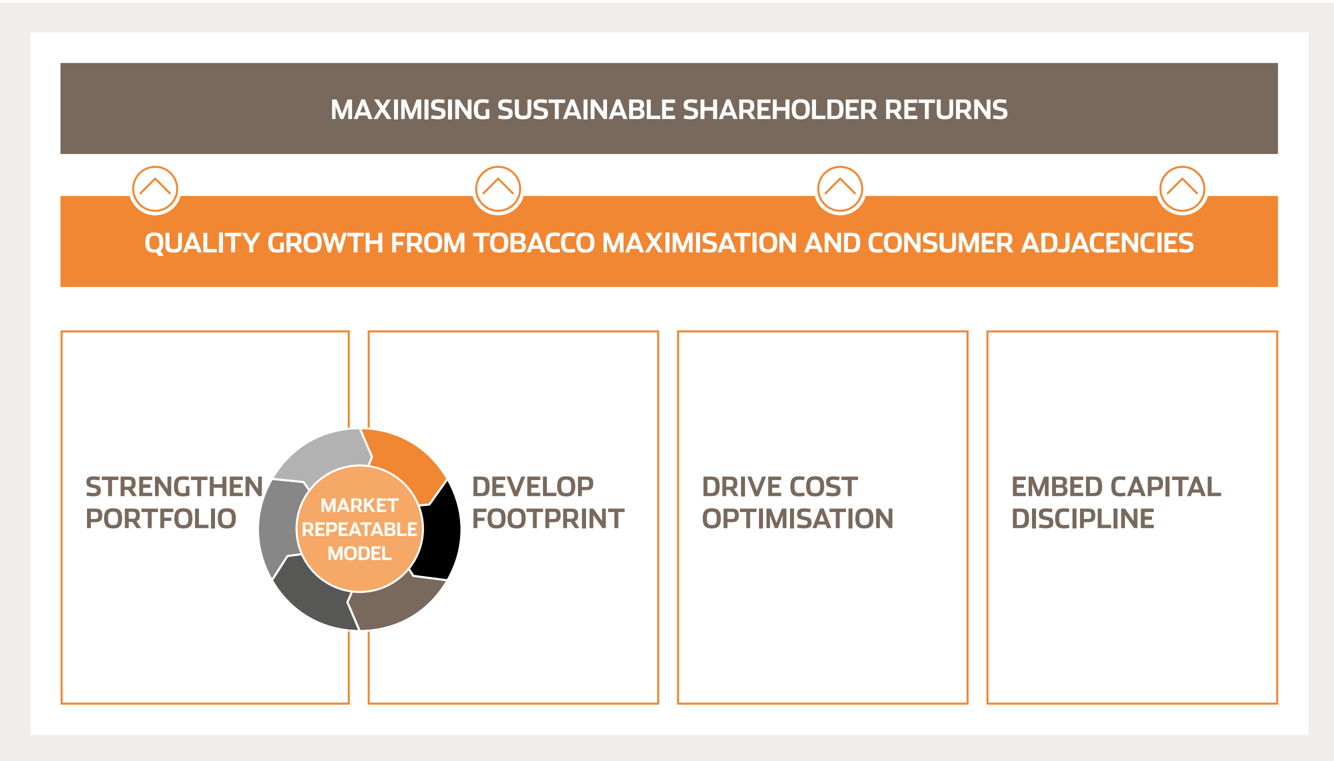
OUR STRATEGY AND BUSINESS MODEL

STRATEGY

Our strategy articulates how we create value for shareholders and is focused on driving performance in four key areas. We are strengthening our portfolio and developing our footprint by deploying our Market Repeatable Model, a structured 'go to market' framework for generating quality growth. Cost optimisation is about being more efficient and effective, and in focusing on cash generation and working capital management, we continue to embed capital discipline in the business. Aligning resource behind these strategic pillars enables us to make the most of growth opportunities in tobacco and consumer adjacencies, while ensuring we remain in a strong position to continue delivering sustainable returns to shareholders.



HOW WE SUPPORT GROWTH

STRONG GOVERNANCE

High standards of governance are critical to our success.

Turn to page 33
for more information

ACTING RESPONSIBLY

Operating responsibly is integral to the way we do business.

Turn to page 29
for more information

MANAGING RISK

We actively identify, manage and mitigate the risks facing our business.

