in the early 00s and 10s, thus leading to very high figures of the foreign direct investment (Generalova et al., 2016).

Figure 5, the Central Bank of the Russian Federation

Source: Reuters, 2022

3.3 Financial Analysis

The financial analysis is a very important domain of the accounting because it helps ordinary users and financial analysts to draw essential insights about performance of business entities. However, as it usually happens with specific kinds of analyses, there are infinitely many techniques that all very by difficulty, application and logic behind those techniques (Higgins et al., 2009).

One of the most common and important techniques of financial analysis is the horizontal analysis. There are two specific approaches to this kind of analysis, where the first one uses the chain indices, which traditionally show the percentual change compared to the previous period and calculated according to the formula (1):

$$Chain\ Index = \frac{X_n}{X_{n-1}} \qquad \text{(White et al., 2002).} \qquad (1)$$

Alternatively, it is possible to implement another kind of statistical measure to see the development of specific financial elements over time. Usually, when performing a specific kind of analysis on the selected time period, the situation in given years is compared against the base year, which is usually taken as the first year on the analysed time horizon. The base index is used in such cases, which is calculated according to the formula (2):

$$Base\ Index = \frac{x_i}{x_0} \qquad \text{(White et al., 2002).} \qquad (2)$$

For convenience purposes, both indices are then transferred to percentages. Furthermore, it is vital to specify the role that the vertical analysis plays in the financial analysis. The vertical analysis is a unique kind of analysis that compares the shares of individual elements against the totals of categories or totals for sections, such as for example total assets or total liabilities. For the purpose of performing the vertical analysis, ordinary shares are calculated, whose calculation is identical to the calculation of both chain and base indices (Gibson, 2012).

One of the most important techniques used in the financial analysis is the ratio analysis that is traditionally performed with regard to 5 categories. Each category reflects the situation with a specific spectrum of traits and characteristics. Nevertheless, the first one is usually regarded as the most important one because it sets the foundation for nearly all operations of the company and ensures further activities of organizations. This domain is the liquidity, which traditionally encompasses three different ratios – the current ratio, indicating if the total current obligations prevail over the total current assets; the cash ratio, indicating if the total current obligations prevail over the total cash and its equivalents, and the acid-test ratio, indicating if the total current obligations prevail over the total current assets minus inventory accounts (Salmi, 1994). For the first and the third ratios, the figures above 1 are preferred, whereas the figures above 1 for the second ratio might not be so good since companies cannot directly make any sales or revenue from cash, so having too much cash is not itself a problem, but it restricts companies by incurring a specific opportunity cost on it. The three ratios are calculated according to formulas (3), (4) and (5):

$$Current\ Ratio = \frac{Total\ Current\ Assets}{Total\ Current\ Liabilities} \qquad (3)$$

$$Cash\ Ratio = \frac{Cash\ and\ its\ Equivalents}{Total\ Current\ Liabilities} \qquad (4)$$

$$Acid - Test\ Ratio = \frac{Total\ Current\ Assets - Inventories}{Total\ Current\ Liabilities}$$ (Breuer et al., 2012) (5)

The second most important category are solvency or stability ratios. Those ratios usually indicate the degree of indebtedness and identifies if the current degree of debt can be considered to be problematic or catastrophic. There are infinitely many ratios, but the most important ones are debt-to-equity and debt-to-assets, where both of them indicate the share of liabilities in the total equity or assets. If the value is above 1, it indicates an excessive debt burden of a company, which is bad. Additionally, the equity ratio is another ratio used, which is mainly implemented for the purpose of identifying the main source of financing of the company with the values above 0.5 indicating that the equity financing is mainly exercised by the given company (Ibendahl, 2016). At last, the interest coverage ratio identifies how easily a company pays interest on its outstanding debt. All ratios are calculated according to formulas (6), (7), (8) and (9):

$$Debt - to - Equity = \frac{Total\ Liabilities}{Total\ Equity} \tag{6}$$

$$Debt - to - Assets = \frac{Total\ Liabilities}{Total\ Assets} \tag{7}$$

$$Equity\ Ratio = \frac{Total\ Equity}{Total\ Assets} \tag{8}$$

$$Interest\ Coverage\ Ratio = \frac{EBIT}{Interest\ Expense}$$ (Brindescu-Olariu, 2016). (9)

The third category of ratios are concerned with the profitability of companies. Given the fact that companies' sources of revenue are usually split into 2 – operating income and non-operating one, there are infinitely many different ratios that are used for this type of analysis. However, only the most important ones will be addressed, where 2 categories particularly stand out – the return ratios and margin ratios. Return ratios, such as the return on equity and return on assets indicate the share of annual net income in the total value of equity and assets, respectively. Margin ratios indicate the share of net income or other elements from the total value of sales or revenue (Laitinen, 2017). For all profitability ratios, higher margins are preferred. Profitability ratios are calculated according to formulas (10), (11), (12), (13), (14) and (15):

$$Return\ on\ Equity = \frac{Net\ Income}{Total\ Equity} \tag{10}$$

$$Return\ on\ Assets = \frac{Net\ Income}{Total\ Assets} \tag{11}$$

$$Gross\ Margin = \frac{Gross\ Profit}{Total\ Sales} \tag{12}$$

$$EBIT\ Margin = \frac{EBIT}{Total\ Sales} \tag{13}$$

$$EBT\ Margin = \frac{EBT}{Total\ Sales} \tag{14}$$

$$Net\ Margin = \frac{Net\ Income}{Total\ Sales} \qquad \text{(Rutkowska-Ziarko, 2020).} \tag{15}$$

The fourth category of financial ratios are quite specific as they are concerned more with micro-management and techniques processed within organizations. Efficiency or activity ratios usually indicate the frequency at which companies either pay their debts, collect their debt or replace their inventory. All ratios show frequencies, whereas it is possible to transform those frequencies into period ratios which indicate the number of days until a particular action will be performed on the part of the company. In some countries, the basis for those period ratios is taken as 360 days, but in the majority of the financial world it is the period of 365 days that is considered (Monea et al., 2010). Efficiency ratios are calculated according to formulas (16), (17) and (18):

$$Payables\ Turnover = \frac{Credit\ Purchases/COGS}{Payables} \tag{16}$$

$$Receivables\ Turnover = \frac{Credit\ Sales/Revenue}{Receivables} \tag{17}$$

$$Inventory\ Turnover = \frac{Credit\ Purchases/COGS}{Inventory} \qquad \text{(Arsyad et al., 2021).} \tag{18}$$

At last, the very last category of financial ratios is not usually included in financial analyses due to their complexity and a need to calculate the same ratios for other companies due to the need of comparing those ratios since the numbers themselves do not directly produce any important information within the context of specific industries. Those ratios are market valuation ratios, and they are traditionally represented by the P/E ratio, which shows the number of monetary units needed to get 1 unit of the EPS, and the P/B ratio, which shows the times by which the company's current valuation exceeds the book value of the company (Campbell & Shiller, 2001). Those ratios are calculated according to formulas (19) and (20):

$$Price - to - Earnings\ Ratio = \frac{Price\ per\ Share}{EPS} \tag{19}$$

$$Price - to - Book\ Value\ Ratio = \frac{Price\ per\ Share}{Book\ Value\ per\ share} \text{ (Hall, 1999).} \tag{20}$$

3.4 FDIs and Subsidiaries

Given the context of the analysis and the fact that the analysed industry in the selected country of the Russian Federation is almost entirely represented by subsidiaries of foreign multinational corporations, it is wise to briefly mention the phenomenon of the FDI and the reasons behind numerous acquisitions that are being performed by international holdings (Helpman, 2006).

The FDI is a specific kind of foreign trade operation where a given foreign company or entity sets its foot into foreign environment by directly owning assets in the country. There are various forms of the FDI, but it is vital to understand that the FDI as a whole is a very complex due to the presence of countless factors that influence the decisions to invest or not to invest in particular environments. Scholars believe that inflation rates, unemployment rates, risk of expropriation, harmonization of accounting, tax system, exchange rates and interest rates are the most important factors that help investors to decide on whether to invest or not in a specific country (Blonigen, 2005).

When it comes to the types of foreign direct investments, it is possible to distinguish the following ones:

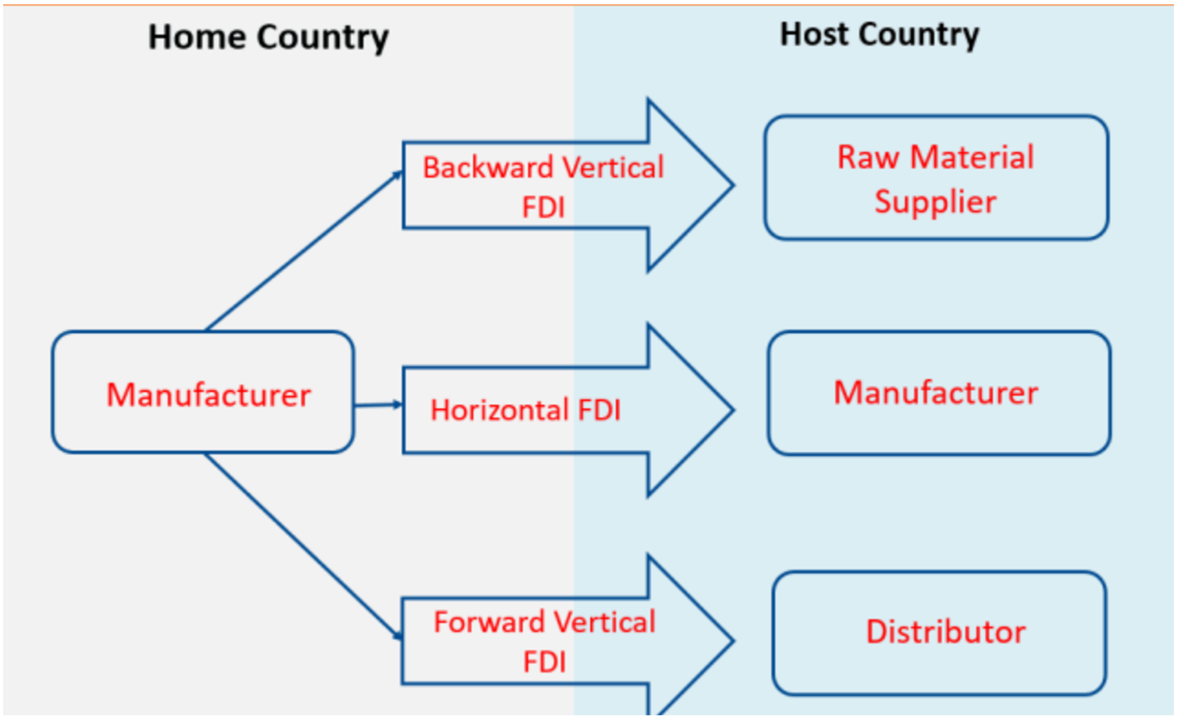
1) Joint-ventures – this type of foreign business activity is usually represented by a series of projects carried jointly with other companies who constantly exchange experience and contribute jointly with their resources and other assets in order to achieve a common success. This is quite common to encounter, but there are still risk such as growing a potential competitor (Kogut, 1988).

2) Acquisitions – a healthy alternative to join-ventures, where one company becomes dependent on another are acquisitions. Acquisitions usually involve either the purchase of an already functioning company, which is technically a takeover, being either a hostile or friendly one. The cases when a company builds the infrastructure from the ground is the riskiest one and they are usually called the greenfield investments (Gaughan, 2010).

3) Mergers – when two companies decide to merge into one and cooperate mostly on equal terms or on predefined shares are mergers, when the outcome of the merger is the creation of a new legal entity rather than the creation of a subsidiary for the parent company (Cartwright & Schoenberg, 2006).

In addition to the general description of the types of FDI, it is also vital to specify that there can be 2 broad types of integration – vertical and horizontal types of integration. Vertical integration is usually described by the situation when a particular company operating in a given industry will purchase another company that lies on the supply chain, such as, for example, a producer of soft drinks acquiring the producer of cans and bottles. Alternatively, the horizontal type of integration is concerned with the acquisition of the companies operating in the same industry and forming the part of the same business environment (Colangelo, 1995). The broader explanation of the situation from the paragraph is presented in Figure 6.

Figure 6, the breakdown of FDI



Source: Yadnya Investment Academy, 2019

4 Practical Part

The practical part of the diploma thesis is mainly split into 2 equally important section – the section containing the results of extensive research about the company's recent history and notable events, and the financial analysis. In the financial analysis, 2 out of 3 companies employ the USD currency, whose exchange rate to the Czech Crown is equal to 21.98 Czech Crowns needed to buy 1 USD. One company employs the Japanese Yen currency, whose exchange rate to the Czech Crown is equal to 0.15 Czech Crowns needed to purchase one yen. Alternatively, 1 USD yields the total number of 144.9 Japanese Yen needed to buy 1 USD.

4.1 Information about the Companies

The companies selected for the analysis were already briefly introduced in the theoretical part of the diploma thesis, where just one company was until now absent from the narrative – British American Tobacco. In this subchapter of the practical part, all the three companies will briefly be addressed and the most important information about them will be specified in the narrative. The first company that will be discussed in the chapter is Japan Tobacco International, whose logo is presented in Figure 7.

