IMPERIAL BRANDS PLC
FULL YEAR RESULTS STATEMENT

16 NOVEMBER 2021

A YEAR OF GOOD RESULTS WHILE BUILDING FOUNDATIONS FOR FUTURE GROWTH

Report for the year ended 30 September 2021

Business Highlights

- Transformation programme underway to create more consumer-focused, efficient and performance-driven organisation
- Operational improvements supporting growth in net revenue, profit and free cash flow
- Sharper focus on top-five priority markets beginning to arrest long-term share declines
- NGP pilots in heated tobacco and vapour on track
- Strong cash flows enabling deleverage progress in line with our plans

Financial Summary

Year ended 30 September 2021		Reported			Organic adjusted[2]			
		2021	2020	Change	**2021**	2020	Actual	Constant currency[3]
Revenue/Net revenue[1]	£m	**32,791**	32,562	+0.7%	**7,589**	7,738	-1.9%	+1.4%
Operating profit	£m	**3,146**	2,731	+15.2%	**3,570**	3,496	+2.1%	+4.8%
Basic earnings per share	pence	**299.9**	158.3	+89.5%	**246.5**	247.2	-0.3%	+2.8%
Free cash flow	£m	**1,524**	3,248	-53.1%	**1,524**	3,248	-53.1%	
Net debt	£m	**(9,373)**	(11,141)		**(8,615)**	(10,299)		
Dividend per share	pence	**139.08**	137.7	+1.0%	**139.08**	137.7	+1.0%	+1.0%

[1] Reported revenue includes duty, similar items, distribution and sale of peripheral products which are excluded from net revenue; net revenue comprises reported revenue less duty and similar items, excluding sale of peripheral products and distribution revenue.
[2] See page 3 for basis of presentation, page 28 and notes 3, 6 and 10 of the financial statements for the reconciliation between reported and adjusted measures. For comparison purposes, the Group uses the term "organic" to exclude the contribution of the Premium Cigar Division, which was divested on 29 October 2020.
[3] Constant currency removes effect of exchange rate movements on the translation of the results of our overseas operations.

Stefan Bomhard Chief Executive

"This has been a year of important progress and significant change, as we begin to deliver on the new, focused strategy we announced in January 2021. We have substantially refreshed our leadership team, making new hires to strengthen our consumer-facing capabilities, while building on our existing deep tobacco experience. We have changed the way we work, placing the consumer at the centre of our decision making. We have simplified the organisation, creating efficiencies for reinvestment. And we have introduced more rigorous performance management, enabling better prioritisation of resources.

"This approach is already delivering improved operational and financial outcomes. In tobacco, our sharper focus and increased investment in the top-five priority markets have begun to stabilise the aggregate market share performance. This is encouraging early progress in addressing the long-term historical declines. We will build on this foundation in the coming year, with further investment in brand building and sales execution.

"Through our focused, consumer-led next generation products strategy, we are committed to making a meaningful contribution to harm reduction over time by offering adult smokers potentially reduced risk products. In line with our plans, we launched market trials for our heated tobacco proposition, Pulze and iD sticks in the Czech Republic and Greece, as well as a trial of an improved consumer marketing proposition for our US vapour product, blu. We will track the consumer data over the coming months to inform our next steps.

"Our five-year plan to transform Imperial is divided into two distinct periods. The year ahead will complete the two-year *strengthening* phase, with further investment in our five priority markets and NGP pilots, the embedding of new ways of working and cost-saving initiatives. This period builds the foundations for the subsequent three-year phase, which focuses on the *acceleration* of returns and sustainable growth in shareholder value."

Delivering Against our Strategic Priorities

Focus on Priority Combustible Markets

- **Stabilising aggregate priority market share performances**: down 2 bps (MAT) vs 17 bps decline last year
- Share gains in US, UK, and Spain broadly offsetting declines in Germany and Australia
- Investing behind clear operational levers in line with our plans for our priority markets, for example:
  - **Expanding our sales force and enhancing sales execution**, e.g. adding 200 new sales people in US
  - **Leveraging our regional sales coverage**, e.g. expanding coverage in south of UK and in eastern Germany
  - **Building brand equity and increasing participation in subpremium**, e.g. JPS in Germany, Winston in US
  - **Optimising our approach to the value segment**, e.g. Parker & Simpson in Australia
  - **Rejuvenating our local jewel brands**, e.g. growing Embassy in the UK, Nobel and Fortuna in Spain
  - **Maximising the potential of fine-cut category**, e.g. leveraging Riverstone in Australia

Drive Value from our Broader Market Portfolio

- Strong Africa performance: net revenue up 8%; adjusted operating profit up 20%; share gains in several markets
- Group tobacco share growth of 20 bps (MAT) with share gains in all regions

Build a Targeted NGP Business

- Building foundations for a sustainable NGP business to underpin our commitment to harm reduction
- Heated tobacco trials of Pulze and iD in Greece and the Czech Republic progressing well
- Trial of a new consumer marketing proposition for our vapour product, blu, in Charlotte, North Carolina
- Resources prioritised behind the markets and categories with best sustainable growth prospects

Adopting New Ways of Working

- Leadership team strengthened with new hires bringing strong consumer goods experience
- New Group Consumer Office created to place consumer at centre of our thinking
- Restructured sales and marketing organisation to align with strategy and drive effectiveness
- Reshaped our divisions and reduced our market clusters from 13 to 10 to support market prioritisation
- Culture change underway with a reset of our purpose, vision and behaviours to support strategic delivery

Results Overview

Net revenue growth driven by resilient tobacco pricing

- **Organic net revenue up 1.4%** driven by tobacco growth of 1.5%; NGP net revenue down 3.9% reflecting market exits
- **Tobacco price mix up 4.4%** more than offset tobacco volume declines of 2.9%
- Excluding Australia stock profit effects, tobacco price mix up 5.6% and tobacco net revenue up 2.7%
- **Reported revenue grew 0.7%,** due to increases in excise duty

Delivering improved profitability

- **Organic adjusted Group operating profit up 4.8%** driven by reduced NGP losses and higher Distribution profit
- **Reported operating profit of £3,146m is higher by £415m,** driven primarily by gains on disposal of the Premium Cigar Division (£281m) and a reduction in amortisation and impairment of acquired intangibles (£73m)
- **Delivering against profit expectations despite absorbing headwinds of:**
  - lower stock profit in Australia (£88m) as previously guided
  - a charge to meet US state litigation costs (£52m), which removes uncertainty
- Excluding these factors, **underlying adjusted organic tobacco profit grew 2.7% or £98m**
- Including these factors, adjusted organic tobacco profit was lower by 1.2% (£42m)
- **NGP losses reduced by 56.7% to £138m** as we optimise investment and begin our market trials
- **Distribution adjusted operating profit (including eliminations) up 11.3%** driven by growth in pharmaceuticals
- **Organic adjusted EPS up 2.8% at constant currency** driven by growth in operating profit, partially offset by an increase in the tax rate to 22.6%
- **Reported basic EPS up 89.5% at 299.9p** reflecting marked to market foreign exchange accounting gains on financial instruments and the impact of the Premium Cigar disposal, with intangible write downs in the prior period and the profit on sale of assets booked this year

Strong free cash flow supporting investment, deleverage and progressive dividend

- **Strong cash conversion of 83%** in line with expectations reflecting unwind of prior year Logista working capital
- **Adjusted net debt reduced by £1.7bn due to strong free cash flow of £1.5bn**, a reduced dividend, proceeds from the sale of the Premium Cigar Division and FX translation
- **Net debt to EBITDA reduced to 2.2x** (2020: 2.7x) or 2.3x at constant exchange rates
- **Reported net debt reduced by £1.8bn**, broadly in line with reduction in adjusted net debt
- **Annual dividend per share up 1.0%** to 139.08 pence per share, in line with our progressive dividend policy

Outlook

We are making good progress with the implementation of our new strategy and we remain on track to deliver the five-year plan we set out in January 2021.

2022 is the second year of our two year strengthening phase, where we will step up investment behind our growth initiatives in our priority combustible markets, in our NGP trials and in our new ways of working. It will be a year of further reorganisation and change as we strengthen our foundations for the future.

At constant exchange rates, we expect to deliver net revenue growth at a similar rate to FY21, while adjusted operating profit is expected to grow slightly slower than net revenue, reflecting the step up in investment in line with our five-year strategic plan and after taking into account the non-repeat of the US state litigation settlement costs (net benefit of c. £40m in FY22).

We expect performance will be weighted to the second half reflecting the phasing of investment and the prior year comparator.

Some uncertainties remain about how the further lifting of COVID-19 restrictions will affect consumer buying patterns and the unwind of the small mix benefit in the past year. There is also risk of inflationary pressures although we are well placed to manage them through our purchasing strategy, high margins and pricing.

A higher effective tax rate of around 24 per cent is expected to be partly offset by lower interest costs. At current exchange rates, foreign exchange translation is expected to be broadly neutral on revenue and earnings per share.

Basis of Presentation

- To aid understanding of our results, we use 'adjusted' (non-GAAP) measures to provide a consistent comparison of performance from one period to the next. Reconciliations between adjusted and reported (GAAP) measures are also included in the relevant notes. Further definitions of adjusted measures are provided in Note 1 of these accounts. Change at constant currency removes the effect of exchange rate movements on the translation of the results of our overseas operations. References in this document to percentage growth and increases or decreases in our adjusted results are on a constant currency basis unless stated otherwise. These are calculated by translating current year results at prior year exchange rates.
- In these results, we also use the term organic to remove the impact of the divestment of our Premium Cigar Division to show a like-for-like performance, which is the basis of the performance commentary. The impact of the divestment is analysed in notes 3, 6 and 10 of the financial statements on adjusted performance measures.
- Stick Equivalent (SE) volumes reflect our combined cigarette, fine cut tobacco, cigar and snus volumes.
- Market share is presented as a 12-month average (MAT – moving annual trend), unless otherwise stated. Aggregate market share is a weighted average across markets within our footprint.

Other Information

Investor Contacts		Media Contacts	
Peter Durman	+44 (0)7970 328 093	Jonathan Oliver	+44 (0)7740 096 018
James King	+44 (0)7581 052 880	Simon Evans	+44 (0)7967 467 684
Jennifer Ramsey	+44 (0)7974 615 739		

Analyst Presentation Webcast

Imperial Brands PLC will be hosting a live webcast at 09:00 (GMT) for investors and investment analysts following the publication of our preliminary results on 16 November 2021. The webcast will be hosted by Stefan Bomhard, Chief Executive, and Lukas Paravicini, Chief Financial Officer. The presentation will be followed by a question and answer session. The presentation slides will be available on www.imperialbrandsplc.com from 07.00 (GMT). An archive of the webcast and the presentation script and slides will also be available.