Turn to page 42
for more information

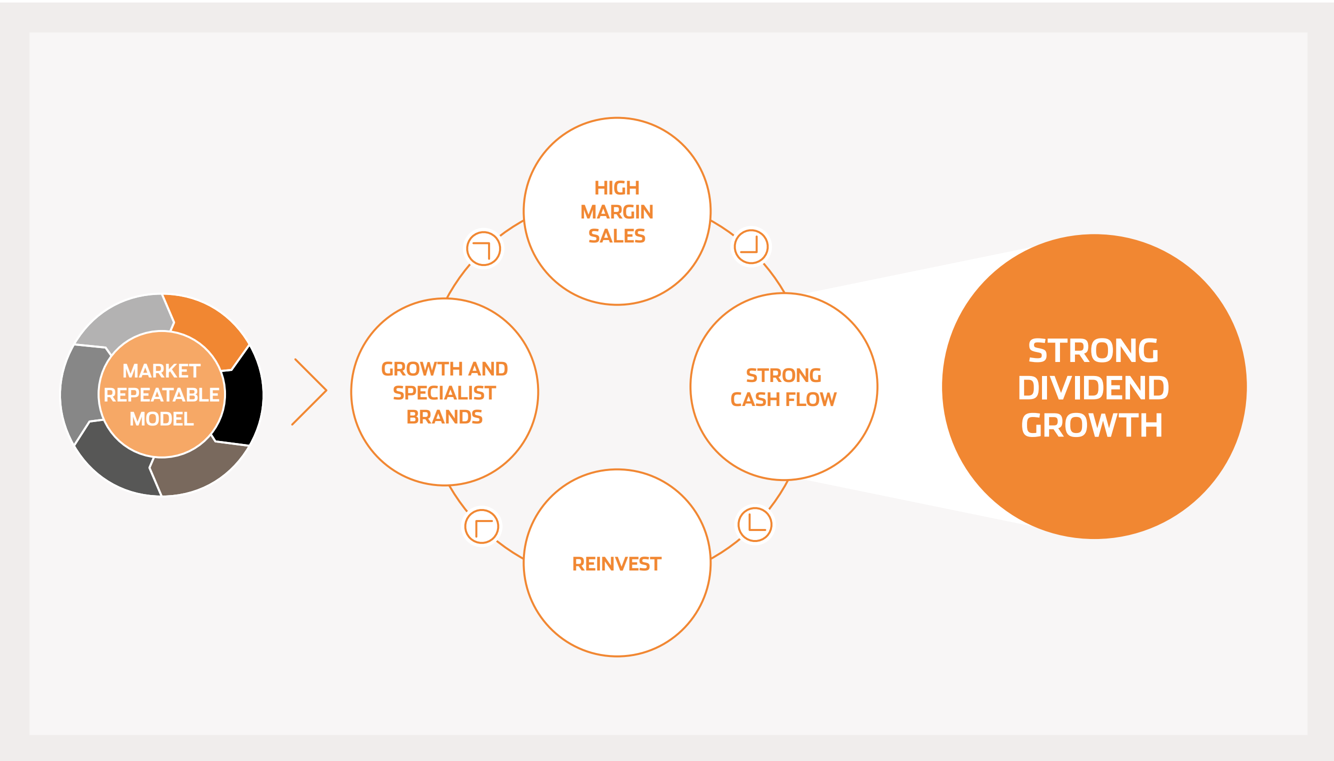
REWARDING SUCCESS

Our people are rewarded fairly and incentivised to deliver our strategy.

Turn to page 52
for more information

BUSINESS MODEL

Our business model illustrates how we create value for shareholders. Consistently applying our Market Repeatable Model to our portfolio drives the performance of our Growth and Specialist Brands. This, combined with effective cost management, delivers quality sales with high operating margins and generates the strong cash flows that are a hallmark of our business. We use this cash to reinvest to support growth, pay down debt or return to shareholders through dividends, which we are committed to growing by at least 10 per cent a year over the medium term.



MARKET REPEATABLE MODEL

As part of the review of our strategy last year we affirmed the capabilities required for delivering long-term quality growth based on our experiences, successes and learnings in key markets. These capabilities were codified into our Market Repeatable Model (MRM) to create a simple, effective and consistent operating framework, building on the Sales Growth Drivers we had been using in the business for many years. All six elements of the MRM are applied together in markets to deliver quality growth across our brand and product portfolio, both in tobacco and related consumer adjacencies such as e-vapour. Find out more over the page.