Figure 7, Japan Tobacco International – the logo

Source: Japan Tobacco International, 2023

Japan Tobacco International (JTI), based in Geneva, Switzerland, is a prominent player in the worldwide tobacco sector, renowned for its dedication to innovation, excellence, and ethical conduct. JTI operates in multiple countries and also in the country of the diploma thesis' focus – the Russian Federation, with the objective of offering consumers tobacco products that meet regulatory standards and align with societal norms, thereby ensuring customer satisfaction.

One noteworthy characteristic of JTI's portfolio is its assortment of varied brands, each strategically designed to appeal to distinct market categories. Winston occupies a key position among its iconic brands. Winston is renowned for its pronounced flavor profile and extensive historical background, making it a preferred choice among individuals in search of a unique and discerning smoking encounter. The commitment of the brand to providing exceptional quality continues to be a fundamental aspect of its identity. Camel is also a significant contributor to JTI's product portfolio. Camel, a brand with a rich history spanning more than a century, has gained widespread recognition for its distinctive blend of tobacco and classic packaging. The ongoing popularity of the brand is attributed to its capacity to adapt to shifting consumer demands while maintaining its timeless core. JTI's brand portfolio is further enhanced by the inclusion of Mevius, a brand renowned for its contemporary approach and pioneering product solutions. Mevius targets the modern smoker by prioritizing a sophisticated and polished encounter with its diverse array of offerings. JTI aggressively promotes reduced-risk products (RRPs) in accordance with its dedication to responsible practices, acknowledging the dynamic nature of tobacco consumption patterns. Ploom TECH, a brand that gives a heated tobacco sensation, serves as a prime example of JTI's commitment to offering alternative options that may have lower health risks in comparison to conventional smoking.

The global operations of JTI encompass more than its range of products. The corporation places a high emphasis on its corporate social responsibility, actively participating in activities that make beneficial contributions to both communities and the environment. The dedication of the company is evident not only in the quality of its products but also in its work to promote sustainable practices and provide support to local initiatives. JTI stays at the forefront of innovation as the tobacco business undergoes ongoing transformation. The corporation's dedication to research and development guarantees a consistent flow of novel products that are in line with evolving trends and shifting consumer tastes.

The next company on the list is Philip Morris International or simply Philip Morris, whose logo is presented in Figure 8.

Figure 8, Philip Morris - the logo

Source: Philip Morris, 2023

Philip Morris International (PMI) is well recognized as a key frontrunner in the global tobacco sector, acclaimed for its steadfast dedication to innovation, excellence, and socially responsible initiatives. PMI's objective is focused on providing satisfactory tobacco experiences while maintaining compliance with rigorous regulatory standards and societal expectations, with activities extending across multiple nations. One notable characteristic of PMI's comprehensive portfolio is its remarkable assortment of brands, which have been carefully developed to effectively appeal to specific groups of consumers. Marlboro holds a prominent position among its iconic brands. Marlboro, renowned for its distinctive branding and rich flavor characteristics, continues to captivate individuals in search of a strong and intense smoking encounter. The enduring legacy of the brand serves as evidence of its unwavering commitment to consistently providing great quality. Apart from Marlboro, the company does also possesses another important brand from the premium segment – Parliament.

Another key technology is IQOS, which is PMI's innovative heated tobacco technology, where the company became the innovator. In alignment with the organization's strategic aim of promoting a smoke-free future, IQOS presents a viable alternative for adult individuals who engage in smoking and are actively pursuing possibly diminished-risk alternatives. The aforementioned unique approach exemplifies PMI's dedication to ongoing development and adaptation in order to effectively address the increasing demands of consumers. PMI has articulated a resolute aspiration to shift towards a future devoid of smoking, aligning with its dedication to responsible activities. This concept is exemplified by brands such as HEETS, which are specifically formulated for utilization with IQOS devices that employ a heating mechanism to generate tobacco vapor rather than relying on combustion. This transformative measure demonstrates PMI's commitment to provide choices that are in line with changing consumer desires and developing scientific knowledge.

PMI demonstrates a dedication to sustainability that goes beyond its product offerings, encompassing a wider range of corporate activities. The company actively participates in projects aimed at promoting environmental conservation and social responsibility, so demonstrating its commitment to generating a beneficial influence within the areas in which it operates. With a commitment to inclusivity and a focus on promoting creativity, PMI's workforce is composed of individuals from all backgrounds, thereby cultivating a culture that appreciates novel viewpoints and innovative problem-solving approaches. The use of a collaborative strategy enhances the company's capacity to effectively facilitate and promote constructive transformation within the industry.

PMI continues to maintain a leading position in the ongoing restructuring of the tobacco industry. The corporation's allocation of resources towards research and development serves as evidence of its dedication to providing groundbreaking products that meet the changing demands of consumers.

The logo of the final company – British American Tobacco, is presented in Figure 9.

Figure 9, British American Tobacco - the logo

Source: British American Tobacco, 2023

British American Tobacco (BAT) holds a prominent place in the global tobacco market due to its strong dedication to innovation, consistent quality, and responsible corporate conduct. BAT's primary objective is to deliver satisfying tobacco experiences while upholding strict regulatory requirements and meeting society expectations, as seen by its extensive activities in several nations.

BAT's wide portfolio is centered around a collection of remarkable and different brands, which have been carefully developed to cater to distinct sectors within the market. Within this selection, a limited number of prominent brands emerge, each making a distinct contribution to the diverse range of offerings provided by BAT.Dunhill is widely regarded for its enduring refinement and sophistication, embodying a seamless fusion of conventional values and contemporary elements. The brand caters to individuals who possess an appreciation for luxurious aspects of existence, desiring a smoking encounter that mirrors their cultivated preferences. Dunhill's goods, characterized by a rich heritage in opulence, exemplify a steadfast dedication to meticulous artistry and superior standards that resonate with aficionados and discerning individuals who indulge in smoking. Lucky Strike, a brand with a rich history spanning several decades, epitomizes qualities of audacity and a strong taste profile. The brand's emblematic logo and easily recognizable packaging have established it as an emblem of American popular culture. The continued popularity of Lucky Strike can be ascribed to its capacity to provide a unique smoking experience that appeals to individuals who choose a boulder and more pronounced taste profile. Pall Mall is widely recognized for its well-balanced blend and smooth characteristics, making it highly appealing to individuals who desire a harmonious and pleasurable tobacco experience. The brand's capacity to deliver a comprehensive smoking experience has garnered a loyal following throughout its existence. Pall Mall exemplifies BAT's commitment to provide readily available choices without compromising on quality. Kent is well-known as a trailblazer in the realm of filter technology, and its name has become linked with ground-breaking advancements in this industry. The introduction of filtered cigarettes by the brand brought about a significant transformation in the act of smoking, with the primary objective of mitigating specific hazards commonly connected with conventional smoking practices. The dedication of BAT to responsible innovation is exemplified by Kent's commitment to utilizing scientific knowledge in order to improve the safety of tobacco consumption.

British American Tobacco (BAT) is positioned as a leading player in the market, actively responding to evolving consumer preferences by providing alternative options. VUSE is a strategic initiative undertaken by British American Tobacco (BAT) in order to address the market need for products that have the potential to offer lower risks. The line of electronic nicotine delivery systems (ENDS) offered by VUSE caters to adult smokers by providing them with a smoke-free option that is in accordance with the latest advancements in scientific knowledge. The aforementioned brand serves as a prime example of BAT's dedication to effecting positive change within the industry.

In addition to its assortment of brands, British American Tobacco (BAT) demonstrates a commitment to ethical business practices throughout all aspects of its operations. The organization is actively involved in endeavors aimed at fostering sustainability, community advancement, and environmental preservation. British American Tobacco (BAT) acknowledges its responsibility in fostering a constructive influence within the communities where it conducts its operations and is dedicated to making significant contributions that extend beyond its primary business activities. The incorporation of diversity and inclusion is fundamental to BAT's corporate culture. The organization prides itself on maintaining a diverse workforce that encompasses a wide range of backgrounds, experiences, and opinions. The presence of a varied personnel pool contributes to the generation of innovative ideas, nurtures creativity, and enables BAT to effectively adapt to the intricate and ever-changing dynamics of the business.

Considering the dynamic changes occurring within the tobacco sector, British American Tobacco (BAT) maintains a steadfast commitment to fostering innovation. The company's significant allocations of resources towards research and development highlight its dedication to providing innovative products that meet the changing demands of consumers and correspond with growing market trends.

4.2 Analysis of Financial Position

4.2.1 Japan Tobacco International

The second subchapter of the practical part is dedicated to the analysis of the financial position of the selected companies, where a large emphasis is put on the situation with three important sections of every balance sheet – liabilities, assets and equity. For this purpose, it is vital to proceed to the first company whose financial position is analyzed – Japan Tobacco International. The assets of the company are presented in Table 1.

Table 1, Japan Tobacco International's assets

	2020	2021	2022
Cash	¥ 538,844	¥ 721,731	¥ 866,885
Account Receivable	¥ 427,104	¥ 475,615	¥ 499,139
Bad Debt	-¥ 1,923	-¥ 1,306	-¥ 2,533
Inventory	¥ 539,762	¥ 563,182	¥ 691,906
Prepaid Expenses	¥ 351,789	¥ 419,022	¥ 475,688
Total Current Assets	**¥ 2,003,919**	**¥ 2,321,289**	**¥ 2,723,591**
Net Property	¥ 759,290	¥ 755,843	¥ 775,957
Accumulated Depreciation	¥ 955,461	¥ 1,043,554	¥ 1,132,061
Total Investments	¥ 152,117	¥ 155,364	¥ 206,804
Intangible Assets	¥ 2,272,996	¥ 2,368,117	¥ 2,692,505
Total Non-Current Assets	**¥ 3,377,463**	**¥ 3,452,920**	**¥ 3,824,487**
Total Assets	**¥ 5,381,382**	**¥ 5,774,209**	**¥ 6,548,078**

Source: analytical contribution based on annual statements

The very first aspect that is worth noting based on Table 1 is the fact that the values are presented in Japenese Yen due to the company's tendency to report it in the domestic currency of Japan, which is pretty logical. Overall, based on the selected time period, it becomes quite apparent that the company was keen on actively augmenting the value of assets that it possessed during the studied period. More comprehensive and detailed overview of the changes in the reported assets can be drawn after focusing on performing the horizontal kind one analysis, which is presented in Table 2.

Table 2, Japan Tobacco International - horizontal analysis of assets

	2021	2022
Cash	33.94%	60.88%
Account Receivable	11.36%	16.87%
Bad Debt	32.09%	-31.72%
Inventory	4.34%	28.19%
Prepaid Expenses	19.11%	35.22%
Total Current Assets	**15.84%**	**35.91%**
Net Property	-0.45%	2.20%
Accumulated Depreciation	9.22%	18.48%
Total Investments	2.13%	35.95%
Intangible Assets	4.18%	18.46%
Total Non-Current Assets	**2.23%**	**13.24%**
Total Assets	**7.30%**	**21.68%**

Source: analytical contribution based on annual statements

As it might strike as obvious, the number of periods included in the horizontal analysis is reduced to just 2 – the year 2020 was selected as the base year for the analysis. First, the value of cash increased in both 2021 and 2022, whereas the company seems to have a tendency to annually increase the value of the liquid asset by approximately 30%, which might be an indicator of the company's strategy to remain liquid. On the other hand, the account receivables did also increase in both 2021 and 2022, but the magnitude of the increase was not so astonishing, which is good. In fact, increase in the value of receivables is a pretty common situation in the world of retail companies – since companies increase their revenue with each year, the number of credit sales does also go up, thus leading to frequent situations of accumulating debts. A more detailed look at the situation with the account receivable will be taken during the analysis of financial ratios, but the situation seems to be rather stable even despite a visible augmentation in the value of the element.

What is, in fact, more important when looking at the receivables is the bad debt allowance account, which indicates doubtful debts about which the company is not sure at all. Thus, the value rose in 2021 by 32.09%, which is not a good sign, whilst in 2022 it dropped below the level of 2020 – 31.72% less than the value in 2020. Inventory is one of the most crucial accounts of any manufacturing and retail company, because it often represents the main generator of revenue. In the case of Japan Tobacco International, the inventory account was gradually increasing – just a minor increase of 4.34% in 2021, which was followed by the increase of 28.19% in 2022, compared to 2020. This specific piece of information is likely to indicate that the company's volume of sales was increasing with approximately the same pace, which would be quite logical.

Another important piece of statistics that indicates a positive retail dynamic of the company is the fact that increased the value of the prepaid expenses in both 2021 and 2022, compared to the original level of the year 2020. Thus, the percentual increase in 2021 accounted for 19.11% and in 2022 it accounted for 35.22%. This indicates that the company was doing quite good, and it did not want to put an additional burden, so they decided to gradually pay off their creditors earlier in order to potentially concentrate on other long-term projects of the company.

All in all, the total current assets increased by 15.84% in 2021 and then the element increased by 35.91% in 2022, which is quite good. Furthermore, it is quite likely that the company's liquidity went up under the condition that the company did not increase the value of the current obligations, which will be evaluated in the same subchapter soon.

