Transcript – Quality Growth: Returns and Growth – Markets that Matter

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Amal Pramanik: Good morning. My name is Amal Pramanik, I'm the division director for Growth Division and of course we have Dominic Brisby who's the division director for the Returns Division.

We also have three of our cluster general managers with us today: Paul Matthews who's looking after the Australasian cluster. Oliver Kutz who's our general manager from Russia and Central Asia, and Alex Kamaras who's our general manager looking after South East Europe.

We are going to focus in this particular session about our commercial strategy. Why we make the unique and distinctive choices on our commercial strategy for Imperial Tobacco.

Together, we look after the tobacco business, excluding ITG brands and premium cigar division which we are not covering here.

It's important to understand the choices that we make with our strategy, what difference it makes in our markets, how it helps us to win in our markets, and we'll talk through some examples to prove that.

Firstly, we're going to cover our differentiated footprint strategy. Why we put some of our markets in the Returns Division and some of them in Growth Division, and Dominic is going to walk through that.

We are also going to talk about how we prioritise our investment choices to decide where we're going to invest today and what we're going to keep for the future.

We've been working with our four sales growth drivers for a number of years and we're going to talk through these elements and how those drivers are helping us win.

You've already heard a lot about our operating model and Dominic is going to explain how that makes a difference in the commercial part of the business.

Dominic Brisby: It's fair to say that one of the key focuses of today is around driving quality growth, not chasing volume for volume's sake but making sure we're selling high quality volume in markets that matter.

When we look at the markets we do it through certain lenses and applying certain criteria in terms of how we make these investment choices.

The first is making sure we have a disciplined and agile approach to how we do that, how we look at Returns Markets, how we look at Growth Markets, and I'll come to talk about that in a second.

We also look at the attractiveness of the market. We model in quite a lot of detail the industry profit pool in each market but we also model and assess our own ability to win in that market.

We make sure we leverage our sales growth drivers quite consistently across our footprint, and as Marcus and Peter were talking about earlier, we make sure we have a simple portfolio strategy, so not the previous situation of a large number of small brands but the current and future situation of a small number of big brands.

Of course, in doing all of that we have our vastly improved new operating model which allows us to execute these things perfectly in the markets.

I think it's worthwhile having a quick reminder in terms of how we divide our two divisions outside the USA in terms of how we run the tobacco business.

As you know, we split the world into what we call the Returns Division which I run and the Growth Division which Amal runs.

Unlike a lot of companies, we haven't set those divisions up based on geographical proximity but instead we've set them up based on the strategic roles of the markets which we've found can give much more coherence and consistency in the way that we manage them.

In the Returns Division generally we have quite high market shares. In pretty well every case we have more than 15% market share. Our average market share in those markets is around 25%.

In these markets we focus on sustainable profit performance and actively managing our strong share positions.

Geographically speaking, most of those markets tend to be in Europe, Western and Central Europe, in Africa, and in Australia.

In terms of the Growth Markets, we invest disproportionately now in order to drive profit and share.

Those are markets where we tend to have a relatively small market share but they're often in big industry profit pools, so it makes sense for us to invest disproportionately now in order to grow significantly our position in those markets.

Amal Pramanik: A few words about our investment prioritisation. When we look after around 160 markets, we need to become choiceful. Even in the Growth Division we have over 55 markets. We are not going to be able to invest in the same intensity everywhere, and this process sets out how we decide to choose to invest in some markets.

You see the factors on screen, they are broadly classified into two categories: the attractiveness of the market; and our ability to win in that market.

It's a fairly quantitative analysis for all these factors. We look at the current situation and how these elements are likely to develop over the next three to five years, and we follow this process every year to retest our investment thesis for the next few years again.

Amal Pramanik: Again, a couple of examples in the Growth Division. Firstly, Saudi. It's one of the very few markets which is still growing in volume. It's a fairly profitable market, relatively stable from the macroeconomic point of view.

