



IMPERIAL
BRANDS

Preliminary Results 2017

Tuesday, 7th November 2017

Overview of Results

Alison Cooper

Chief Executive Officer, Imperial Brands

Welcome

Well, good morning everyone, and welcome to our results presentation. It's been an important year of progress for Imperial, and I'm pleased to be presenting today, not only with Oliver Tant, our CFO; Matthew Phillips, our Chief Development Officer; but also Amal Pramanik, who heads up our Growth division; and Dominic Brisby, who heads up our Returns division.

Strategy

Enhanced focus on key priorities

Let me start by keying into our strategy. You'll remember that in 2016, following the US deal, that the Board took some time to look at the strategy for the next decade, and spent some time over the course of that year really reviewing and looking at the options that we had for the next decade. The results of the review were a confirmation of the strategy for Imperial, but with a real sense of enhanced focus behind the key priorities, a much sharpened focus behind the priorities for the business.

So at Imperial, we're clear about the portfolio, we're clear about the key equities and brands that we have that we want to grow going forward. And within that, that's not only about our cigarette and our fine-cut brands, but clearly also about our premium cigar brands, Skruf, the strong equities we have in these other categories, but also clearly about blu, which is one of the stand-out brands in the e-vapour space, and one in which we very much want to continue to realise opportunities behind, going forward, and significantly so. We've got a clear focus behind the footprint, the priority markets, where we want to invest and we want to grow, where we want to maximise our opportunities going forward.

Market Repeatable Model

We're focused on how we want to win in those markets; that's our Market Repeatable Model, our codified approach for growing market share. As always, we've got a clear focus on the cost opportunities and cost realisation in the business, and also on generating cash and capital discipline, all supporting our quality growth agenda and our delivery of returns for shareholders.

Investment

Increase in 2017

And in 2017, as I said this time last year, we stepped up investment behind that strategy. And that was based on the work we've done over a number of years now on the portfolio, making sure we're focused on fewer, stronger brands, significant work on migrations and on SKU reductions. It's based on us focusing on the profit pools that are important to us, both now and in the future, from a detailed analysis on the development of profit pools over the next five to ten years. It's based on the Market Repeatable Model – how we win, where we see the opportunities for investment behind that model. And it's also based on the fact that

we've been generating significant cash as a business, and therefore that we have the resources to really invest behind it.

So, in 2017 we made some focused additional investment choices, focused around the Market Repeatable Model in the priority markets and behind the brands that are most important to us. And that's around driving stronger sustainable share growth in Imperial as we look forward. And as we said this time last year, that investment has impacted the financials, and that's been compounded by a particularly tough year of the trading environment in tobacco. But we've prioritised the investment, we've taken decisive action in terms of our cost base, to protect that investment and continue to drive the share and the returns we wanted to in 2017.

Improved share growth in priority markets

So, what has that investment delivered? Well, it's delivered improved share growth in our priority markets. We're growing share in Russia, we're growing share in Italy, we're growing share in Japan, we're growing share in Saudi, we're growing share in the UK, we're growing share in Germany, we're growing share in Australia. We've got improving share trends, particularly in the blonde segment in both France and Spain, and in the USA we're growing share in our priority brands, in Kool and in Winston.

Growth in the right brands

And those performances have not just been about share growth, they've been about share growth in the right brands, in our growth brands. And you can see that in the improving growth brand share, up 80 basis points year on year. That's part reflection of our successful migration programme but organically those brands have grown over 1% year on year. They're up over 8% in the Growth division, they're up over 4% in the Returns division: strong performances from those key equities. They also contributed to the asset brand percentage of revenue, which is up to 63%.

But that also reflects some very strong performances from our specialist brand categories: from mass market cigars in the US, from premium cigars, which you can see here, the revenue's up 9%, Snus, revenue up 8%, and also a good first year's contribution from our new joint venture in China.

Improved second-half performance

And those share performances have supported an improved second-half performance: volumes down 2.6%, outperforming the market, which was down 4.5%. And that has clearly supported the improved revenue performance, as well as it being added to by the savings that we've generated and the cash that we've generated in the second half and throughout the year. The financials have been impacted, as I mentioned previously, but into 2018 with a stronger share position and a stronger basis for growth going forward.

Next Generation Products

So, 2017 has also been about gearing up in next generation products. We see a significant opportunity in this space, and we see it being a material part of Imperial, going forward. We've assembled a great asset portfolio. We have a phenomenally strong equity in blu, which is about the emotional dimension in this space, not just the functional attributes that many focus on.

Enhanced Innovation Capabilities

We've enhanced our innovation capabilities. We've recently acquired a business called Nerudia, which has really added to those yet further for the back end of the year. We're also developing the capabilities in the business which are required to really exploit our opportunities in this space. Yes, tobacco skills are important – we need to leverage those – but this is about different ways of thinking, a different mind-set to drive growth, an exponential growth mind-set in the business. And we're building that to enhance our opportunities with these products as we go into 2018 and beyond.

In 2018 we've got some fantastic new products, we've got new market launches; it's going to be an exciting year. And Matt will talk to you a bit more about that later.

Delivering our Strategy

So delivering our strategy. Dominic and Amal will come up shortly to talk about how we're winning in our priority markets. Matt will pick up on next generation products, and Oliver will talk to us about some discipline on cost and cash. But first of all let me kick off with the Market Repeatable Model.

Market Repeatable Model

We've talked about this on our webinar, we've talked about it before when we've been talking about our results. This is the foundation of how we win in market. It came out of the work in 2016, when we looked at our sales growth drivers. And we really thought about how do we really optimise these, codify these to really drive our success in market going forward?

It starts with a simple market-focused portfolio, and this you know we've been doing a lot of work on, migrations, but also more radical SKU reductions, which Amal and Dominic will also pick up on shortly. Next part of the wheel is sustained brand investments, consistently investing behind that portfolio, including consumer activations.

Price strategy

Let me pick up on price strategy, the next segment. Always on price segment, it is about having a competitive position for our brands. It's around matching the key competition brands in market; it's not about undercutting, it's about matching those key price points. Then with the right portfolio, we want to make sure it's extensively available in our markets, particularly important in the darker market. And we work with our retailers to really tailor the opportunities with them for 'win win' solutions to drive advocacy of our brands in market.

