# Investor Day Presentation

12 July 2011

## Arthur van Benthem – Group Sales Director

## Unlocking Our Potential – Fewer, bigger, better execution

Thank you and good morning everyone.

As you know Roberto and I are both new to this company and we have a very similar FMCG background, we speak the same FMCG language, bring a new/fresh perspective to Imperial Tobacco.

Whereas Roberto brings a new mindset to our Tobacco business, my job is to build a skill set to do things differently across our markets and focus on “fewer, bigger, better” sales execution.

But before I proceed with my section, a few words to introduce myself.

## My Journey

I have lived and worked in eight different countries across Europe and Asia/Pacific.

I completed a Masters degree in business administration at the Rotterdam School of Management in the Netherlands before joining Unilever where I worked for several years in various sales and marketing roles.

I left Unilever and joined the Coca-Cola Company where I worked mostly in Managing Director roles within Asia-Pacific for more than 11 years.

I returned to the Netherlands five years ago to become Chief Operating Officer on the board of a dairy company and helped create Friesland Campina as a global challenger to Danone.

Shortly after joining Metro as Chief Customer Officer on the board in Germany, I received a call that led me to join Imperial, and here I am.

Since joining Imperial, I have been extremely impressed by the Group’s opportunity for growth as well as the quality of the leadership team. I am particularly excited because my role allows me to help shape a new “sales growth” future in an industry with significant headroom for growth, in a company with a true challenger culture, free from restrictive bureaucracy that you often find in companies of this size.

## Unlocking Our Potential

Let me share some key observations from my first four months on how Imperial executes its sales growth strategy:

- I see organic volume growth that outperforms the peer group, Imperial has in fact outperformed the peer group over the last 5 years;
- I see significant expansion of the global and international brand portfolio, strategic and international brands are now a very significant third of our total volume and growing volume by 2% every year;
- I see share growth, within EU and Non-EU markets, and in key growth segments such as lights, menthol and new formats; and finally
- I see a continued positive pricing trend despite significant events like Spain. The current 2011 expected pricing benefit is well ahead of 2009 and just under that for 2010

So where do I see the opportunity?

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You have heard Roberto talk about a new way of looking at tobacco, a new mindset, an FMCG mindset and strategies to pursue growth, and clearly, the best strategies only succeed with excellent execution.

Therefore, my agenda is to talk to you about a fresh new perspective on doing things differently going forward - and specifically:

- How we are investing in growth, with a focus on executing fewer, yet bigger and better initiatives;
- Give more context regarding the four sales growth drivers that we have prioritised to be the best at; and lastly
- Talk about how we engage with customers by leveraging our insights into customer and shopper needs.

## Unlocking Our Potential

So we will go straight into the first topic: investment in growth drivers with fewer, bigger, better execution.

## Priority Sales Growth Drivers

Alison introduced these four sales growth drivers earlier this morning. These are the areas in which we want to be the best in the industry.

I want to briefly outline the picture of success in each of these, and give you an indication of the size of potential for Imperial.

Firstly, portfolio management is all about driving a consumer-centric brand portfolio that maximizes share of consumers' consumption.

We intend to develop a centrally-defined integrated strategic framework and toolbox rooted in deep consumer insights not only for global brands but also for regional and local brands across our Total Tobacco portfolio in cigarettes, fine cut tobacco, mass market cigars and smokeless.

This has the potential to accelerate our five-year CAGR volume growth performance.

Secondly, pricing is about the optimisation of brand, pack and price per channel as well as excise management to maximise revenue growth.

Again, we are developing analytical frameworks and toolboxes for proactive and reactive pricing strategies in a centre of excellence and build wide and deep local capability.

This has the potential to significantly accelerate our revenue growth performance.

Thirdly, innovation, which is about having a scalable consumer-needs based pipeline of game-changing innovations that generate incremental growth.

Innovation in the tobacco industry is still very driven by technology rather than the consumer. Herein lies a tremendous volume and margin opportunity that Roberto has spoken about. We can drive the fast rollout of proven concepts and scale these innovations into being truly global initiatives.

And lastly, customer engagement, which is about a customer centric route to market with a superior processes and best in class Trade Marketing. Our approach is to view existing out-of-stock levels as an opportunity, particularly for the company that gets this right. We believe the solution is not in a one-size-fits-all, van-selling, direct store delivery model, which is very expensive, but a route to market that is customer centric and maximises availability and customer advocacy, which is increasingly more critical in darkening markets. This has the potential to bring significant extra revenue from otherwise lost sales.