MARKET REPEATABLE MODEL

Our Market Repeatable Model has become an integral component of our strategy, strengthening our ability to maximise the performance of our brands and markets. All six elements of the model are holistically applied to deliver quality market share growth.

SIMPLE MARKET FOCUSED PORTFOLIO

Our Market Repeatable Model starts with a simple market focused portfolio that is built around an optimal number of brands and stock keeping units that are aligned with consumer needs. Our strongest assets are our Growth and Specialist Brands and we focus on driving their performance to generate quality market share growth.

SUSTAINABLE BRAND INVESTMENTS

Our simple portfolios drive a sharper focus on investments, as the lack of complexity makes it easier to prioritise investment behind our Growth and Specialist Brands. We build brand equity through a regular drumbeat of targeted initiatives, including above-the-line and point of sale advertising and consumer activations to create brand awareness.

ALWAYS ON PRICE STRATEGY

The third element of this dynamic growth model is about the pricing of our brands. We make sure that all markets across our geographic footprint develop and implement a consistent pricing strategy for their portfolios and continually monitor our operating environment to ensure that the pricing of our brands remains competitive.

CORE RANGE EVERYWHERE, ALL THE TIME

Ensuring the core range of our brands is always available is crucial for building consumer loyalty. We make sure that the right brands are available in the right outlets at all times. This targeting is enabled by the simplicity of our portfolios, which are welcomed by retailers as they have less complexity to deal with and enjoy lower working capital.

TAILOR CUSTOMER SOLUTIONS

In a continually evolving regulatory environment, retailers are an increasingly important part of the shopper brand purchasing experience. We focus on developing strong retail partnerships, creating tailored customer solutions that provide retailers with real commercial benefits and encourage them to become advocates for our brands.

HONEST ACCURATE LEARNING

The final step of the model is about continuous improvement through honest and accurate learning. Markets measure their performance against agreed metrics and learnings are shared with the wider business. This includes being honest, both when things go well and when things do not turn out as planned, ensuring we build capabilities, improve together and continually optimise the model.

HOW WE MEASURE OUR PERFORMANCE

We use key performance indicators and the supporting metrics in the Operating Review to measure the progress we make in delivering our strategy. These measures reflect our priorities and are used to monitor and drive business performance.

RETURN ON INVESTED CAPITAL (%)

PERFORMANCE
Return on invested capital increased to 14.3 per cent, underlining our continued focus on capital discipline.

DEFINITION
Return on invested capital measures the effectiveness of capital allocation and is calculated by dividing adjusted net operating profit after tax by invested capital. Invested capital is reported equity adding back amortisation of intangibles and adjusting back to foreign exchange rates at the time of relevant acquisitions.

ADJUSTED EARNINGS PER SHARE[1] (PENCE)

PERFORMANCE
Adjusted earnings per share rose by 7 per cent but declined by 2.2 per cent on a constant currency basis.

DEFINITION
Adjusted earnings per share represents adjusted profit after tax attributable to the equity holders of the Company divided by the weighted average number of shares in issue during the period, excluding shares held to satisfy employee share plans and shares purchased by the Company and held as treasury shares.

MAXIMISING SHAREHOLDER RETURNS

STRENGTHEN PORTFOLIO

GROWTH BRAND VOLUMES[1] (BN)

PERFORMANCE
We continued to focus on driving the performance of our Growth Brands, increasing volumes by 5.5 per cent and market share by 80 basis points.

DEFINITION
Volumes are measured on a stick equivalent basis to reflect combined cigarette and fine cut tobacco volumes.

DEVELOP FOOTPRINT

TOBACCO NET REVENUE[1] (£BN)

PERFORMANCE
Tobacco net revenue declined 2.6 per cent on a constant currency basis and increased 8.2 per cent at actual rates. Sixty-three per cent of tobacco net revenue is now generated by our Growth and Specialist Brands, up on last year, reflecting our focus on quality growth.

DEFINITION
Tobacco net revenue comprises tobacco and Fontem Ventures revenue less duty and similar items, excluding peripheral products.

1. KPIs used as bonus and LTIP performance criteria for Executive Directors. See Remuneration Report on page 52 for more information.