Learning

And finally, clearly, a learning segment, not only within market but to make sure we learn across Imperial from our successes and failures. It's quite simple but it's the holistic application of the model where the power is, and it's this MRM that we've invested behind to drive the quality share growth I was talking about. We've stepped up investment behind it across all segments in our priority markets. But in the other markets as well, we've optimised investment behind the MRM to drive growth.

Markets – United States

So moving on to some of the markets – David couldn't be here today so I'm standing in, and I haven't got the accent but you'll bear with me – US, great year for us in the US.

Stepped-up investment

We've stepped up investment behind what you already know is quite a simple, focused portfolio, Winston and Kool being the priorities, Maverick and USA Gold being the secondary priorities. We've got new equity campaigns behind Kool, behind Winston. We've got a new brand – we've got a new brand pack for Winston; we've also got a new gold variant for the Winston portfolio as well, all adding to the brand appeal for consumers.

Price strategy

The price strategy has been fully implemented in 2017; that's a significant part of the investment that we've made, of the \$300 million. It's an important part of the investment we've made. Through the back end of 2016 we were trialling different buy-down levels in terms of the competitive positioning of the brands in the market. In 2017 we've got the full-year effect of those coming through, through that buy-down programme, supporting the brands in the market.

Distribution

And you're aware of the distribution drive – we've now got 172,000 retailers in the market, making sure our brands are very much available and advocated by retailers. So the MRM in action in the US, market share was down overall, down to the drag of the portfolio brands that were not focused on, but Winston and Kool up 20 basis points respectively.

Mass Market Cigars

And it's been a great year for us in mass-market cigars. We have an iconic portfolio in mass-market cigars. We have Backwoods, we have Dutch Masters and we have Phillies. We've done some significant work, as you can see, on the portfolio to get that focused down on the SKUs that really matter, and we've got some fantastic initiatives supporting the brands through digital activations and consumer events across the US.

In terms of the distribution, we've done a lot of work in store to make sure we're driving the pull with consumers, rather than the push model that was prevalent in mass-market cigars historically. Overall, driving share growth, driving significant increase in volumes in revenues and profits. So overall in the US, if I look back over the last couple of years, a significant and successful time for us with this acquisition and really generating returns for shareholders.

Let's move on from the US to the UK. Dominic?

Markets in the Returns Division

Dominic Brisby

Division Director, Returns, Imperial Brands

United Kingdom

Thank you Alison, and good morning everyone. I'm going to talk through a number of markets in the returns division, starting with the UK.

A tough market

We're very pleased with the performance of the UK in 2017. This has been a tough market, as you know, for some years, and we always expected 2017 to be challenging for various reasons: firstly, the introduction of a EUTPD and plain packaging, and also a significant amount of price discounting in the sub-economy segment. So, a challenging market: it clearly presents risks but it also presents opportunities. And in the case of the UK, we made a clear and conscious decision to take a leadership position in this market and invest behind our MRM. And if you look around the wheel you can see some of the effects that this is having, starting with portfolio. So, having an increasingly focused portfolio has helped our consumers navigate the EUTPD changes. We've also had a significant reduction in the number of SKUs in this market.

Price strategy

Moving around the wheel, on price, you can see that we've also been on price strategy in the UK this year. As Alison said, this is not about undercutting but it is about matching our key competitor brands, and we've been particularly successful with the brand players in driving our growth in the sub-economy segment. It's a brand with strong heritage and brand equity, and it's a winning proposition when priced at parity to other brands in this segment.

Distribution

In distribution we've significantly up-weighted our distribution strength. We've further empowered our sales people with better information and better CRM tools, and we've also helped retailers through the transition to EUTPD. You can see in key accounts, we've significantly increased our share performance. And in the UK overall in 2017, which has been a year of significant change and significant challenge, we've grown our share by 80 basis points.

Germany

Moving on to Germany, which continues to be a significant and growing profit pool. Again we've added to our investment this year.

Portfolio

So on portfolio, in Germany we already had a strong and focused portfolio with strong brand equity but we've stepped up our investments, particularly focused on a number of new campaigns around our growth brands, like the new successful JPS 'Make Your Day' campaign, as well as launching Gauloises L'Autre as a lighter proposition. We've increased distribution, particularly of our core SKUs, by investing in more sales reps, so our core range distribution has increased by 11% versus the previous year.

Learnings

There have also been a number of learnings. The EUTPD have a bigger effect that we anticipated it would do on market size in Germany, and we've also found that specification and packaging has become more important post the EUTPD than it has done previously. And as a result of this we're taking the opportunity to change our pack design for Gauloises, which will be implemented this financial year.

Share

In terms of share, we've had a particularly good fine-cut tobacco performance, driven by JPS and Fairwind; and on FMC, the JPS 40-box introduction has been a big success. And we've seen second-half trends picking up versus first half, leading overall to an increase of 20 basis points in the German market.

Good Progress in Other Markets

Spain

We've also made good progress in a couple of the more difficult markets, like Spain and France. Starting with Spain, where investment in Fortuna via POS activations is increasing market share in this brand, for a first time in a number of years. We've responded to consumer demands with the launch of West queen-size, although it's worth noting that in Spain dark tobacco drags overall market share down, albeit we have a better blonde market share trend than previously.

France

France has been the pilot market for a more radical SKU rationalisation. So, this year we cut SKUs by 40% in order to deliver a more focused portfolio to retailers, and improve the availability of our core range. And this has resulted in a significant improvement in the number of retailers holding our core SKUs. News is performing particularly strongly – up 46 basis points versus the previous year – and is now the number two brand in France, meaning increasingly it's a must-stock brand for retailers.

There's a similar drag from dark tobacco in France as there is Spain, but we also have a better blond share trend. As you know, in France there's a particularly tough regulatory environment with the introduction of plain packaging, as well as significant planned excise increases, leading to the government's aim ultimately to have a price point of €10 per pack. And this challenging environment reinforces the importance of consistently applying our MRM to this market.

Australia

Finally, looking at Australia, Australia is a market, which, as you know, we've been successful in for a number of years. And probably more than any other market, it's defined our whole approach to the MRM. And the success story is continuing. So JPS continues to gain share and reinforce its market leadership in France. Our market share growth is supported both by brand strength and by superb customer engagement, and I think this demonstrates our credentials in building brands in a tough regulatory environment, and particularly in an environment of plain packaging. The value and sub-value segments are growing market share as well, leaving us quite well-positioned for further growth.

