

British American Tobacco Balance Sheet Up in Smoke



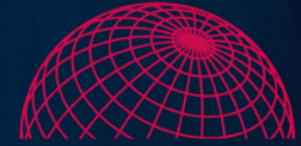
CASE STUDY
VALUATION MASTER CLASS

by
A. Stoltz INVESTMENT
RESEARCH



For over 100 years, British American Tobacco has been the leading brand in cigarettes

- ★ But now, as smoking rates decline, BAT is betting on a bold new future



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Andrew Stotz, PhD, CFA

For over 100 years, British American Tobacco has been the leading brand in cigarettes

- ★ What are they doing?
- ★ Well, it starts with them writing down about a quarter of their asset value on the balance sheet
- ★ More on that in a bit



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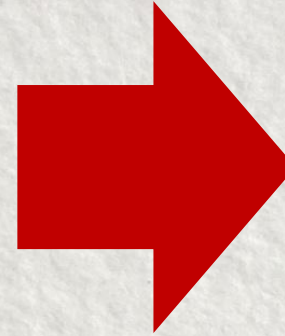
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Welcome to this...



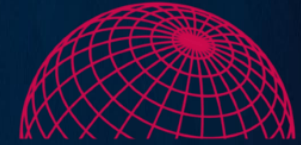
**Click the link in the description to grab my
Top 500 Global Companies Cheat Sheet**



Valuation Master Class

In this video you will learn

- ★ British American Tobacco's response to falling smoking rates
- ★ Assess the effectiveness of British American Tobacco's competitive advantage
- ★ Evaluate British American Tobacco's potential using my cheat sheet for assessing any stock's attractiveness



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- 🌐 And you can get that Cheat Sheet and this presentation for free by clicking on the link in the description

Is British American Tobacco Going Up in Smoke?



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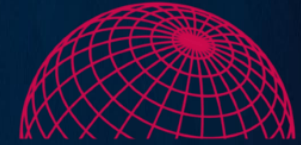
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- 🌐 What is the company's background?
- 🌐 What is its competitive strategy?
- 🌐 Does that strategy lead to a competitive advantage?
- 🌐 What does the valuation look like?

A leading name in the global nicotine industry

- ★ British American Tobacco is one of the world's largest producers of tobacco and nicotine products
- ★ It operates in over 180 countries with a portfolio of traditional tobacco products and newer reduced-risk products
- ★ It holds the 2nd largest global market share of 21% in the cigarette industry



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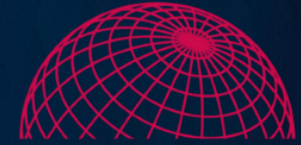
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Nicotine is a highly addictive chemical present in tobacco leaves

- ★ Nicotine triggers the release of dopamine, a “feel-good” chemical, creating feelings of pleasure and relaxation
- ★ Over time, the brain adapts, requiring larger doses to achieve the same effects, creating a cycle of craving and use
- ★ British American Tobacco generates billions by innovating and diversifying nicotine products



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81% of revenue from combustibles, cigarettes and cigars that release nicotine through burning



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12% of revenue from new products: Vapour – E-cigarettes heat liquid to produce nicotine vapour



Vapour



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12% of revenue from new products: Heated – Heat, rather than burn tobacco to get nicotine



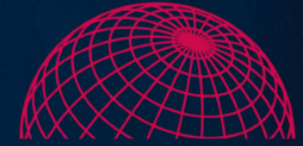
Vapour

Heated Products

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Sources: bat.com

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12% of revenue from new products: Modern orals – Tobacco-free nicotine pouches



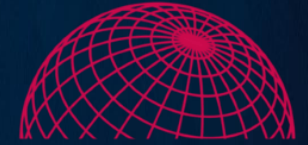
Vapour



Heated Products



Modern Orals



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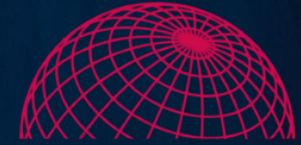
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5% from traditional orals, made from fermented or processed tobacco leaves inhaled or snorted



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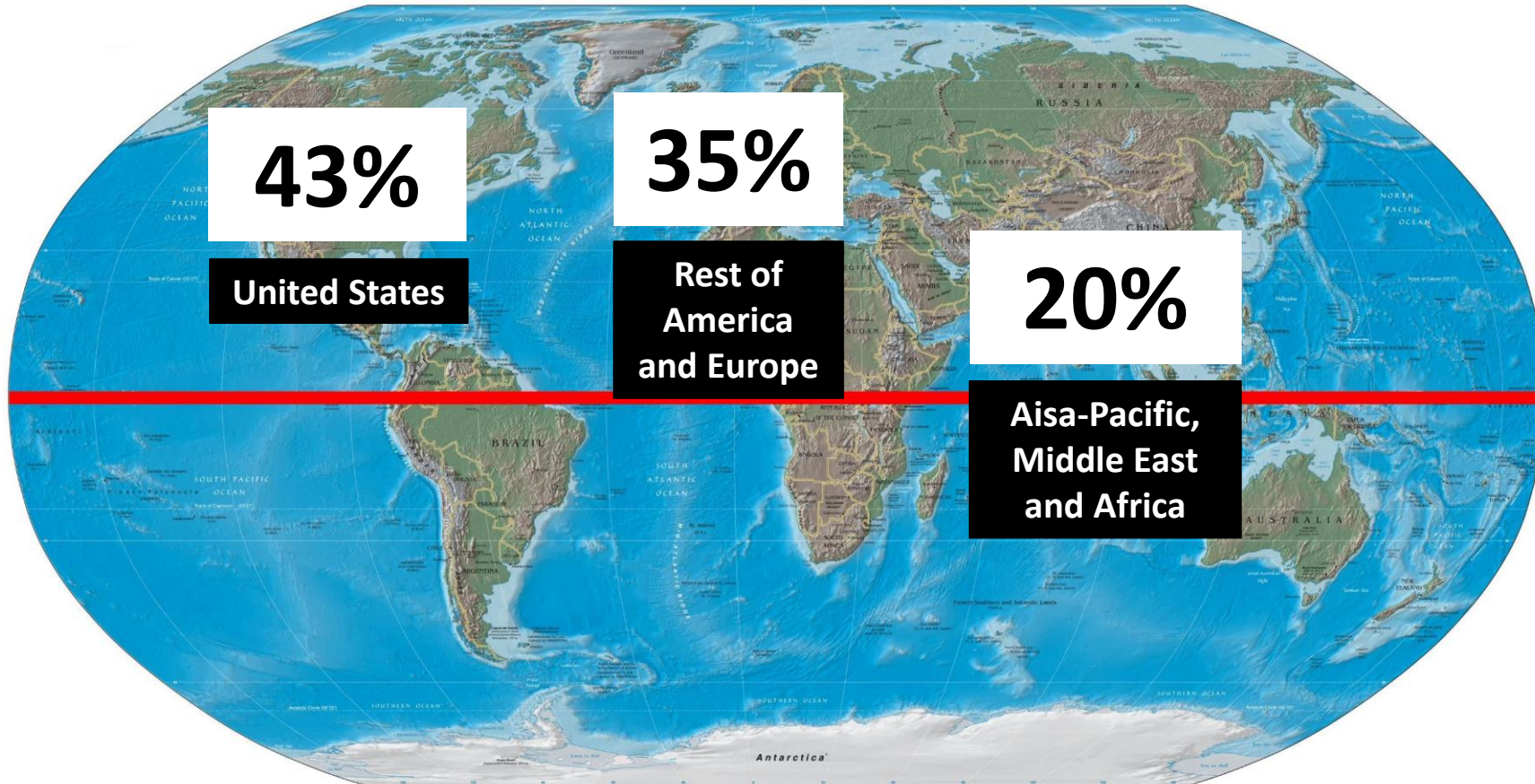
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Strong US premium demand and combustibles growth in Japan, Korea, and the Middle East



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1902: BAT was formed as a JV between Imperial Tobacco (UK) and American Tobacco (US)



AMERICAN
TOBACCO



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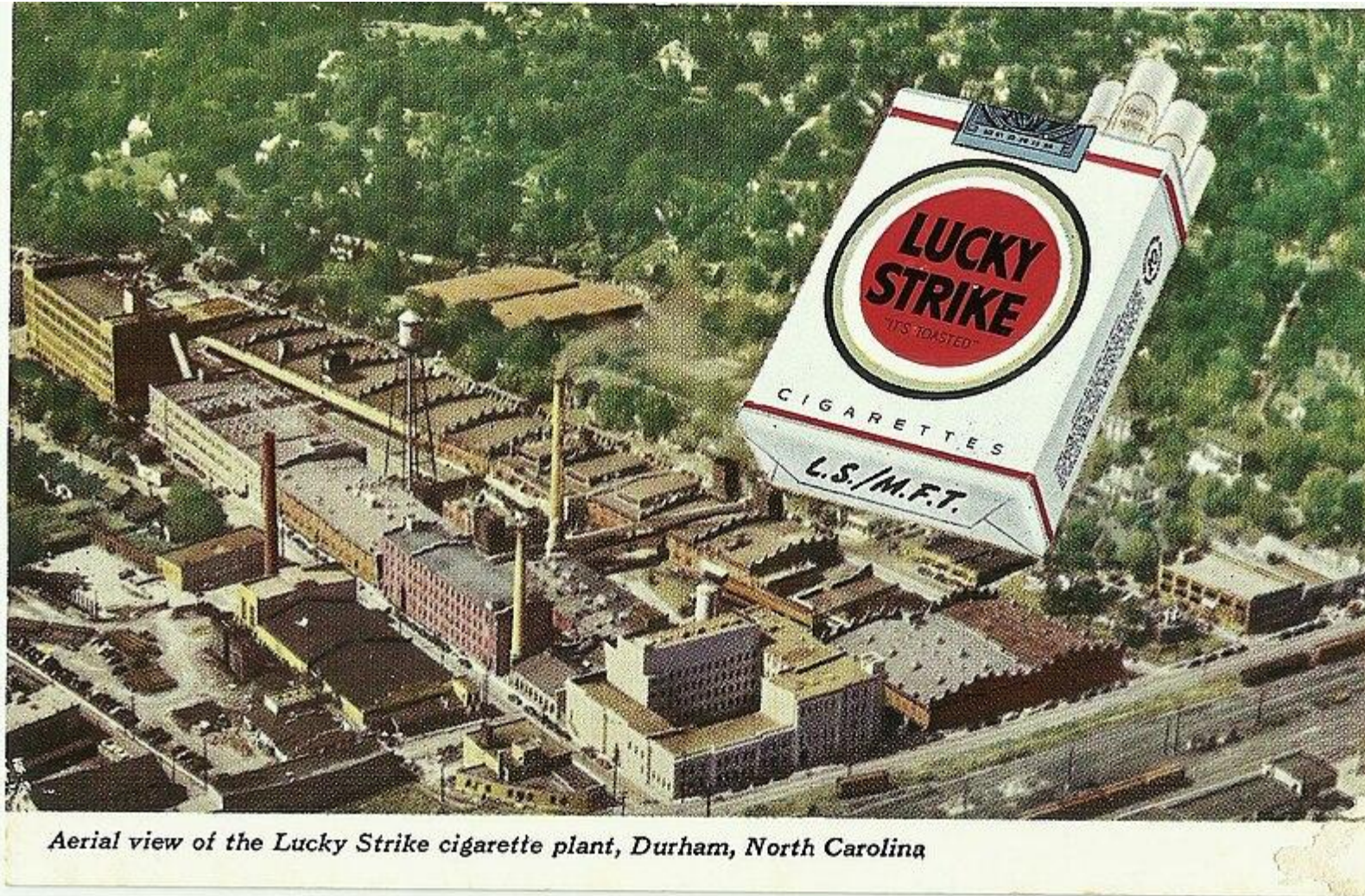
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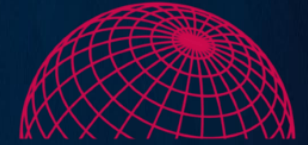
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- 🌐 This stopped each from competing in their respective markets

