

Sanford Bernstein Conference 2011

21 September 2011

Alison Cooper, Chief Executive Sanford Bernstein 2011 Conference

Hello and welcome to the Imperial Tobacco Group presentation at this year's Sanford Bernstein conference.

Unlocking Our Potential

My name is Alison Cooper, Chief Executive of Imperial Tobacco.

The theme of my presentation today is "Unlocking our Potential".

Over the past two years we have enhanced our focus on sales growth and are building momentum behind the top line.

In my presentation today I will be looking at examples of how we are delivering against our top line objectives and how we see opportunities to further unlock our potential and deliver high quality sustainable earnings growth.

Our Strategy

Our strategy will be familiar to most of you by now, comprising sales growth, cost optimisation and cash utilisation, which all drive to deliver sustainable shareholder returns.

Sales growth sits at the heart of the strategy, supported by our key assets, particularly total tobacco, as well as our core capabilities.

I introduced the 4 growth drivers at our investor day in July this year and I will talk about these in more detail later in this presentation.

HY11 – Delivering Our Strategy

We are driving growth through total tobacco and as we saw at the half year we're making gains across our market footprint.

We made gains in EU and non-EU markets with volumes of our global strategic cigarette brands and fine cut tobacco both up five per cent.

Our disciplined cost management resulted in margins increasing despite investing for growth and our focus on effectively managing our cash created further value for shareholders.

Unlocking Our Potential

How do we move to the next step and unlock our true potential?

It's about changing our mindset – seeing things differently, doing things differently, different to the industry, different to how Imperial has approached things in the past.

Seeing things differently includes developing a deep understanding of what drives consumers, and how we can translate these consumer insights into opportunities for our total tobacco portfolio.

Doing things differently is about delivering execution excellence through fewer, bigger and better initiatives that will accelerate sales growth.

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Sales Growth Drivers

To do this we have identified the four sales growth drivers at which we want to excel:

Firstly portfolio management – this is about our total tobacco focus; leveraging this unique asset to maximise our share of consumers and consumption – more consumers, more occasions.

The second driver is innovation. We are building on our existing innovation pipeline to create a bigger pipeline of scalable consumer-needs based innovations to expand our portfolio and accelerate incremental growth.

Next we have customer engagement. This is about developing a deeper understanding of customer and shopper needs as a basis for customer management. It's about optimising the availability and advocacy of our brands and products.

And finally, the fourth driver is about pricing and includes our excise strategies in individual markets. This is not just about price increases, it's about developing a better approach to pricing by brand, by pack and by channel to maximise revenue growth.

Our Key Enablers

Our success in these growth drivers will be supported by how well we perform these three areas which we call our enablers:

The first enabler is consumer insight and foresight, this is an essential pre-requisite for growth, we will continue to engage with consumers, understanding their needs, decoding their behaviours to take the business in the right direction, aligned with and fulfilling consumer needs.

Operation and Supply alignment is a core part of our focus on execution – using our agility to bring ideas to market efficiently and effectively.

And finally, shaping our environment, this is an area in which we've always been proactive, proactive in defending the tobacco industry, and increasingly, proactive in defending our consumers.

Maximising Shareholder Returns

Here you can see how these elements come together to maximise shareholder value.

The four growth drivers are supported by our key enablers to deliver sustainable sales growth and that sales growth drives high margins. These margins generate strong cash flows, which we use to maximise returns and reward our shareholders whilst also reinvesting in the business.

Sales Growth Drivers – Portfolio Management

Let me explore the four growth drivers with you in more detail.

As I touched on earlier, portfolio management is about taking advantage of our total tobacco portfolio to increase our share of consumer consumption.

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More Consumers, More Occasions

Our total tobacco approach is unique to Imperial – it's a key advantage in driving sales growth.

It means we have more consumers in more markets, with more consumption occasions, as well as benefitting our relationships with the trade.

It means we see growth in every market. We cover all the bases and there are opportunities in all markets on which we can capitalise.

Total tobacco is also key to risk mitigation – we have a broader portfolio to work with and to innovate with as consumers are impacted by regulation and the economic environment. Our strong relationships with the trade, in part driven by our total tobacco approach, mean we are very well placed in highly regulated environments.

Same Consumer, Multiple Needs for Multiple Occasions

Delivering sustainable sales growth is not just about having the assets. It's about how you apply and deploy them.

Each consumer is different, each has different needs, and these needs can vary based on any given scenario.

In this slide we have one individual, but viewed in many different scenarios, some formal, some informal, some with a few friends, some with many friends, and some where he is alone.

His clothes differ, his choice of drink differs, his needs differ based on the given set of circumstances.

This is typical of all consumers and presents an opportunity for all FMCG companies to develop a portfolio of products that can target multiple needs, behavioural opportunities as well as motivational opportunities, and our total tobacco portfolio and consumer insight gives us a significant advantage.

Davidoff in 2006

We are in a great position to use our capabilities to drive further growth in the future, but we have already been very successful.

Let's look at Davidoff; Davidoff is still a young brand relative to other global tobacco brands, having been launched in the mid-1980s.