What is quite interesting to note, in fact, is that the company's net property was not increasing and furthermore, the value did decrease by 0.45% in 2021, which is pretty uncommon given that the year 2021 is traditionally regarded as the year when the majority of companies initiated their recovery from the pandemic. On the other hand, there might be 2 potential explanations of this phenomenon – the first explanation is that the company did not want to risk and venture into any long-term projects, or the second option is that the company faced some serious problems with the accumulated depreciation, which is pretty logical after all. In fact, the percentual increase in the value of the accumulated depreciation – 9.22% in 2021 and 18.48% in 2022 indicates that it might be the case indeed.

The value of the total investments rose by 2.13% in 2021 and then by 35.95% in 2022, which is a good sign indicating that the company was not just accumulating short-term assets, but it was also keen on making important investments that are likely to generate future cashflows. The same applies to intangible assets, which increased in both 2021 and in 2022 by 4.18% and 18.46%, respectively. Finally, the increase in the non-current assets was visibly lower than the one registered for the current section of assets, but it is still quite good – 2.23% in 2021 and 13.24%.

To draw the bottom line, it is important to address the changes that took place in the total value of assets. In 2021, the increase in the value of assets accounted for 7.3%, whilst the total value of assets increased by 21.68% in 2022, which is a very good sign indicating a positive overall dynamic of the company. On the other hand, it is quite logical to anticipate that there will be an increase in the liabilities and equity, which will have the same magnitude. However, before addressing the other part of the balance sheet equation, it is first essential to perform the vertical kind of analysis on the company's assets, which is presented in Table 3.

Table 3, Japan Tobacco International - vertical analysis of assets

	2020	2021	2022
Cash	10.01%	12.50%	13.24%
Account Receivable	7.94%	8.24%	7.62%
Inventory	10.03%	9.75%	10.57%
Prepaid Expenses	6.54%	7.26%	7.26%
Total Current Assets	**37.24%**	**40.20%**	**41.59%**
Net Property	14.11%	13.09%	11.85%
Total Investments	2.83%	2.69%	3.16%
Intangible Assets	42.24%	41.01%	41.12%
Total Non-Current Assets	**62.76%**	**59.80%**	**58.41%**
Total Assets	**100.00%**	**100.00%**	**100.00%**

Source: analytical contribution based on annual statements

The logic behind the vertical analysis is crystal clear – the framework addresses the proportions that each element has in the total value of assets. Starting with the current section of the balance sheet, it is pretty apparent that the value that the cash and its equivalents account represents from the total assets is rather large – approximately from 10 to 13%, which is quite a large figure. On the other hand, the share of the account receivables is not so large and it started to decrease in 2022, so it is logical to anticipate a similar kind of tendency for the upcoming fiscal year. The share of inventory is high, but it is pretty normal for a company specializing in the retail. Effectively, there are cases when the share is even higher, so for one of the biggest international manufacturers of tobacco, this can be regarded as a relatively modest share in the total value of assets. The value of prepaid expenses is not so high, but it is quite logical since this is not the most important asset possessed by the company. In total, the share of current assets in the total assets was rapidly increasing – from 37.24% in 2020 to 40.20% in 2021 and finally until reaching the share of 41.59% in 2022.

Consequently, it is important to address the long-term section of the company's balance sheet using the same framework. The share of net property is inadequately small, especially in 2022 when it reached the bottom with the share of 11.85%, whereas at the beginning it accounted for 14.11%. On the other hand, the share of total investments is rising, which is good, but it is still unlikely that the element will represent a significant portion of the total assets anywhere soon, especially when bearing in mind the fact that Japan Tobacco International is a retailer of tobacco. Finally, what is quite surprising here is the fact that the company has an enormous share of intangible assets in the total assets, accounting for slightly more than 40%. In total, the share of long-term assets is larger than the share of current assets, which is pretty common, but the tendency is rather concerning as it is rapidly diminishing as of 2022 and it is quite logical to anticipate a further decline. Finally, the other side of the equation will be addressed shortly in the narrative, with the presentation of the compilation of the company's liabilities and equity presented in Table 4.

Table 4, Japan Tobacco International's liabilities and equity

	2020	2021	2022
ST Debt	¥ 160,500	¥ 161,347	¥ 157,629
Payables	¥ 233,723	¥ 272,327	¥ 273,028
Income Tax	¥ 46,462	¥ 30,794	¥ 37,470
Other Current	¥ 883,108	¥ 1,035,858	¥ 1,094,537
Total Current Liabilities	**¥ 1,323,793**	**¥ 1,500,326**	**¥ 1,562,664**
LT Debt	¥ 864,912	¥ 817,811	¥ 861,010
Provision for Risks	¥ 363,090	¥ 319,043	¥ 270,606
Other Liabilities	¥ 165,646	¥ 180,990	¥ 196,976
Total Non-Current Liabilities	**¥ 1,458,095**	**¥ 1,387,803**	**¥ 1,368,653**
Total Liabilities	**¥ 2,781,888**	**¥ 2,888,129**	**¥ 2,931,317**
Paid-In Capital	¥ 736,400	¥ 736,400	¥ 736,400
Retained Earnings	¥ 2,783,718	¥ 2,863,843	¥ 3,089,909
Treasury Stock	-¥ 491,507	-¥ 490,899	-¥ 490,183
Total Equity	**¥ 2,599,494**	**¥ 2,886,081**	**¥ 3,616,761**
Total Liabilities and Equity	**¥ 5,381,382**	**¥ 5,774,210**	**¥ 6,548,078**

Source: analytical contribution based on annual statements

It was quite logical to anticipate that the total value of L+E will increase accordingly, which is the case with Japan Tobacco International. Overall, it seems that the company's main emphasis in terms of financing is put on the equity type of financing with the change occurred in 2022 – until then, the company had been keen on relying on the debt financing. Nevertheless, it is vital to proceed to the horizontal analysis of the liabilities and equity, which is presented in Table 5.

Table 5, Japan Tobacco International - horizontal analysis of liabilities and equity

	2021	2022
ST Debt	0.53%	-1.79%
Payables	16.52%	16.82%
Income Tax	-33.72%	-19.35%
Other Current	17.30%	23.94%
Total Current Liabilities	**13.34%**	**18.04%**
LT Debt	-5.45%	-0.45%
Provision for Risks	-12.13%	-25.47%
Other Liabilities	9.26%	18.91%
Total Non-Current Liabilities	**-4.82%**	**-6.13%**
Total Liabilities	**3.82%**	**5.37%**
Paid-In Capital	0.00%	0.00%
Retained Earnings	2.88%	11.00%
Treasury Stock	0.12%	0.27%
Total Equity	**11.02%**	**39.13%**
Total Liabilities and Equity	**7.30%**	**21.68%**

Source: analytical contribution based on annual statements

The situation with the company's liabilities is rather straightforward – there was almost no increase in the value of the short-term debt, which is a very good sign, especially when considering the fact that this kind of debt usually entails the highest interest rates. Henceforth, it is logical to anticipate that the interest expense of the company has fallen accordingly. On the other hand, the company experienced a logical increase in the value of payables in 2021, which remained pretty constant in 2022, which might be a sign that the company quickly paid off its previous liabilities from the same dimension. This is not a good sign as a whole, but when considering that payables are traditionally regarded as the main fuel of operations and relationships with suppliers, the situation becomes less concerning.

The income tax liability was diminishing in 2021, but it slightly increased in 2022, which is after all a pretty normal situation, especially if one assumes that the company made higher volume of sales in the year. As a whole, the total value of the short-term obligations increased by 13.34% compared to 2021 and by 18.04% compared to 2022, which is seen as a very steep and adequate increase. On the other hand, the situation with the long-term assets is rather surprising – the company experienced a rapid diminishing pattern for almost all accounts from this section – both the long-term debt and provisions for risks decreased by significant amounts, whereas there was a partial recovery to the level of 2020 for the long-term debt element in 2022. As a whole, there was a decrease in the total value of the non-current liabilities, which definitely confirms that the company was focused on transforming to the equity financing.

When it comes to the equity section, the increase in the section was mainly explained by the increase in the value of the retained earnings that accounted for 2.88% in 2021 and by 11% in 2022, which is a very good tendency indicating that the company was making strong gains during the studied period of time. Overall, the total equity of the company increased by 11.02% and by 39.13% in 2021 and 2022, respectively, which is an outstanding result. Finally, the value of the total liabilities and equity increased by the same amounts as the previously discussed section of assets – 7.3% in 2021 and 21.68% in 2022. Now, the vertical analysis is performed – the results are presented in Table 6.

Table 6, Japan Tobacco International - vertical analysis of liabilities and equity

	2020	2021	2022
ST Debt	2.98%	2.79%	2.41%
Payables	4.34%	4.72%	4.17%
Income Tax	0.86%	0.53%	0.57%
Other Current	16.41%	17.94%	16.72%
Total Current Liabilities	**24.60%**	**25.98%**	**23.86%**
LT Debt	16.07%	14.16%	13.15%
Provision for Risks	6.75%	5.53%	4.13%
Other Liabilities	3.08%	3.13%	3.01%
Total Non-Current Liabilities	**27.10%**	**24.03%**	**20.90%**
Total Liabilities	**51.69%**	**50.02%**	**44.77%**
Paid-In Capital	13.68%	12.75%	11.25%
Retained Earnings	51.73%	49.60%	47.19%
Total Equity	**48.31%**	**49.98%**	**55.23%**
Total Liabilities and Equity	**100.00%**	**100.00%**	**100.00%**

Source: analytical contribution based on annual statements

The share of the short-term debt in the total value of the liabilities and equity is low – under 3%, which is a good sign potentially indicating high solvency of the company.

Payables' impact is much more considerable – under 5%, while the share of the income tax is extremely low, which is a pretty common situation after all. Overall, the share of the total current liabilities in the total liabilities and equity accounts for approximately 25%, which is a good sign almost certainly meaning that the company has no problems with liquidity. On the other hand, one of the largest accounts that the company has is the long-term debt, which has the share ranging between 13.15% and 16.07%, which is quite common for a multinational holding. The share of non-current liabilities is ranging between 20.9% in 2022 and 27.1% in 2020, but there is an obvious tendency that is aimed at decreasing the burden that this account has. Overall, the share of liabilities in the company's liabilities and equity was initially equal to 51.69% but then rapidly dropped to 44.77%, which is an outstanding result.

On the other hand, the company did experience a decrement in the share of retained earnings, but it did not stop the company from effectively increasing the share of equity from 48.31% in 2020 to 55.23% in 2022, which makes the conclusion that the company, as of 2022, is focused on the equity financing possible.

4.2.2 Philip Morris

The next company on the list is Philip Morris, where the same sequence is applied once more, where the asset section of the company's balance sheet is introduced first. This is presented in Table 7.

Table 7, Philip Morris' assets

	2020		2021		2022	
Cash	$	7,285	$	4,500	$	3,217
Account Receivable	$	3,761	$	3,940	$	4,756
Bad Debt	$	-23	$	-70	$	-42
Inventory	$	9,591	$	8,729	$	9,886
Other Assets	$	855	$	557	$	1,760
Total Current Assets	**$**	**21,492**	**$**	**17,717**	**$**	**19,619**
Net Property	$	7,062	$	6,694	$	7,304
Accumulated Depreciation	$	8,544	$	8,564	$	8,733
Total Investments	$	4,804	$	4,485	$	4,772
Intangible Assets	$	7,983	$	9,498	$	26,387
Total Non-Current Assets	**$**	**23,323**	**$**	**23,573**	**$**	**42,062**
Total Assets	**$**	**44,815**	**$**	**41,290**	**$**	**61,681**

Source: analytical contribution based on annual statements

This time, the values for different elements are reported in millions of US dollars. For sure, the tendency identified for the next company is quite different from what has been observed earlier. At first glance, Philip Morris is developing in drastic manner with no specific pattern that is observed for all the three studied years. Nevertheless, the horizontal analysis is applied in Table 8.

Table 8, Philip Morris - horizontal analysis of assets

	2021	2022
Cash	-38.23%	-55.84%
Account Receivable	4.76%	26.46%
Bad Debt	-204.35%	-82.61%
Inventory	-8.99%	3.08%
Other Assets	-34.85%	105.85%
Total Current Assets	**-17.56%**	**-8.71%**
Net Property	-5.21%	3.43%
Accumulated Depreciation	0.23%	2.21%
Total Investments	-6.64%	-0.67%
Intangible Assets	18.98%	230.54%
Total Non-Current Assets	**1.07%**	**80.35%**
Total Assets	**-7.87%**	**37.63%**

Source: analytical contribution based on annual statements

Cash and its equivalents were not rising for the case of Philip Morris, unlikely for the case of Japan Tobacco International. In 2021, there was a decrease in the magnitude of 38.23%, which was followed by even larger decrease compared to the base year – 55.84% in 2022. This might be a consequence of the policy adopted by the company and aimed at increasing liquidity as a response to the pandemic of coronavirus, which was exercised by many companies around the globe and apparently, the tobacco industry is not an exception in that regard.

There was an increase in the value of receivables, first by 4.76% in 2021 compared to 2020 and then by 26.46% in 2022 compared to the base year. This is a sign that the company might have quite likely increased the total value of earned revenue, a significant portion of which was represented by credit sales. In addition to that, it is important to mention that the company faced a problem with bad debt or doubtful accounts because the increase in the value in 2021 was enormous – 204.35% until partially recovering and dropping to just 82.61% lower than in the year 2020. This is a problem that indicates that some of the company's partners are not fully reliable and trustworthy, so the company would definitely have to further diversify its partners.