In 1907 the US gov't charged American Tobacco Co. with being a monopoly



Aerial view of the Lucky Strike cigarette plant, Durham, North Carolina

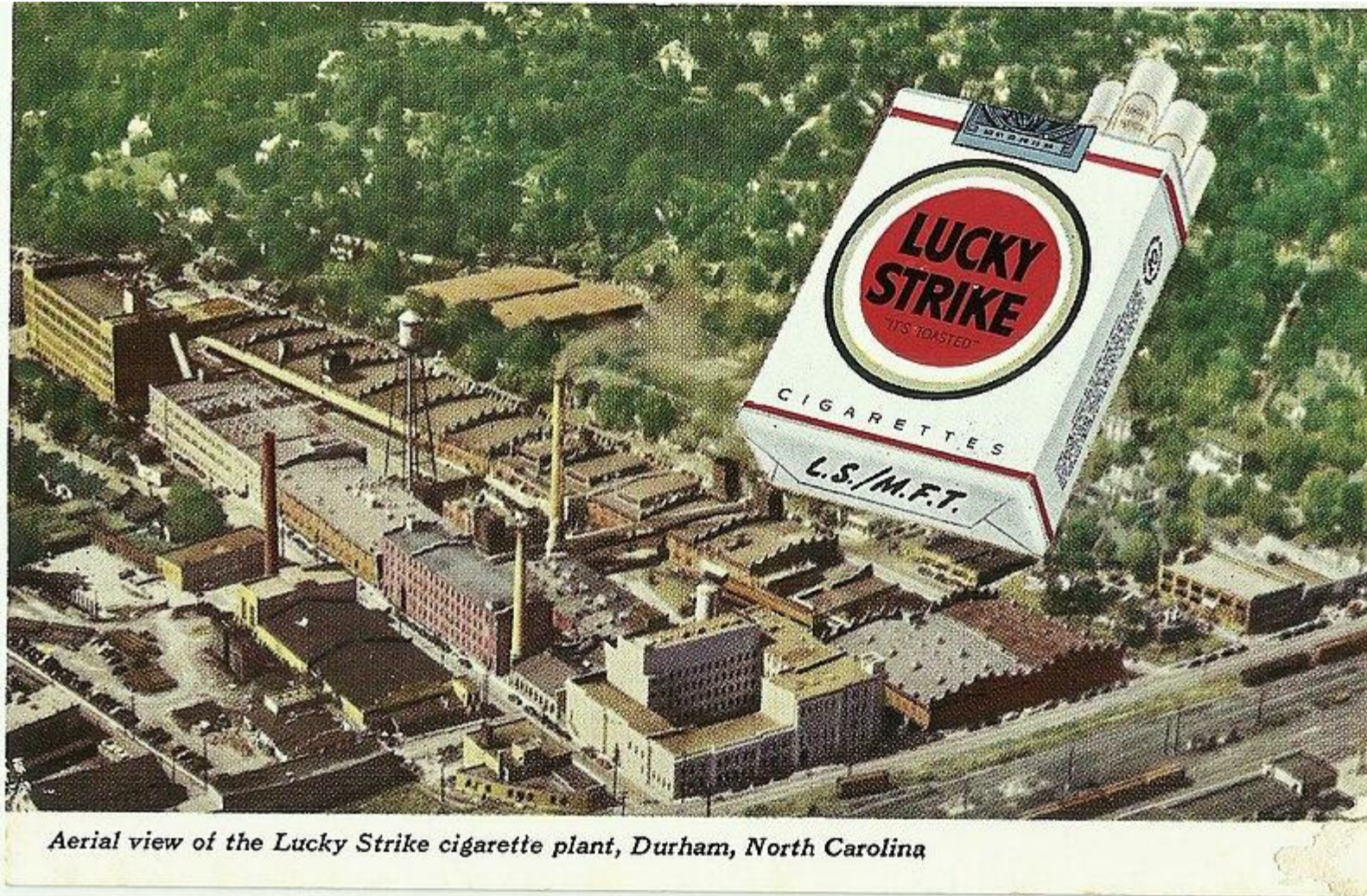


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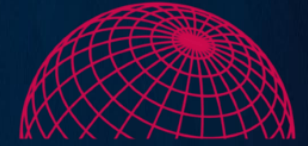
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In 1911, the Supreme Court dissolved American Tobacco for monopolistic practices



Aerial view of the Lucky Strike cigarette plant, Durham, North Carolina

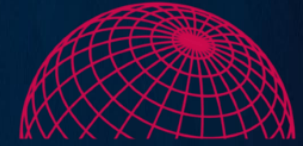


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1911: American Tobacco was forced to divest its BAT shares, making BAT independent



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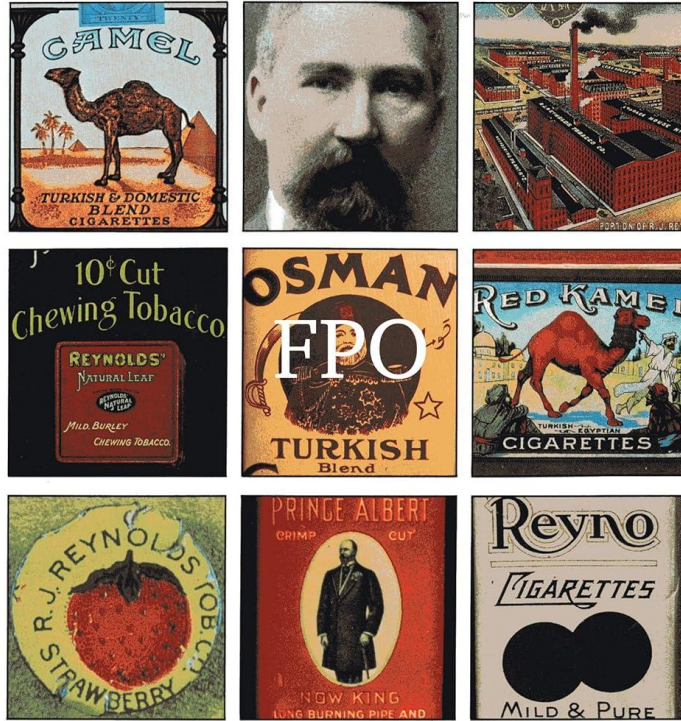
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American Tobacco was also forced to sell its shares in R.J. Reynolds after 1911

The **R.J. Reynolds** Tobacco Company



NANNIE M. TILLEY

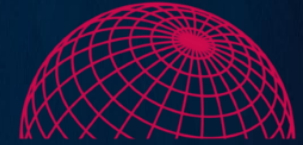
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Richard Joshua Reynolds founded R.J. Reynolds in 1875



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Sources: [En.wikipedia.org/wiki/R._J._Reynolds#/media/File:RJ_Reynolds.jpg](https://en.wikipedia.org/wiki/R._J._Reynolds#/media/File:RJ_Reynolds.jpg)



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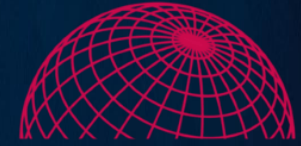
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- 🌐 He was forced into American Tobacco in 1899

After gaining independence in 1911, R.J. Reynolds

- ★ Introduced Camels, revolutionizing the market
 - **Blended smooth tobacco, low-cost, convenient, and marketed for mass appeal**
- ★ In 1954, launched Winston, the first filter-tipped cigarette
- ★ 1989: Merged with Nabisco to form RJR Nabisco; then split in 1999



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After gaining independence in 1911

- ★ In 1999, Brown & Williamson merged with R.J. Reynolds to form Reynolds American Inc. (RAI); BAT retained a 42% stake



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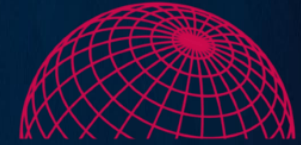
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In 2004, BAT privatized ETI SpA (Europe's second-largest tobacco company)



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- 🌐 Ente Tabacchi Italiani - ETI S.p.A (Italian Tobacco Company)
- 🌐 This helped to secure leadership in the European market

In 2017, BAT bought the remaining 58% of RAI, gaining full ownership



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- 🌐 Becoming the world's largest listed tobacco company
- 🌐 Today, the company operates under BAT

2020: Investment in Reduced-Risk Products like vaping devices and nicotine pouches



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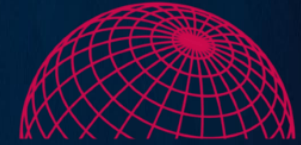
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- 🌐 This shift reflects BAT's commitment to consumer health and responding to the evolving preferences of adult nicotine users