Prior to 2006 Imperial owned limited tobacco licensing rights to the Davidoff brand and Davidoff had a light presence within only a few product segments.

Davidoff Today

In August 2006, we acquired global tobacco licensing rights, allowing us to execute a strategy that has led to the development of new and exciting variants across a full spectrum of segments.

In doing so, the brand has grown within growing segments in markets such as Taiwan, Russia, Ukraine, Azerbaijan and Saudi Arabia, and its premium pricing has provided significant profitability to the Group.

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Davidoff Volume Growth

As a result of this investment, we grew Davidoff global cigarette volumes at a compound annual growth rate of 6 per cent in the five years to 2010.

Davidoff is well suited to our focus on consumer needs-based portfolio management, and given its relative youth to other global brands, we are confident there is significant growth to come for this brand.

Habanos Growth

We have also been actively managing our portfolio within our luxury cigar portfolio.

Whilst many smokers have been seeking value, those smokers who appreciate luxury cigars are being attracted to some of the exclusive editions developed within our Cuban Habanos range. These were a key driver of our 16 per cent sales growth in Habanos volumes outside the EU in HY11.

Dynamic German Portfolio

If I talk now about the value end of our portfolio.

Germany is a good example of how we have managed our portfolio to maximise opportunities within fine cut tobacco and the value to low price cigarette segments. These segments have been the growth segments over the past few years and collectively accounted for 64 per cent of the German market stick equivalents in FY10, as shown by the chart on the left.

The second chart illustrates that, by developing some of our key brands both within cigarette and fine cut variants, we grew our stick equivalent share of the sub-mid price cigarette and fine cut tobacco segments by almost 200 basis points between FY06 and FY10, and we expect this strong momentum to continue.

JPS Stick Equivalent Volumes

A key driver of this growth in Germany has been JPS which grew total stick equivalent volumes on a compound annual basis by 14 per cent in Germany and 11 per cent at a total brand level between FY06 and FY10.

Poland Portfolio Success

Poland is another market where we have demonstrated how our agile portfolio management has responded to consumer demands and maximised growth.

The chart on the left illustrates how stick equivalent volumes of value cigarettes and fine cut tobacco remained above 60 per cent of the market in 2010, whilst the chart on the right shows how we have increased our share of these segments by approximately 560 basis points.

Our success has been largely driven by our fine cut tobacco share which grew from 3.2 per cent in FY09 to be 28.6 per cent in FY10 and almost 55 per cent in HY11.

Route 66 Stick Equivalent Volumes

This outstanding share growth is predominantly due to the success of our Route 66

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brand, which grew stick equivalent volumes by 34 per cent on a compound annual growth rate basis in Poland alone and 41 per cent at a total brand level, between FY06 and FY10.

Sales Growth Drivers - Innovation

The second growth driver is innovation. We are building on our existing innovation pipeline and will develop a broader set of scalable consumer-needs based innovations, looking to expand our portfolio and accelerate incremental growth rather than simply replacing existing formats.

Incremental Growth Pipeline

We already have a selection of innovations that have been delivered into markets, and as you can see, we have made good progress since April of this year.

The key now is to build and manage a very strong pipeline so that we generate more ideas, bring more into feasibility phase, and have more developments that make it to market.

By executing this approach, we will build more consumer-lead ideas, bring more products to market.

High Return Innovation Model

Historically, the mindset of the industry towards innovation has been to focus on making product feature improvements, often based on technology, and to feed growth by replacing slow moving products with newer fresher products. This can be a costly exercise and one that restricts the ability to drive incremental growth.

At Imperial we are focussed on meeting the needs of consumers by working with consumers. We aim to deepen our understanding of what drives consumer choice and then manage and develop our category and brand portfolio to ensure we maximise our share of consumption, and we have a total tobacco portfolio and an extensive market footprint with which to do so.

Exploiting Scalable Innovation

We intend to be the best at consumer insights based innovation, and an excellent example of this is the new patented GlideTec pack.

This innovation really creates a wow factor – it stands out for consumers who are intrigued, curious, think it's smart and want one.

This pack is based on the consumer insights of “sociability of smoking”, and the ability to offer a cigarette with a one-hand motion.

The Consumer research on this has been some of the most positive we have ever seen. We have launched this pack in selected accounts in the UK since end of April and the results have been tremendous, confirming our expectations for share, volume and margin growth.

Innovation Within Value Segment

Our GlideTec initiative not the only recent innovation to go to market.

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As I mentioned earlier, our JPS brand has been very successful in markets such as Germany, and much of this success is driven by our innovations with this brand.

One such innovation launched just this month is the new JPS round pack. It is the only pack we know of that has these dimensions, which are in tune with the brand's attribute of modernity and creativity.

West Fusion in Russia

We have proven that we don't always have to be first to market with new innovations in order to grow sales. Our business is agile and our ability to respond quickly to changing market trends is one of our competitive advantages.

We are able to introduce innovation to all parts of our portfolio, from our luxury cigar and premium cigarette brands to our value cigarette and fine cut.