When it comes to inventories, the situation is rather surprising because it is anticipated that companies will initiate the recovery from the pandemic in 2021 and slowly increase the total value of investments, but it is not the case since there was a decrease registered in 2021 equal to 8.99%. The tendency did change in 2022, but the magnitude of just 3.08% is not an impressive result that indicates that the company might have not in fact achieved any increase in the total number of sales. Overall, there was a decrease in the total value of current assets in both 2021 and 2022, whereas the decrease in 2021 was rather large – 17.56% compared to the base year, whilst in 2022 it accounted for just 8.71%.

Continuing with the long-term section of the asset accounts, there was a slight decrease in 2021 in the net property account, but it soon turned out to be an increase in 2022, when the value of the element became 3.43% larger than the value of the same element in 2020. This is quite logical because the companies were hesitating to carry the majority of the planned long-term projects forward due to the uncertain nature of the business environment in the period between the first and the second wave of COVID-19. Accumulated depreciation increased by inconsiderable figures, which is a good sign.

On the other hand, the fact that the total investments did not increase at all and remained on more or less the same level in 2022 as in 2020 is not a good sign, because there is no way for the company to ensure future cashflows from their investment projects, which might be a crucial factor for the company's profitability in the future. Yet, the company was following something that was already noticed in the case of Japan Tobacco International – both companies experienced a tremendous increment in the value of intangible assets. This, undeniably, could be a direct consequence of the WTO's efforts in the domain of intellectual property and patents, which become more and more protected nowadays and companies do not hesitate to rely on them. Overall, compared to the total current assets, the total non-current assets first experienced a decrease in 2021, but then quickly recovered and almost doubled the figures of the base year in 2022 – a 80.35% increase, which is a very good result.

Consequently, it is possible to highlight that the total assets' value first decreased in 2021 by 7.87% and then reached the value 37.63% higher in 2022 than in 2020, which somewhat follows the pattern spotted for the total non-current assets. This is a good sign, but the tendency is not so straightforward as it would have been more logical to witness a non-ambivalent pattern of development. The next analysis applied to the case of Philip Morris is the vertical one, which is presented in Table 9.

Table 9, Philip Morris - vertical analysis of assets

	2020	2021	2022
Cash	16.26%	10.90%	5.22%
Account Receivable	8.39%	9.54%	7.71%
Inventory	21.40%	21.14%	16.03%
Other Assets	1.91%	1.35%	2.85%
Total Current Assets	**47.96%**	**42.91%**	**31.81%**
Net Property	15.76%	16.21%	11.84%
Total Investments	10.72%	10.86%	7.74%
Intangible Assets	17.81%	23.00%	42.78%
Total Non-Current Assets	**52.04%**	**57.09%**	**68.19%**
Total Assets	**100.00%**	**100.00%**	**100.00%**

Source: analytical contribution based on annual statements

The share of cash was enormous in 2020, but it soon changed as the company entered the recovery stage from the pandemic, where there was a tactic of gradually decreasing the share of cash in the total value of assets, which is pretty common because the cash itself cannot generate any revenue, unlikely inventories. Receivables do not have a really high share as they fluctuate between 7.71%, which was identified in 2022 and 9.54%, identified in the year earlier, 2021. However, the analyzed company does follow something quite common for manufacturing organizations since the share of inventories in the total value of assets is quite high – well above 20% in 2020 and 2021, but then diminished to 16.03%, which might potentially be related to changes in the inventory management or changing demand for the products. Overall, the total current assets account for less than 50% in every single year: 47.96% in 2020, 42.91% in 2021 and 31.81% in 2022. The tendency of loosening the grip that the current assets have on the total value of assets is pretty visible, which is likely to be tied to the fact that the company was able to promptly initiate the recovery from the pandemic.

When it comes to long-term assets, the majority of them do remain on the level somewhat close to 10%, notably the net property element and the total investments, but the prevalence of the intangible assets element is pretty obvious, so it is vital to highlight the findings by saying that the company is explicitly focused on patents and intellectual property, which largely contributed to the fact that the company has more long-term assets than short-term ones – 52.04% in 2020, 57.09% in 2021 and 68.19% in 2022. The next step is dedicated to the analysis of the company's liabilities and equity, where all the required information is demonstrated in Table 10.

Table 10, Philip Morris' liabilities and equity

	2020	2021	2022
ST Debt	$ 3,558	$ 3,215	$ 8,248
Payables	$ 2,780	$ 3,331	$ 4,076
Income Tax	$ 1,091	$ 1,025	$ 1,040
Other Current	$ 12,186	$ 11,684	$ 13,972
Total Current Liabilities	**$ 19,615**	**$ 19,255**	**$ 27,336**
LT Debt	$ 28,685	$ 25,127	$ 35,311
Provision for Risks	$ 4,470	$ 2,968	$ 1,984
Other Liabilities	$ 1,992	$ 1,422	$ 1,405
Total Non-Current Liabilities	**$ 35,831**	**$ 30,243**	**$ 40,656**
Total Liabilities	**$ 55,446**	**$ 49,498**	**$ 67,992**
Paid-In Capital	$ 2,105	$ 2,225	$ 2,230
Retained Earnings	$ 31,638	$ 33,082	$ 34,289
Treasury Stock	$ -35,129	$ -35,836	$ -35,917
Total Equity	**$ -10,631**	**$ -8,208**	**$ -6,311**
Total Liabilities and Equity	**$ 44,815**	**$ 41,290**	**$ 61,681**

Source: analytical contribution based on annual statements

The situation at the first glance of the company is not so good, especially when seeing the negative sign for the total equity that indicates that the value of liabilities prevails over the value of assets, and this cannot anyhow be considered as a positive sign. Nevertheless, a more comprehensive overview can only be made possible through the utilization of both horizontal and vertical techniques, where the first one is presented in Table 11.

Table 11, Philip Morris - horizontal analysis of liabilities and equity

	2021	2022
ST Debt	-9.64%	131.82%
Payables	19.82%	46.62%
Income Tax	-6.05%	-4.67%
Other Current	-4.12%	14.66%
Total Current Liabilities	**-1.84%**	**39.36%**
LT Debt	-12.40%	23.10%
Provision for Risks	-33.60%	-55.62%
Other Liabilities	-28.61%	-29.47%
Total Non-Current Liabilities	**-15.60%**	**13.47%**
Total Liabilities	**-10.73%**	**22.63%**
Paid-In Capital	5.70%	5.94%
Retained Earnings	4.56%	8.38%
Treasury Stock	-2.01%	-2.24%
Total Equity	**22.79%**	**40.64%**
Total Liabilities and Equity	**-7.87%**	**37.63%**

Source: analytical contribution based on annual statements

There was first a sharp decrease in the value of the short-term obligations in 2021 in the magnitude of 9.64%, but it soon turned out to become a 131.82% increase in 2022 compared to the base year. Presumably, the company faced some operational problems and had to borrow huge amounts in order to quickly tackle the encountered problems. The value of payables increased first by 19.82% in 2021 and then by 46.62% in 2022, but this is a pretty normal situation for a company specializing in the retail industry. The income tax was decreasing in both 2021 and 2022 compared to 2020, which might indicate that the total revenue in those years was slightly lower than in 2020. Overall, the total value of the current liabilities decreased by 1.84% in 2021, but then rose by 39.36% in 2022, which is not a good sign indicating that the company was keen on indebting oneself more and more.

Continuing with the long-term debt, the situation is quite similar to the one observed for the short-term debt – there was a decrease in 2021 by 12.4%, but then there was a quick increase by 23.10% in 2022 compared to 2020. This is a sign that the company was potentially focused on the expansion of its business overseas by carrying specific capital projects forward. Overall, the total value of the long-term assets decreased 10.73% in 2021 but then rose by 13.47% compared to 2020, which is an indicator that the company was quickly borrowing and did not plan to stop with this particular tendency, which might potentially have its implications on its solvency and stability.

When it comes to the equity section of the balance sheet, these elements all experienced an increase apart from the treasury stock. Thanks to the efforts of the company, there was a visible progress that resulted in the increase in the total value of equity by 22.79% in 2021, which was then followed by an increase of 40.64% in 2022, compared to 2020, which cannot be treated in any other way apart from the positive one.

Table 12, Philip Morris - vertical analysis of liabilities and equity

	2020	2021	2022
ST Debt	7.94%	7.79%	13.37%
Payables	6.20%	8.07%	6.61%
Income Tax	2.43%	2.48%	1.69%
Other Current	27.19%	28.30%	22.65%
Total Current Liabilities	**43.77%**	**46.63%**	**44.32%**
LT Debt	64.01%	60.85%	57.25%
Provision for Risks	9.97%	7.19%	3.22%
Other Liabilities	4.44%	3.44%	2.28%
Total Non-Current Liabilities	**79.95%**	**73.25%**	**65.91%**
Total Liabilities	**123.72%**	**119.88%**	**110.23%**

Source: analytical contribution based on annual statements

According to the vertical analysis of Philip Morris' liabilities and equity accounts, it is possible to suggest that the share of liabilities was increasing quite quickly, especially the short-term ones, which make up for nearly 50% in 2020-2022 and this is definitely not a good sign indicating an excessive degree of indebtedness. On the other hand, the situation with the non-current liabilities is not significantly better because the long-term debt takes a very huge proportion exceeding 60% in 2020 and 2021 and being slightly lower the level of 60% in 2020. Overall, the situation with the company's solvency is really concerning since the liabilities account for more than 100% of the total liabilities and equity. However, there is a sign of an improvement since the share is constantly dropping – from 123.72% in 2020 to 110.23% in 2022. If the company will continue at the same pace, there are chanced that this burden will eventually be taken care of.

4.2.3 British American Tobacco

The very final company to be addressed in the subchapter dedicated to the financial position is British American Tobacco, whose reported assets for the time period between 2020 and 2022 are reported in Table 13.

Table 13, British American Tobacco's assets

	2020		2021		2022	
Cash	$	3,139	$	2,809	$	3,446
Account Receivable	$	3,800	$	4,068	$	3,446
Bad Debt	$	-41	$	-37	$	-51
Inventory	$	5,998	$	5,279	$	5,671
Other Assets	$	433	$	195	$	1,197
Total Current Assets	**$**	**13,612**	**$**	**12,807**	**$**	**15,409**
Net Property	$	5,060	$	4,953	$	4,867
Accumulated Depreciation	$	4,044	$	4,018	$	4,639
Total Investments	$	2,185	$	2,241	$	2,272
Intangible Assets	$	115,343	$	115,625	$	129,075
Total Non-Current Assets	**$**	**124,078**	**$**	**124,558**	**$**	**138,137**
Total Assets	**$**	**137,690**	**$**	**137,365**	**$**	**153,546**

Source: analytical contribution based on annual statements

The analysis of the third company follows the same logic as the one implemented for the previous two and the elements are reported in millions of US dollars for all elements of the company's balance sheet – just as it was the case for Philip Morris. In this case, it is pretty apparent that the company experienced a period of stagnation in 2021, when the majority of accounts experienced just a slight increase compared to the figures of 2020, which is pretty understandable given the presence of high degree of uncertainty and the pandemic. The horizontal analysis is reported in Table 14.

Table 14, British American Tobacco - horizontal analysis of assets

	2021	2022
Cash	-10.51%	9.78%
Account Receivable	7.05%	-9.32%
Bad Debt	9.76%	-24.39%
Inventory	-11.99%	-5.45%
Other Assets	-54.97%	176.44%
Total Current Assets	**-5.91%**	**13.20%**
Net Property	-2.11%	-3.81%
Accumulated Depreciation	-0.64%	14.71%
Total Investments	2.56%	3.98%
Intangible Assets	0.24%	11.91%
Total Non-Current Assets	**0.39%**	**11.33%**
Total Assets	**-0.24%**	**11.52%**

Source: analytical contribution based on annual statements

Indeed, the company visibly experienced a considerable number of problems in 2021. First, the value of the cash account dropped by approximately 10.51%, which is itself not a bad thing, but it just indicates the start of the recovery process from the pandemic, when the cash was converted to other assets. In 2022, the company reached the figures for the account 9.78% higher than in 2020, which is quite a good sign.

The situation with receivables is quite identical to the two previously addressed companies but instead of facing a logical increase in 2022, the company experienced a sharp decrease in the net receivables. When looking at the doubtful accounts, it becomes pretty apparent that this situation is presumably mainly influenced by the fact that the temporary adjusted significantly diminished the total figure for the account. This is a good sign, and the situation is quite similar to the first company that was not also managing to come to grips with its doubtful accounts.

Furthermore, the situation with inventories is quite concerning – there was a decrease in both 2021 and 2022, when the first one accounted for almost 12% and the second one is 5.45%. This can be a sign of a potential change in the inventory management system, or it simply indicates that the number of sales dropped, so there was no such need for having too much of inventories. The situation with other assets that traditionally incorporate prepaid expenses is quite drastic – there was a quick decrease in 2021, but then in 2022 the value of those accounts exceeded the original figures of 2020 by almost 2 times. Overall, the total current assets first decreased by 5.91% during 2021 but then the value rose by 13.25% compared to 2020, which is quite good, but the magnitude is not really large.