In this video you will learn

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- ★ Assess the effectiveness of British American Tobacco's competitive advantage
- ★ Evaluate British American Tobacco's potential using my cheat sheet for assessing any stock's attractiveness

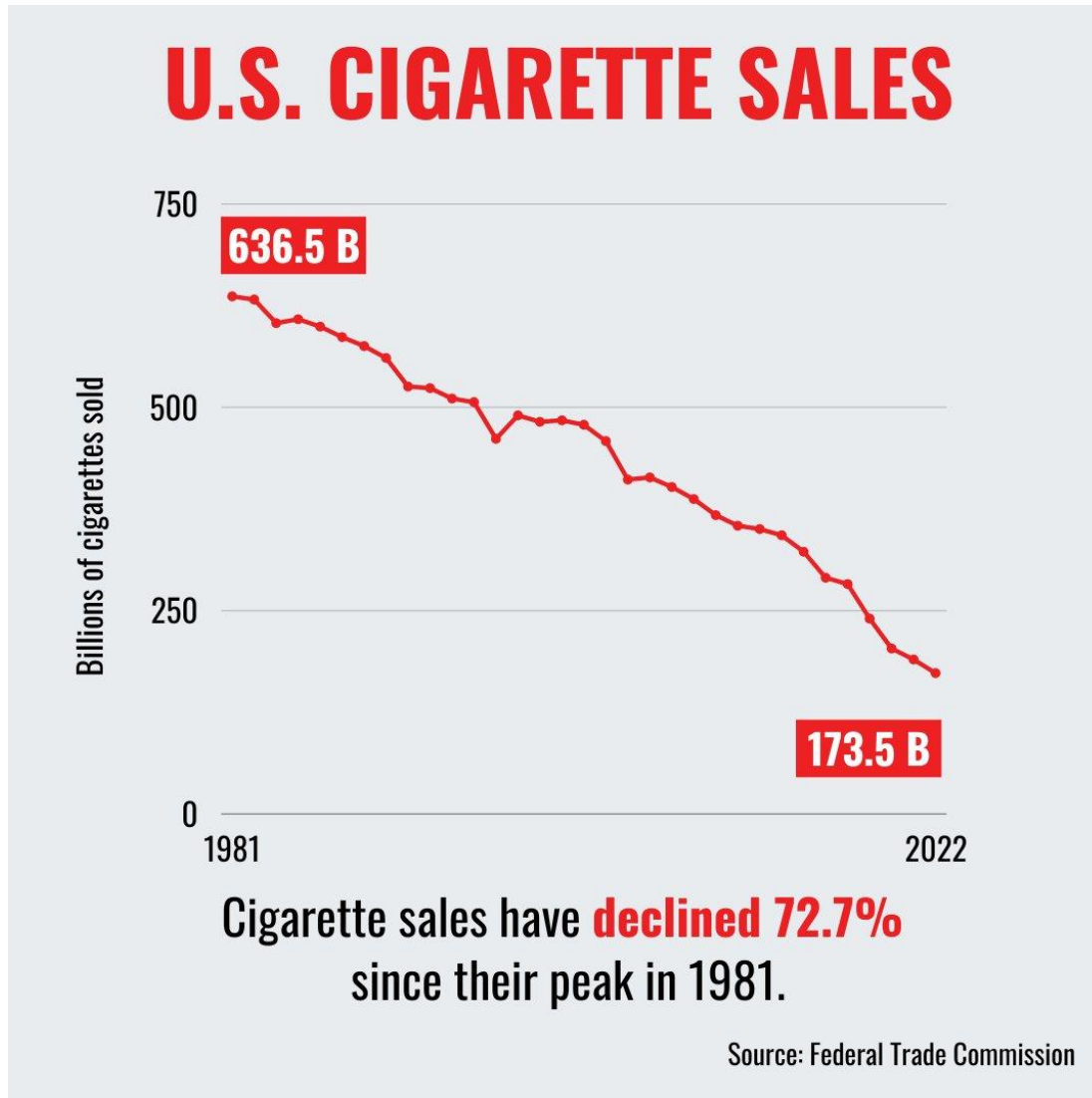


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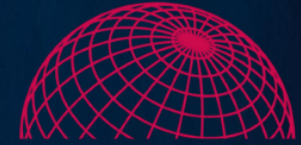
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Like all cigarette makers, British American Tobacco faces a major challenge



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Sources: bat.com



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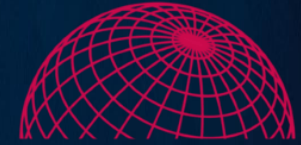
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- 🌐 Their core product, cigarettes, is in long-term decline

BAT's response

- ★ In 2023, BAT acknowledged this challenge with a significant impairment charge, writing down the value of its US operations
- ★ They also decided to amortize their US cigarette brands over no more than 30 years, signaling uncertainty about their long-term viability



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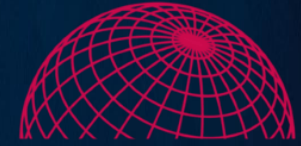
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At the end of 2023, BAT took a GBP27bn charge that reduced total assets by 23%

- ★ 41% of that was a GBP11bn write-down of its Newport brand
- ★ 21% came from a GBP5.7bn hit to Camel
- ★ 16% came from a GBP4.3bn write-down of the Reynolds American Goodwill
- ★ And finally, 13% of that was a GBP3.5bn write-down of Pall Mall



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BAT's future lies in its new categories division

- ★ A growing number of adult smokers are transitioning to smokeless alternatives such as vapour products, heated products, and modern oral nicotine
- ★ British American Tobacco has played a key role in this industry transformation through its multi-category strategy, designed to meet the evolving preferences of adult consumers while driving business growth



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BAT's 3 leading smokeless brands have generated over US\$3bn in revenue within a decade



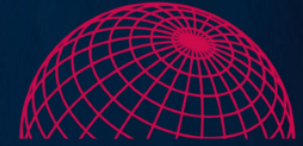
Vuse



Glo



Velo



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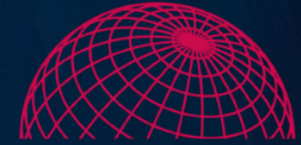
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- 🌐 BAT is committed to building a smokeless world by encouraging smokers to switch to smokeless alternatives

However, these products face significant scrutiny regarding their safety

- ★ Governments are imposing strict regulations like flavor bans, packaging rules, and high taxes on nicotine products
- ★ BAT faces rising competition from grey market sales, especially in the US and EU, where illegal vapes and counterfeits undermine growth
- ★ Traditional tobacco products enjoy strong brand loyalty built over decades, but new categories lack this loyalty



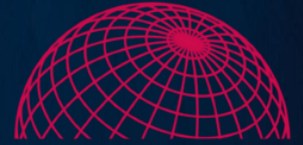
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Recap: What is the company's background?

- British American Tobacco remains heavily reliant on its combustible products
- It is investing to build a smokeless future, the transition remains gradual, with sticky customers



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Is British American Tobacco Going Up in Smoke?



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- 🌐 What is the company's background?
- 🌐 **What is its competitive strategy?**
- 🌐 Does that strategy lead to a competitive advantage?
- 🌐 What does the valuation look like?

British American Tobacco - US - 1902

Cons. staples industry, 46,000+ employees, US\$34bn revenue

Main segments/products/divisions

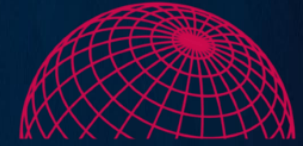
- New categories (vapour, heated products, modern oral)
- Traditional orals
- Combustibles

Its competitive advantage

Competitive advantage through strong brand portfolio, geographic diversification, regulatory pricing power and Innovation in reduced-risk products

How it achieved its competitive advantage

Achieved by transitioning to a dual product company in traditional and new categories, addiction-driven customer loyalty, economies of scale, and operational efficiency



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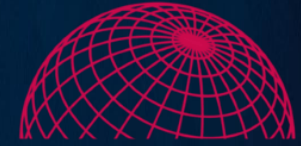


BAT leverages its cigarette brands to maintain market dominance and strong cashflows



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Sources: bat.com



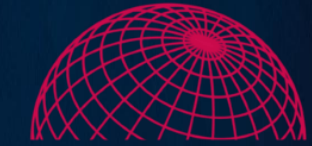
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- While also investing heavily in reduced-risk products to meet evolving consumer demands and regulatory trends

Iconic brands like Dunhill, Lucky Strike, and Pall Mall enjoy strong consumer loyalty



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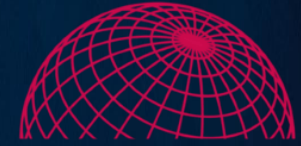
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- 🌐 BAT invests in targeted marketing campaigns, especially for premium and innovative products, to sustain brand equity

BAT's strong brand image lets it increase prices for premium products

- ★ British American Tobacco raised prices across key markets to counter declining volumes, achieving a 4% organic price/mix growth in 2024 despite a 7% volume drop
- ★ In the UK, following a government duty hike in 2024, BAT adjusted prices, pushing the cost of a 20-pack to £17 from £15



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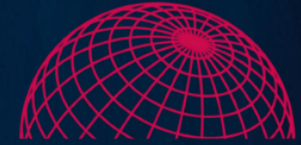
Sustainability vision of “A Better Tomorrow”



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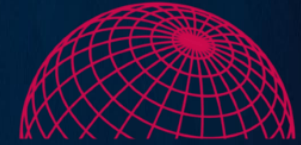
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- 🌐 BAT emphasizes environmental and social responsibility, aiming for carbon neutrality across operations by 2030

An ESG champion

- ★ **S&P Global (2023)**: Scored 81/100; hence in Dow Jones Sustainability Index for 22 years
- ★ **CDP (2023)**: A- in Climate Change, Water Security, and Forests assessments
- ★ **ISS ESG (2024)**: Awarded Prime Status, indicating strong ESG performance
- ★ **Sustainalytics**: Scored 30.3 (high risk), ranked 208th out of 574 in the tobacco industry
- ★ **Refinitiv (2023)**: Scored 91/100, 3rd in the FTSE 100 and top in global food and tobacco



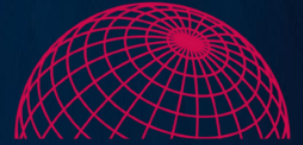
The ESG paradox

- ★ Governments penalize BAT for harmful products, yet impressive ESG performance
- ★ Gov't taxes tobacco to deter use, but BAT earns praise for emissions cuts
- ★ Smoking is condemned, yet BAT is celebrated for corporate responsibility
- ★ BAT's harmful products are vilified, but sustainable packaging gets applause
- ★ Harming health, yet praised for protecting the planet



Recap: What is its competitive strategy?