Please either listen to the Q&A session via the webcast link: https://edge.media-server.com/mmc/p/uha45788 or to ask a question, please use the dial-in details below. Please dial-in at least 10 minutes prior to the start time to provide sufficient time to access the event. You will be asked to provide the conference ID number below.

Conference ID No: 5084104

United Kingdom: +44 (0) 20 7192 8338 or toll free: 0800 279 6619

USA: +1 646 741 3167 or toll free: +1 877 870 9135

Cautionary Statement

Certain statements in this announcement constitute or may constitute forward-looking statements. Any statement in this announcement that is not a statement of historical fact including, without limitation, those regarding the Company's future expectations, operations, financial performance, financial condition and business is or may be a forward-looking statement. Such forward-looking statements are subject to risks and uncertainties that may cause actual results to differ materially from those projected or implied in any forward-looking statement. These risks and uncertainties include, among other factors, changing economic, financial, business or other market conditions. These and other factors could adversely affect the outcome and financial effects of the plans and events described in this announcement. As a result, you are cautioned not to place any reliance on such forward-looking statements. The forward-looking statements reflect knowledge and information available at the date of this announcement and the Company undertakes no obligation to update its view of such risks and uncertainties or to update the forward-looking statements contained herein. Nothing in this announcement should be construed as a profit forecast or profit estimate and no statement in this announcement should be interpreted to mean that the future earnings per share of the Company for current or future financial years will necessarily match or exceed the historical or published earnings per share of the Company. This announcement has been prepared for, and only for the members of the Company, as a body, and no other persons. The Company, its Directors, employees, agents or advisers do not accept or assume responsibility to any other person to whom this announcement is shown or into whose hands it may come, and any such responsibility or liability is expressly disclaimed.

CHIEF EXECUTIVE'S STATEMENT

The right strategy, purpose and mindset

The strategy of Imperial Brands has three simple priorities. The first is to create sustained value in the combustible market through a focus on our priority markets where we can leverage our strengths. The second is to build a distinctive presence in next generation products (NGP), which, over time, delivers a material contribution both to harm reduction, through offering potentially reduced harm products to consumers, and investor returns. The third is to drive value from our broader global portfolio.

These priorities are mutually supportive. Scalable success in NGP requires both consumer focus and the full mobilisation of Imperial's core strengths in marketing, manufacturing and strong retail partnerships. At the same time, I believe our responsible, long-term commitment to improving the wellbeing of consumers provides a defining mission that energises the entire organisation.

Delivering on this strategy requires us to put the consumer at the centre of everything we do, to simplify our operations and to develop a rigorous performance culture.

As we build the foundations of this new culture, over the past year we have conducted a range of listening exercises with our 27,700 colleagues. Through this process, we developed a new statement of purpose: "Forging a path to a healthier future for moments of relaxation and pleasure".

Alongside the new strategy we have developed a vision statement which is "To build a strong challenger business powered by responsibility, focus and choice".

Our challenger mindset is an important and distinctive attribute. Although our brands have deep heritage, Imperial is, in important ways, a young company. This year marks our 25th anniversary as an independent public company and the key acquisitions that completed our global footprint occurred only in the past decade. In our recent history, we have been at our best when we have acted as an ambitious challenger, providing genuine choice for our customers and consumers, and an additional responsible industry player for regulators and policymakers.

After just over a year as CEO and having met many hundreds of colleagues, both virtually and face-to-face, I can confirm that this business retains that challenger spirit in abundance. However, as I said at the launch of our new strategy in January 2021, in order to make a reality of our ambition to put the consumer at the centre, we need to supplement our core strengths with additional capabilities in insights, innovation and product development.

I'd like to take this opportunity to thank our colleagues for their significant contribution, particularly with the challenges of a global pandemic.

Over the past 12 months we have assembled a diverse, new senior team and refreshed the way we work. This approach, bringing together our traditional strengths and future-facing capabilities, has led to improved operational and financial outcomes in line with our expectations.

The right team

Driving this new culture is the newly formed Executive Leadership Team (ELT). During the year, Andy Dasgupta joined in the newly created role of Chief Consumer Officer and a re-organisation of our reporting regions led to the appointment of Kim Reed as President and CEO of our Americas Region and Paola Pocci as President of Africa, Asia and Australasia (AAA). This new regional structure enables a sharper focus both on our largest market, the United States, and the portfolio of emerging markets that have the potential to become an important future growth engine. Javier Huerta joined as Chief Supply Chain Officer and Lukas Paravicini as Chief Financial Officer. A strengthened ELT team, collaborating closely with our experienced functional and market leaders, means Imperial now has the right blend of deep expertise of the tobacco industry and fresh ideas and perspectives from blue chip consumer goods companies, such as Nestlé, Unilever, P&G and Pepsi.

Placing the consumer at the centre of all our decisions

As Chief Consumer Officer, Andy Dasgupta is leading our focus on the consumer. Under him, we have adopted a more co-ordinated approach to how we collect and use consumer and competitor insights and data, which is leading to better-informed and faster decision-making. We are now building the right marketing, brand and portfolio management capabilities to support growth. In addition, Andy is leading a newly defined innovation programme that sits across tobacco and NGP to ensure we can meet consumer needs for new products, formats and experiences.

Embedding a high performance culture
We have taken action to embed a performance-based culture; one that holds our teams to account and rewards teamwork. For our top-five priority combustible markets this involved detailed monthly executive reviews of each market. We have revised incentive metrics for the Annual Bonus and Long-Term Incentive Plans (LTIP) to support our strategic objectives. We also have defined the new behaviours which will support the challenger-minded, consumer-centric and responsible culture we are creating at Imperial. In the coming year we will be rolling out a global programme to help our colleagues understand and embrace how they can best play a practical role in driving our transformation.

Simplifying our operations
To simplify our operations, we are restructuring the organisation to reallocate resources to the customer and consumer-facing areas in our priority markets while simplifying other aspects of operations. This is realising savings to fund our investment plans. For example, we have already restructured our sales and marketing organisation, reducing the number of market clusters from 13 to 10. In addition, our business services are implementing modern operating models, which will embed more effective ways of working.

The right performance

Our results reflect the actions taken to focus our investment tightly behind our priority markets and to drive a more rigorous approach to managing performance in tobacco and NGP. In tobacco, we have begun to stabilise the long-term aggregate market share declines in our five priority markets through a greater focus on performance management, brand refreshes and enhancing our sales footprint in select areas. On a constant currency basis, Group net revenues grew 1.4 per cent year-on-year reflecting continued strong pricing dynamics. Reported revenue grew 0.7 per cent at actual exchange rates. As anticipated, we grew our Group adjusted operating profit by 4.8 per cent in the year on a constant currency basis driven by a reduction in our NGP losses and higher Distribution profit from Logista. Reported operating profit grew 15.2 per cent at actual exchange rates. We delivered solid cash flow performance, generating £1.5 billion of free cash flow.

Focus on priority combustible market portfolio
Aggregate market share in our five priority combustible markets declined by just two basis points, compared to a 17 basis point decline last year. Share gains in the US, UK and Spain partially offset declines in Germany and Australia. This relative improvement reflects the benefit of the changes we are making to focus greater resource and more detailed performance management on these priority markets. We have begun to increase investment in these markets behind some clear operational levers, such as increased sales force and key account management, areas which were identified by the local teams. We are making good progress, although the main investment increase begins in the coming year. Further details are provided in the Operating Review.

Build a targeted NGP business
The NGP category remains relatively nascent in the majority of markets. We have an exciting opportunity to make a meaningful contribution to harm reduction by building a targeted and sustainable business in this market, offering potentially reduced risk products. Our new approach offers consumers greater choice in markets where they already express a preference for a particular proposition.

In heated tobacco, two trials in the Czech Republic and Greece with our Pulze and iD propositions have received a positive response from our trade partners and consumers. These are attractive markets because heated tobacco is already a well-established NGP category and we can leverage our existing route to market for combustible tobacco products. The valuable consumer insights we gain from these pilot initiatives will inform the scale and pace of further market rollouts.

In the United States we have also started trials for a revised proposition for our vapour product, blu, including more innovative consumer communication and customer support. We have chosen to do this in a focused geographic area to best assess the impact of our new approach.

Modern oral nicotine continues to perform well in Norway and Austria, markets where consumers have a preference for this type of proposition.

Deliver value from broader market portfolio
Our detailed strategic review created a clear role for each of Imperial's markets. The structured approach to market segmentation will drive our allocation of resources in terms of management time and investment. Our more focused approach has supported market share gains across the Group with overall tobacco share up 20 basis points year-on-year. Highlights include a strong performance from the African market cluster, which has grown share, net revenue and profit.

Environmental, social & governance (ESG)

Our approach to ESG supports our new business strategy and defines our responsibilities as a business. It is aligned with those UN Sustainable Development Goals which are most relevant to our Company strategy, namely consumer health, climate and energy, farmer livelihoods and welfare, human rights, and waste.

Furthermore, we have recently made a commitment to be net zero by 2040. We already have targets which are consistent with reductions required to limit climate warming to 2°C, which have been approved by the Science Based Targets initiative (SBTi). We intend to re-engage with SBTi to approve revised and more ambitious goals consistent with climate warming of 1.5°C and our net zero ambition.

We have strengthened our ESG team with the hiring of Tony Dunnage as global lead on ESG. Tony brings more than 30 years' experience in Unilever, directing end-to-end supply chain and manufacturing sustainability for 250-plus factories and reports directly to the ELT.

Capital allocation priorities

We have a clear capital allocation framework linked to our strategy to maximise returns for shareholders, with four clear capital priorities:

- Invest behind the new strategy to deliver the growth initiatives.
- Deleverage to support a strong and efficient balance sheet with a target leverage towards the lower end of our net debt to EBITDA range of 2-2.5 times.
- A progressive dividend policy with dividend growing annually taking into account underlying business performance.
- Surplus capital returns to shareholders to be considered once target leverage has been achieved.

This year we reduced adjusted net debt by £1.7 billion, on a constant currency basis, with net debt to EBITDA gearing reduced by 0.5 times to 2.2 times, at constant currency. At actual exchange rates, reported net debt reduced by £1.8 billion.

In line with our progressive dividend policy, the Board has decided to increase the dividend by 1.0 per cent, and we remain committed to providing a reliable, consistent cash return to shareholders.

Outlook

We remain on track to deliver against our strategy with our expectations for the coming year in line with the guidance we provided at our Capital Markets Day in January this year. At constant exchange rates, we expect to deliver net revenue growth at a similar rate to the 2021 financial year, while adjusted operating profit is expected to grow slightly slower than net revenue, reflecting the increased investment in line with our strategic plan.