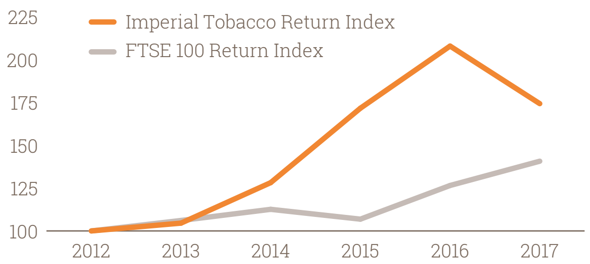
DIVIDEND PER SHARE (PENCE)

2017	170.7
2016	155.2
2015	141.0

PERFORMANCE
Dividend per share increased by 10 per cent for the ninth consecutive year.

DEFINITION
Dividend per share represents the total annual dividends being the sum of the paid interim dividend and the proposed final dividend for the financial year.

TOTAL SHAREHOLDER RETURN[1]



PERFORMANCE
Over a five year period we have outperformed the FTSE 100 but underperformed by 27 per cent in 2017. With dividends reinvested, £100 invested in Imperial Brands in 2012 would now be worth £174 compared with £155 if invested in the FTSE 100 Index.

DEFINITION
Total shareholder return is the total investment gain to shareholders resulting from the movement in the share price and assuming dividends are immediately reinvested in shares.

MAXIMISING SHAREHOLDER RETURNS

COST OPTIMISATION

TOBACCO OPERATING MARGIN (%)

2017	46.3
2016	46.9
2015	46.3

PERFORMANCE
Our focus on cost optimisation has resulted in consistently strong tobacco operating margins.

DEFINITION
Tobacco operating margin is adjusted operating profit divided by tobacco net revenue expressed as a percentage.

CAPITAL DISCIPLINE

CASH CONVERSION RATE[1] (%)

2017	91
2016	95
2015	97

PERFORMANCE
Strong cash generation and effective working capital management delivered cash conversion above 90 per cent for the fourth consecutive year.

DEFINITION
Cash conversion is calculated as cash flow from operations before interest and tax payments less net capital expenditure relating to property, plant and equipment, software and intellectual property rights as a percentage of adjusted operating profit.

OUR OPERATING ENVIRONMENT

Although tobacco volumes continue to decline year-on-year the value of the world tobacco market remains significant at around US$770 billion, with around a billion adult smokers consuming more than five trillion cigarettes a year.

OUR GEOGRAPHIC FOOTPRINT

Our operations extend across a broad spread of markets, providing us with a balanced geographic footprint that supports our drive to deliver quality growth and sustainable shareholder returns.

The macro-economic environment continues to impact consumer spending in some territories and political instability, including Brexit, creates further uncertainty.

We are experienced at developing our business in challenging conditions and continue to focus on realising quality growth opportunities to create further value for shareholders.

REGULATING TOBACCO

The tobacco industry is one of the most highly regulated in the world.

Regulation is largely driven by three organisations: the World Health Organization (WHO, through the Framework Convention on Tobacco Control, the FCTC), the USA's Food and Drug Administration (FDA) and the European Commission (through the European Union Tobacco Products Directive, the EUTPD).

During the year the FDA said it would begin public dialogue about lowering nicotine levels in cigarettes as a way of transitioning smokers to 'alternative and less harmful' sources of nicotine and we look forward to taking part in this dialogue.

We encourage regulators to draw on our expertise when they are considering regulation and oppose attempts to exclude tobacco companies from the ongoing debates about our industry and our products.

We support reasonable regulation, especially when it aims to reduce illicit trade and prevent children smoking. We also support appropriate ingredients disclosure and ensure that our products display written health warnings.

We oppose disproportionate regulation, such as legislation that seeks to ban smoking in public or private places, plain packaging, pictorial health warnings and bans on the display of tobacco products in retail outlets.

We market and sell our products responsibly and adhere to regulation at all times, wherever we do business. Our International Marketing Standard (IMS) sets out clear rules and principles to ensure our advertising and marketing is only ever aimed at adult smokers across the world. The IMS applies to all our employees, as well as the agencies who work with us, and is published in full on our corporate website www.imperialbrandsplc.com

ILLICIT TRADE

Every year around 500 billion illegal cigarettes are consumed, depriving governments of around £30 billion in taxes.