- BAT's strong brand image allows it to raise prices on premium products
- Its investment in non-smoking alternatives drives growth
- ESG rewards for compliance to scorecards



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- 🌐 What is the company's background?
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**Is the company
financially world class?**



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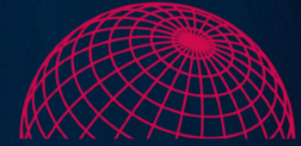


I use my **World Class Benchmarking** scorecard to measure if a company has a **competitive advantage**



I developed this scorecard ten years ago; here's how we construct it

- ★ My team gathers the yearly and quarterly financial data of 26,000 companies worldwide
- ★ We then calculate each company's **Profitable Growth** score
 - Which is a composite measure of both profitability and growth



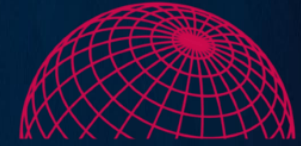
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I developed this scorecard ten years ago; here's how we construct it

- ★ After that, we rank the company relative to sector peers of similar size
 - A decile ranking of 1 or 2 is financially world class, while 10 is the worst
- ★ We assess the company's performance over the prior four years and the past 12 months (PTM)



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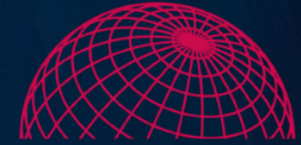
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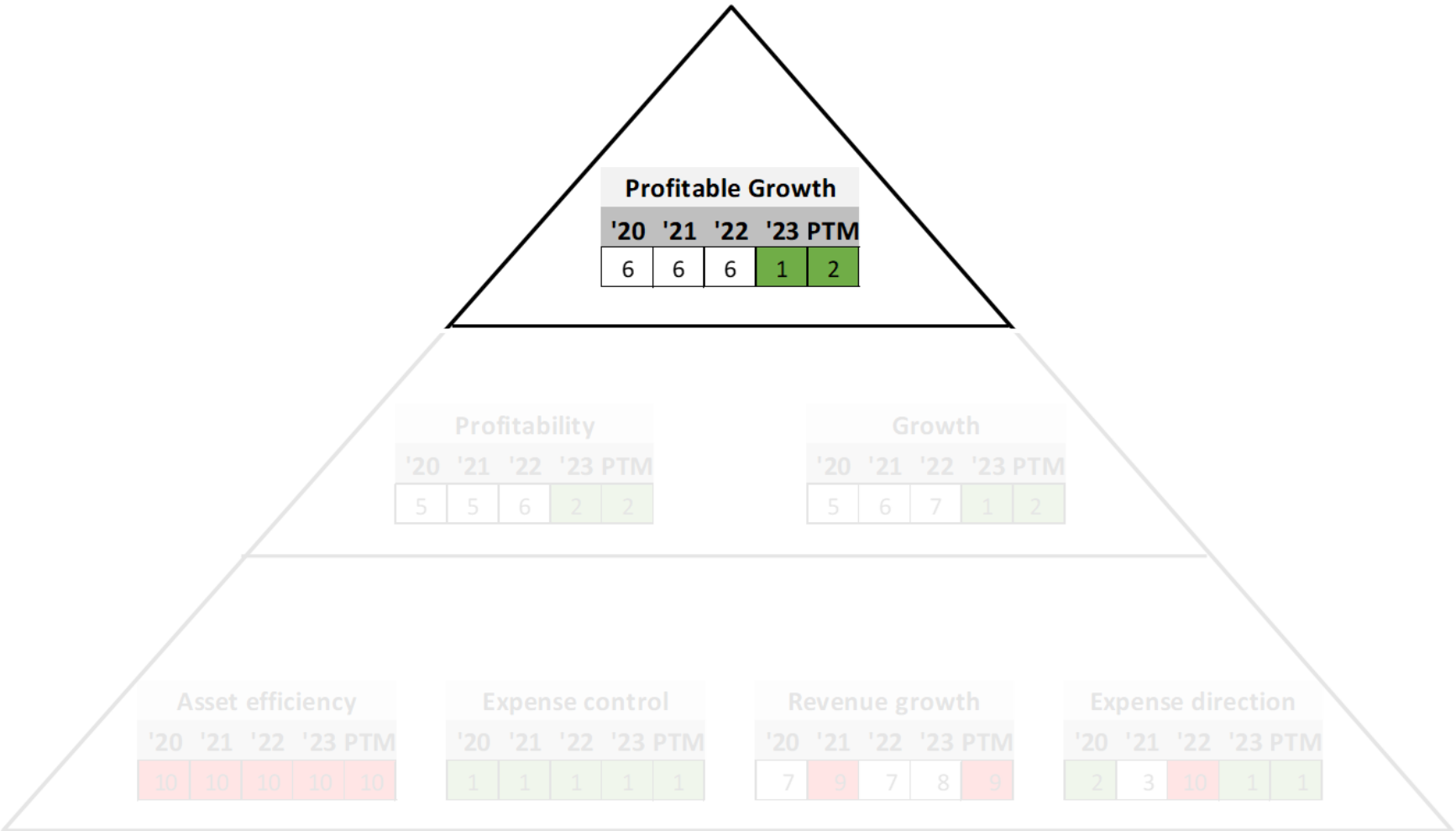


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BAT: A. Stotz Profitable Growth



Benchmarked against 550 large Cons. Staples companies worldwide.

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Sources: A. Stotz Investment Research. Notes: 1 = top ranking and 10 = worst. Most recent year's data is based on the past 12 months (PTM) of published data.



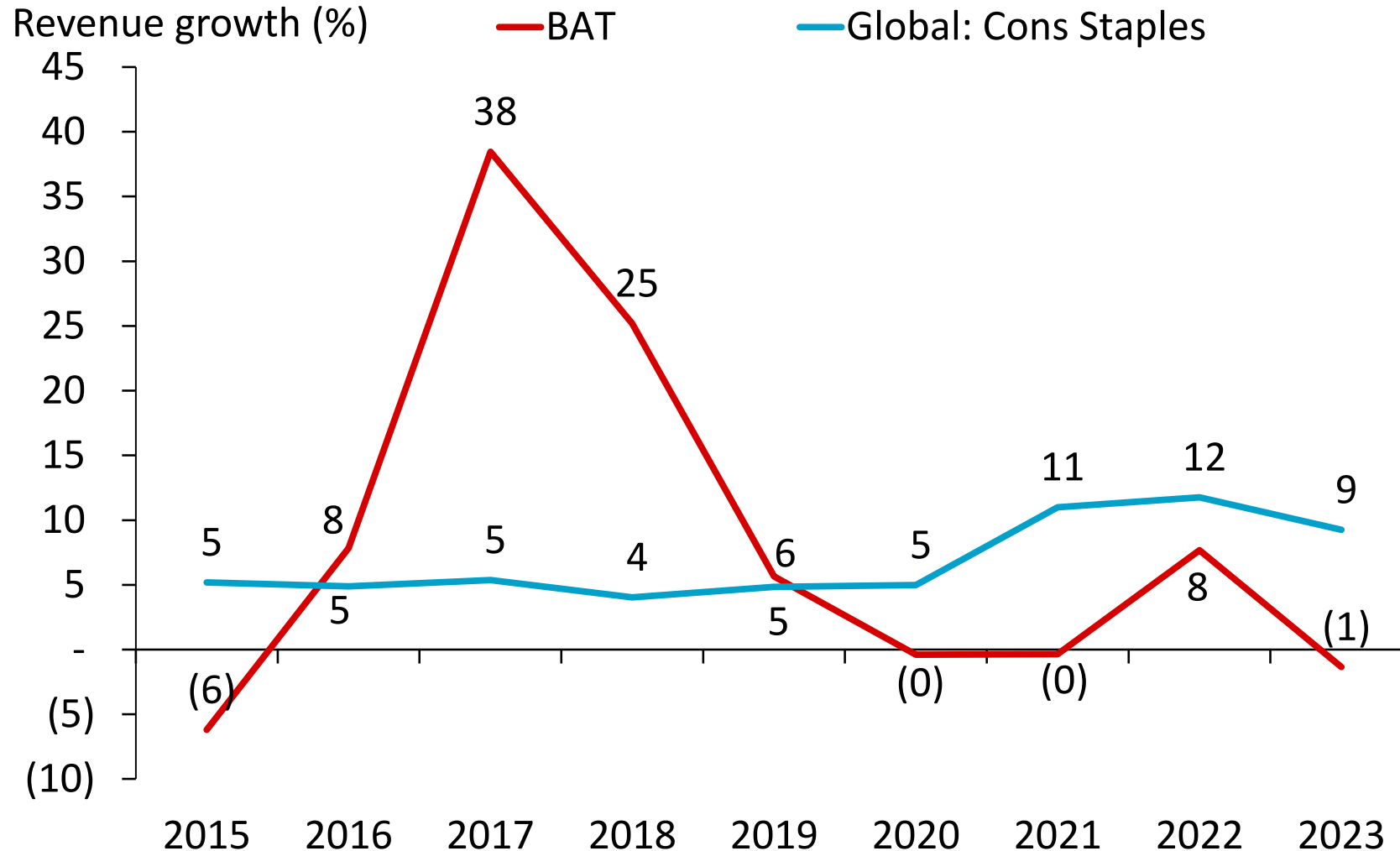
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Revenue growth has been underperforming the global sector average in recent years



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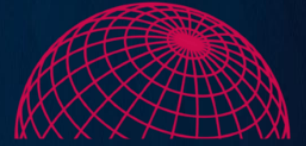
by
A. Stotz INVESTMENT
RESEARCH

Andrew Stotz, PhD, CFA

- 🌐 The 2017 surge came from the US\$49bn acquisition of remaining 58% of Reynolds American Inc. (RAI)

Recap: Does its strategy lead to a competitive advantage?

- Partially
- BAT has shown profitable growth in recent years, according to our scorecard



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Is British American Tobacco Going Up in Smoke?