Summary

So across the division we've got some good examples of executing our MRM successfully and delivering clear and tangible results. We've also seen similar strong performances in market share growth in a number of other markets across the division, such as Portugal, the Netherlands and Poland.

I'll now pass over to Amal to talk through the growth markets.

Four Priority Markets in the Growth Division

Amal Pramanik

Division Director, Growth, Imperial Brands

Thank you Dominic, good morning everyone. I'll cover our four priority markets in the growth division, and look at how we've done in these four markets.

Russia

Business has performed well

To start with, let's look at Russia. We are extremely happy with the way our Russian business has performed, especially keeping in mind the challenges that we faced in this market, and what transformation that we have done to the portfolio in this market in the last two years.

Portfolio

Let's look at the investments we made and start with portfolio. It's a market where we have de-listed more than 60% of our brands, more than 70% of our SKUs. It's a market where more than 30% of our volume got de-listed because of a big pack ban that came into force this year. And also we undertook the biggest global migration in this market in the form of Balkan Star moving to Parker and Simpson, which was over 2 billion sticks worth of volume. This massive simplification of the portfolio helped us to focus our investments behind Parker and Simpson, particularly queen size.

Pricing

As you know, in Russia it's been quite a difficult year on pricing. There are many international brands which had their limited edition packs sitting at the bottom of the market, and that has had some impact on our local brand Maxim, as you can see on the chart. We made significant investments on our market presence in Russia in the last year in terms of increasing our sales force, improving our visibility and distribution. And when you have a more efficient portfolio, it helps to be able to improve your visibility on the shelf much better.

Key accounts

And finally, key accounts is a very big, well-performing segment right now, and we are improving our presence in key accounts through new deals. We started with a call centre, which did not work out particularly well, and therefore we learnt quickly from that and re-invested those funds into key accounts again, which is why we've got a phenomenally good performance in key accounts.

Market share

Overall in Russia, we grew our market share by 12 basis points. In the latest SPOT share it is even better. But what is particularly pleasing is that we are growing in the queen-size segment, which is a growing segment in the country, we are growing in the key accounts, and we do not any more have the drag of a local brand called Balkan Star, which has been declining over the years. So in a much better, healthier position in this market.

Japan*Volumes*

Moving on to Japan, as you know, the Japanese market has declined by over 10%, and I'm very pleased to say in that environment, our absolute volumes have grown by 15%. We play with West, which is a value-for-money brand, a segment which is growing in this down-trading environment. And over the years, as the bottom of the price ladder moves up, as the excise duties change for those specific brands, we are going to benefit out of that as well. All our investments in Japan in the last year were based on improving our presence in the market in national accounts, in key retailers and also in the digital channel.

West

West is growing by over 30%, making it the fastest growing brand in this market. And we are close to 1% market share already in about three years, which not a lot of consumer brands have managed to do in this very big profitable market.

Saudi

Moving on to Saudi, at over 250 basis point share growth during the year, it is our fastest-growing priority market. Our investments are focused on Davidoff and West, one in premium obviously and the other one is the value for money. What we're doing here are growing our distribution. We are improving our activation in the Horeca channel, and in our regular outlets, through a programme that we've been running, and with the investments we've been able to accelerate that. And we are extremely pleased to say that after June 2017 doubling of prices due to selective tax, Davidoff is beginning to hold its share of segment, and West has grown to be the number one brand in the country. And in the last 12 months we are the only company which have grown share on a MAT basis.

Italy*Accelerated growth*

Finally to Italy. We've been doing well in Italy anyway for a few years, but we've accelerated growth this year, which has come about because of the investments we have made, based on the MRM analysis we have done and the additional investment that we put into the market. Our investments are focused here on Davidoff and JPS.

Davidoff

On Davidoff, we used to be presenting three cities; now we have extended to 32 cities. And on JPS we've built a national network for distribution, because it's a growing brand. We also have a successful call centre in Italy, which is also helping, and particularly we are investing behind a specific channel called Patentini. It is a Horeca channel, where we are one of the dominant players, which we have created a special programme for them, to improve our visibility and distribution in this channel for both Davidoff and JPS. So, overall our share growth is 60 basis points, which is very pleasing indeed.

Summary

So, in Growth division, we have grown share in all four priority markets. Through MRM investments, we have grown in many other growth division markets, namely Greece, Romania, Sweden and even Taiwan in the most recent share numbers, giving us an overall share growth of 20 basis points for the division as a whole.

That's all from me. I'll now pass it on to Matt, to talk us through NGP.

New Generation Products

Matthew Phillips

Chief Development Officer, Imperial Brands

Introduction

Thank you Amal, and good morning ladies and gentlemen. I'm going to take a few minutes to talk to you about NGP and how we're thinking about it. I'm going to start with a bit of context and few insights in terms of the way we think about this category.

Additive revenue and profit potential

The first way that we view this category is, from a revenue and a profit perspective, we see this as having meaningful and additive potential for Imperial. And the reason I say that is two-fold. One, it's a bi-product of our scale and our size versus some of our bigger competitors, but it also comes from being number four in the tobacco industry. And I'll talk about that a bit further in a minute.

Focus on transition of smokers to next generation products

The second thing is that whilst there are already tens of millions of vapers in the world, actually the way we're going to be successful in this space is to stay relentlessly focused on the smokers and on the transition of smokers to next generation products.

Impact of regulatory attitude on next generation products

And the third way that we think about it is actually there's a fundamental difference between tobacco and tobacco-related products, and tobacco-free products. And one of the key differences is in the way that those products are thought about from a regulatory perspective. Now, if you think about the three main categories within next generation products, you've got oral tobacco products, you've got heated tobacco products and you've got e-vapour, vaping products. And what the regulators are trying to do is strike a balance between encouraging innovation whilst also protecting public health – increasingly trying to protect public health.

And the regulatory attitude is massively, massively important because mixed messages, which there have been in next generation products, slows down smoker transition to next generation products. Positive regulatory perspectives increase and speed up that transition.