The smuggling and counterfeiting of tobacco has considerably wider impacts: children can more easily obtain cigarettes, consumers are deprived of the quality they associate with their favourite brands and the livelihoods of independent retailers are threatened.

We apply stringent controls to our distributors and have a dedicated team of specialists leading our anti-illicit trade initiatives.

We invest in systems with law enforcement agencies to improve the security and traceability of our products and share intelligence to help disrupt the supply of illegal cigarettes.

We also talk to governments to highlight the scale of the problem and encourage them to recognise how high tobacco taxes and extreme regulation can fuel the growth of illicit trade.

NEXT GENERATION PRODUCTS

Next Generation Products (NGP) provide smokers with alternatives to combustible tobacco and are broadly divided into two categories: e-vapour products and heated tobacco products.

E-vapour is by far the largest and most developed opportunity within NGP. It is estimated that sales of e-vapour products (EVPs) are currently worth around $4 billion a year and could be worth more than $30 billion by 2020.

E-cigarettes are the most common EVPs and we are represented in this category by blu, which has strong positions in the USA and UK – the world's two largest e-vapour markets – and is managed by our subsidiary Fontem Ventures.

Fontem Ventures has its own stringent marketing standards and ensures that all marketing activity is aimed solely at adult smokers who are seeking an alternative to tobacco. EVPs are not for children and Fontem actively supports bans on the sale of EVPs to anyone under the age of 18.

A growing number of regulators and public health bodies have concluded that EVPs are safer than cigarettes and therefore have a role to play in reducing tobacco-related disease.

The regulation of EVPs is evolving and we continue to engage with stakeholders to support the development of effective legislation.

Heated tobacco is a considerably smaller category but one that is growing, most notably in Japan. We do not currently sell these products but continue to monitor their development. This includes planning for the potential launch of our own heated tobacco products, should the category start showing broader signs of significant and sustainable growth.

Unlike EVPs, heated tobacco products contain tobacco and in our view should therefore be regulated and taxed as conventional tobacco products.

INVESTING FOR GROWTH

CREATING VALUE FOR SHAREHOLDERS

"This was an important year of progress in which we improved our share position in a number of priority markets. We invested significantly behind our Growth and Specialist Brands to deliver these results, creating a stronger platform for generating further quality growth in the years ahead."

ALISON COOPER
Chief Executive

Last year the Board and my senior leadership team conducted a review of our strategy to refine our priorities for growth over the next decade in tobacco and consumer adjacencies, including e-vapour.

A key element of our strategy is the simplification of our brand portfolio. By reducing the number of brands and stock keeping units, and prioritising our strongest equities, our Growth and Specialist Brands, we have created a more powerful portfolio that is delivering a higher quality of growth.

We increased investment in these brands by £310 million in the year, focusing spend in a number of areas including portfolio simplification, advertising and marketing, consistent pricing, our sales force and customer engagement. This higher level of support, aligned with the roll-out of our Market Repeatable Model, delivered market share gains in many of our priority markets and improved share trajectories in others. Growth Brands performed well, outperforming the market with volume growth and a share gain of 80 basis points. We also continued to make good progress in e-vapour, further building our capabilities and consumer insights in preparation for an enhanced programme of activity in 2018.

The increased investment in our brands impacted full year revenue and profit, while supporting a stronger second half revenue and share performance in a tough industry environment. It has also strengthened the business to support improved top-line growth over the medium term.

The drive and commitment of our people have been integral to the delivery of these results and I would like to thank everyone for their hard work and continued support.

MARKET REPEATABLE MODEL: OUR FOCUS FOR GROWTH

Our investments were aligned behind our Market Repeatable Model. This model builds on the success of the Sales Growth Drivers we have been using in the business for many years and provides a structured framework for quality growth that is being deployed across our markets.

The six elements of the model ensure that wherever we operate we always have: a simple market-focused portfolio, sustained brand investments, a consistent price strategy, a focus on maximising the availability of our core range, tailored customer solutions and honest and accurate learning mechanisms. How each section is applied in our markets is explained on page 7.

Our investments supported all six elements of the model, strengthening our ability to maximise the performance of our brands in market.

STRENGTHENING OUR PORTFOLIO: EXCELLENT RESULTS FROM GROWTH BRANDS

Streamlining our portfolio has not only improved our quality of growth, it has also substantially cut the level of complexity and cost in the business.