Our five-year strategy to strengthen performance and deliver growing shareholder returns is divided into two distinct phases. The year ahead will complete the two-year 'strengthening' phase with further investment in our five priority markets and NGP pilots, the embedding of new ways of working and cost-saving initiatives in line with our plans. This builds the foundations for the subsequent three-year phase of our plan, in which we will accelerate returns and deliver sustainable growth in shareholder value.

STEFAN BOMHARD
CHIEF EXECUTIVE OFFICER

EUROPE REGION

		Full year result		Change	
		2021	2020	Actual	Constant currency
Tobacco volume	bn SE	**126.7**	130.1	-2.6%	
Total net revenue	£m	**3,551**	3,569	-0.5%	+0.2%
Tobacco net revenue	£m	**3,425**	3,471	-1.3%	-0.6%
NGP net revenue	£m	**126**	98	28.8%	28.8%
Adjusted operating profit	£m	**1,670**	1,582	5.6%	5.6%

Positives

- Germany and UK continue to deliver strong financial performances, with market size benefiting from reduced travel
- Local jewel brand focus benefits market share gains in Spain and the UK
- Heated tobacco market trials underway and targeted investment behind blu holding share

Negatives

- Reduced travel impacts sales in global duty free and traditional holiday destinations
- German share still declining although with an improving trend
- Travel recovery continues to remain difficult to predict due to varying COVID-19 restrictions across Europe

Europe delivered gains in regional market share and a 5.6 per cent increase in adjusted operating profit. These results have been achieved despite COVID-19 restrictions reducing travel and affecting market and channel trends, particularly the global duty free channel. Stronger market size trends in Northern Europe, together with share growth in the UK and Spain and improved NGP performance, were partly offset by lower sales in our global duty free business, despite a small second-half recovery, and in traditional holiday destination markets in Southern Europe.

Share gains in the UK and Spain were driven by our tobacco portfolio work and a new strategic focus on local jewel brands, such as Embassy and Nobel. In Germany, investments in enhancing the effectiveness and coverage of our sales force and distribution have driven an encouraging improvement in market share trend in recent months. It will take time though for our brand initiatives and portfolio investments to rejuvenate our overall share performance.

Tobacco volumes decreased by 2.6 per cent, driven by relative market size improvements in the Northern Europe markets of UK, Germany and Norway from consumers staying at home. A gradual recovery from COVID-19 led to a modest increase in travel numbers in the second half and a small improvement to our global duty free sales and southern European markets. Volume trends in Spain, Italy and Greece were still down relative to historic levels.

Total net revenue grew 0.2 per cent at constant currency, with tobacco net revenue down 0.6 per cent at constant currency. This reflects a price mix increase of 2.0 per cent, which is lower than recent years, as a result of temporary one-off benefits last year related to VAT changes in Germany and UK anti-forestalling arrangements. Excluding these temporary changes, price mix would have been 3.0 per cent, impacted by lower global duty free and travel retail sales. NGP revenues were up 28.8 per cent, with sales growth across a number of markets.

Our blu share in several markets such as the UK, France and Italy remains relatively stable. In heated tobacco we are on track with our pilot launches in the Czech Republic and Greece, although it is too early to draw conclusions until we review repurchase rates.

Adjusted operating profit was up 5.6 per cent at constant currency, benefiting from reduced losses in our NGP business and lower regulatory related costs.

Priority Markets in Europe

GERMANY

13% of Group net revenue

Duty paid sales in Germany continued to remain strong, with fewer travel and border restrictions benefiting market size. We increased investment to improve sales coverage and strengthen our sales execution to address the share declines. We have also begun to implement the planned brand investments to reposition certain brands over time. This includes innovation targeted at meeting consumer preferences for larger pack formats. In NGP, blu vapour brand share has been maintained with increased pricing and lower levels of investment improving returns. The modern oral nicotine category continues to wait for a clear legal definition, resulting in delays in category development.

UK

9% of Group net revenue

Reduced travel, lower levels of illicit trade and the absence of a manufacturing price increase benefited duty-paid tobacco market size, with an improved trend against historic norms. Our tobacco share performance benefited from an enhanced regional and key account focus, with growth driven from the launch of Embassy Signature. Market share was partly impacted by pressure following the characterising flavours ban in May 2020. Our blu vapour brand share remains stable, with refinements in our investment levels supporting improved profitability.

SPAIN

4% of Group net revenue

Reduced tourist numbers as a result of the global pandemic continue to negatively impact market size in Spain. Despite this, our domestic performance has benefited from a renewed focus on leveraging the strong heritage of our local brand portfolio. Increased investment behind our local brands, Fortuna and Nobel, combined with limited edition formats have supported market share growth. We also had success with a super-king variant of our West brand. blu remains market leader of the vapour category, with market share holding up well despite lower levels of investment.

AMERICAS REGION

		Full year result		Change	
		2021	2020	Actual	Constant currency
Tobacco volume	bn SE	**21.5**	21.3	1.1%	
Total net revenue	£m	**2,534**	2,480	2.2%	9.6%
Tobacco net revenue	£m	**2,478**	2,409	2.9%	10.4%
NGP net revenue	£m	**56**	71	-21.2%	-15.5%
Adjusted operating profit	£m	**1,037**	1,032	0.4%	8.0%

Positives

- Cigarette share growth up 20 basis points to 9.1 per cent
- Cigarette pricing remains strong
- Backwoods and Dutch Masters continue to perform strongly in the mass market cigar segment

Negatives

- Results affected by US state litigation settlement charges
- PMTA outcome still pending, creating lack of clarity for vapour category development

We delivered a strong combustible tobacco performance in the US, which is our largest single market, contributing 33 per cent of Group net revenue. Market fundamentals remain attractive, with strong cigarette pricing continuing to offset relatively reduced rates of tobacco market size decline as well as further growth in the mass market cigars segment.

We have increased investment behind our strategic priorities, including the recruitment and training of 200 additional sales people to enhance our coverage and distribution. We have also invested in brand initiatives for Winston, which we are trialling in Texas.

The investment and additional focus on performance management delivered a third consecutive year of share gains in the US cigarette market, up 20 basis points, to 9.1 per cent. Share growth has been driven by Sonoma and Crowns in the deep discount segment, while we have maintained Winston and Kool's share of their sub-premium categories and managed the ongoing decline in our non-focus brands.

Tobacco volumes were up 1.1 per cent, driven by strong mass market cigar growth, which more than offset the more moderate cigarette volume declines.

Our mass market cigar portfolio performed well with volumes up 45 per cent and share growth of 500 basis points driven by Backwoods and the launch of a Dutch Leaf variant in the value segment. We are now established as the second largest manufacturer in the US market, having been number four a year ago. Sales in the premium natural leaf segment have benefited from increased activations and limited edition launches of Backwoods. Overall mass market cigar performance also benefited from manufacturing and investments in improved leaf supply.

On a constant currency basis, tobacco net revenue increased by 10.4 per cent, benefiting from strong cigarette pricing and the success of our mass market cigar sales in a growing category.

Our NGP revenues were down 15.5 per cent on a constant currency basis, with second half revenues affected by the increasingly competitive environment with greater discounting in the category. In the second half, we launched a pilot to test a new consumer marketing proposition for blu, with a new packaging and consumer communication approach.

Adjusted operating profit was 8.0 per cent higher at constant currency, driven by the strong growth in mass market cigar sales, tobacco pricing and lower NGP write-offs. Profitability was also impacted by a £52 million charge for litigation settlement costs in Minnesota and Texas, which removes uncertainty at a reasonable cost. Excluding these settlement costs, adjusted operating profit grew by 13.1 per cent at constant currency.

AFRICA, ASIA AND AUSTRALASIA REGION

		Full year result		Change	
		2021	2020	Actual	*Organic constant currency
Organic tobacco volume	bn SE	**83.7**	87.4	-4.2%	
Total organic net revenue	£m	**1,504**	1,689	-11.0%	-8.2%
Organic tobacco net revenue	£m	**1,498**	1,657	-9.6%	-6.8%
NGP net revenue	£m	**6**	32	-81.1%	-78.3%
Organic adjusted operating profit	£m	**598**	643	-7.0%	-4.7%

* Organic performance excludes the contribution of the Premium Cigar Division from both financial reporting periods following its divestment in October 2020. The Premium Cigar Division contributed £21m to net revenue in 2021 (2020: £247m) and £3m to adjusted operating profit (2020: £31m). Further details are provided in notes 3, 6 and 10 of the financial statements.

Positives

- Australia share performance improved during the second half in response to investment
- Africa market share and financial performance benefits from focus on local jewel brands

Negatives

- Financial results affected by changes to Australia excise duty regime (£88m)
- NGP revenues lower due to strategic exits in Japan and Russia

Our results were affected by two events: the sale of the Premium Cigar Division in October 2020 and changes to the Australian excise regime. Notwithstanding these impacts, our Africa, Middle East and Asia regions reported solid performances and supported a 30 basis point improvement in overall regional share.

The results presented here are on an organic basis, excluding the contribution from the Premium Cigar Division in both periods to aid comparison of performance on a like-for-like basis. The impact of the divestment is analysed in notes 3, 6 and 10 of the financial statements on adjusted performance measures.

Our performance was also affected by changes in the Australian excise regime, which resulted in an impact on net revenue and adjusted operating profit of £88 million. This has been driven by the Australian Government's decision to step away from the 12.5 per cent annual excise duty accelerator and the associated reduction in inventory levels and the phasing of stock profit. Looking ahead, there will be a further net headwind of c. £10 million to net revenue and adjusted operating profit in the first half of FY22 as the lower stock profit is partially offset by favourable inventory movements.

The Africa region continues to be an attractive portfolio of markets with opportunities for further value growth. Gauloises gained share in Morocco by leveraging its international brand equity, while our focus on local jewel brands delivered share gains in Burkina Faso and the Côte d'Ivoire.

Our results in the Middle East were driven primarily by Saudi Arabia, where travel restrictions benefited our domestic sales, driving a good performance of Davidoff and West with strong demand for fresh seal formats.

In Asia, we delivered a stable performance in Taiwan driven by share growth of the Davidoff Absolute range supported by its strong equity and by West, which has benefited from value seeking consumers.

Organic tobacco volumes were 4.2 per cent lower, with volume declines in Turkey and Australia, partially offset by market share-driven volume gains in Morocco, the Côte d'Ivoire and Saudi Arabia.