The regulatory attitude also impacts excise, the freedoms to innovate, the freedoms to enjoy, the responsibilities and investments that are required by legitimate, or more importantly, the not-legitimate players in this sector, and therefore the responsibilities that are required of them going forward.

So, we embrace the whole concept that we are starting to see emerge around the continuum of risk, trying to transition smokers increasingly to next generation products. And we are encouraged by the way the debate is developing, to an extent, from a vaping perspective, that some of the messaging coming out from some of the bodies that you can see on the slide, is enormously supportive and enormously positive. To the extent that the Stoptober

campaign, which I'm sure you're all aware in the UK last month, which is a government-driven anti-smoking campaign, was positively encouraging and endorsing smokers to be moving and trialling vaping products. We think it's a big shift and it's one that we welcome.

Oral Tobacco

Now, turning to two of the three categories that I was talking about a second ago, from an oral tobacco perspective, as you will know, we've had an enormously successful business in this space for a number of years. We acquired it back in 2010 and we've invested for growth, and the results of that business have been quite astonishing. Our market share in Sweden, which was the heartland of this product, is up by a factor of five. Our market share in Norway, which is the other main market for this, is now at 44%, up materially, nearly double what it was when we acquired it.

So, as we look at the oral tobacco business and the iconic brands that we've got sitting within it, we see opportunities. We see opportunities for new markets, absolutely, but we also see opportunities for new innovation and for developments.

Heated tobacco

On the heated tobacco side, you'll remember that we said a number of months ago, that we would be able to bring forward heated tobacco products relatively quickly. And I'm pleased to confirm that next month we'll be going into consumer trials with a number of platforms. Now, I hope you'll accept that I'm not going to talk further today about actually what those platforms are, or indeed which countries, that those trials are going to be taking place. But I do want to underscore that, from our perspective vapour, remains the biggest opportunity, and the markets that we are focused on, the markets where we have the strength and the market where we think we have the biggest opportunity to win, vaping, remains our focus. But we do recognise that both on the oral tobacco side and on the heated tobacco side, maintaining optionality is important.

Vapour

So turning to vapour, we've got big plans in 2018. Before I come on to tell you a bit more about what those look like, I'm going to give you a flavour of how we think about vapour and what we think is important in order to be successful in this category. It's about capabilities, it's about the portfolio and it's about being in the right market.

Capabilities

Now from a capabilities perspective, innovation is fundamentally important; I'll come on to that in a second. But the other capability that I'd call out is actually the omni-channel capabilities, which tobacco companies don't really possess. If you think about the route to consumer for next generation products, certainly for vaping products, 30-40% on average sits in the channels that you guys can see and track, i.e. convenience stores and key accounts; the rest of it sits in other channels and online. So, therefore the kind of capabilities that are required in order to execute against vapour are on top of the capabilities that one already has in a tobacco market, and we've been focused from the beginning of this journey on how do you integrate those capabilities into the same place, in order to be able to execute across the entire opportunity.

Portfolio

From a portfolio perspective I'll come on to talk about some of the formats but I would also call out our brand – Alison mentioned it earlier on, the blu brand. It's different, in my view, to the other brands that are on the market in this space. blu is about a lifestyle, blu is about emotion, blu is about engagement of the consumer and it's not about functional delivery. And that I think is going to play out quite significantly over the next year or two, particularly the ability to premiumise as a brand versus having to commoditise, which you're seeing other people having to do.

And from a footprint perspective, we're focused in the markets that we think are the right ones for us to win in. And we could easily spend a lot of money going into an awful lot of markets, and that's not the way we think about it. We think about how we can drive returns for shareholders, and therefore what are the markets that we think are ought to be focused on? And I'll come on and tell you a bit more about that in a minute.

Nerudia

Nerudia, going back to the capabilities, is a fantastic acquisition. We are absolutely thrilled with the potential and the addition that this brings. We've been focused on innovation for a few years. And what Nerudia bring is not only a new spark and a new insight into ways of thinking in this space, but they also bring a pipeline of absolutely fabulous ideas, which we're going to be looking to develop further. These are guys who've been at the forefront of nicotine and e-vapour innovation for the last nine or ten years. The kind of skillsets, to give you an idea of what their set-up is: they take their ideas, they rapidly prototype them; they science-test those ideas in real time, so that they know that there is an assured product that can go in a minimum viable product state to consumers quickly.

Now, that capability is not something that I think is widely held in the industry, and I think it's something that is going to bring a real advantage to us. I'm excited about the opportunity that they represent. They back that up with high quality pharma-grade manufacturing, regulatory assurance, testing capabilities; all of those sorts of things that you'd expect from a responsible manufacturer in this space. So I think it's a genuinely exciting opportunity. Everybody so far from Imperial and Fontem that have spent time with them come away in a completely different energetic space. Now, it's impossible to give you an insight really in terms of what their energy is like but we've tried. This video was put together by the Head of Innovation at Nerudia, who was asked by his boss to try and explain to other people in what does innovation mean for them, and this is what they came up with.

[VIDEO]

I hope to get them up here at some point for you to be able to actually engage with them, so you can get a better feel for it yourself.

Launches in FY18

Now, in terms of the launches that we are going to be bringing to market in FY18, they are significant. And to try and help you visualise the way that we're seeing the opportunity: we simplistically divide consumers into two camps.

The quitters

The first of those is the quitters, and they are people who are smokers who want to get away from a negative experience, are looking for something else. They're looking for a format that actually is fairly familiar with what they're used to. And they're really looking for a replication of the cigarette world but actually in a way that they think is a better choice. So, we've had a product for a number of years operating in this area, which is a product called blu PLUS, which is still an enormously successful product for us. It's got high loyalty, it makes us money, but actually it is in need of an upgrade. The technology is relatively old now and what we are bringing to market this year is a product called blu Max. So it's the same cigar-like format that smokers would recognise but it comes with more power and it comes with a responsive draw, which we think is one of the things which will overcome one of the barriers to smoker trial that has existed.

The enjoyers

The other end of the spectrum is the group of consumers that we internally call 'enjoyers.' Now, they're involved in vaping for a completely different reason. They have positive motivations for being in the category: they love the category, they love the devices, they love the flavours, they love customising. They are in a completely alternative world. It's not a smoking-world – left it behind, not interested, they've moved on. And we've had a product, or a platform, that has been trying to service this group of consumers, called blu PRO. There's a picture of it outside actually, and it makes you realise quite how quickly stuff moves on – it looks really old-fashioned now already. And what we're bringing to market in FY18 is an advanced tank, which actually provides the kind of experience that the enjoyers are looking for.