CASE STUDY

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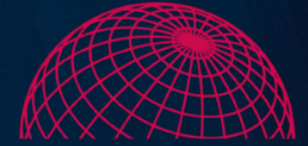
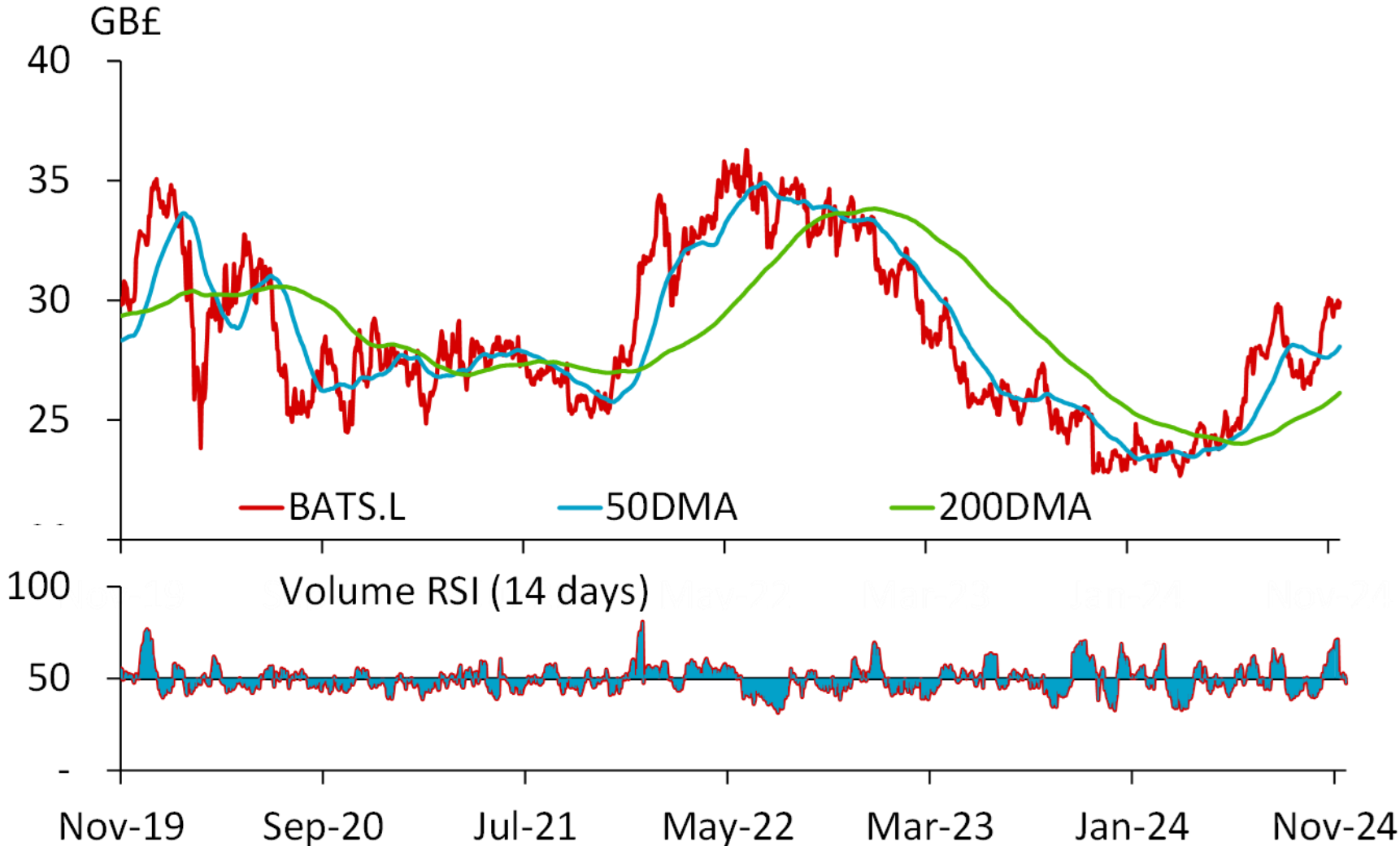
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**This is not a recommendation
or investment advice.**

- 🌐 What is the company's background?
- 🌐 What is its competitive strategy?
- 🌐 Does that strategy lead to a competitive advantage?
- 🌐 **What does the valuation look like?**

The chart shows a positive trend reversal with rising momentum and volatility



CASE STUDY

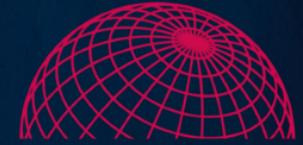
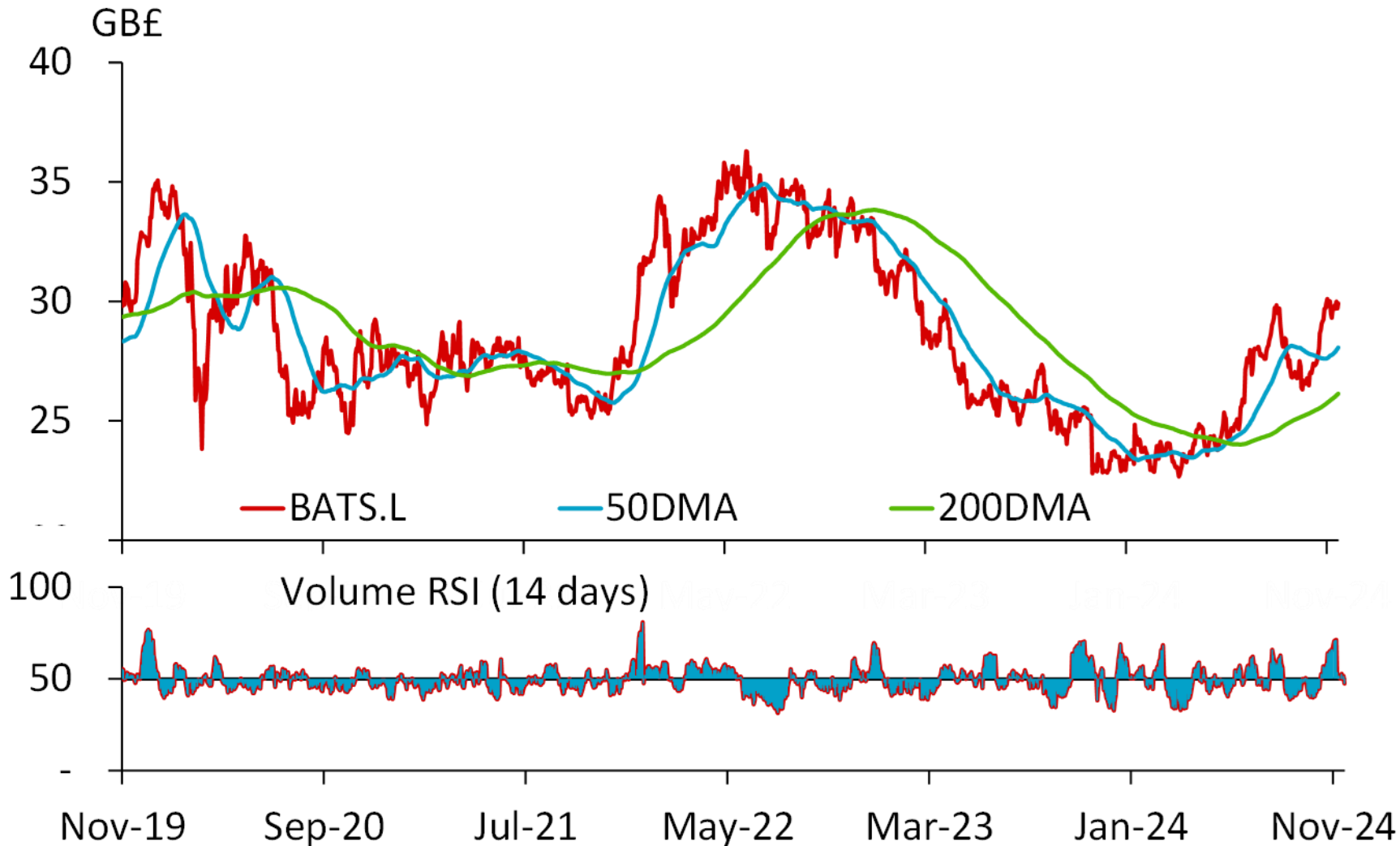
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Recent trends show recovery with the short-term average surpassing the long-term



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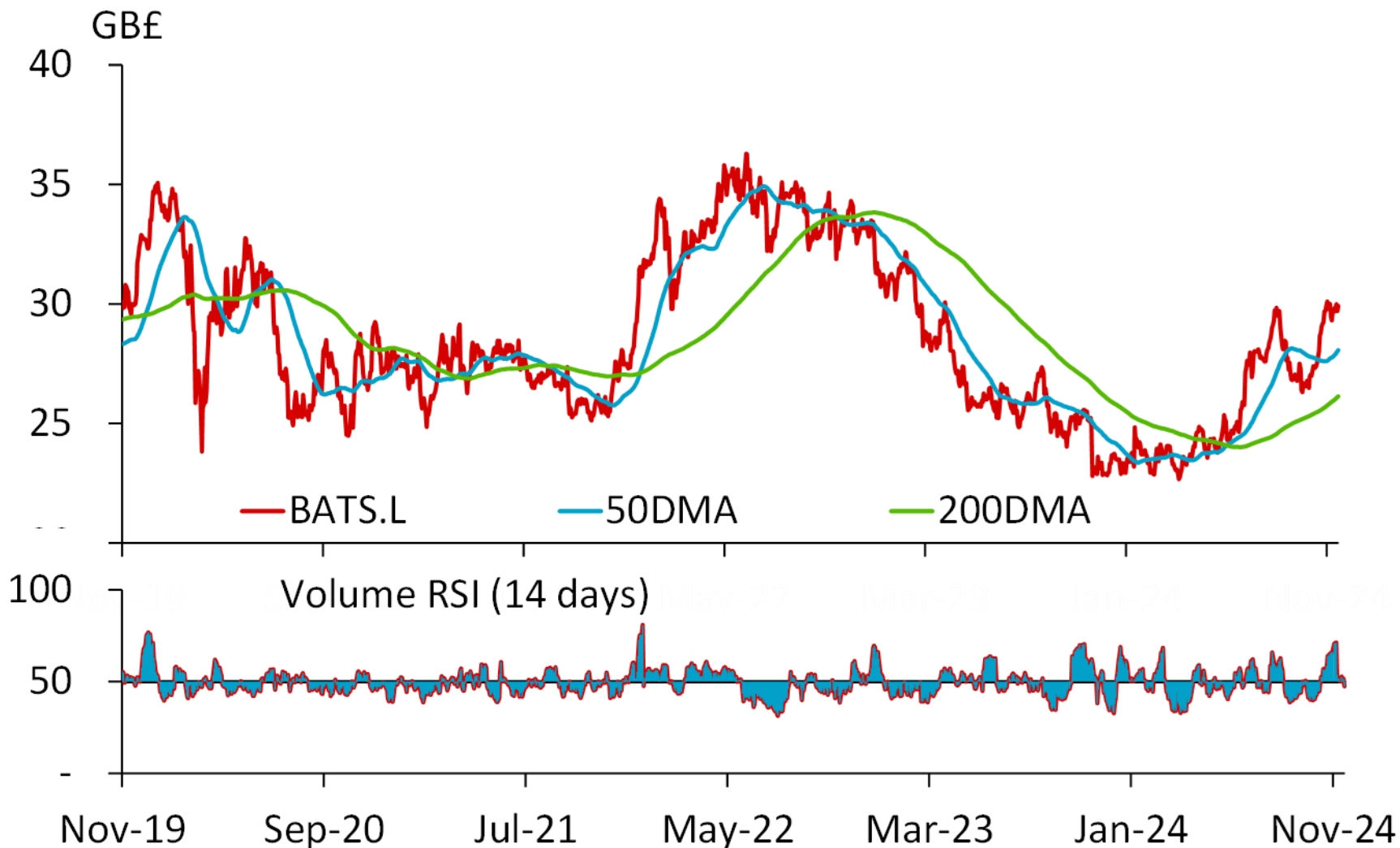
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Volume RSI spikes signal intense market activity during price swings