The core principle behind the reshaping of our portfolio has been to reduce the number of weaker Portfolio Brands through migrations and delistings, while driving the performance of our Growth and Specialist Brands.

As a result we have consistently increased the contribution that Growth and Specialist Brands make to our success and in doing so, we have steadily improved our quality of growth. These brands now deliver around 63 per cent of the Group's tobacco net revenue and our target is for them to eventually account for 75 per cent.

During the year we migrated multiple Portfolio Brands into Growth Brands in a variety of markets. We also began rolling out a more radical portfolio simplification exercise to reduce complexity and improve on-shelf availability of our brands in Russia, France, Germany, Italy, Spain and Australia, with other markets to follow.

Our Growth Brands delivered good results, with the performance of JPS, West, Winston, Davidoff and Gauloises Blondes benefiting from higher investment in a range of priority markets, including the UK, Germany, Italy, Japan, Australia and the USA.

This was complemented by strong revenue growth from a number of our Specialist Brands, including Skruf in Scandinavia, Backwoods in the USA and Premium Cigars in a number of markets.

NEXT GENERATION PRODUCTS: EXPANDING OUR POSITION

Next Generation Products (NGP) offer considerable growth opportunities and we will be significantly stepping up our level of activity in 2018, expanding our portfolio with new product launches in new and existing markets. This is building on the strong foundations and capabilities we have established over recent years.

E-vapour remains our priority; in our view this is by far the largest NGP opportunity and we believe it offers the greatest current potential for long-term sustainable growth.

In blu, we have one of the best e-vapour brands in the world and we continue to focus on improving the consumer experience. Vaping technology is continually evolving and in October 2017 we substantially enhanced our technical capabilities with the acquisition of the e-vapour innovation business Nerudia.

During the year we also continued to secure intellectual property royalties from companies using our first generation technology.

Heated tobacco is currently a much smaller NGP category that is growing, most notably in Japan. While our investments will continue to be focused on supporting e-vapour we have developed options in heated tobacco which can be deployed if we see broad-based sustainable growth developing and we will begin consumer trials of our own heated tobacco products in December 2017.

IMPERIAL BRANDS AND CHINA TOBACCO

In January we announced a long-term joint venture business with China Tobacco, aimed at developing growth opportunities in China and international markets.

China is the world's largest tobacco market, with annual volumes close to 2.5 trillion cigarettes.

The joint venture, Global Horizon Ventures Limited (GHVL), is based in Hong Kong and is focused on:

- leveraging the expertise of China's largest tobacco company, Yunnan Tobacco, to drive the sustainable development of our Growth Brands West and Davidoff in China
- maximising the potential of two Yunnan Tobacco cigarette brands, Jadé and Horizon, in markets outside of China

An early focus for GHVL was the migration of Style to Jadé. This was successfully completed and Jadé is now one of our Specialist Brands.

We have been very encouraged by the performance of GHVL in the first nine months of operation and believe that over the coming years, the joint venture has the potential to deliver additional meaningful Growth Brand volumes.

As well as driving the performance of the four cigarette brands, GHVL will also be evaluating other tobacco and Next Generation Product launches, along with potential merger and acquisition opportunities.

The joint venture builds on a track record of co-operation between Imperial and Yunnan Tobacco, which began in 2003.

DEVELOPING OUR FOOTPRINT: DRIVING SUCCESS IN PRIORITY MARKETS

We delivered a number of good performances in priority markets across our geographic footprint.

Our successes in Growth Markets included strong share gains in Japan, Saudi Arabia, Italy and Russia. In China, the world's largest tobacco market, we have been very encouraged by the performance of our new joint venture with China Tobacco.

ITG Brands delivered another strong performance in the USA, underpinned by volume and share gains from our Growth Brand Winston and our Specialist Brand Kool, offset by declines in our defocused Portfolio Brands. In addition, our mass market cigar business continues to perform well following last year's changes to our route to market.

In Returns Markets we achieved share increases in three of our most important markets, the UK, Germany and Australia, complemented by additional share gains in other markets including Poland and Portugal. We also delivered improved share trends in France and Spain.

COST OPTIMISATION AND CAPITAL DISCIPLINE: NINTH YEAR OF 10 PER CENT DIVIDEND GROWTH

Effective cost and cash management supports our strategy by improving efficiencies and releasing funds to fuel growth.