My blu

But the one that I'm excited about actually, is a product called called My blu, which is going to be launched in the US next month, and then it's going to be rolled out across our footprint. And this is a product that we think – it's a platform that we think is going to be of interest to both the quitters and to the enjoyers. Now, this is a platform which is a pod-based platform, so it's a closed system. And if you look at what's going on in the US market, you'll have heard of a brand called JUUL, I suspect, a number of you. They're operating with a similar format. And if you look at the growth in the US, actually largely vaping devices are fairly static, growing slightly but the growth is coming from this format. And we're excited to be bringing that to market next month. So those are the main platforms.

Juices

But just as important and what gets lost sight of, is that actually 70% of the NSV of this whole category sits in juices. It doesn't sit in the devices, it sits in the juices. Those are the reason that people come back, the brands and the juices; that's the loyalty. That's the razor blade of the razor blade model. And we think that that is a massive opportunity for us in the course of this year. We're going to be bringing to market more than 20 new juices during the course of 2018. And as you'd expect, they're going to be in a variety of nicotine down to non-nicotine strengths because there's a variety of consumers who – or a spectrum of consumers for whom this appeals.

But also interestingly, across the world as well we have the opportunity to be able to use not only free-based nicotine but also nicotine-salt, which is going to drive a significant trial but then retention from smokers. And the FDA has caused some complications to companies' ability to be able to use both this kind of technology but also those kind of juices, but that's not going to be a problem for us.

Footprint of Next Generation Products

Expansion in 2018 and 2019

So, finally just coming on to the footprint. This year we are going to move from the four core markets, the biggest four vaping markets that we have been focused on, and we're going to move to ten markets during 2018. And then we're going to go to at least 20 the following year.

A big opportunity from a smoker-transition perspective

Now, there are three messages I would leave you with in terms of how to think about this expansion. Our new products, as they get launched in 2018 – they haven't been launched yet – as they get launched in 2018, the numbers of smokers that those products will be targeting is more than 60 million currently. And as we move to the ten markets that number is going to double to more than 120 million smokers. Now, we see the ability with our products to be able to attract and transition those smokers as being a very real one. On top of those numbers, you've got the existing vapers, who are already significant. I'd remind you in the UK for example there are 3 million vapers currently – as many heated tobacco consumers as there are elsewhere in the world, there's already that many number of vapers in the UK; three or four times that number in the US. So they're on top of these sorts of numbers. So, a big opportunity from a smoker-transition perspective.

Additive revenue and profit opportunity

But the other interesting dynamic is that our market share, tobacco market share in these markets, is relatively low. So, you can see from the slide, we're averaging 13% market share on average across those ten markets, which actually means that more than 85% of our target consumers are not ours on the tobacco side. And therefore we think from an incremental and an additive revenue and profit perspective, represents a really interesting opportunity for Fontem and Imperial brands.

Interesting 'up-spending' opportunity

And the last thought to sort of leave you is that if you look at the spend of an average tobacco consumer in these markets, it's around £1,000 a year. In some places it'll be higher, some places it'll be slightly lower, but that's an average. And the average that vapers spend is significantly less than that, which, on the one hand, is great because with the products that we've coming now that drives trial, it drives people being willing to actually try it because it's a cheaper experience for them.

But the more interesting opportunity is that the up-spending potential, for want of a – I don't even know if that's a word but for an up-spending potential from a consumer perspective is significant because in their mind they're used to spending £1,000 a year. Our blu consumers on average probably spend with us about £300 a year. But actually the opportunity and the willingness to spend more than that, with the right products, I think is significant indeed, and it's something that we are focused on.

Summary

So, for all of those reasons, I think our relative size, our relative market share, our positioning with our brands: I think we've got an opportunity over the next year or two to make next generation products a really meaningful and additive element of our business going forward.

But I've done enough numbers so I'm going to hand over to Oliver.

Financial Overview and Looking Ahead

Oliver Tant

Chief Financial Officer, Imperial Brands

Overview of the Year*A year of significant investment*

Thank you very much Matt, and good morning everybody. I'm going to start with a slide which basically sets out a summary of our financial results, the results that we announced this morning. As I'm sure you're all aware, FY17 has been a significant year of investment to drive sustainable growth for the Group. And, as you've heard from my colleagues, we've deliberately focused this investment on our growth and specialist brands in those markets that are for us, as a business, the greatest opportunity. As a result of that, net revenue grew 8%, supported by a positive currency translation tailwinds. On a constant currency basis, revenue fell by 2.6%; that's reflecting the impact of a tougher industry environment and the additional investment we announced at the beginning of the year. As you can see, these impacts are reflected down through the P&L at adjusted operating profit and EPS, although we've sought to mitigate them through the profit line by taking decisive action on costs.

A year of two halves

It was also very much a year of two halves, as Alison has already highlighted. The first-half results were affected by our decision to substantially increase levels of investment and by lagging volumes, which had yet to really benefit from our investment activity. The second half, however, was quite different as we started to see the fruits of our investment. As our investment gained traction, we began to see more consistent share gains and volumes outperforming, which supported improving net revenue and profitability. Second-half volumes were down 2.6%, and price mix improved to deliver a return to modest growth in second-half revenue and profit against a tough industry environment.

Cash delivery

We also had another good year on cash delivery, with operating cash conversion at 91%. We generated £0.8 billion of available cash flow after dividend, to repay debt and strengthen our balance sheet. And we also grew our dividend by 10%; that's the ninth consecutive year of 10% dividend growth from Imperial Brands.

Cost optimisation

We've maintained our relentless focus on cost optimisation, and further benefits in the year to fund our investment and mitigate the trading environment. Our cost programmes remain on track to deliver combined incremental savings of £600 million by 2020, of which we've

realised £370 million to date. We're expecting to deliver another £100 million in the coming year, with a higher restructuring cash cost as compared to the current year – we're expecting at least £400 million in FY18. We've also sought to prioritise our cost saving and our investment behind a higher proportion of costs being dedicated to front-line activities, while continuing to refine our operating model to improve processes and reduce overhead cost.