A good example of recent fast follower success is the growth of West Fusion in Russia's king sized super slim segment.

West's share of this growing segment reached 3 per cent in September 2010 having been launched just 12 months prior, and volumes for the nine months to June 2011 have grown 150 per cent on the same period last year.

Sales Growth Drivers – Customer Engagement

Moving to the third growth driver – customer engagement.

This is about a deeper understanding of customer and shopper needs as a basis for enhanced customer management.

By building on our understanding of specific shopper profiles, channel trends and market environments, we can tailor a route-to-shopper proposition that will best meet the needs of the consumer and retailer.

Morocco RTM Strategy

Our Moroccan business is an excellent example of how we have developed customer-centric solutions that generate benefits for us and our customers.

The monopoly in Morocco ended in January 2011. In order to maintain our strong position, our team implemented a new business strategy last year focussing on 5 key points, the first of which was to create a route to market system.

By placing the retailer firmly at the centre of our strategy, we changed from a model that relied solely on 27 Cash & Carry's offering the retailer a supermarket-like shopping experience to a free door-to-door delivery service utilising only 19 order preparation sites.

To strengthen our sales and marketing activity, a telephone sales centre was created in Casablanca to take orders and influence the retailers' choice of purchases.

The result is that we have stronger relationships with our retail customers as evidenced by our growth in cigarette market share in HY11 to 83.9 per cent despite the more competitive market conditions.

Outperforming in Dark Markets

Imperial has invested significantly in the development of its sales forces and we measure their performance growth across 30 markets worldwide.

The litmus test of our effectiveness in driving customer engagement is of course in dark markets and this chart demonstrates that in the darkest markets – like Australia and Norway – we are growing market share.

Our clear focus across display ban markets has been on:
optimising the portfolio;

- aligning call frequency to influence outlets;
- ensuring on-shelf availability;
- ensuring on-shelf availability;
- trade investment; and importantly
- education programs for our sales forces and customers.

As you can see this is paying off with share gains in Australia where our MAT share in HY11 was up 1.5 per cent despite last year's 25 per cent tax increase, and in Norway where our snus and FMC shares were up 1.1 and 0.3 per cent respectively.

Sales Growth Drivers - Pricing

Our fourth key growth driver, pricing, or more specifically, how we use all aspects of pricing to maximise our revenue growth.

Clearly pricing is a major value creation driver in tobacco, more so than other FMCG industries and, despite occasional price skirmishes, this driver is very much intact with 2011 estimated pricing benefits being well ahead of 2009 and just under 2010.

Enhancing Our Capabilities

This growth driver incorporates our strategies on excise management, as well as focusing on how we can best use pricing across the multiple sales channels.

By enhancing our ability to model various scenarios and deepening our market and consumer insight, we aim to identify segmented opportunities where we can create consumer value, and then develop tailored sales solutions to capture these profitably.

By abandoning a one-size-fits-all approach, we can place selected brands and products in specific channels and differentiate our pricing to reflect how effectively we satisfy our consumers' needs.

Many examples exist throughout Imperial. For example, in the UK we introduced the 10-pack Lambert & Butler which caters for those who trade up to an L&B for a night out.

In Germany, we offer German consumers who seek value the ability to purchase larger pack sizes containing more cigarettes. This reduces the price per stick when compared to a pack of 19s and has proved very popular as evidenced by our competitors following with similar offerings.

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Pricing Strategy Drives Growth

Managing pricing proactively and reactively is about capabilities in analytical skills and the application of specific tools.

By developing a common framework and toolbox, we will widen and deepen our capability across our market footprint, but clearly we have “pockets of excellence” we can leverage.

For example, in Australia we developed an analytical tool that gave us a deeper understanding of price elasticities by individual brand. Using this tool led us to strategically reposition our Horizon brand, which resulted in a sharp turnaround in the brand’s market share trend. This was a key driver behind the growth in our overall market share in Australia of 1.5 per cent in HY11.

Another example is here in the UK where we analysed the relationship between brand prices and share in more detail. Our insight led us to increase the price of Windsor Blue relative to its previous benchmark of Sterling.

As you can see in the chart on the right, Windsor Blue market share has been boosted, as has this brand’s profit contribution, whilst Sterling share has begun to decline.

Sales Growth Drivers

Having looked at our four key sales growth drivers I would like now to close by talking about how sales growth translates into maximum returns to our shareholders.

Maximising Shareholder Returns

Maximising shareholder returns is about growing the business, maximising our cash flow, and successfully redeploying that cash.

We have identified the critical sales growth drivers and we know the enablers that are best used to drive sales growth.

From that revenue growth, our high gross margins and efficient operations will drive cash flow growth, which we will reinvest in the business while also managing the capital we deploy to further maximise returns and reward our shareholders.

We have demonstrated our ability to drive growth through total tobacco, particularly within growth segments, and there are growth segments in all markets. By focussing on the things I have mentioned today, we see opportunities to further unlock our potential and deliver high quality sustainable earnings growth.

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Thank you for your attention. I would now like to invite any questions.