The net property decreased in both 2021 and 2022, but the decrease was not really large, so it might potentially be influenced by the ongoing depreciation of fixed long-term tangible assets. In 2021, the decrease accounted for 2.11% and in 2022, it accounted for 3.81%. On the contrary, the accumulated depreciation dropped by 0.64% in 2021, which might be explained by the fact that some old assets were written off, but it soon rose by 14.71% in 2022 compared to 2020. This might be one of the main reasons for the degrowth of the net property of the company, or it was simply reluctant to carry any long-term projects.

The total investments rose, but the magnitude was rather modest – just 2.56% in 2021 compared to 2020 and 3.98% in 2022 compared to 2020. The same could have been said about intangible assets of the company, but the increase in the value in 2022 was rather large – 11.91% compared to 2020. Overall, the increase in the total value of long-term assets was much smaller than the one identified for liquid assets – just 11.33% in 2022 compared to 2020. Quite similar numbers are encountered when looking at the total assets, where there was first a decrease of 0.24% in 2021 and then an increase of 11.52% in 2022, which indicates a positive dynamic for the company, but it is also vital to anticipate that both debt and equity accounts have increased by similar percentages. The next step is the vertical analysis, whose results are presented in Table 15.

Table 15, British American Tobacco – vertical analysis of assets

	2020	2021	2022
Cash	2.28%	2.04%	2.24%
Account Receivable	2.76%	2.96%	2.24%
Inventory	4.36%	3.84%	3.69%
Other Assets	0.31%	0.14%	0.78%
Total Current Assets	**9.89%**	**9.32%**	**10.04%**
Net Property	3.67%	3.61%	3.17%
Total Investments	1.59%	1.63%	1.48%
Intangible Assets	83.77%	84.17%	84.06%
Total Non-Current Assets	**90.11%**	**90.68%**	**89.96%**
Total Assets	**100.00%**	**100.00%**	**100.00%**

Source: analytical contribution based on annual statements

As a matter of the fact, the shares of liquid assets are quite inconsiderable, especially when noticing that the entirety of total current assets account for approximately 10% or even lower, such was the case for 2020 and 2021. On the other hand, the company is also strongly relying on its intangible assets which represent approximately 80% of the total assets of the company. Overall, there is a split of 10 to 90 per cent in assets, which itself is not bad, but the company might potentially be subject to problems with liquidity to its very large emphasis on the long-term section of assets. Now, it is the time to present the liabilities and equity section that is presented in Table 16.

Table 16, British American Tobacco – liabilities and equity

	2020	2021	2022
ST Debt	$ 3,542	$ 3,532	$ 142
Payables	$ 3,722	$ 3,923	$ 4,055
Income Tax	$ 868	$ 879	$ 1,049
Other Current	$ 7,346	$ 6,810	$ 12,607
Total Current Liabilities	**$ 15,478**	**$ 15,144**	**$ 17,853**
LT Debt	$ 39,927	$ 35,666	$ 38,726
Provision for Risks	$ 1,911	$ 1,631	$ 1,383
Other Liabilities	$ 1,105	$ 1,061	$ 1,446
Total Non-Current Liabilities	**$ 59,257**	**$ 54,820**	**$ 59,983**
Total Liabilities	**$ 74,735**	**$ 69,964**	**$ 77,836**
Paid-In Capital	$ 103	$ 107	$ 113
Retained Earnings	$ 73,605	$ 75,748	$ 77,611
Treasury Stock	$ -5,150	$ -5,122	$ -7,116
Total Equity	**$ 62,955**	**$ 67,401**	**$ 75,710**
Total Liabilities and Equity	**$ 137,690**	**$ 137,365**	**$ 153,546**

Source: analytical contribution based on annual statements

Seemingly, the situation of British American Tobacco is much better than the situation of the earlier analyzed company – Philip Morris, notably due to the fact that the value of liabilities does not prevail over assets. This observation is explained by the fact that the value of equity is not negative. Nevertheless, it is important to apply the same framework once more with the horizontal analysis presented in Table 17.

Table 17, British American Tobacco – horizontal analysis of liabilities and equity

	2021	2022
ST Debt	-0.28%	-95.99%
Payables	5.40%	8.95%
Income Tax	1.27%	20.85%
Other Current	-7.30%	71.62%
Total Current Liabilities	**-2.16%**	**15.34%**
LT Debt	-10.67%	-3.01%
Provision for Risks	-14.65%	-27.63%
Other Liabilities	-3.98%	30.86%
Total Non-Current Liabilities	**-7.49%**	**1.23%**
Total Liabilities	**-6.38%**	**4.15%**
Paid-In Capital	3.88%	9.71%
Retained Earnings	2.91%	5.44%
Treasury Stock	0.54%	-38.17%
Total Equity	**7.06%**	**20.26%**
Total Liabilities and Equity	**-0.24%**	**11.52%**

Source: analytical contribution based on annual statements

The dynamic of the company's financing is quite good, especially when looking at the situation with the short-term debt. First, it decreased by just a minor percentage in 2021 – 0.28%, but then it decreased by almost twice in 2022 compared to 2020 – 95.99%. This is quite a good result that must have certainly had a good impact on both liquidity and solvency. Payables increased, but the increase was not really high, which might be explained in two ways – it is either the company was able to fix prices with suppliers prior to the increase in sales or the increase in sales was not really high, so the company did not really face considerable expenses.

The income tax rose by significant figures, which almost certainly means that the company started to make much more profit, or it is just the tax policy that changed, which is quite unlikely – will be addressed in more detail during the analysis of the financial position of the company. All in all, the value of total current liabilities decreased by 2.16% in 2021, but then rose by 15.34% in 2022, compared to the base year of 2020. This is not a bad sign, but this will definitely have its implications on the liquidity of the company.

Long-term debt of the company decreased by 10.67%, which might be either explained by the reluctance of the company to venture into any new capital projects or by the company quickly paying off its outstanding debts, such as mortgages. The value increased a bit in 2022, but it was still 3.01% less than in 2020. Overall, the magnitude of the change in the total long-term liabilities is quite unusual, since there was first a drop of 7.49% in 2021 and then an increase equal to 1.23% in 2022, compared to 2020.

Finally, the equity accounts of the company experienced a very obvious increase, especially the value of retained earnings and paid-in capital. Furthermore, these changes in equity resulted in 7.06% in 2021 compared to 2020 and then by 20.26% in 2022 compared to 2020, which is quite a good result that must have almost certainly improved the situation with solvency of the company. The very last piece of analysis applied to balance sheets is the vertical one for British American Tobacco that is presented in Table 18.

Table 18, British American Tobacco – vertical analysis of liabilities and equity

	2020	2021	2022
ST Debt	2.57%	2.57%	0.09%
Payables	2.70%	2.86%	2.64%
Income Tax	0.63%	0.64%	0.68%
Other Current	5.34%	4.96%	8.21%
Total Current Liabilities	**11.24%**	**11.02%**	**11.63%**
LT Debt	29.00%	25.96%	25.22%
Provision for Risks	1.39%	1.19%	0.90%
Other Liabilities	0.80%	0.77%	0.94%
Total Non-Current Liabilities	**43.04%**	**39.91%**	**39.07%**
Total Liabilities	**54.28%**	**50.93%**	**50.69%**
Paid-In Capital	**0.07%**	**0.08%**	**0.07%**
Retained Earnings	**53.46%**	**55.14%**	**50.55%**
Treasury Stock	**-3.74%**	**-3.73%**	**-4.63%**
Total Equity	**45.72%**	**49.07%**	**49.31%**
Total Liabilities and Equity	**100.00%**	**100.00%**	**100.00%**

Source: analytical contribution based on annual statements

The vertical analysis reveals that the company is mainly concentrated on the debt financing, but the tendency is rapidly changing and in 2023, it is quite likely that the share of equity will prevail over debt. When it comes to liabilities, the company is mainly concerned with long-term debt, which has the share of 40%, whilst the short-term ones make up just a small portion approximately equal to 10%.

4.3 Analysis of Financial Performance

4.3.1 Japan Tobacco International

After finishing with the analysis of the financial position of each company, it is time to proceed to another crucial indicator – financial performance. For evaluating the performance with regard to this domain, the income statement is the financial statement that is usually scrutinized. The overview of income statements of Japan Tobacco International is presented in Table 19.

Table 19, Japan Tobacco International – income statement

	2020	2021	2022
Sales/Revenue	¥ 2,092,561	¥ 2,324,838	¥ 2,657,832
COGS	¥ 1,001,667	¥ 1,065,824	¥ 1,205,247
Gross Income	**¥ 1,090,894**	**¥ 1,259,014**	**¥ 1,452,585**
SG&A Expense	¥ 658,221	¥ 718,282	¥ 791,001
EBIT	**¥ 432,673**	**¥ 540,732**	**¥ 661,584**
Unusual Expense	¥ 10,552	¥ 51,191	¥ 31,054
Non Operating Income/Expense	¥ 10,870	-¥ 5,845	-¥ 33,754
Non Operating Interest Income	¥ 6,389	¥ 12,435	¥ 25,016
Interest Expense	¥ 23,360	¥ 27,738	¥ 36,351
EBT	**¥ 420,063**	**¥ 468,393**	**¥ 585,441**
Income Tax	¥ 108,034	¥ 132,208	¥ 149,277
Net Income	**¥ 310,254**	**¥ 338,490**	**¥ 442,716**
EPS	¥ 175	¥ 191	¥ 249

Source: analytical contribution based on annual statements

The income statements of Japan Tobacco International are once again reported in special monetary unit – Japanese Yen. However, this does not stop from suggesting that the company's financial performance is quite good – the company was making net income for every single year. Yet, whether this net income was increasing proportionally to the company's revenue or not can be revealed with the help of both horizontal and vertical analyses of the income statements. First, the horizontal analysis is conducted, which is presented in Table 20.

Table 20, Japan Tobacco International – horizontal analysis of income statement

	2021	2022
Sales/Revenue	11.10%	27.01%
COGS	6.41%	20.32%
Gross Income	**15.41%**	**33.16%**
SG&A Expense	9.12%	20.17%
EBIT	**24.97%**	**52.91%**
Unusual Expense	385.13%	194.29%
Non Operating Income/Expense	-153.77%	-410.52%
Non Operating Interest Income	94.63%	291.55%
Interest Expense	18.74%	55.61%
EBT	**11.51%**	**39.37%**
Income Tax	22.38%	38.18%
Net Income	**9.10%**	**42.69%**
EPS	9.08%	42.64%

Source: analytical contribution based on annual statements

First, the company's total value of sales increased in 2021 by 11.1%, and the increase continued in 2022, when the increase compared to 2020 accounted for 27.01%, which is a very decent result indicating that the company was constantly keen on increasing its sales. Furthermore, the percentual increase in the costs of goods sold account in both 2021 and 2022 is slightly lower than the percentual increase in sales, which indicates that the gross income of the company increased, as well as the gross margin.

On the other hand, it is quite logical to anticipate that the total value of operating expenses increased as well, which is indeed the case of Japan Tobacco International – 9.12% increase in 2021 and 20.17% increase in 2022. As a whole, it did not stop the EBIT from increasing first by 24.97% in 2021 and then by 52.91% in 2022. The company's non-operating section is explained by rapid changes, especially in the value of the non-operating interest income and unusual expense, which is quite anticipated due to a very unstable international business environment that had not been fully able to recover after the pandemic of COVID-19.

The EBT of the company rose first by 11.51% in 2021 and then by 39.37% in 2022, which is also a positive dynamic. Following the increase in the value of the EBT, it is logical to anticipate an increase in the income tax, which was the case – 22.38% in 2021 and then the increase of 38.18% in 2022, which is quite a normal situation. Finally, the net income of Japan Tobacco International increased by 9.1% in 2021 and by 42.69% in 2022, compared to 2020 with almost identical percentual increase identified for the EPS element. On the surface, the situation seems downright favorable, but it is still vital to continue to the vertical analysis of the income statement that will provide more information in the context. This analysis is presented in Table 21.

Table 21, Japan Tobacco International – vertical analysis of income statement

	2020	2021	2022
Gross Margin	52.13%	54.15%	54.65%
EBIT Margin	20.68%	23.26%	24.89%
EBT Margin	20.07%	20.15%	22.03%
Net Margin	14.83%	14.56%	16.66%

Source: analytical contribution based on annual statements

The gross margin, as it was already mentioned earlier, increased, which is a good sign, but the magnitude of the increase was not high – just 2-3 per cent. Yet, the company had already had quite high figures for the gross margin, so it is not surprising that the company faces difficulties with increasing this indicator. The EBIT margin did also increase by quite similar magnitude as the gross margin, which is a good result. The same applies to the EBT margin, which is also on a very decent level of approximately 20%. Finally, positive changes in the previous profitability margins impacted the net margin, which also rose from 14.56% in 2021 to 16.66% in 2022. The profitability of the company seems to lie on a very solid level.

4.3.2 Philip Morris

The next company on the list of Philip Morris, whose income statements for the same time period in million US dollars is presented in Table 22.