We have a decent sized business and therefore decent amount of ability to be able to win in that market, and it is one of the markets we have continued to invest and will invest in the future.

Because it is a priority market, we will talk through an example of what we're doing there in a few minutes.

India. I think all of you know that there is a foreign direct investment ban in India for tobacco, so even if there's a fairly good sized business of tobacco in India in terms of affordability and other factors, it is impossible for us to penetrate there, and therefore obviously we are not looking at investing in India.

In a few minutes we're going to go through quite a few examples of our markets. These examples have been chosen based on our priority markets, and the priority markets are decided based on these factors that we are talking about.

Dominic Brisby: Of course the clearest way to measure quality of growth is in terms of portfolio transformation and the percentage of our revenue which comes from Growth Brands.

If you look at the left hand chart, you can see that within Returns Markets, we've gone from 38% of our revenue coming from Growth Brands in 2012 to more than 50% now.

There's been a very steady and quite dramatic growth in the quality of volume, the quality of revenue that we're generating year-on-year.

Amal Pramanik: For the Growth Division the story is very similar, that we've gone up to 56% of our net sales value in Growth Brands, mainly through migration, and we are currently doing one of the big migrations in Russia, Balkan Star moving to Parker and Simpson.

Dominic Brisby: Central to implementing all of this is the operating model and making sure that there's a lot of clarity in terms of who's responsible for what and how they can implement it.

As John mentioned earlier, this has been very clear in terms of making sure that the markets are in the best position to execute the group strategy and it's very clear who's responsible for what.

We've driven a lot of change in the way that we're managing the markets. The Group and the division shape the strategy and shape the investment prioritisation.

The clusters, because you remember we clustered a lot of markets, plan and support the markets, and then the markets are absolutely focused on executing the group strategy.

They're spending very little or none of their time bothered by peripheral things or things which don't make a lot of difference on the ground but instead they're absolutely, relentlessly focused on driving that strategy.

They're also very clearly measured in terms of certain executional KPIs which they can deliver, and we've found that that's made a big difference in the markets.

It's also and interestingly by our people been very positively welcomed. A salesperson now knows exactly what they need to do, exactly what they need to achieve, and they're less bothered by some of the other activities which previously they might have been doing.

Not only has this made it much clearer in terms of how we execute the strategy and who does what, it's also been enormously positively welcomed by the people because in a way it's freed them and empowered them from some of the things that they were focusing on before.

Amal Pramanik: Now we move on to the sales growth drivers. As we said before, we've been working with these four sales growth drivers for a number of years, and I'm sure you've seen us articulate these over the years.

Let's take a couple of minutes looking at each of these drivers, and then we'll look through some of the examples of how these drivers help us win in the market.

Firstly, portfolio management. It's about keeping our brands relevant with the consumers.

There are two factors which are highly critical for us, one, to focus on the Growth Brands and choosing our Growth Brands, chassis, carefully, which we've already heard about, and simplifying our portfolio to move all our portfolio brand volume into growth brand.

Secondly, innovation. When you see the examples you'll see the West mouthpiece in Russia has a good example of using this part of the sales growth driver and the next one which is a very important one for us, pricing and excise.

How we decide our pricing corridors and decide on our global pricing strategy, and using our excise structures looking at competitive positions that we can build in different markets, and again, the West mouthpiece is a good example to look at.

When you see the Australian example, you'll see a very relevant case study for pricing as well as customer engagement.

I believe being the fourth tobacco player in the market gives us an undue advantage. It helps us to stay humble. It helps us to try harder.

When you look through the examples, you'll see why that makes a difference for us to win in markets.

Now let's look through the examples that we want to show you. It's important to remember to win, all these four sales growth drivers have to work in tandem, they're all important and they need to work together.

The examples we'll choose are based on our priority markets. So the first one is Germany.

Dominic Brisby: In a minute we'll hand over to some of the cluster GMs to talk you through their own markets, how they're managing the sales growth drivers.