## Fewer, Bigger, Better Execution

I have mentioned “Fewer, Bigger, Better” quite a few times now. Let me land this concept with you.

Clearly, Imperial has an M&A background and whilst our acquisitions have been fully integrated we see significant growth potential for global strategy frameworks that allow a level of local implementation flexibility.

To that end, we have prioritized the four sales growth drivers and developed the following framework for creating competitive advantage:

- Fewer, this translates into “Focus”, do fewer things, apply real focus in all our markets on these four drivers, and nothing else;
- Bigger, this means “Scale”, fewer initiatives enables us to scale these initiatives more effectively, within and across markets; and
- Better, strong execution, delivering sustainable benefits as we become the best at what we do.

This framework outlines the discipline required to translate growth drivers into tangible sales growth.

## Reinvestment for Growth

Most of you will be familiar with our strategy slide where we outline our key assets, being brand equity, total tobacco, market footprint and our people. These assets are the key focus for us when looking to reinvest for future growth.

We use a very simple principle: make high quality investments to drive high returns. This is not a new principle for Imperial, but I see scope for an even more focused investment strategy across our market footprint.

To this end we have categorised countries into three areas with a specific role within the portfolio as their name suggests:

- Drive profit markets, largely EU;
- Drive share markets, largely non-EU; and
- Markets which are in transition, such as Spain and Greece

Although you will appreciate that I am not willing to give you more detail, this simple focus on maximising the role of specific geographies in our footprint ensures we allocate resources to get the biggest bang for our buck.

Furthermore, there is scope for further efficiency improvement of our A&P investment by driving return on investment from fewer, bigger and better initiatives. Just this year, this has enabled a re-allocation of A&P investments toward Russia, Ukraine and USA to increase 18% over last year.

But clearly A&P is just one type of investment in growth, and given tobacco regulation, it is not necessarily the most influential in driving sales.

We are also stepping up our investment in cost of sales, route to market, people, capacity and anti illicit trade (or AIT):

- We invest in COGS – to ensure we deliver on the consumer expectation for product quality
- We invest in our Route to Market – with significant increases in the size of our sales forces in Russia and the USA
- We are stepping up investment in people development – both in sales & marketing as well as our sales force
- We are stepping up investments in capacity – in fact we have doubled our growth capex in the last 2 years exploiting consumer demand shifts which require new cigarette making and packing machines
- And in AIT we invest in the OLAF agreement and major initiatives to stop illicit trade

To maximise the return on this focused investment, we felt we needed a more rigorous performance management program. To that end, we are creating a superior planning process that enables a focus on fewer, bigger, better initiatives across markets.

We have designed an operating model with clear roles and responsibilities to enable more consistent and rigorous performance management. This model aligns key knowledge, behavior and skills areas across the 4 key sales growth drivers.

We have also commenced with Quickscan of existing capabilities across the top 15 markets prior to the roll-out of a leadership development and organisation capabilities program, which should happen over the coming weeks.

## Fewer, Bigger, Better – Portfolio

Let me walk you through some good examples of successful execution in these four key sales growth drivers and show you that we have "pockets of excellence" in our business today, which we look to scale into fewer, bigger, better initiatives, across markets and also in some areas we intend to step up our capability into new territory by adopting FMCG best practice.

I will start with portfolio management.

## Davidoff Driving Premium Growth

In looking at portfolio, I wanted to start with a Davidoff example.

With Davidoff we have a clear and successful global brand template, the trick is to apply the template consistently.

Here we look at Ukraine as an example, where we have prioritised A&P investment on the Davidoff brand and de-prioritised, or stopped outright, other initiatives, a clear demonstration of "fewer, bigger, better".

We have also created momentum on the premium line as well as introduced new SKUs – the most recent of which is the king size superslim range, which is delivering significant volume and value share gains. In fact brand volumes has doubled in the past two years.

## Gauloises Success in North Africa

Another good example is Gauloises Blondes, where we are getting traction in North

African markets by successfully:

- profiting from the growth of the international segment post state monopolies – Gauloises Blondes now has a third of the segment in Morocco and Algeria;
- applying the global template, which means leveraging the French heritage, driving high awareness with limited edition packs and providing differentiation and affordability for young adult smokers with pricing just below Marlboro;
- demonstrating leadership at the point of sale with 'Big Brand' presence – furniture and planograms well above our fair share; and
- creating customer programs which make us preferred partners with tailor-made key accounts programs such as Gauloises trade events.