Our organic financial results were affected primarily by the excise duty changes in Australia. Organic tobacco price mix of -2.6 per cent contributed to the tobacco net revenue decline of 6.8 per cent at constant currency, primarily reflecting the Australian excise duty changes. Excluding this impact, organic tobacco price mix was up 2.7 per cent and tobacco net revenue was down 1.5 per cent.

NGP net revenues declined 78.3 per cent at constant currency, reflecting our strategic decision to exit the vapour market in Russia and Japan and the heated tobacco market in Japan, as we prioritise investment in other market category combinations in line with our strategy.

Organic adjusted operating profit was down 4.7 per cent at constant currency, primarily reflecting the excise duty changes in Australia.

Priority Market in Africa, Asia and Australasia

AUSTRALIA

4% of Group net revenue

Our share performance has been affected by the timing of our price increase and competitor discounting, particularly in the first half of the year. We made changes to our sales force execution and enhanced our key account management, which delivered a much improved share trend in the second half. Our results were also affected by a market size decline of 9% and continued downtrading to the fifth price tier, which now accounts for more than a third of the market. Our Parker & Simpson brand continues to perform well within the 'fifth price tier'.

DISTRIBUTION

		Full Year Result		Change	
		2021	2020	Actual	Constant Currency
Net revenue	£m	**1,069**	1,015	+5.3%	+5.8%
Adjusted operating profit	£m	**258**	226	+14.2%	+ 14.8%
Adjusted operating profit margin	%	**24.1**	22.3	+180 bps	+180 bps
Eliminations	£m	**7**	13	-50.3%	-50.0%
Adjusted operating profit (inc. eliminations)	£m	**265**	239	+10.7%	+11.3%

Positives

- Continued distribution through COVID-19 as products and services classified as essential
- Strong performance in courier and long-distance transportation businesses
- New contracts in pharmaceutical distribution
- Efficiency improvement initiatives effective

Negatives

- Unwind of FY20 COVID-19 duty deferral impacted cash flow in the year

Logista has continued to distribute products to customers with almost all the points of sale, products and services classified as essential by governments, even during the periods when COVID-19 still restricted movements in many of its end markets.

Net revenue grew 5.8 per cent at constant currency driven by growth in all markets and activities except tobacco distribution in France and Portugal. Pharmaceutical distribution, parcel transport (Nacex) and the distribution of convenience products in Spain and Italy recorded double-digit growth. Adjusted operating profit increased 14.8 per cent at constant currency due to efficiency improvement initiatives.

The adjusted operating profit contribution to the Group, after eliminations, increased by 11.3 per cent. This reflects the positive performance of Logista's adjusted operating profit delivery as outlined above, the benefit of inventory valuations following tax and price movements in tobacco products and the recovery from negative COVID-19 impacts last year.

In line with other Imperial-owned entities, we continue to benefit from an intercompany cash pooling arrangement with Logista, which further enhances the Group's liquidity. On a 12-month basis, the daily average cash balance loaned to the Group by Logista was £2.0 billion, with movements in the cash position during the 12-month period varying from a high of £4.0 billion to a low of £1.3 billion, primarily due to the timing of excise duty payments. At the period end, the loan position was £1.8 billion compared to £2.4 billion at 30 September 2020.

This year's financial results reflect the good start we have made in implementing our new strategy. Excluding the divestment of our Premium Cigar Division, net revenues grew 1.4 per cent and organic Group adjusted operating profit rose 4.8 per cent, both on an organic constant currency basis.

Reported operating profit rose 15 per cent, mainly due to a profit of £281 million related to the disposal of the Premium Cigar Division.

Our business remains cash generative, delivering £1.5 billion of free cash flow, and this, together with other actions taken, has enabled us to reduce reported net debt by £1.8 billion to £9.4 billion.

Capital discipline remains a key focus and our objective to delever continues, with net debt/EBITDA reducing from 2.7x in 2020 to 2.2x in 2021. We remain committed to delivering leverage at the lower end of 2.0x to 2.5x.

In line with our strategic ambition, 2021 was a key transitional year in our two year strengthening phase during which we are building the foundations for future growth, underpinned by investments behind our operational and strategic levers and significant organisational and cultural change.

SUMMARY INCOME STATEMENT

	Reported		Adjusted		Organic Adjusted	
£ million (unless otherwise indicated)	**2021**	2020	**2021**	2020	**2021**	2020
Operating profit						
Total Tobacco & NGP	**2,991**	2,587	**3,308**	3,288	**3,305**	3,257
Distribution	**148**	131	**258**	226	**258**	226
Eliminations	**7**	13	**7**	13	**7**	13
Group operating profit	**3,146**	2,731	**3,573**	3,527	**3,570**	3,496
Net finance costs	**81**	(610)	**(417)**	(429)	**(417)**	(429)
Share of profit of investments accounted for using the equity method	**11**	45	**11**	45	**7**	1
Profit before tax	**3,238**	2,166	**3,167**	3,143	**3,160**	3,068
Tax	**(331)**	(608)	**(716)**	(642)	**(714)**	(635)
Profit for the year	**2,907**	1,558	**2,451**	2,501	**2,446**	2,433
Earnings per ordinary share (pence)	**299.9**	158.3	**247.1**	254.4	**246.5**	247.2
Dividend per share (pence)	**139.08**	137.71	**139.08**	137.71	**139.08**	137.71

Adjusted performance measures

When managing the performance of our business we focus on non-GAAP measures, which we refer to as adjusted measures. Management believes that adjusted measures provide an important comparison of business performance and reflect the way in which the business is controlled. These adjusted measures are supplementary to, and should not be regarded as a substitute for GAAP measures, which we refer to as reported measures. The basis of our adjusted measures is explained in our accounting policies note, which is detailed within our financial statements.

Reconciliations between reported and adjusted measures are included in the appropriate notes to our financial statements and within this financial review. Percentage growth figures for adjusted results are given on a constant currency basis, where the effects of exchange rate movements on the translation of the results of our overseas operations are removed.

This year we also show organic numbers which exclude the disposed operations of our Premium Cigar Division from both years to show a like-for-like performance; these measures are termed "organic adjusted" and are considered the relevant headline measures for performance commentary. The impact of these changes can be seen in our adjusted performance measures note.

SUMMARY CASH FLOW STATEMENT – STATUTORY RECONCILIATION

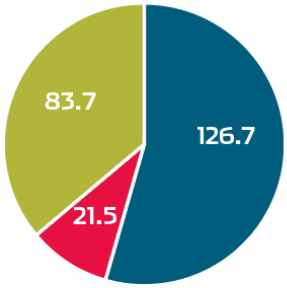
	Reported		Adjusted	
£ million (unless otherwise indicated)	**2021**	2020	**2021**	2020
Group Operating Profit	**3,146**	2,731	**3,573**	3,527
Depreciation, amortisation and impairments	**815**	910	**269**	311
EBITDA	**3,961**	3,641	**3,842**	3,838
Profit on disposal of subsidiary	**(281)**	–	**–**	–
Other non-cash movements	**(29)**	(85)	**(79)**	(137)
Operating Cash Flows before movement in Working Capital	**3,651**	3,556	**3,763**	3,701
Working capital	**(664)**	1,042	**(664)**	1,042
Tax cash flow	**(820)**	(568)	**(820)**	(568)
Cash Flows from Operating Activities	**2,167**	4,030	**2,279**	4,175
Net capex	**(150)**	(274)	**(150)**	(274)
Restructuring	**–**	–	**(112)**	(145)
Cash interest	**(400)**	(420)	**(400)**	(420)
Loan to third parties	**–**	(3)	**–**	(3)
MI dividends	**(93)**	(85)	**(93)**	(85)
Free Cash Flow	**1,524**	3,248	**1,524**	3,248
Acquisitions / disposals	**845**	(155)	**845**	(155)
Shareholder dividends	**(1,305)**	(1,753)	**(1,305)**	(1,753)
Net Cash Flow	**1,064**	1,340	**1,064**	1,340
Cash Flows from Operating Activities (as above)			**2,279**	4,175
Tax cash flow			**820**	568
Net capex			**(150)**	(274)
Net Cash Flow from Operating Activities post Capital Expenditure pre Interest and Tax			**2,949**	4,469
Cash Conversion			**83%**	127%

GROUP RESULTS – ORGANIC ADJUSTED CONSTANT CURRENCY ANALYSIS

£ million (unless otherwise indicated)	**Full year ended 30 September 2020**	**Foreign exchange**	**Constant currency movement**	**Full year ended 30 September 2021**	**Change**	**Organic constant currency change**
Organic Tobacco & NGP Net Revenue						
Europe	3,569	(27)	**9**	**3,551**	**-0.5%**	**0.2%**
Americas	2,480	(184)	**238**	**2,534**	**2.2%**	**9.6%**
Africa, Asia and Australasia	1,689	(47)	**(138)**	**1,504**	**-11.0%**	**-8.2%**
Total Group	7,738	(258)	**109**	**7,589**	**-1.9%**	**1.4%**
Organic Tobacco & NGP Adjusted Operating Profit						
Europe	1,582	(1)	**89**	**1,670**	**5.6%**	**5.6%**
Americas	1,032	(78)	**83**	**1,037**	**0.4%**	**8.0%**
Africa, Asia and Australasia	643	(15)	**(30)**	**598**	**-7.0%**	**-4.7%**
Total Group	3,257	(94)	**142**	**3,305**	**1.5%**	**4.3%**
Distribution						
Net revenue	1,015	(5)	**59**	**1,069**	**5.3%**	**5.8%**
Adjusted operating profit including eliminations	239	0	**26**	**265**	**10.7%**	**11.3%**
Group Organic Adjusted Results						
Organic adjusted operating profit	3,496	(94)	**168**	**3,570**	**2.1%**	**4.8%**
Adjusted net finance costs	(429)	(1)	**13**	**(417)**	**2.7%**	**3.1%**
Organic adjusted EPS (pence)	247.2	(7.7)	**7.0**	**246.5**	**-0.3%**	**2.8%**

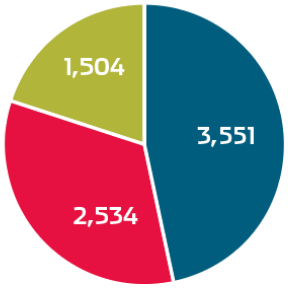
Financials are Organic and adjusted for the impact the Premium Cigar Divisions disposal, all of which is in the Africa, Asia and Australasia segment. Net Revenue has been deducted £247m in 2020 and £21m in 2021. Adjusted Operating Profit has been deducted £31m in 2020 and £3m in 2021.