Before then, it's worth touching on a couple of our biggest markets and what's going on, and particularly how we're executing and implementing the sales growth drivers within those markets.

As I said before, Germany is an incredibly attractive market, almost any metric that one would look at, and it's also somewhere where we very clearly focus on executing these sales growth drivers.

In terms of portfolio management, we're absolutely focused on two brands in those markets: Gauloises and JPS, which are fully supported across every consumer touchpoint and will continue to be.

One of the things we've particularly gained from in Germany is the quality of the Gauloises campaign which has resulted in consistent and steady share growth of that brand.

We activate growth pockets in terms of innovation. Particularly relevant to that is the additive-free format which is doing very well in Germany, as well as making sure that we cover the value bases properly with big pack formats and fine cut tobacco offerings.

Germany is a market where we've been able consistently to grow our net sales value and to grow our operating profit.

One of the key points in Germany which we're very strong at and can get even stronger at is the question of customer engagement. It's very strongly a key account driven market.

We're particularly good at managing those key accounts with strong category management initiatives. A recognition of that is that our business in Germany has been voted by the trade as the number one tobacco supplier, so our partnerships are very strong and we're really capitalising on those partnerships.

If we move now to look at the UK. The UK is in a different situation, quite a complicated situation, with strong regulatory headwinds with the implementation of plain packaging, also a fair amount of discounting going on at the bottom end of the market.

Having said that, within that environment our strategy remains resolutely clear. We focus on the brands with the biggest equity, those brands are L&B, JPS and Golden Virginia.

We have a complicated portfolio in the UK, a lot of SKUs, quite a lot of small brands, so we're working very hard to simplify that portfolio, in line with the comments that Marcus gave you earlier.

One of key points in this market has been making sure we gain our fair share of the sub-economy segment. This is a segment which has been growing over the past few years very significantly in terms of volume, and it was a segment where Imperial previously punched below its weight, so we've worked hard to make sure that we gain our fair share of that segment, and have succeeded in doing so with Players and Carlton.

Central to all of this and one of the things that we really learnt from Australia is the importance of strong retail coverage in advance of the introduction of plain packaging.

Moving to Spain, you heard about the successful migration of Brooklyn into West. This is really a key segment in Spain at the moment, the four euro price point, and following this migration West continues to perform very well. It continues to grow share and we continue to lead that segment which is the fastest growing segment within the market.

There's also a lot of work to do with one of our big migrations migrating Ducados Rubio into JPS and making sure that we build enough equity around JPS as a brand as well as West as a relatively new proposition in the market.

As the regulation changes, particularly the route to market changes, making sure that our customer engagement strategy is absolutely focused on strengthening the partnership with the customers.

In the breakout session we'll be explaining more to you about how they do that in Spain since it's a very different market versus somewhere like Germany given that the trade is unorganised and lots of independent retailers.

That quickly touches on some of our big markets. There's one big market which we haven't spoken about much other than the video at the start which is Australia, a market where, according to pretty well any metric you'd care to look at, we're percentage extraordinarily well whether you look at volume, whether you look at revenue, share or operating profit.

We continue to perform very well in that market and it's the darkest tobacco market in the world, so we'd like to focus a little bit on that.

Paul Matthews who's the general manager of Australia will come and take you through that.

Paul Matthews: Thanks, Dominic, and thank you, Amal. Just in case you don't know, Australasia comprises three individual markets, John talked about clusters earlier, and they are Australia, New Zealand and the Pacific Islands, but today I'm going to talk to you about Australia which is the biggest part of the cluster with a tremendous amount of pride. I hope you enjoyed the video earlier.

As Peter showed you earlier, and Dominic referenced it, Australia is the darkest market in the world, and from a distance it's easy to get dispirited by that.

For those of you who don't know it, Australia is known as the lucky country, and it deserves that title because we have enjoyed economic growth consistently since the early '90s, I think 22 years of continuous economic growth.