The region is planning a further roll-out, most notably in Tunisia where the results are very encouraging, albeit off a low base.

## Building JPS International Profile

We reached a landmark in Germany this year with JPS reaching over 10 per cent share of market for the first time.

JPS offers consumers "heritage at great value" and the results have been spectacular with total volumes up 16 per cent at the half year.

We learnt what worked well in Germany and applied this to the UK and Australia with excellent results: JPS is approaching eight per cent of market in the UK and over two and a half per cent in Australia.

These launches mean we expect to sell over 20 billion sticks this year in JPS which is almost six times more than we sold in 2004.

An excellent example of "fewer, bigger, better", where in this case we understand the consumer needs and have applied the brand template consistently across various markets.

## Driving FCT Growth in EU Accession

A key area of growth has been in fine cut tobacco in the EU accession countries.

Here we see the combined cigarette and fine cut markets in Poland, Hungary, Czech and Slovakia. Fine cut has grown seven per cent compound over the last six years whilst cigarettes have declined two per cent compound.

FCT has grown from less than six per cent of the market in these four countries to around nine and a half per cent.

## EU Accession Share Momentum

And look how our total tobacco expertise has generated significant share growth against this changing market dynamic.

Our cigarette share has climbed from 17 per cent to over 23 per cent and our fine cut share from seven per cent to nearly 40 per cent.

## Rolling Out Central Europe Growth Model

Fewer, bigger, better means that we intend to scale the success with fine cut tobacco beyond Central Europe and are today replicating this success in Spain.

We expanded the make your own category with an FMC branded product using consumer-preferred “expanded tobacco”, which leverages the excise structure. We will now progress with segmenting the portfolio as Ducados Rubio make your own tobacco (or MYO) has achieved a 25 per cent market share in May.

This sort of growth is even more impressive when you consider that fine cut tobacco pricing remains strong in Spain at a time when cigarette margins are under threat.

In summary, we have scaled the fine cut tobacco strategy successfully in Spain where the category is fuelled by consumers searching for value.

## Fewer, Bigger, Better – Innovation

Moving on now to provide you with examples of fewer, bigger better in the area of innovation. I will keep this relatively light because this has been a major element of Roberto’s presentation.

## Capitalising on Eastern Europe Growth

I want to talk about two key examples where we are applying fewer, bigger, better in innovation.

Firstly in being a very fast follower in diameter innovation in slims and superslims.

Year to date we have sold 69 per cent more new formats such as king size superslims and superslims, than we did last year, driving strong sector share growth.

In fact our share of the superslims segment has grown to almost 6 per cent within Eastern Europe, whilst our share in king size superslims has grown by almost eight percentage points in Eastern Europe, where almost 1 in 4 consumers of this format now smoke one of our brands.

Our share across Eastern Europe is around 13 per cent and the chart shows our share of superslims is growing in line with our share, meaning our share of superslims will climb over time from its current 6 per cent and our share of king size superslims growth is materially above our 13 per cent market share level meaning our share of king size superslims will also continue to grow, and we have also successfully rolled out this innovation to the Middle East and the EU.

So “Fewer, Bigger, Better” means we are rolling out consumer relevant innovation across our market footprint faster than ever before.

## 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 which Roberto has shown you.

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 April and the results have been tremendous, confirming our expectations for share, volume and margin growth.

We have invested into capacity to enable a roll out across various markets.

Let me show you this video to demonstrate this.

## Fewer, Bigger, Better – Pricing

Let me move on to pricing, the third sales growth driver.

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

But pricing in the context of fewer, bigger, better is not just looking at taking manufacturer price increases.

The pricing driver is about excise management across Total Tobacco to maximise revenue growth and the optimisation of brand, pack and price per channel.

## Excise Engagement Germany

As I mentioned, this driver is about excise management across a Total Tobacco portfolio to maximise revenue growth.

A good example where we get this right is in Germany where we maximise returns working within the country's excise structure. Fewer, bigger, better means leveraging the extensive capabilities of our German team in developing excise strategies against this structure in the rest of our business.

## Enhancing Our Capabilities - in brand, pack, price by channel

The second arm to the pricing sales growth driver is about optimisation of BPPC or brand/pack/price per channel, which is about identifying segmented opportunities to create consumer value and developing tailored solutions to capture these profitably.

This is a capability area that potentially holds a significant value opportunity for us in moving away from a one size fits all approach and seeking out specific opportunities for brand-pack-price solutions in different channels at potentially higher margins.