Strong cash performance

Our continued focus on capital discipline has delivered another strong cash performance to support increased investment and dividend growth. We achieved a fourth consecutive year of cash conversion in excess of 90%; this at a time of increased investment and after over £200 million of cash restructuring spend.

Cash conversion would've been 96% if we'd excluded the restructuring spend; the exclusion of restructuring spend is something that many of our peers do in calculating their cash conversion numbers. This supported an £800 million net debt reduction, such that our net-debt-to-EBITDA ratio now stands at three times.

Looking ahead, we expect our priorities for free cash to focus on the 10% dividend promise, continued debt reduction to support a continued improvement in our gearing metrics. However, this will be balanced by an increasing level of investment in future growth, particularly next generation products, as outlined by Matt just a minute ago.

Operating profit

Adjusted operating profit has benefited from positive foreign exchange translation, and was up 6.2% at actual exchange rates. At constant currencies, operating profit declined by 3.2%, primarily reflecting the impact of the investment of £310 million. As you've already heard from my colleagues, there was a particularly tough trading environment this year, for example, in markets like Russia, Saudi Arabia and France. We estimate the impact of the tougher trading resulted in an additional headwind of around £200 million for the business.

Logista profitability also reflected that tougher trading environment, with a lower contribution particularly in the second half. However, we sought to offset this through further self-help measures, by managing some of our ongoing obligations through greater capital discipline. By making additional cost savings and realising non-core assets, this generated non-operating income of £114 million, which included £81 million from the UK pension scheme restructure. I'll address this in a bit more detail on the next slide.

Changes in the Operating Environment

Compared with when we announced the investment programme in November last year, as I said, the main thing that changed has been the operating environment has become much tougher. To respond to this, we were able to realise some of the cost optimisation savings earlier than originally anticipated, but we also took decisive action to realise other benefits.

Restructure of the UK pension fund

The largest contribution came from the difficult decision to restructure the UK pension scheme, in order to partly cap the company's liabilities and to strengthen the sustainability of the fund. Similar action has been undertaken by many other companies to manage future pension obligations. We also benefited from the disposal of non-core assets, such as from Logista's decision to sell their bank shares.

Priority to protect our investments

Now, individually all of these things were sensible actions to take, to either realise value or minimise liabilities, when managing a large business like Imperial Brands with a portfolio of assets and liabilities. Our priority over FY17 was to protect our investments. The easiest thing for us to have done would've been to cut those investments. Instead we looked hard for opportunities to fund the investment and mitigate the tough trading environment that we experienced. However, we do recognise we should probably have been a little more transparent with our disclosure around these activities, and therefore I'm undertaking to provide you with greater clarity and transparency in future.

Looking Ahead to FY18*More opportunities for non-operating income*

We have more opportunities to realise more non-operating income, and we expect around £50–100 million in FY18, and we'll keep you informed over the year how that progresses. Looking ahead to FY18, we'll maintain our focus on driving sustainable quality top-line growth.

Investment and cost discipline

We're pleased with how our investment is delivering stronger market share performances, as you can see from the presentations this morning. And this means for us sustaining FY17 levels of investment in tobacco. We'll also maintain our discipline around costs to support our sales agenda, including the cost optimisation programme, and the around £50–100 million of further non-operating income I just referred to.

Trading environment

We expect in FY18 the tax rate to remain broadly speaking around 20% and we expect the finance charge to be lower, reflecting the impact of deleverage. FX translation is currently expected to be about a 2% headwind, and we provide guidance on some of the other finance items in the appendices to this presentation. We do, however, remain cautious about the volatile trading environment following what we saw in FY17.

Guidance

Subject to this backdrop, we are targeting to return to our medium-term constant currency guidance in FY18 of 1–4% revenue growth and 4–8% of EPS growth, although EPS will be towards the lower end, given the increase in NGP investment which we've assumed in our plans. The phasing of the investment and the environment backdrop, which continues to be relatively challenging, is likely to weight that performance to favour a stronger second half.

Prospects

We have a strong balance sheet and industry-leading cash generation, which will continue to support our investment strategies and drive growth in our tobacco and next generation products, as well as further debt reduction and growing returns for shareholders.

Thank you very much. I'll hand back to Alison.

Closing Comments

Alison Cooper

Chief Executive Officer, Imperial Brands

Thanks Oliver. So a few brief closing comments. It's been a significant year of progress for Imperial. We've really stepped up investment in 2017, and that's delivered improved share gains and has very much strengthened the business for growth. The step-up of investment has clearly impacted the financials, along with the tough trading environment; we've taken action on cost to maintain and protect those investment. Difficult decisions but important decisions for the business.

It's been a significant year of progress for Imperial in 2017 and that sets us up well for 2018. We're going to build on the improved performance in the second half, both in our tobacco business but also as we look to realise opportunities in NGP in 2018. They're significant opportunities, and I'm excited about the pipeline of activities we have for 2018.

We're going to continue to sustain and protect the investment in the business, taking action on cost as necessary and also maintaining clearly the capital and cash discipline that we have in Imperial. This is really an important year for us in terms of further quality growth for the Group, but also continuing to support those shareholder returns.

So, thank you – it's been a much more significant length of presentation than usual. There's a lot of ground we wanted to cover with you but clearly there's always plenty of time for questions.

Q&A

Adam Spielman (Citi): Hi, it's Adam Spielman from Citi here. Can I ask two questions please? First of all, on the tougher operating environment, how should we think about that going forward? My understanding is you're referring to Saudi, and presumably the whole of the Gulf. We've had a tax increase. Presumably once we pass the anniversary that should improve. What about France? Let's talk about pricing of the tax increases there please. And Russia, some people are saying it's getting better. So that's one question. The other question: if the US tax reforms go through as they are currently planned, what will that do to your tax rate, and how do you think about it? Thank you.

Alison Cooper: Let me – I'll pick up on the tougher environment broadly. I'll get the guys to comment on the specific markets briefly, and then I think you get Oliver to talk tax. So, in terms of the tougher environment, I mean, it was significantly tougher in 2017 no doubt. And that's commentary that I think you've heard from the various industry players in terms of the environment in 2017, with various markets being called out. I think there's also commentary at the moment around people seeing an improving environment going into 2018, and we would echo that as well in a number of our markets. But there are a few that continue to be tough, who we're working through at the moment, considering some of the actions that have been taken, particularly by government as well.