Table 22, Philip Morris – income statement

	2020	2021	2022
Sales/Revenue	$ 28,697	$ 31,346	$ 31,529
COGS	$ 9,649	$ 10,126	$ 11,402
Gross Income	**$ 19,048**	**$ 21,220**	**$ 20,127**
SG&A Expense	$ 6,984	$ 8,248	$ 7,776
EBIT	**$ 12,064**	**$ 12,972**	**$ 12,351**
Unusual Expense	$ 252	$ -205	$ -41
Non Operating Income/Expense	$ 13	$ -118	$ 33
Non Operating Interest Income	$ 110	$ 109	$ 180
Interest Expense	$ 982	$ 936	$ 971
EBT	**$ 10,953**	**$ 12,232**	**$ 11,634**
Income Tax	$ 2,377	$ 2,671	$ 2,244
Net Income	**$ 8,036**	**$ 9,083**	**$ 9,024**
EPS	$ 5.16	$ 5.83	$ 5.81

Source: analytical contribution based on annual statements

The second company, despite obviously facing a series of difficulties with solvency, is doing quite good from the point of view of financial performance. The net income is also positive, and it visibly increased from the yar 2020, but not by a significant amount. Nevertheless, the horizontal technique of analysis is applied once more with the output presented in Table 23.

Table 23, Philip Morris – horizontal analysis of income statement

	2021	2022
Sales/Revenue	9.23%	9.87%
COGS	4.94%	18.17%
Gross Income	**11.40%**	**5.66%**
SG&A Expense	18.10%	11.34%
EBIT	**7.53%**	**2.38%**
Unusual Expense	-181.35%	-116.27%
Non Operating Income/Expense	-1007.69%	153.85%
Non Operating Interest Income	-0.91%	63.64%
Interest Expense	-4.68%	-1.12%
EBT	**11.68%**	**6.22%**
Income Tax	12.37%	-5.60%
Net Income	**13.03%**	**12.29%**
EPS	12.98%	12.60%

Source: analytical contribution based on annual statements

The company's revenue first increased by 9.23% in 2021, but this increase did not go any further as in 2022, the level of revenue remained on quite the same level as in 2021 with just a minor inconsiderable increase. When it comes to the cost of goods sold, it is not possible to say the same about the company since the element rose quite quickly in 2022 and almost certainly took a serious toll on the company's profitability and decreased the gross margin. In fact, the percentual differences of the gross income confirm that the gross margin decreased in 2022, when the profitability of the company took a blow after being unable to increase the level of revenue.

The operating expenses of Philip Morris rose quite drastically – 18.1% increase in 2021, which was then decreased and the value of operating expenses in 2022 was 11.34% higher than in the base year of 2020. The situation with non-operating income of the company was not stable at all, especially with the non-operating income and unusual expense. EBIT did diminish, but the EBT in fact experienced a more vivid increase in 2021 – 11.68% and a higher increase in 2022, which was equal to 6.22% compared to 2020. The income tax of the company did fall by 5% in 2022, which might indicate that the net income of the company has fallen by quite the same amount. In fact, the company did go through a positive period in 2021, when the net income increased by 13.03%, but there was no further movement and the company did even experience a partial degrowth – 12.29% in 2022 compared to 2020, which is an indicator of a stagnation in 2022. The next step is the vertical analysis, which is presented in Table 24.

Table 24, Philip Morris – vertical analysis of income statement

	2020	2021	2022
Gross Margin	66.38%	67.70%	63.84%
EBIT Margin	42.04%	41.38%	39.17%
EBT Margin	38.17%	39.02%	36.90%
Net Margin	28.00%	28.98%	28.62%

Source: analytical contribution based on annual statements

As it was assumed earlier, there is an evident problem in 2022 – the gross margin did decrease, but the situation with the EBIT margin started to get worse already in 2021, so it is possible to highlight that year as the one when the problems occurred. Despite this, the

EBT margin did increase in 2021, but it did soon diminish in 2022, which led to the situation with the drop in the overall net margin in 2022. However, the net margin of the company is high enough, especially when comparing it with Japan Tobacco International, which is a sign that Philip Morris is much more successful when it comes to turning revenue into profit.

4.3.3 British American Tobacco

The final company whose financial performance is addressed is British American Tobacco, whose income statements for the period between 2020 and 2022 is presented in Table 25.

Table 25, British American Tobacco – income statement

	2020	2021	2022
Sales/Revenue	$ 25,760	$ 25,713	$ 27,671
COGS	$ 7,644	$ 7,894	$ 8,270
Gross Income	**$ 18,116**	**$ 17,819**	**$ 19,401**
SG&A Expense	$ 6,950	$ 6,957	$ 8,217
EBIT	**$ 11,354**	**$ 11,058**	**$ 11,906**
Unusual Expense	$ 1,358	$ 754	$ 858
Non Operating Income/Expense	$ -175	$ -98	$ -610
Non Operating Interest Income	$ 50	$ 35	$ 92
Interest Expense	$ 1,654	$ 1,493	$ 1,648
EBT	**$ 8,217**	**$ 8,748**	**$ 8,882**
Income Tax	$ 2,108	$ 2,189	$ 2,478
Net Income	**$ 6,400**	**$ 6,789**	**$ 6,617**
EPS	$ 2.80	$ 2.97	$ 2.93

Source: analytical contribution based on annual statements

The third company does also experience a positive net income, which is a sign of good financial performance. Also, the company does seem to have experienced considerable problems in 2021 but managed to recover quite soon. Nevertheless, a more comprehensive overview can be concluded based on the horizontal analysis presented in Table 26.

Table 26, British American Tobacco – horizontal analysis of income statement

	2021	2022
Sales/Revenue	-0.18%	7.42%
COGS	3.27%	8.19%
Gross Income	**-1.64%**	**7.09%**
SG&A Expense	0.10%	18.23%
EBIT	**-2.61%**	**4.86%**
Unusual Expense	-44.48%	-36.82%
Non Operating Income/Expense	44.00%	-248.57%
Non Operating Interest Income	-30.00%	84.00%
Interest Expense	-9.73%	-0.36%
EBT	**6.46%**	**8.09%**
Income Tax	3.84%	17.55%
Net Income	**6.08%**	**3.39%**
EPS	6.07%	4.64%

Source: analytical contribution based on annual statements

The company's revenue did in fact experience a drop in 2021, but the magnitude of this drop was not really huge – just 0.18%, but the company quickly recovered in 2022 reaching a 7.42% increase compared to the base year of 2020. The company becomes the first one to have experienced a drop in the value of gross income because of the 1.64% decrease in 2021 compared to 2020. However, this was overcome in 2022 when the company achieved an increase in the gross income equal to 7.09% of the value in 2020. The drop in the gross income is largely attributed to the increase in the value of COGS which was not accompanied by any increase in the value of sales.

Operating expenses of the firm were rapidly rising – first by 0.10% in 2021 and then by 18.23% in 2022, which is quite normal considering that the world entered into the stage of high inflation in 2022. This resulted in a drop in the value of EBIT in 2021 equal to 2.61%, but it was quickly overcome when the company achieved an increase in the value of EBIT equal to 4.86% in 2022 compared to 2020. Overall, there was a positive tendency in the value of the company's EBT, which first increased by 6.46% even despite the problem with the gross income and then by 8.09% in 2022, which both are decent results. Overall, the net income of the company in 2021 was still considerably higher than in 2022, when judging by the percentual changes. Overall, the company did experience a positive dynamic. Further insights can be drawn after looking at the vertical analysis of the income statement, which is presented in Table 27.

Table 27, British American Tobacco – vertical analysis of income statement

	2020	2021	2022
Gross Margin	70.33%	69.30%	70.11%
EBIT Margin	44.08%	43.01%	43.03%
EBT Margin	31.90%	34.02%	32.10%
Net Margin	24.84%	26.40%	23.91%

Source: analytical contribution based on annual statements

The company, when judging by figures in the vertical analysis, did experience problems in 2021 but only from the operating point of view. Despite the fact that there was a decrease in the gross margin which was astonishingly high – well above 70% for the most years, the company did manage to increase its EBT margin in 2021 and reach the highest level on the studied period. Presumably, this suggests that once the company understood that there are problems with the operating side of the business, they tried to rely on their non-operating sources of revenue. Nevertheless, the situation in 2022 became better from the operating point of view, but did also become considerably worse from the non-operating point of view, thus leading to the situation when the net margin reached the bottom on the analyzed time period equal to just 23.91%, which is indeed lower than for the previous years, but this is still a very good result.

4.4 Analysis of Cash-Flow

4.4.1 Japan Tobacco International

After addressing the first two important sides of the business, it is important to take a quick look at the changes in cash for each company. The first company whose statement of cash-flows is analyzed is Japan Tobacco International with the compilation presented in Table 28.

Table 28, Japan Tobacco International - cash-flow statement

	2020	2021	2022
Operating	519,833	598,909	483,799
Investing	2,339	-97,458	-101,796
Financing	-294,389	-353,179	-306,202

Source: analytical contribution based on annual statements

The first sequence of actions that is needed to be performed before applying the horizontal technique of analysis is the identification of the main tendencies and the overall picture based on the signs of each component. The operating cash-flow of the company was positive and increased in 2021, which is very good. It did decrease in 2022, but it still remained positive, so the situation with the operating cash-flow of the company is quite favorable.

The investing cash-flow is negative in 2021 and 2022, which indicates that the company resumed active participation in different investment projects and capital budgeting projects after the year 2020, when the company was reluctant to make any major investments due to the pandemic of COVID-19. The situation in 2020 was not so favorable, but it quickly changed in 2021 and 2022, so it is possible to indicate that the situation is quite favorable once more.

Finally, the negative sign of the financing cash-flow is absolute acceptable, especially when recalling the fact that the company is paying dividends and the yield is quite large – above 5%. Overall, the situation with cash-flows is positive. At last, the horizontal analysis is indicated and presented in Table 29.

Table 29, Japan Tobacco International – horizontal analysis of cash-flow statement

	2021	2022
Operating	15.21%	-6.93%
Investing	-4266.65%	-4452.12%
Financing	-19.97%	-4.01%

Source: analytical contribution based on annual statements

4.4.2 Philip Morris

The next company to be addressed from the cash-flow perspective is Philip Morris, whose cash-flow statements for the period between 2020 and 2022 are presented in Table 30.

Table 30, Philip Morris - cash-flow statement

	2020	2021	2022
Operating	**9,812**	**11,967**	**10,803**
Investing	**-1,930**	**-2,938**	**-18,028**
Financing	**-7,720**	**-11,397**	**6,155**

Source: analytical contribution based on annual statements

The operating cash-flow of the company is positive, which is quite good indicating that the company is pretty capable of sustaining its daily operations by the operating activity. The value of the operating cash-flow in 2021 and 2022 is higher than in 2020, which indicates the fact that the company managed to undergo through the pandemic in quite a solid way.

The investing cash-flow was negative all the way around, but the values are significantly different in 2022 and at the beginning of the studied period, which is inevitably associated with a higher degree of uncertainty back then caused by the pandemic of COVID-19.

The financing cash-flow is also negative for the most period, but it is mainly influenced by 2 factors. The first factor is identical as in the case of Japan International Tobacco – Philip Morris is a dividend-paying company whose dividend yield is higher than 5%, so it is quite common for such companies to have a negative financing cash-flow. Furthermore, the company was aiming at decreasing the dependence it had on the debt financing and the company was aiming at becoming more solvent in the long-term perspective, so this is pretty comprehensive. The horizontal analysis is presented in Table 31.

Table 31, Philip Morris – horizontal analysis of cash-flow statement

	2021	2022
Operating	**21.96%**	**10.10%**
Investing	**-52.23%**	**-834.09%**
Financing	**-47.63%**	**179.73%**

Source: analytical contribution based on annual statements

4.4.3 British American Tobacco

The final company is British American Tobacco, and its cash-flow can be found in Table 32.

Table 32, British American Tobacco - cash-flow statement

	2020	2021	2022
Operating	**8,097**	**8,271**	**8,901**
Investing	**-814**	**-1,172**	**-791**
Financing	**-6,177**	**-7,271**	**-7,299**

Source: analytical contribution based on annual statements

Quite similar situation is encountered for the case of the third company. The company does have an operating cash-flow, which indicates that it is capable of maintaining its expenses with the current level of operations, which is, undeniably, a good sign.

Furthermore, the investing section is negative, and the company did not really stop investing in 2020 as it had quite high figures back then. The fact that the company's investing cash-flow is negative indicates that it did have enough cash to do so, which is a good sign after all.

At last, the company is the highest dividend-yielding one out of the three, which is expressed by the annual dividend of approximately 9%, which is a very huge figure. Therefore, seeing a negative financing cash-flow is a pretty common situation indicating that the company is keen on paying its shareholders, which is a good sign as well.

4.5 Analysis of Financial Ratios

4.5.1 Japan Tobacco International

The final analytical tool implemented in the diploma thesis is the analysis of financial ratios, which is split into 5 different categories: liquidity, solvency, profitability, efficiency and market valuation. The complete overview of financial ratios is presented in Table 33.

Table 33, Japan Tobacco International - financial ratios

	2020	2021	2022
Current Ratio	1.51	1.55	1.74
Cash Ratio	0.41	0.48	0.55
Acid-Test Ratio	1.11	1.17	1.30
Return on Assets	0.06	0.06	0.07
Return on Equity	0.12	0.12	0.12
Debt to Equity	1.07	1.00	0.81
Debt to Assets	0.52	0.50	0.45
Interest Coverage Ratio	18.52	19.49	18.20
Equity	0.48	0.50	0.55
Payables Turnover	4.29	3.91	4.41
Receivables Turnover	4.90	4.89	5.32
Inventory Turnover	1.86	1.89	1.74
P/E Ratio	12	12.2	11.7
P/B Ratio	1.7	1.6	1.57

Source: analytical contribution based on annual statements

The company does not have any problem with liquidity: the current ratio of the company was always greater than 1 – 1.51 in 2020, 1.55 in 2021 and 1.74 in 2022. Furthermore, there is a clear upward tendency, which indicates that the company was constantly increasing its liquidity. The situation with the cash ratio is also favorable – there is not too much of cash and the volume of cash is quite favorable. Furthermore, once the inventory is subtracted, the company does not really experience any major problems with its liquidity because the acid-test ratio does also have numbers above 1. The situation of Japan Tobacco International with liquidity is quite favorable.