It's a market or an economy that's hallmarked by very low unemployment, you really don't have a job unless you don't want to work, very low inflation, and it's a very high wage economy, particularly for the critical demographic, our consumers, the average wage is more than US$1,000 per week.

So even through the next four years where we will see excise increasing, consumers will still be able to afford to consume our products.

QAD is very much an opposite acronym for how we've built our success in Australia, the quality of our brands, the quality of our people, the two key assets of any tobacco business, our agility in front of the customer and through to the consumer, and very much our discipline, the way in which we execute our strategy through the retail trade.

All of this started years before plain packaging. We positioned JPS in the sub-value segment, we knew it was going to be the race to win.

All our competitors had one, two, three horses and that race we had one, it was JPS, and it was the right brand to pick.

We migrated several other low price brands into JPS and we very much focused on what we call accessibility, the right assortment, the right SKUs for the right consumer.

There have been plenty of innovations within our portfolio. Other brands in our portfolio, like Peter Stuyvesant referred to earlier by Peter and the Horizon brand. We have a whole portfolio of quality brands.

So pricing for us has been a key driver, enabling us to build on the equity in our brands to firm our pricing and improve our net revenue.

But it's really customer engagement that's been the sales growth driver, that's been the real differentiator of success for us.

What does all this mean, and this really is a remarkable story. Last year we eclipsed the iconic Winfield brand which had been number one in Australia for decades.

JPS is now the biggest brand in Australia, and it's taken us fewer than seven years to do that.

On a corporate share perspective we see our development very much in phases. We had a phase that we called the accelerate phase. That was between 2012 and 2014. Dramatic share growth, unbelievable share growth.

In the last few years we've taken a more considered position. Now as one of the big players in the marketplace it was up to us to capitalise on the equity we built.

Going forward, what does it mean? We see the next few years as the sustain phase where we keep growing our share but ultimately improve our net revenue and the quality of our operating profit, and that is the story from Australia, thank you.

Amal Pramanik: Thank you, Paul. I've talked through Japan. Before even you look at any of the sales growth drivers, the first question that should pop up in any of our heads is it's a very developed market. There are three very big tobacco players who are extremely strong. They are very strong brands. You have absolutely no chance to win.

I think it is good for us to be able to demonstrate how using the quality, agility and discipline and our four sales growth drivers, we are winning every year, bit by bit but we are winning every year.

What are the parameters? Firstly we are focused on one brand: West.

We priced it at 380 Yen which is about 15% lower than the mid-price segment.

It has a range which caters to a majority of the taste segments. We're using innovation. Peter mentioned about Japan being quite bright. We're using innovation in being able to contact potential consumers through our digital platform.

We started with three cities, then we expanded, once successful, to three provinces, and only now having tasted success we are going national.

The priority today in Japan is to build our sales infrastructure and improve our availability and distribution.

In the last three years we've grown our market share by 50 basis points in Japan.

If you know the volume and the profitability of that market, you can realise how significant that is already.

The next one is about Saudi. We have a two-brand strategy there: Davidoff at the premium end and West at the value for money end.

You would have seen during half year lead result announcement we've just launched a fresh box of Davidoff in Saudi after successful launch in other GCC markets.

We are growing our availability and distribution through our very unique retail engagement programme which is designed for the market there.

I'm very pleased to again say in Saudi we've grown our market share in the last 3 years by 90 basis points playing all the 4 sales growth drivers well.

Having looked at these two, let's look at a couple of other examples from the Growth Division and now I'd like to hand over to Oliver Kutz who'll talk us through the example in Russia.

Oliver Kutz: Thank you, Amal, good morning, everybody. I would like to give you a short update on the Russian market and I would like to show you our portfolio transformation which changes the way we operate in Russia.

Let me start with a few words about the macroeconomic environment. Russia is in a crisis. The Russian rouble has depreciated by 100% to the U.S. Dollar over the last 2 years, this is mainly driven by the fall in oil price.