So maybe it's worth a very brief comment on Saudi, Amal, and maybe on Russia as well. And I think if you can just pick up on France, although I know you've both commented in your presentation so, I think, keep it fairly brief.

Amal Pramanik: On Saudi, I think, as we see when there's a massive price increase that you have a big dip in the initial period and it bounces back to a large extent. It's too early to say how much it'll bounce back but definitely we are looking for FY18 to have some bounce-back. As you know, it happened only in June 2017 so we haven't had a long period of time yet. In terms of the premium segment decline, it is in line with what we were expecting, so it is not unusual.

In Russia, the regulatory change on the big pack, of course that has happened. We have now fully moved away from those big packs so there is nothing residual impact in FY18 for that. And of course the pricing environment has been quite tough. And current situation is possibly slightly better than what we had seen in the last six months, so that's all we are seeing right now. But of course let's see how the year pans out.

Dominic Brisby: Yes, in the case of France there have been a number of factors, so firstly, the introduction of plain packaging, which has had an impact. Secondly, a big tax increase which took place in FY17, which will be followed by a succession of quite large tax increases with the aim of getting the retail price to €10 per pack. So, that's been announced by the government.

Now, what's unclear in the case of France is whether the appetite for such significant excise increases will still be there when they assess what impact that has on their revenues. Because if you look at the nearest comparator in terms of heavy anti-tobacco legislation, the nearest comparator probably would be Australia. Of course, Australia doesn't have borders with anybody else and is quite a long way from other countries. In the case of France I think the risk of increased inflows from other markets having an impact, a heavy impact, on government revenues is quite significant. So we'll have to see how that finally pans out. But certainly at it stands at the moment, it's quite a tough market in terms of regulation and pricing.

Adam Spielman: And what about the fact that price was absorbed earlier this calendar year. Do you think that will continue with the next tax increase?

Dominic Brisby: I mean, we don't know what will happen with the next tax increase, clearly. What's odd in France is the mechanism for increasing prices is quite convoluted. So, the risk of that occurring in France are probably higher than the risk of it occurring elsewhere. But equally, the scale of tax increases, as they're currently planned, is so significant that that may also have an impact on what happens.

Oliver Tant: With regard to the exciting question of tax, of course, we welcome any reduction in the tax burden from a corporate perspective. And I guess, as I'm sure you all observed our US business is performing exceptionally strongly with a 23% increase in its profitability in FY18 in terms of actual. And, therefore, profit that would fall to tax. The reality is that we have a concession as a result of the ability to write off goodwill over a period of time against our US profits, which means a substantial portion of those profits actually don't fall to tax under that, or aren't actually taxed the marginal rate because we get that protection. So, the impact on our effective tax rate is, to some extent, diluted by the fact

that we're not paying a lot of tax on our US profits at the moment as it is. However, clearly, it will have an impact and I would expect it to provide against some other threats some relief to our effective tax rate over the longer term.

Fulvio Cazzol (Goldman Sachs): Good morning, this is Fulvio Cazzol from Goldman Sachs. I've got a couple of questions on NGPs, please. The first one is, are you able to give us what your average market share is across the four markets which have been in focus for you, i.e. to compare it with the 15% combustibles share? And then my second question is, can you give us an update of how much you have invested behind NGPs to date, i.e. excluding the £300 million that you've announced for 2018? Thank you.

Matt Phillips: I'll take the first one. The market share is not the right way of thinking about it, as I tried to explain, because the tracked retail is 30%-40% of the total. And it doesn't give a real insight in terms of the total market. So, it's difficult, is the answer. So, if I look at the US in your track channels, we're sitting at about 15%. If you're looking at the UK, it would slightly less. If you looked at Italy, it would be 40%. But actually, the tracked channel is an even smaller element of the total there. So, therefore, it's not the right way of trying to think about it.

In terms of the size of the opportunity, if that's what you're trying to get your mind around, the size of the opportunity is enormous. So, there are 10 million vapers in the US and there are 40 million smokers. That's the audience that we're focused on. And vaping tends to be 2-3% of the total nicotine market, but I think it's going to grow significantly.

Alison Cooper: And in terms of investment so far, we've currently spent roughly £400 million in terms of investment in the NGP space, a mixture of capital, but also some operating investment as well. The £300 million we're talking about, in terms of 2018, includes an increment of £50 million from an operating perspective – so it's £150 million total, but increment of £50 million on the operating side – and £150 million from a capital perspective, again, of which roughly £100 million is incremental. That just gives you the dimension on it. So, of the £300 million – Adam's looking slightly puzzled at me – £150 million is around operating investment, of which £50 million is incremental; £150 million is capital of which £100 million is incremental. Okay?

Okay. John. Someone else's got the microphone at the back, and then we'll come to John afterwards.

Owen Bennett (Jefferies): A couple of questions, please. I'm Owen Bennett at Jefferies. Firstly, you're targeting kind of the bottom end of your EPS guidance next year. I was just wondering given pricing industry-wide has been headwind this year, what sort of pricing you need to hit that guidance next year? And then secondly just on My blu, which sounds quite exciting in terms that you use the dual format, is that in the US already or that requires MRTB/BMT applications? And if so, what stage are you at with those applications? Thank you.

Alison Cooper: Okay. Just briefly in terms of the pricing we're assuming, we're assuming slightly better pricing in terms of our plans for next year, which aligns to the guidance we're giving in terms of the lower end of the EPS range. So, not to the lower end of FY17, but not to the levels that we've seen historically either. So, more to the 4-5% range in terms of price mix next year. And on My blu –

Matt Phillips: Yeah, it was in the US market ahead of the FDA deadline.

Matt Phillips: So, therefore, it will need supporting ahead of 2022, but it doesn't need anything ahead of that.

Alison Cooper: And it's going in next month.

John Leinster (Barenberg): John Leinster, Berenberg. A couple of things. Last year when you talk about the sort of rationalisation or the investment programme, there's obviously the price reductions but also the sort of big SKU reductions. Going forward, we've obviously heard about France and Russia, but where have the other big SKU reductions actually been completed, and what has been the response? And also, just have all those price repositions now been done? And secondly, on the blu, you mentioned sort of omni channels. How much of blu is actually sold online?