VOLUMES BN SE



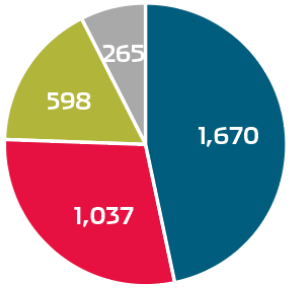
Europe	126.7
Americas	21.5
Africa, Asia and Australasia	83.7

ORGANIC NET REVENUE (ACT RATE), £M



Europe	3,551
Americas	2,534
Africa, Asia and Australasia	1,504

ORGANIC OPERATING PROFIT, £M



Europe	1,670
Americas	1,037
Africa, Asia and Australasia	598
Distribution	265

SALES PERFORMANCE

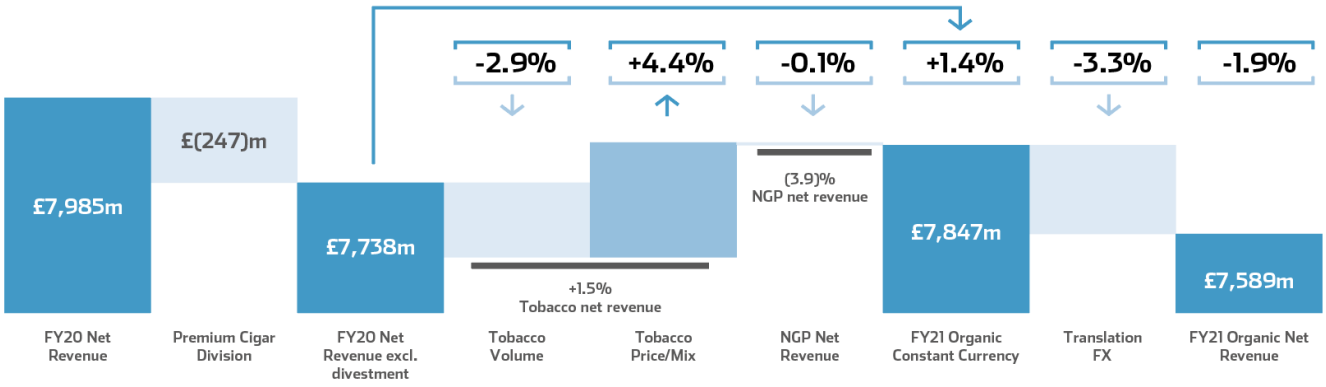
REPORTED REVENUE

+0.7%

ORGANIC ADJUSTED NET REVENUE

+1.4%

- Reported revenue grew 0.7% due to increases in duty and similar items.
- Organic net revenue grew 1.4% at constant currency comprising +1.5% from tobacco and -0.1% from NGP.
- Organic tobacco volumes were down 2.9%, in line with the market decline reflecting weaker duty free and travel retail volumes. This was partly offset by stronger market size in domestic markets such as the UK, Germany and the Nordics.
- Weighted share in our priority markets declined marginally by 2bps, compared to a 17bps decline in the prior year.
- Tobacco price mix of 4.4% was below historic levels, as a result of changes to the Australian excise regime. Excluding this impact price mix was 5.6% driven by pricing and positive market mix as a result of significant growth in US mass market cigars and repatriation of volumes due to travel restrictions.
- NGP revenue decreased 3.9% at constant currency as we exited a number of markets and refocused the category in line with the revised strategy.
- Translation FX was adverse due to sterling strengthening against the US dollar.



OPERATING PROFIT

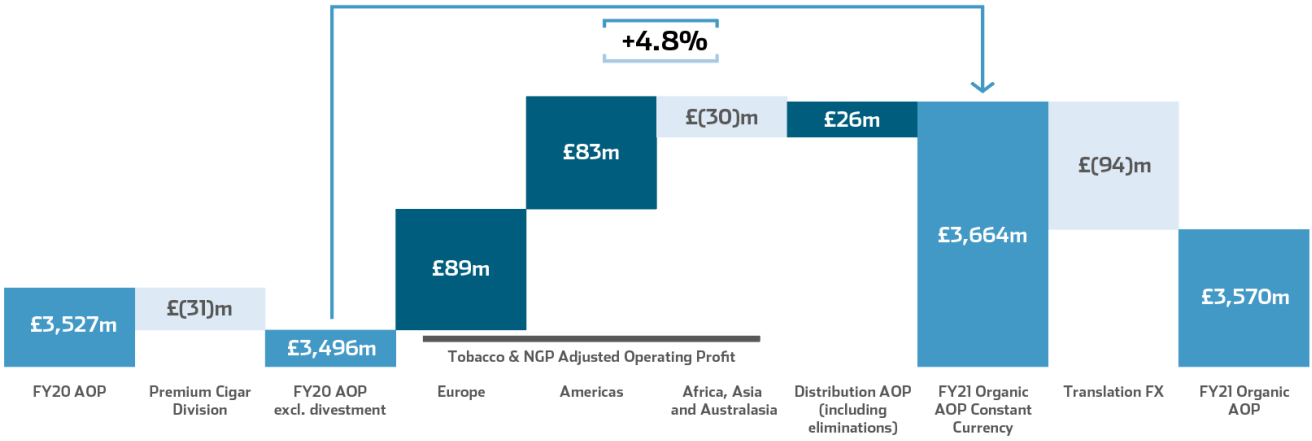
REPORTED OPERATING PROFIT

+15.2%

ORGANIC ADJUSTED OPERATING PROFIT

+4.8%

- Reported Group operating profit of £3,146 million grew 15.2%, driven by gains on disposal of the Premium Cigar Division.
- Organic adjusted Group operating profit increased 4.8% at constant currency.
- Tobacco and NGP adjusted operating profit grew £142m or 4.3% at constant currency.
- Tobacco organic adjusted operating profit was down £42 million (-1.2%) at constant currency. Strong underlying performance, led by mass market cigar volumes and pricing, was more than offset by lower stock profit in Australia (£88 million) and a charge to meet US state litigation (PSS) costs (£52 million)
- NGP losses reduced by £184 million or 57% as we optimised investment and as prior year write-downs (£124 million) were not repeated to the same extent.
- Distribution profit grew 11.3% reflecting good performance in pharmaceutical, parcel and convenience distribution.
- Translation FX was adverse due to sterling strengthening against the US dollar.



EARNINGS PER SHARE

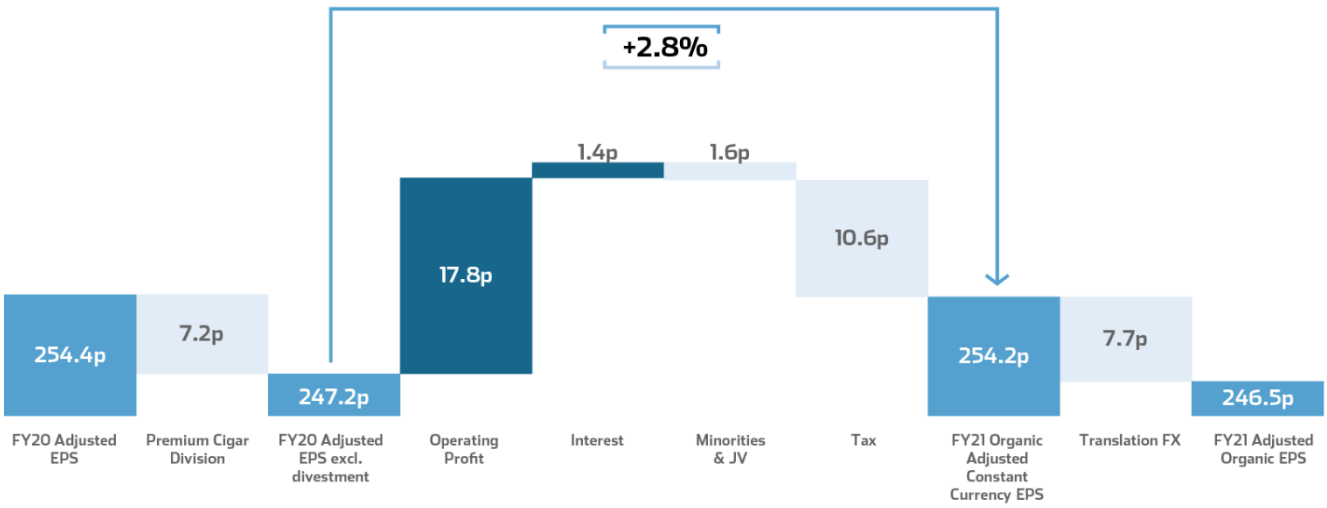
REPORTED EPS

+89.5%

ORGANIC ADJUSTED EPS

+2.8%

- Reported EPS increased 89.5% to 299.9 pence driven by marked to market foreign exchange accounting gains on financial instruments caused by a 6.0% weakening in the euro against sterling and the year-on-year impact of the Premium Cigar Division disposal.
- Organic adjusted EPS was 246.5 pence, up 2.8% at constant currency due to lower NGP losses, partially offset by an increase in the effective tax rate to 22.6%.
- Adjusted net finance costs are impacted by the buyback of a $1.25 billion US bond, with corresponding savings expected in 2022.



CASH FLOW

Cash flows from operating activities were £2,167 million (2020: £4,030 million), impacted primarily by an expected working capital outflow driven by changes to duty payment dates that we announced in 2020.

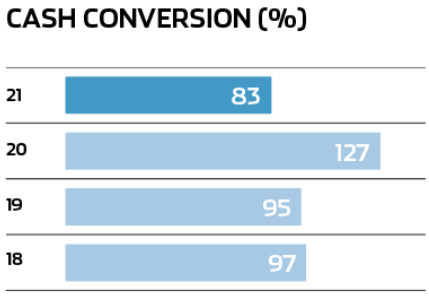
This also impacted free cash flow, with a £1.7 billion movement in working capital coming largely from our Logista markets in Western Europe, where governments changed the dates of excise collection linked to the COVID-19 pandemic.

Net cash flow of £1,064 million (2020: £1,340 million) benefited from the proceeds from the sale of the Premium Cigar Division and the planned rebase of shareholder dividends that partly offset the working capital outflow.

Capital expenditure was £0.2 billion, a reduction of £0.1 billion on the prior year. The reduction was due to the suspension of some projects whilst the strategic review was undertaken together with COVID-19 related delays on other projects.

Cash conversion was 83%, in line with expectations (2020: 127% headline / 107% underlying) driven by the previously signalled working capital outflow.

Active capital discipline remains a key focus for 2021 and beyond and this year's strong cash flows along with proceeds from the Premium Cigar Division disposal have supported our reduction in gearing to 2.2 times (2020: 2.7 times).