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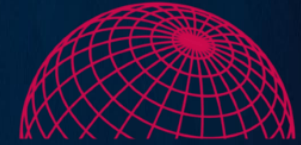
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I use my **FVMR** methodology
to determine the
attractiveness of the
company



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Net profit margin (NPM)
Return on assets (ROA)

MANAGEMENT

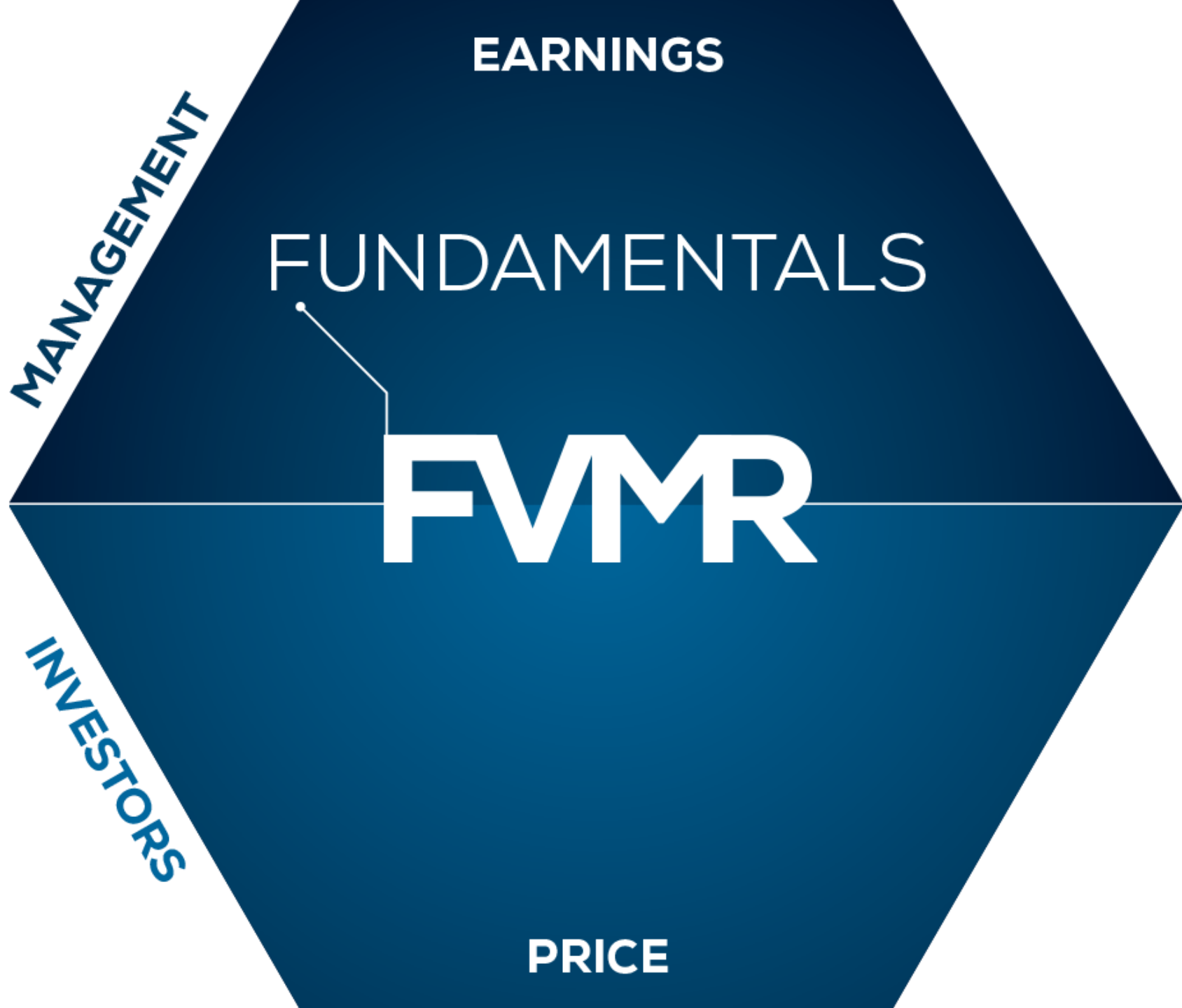
EARNINGS

FUNDAMENTALS

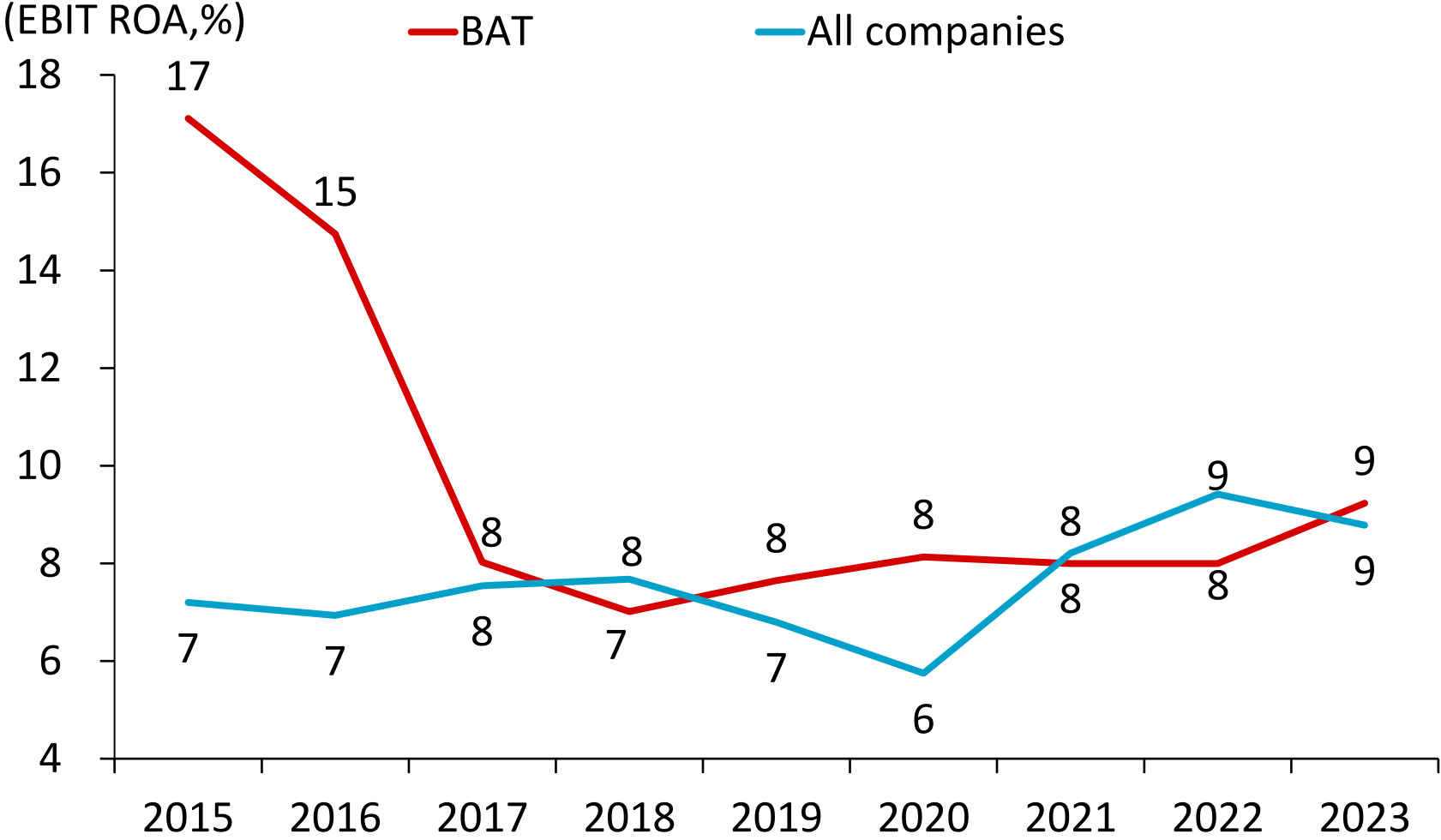
FVMR

INVESTORS

PRICE



EBIT ROA is in line with 10,000 globally



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The company has also benefited from cost-cutting initiatives and operational efficiencies