Alison Cooper: Okay. I'll pick up with the first piece, but then Amal can also briefly comment on other markets with the significant SKU reductions. I mean, as I talked about in the Market Repeatable Model, that simple market focus portfolio – the orange segment – is a really important part of what we're doing, from a driving sustainable and quality share growth perspective in those markets. So, the work on migrations that we've done over recent years, which I think we've done about 68 now with around about 95% consumer retention overall. But also, as you say, the radical SKU reductions, that's been an important part of our focus in different markets. Some of them have not had quite the level of percentage reduction opportunity that Russia and France have done, but still quite significant opportunities in terms of reduction. I showed you the MMC one in the US earlier as well. So, that's the – it's a very important area of our focus around the MRM. Do you want to just briefly comment on a couple of the markets, before I come onto the pricing?

Amal Pramanik: There are plenty of markets, like the Adriatic, that we've done analysis of all the markets. Just to give you a global perspective, we have already reduced our total brand count by 32% against the 50% that we had targeted by 2020. So, we have already achieved 32% in sales and marketing. And, in manufacturing we have already reduced by 40%. So, the impact in manufacturing has been even bigger than sales and marketing.

Dominic Brisby: I think the other point to add to this, of course, the SKU reduction is a means to an end. And the end is the optimal portfolio in the market. So, if you look at the markets where we've been particularly successful in growing market share this year, these are usually – not without exception, but usually the markets where we've been quite assiduous in reducing the number of SKUs. So, we make sure that our core range really is available in all the retailers. And then I'd say the two things have gone very much hand-in-hand.

Alison Cooper: On the pricing, I spoke specifically about the US earlier and I was clear this time last year that of the £300 million investment, £100 million of that was US and the vast majority of that was the full-year effect of the buy-down programmes in the US. So, you could describe the US clearly as getting the price positioning right there for the consumer in terms of the US brands.

In other markets, what we've been doing is really just making sure we're on competitive matching point in terms of our price points with those brands. So, it's been a little bit in the

UK where Player's was priced above where the competitive set was, which we've aligned. But other than that, it's really just been about consistently sticking with the right price points, matching the competitor brands during the year. The balance of the investment in terms of the £300 million has been around the other aspects of the MRM wheel, as I was articulating earlier.

Matthew Phillips: In terms of percentage of sales, online, I don't know off the top of my head. I mean, the important thing, though, is that from an execution perspective, online is going to be a much bigger focus in 2018 than it has been for us up until now. The digital strategy, the e-commerce strategy, a whole variety of different angles, which are all geared towards driving the number of consumers in the blu, which we call internal ecosystem in terms of – it is going to be a big focus for us. And if you think about retail margins in some of these markets, online is a significant opportunity. So, it's sort of redundant today, but I think over the – ask me again in a year, and my answer will be that online is very material.

Alison Cooper: Okay. Any more questions?

Fulvio Cazzol: Thank you for the follow-up. Can I just ask a follow up question to that? When do you expect your NGP business to become profitable?

Matthew Phillips: Our US business is profitable today. So, it depends on the speed of rollout and the number of markets and the level of investment. So, it will be a material revenue and profit generator for us, is the steer I'll give you, but I'm not putting a timeframe on it.

Fulvio Cazzol: And then another follow-up on heated tobacco. I know you didn't – you weren't – wouldn't be giving us more details, but you said it's about the optionality. So is the whole thinking behind that having a competitive product, so that if and when the category takes off in Europe, you'll have a response? Or would you be also thinking about expanding your geographic footprint if the product does stand up well to competitors?

Matthew Phillips: It's multiple platforms that we're going into testing with and we'll see how they do. Now right here, right now, our focus is on vapour. And in the markets that we think are the right ones for us to be winning in, we still think vapour is the right opportunity. But, the kind of scenarios you outline are absolutely the kind of things that we think about. It's important to maintain the optionality. But in terms of launch plans, let's see how the testing goes first.

Adam Spielman: Can I ask two follow-ups? First on the tobacco side, are there any markets that you're thinking about in 2018, do you think beyond the ones we've talked about, that will either be significantly harder or significantly more opportunity in? So, I'm just looking for, I don't know, let's say Netherlands – I'm making it up – is getting much easier for you. That's one question. The other question is the reason why I'm a little bit surprised is if I – just to make sure I've got this right, historically, in total, you've spent £400 million, a combination of CAPEX and operating investments, if you like, on next generation. In 2018, it's £300 million. I mean, that seems to me a huge step up. Have I heard that – have I understood that correctly? I mean, historically £400 million over n years.

Alison Cooper: It is not a huge step up on 2017. But yes, I suppose if you accumulate the other stuff that the cumulative up to 2017 is £400 million, basically. So, yeah. Harder

markets next year. France, I think that's probably the standout one in terms of harder markets.

Oliver Tant: Taiwan.

Alison Cooper: And Taiwan, which has also had a significant health tax increase, but we were already working through that. That's already in train and known about. Whereas France is the still the one that's just slightly uncertain in terms of how that's going to be implemented. In terms of better markets, I'd probably highlight Germany being a bit better, because of the additional industry headwinds we hit in 2017. It wasn't all about price and excise. About £50 million of that £200 million was in relation to markets being softer, particularly post EUTPD. And therefore, Germany, we're now seeing getting a bit better in terms of market size. So, that's going back to its more positive trajectory that we normally see in Germany. So, that one's I would think better compared to 2017, in terms of being significantly better.

John Leinster (Berenberg): Just a very quick one. Why the cash cost of restructuring is as much as £400 million going into 2018?

Oliver Tant: Well, it's around the timing of a number of programmes and the time to execution of those programmes. So, we have essentially a more significant outflow around a number of product cost programmes that occurs in FY18 as compared to FY17. In terms of factories there are some where we have scaled back. So, there are a number in France, which take effect. There are a number – but I'd rather not go through the precise detail of all the footprint that's in the £400 million, John, if that's alright, because we're not necessarily there with all of them.

Alison Cooper: Okay. Well thank you everyone. And no doubt, there's follow-up questions. We'll pick them up with the team. Have a good day.