£ million (unless otherwise indicated)	2021	2020
Reported Cash Flows from Operating Activities	**2,167**	4,030
Reported Free Cash Flow	**1,524**	3,248
Reported Net Cash Flow	**1,064**	1,340
Cash Conversion	**83%**	127%

RETURN ON INVESTED CAPITAL

Return on invested capital (ROIC) increased by 130 basis points, driven primarily by a reduction in annual average capital.

As part of our FY21-23 LTIP we redefined our return on invested capital metric to better reflect management influence which resulted in a new, tightly defined and transparent ROIC calculation, which can be directly calculated from information contained within the Annual Report and Accounts.

Based on this new measure, 2021 average annual ROIC was 16.5% (2020: 15.2%, on equivalent basis).

A strong cash focus led to a £1.7 billion reduction in our annual average capital, driving an improvement in returns, with the benefit of increased adjusted operating profit offset by a higher effective tax rate of 22.6% (2020: 20.7%).

Our FY21 invested capital was lower than 2020, benefiting from the disposal of c. £1.0 billion of assets held for sale from the Premium Cigar Division and a c. £1.5 billion reduction in intangible assets due to a combination of the amortisation of historic acquisitions and beneficial foreign exchange movements. This was partly offset by an increase in working capital.

£m	2021	2020*	2019
Reported Operating Profit	**3,146**	2,731	
Adjusting Items (see note 6)	**427**	796	
Adjusted Operating Profit	**3,573**	3,527	
Implied Tax (at adjusted effective tax rate)	**(807)**	(730)	
Net Adjusted Operating Profit after tax	**2,766**	2,797	
Working capital	**(2,523)**	(3,467)	(2,461)
Intangible assets	**16,674**	18,160	18,596
Property, plant & equipment	**1,723**	1,899	1,979
Assets/(Liabilities) held for disposal	**(3)**	1,024	1,111
Invested Capital	**15,871**	17,616	19,225
Average Annual Invested Capital	**16,744**	18,421	
Average Annual ROIC	**16.5%**	15.2%	

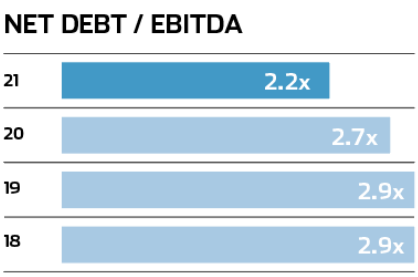
* 2020 calculated on the same basis as 2021.

ADJUSTED NET DEBT/EBITDA

Adjusted net debt/EBITDA reduced to 2.2x in 2021 from 2.7x in 2020. This was driven by a reduction in net debt from our cash flow generation and proceeeds from the Premium Cigar Division disposal. The Group also benefited from foreign exchange movements on our net debt position through the strengthening of sterling against the euro and US dollar. This lowered the Group's adjusted net debt based on the year-end balance sheet FX rates when compared to the prior year.

We remain committed to delivering leverage to the lower end of 2.0x to 2.5x.

Reported net debt reduced by £1,768 million to £9,373 million (2020: £11,141 million). Excluding accrued interest, lease liabilities and the fair value of derivative financial instruments providing commercial hedges of interest risk, Group adjusted net debt was £8,615 million (2020: £10,299 million).



£ million	2021	2020
Reported net debt	**(9,373)**	(11,141)
Accrued interest	**140**	156
Lease liabilities	**251**	299
Fair value of interest rate derivatives	**367**	387
Adjusted net debt	**(8,615)**	(10,299)

RECONCILIATION BETWEEN REPORTED AND ADJUSTED PERFORMANCE MEASURES

£ million unless otherwise indicated	Operating profit		Net finance costs		Earnings per share (pence)	
	2021	2020	**2021**	2020	**2021**	2020
Reported	**3,146**	2,731	**81**	(610)	**299.9**	158.3
Acquisition and disposal costs	**17**	26	**–**	–	**1.8**	2.8
Amortisation & impairment of acquired intangibles	**450**	523	**–**	–	**44.3**	49.2
Excise tax provision	**(1)**	(20)	**–**	–	**(0.1)**	(1.7)
Fair value adjustment of loan receivable	**(15)**	62	**–**	–	**(1.6)**	6.6
Profit on disposal of subsidiaries	**(281)**	–	**–**	–	**(29.7)**	–
Restructuring costs	**257**	205	**–**	–	**19.6**	18.4
Fair value and exchange movements on derivative financial instruments	**–**	–	**(496)**	176	**(60.7)**	25.3
Post-employment benefits net financing costs	**–**	–	**(2)**	5	**(0.3)**	0.4
Tax on disposal of premium cigar division	**–**	–			**(1.2)**	2.0
Previously unrecognised tax credits	**–**	–	**–**	–	**(25.3)**	(7.1)
Uncertain tax positions	**–**	–	**–**	–	**–**	8.2
Tax on unrecognised losses	**–**		**–**	–	**5.0**	(4.3)
Adjustments above attributable to non-controlling interests	**–**	–	**–**	–	**(4.6)**	(3.7)
Adjusted	**3,573**	3,527	**(417)**	(429)	**247.1**	254.4
Premium Cigar Divestment impact	**(3)**	(31)	**–**	–	**(0.6)**	(7.2)
Adjusted Organic	**3,570**	3,496	**(417)**	(429)	**246.5**	247.2

Adjusting items

In the 2020 Annual Report and Accounts we committed to reviewing our treatment of restructuring costs as an adjusted measure by the end of 2020 in line with the completion of the Cost Optimisation Programmes, which were due to conclude that year. However, as previously announced, the COVID-19 pandemic meant some of these programmes' projects were delayed into 2021, therefore we deferred the review of the treatment of restructuring costs as an adjusted item until the end of this year.

In January, we announced the outcome of our initial strategic review, including an associated and specific time-bound restructuring programme to deliver new ways of working and efficiencies, which we refer to as the 2021 Strategic Review Programme. This resulted in one-off costs to reshape the business to support delivery of the new strategy. The programme excludes any costs associated with factory footprint rationalisation. The restructuring costs for the 2021 Strategic Review Programme will be treated as an adjusting item in 2021 and 2022, by which time the activities are expected to have been actioned. No further costs outside of approved restructuring programmes will be charged to restructuring in 2022.

A reconciliation of the Group's adjusted to reported operating profit is shown above.

The profit on disposal of £281 million relates to the profit arising on the divestment of our Premium Cigar business that was recognised at half year 2021.

As part of the strategic review, a charge of £118 million was made in relation to the impairment of NGP intangible assets. Of this, £45 million was recognised as amortisation & impairment of acquired intangibles, these having previously been acquired as part of the Nerudia acquisition. The further amount of £73 million relates to internally generated intangibles and was recognised as restructuring costs.

The Auxly loan receivable was revalued as at 30 September 2021, with a £15 million gain recorded due to a positive credit risk reassessment.

Adjusting items also includes restructuring costs of £257 million, with further details available in the restructuring section below.

Following the announcement of the completion of the Premium Cigar Division divestment in September 2020, proceeds of €1,041 million were received as expected in FY21, with a further €88 million received in October 2021.

A further €69 million is expected to be received in 2022 in relation to the transfer of the La Romana factory in the Dominican Republic.

The 2021 charges in relation to these restructuring programmes are shown below.

£m	2021 Income Statement	2021 Cash
COP I	**7**	**12**
COP II	**16**	**41**
2021 Strategic Review Programme	**226**	**48**
Other	**8**	**11**
Total	**257**	**112**

An overview of the three programmes' cumulative charges, cash spend and annualised savings is shown below.

Restructuring charge & cash spend

	Income Statement Charges		Cash Costs		Savings
£m	Cumulative to date	Anticipated Total	Cumulative to date	Anticipated Total	Annualised Savings
COP I (2013)	945	945	571	634	305
COP II (2018)	848	848	548	650	320
2021 Strategic Review Programme	226	375-425	48	275	100-150

Restructuring

There are three restructuring programmes reflected in our 2021 results.

Cost Optimisation I Programme (COP I) announced in 2013 is now complete with small residual charges around the factory footprint activity.

Cost Optimisation Programme II (COP II), announced in 2018, is also now largely complete but did see a small carry over from activities scheduled for 2020 that were delayed due to the COVID-19 pandemic.

During the course of 2021, the Group announced a third programme as an output from the strategic review. This restructuring programme aims to reorganise and simplify the business, unlocking efficiency savings to enable increased investment in our core capabilities such as sales and marketing to support the five-year strategic plan. The majority of activity under this programme is expected in 2022 and will be treated as an adjusting item.

Since the strategy announcement, we have been working on detailed plans across a number of different initiatives. Following our detailed work we expect cash costs to be around £275 million, that will extend into 2023 and beyond with the associated restructuring costs expected to be in the range of £375 – £425 million.

The £257 million restructuring charge in 2021 comprised £226 million for the 2021 Strategic Review Programme, £23 million for COP I and II and £8 million of other costs that mainly related to Logista.

Finance costs

Adjusted net finance costs were lower at £417 million (2020: £429 million), reflecting lower adjusted net debt balances during the year. Reported net finance income was £81 million (2020: costs of £610 million), incorporating the impact of net fair value and exchange gains on financial instruments of £496 million (2020: losses of £176 million) and post-employment benefits net financing income of £2 million (2020: costs of £5 million). The gains on financial instruments primarily stem from foreign exchange accounting gains of £445 million as the value of euro financial instruments increased after sterling strengthened 6.0 per cent against the euro during the year.

Our all-in cost of debt increased to 4.0 per cent (2020: 3.4 per cent) as lower cost debt instruments matured in the year.

Our interest cover increased to 9.2 times (2020: 8.9 times) reflecting the lower adjusted finance costs.

Taxation

Our adjusted effective tax rate is 22.6 per cent (2020: 20.7 per cent) and the reported effective tax rate is 10.2 per cent (2020: 28.1 per cent). The increase in the adjusted effective tax rate was due to a less favourable profit mix and remeasurement of UK deferred tax balances. The adjusted tax rate is higher than the reported rate due to recognition of tax credits arising on an internal reorganisation of the Group's Spanish business and limited tax arising on both foreign exchange gains that arise on consolidation and on the disposal gain on the Premium Cigar Division disposal.

During the year a payment of £101 million was made to HMRC in respect of an on-going EU State Aid enquiry. A recoverable of the same value has also been recorded, as based on advice, we believe the Group has not received any State Aid. Further details are provided in Note 8.

We expect our adjusted effective tax rate for the year ended 30 September 2022 to be around 24 per cent. The increase in the rate in 2022 is due to legislative changes and certain historic tax losses being fully utilised in 2021.

The effective tax rate is sensitive to the geographic mix of profits, reflecting a combination of higher rates in certain markets such as the USA and lower rates in other markets such as the UK.