Consumer confidence is low, and consumers have reduced their spending.

I attended an external market meeting a few weeks ago and there was one statement: saving is a new fashion in Russia, and this is true.

Consumers are trading down, they're looking for more affordable offers, and they're looking for value for money. The positive thing is they find in our category cigarettes are still very affordable, particularly compared to other categories.

In fact, the price of one pack of cigarettes starts at 6 roubles which is slightly more than 60p, so if you go to a Russian supermarket, you pay exactly the same price for 1 litre bottle of a soft drink, so extremely affordable.

There are challenges in the Russian environment, but the market remains extremely attractive. The market size is 200bn sticks. It is the second largest market in the world.

The profit pool is £1.9bn and it's a long term growth mainly driven by strong pricing. We believe it is continuous given the high affordability in the market.

Imperial market share is 7%, and we aim to grow over the next years.

Consumers are looking for good value for money. We are responding to this need by applying our sales growth drivers.

First of all, we shifted our portfolio focus to Growth Brands and we have launched a new international value for money brand, P&S, after an extremely successful test market.

At the same time we're reducing the complexity of our portfolio, and I will give you more details in a minute.

Queen size is the fastest growing segment in Russia.

We have updated our portfolio in the segment and we have added recessed filter to all of our products.

We've also launched a new product that Amal already mentioned, so West mouthpiece. This is a non-filter product which looks almost the same as a filter cigarette.

We launched it three, four months ago in the market and had a very successful start.

Last year we increased prices on most brands by 70 rouble, this is a 36% increase on our largest brand Maxim.

This year in the first 8 months we have already increased by 50 rouble which is another 23% increase.

In terms of customer engagement, we're driving distribution for our new brand P&S on a nationwide level, and we are improving our position in discount. Discount is the fastest growing segment and already accounts for 30% of the total market volume.

This shot is an overview about our portfolio simplification. One year ago we had 14 brands in the market, we are now in the process of reducing it to only 5 brands. This includes 4 existing brands and 1 new brand, and we're also clearly classifying these brands.

Maxim, our biggest brand, and our new brand P&S are the two primary brands and these two brands enjoy the largest investments.

P&S is also a destination for many of our migrations. We started four migrations, including the migration of Balkan Star, our second biggest brand, into P&S. In fact, this is the biggest migration in the Russian market so far.

We're delisting five brands, these are lower volume brands with a limited consumer relevance, and we believe that we've offset the volume impact by giving the share space to our stronger brands including their availability.

What are the benefits of the portfolio simplification? First of all, we're improving the quality of our portfolio. We have a higher share of our volume in Growth Brands, and these are the brands with a better brand equity.

Secondly, reducing the complexity across our whole organisation. In fact, our marketing team, our logistics department, our field force, they can now focus on the brands that are really important to the business.

We also received very positive feedback from the trade. They have limited cash, particularly in the current economic environment, and they prefer to spend their money in brands, into SKUs with a high turnover.

Finally, I would like to show you our market share shot which shows a market share of our growth in Specialist Brands. I think it's extremely encouraging to see that we have improved the share trend by focusing on fewer brands and by simplifying our portfolio.

That's it from Russia, I would like to now hand over to Alex Kamaras to talk about Italy and Greece.

Alex Kamaras: Thank you, Ollie. Kalimera or buongiorno or good morning. In the next five minutes or so I will take you through, starting with Italy and I will continue with Greece, I will take you briefly through our main strategic choices and some performance highlights.

Starting with Italy, despite the headwinds in the environment in the last years including a recession, including high unemployment, and very recently the new European legislation, the market is highly attractive.

Why? Because it is the third largest market in Western Europe with a volume of almost 80 billion sticks, and this market, and this market is stable in the last years.

In this market, although we are growing in the last years, still we are only at 4% market share which means that there is a huge space for us to grow.

Moving on to our strategy which has been founded on the sales growth drivers, namely portfolio management, pricing and customer engagement.