The profitability of the company is not enormous, just 0.06 for the return on assets and 0.12 for the return on equity. This is not high profitability, but it is also important to recall that the company had quite good profitability ratios that were discussed in one of earlier chapters. In total, the profitability of Japan Tobacco International is quite good even despite it not being rather large.

The situation with solvency was much worse at the beginning of the analyzed period, especially when taking the value of the debt-to-equity ratio into consideration due to the presence of a figure above 1 in the first and second studied years. On the other hand, there is no single case when the total debt would prevail over the value of assets, which is good. Furthermore, the interest coverage ratio does also indicate a positive dynamic, as well as the equity ratio. At the beginning, the company was mainly concerned with the debt financing, but then turned to the equity financing, which is a very good result.

The domain of efficiency indicates that the company on average pays its creditors 3.91-4.41 times per year, approximately totaling 90 days for the payment, which might indicate that this is a traditional outstanding time of invoices received by the company. When it comes to the debt collection, there is a similar tendency, but the company does collect debts slightly more frequent than pays – from 4.89 to 5.32 times per year. At last, the company does not replace its inventory quite frequently – just 1.74 – 1.89 times per year, which is a very surprising number, but might indicate a particular tendency in the tobacco industry if similar numbers will be encountered for the case of other companies.

At last, the P/E ratio indicates that investors need to pay 12 USD in 2020 to get 1 USD in earnings, 12.2 USD in 2021 to get 1 USD in earnings and 11.7 USD in 2022 to get 1 USD in earnings. Over time, there was a slight improvement in the situation with the ratio, but it is still quite low, which is good for potential investors. Finally, the P/B ratio is low, which states that the company is traded at the price exceeding its book value by 1.57-1.7 times, which is also quite low and good from the investment attractivity point of view.

4.5.2 Philip Morris

Financial ratios of Philip Morris are presented in Table 34.

Table 34, Philip Morris – financial ratios

	2020	2021	2022
Current Ratio	1.10	0.92	0.72
Cash Ratio	0.37	0.23	0.12
Acid-Test Ratio	0.61	0.47	0.36
Return on Assets	0.18	0.22	0.15
Return on Equity	-0.76	-1.11	-1.43
Debt to Equity	-5.22	-6.03	-10.77
Debt to Assets	1.24	1.20	1.10
Interest Coverage Ratio	12.29	13.86	12.72
Equity	-0.24	-0.20	-0.10
Payables Turnover	3.47	3.04	2.80
Receivables Turnover	7.63	7.96	6.63
Inventory Turnover	1.01	1.16	1.15
P/E Ratio	14.04	15.04	16.96
P/B Ratio	-10.63	-16.56	-24.2

Source: analytical contribution based on annual statements

The domain of liquidity indicates that there was a visible deterioration over time – the company started with a good liquidity, when the current ratio was 1.1 in 2020, but then the situation turned out to become worse after the current ratio dropped to 0.92 in 2021. Finally, the negative tendency continued in 2022, when the ratio became equal to 0.72 indicating a very concerning tendency. The same applies to other liquidity ratios, especially the acid-test ratio, which indicates that almost the half of the company's current assets are represented by inventories that cannot anyhow be sold due to their utilization in the production process. Overall, the situation of Philip Morris with liquidity is not good at all.

The situation with profitability is also not good, where the return on equity ratio returns a very high negative value, which is a consequence of the fact that the company's debts prevail over its assets. The figure for the return on assets is quite good – ranging from 0.15 and 0.22, which is a sign of a quite good profitability. However, the situation with the company's equity does significantly worsen the whole picture with the company's profitability.

Solvency ratios indicate a very concerning tendency in terms of all selected ratios. The debt-to-equity ratio is negative and kept decreasing on the studied time interval, which is a sign of the company becoming more and more indebted without any significant improvements in equity accounts. Debt-to-assets ratio does also indicate that the situation is not good since the value of debts prevail over the value of assets, but the company is approaching the moment when the tendency will be changed, which might take two more years at maximum. Interest coverage ratio is quite good, but it steadily decreases, which is not good. Equity ratio does indicate that the company's assets are fully funded with debt, which is not a good tendency especially when considering the degree to which the company is indebted.

Continuing to the payable's turnover, the company pays its creditors between 2.8 and 3.47 times per year, which is a bit less frequent than Japan Tobacco International, potentially meaning that the average time of outstanding invoices of Philip Morris is larger. Receivables turnover practically means that the company does collect its debts quite frequent – from 6.63 times per year to 7.96 times per year, which indicates a much stricter policy of debt management than the one identified for Japan Tobacco International. The situation with the inventory turnover does indicate that it is quite likely that all companies from the tobacco industry are keen on replacing their inventories just 1-2 times per year since the second company in the row does have a very low figures for the inventory turnover.

The P/E ratio does indicate that investors pay a larger sum of money to get 1 USD in earnings – between 14.04 USD and 16.96 USD. The situation with the P/B ratio is not good because it is negative, arising from the fact that the company's book value is negative because of the prevalence of liabilities over assets.

4.5.3 British American Tobacco

Table 35, British American Tobacco – financial ratios

	2020	2021	2022
Current Ratio	0.88	0.85	0.86
Cash Ratio	0.20	0.19	0.19
Acid-Test Ratio	0.49	0.50	0.55
Return on Assets	0.05	0.05	0.04
Return on Equity	0.10	0.10	0.09
Debt to Equity	1.19	1.04	1.03
Debt to Assets	0.54	0.51	0.51
Interest Coverage Ratio	6.86	7.41	7.22
Equity	0.46	0.49	0.49
Payables Turnover	2.05	2.01	2.04
Receivables Turnover	6.78	6.32	8.03
Inventory Turnover	1.27	1.50	1.46
P/E Ratio	31.14	33.6	32.51
P/B Ratio	1.68	1.5	1.58

Source: analytical contribution based on annual statements

The company just as the previously discussed one, does suffer from not very favorable situation with liquidity due to the fact that the current ratio is below 1 for all studied years – 0.88 in 2020, 0.85 in 2021 and 0.86 in 2022. This is not good and there is no substantial progress made in that frontier since there was no improvement so far. Cash ratio is quite low, but this is not critical, but what is quite critical is the fact that the acid-test ratio is extremely low – 0.49 in 2020, 0.50 in 2021 and 0.55 in 2022. However, there is a visible improvement with the last ratio, which is quite good. Overall, the company suffers from low liquidity.

When it comes to profitability, it is much better than the one identified for the case of Philip Morris because both ratios are positive. Yet, the figures are not really high, especially the one for the return on assets – just 4-5 per cent, which is not quite high. Yet, when recalling the company's margin ratios, it is possible to draw a conclusion that the company's profitability is quite favorable.

He company does not suffer from significant problems with its solvency, as it is revealed after looking at debt-to-equity and debt-to-assets. The first ratio is not perfect as the value is above 1, but the situation is rapidly improving. However, the second ratio indicates that the situation with indebtedness is under control because the debt does not prevail over assets. The interest coverage ratio has quite a good value as well. At last, the equity ratio indicates that the company is still focused on the debt financing, but there was a huge progress made in that frontier and it is likely that the company will mostly switch to the equity financing in the future.

Payables turnover indicates that the company pays its creditors just approximately two times per year, thus potentially resulting in the average time of an outstanding invoice equal to 180 days, which is pretty acceptable. Receivables turnover indicates that the company tends to collect its debts quite often – between 6.32 times per year and 8.03 times per year. The inventory turnover confirms that there is an evident tendency for tobacco companies not to replace its inventories quite often – just approximately 1-2 times per year.

The company is the least attractive one in terms of a potential investments made because the price that investors would pay to get 1 USD in earnings for British American Tobacco is higher than for other two companies. The P/B ratio is not high, which is a good aspect indicating that the company is not likely to be considerably overvalued.

5 Results and Discussion

5.1 Comparison of Financial Positions

To begin with, it is essential to summarize what has been achieved so far. It was identified that neither of the companies suffers from an extremely bad financial position, but there are certain peculiarities of all companies that are worth being noted. When it comes to Japan Tobacco International, the company seems to have the most balanced situation in terms of all domains – liquidity, solvency, profitability, activity and market valuation. Notably, there are no problems at all with liquidity and solvency, which are often treated as the main indicators associated with the financial position.

Contrary to Japan Tobacco International, Philip Morris does have considerable problems, notably with the degree of indebtedness. The company suffers from an uncommon situation for multinational companies with the value of liabilities exceeding the value of assets, which is a very negative situation. Furthermore, the company's liquidity is far from being perfect, especially when considering that a significant portion of current assets are represented by inventories that cannot be sold quickly due to the fact that the revenue and sales are generated from it.

Based on Tables 33, 34 and 35, British American Tobacco's situation is quite close to the situation of Japan Tobacco International, but its liquidity is slightly worse, as well as solvency. Finally, when comparing all companies, it is possible to draw the conclusion that the best financial position is identified for the case of Japan Tobacco International which confirms that the company has no problems with its accounts, while Philip Morris' situation is the least favorable with very huge dependency on the debt financing, whilst British American Tobacco has a somewhat moderately good situation with its financial position.

5.2 Comparison of Financial Performances

When it comes to financial performance, it is possible to highlight that all companies are quite profitable as they make the net profit on an annual basis, which is a very good sign. However, when looking at the figures of profitability, it is possible to indicate that the best-performing company is British American Tobacco that has the highest net margin, followed by Philip Morris and by Japan Tobacco International. Furthermore, it is important to indicate that Philip Morris suffers from the problem of static revenue and inability to significantly increase the income from operating activities, which is not good.

Overall, the companies remain quite profitable and successful on the studied time period with an evident leadership of British American Tobacco. However, it is important to mention that there is a big emphasis put by all companies on non-operating income and intangible assets, which might indicate that companies are keen on selling their licenses and specific patents, which is not something strongly anticipated in the tobacco industry.

5.3 Factors Affecting Profits

For sure, it is possible to draw a very important finding that for all tobacco companies studied in the diploma thesis, the non-operating income accounts for a relatively huge share of revenue. Furthermore, the companies' operating income seems to be in a serious stagnation that is likely to be associated with the tendency of governments all over the world to increase the value of the excise tax imposed on tobacco-related products. In addition to that, the rise of alternative vaping tools has created additional implications for tobacco companies that had to face a countless number of competitors.

The latter mentioned phenomenon has become quite common in the last years, which led to the fact that many smokers shifted to alternative smoking devices that promised to reduce the damage imposed on smokers' health thus leading to the fact that the companies had to invest huge amounts of money to develop their own products and open new subsidiaries. One of such examples is the line of heated tobacco – IQOS that was originally introduced by Philip Morris International – the company that was discussed in the diploma thesis. A higher degree of competition and lower barriers to entry led to a particular stagnation of revenue for the biggest international manufacturers of tobacco, which is an obvious downturn.

Henceforth, it is possible to distinguish two specific reasons – increase of the excise tax in the majority of countries on the governmental level and the growing competition arising from the entry of companies specializing in the heated tobacco and vaping that significant decreased the number of customers of tobacco-manufacturing companies.

5.4 Risks

When it comes to risk, there was already one specific risk mentioned – the threat of substitution, which is also mentioned by the three major companies in their annual reports. However, when taking into consideration the main motivation for writing the diploma and considering that the choice of the companies was made based on the Russian market, it is important to stress the risks that companies face once they will leave the Russian market once and for all.

Japan Tobacco International is the biggest company when it comes to its share in Russia and the company's profitability is not quite high by default, which is likely to become quite worse if the company will exclude itself from the market of approximately 75 million smokers. The same applies to both Philip Morris and British American Tobacco whose revenue was not increasing much in the last two years. In addition to that, the companies have just made it through the pandemic of COVID-19, as well as the companies today are facing countless competitors that have recently entered the market thanks to their vaping devices and heated tobacco.

Henceforth, leaving the Russian market entails a huge number of risks given the size of the market and the number of assets owned in the country, where there is a huge risk of the nationalization of the companies' assets once they will announce their decision to sell their businesses, which was already the case for Danone and Carlsberg in Russia. On the other hand, the companies can easily face reputational losses by refusing to leave the Russian market, but it is yet uncertain if smokers are quite sensitive to geopolitical tensions and they will abandon those companies. After all, the tobacco industry is not a very saturated one, where many brands are owned by just three companies – Japan Tobacco International, Philip Morris and British American Tobacco, so the main assumption is that there will be not much of reputational losses. The same cannot be said about the company's decision to part ways with the Russian market, which is likely to entail a lot of financial losses.