The rate is also sensitive to future legislative changes affecting international businesses such as changes arising from the OECD's (Organisation for Economic Co-operation and Development) Base Erosion and Profits Shifting (BEPS) work. Whilst we seek to mitigate the impact of these changes, we anticipate there will be further upward pressure on the adjusted and reported tax rate in the medium term.

Our Group Tax Strategy is publicly available and can be found in the governance section of our corporate website.

Exchange rates

Foreign exchange had an adverse impact on Group adjusted operating profit and earnings per share at average exchange rates (2.7 per cent and 3.1 per cent, respectively) as sterling strengthened against the US dollar (7.3 per cent). Other major currencies remained broadly flat compared to the prior year.

Dividend payments

The Group paid two interim dividends of 21.06 pence per share in June and September 2021.

The Board has approved a further interim dividend of 48.48 pence per share and will propose a final dividend of 48.48 pence per share, bringing the total dividend for the year to 139.08 pence.

The third interim dividend will be paid on 31 December 2021 to shareholders registered on 26 November 2021. Subject to AGM approval, the proposed final dividend will be paid on 31 March 2022 to shareholders registered on 18 February 2022.

In the year there were £1,305 million of shareholder dividend payments (2020: £1,753 million). The 25 per cent reduction represents the FY21 impact of the one-third rebasing of the dividend announced in May 2020 as part of the revised capital allocation policy to accelerate debt reduction.

Funding/Liquidity

During the year we repaid three bonds totalling £2.3 billion equivalent including the early repayment of a bond with a maturity date of July 2022. This was repaid from excess cash, which has the benefit of reducing gross debt as well as counterparty exposures. One bond of €1 billion was issued in the year with a maturity date in 2033. The denomination of our closing adjusted net debt was split approximately 77 per cent euro and 23 per cent US dollar. As at 30 September 2021, the Group had committed financing in place of around £12.7 billion, which comprised 24 per cent bank facilities and 76 per cent raised from capital markets. During the year the maturity date of our existing revolving credit facility of €3.5 billion was extended to September 2024 and bilateral facilities totalling €1.7 billion were cancelled.

The Group remains fully compliant with all our banking covenants and remains committed to retaining our investment grade ratings.

Liquidity and going concern statement

The Group's policy is to ensure that we always have sufficient capital markets funding and committed bank facilities in place to meet foreseeable peak borrowing requirements.

The Directors recognise that the current environment brings uncertainty due to the COVID-19 pandemic; however, over the last 18 months, the Group has effectively managed operations across the world, and has proved it has an established mechanism to operate efficiently despite the uncertainty. The Directors consider that a one-off discrete event with immediate cash outflow is of greater concern to short-term liquidity than any effect from the on-going COVID-19 pandemic.

The Directors have assessed the principal risks of the business, including stress testing a range of different scenarios that may affect the business. These included scenarios which examined the implications of:

- A one-off discrete event resulting in immediate cash outflow such as unexpected duty and tax payments of c£900m or non-receipt of the Premium Cigar Division deferred consideration of c£60m.
- A rapid and lasting deterioration to the Group's profitability because markets become closed to tobacco products or there are sustained failures to our tobacco manufacturing and supply chains. These assumed a permanent reduction in profitability of 15 per cent from 1 January 2022.

- The additional impact of potential bad debt risks arising from a recession of c£170m.
- The withdrawal of facilities that provide receivables factoring of c£670m.

The scenario planning also considered mitigation actions including reductions to capital expenditure and dividend payments. There are additional actions that were not modelled but could be taken including other cost mitigations such as staff redundancies, retrenchment of leases, and discussions with lenders about capital structure.

Under the worst-case scenario, where the largest envisaged downside scenarios all take place at the same time, the Group would have sufficient headroom until February 2022. The Group believes this worst-case scenario to be highly unlikely given the relatively small impact on our trading performance and bad debt levels during the Covid-19 pandemic. In addition, the Group has a number of mitigating actions available, as described above, that could be implemented should such a scenario arise.

Based on its review of future cash flows covering the period through to March 2023, and having assessed the principal risks facing the Group, the Board is of the opinion that the Group as a whole and Imperial Brands PLC have adequate resources to meet their operational needs from the date of this Report through to 31 March 2023 and concludes that it is appropriate to prepare the financial statements on a going concern basis.

LUKAS PARAVICINI
CHIEF FINANCIAL OFFICER

FINANCIAL STATEMENTS

The figures and financial information for year ended 30 September 2021 do not constitute the statutory financial statements for that year. Those financial statements have not yet been delivered to the Registrar.
The auditors have reported on those accounts and their report was (i) unqualified, (ii) did not include references to any matters to which the auditors drew attention by way of emphasis without qualifying their reports and (iii) did not contain a statement under section 498(2) or (3) of the Companies Act 2006 in respect of the accounts. The financial statements have been prepared in accordance with our accounting policies published in our financial statements available on our website www.imperialbrandsplc.com.

CONSOLIDATED INCOME STATEMENT

for the year ended 30 September 2021

£ million unless otherwise indicated	Notes	2021	2020
Revenue	3	**32,791**	32,562
Duty and similar items		**(16,229)**	(15,962)
Other cost of sales		**(10,535)**	(10,420)
Cost of sales		**(26,764)**	(26,382)
Gross profit		**6,027**	6,180
Distribution, advertising and selling costs		**(2,118)**	(2,329)
Acquisition and disposal costs		**(17)**	(26)
Profit on disposal of subsidiaries	11	**281**	–
Amortisation and impairment of acquired intangibles	12/15	**(450)**	(523)
Excise tax provision	8	**1**	20
Fair value adjustment of loan receivable		**15**	(62)
Restructuring costs	5	**(257)**	(205)
Other expenses		**(336)**	(324)
Administrative and other expenses		**(763)**	(1,120)
Operating profit	4	**3,146**	2,731
Investment income		**1,060**	770
Finance costs		**(979)**	(1,380)
Net finance income/(costs)	6	**81**	(610)
Share of profit of investments accounted for using the equity method	15	**11**	45
Profit before tax	4	**3,238**	2,166
Tax	8	**(331)**	(608)
Profit for the year		**2,907**	1,558
Attributable to:			
Owners of the parent		**2,834**	1,495
Non-controlling interests		**73**	63
Earnings per ordinary share (pence)			
– Basic	10	**299.9**	158.3
– Diluted	10	**299.1**	158.1

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

for the year ended 30 September 2021

£ million	Notes	2021	2020
Profit for the year		**2,907**	1,558
Other comprehensive income			
Exchange movements		**(680)**	151
Exchange movements recycled to profit and loss upon disposal of subsidiaries	11	**(337)**	–
Current tax on hedge of net investments and quasi-equity loans		**(105)**	(10)
Deferred tax on hedge of net investments and quasi-equity loans		**(12)**	(80)
Items that may be reclassified to profit and loss		**(1,134)**	61
Net actuarial gains on retirement benefits	24	**41**	277
Current tax relating to net actuarial gains on retirement benefits		**2**	–
Deferred tax relating to net actuarial gains on retirement benefits		**(21)**	(53)
Items that will not be reclassified to profit and loss		**22**	224
Other comprehensive (loss)/income for the year, net of tax		**(1,112)**	285
Total comprehensive income for the year		**1,795**	1,843
Attributable to:			
Owners of the parent		**1,761**	1,762
Non-controlling interests		**34**	81
Total comprehensive income for the year		**1,795**	1,843

CONSOLIDATED BALANCE SHEET

at 30 September

£ million	Notes	2021	2020
Non-current assets			
Intangible assets	12	**16,674**	18,160
Property, plant and equipment	13	**1,715**	1,899
Right of use assets	14	**242**	293
Investments accounted for using the equity method	15	**88**	117
Retirement benefit assets	24	**1,046**	940
Trade and other receivables	17	**62**	57
Derivative financial instruments	21/22	**391**	813
Deferred tax assets	23	**564**	381
State aid tax recoverable	8	**101**	–
		20,883	22,660
Current assets			
Inventories	16	**3,834**	4,065
Trade and other receivables	17	**2,749**	2,638
Current tax assets	8	**234**	206
Cash and cash equivalents	18	**1,287**	1,626
Derivative financial instruments	21/22	**68**	53
Current assets held for disposal	11	**35**	1,062
		8,207	9,650
Total assets		**29,090**	32,310
Current liabilities			
Borrowings	20	**(1,107)**	(1,442)
Derivative financial instruments	21/22	**(62)**	(41)
Lease liabilities	21	**(57)**	(64)
Trade and other payables	19	**(9,106)**	(10,170)
Current tax liabilities	8	**(253)**	(350)
Provisions	25	**(188)**	(220)
Current liabilities held for disposal	11	**(35)**	(38)
		(10,808)	(12,325)
Non-current liabilities			
Borrowings	20	**(8,715)**	(10,210)
Derivative financial instruments	21/22	**(984)**	(1,641)
Lease liabilities	20/21	**(194)**	(235)
Trade and other payables	19	**(7)**	(5)
Deferred tax liabilities	23	**(1,037)**	(924)
Retirement benefit liabilities	24	**(1,199)**	(1,256)
Provisions	25	**(206)**	(196)
		(12,342)	(14,467)
Total liabilities		**(23,150)**	(26,792)
Net assets		**5,940**	5,518
Equity			
Share capital	26	**103**	103
Share premium and capital redemption		**5,837**	5,837
Retained earnings		**(788)**	(2,364)
Exchange translation reserve		**200**	1,295
Equity attributable to owners of the parent		**5,352**	4,871
Non-controlling interests		**588**	647
Total equity		**5,940**	5,518