We made good progress with our two cost optimisation programmes. The first programme will deliver annual savings of £300 million from the end of the 2018 financial year. The second programme will deliver a further £300 million of savings from the September 2020 financial year.

In 2017 we realised total savings of £130 million through a range of initiatives that are reducing complexity and enhancing the way we operate.

Strong cash flow is a hallmark of our business and we use this cash to reward our shareholders, invest in the business and pay down debt.

Cash conversion remained strong at 91 per cent and we grew the dividend per share by 10 per cent for the ninth consecutive year.

In September we sold 13,275,000 shares in our European distribution business Logista, reducing our stake by 10 per cent to approximately 60 per cent of Logista's issued share capital. The sale raised around £220 million, which has been used to buy back shares in Imperial Brands and reduce net debt.

OUTLOOK: PRIORITISING VALUE CREATION OPPORTUNITIES

The execution of our strategy has resulted in a stronger and more focused portfolio and footprint, which we have invested behind to deliver improving share performances in priority markets. Central to this has been the embedding of our codified Market Repeatable Model, which provides a structured approach for generating sustainable quality growth.

We will build on this momentum in the coming year and will continue to take necessary actions to protect our investments and deliver quality revenue growth in tobacco.

We will also be further enhancing our presence in Next Generation Products. We have added to our innovation capabilities and will be launching new e-vapour products in new and existing markets, as we look to realise the significant growth opportunities that e-vapour offers.

As always, our focus on driving the performance of our brands and products will be supported by our diligent approach to cost, capital discipline and cash management.

In the context of a volatile industry environment and our continued commitment to investing behind our tobacco and next generation products businesses, we are targeting delivery of constant currency revenue and earnings per share growth within our medium-term guidance.

We have the strategy and people to succeed in a challenging and changing world and will continue to prioritise opportunities that sustainably create value for our shareholders.

ALISON COOPER
Chief Executive

WHY INVEST IN IMPERIAL BRANDS?

Imperial Brands offers a clear proposition to investors, built around four key benefits: the attractiveness of our brand portfolio and geographic footprint, simplification and cost efficiencies, strong cash conversion and annual 10 per cent dividend growth.

INVESTING FOR QUALITY GROWTH; BRANDS, PRODUCTS AND MARKETS WITH LONG-TERM PROFIT POTENTIAL

INVESTING FOR QUALITY GROWTH

Imperial Brands has an attractive portfolio of brands and markets which can deliver long-term profitable growth.

Our strategy is to strengthen our tobacco and non-tobacco portfolio by generating an increasing proportion of revenue from our strongest brands, while also prioritising our investment in those markets and products that offer the best returns.

Over many years we have had a proven track record of achieving strong price/mix growth to offset industry volume declines and enhance profitability. We are also investing in non-tobacco products and experiences through our subsidiary, Fontem Ventures, to deliver future growth opportunities alongside our tobacco business.

VALUE CREATION SUPPORTED BY SIMPLIFICATION AND COST EFFICIENCIES

SIMPLIFICATION AND COST EFFICIENCIES CREATE VALUE

Our strategic agenda means we are changing the way we operate to strengthen the business and improve our quality of growth.

Simplification and focus are at the heart of our new ways of working, as we reduce complexity and instil a more cost-conscious culture. We are also adopting lean principles through continuous improvement in everything we do.

This provides opportunities to reduce costs, improve effectiveness and create a more agile organisation that can drive consistent returns for shareholders in an ever changing world.

91% CASH CONVERSION

STRONG CASH GENERATION

Our business generates strong cash flows as a result of our intrinsically high operating profit margins, coupled with our ability to convert a very high proportion of these profits to cash.

Over recent years we have improved our cash conversion by reducing our working capital and prioritising our investments more effectively. Our current focus for our cash resources are: investment in our priority brands and markets, supporting double digit dividend growth for shareholders and reducing our net debt.

10% DIVIDEND GROWTH PA OVER MEDIUM TERM

ANNUAL 10% DIVIDEND GROWTH OVER MEDIUM TERM

A core part of our investment proposition is our commitment to grow the dividend by at least 10 per cent per annum over the medium term. This is a commitment we have now achieved for nine consecutive years.

Our ability to improve profitability and generate strong cash flows will enable us to continue to deliver this income growth to our shareholders.