How have we been delivering these sales growth drivers? Very briefly, by simplifying significantly our portfolio. As we speak, our simplification process is underway and we have been reducing our number of SKUs by 50% by delisting the smaller of them and also by migrating some of our smaller brands to some others, like Fortuna to JPS which has already been completed with 100% retention rate.

It means that we managed to keep all our consumer base by mitigating to JPS.

Second, by focusing just on two brands. We used to focus on five and now we are just focusing on two brands: on JPS, in order to be able to capture the increase in down trading; and on Davidoff in order to strengthen our presence in the premium segment which although declining still accounts for 25% of the Italian market.

Third by further enhancing and accelerating our consumer activation and our retail advocacy programmes which are selectively focused on the most important outlets.

Focusing now on customer engagement, this has been maybe the most important sales growth driver for our strategy and our success story in Italy.

This was built on three pillars. First on annual trades and incentive programmes aimed at retailers which have generated very high rates of participation and reward, and which were coupled with full mix of visibility tools for our communication at the point of sales.

The second pillar has to do with the recent expansion of our field force in order to be able to cover a larger part of the market and also to be able to visit more frequently so to increase our focus on the key outlets.

The third pillar has to do with our unique call centre in Italy which is offering to our outlets, to the outlets in the market, superior support and service, and it's mainly aimed at the smaller outlets which we did not directly cover.

As a result, we have managed to deliver sustainable growth in Italy in the last years. Having started in a very competitive market and in a very competitive segment, almost from nowhere in a financial '13, and having reached 2.1 Nielsen market share in financial '15, and 2.3 in April '16.

Also we have delivered significant volume growth over this period of 1.4 billion sticks.

JPS is a value for money brand, however it has an aspirational brand image in the market and this is thanks to its element pack, the superior blend, and the roll that way campaign which we have been exploiting in the last years in Italy.

My last slide has to do with our success story in Greece for which we are really proud of, since we have managed in a very challenging operating environment to continue to deliver share growth during the years of the crisis with a premium brand.

As a result, we managed to continue to grow all these difficult years in Greece from 4.3% in financial '11 to 6.2% in financial '15, having reached a new record of 6.9% market share in April '16.

You may understand that I could keep on speaking for hours about Davidoff in Greece, however, I will not do so and I will handover to Dominic and Amal for some concluding comments. Thank you very much.

Dominic Brisby: Thank you, Alex. I hope we've given you a flavour of how we drive quality growth in markets that matter.

Firstly, we take a very disciplined approach to how we invest in the markets but also a very agile approach. We can determine very quickly whether we want to invest but also if there's a very good reason not to invest, we can step away pretty quickly as well.

We constantly analyse total industry profit pool in quite a lot of depth and a lot of detail and marry that up against our own ability as a business to succeed and to win in that market.

Wherever we're operating, we leverage our sales growth drivers very consistently. The execution of sales growth drivers might vary from one market to another, but the sales growth drivers themselves are absolutely universal.

We also make sure that within that, analytical rigour is at the heart of what we do, that we drive the portfolio strategy, we drive the simplicity very consistently across the markets, making sure we have the big brands that we want and the consumers want and that the trade wants.

Of course all of this is done via the operating model, making sure that the people in the markets are empowered to deliver the group strategy and are not bothered by the peripheries which don't add value and don't drive the sales immediately in those places.

Amal Pramanik: Hopefully in the last few minutes, we've been able to demonstrate how our strategy is uniquely different from other tobacco companies and how our different pillars of strategy are helping us to win in some of the markets that we've talked through.

Before we end, in this time of Brexit discussions, we'd like to take you back a few months from a time of Grexit discussions that we had a few months ago, and let's take a look at a film from Greece on how they managed to continue to grow Davidoff, even at this point in time.

The point I wanted to make is strategy comes to nothing without people and the attitude of people, and this demonstrates that point very well.

Video shown here

Amal Pramanik: Thank you.

Dominic Brisby: Thank you.