6 Conclusion

The diploma thesis titled “Financial Analysis and Assessment of the Companies Operating in the Tobacco Industry in the Russian Federation” was concerned with the analysis of financial performance, position, cash-flows and ratios of the three selected companies that almost entirely represent the Russian tobacco industry – Japan Tobacco International, Philip Morris International and British American Tobacco. Qualitative and quantitative methods were applied to identify the best-performing company and the company with the best financial position, to find out the main factors influencing the companies' profits and to evaluate the potential decision to part ways once and for all with the Russian market under the international pressure.

It is identified that Japan Tobacco International has the best financial position with outstanding liquidity and high solvency, while also having quite a decent level of valuation and profitability. The second-best company in terms of the financial position is British American Tobacco, while the absolute worst situation is identified in Philip Morris International, which has the value of liabilities significantly exceeding the value of assets. In addition to that, the company has significant problems with liquidity, but the situation is rapidly improving.

When it comes to the financial performance, the best-performing company is British American Tobacco whose net margin is quite high and significantly exceeds the net margins of other companies. The second best-performing company is Philip Morris, while the net margin of Japan Tobacco International is still positive but considerably lower than for other companies. Furthermore, all companies seem to suffer from static revenue with a huge emphasis being put on non-operating sources of income, which is not quite good. Overall, the situation is worsened by the presence of new entrants to the market that supply heated tobacco and vaping devices, thus leading to the situation when a lot of existing customers switched to “healthier” alternative thus hitting the biggest and oldest players in the market.

At last, the decision to leave the Russian market in 2023 is likely to generate a lot of damage to all three companies because excluding themselves from the market of approximately 75 million smokers can lead to the situation when the revenue will not just become static but will fall accordingly. It is still dubious of whether there will be any negative damage inflected from the reputational losses if they decide to remain in the Russian Federation's business environment.

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8 Appendices

Table 36, Japan Tobacco International - published income statement

(2) Consolidated Statement of Income and Consolidated Statement of Comprehensive Income

Consolidated Statement of Income

(Millions of yen)

	Year ended December 31, 2021	Year ended December 31, 2022
Revenue	2,324,838	2,657,832
Cost of sales	(956,861)	(1,090,989)
Gross profit	1,367,976	1,566,843
Other operating income	15,622	20,262
Share of profit in investments accounted for using the equity method	3,997	8,009
Selling, general and administrative expenses	(888,574)	(941,538)
Operating profit	499,021	653,575
Financial income	19,013	31,147
Financial costs	(45,645)	(91,272)
Profit before income taxes	472,390	593,450
Income taxes	(132,208)	(149,277)
Profit for the period	340,181	444,174
Attributable to:		
Owners of the parent company	338,490	442,716
Non-controlling interests	1,691	1,458
Profit for the period	340,181	444,174
Earnings per share		
Basic (Yen)	190.76	249.45
Diluted (Yen)	190.68	249.36

Source: Japan Tobacco International, 2023

Table 37, Japan Tobacco International - published assets

(Millions of yen)

	As of December 31, 2021	As of December 31, 2022
Assets		
Current assets		
Cash and cash equivalents	721,731	866,885
Trade and other receivables	456,587	477,239
Inventories	563,182	691,906
Other financial assets	17,254	37,677
Other current assets	562,034	649,181
Subtotal	2,320,789	2,722,889
Assets held for sale	500	702
Total current assets	2,321,289	2,723,591
Non-current assets		
Property, plant and equipment	755,843	775,957
Goodwill	2,060,965	2,446,063
Intangible assets	307,152	246,442
Investment property	4,985	9,495
Retirement benefit assets	53,177	57,792
Investments accounted for using the equity method	41,721	56,943
Other financial assets	108,658	140,366
Deferred tax assets	120,419	91,430
Total non-current assets	3,452,920	3,824,487
Total assets	5,774,209	6,548,078

Source: Japan Tobacco International, 2023

Table 38, Japan Tobacco International - published liabilities and equity

(Millions of yen)

	As of December 31, 2021	As of December 31, 2022
Liabilities and equity		
Liabilities		
Current liabilities		
Trade and other payables	555,777	540,089
Bonds and borrowings	142,901	137,308
Income tax payables	30,794	37,470
Other financial liabilities	28,342	40,065
Provisions	24,858	26,610
Other current liabilities	717,653	781,093
Subtotal	1,500,326	1,562,635
Liabilities directly associated with assets held for sale	-	29
Total current liabilities	1,500,326	1,562,664
Non-current liabilities		
Bonds and borrowings	775,721	821,003
Other financial liabilities	43,885	41,735
Retirement benefit liabilities	296,176	244,116
Provisions	22,867	26,490
Other non-current liabilities	179,195	195,248
Deferred tax liabilities	69,959	40,061
Total non-current liabilities	1,387,803	1,368,653
Total liabilities	2,888,128	2,931,317
Equity		
Share capital	100,000	100,000
Capital surplus	736,400	736,400
Treasury shares	(490,899)	(490,183)
Other components of equity	(400,086)	104,309
Retained earnings	2,863,843	3,089,909
Equity attributable to owners of the parent company	2,809,258	3,540,435
Non-controlling interests	76,823	76,326
Total equity	2,886,081	3,616,761
Total liabilities and equity	5,774,209	6,548,078

Source: Japan Tobacco International, 2023

Table 39, Philip Morris - published income statement

Consolidated Statements of Earnings

(in millions of dollars, except per share data)

for the years ended December 31,	2022	2021	2020
Revenues including excise taxes (includes $8,269 in 2022, $7,822 in 2021 and $7,572 in 2020 from related parties)	**$ 80,669**	$ 82,223	$ 76,047
Excise taxes on products	**48,907**	50,818	47,353
Net revenues (includes $3,658 in 2022, $3,330 in 2021 and $3,233 in 2020 from related parties) (Note 18)	**31,762**	31,405	28,694
Cost of sales (Notes 4 & 5)	**11,402**	10,030	9,569
Gross profit	**20,360**	21,375	19,125
Marketing, administration and research costs (Notes 3, 4, 5, 13 & 20)	**8,114**	8,400	7,457
Operating income	**12,246**	12,975	11,668
Interest expense, net (Note 15)	**588**	628	618
Pension and other employee benefit costs (Note 14)	**24**	115	97
Earnings before income taxes	**11,634**	12,232	10,953
Provision for income taxes (Note 12)	**2,244**	2,671	2,377
Equity investments and securities (income)/loss, net	**(137)**	(149)	(16)
Net earnings	**9,527**	9,710	8,592
Net earnings attributable to noncontrolling interests	**479**	601	536
Net earnings attributable to PMI	**$ 9,048**	$ 9,109	$ 8,056
Per share data (Note 11):			
Basic earnings per share	**$ 5.82**	$ 5.83	$ 5.16
Diluted earnings per share	**$ 5.81**	$ 5.83	$ 5.16

Source: Philip Morris, 2023

Table 40, Philip Morris - published assets

Consolidated Balance Sheets
(in millions of dollars, except share data)

at December 31,		2022		2021
Assets				
Cash and cash equivalents	$	**3,207**	$	4,496
Trade receivables (less allowances of $42 in 2022 and $70 in 2021) (1)		**3,850**		3,123
Other receivables (less allowances of $32 in 2022 and $36 in 2021)		**906**		817
Inventories:				
Leaf tobacco		**1,674**		1,642
Other raw materials		**2,028**		1,652
Finished product		**6,184**		5,426
		9,886		8,720
Other current assets (Note 3)		**1,770**		561
Total current assets		**19,619**		17,717
Property, plant and equipment, at cost:				
Land and land improvements		**545**		565
Buildings and building equipment		**4,291**		4,293
Machinery and equipment		**9,549**		9,275
Construction in progress		**1,058**		599
		15,443		14,732
Less: accumulated depreciation		**8,733**		8,564
		6,710		6,168
Goodwill (Note 5)		**19,655**		6,680
Other intangible assets, net (Note 5)		**6,732**		2,818
Equity investments (Note 6)		**4,431**		4,463
Deferred income taxes		**603**		895
Other assets (less allowances of $20 in 2022 and $21 in 2021) (Note 3)		**3,931**		2,549
Total Assets	**$**	**61,681**	$	41,290

Source: Philip Morris, 2023

Table 41, Philip Morris - published liabilities and equity

at December 31,	2022	2021
Liabilities		
Short-term borrowings (Note 8)	**$ 5,637**	$ 225
Current portion of long-term debt (Note 8)	**2,611**	2,798
Accounts payable	**4,076**	3,331
Accrued liabilities:		
Marketing and selling	**695**	811
Taxes, except income taxes	**7,440**	6,324
Employment costs	**1,168**	1,146
Dividends payable	**1,990**	1,958
Other	**2,679**	1,637
Income taxes (Note 12)	**1,040**	1,025
Total current liabilities	**27,336**	19,255
Long-term debt (Note 8)	**34,875**	24,783
Deferred income taxes	**1,956**	726
Employment costs	**1,984**	2,968
Income taxes and other liabilities (Note 12)	**1,841**	1,766
Total liabilities	**67,992**	49,498
Contingencies (Note 18)		
Stockholders' (Deficit) Equity		
Common stock, no par value (2,109,316,331 shares issued in 2022 and 2021) (Note 9)	—	—
Additional paid-in capital	**2,230**	2,225
Earnings reinvested in the business	**34,289**	33,082
Accumulated other comprehensive losses (Note 17)	**(9,559)**	(9,577)
	26,960	25,730
Less: cost of repurchased stock (559,098,620 and 559,146,338 shares in 2022 and 2021, respectively)	**35,917**	35,836
Total PMI stockholders' deficit	**(8,957)**	(10,106)
Noncontrolling interests	**2,646**	1,898
Total stockholders' deficit	**(6,311)**	(8,208)
Total Liabilities and Stockholders' (Deficit) Equity	**$ 61,681**	$ 41,290

Source: Philip Morris, 2023

Table 42, British American Tobacco - published income statement

	Notes	2022 £m	2021 £m	2020 £m
		For the years ended 31 December		
Revenue[1]	2	**27,655**	25,684	25,776
Raw materials and consumables used		**(4,781)**	(4,542)	(4,583)
Changes in inventories of finished goods and work in progress		**227**	160	445
Employee benefit costs	3	**(2,972)**	(2,717)	(2,744)
Depreciation, amortisation and impairment costs	4	**(1,305)**	(1,076)	(1,450)
Other operating income	5	**722**	196	188
Loss on reclassification from amortised cost to fair value		**(5)**	(3)	(3)
Other operating expenses	6	**(9,018)**	(7,468)	(7,667)
Profit from operations	2	**10,523**	10,234	9,962
Net finance costs	8	**(1,641)**	(1,486)	(1,745)
Share of post-tax results of associates and joint ventures	2,9	**442**	415	455
Profit before taxation		**9,324**	9,163	8,672
Taxation on ordinary activities	10	**(2,478)**	(2,189)	(2,108)
Profit for the year		**6,846**	6,974	6,564
Attributable to:				
Owners of the parent		**6,666**	6,801	6,400
Non-controlling interests		**180**	173	164
		6,846	6,974	6,564
Earnings per share				
Basic	11	**293.3**	296.9	280.0
Diluted	11	**291.9**	295.6	278.9

Note:

Source: British American Tobacco, 2023

Table 43, British American Tobacco - published balance sheet

	Notes	2022 £m	2021 £m
		31 December	
Assets			
Intangible assets	12	**129,075**	115,625
Property, plant and equipment	13	**4,867**	4,953
Investments in associates and joint ventures	14	**2,020**	1,948
Retirement benefit assets	15	**1,000**	918
Deferred tax assets	16	**682**	611
Trade and other receivables	17	**241**	210
Investments held at fair value	18	**121**	50
Derivative financial instruments	19	**131**	243
Total non-current assets		**138,137**	124,558
Inventories	20	**5,671**	5,279
Income tax receivable		**149**	117
Trade and other receivables	17	**4,367**	3,951
Investments held at fair value	18	**579**	456
Derivative financial instruments	19	**430**	182
Cash and cash equivalents	21	**3,446**	2,809
		14,642	12,794
Assets classified as held-for-sale	27(d)	**767**	13
Total current assets		**15,409**	12,807
Total assets		**153,546**	137,365
Equity – capital and reserves			
Share capital	22(a)	**614**	614
Share premium, capital redemption and merger reserves	22(b)	**26,628**	26,622
Other reserves	22(c)	**2,655**	(6,032)
Retained earnings	22(c)	**44,081**	44,212
In respect of assets held-for-sale	22(c)	**(295)**	—
Owners of the parent		**73,683**	65,416
Perpetual hybrid bonds	22(d)	**1,685**	1,685
Non-controlling interests	22(e)	**342**	300
Total equity		**75,710**	67,401
Liabilities			
Borrowings	23	**38,726**	35,666
Retirement benefit liabilities	15	**949**	1,239
Deferred tax liabilities	16	**18,428**	16,462
Other provisions for liabilities	24	**434**	392
Trade and other payables	25	**944**	982
Derivative financial instruments	19	**502**	79
Total non-current liabilities		**59,983**	54,820
Borrowings	23	**4,413**	3,992
Income tax payable		**1,049**	879
Other provisions for liabilities	24	**1,087**	461
Trade and other payables	25	**10,449**	9,577
Derivative financial instruments	19	**427**	235
		17,425	15,144
Liabilities associated with assets classified as held-for-sale	27(d)	**428**	—
Total current liabilities		**17,853**	15,144
Total equity and liabilities		**153,546**	137,365

Source: British American Tobacco, 2023