MANAGEMENT

EARNINGS

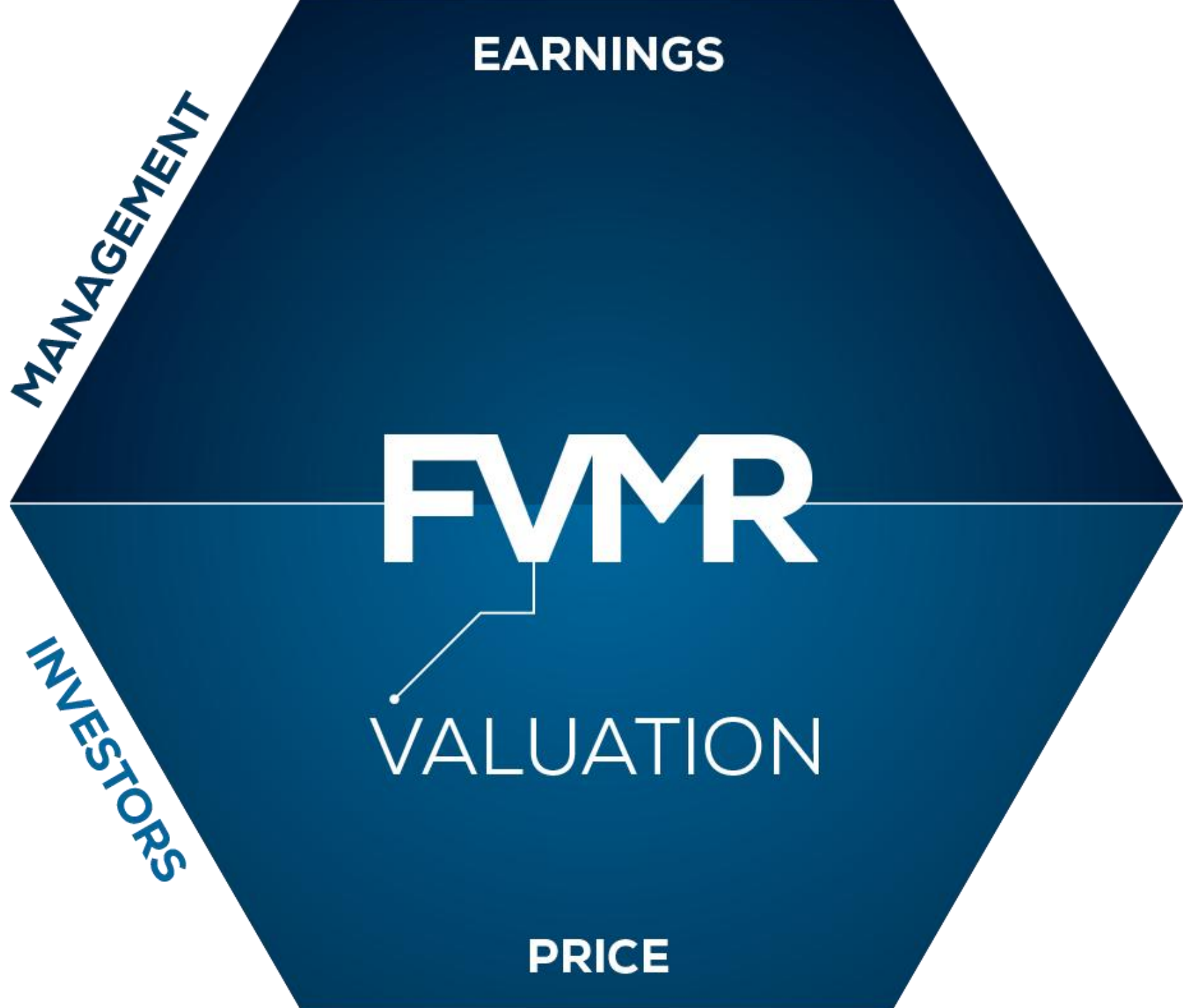
FVMR

VALUATION

INVESTORS

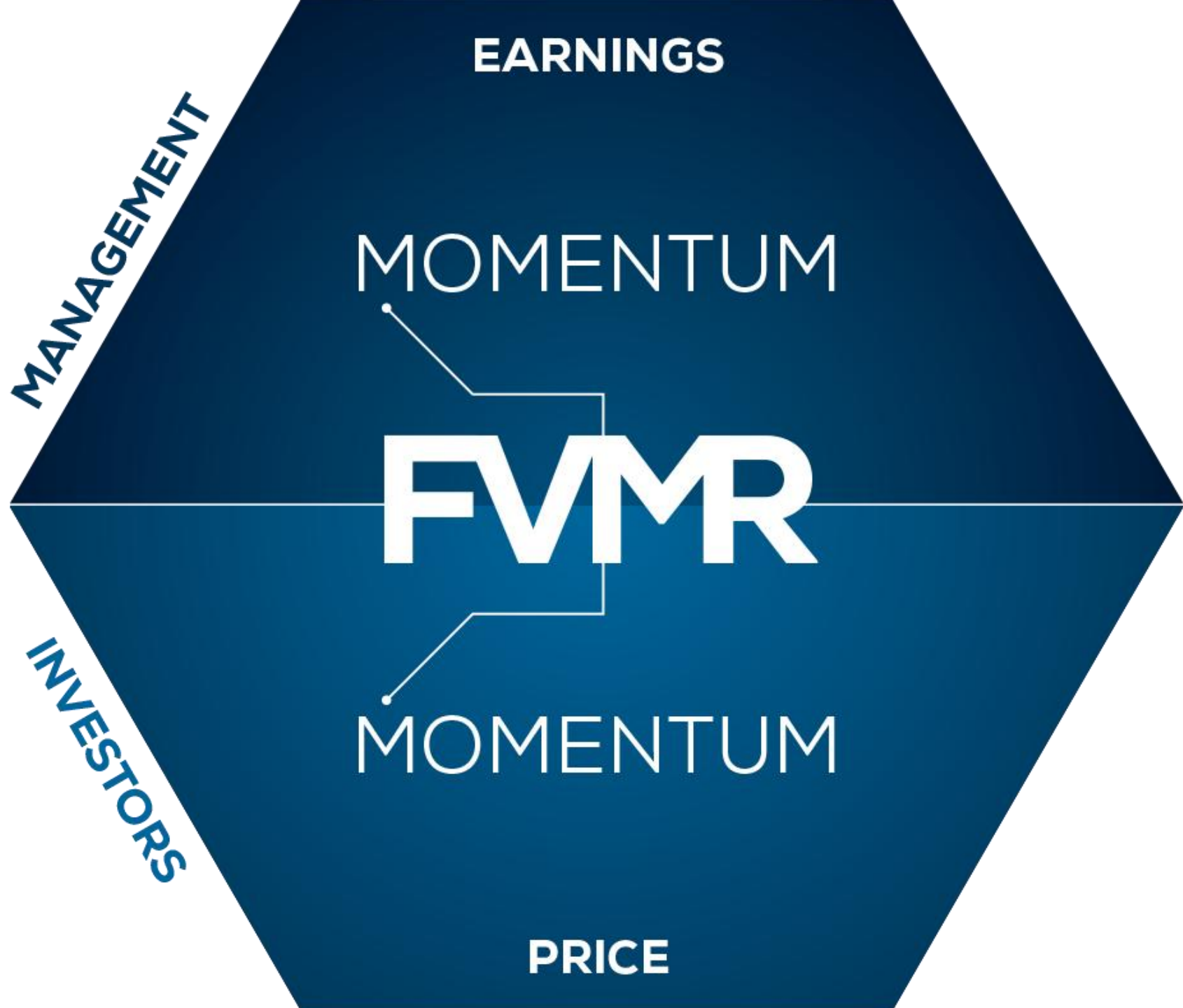
PRICE

Price-to-earnings (PE)
Price-to-book value (PB)

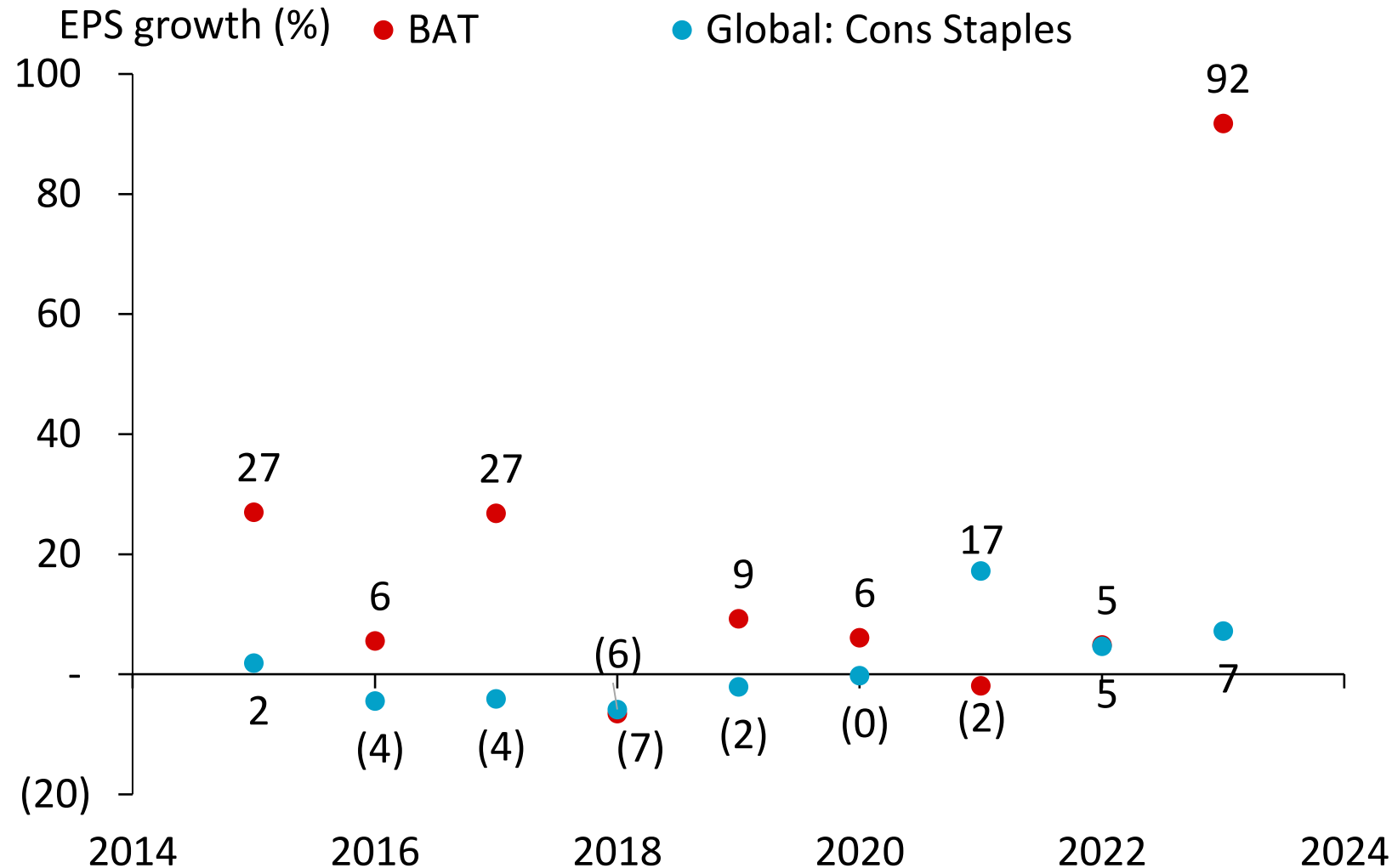


EPS growth (EPS)