Consumer needs on different occasions is key to doing this effectively as witnessed in other FMCG industries. In Imperial we have pockets of excellence such as with the introduction of the 10-pack Lambert & Butler in the UK, which caters for those who trade up to an L&B for a night out.

Also, 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.

## Pricing Strategy Drives Growth

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

Developing a common framework and toolbox 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 invested in developing a "Brand Price Trade Off" tool that gives us a deeper understanding of price elasticities by individual brand. Using this tool, we analysed the price elasticity of Horizon versus its benchmark brand with very high precision. Based on this analysis, we repositioned the brand and have since seen a turnaround in the brand's market share trend (from negative to slightly up). Given Horizon's volumes, this improvement is a key reason for the growth in our overall market share in Australia of 180 basis points in the year to date.

Another example of analytical tools which we can scale across our market footprint is in the UK. Here we have invested in a technique called "Conjoint Price Research" which gives us a detailed understanding of the share development across a competitive set of brands at different price points.

You may argue that anyone can reduce price to try and grow share. However, the insight gained in using this tool led us to increase the price of Windsor Blue by four pence 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.

## Fewer, Bigger, Better – Customer Engagement

"Fewer, Bigger, Better" also applies to Customer engagement, the last of the four sales growth drivers we have prioritised.

## 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, Norway and Ireland – 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;
- 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 is up 1.8 per cent despite last year's 25 per cent tax increase, and in Norway where our snus and FMC shares are up 1.1 and 0.3 per cent respectively.

## Integration to Maximise USA Growth

Another example of "Fewer, Bigger, Better" is the recently announced decision to merge the cigarette and mass-market cigar businesses in the USA.

Both companies were visiting customers with their separate sales forces: Altadis USA from a position of strength being the number two in the market with leading brands like Dutch Masters, Backwoods and Phillies; and Commonwealth Brands as a challenger with USA Gold and Sonoma.

The decision to merge is one of creating critical mass and selling a Total Tobacco portfolio to customers with a combined sales force of up to 1,000 people from which both businesses gain:

- as outlet coverage increases from 7 to 11 calls per year
- market coverage of independents grows to 97 per cent of volume
- a 16 per cent increase in mass cigar market coverage
- and improvement in the effectiveness of calls

## Unlocking Our Potential

That concludes my second section on sales growth drivers.

I now would like to take you into more detail on Customer Engagement.

## Shout v Listen

We think that developing plans upon listening and understanding how we can create value is relevant not only for consumers but also for our shoppers and customers.

Which is why we recently undertook an activity to watch over 18,000 shoppers and speak to over 4,000 of them in eight different markets, with the key outcomes being analysed and shared amongst our sales and marketing teams. We consider this consumer insight to be critical to the success of our strategy.

## Understanding Stakeholder Needs

Understanding the needs of shoppers and retailers is shaping our customer engagement strategy. For shoppers "availability" is their number one need, "my brand available where and when I want it."

A shopper will purchase within a short period of time of wanting to buy and is likely to switch if their brand is not available.

Our customers need to be able to meet the needs of their shoppers and attract new shoppers, whilst optimising their working capital and manage cash flows.

This means we have to focus on optimising our on-shelf availability, aligned to the needs of shoppers within specific demographics.

## Customer Engagement Agenda

Based on these insights we are developing a global framework and toolbox for the Customer Engagement sales growth driver.

We are prioritising "Where we compete" based on economic and strategic values with a distinctive proposition that focuses on "availability" and "retailer advocacy" with "jointly agreed growth" objectives and plans per store.

The global framework specifies that we deliver it through a route to market optimisation, which we call "At-Your Service", and it is all about regaining control of the order capture to ensure frequency of contact and cross selling.

By using in/outbound call centres and online ordering tools in combination with our sales force and a third party logistics provider, we can make it happen through rigorous account planning and performance management and continued development of organisation capabilities through quick scan audits and learning and development programs.

## Maximising Shareholder Returns

I have spoken about the four growth drivers and contextualised these drivers within the framework of executing "Fewer, Bigger, Better". A more focused approach, with an eye to scaling innovations and ideas within and across markets, and continually executing to a very high standard, will drive our sales growth. Our ability to engage and understand customer and consumer needs will also be key to driving this growth sustainably.

Bob has highlighted how our already high margins mean our sales growth translates into strong profitability, and we know that most of this is converted into cash, which we use to maximise shareholder returns whilst taking some to invest into the business.

That concludes my presentation. I hope I have successfully conveyed my perspective and areas of opportunity within sales execution.

Thank you for your attention. I will now be happy to answer any of your questions.