% Price change (Price*)



EPS CAGR of 5% from 2015-2023, 5 ppts above the global industry average



MANAGEMENT

EARNINGS

RISK

FVMR

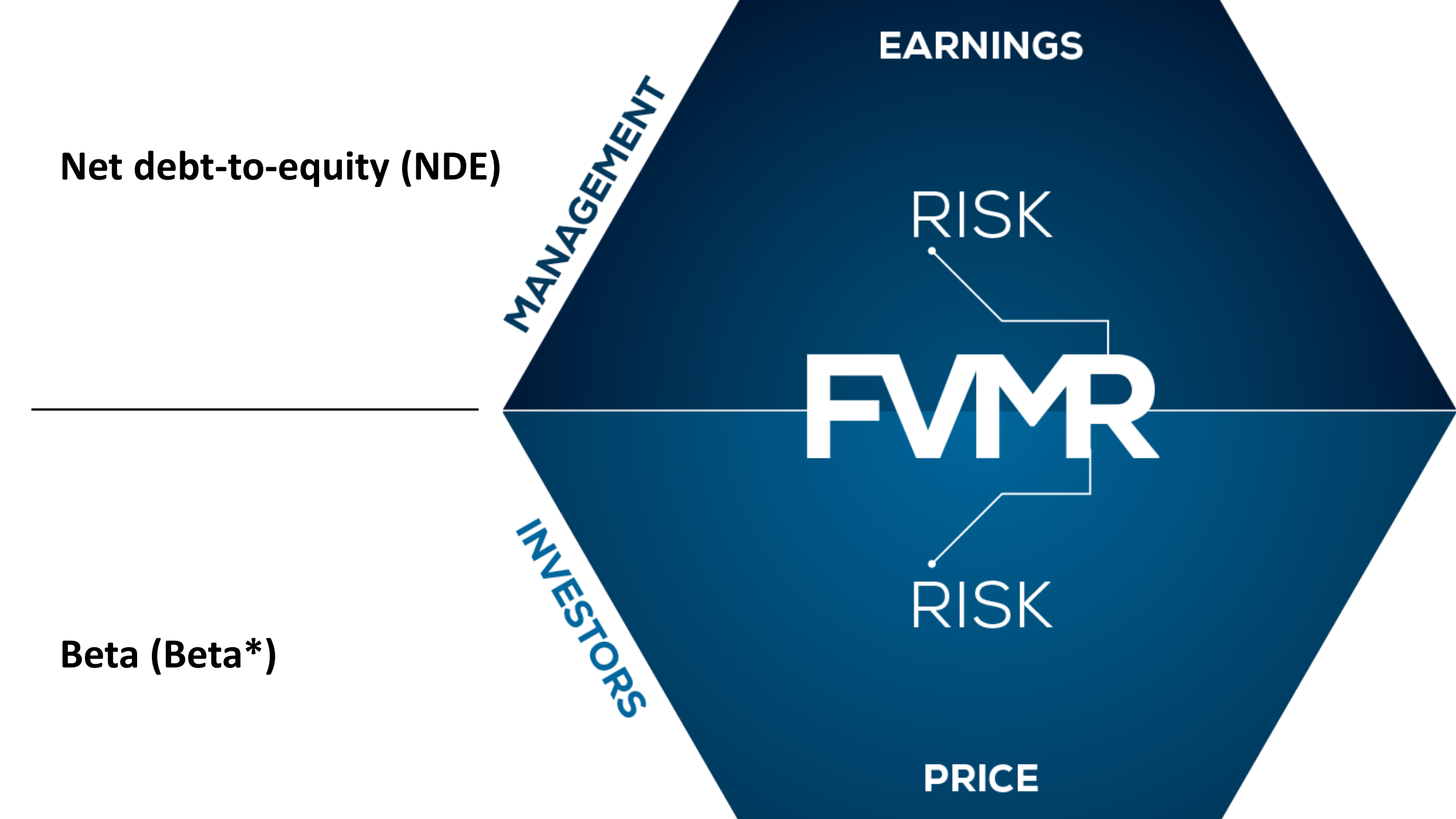
RISK

INVESTORS

PRICE

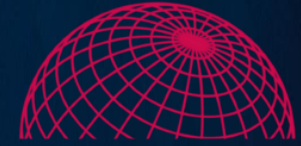
Net debt-to-equity (NDE)

Beta (Beta*)



In this video you will learn

- ★ British American Tobacco's response to falling smoking rates
- ★ Assess the effectiveness of British American Tobacco's competitive advantage
- ★ Evaluate British American Tobacco's potential using my cheat sheet for assessing any stock's attractiveness

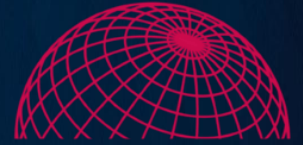


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Let's take a look at the abbreviated **FVMR** Scorecard of **British American Tobacco**



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Relatively cheap 1.3x price-to-book value after its asset write down

A. Stotz FVMR Methodology - Cons. Staples: Food, Bev. & Tob.

Company	Exchange	Mcap US\$bn	Fund. (%)		Valuation (x)		Momo (% chg)		Risk (x)	
			NPM	ROA	PE	PB	EPS	Price*	NDE	Beta*
Cons. Staples: Food, Bev. & Tob.		2,419	18.9	12.7	23.4	6.0	(4.3)	1.6	(0.0)	0.3
Coca-Cola Co	USA	275.0	22.4	10.5	26.4	10.4	(2.9)	(10.4)	1.1	0.1
Kweichow Moutai Co Ltd	China	270.9	49.1	30.9	23.4	9.0	16.1	17.3	(0.2)	0.5
Nestle SA	Switzerland	221.9	12.2	8.5	17.2	5.9	17.9	(14.8)	1.4	0.3
PepsiCo Inc	USA	218.0	10.2	9.6	23.3	11.2	13.2	(10.4)	1.9	0.2
Philip Morris International Inc	USA	197.5	26.3	15.3	20.1	nm	22.5	1.9	(4.8)	(0.7)
Altria Group Inc	USA	93.2	42.7	28.2	9.1	nm	20.8	4.5	(6.9)	(0.8)
Mondelez International Inc	USA	83.8	10.6	5.3	21.9	3.0	(15.8)	(15.8)	0.7	0.2
British American Tobacco plc	UK	83.7	(52.8)	(10.3)	nm	1.3	(258.8)	0.7	0.5	(0.5)
Wuliangye Yibin Co Ltd	China	81.2	36.8	21.3	16.5	4.5	19.0	33.9	(0.8)	1.0
Diageo PLC	UK	72.6	19.1	8.4	18.8	7.2	(11.7)	2.1	2.0	0.9
Nongfu Spring Co Ltd	HK	54.7	28.3	25.9	31.3	15.1	29.8	28.6	(0.7)	2.4
Monster Beverage Corp	USA	51.5	21.7	17.9	32.1	8.9	5.3	6.0	(0.4)	0.6
Danone SA	France	46.4	3.7	2.2	43.4	2.5	(23.2)	(0.6)	0.6	0.2
Keurig Dr Pepper Inc	USA	45.9	15.0	4.4	20.1	1.8	20.4	(8.7)	0.5	0.4
Constellation Brands Inc	USA	43.5	5.7	2.3	75.0	5.5	(61.4)	(4.9)	1.3	0.3
Heineken NV	Netherlands	42.5	3.4	1.9	36.4	2.0	(58.3)	(15.4)	0.9	0.3
Kraft Heinz Co	USA	38.2	5.2	1.5	27.8	0.8	(54.0)	(10.4)	0.4	0.3
Hershey Co	USA	37.2	16.2	15.0	21.0	8.9	(17.7)	(7.3)	1.1	(0.0)
Foshan Haitian Flavouring and Food (China		37.1	23.2	17.3	43.4	9.5	3.9	34.8	(0.9)	0.8
General Mills Inc	USA	36.7	12.1	7.7	15.3	4.0	2.4	(9.5)	1.3	(0.2)
Coca-Cola Europacific Partners PLC	USA	36.5	8.4	5.4	20.8	4.0	(5.2)	(1.9)	1.3	0.8
Shanxi Xinghuacun Fen Wine Factory	China	35.3	33.8	27.9	20.5	8.3	18.6	36.2	(0.3)	0.9

Sector data is market cap weighted. *Price change and beta over the past three months as of 12 December 2024

This is not a recommendation or investment advice.

Sources: A. Stotz Investment Research LSEG., Refinitiv

The scorecard ranking should not be seen as investment advice, do your own research.



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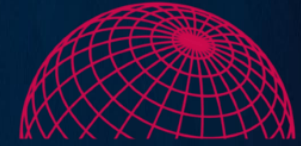
by *A. Stotz* INVESTMENT RESEARCH

Andrew Stotz, PhD, CFA

- Low valuation metrics like negative NPM and ROA
- Negative EPS growth

Relatively cheap 1.3x price-to-book value after its asset write down

- ★ Click the link in the description to get the Abbreviated FVMR Scorecard for the world's top 500 companies
- ★ Drop your email and you will receive the updated FVMR scorecard in your inbox every week



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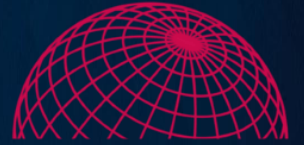
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Andrew Stotz, PhD, CFA

Recap: What does the valuation look like?

- Relatively cheap 1.3x price-to-book value after its asset write down



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A. Stotz

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Andrew Stotz, PhD, CFA

British American Tobacco Balance Sheet Up in Smoke



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