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

for the year ended 30 September 2021

£ million	Share capital	Share premium and capital redemption	Retained earnings	Exchange translation reserve	Equity attributable to owners of the parent	Non-controlling interests	Total equity
At 1 October 2020	**103**	**5,837**	**(2,364)**	**1,295**	**4,871**	**647**	**5,518**
Profit for the year	–	–	**2,834**	–	**2,834**	**73**	**2,907**
Exchange movements on retranslation of net assets	–	–	–	**(1,034)**	**(1,034)**	**(39)**	**(1,073)**
Exchange movements on net investment hedges	–	–	–	**476**	**476**	–	**476**
Exchange movements on quasi-equity loans	–	–	–	**(83)**	**(83)**	–	**(83)**
Exchange movements recycled to profit and loss upon disposal of subsidiaries	–	–	–	**(337)**	**(337)**	–	**(337)**
Current tax on hedge of net investments and quasi-equity loans	–	–	–	**(105)**	**(105)**	–	**(105)**
Deferred tax hedge of net investments and quasi-equity loans	–	–	–	**(12)**	**(12)**	–	**(12)**
Net actuarial gains on retirement benefits	–	–	**41**	–	**41**	–	**41**
Current tax relating to net actuarial gains on retirement benefits	–	–	**2**	–	**2**	–	**2**
Deferred tax relating to net actuarial gains on retirement benefits	–	–	**(21)**	–	**(21)**	–	**(21)**
Other comprehensive income	–	–	**22**	**(1,095)**	**(1,073)**	**(39)**	**(1,112)**
Total comprehensive income	–	–	**2,856**	**(1,095)**	**1,761**	**34**	**1,795**
Transactions with owners							
Costs of employees' services compensated by share schemes	–	–	**25**	–	**25**	–	**25**
Dividends paid	–	–	**(1,305)**	–	**(1,305)**	**(93)**	**(1,398)**
At 30 September 2021	**103**	**5,837**	**(788)**	**200**	**5,352**	**588**	**5,940**
At 1 October 2019	103	5,837	(2,255)	1,252	4,937	647	5,584
Profit for the year	–	–	1,495	–	1,495	63	1,558
Exchange movements on retranslation of net assets	–	–	–	(130)	(130)	18	(112)
Exchange movements on net investment hedges	–	–	–	12	12	–	12
Exchange movements on quasi-equity loans	–	–	–	251	251	–	251
Current tax on quasi-equity loans	–	–	–	(10)	(10)	–	(10)
Deferred tax on quasi-equity loans	–	–	–	(80)	(80)	–	(80)
Net actuarial gains on retirement benefits	–	–	277	–	277	–	277
Deferred tax relating to net actuarial losses on retirement benefits	–	–	(53)	–	(53)	–	(53)
Other comprehensive income	–	–	224	43	267	18	285
Total comprehensive income	–	–	1,719	43	1,762	81	1,843
Transactions with owners							
Costs of employees' services compensated by share schemes	–	–	20	–	20	–	20
Current tax on share-based payments	–	–	1	–	1	–	1
Repurchase of shares	–	–	(92)	–	(92)	–	(92)
Changes in non-controlling interests (note 12)	–	–	(4)	–	(4)	4	–
Dividends paid	–	–	(1,753)	–	(1,753)	(85)	(1,838)
At 30 September 2020	103	5,837	(2,364)	1,295	4,871	647	5,518

CONSOLIDATED CASH FLOW STATEMENT

for the year ended 30 September 2021

£ million	2021	2020
Cash flows from operating activities		
Operating profit	**3,146**	2,731
Dividends received from investments accounted for under the equity method	**4**	43
Depreciation, amortisation and impairment	**815**	910
Profit on disposal of non-current assets	**2**	(2)
Profit on disposal of subsidiary	**(281)**	–
Post-employment benefits	**(63)**	(88)
Costs of employees' services compensated by share schemes	**25**	20
Fair value adjustment of loan receivable	**(15)**	63
Movement in provisions	**18**	(121)
Operating cash flows before movement in working capital	**3,651**	3,556
Decrease in inventories	**70**	67
(Increase)/decrease in trade and other receivables	**(201)**	241
(Decrease)/increase in trade and other payables	**(533)**	734
Movement in working capital	**(664)**	1,042
Tax paid	**(820)**	(568)
Net cash flows generated from operating activities	**2,167**	4,030
Cash flows from investing activities		
Interest received	**15**	9
Loan to third parties	**–**	(3)
Proceeds from the sale of non-current assets	**50**	28
Net proceeds from sale of subsidiaries (note 11)	**845**	–
Deposit received from sale of asset held for sale	**–**	83
Purchase of non-current assets	**(200)**	(302)
Purchase of brands and operations (note 12)	**–**	(146)
Net cash used in investing activities	**710**	(331)
Cash flows from financing activities		
Interest paid	**(415)**	(429)
Lease liabilities paid	**(69)**	(72)
Increase in borrowings	**858**	1,240
Repayment of borrowings	**(2,224)**	(3,096)
Cash flows relating to derivative financial instruments	**41**	(23)
Repurchase of shares	**–**	(92)
Dividends paid to non-controlling interests	**(93)**	(85)
Dividends paid to owners of the parent	**(1,305)**	(1,753)
Net cash used in financing activities	**(3,207)**	(4,310)
Net decrease in cash and cash equivalents	**(330)**	(611)
Cash and cash equivalents at start of year	**1,626**	2,286
Effect of foreign exchange rates on cash and cash equivalents	**(9)**	13
Transferred to held for disposal (note 11)	**–**	(62)
Cash and cash equivalents at end of year	**1,287**	1,626

1. ACCOUNTING POLICIES

BASIS OF PREPARATION

The consolidated financial statements have been prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006 and International Financial Reporting Standards adopted pursuant to Regulation (EC) No.1606/2002 as it applies in the European Union.

The financial statements have been prepared under the historical cost convention except where fair value measurement is required under IFRS as described below in the accounting policies on financial instruments, and on a going concern basis.

BASIS FOR GOING CONCERN

The financial statements have been prepared under the historical cost convention except where fair value measurement is required under IFRS as described below in the accounting policies on financial instruments, and on a going concern basis. The Group's policy is to ensure that we always have sufficient capital markets funding and committed bank facilities in place to meet foreseeable peak borrowing requirements.

The Directors recognise that the current environment brings uncertainty due to the COVID-19 pandemic; however, over the last 18 months, the Group has effectively managed operations across the world, and has proved it has an established mechanism to operate efficiently despite the uncertainty. The Directors consider that a one-off discrete event with immediate cash outflow is of greater concern to short term liquidity than any effect from the on-going COVID-19 pandemic.

The Directors have assessed the principal risks of the business, including stress testing a range of different scenarios that may affect the business. These included scenarios which examined the implications of:

- A one-off discrete event resulting in immediate cash outflow such as accelerated duty and tax payments of circa £900 million or non-receipt of the Premium Cigar Division (PCD) deferred consideration of circa £60 million.
- A rapid and lasting deterioration to the Group's profitability because markets become closed to tobacco products or there are sustained failures to our tobacco manufacturing and supply chains. These assumed a permanent reduction in profitability of 15 per cent from 1 January 2022.
- The additional impact of potential bad debt risks arising from a recession of circa £170 million.
- The withdrawal of facilities that provide receivables factoring of circa £670 million.

The scenario planning also considered mitigating actions including reductions to capital expenditure and dividend payments. There are additional actions that were not modelled but could be taken including other cost mitigations such as staff redundancies, retrenchment of leases, and discussions with lenders about capital structure.

Under a worst-case scenario, where the largest envisaged downside scenarios all take place at the same time the Group would have sufficient headroom until February 2022. The Group believes this worst-case scenario to be highly unlikely given the relatively small impact on our trading performance and bad debt levels during the Covid-19 pandemic. In addition, the group has a number of additional mitigating actions available that could be implemented should such a scenario arise.

Based on the review of future cash flows covering the period through to March 2023, and having assessed the principal risks facing the Group, the Board is of the opinion that the Group as a whole and Imperial Brands PLC have adequate resources to meet their operational needs from the date of this Report through to 31 March 2023 and concludes that it is appropriate to prepare the financial statements on a going concern basis.

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses during the period and of assets, liabilities and contingent liabilities at the balance sheet date. The key estimates and assumptions are set out in note 2 Critical Accounting Estimates and Judgements. Such estimates and assumptions are based on historical experience and various other factors that are believed to be reasonable in the circumstances and constitute management's best judgement at the date of the financial statements. In the future, actual experience may deviate from these estimates and judgements. This could affect future financial statements as the original estimates and judgements are modified, as appropriate, in the year in which the circumstances change.

Imperial Brands PLC (the Company) provides guarantees to a number of subsidiaries under section 479A of the Companies Act 2006, whereby the subsidiaries, incorporated in the UK and Ireland, are exempt from the requirements of the Act relating to the audit of individual accounts for the financial year ending 30 September 2021. See note VII Guarantees of the Imperial Brands Plc financial statements for further details.

The principal accounting policies, which have been applied consistently other than where new policies (detailed below) have been adopted, are set out below.

BASIS OF CONSOLIDATION

The consolidated financial statements comprise the results of the Company, a public company limited by shares, incorporated in England and Wales, and its subsidiary undertakings, together with the Group's share of the results of its associates and joint arrangements. The Company's registered number is 3236483 and its registered address is 121 Winterstoke Road, Bristol, BS3 2LL.

Subsidiaries are those entities controlled by the Group. Control exists when the Group is exposed to, or has the rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Where necessary, accounting policies of subsidiaries are changed to ensure consistency with the policies adopted by the Group.

The acquisition method of accounting is used to account for the purchase of subsidiaries. The excess of the value transferred to the seller in return for control of the acquired business together with the fair value of any previously held equity interest in that business over the Group's share of the fair value of the identifiable net assets is recorded as goodwill.

Intragroup transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless costs cannot be recovered.

JOINT VENTURES

The Group applies IFRS 11 to all joint arrangements. Under IFRS 11 investments in joint arrangements are classified as either joint operations or joint ventures depending on the contractual rights and obligations of each investor. The Group has assessed the nature of its joint arrangements and determined them to be joint ventures. The financial statements of joint ventures are included in the Group financial statements using the equity accounting method, with the Group's share of net assets included as a single line item entitled 'Investments accounted for using the equity method'. In the same way, the Group's share of earnings is presented in the consolidated income statement below operating profit entitled 'Share of profit of investments accounted for using the equity method'.

FOREIGN CURRENCY

Items included in the financial statements of each Group company are measured using the currency of the primary economic environment in which the company operates (the functional currency).

The income and cash flow statements of Group companies using non-sterling functional currencies are translated to sterling (the Group's presentational currency) at average rates of exchange in each period. Assets and liabilities of these companies are translated at rates of exchange ruling at the balance sheet date. The differences between retained profits and losses translated at average and closing rates are taken to reserves, as are differences arising on the retranslation of the net assets at the beginning of the year.

Transactions in currencies other than a company's functional currency are initially recorded at the exchange rate ruling at the date of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at exchange rates ruling at the balance sheet date of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated income statement with exchange differences arising on trading transactions being reported in operating profit, and those arising on financing transactions being reported in net finance costs unless as a result of net investment hedging they are reported in other comprehensive income.

The Group designates as net investment hedges certain external borrowings and derivatives up to the value of the net assets of Group companies that use non-sterling functional currencies after deducting permanent intercompany loans. Gains or losses on these hedges that are regarded as highly effective are transferred to other comprehensive income, where they offset gains or losses on translation of the net investments that are recorded in equity, in the exchange translation reserve.

The Group's financial results are principally exposed to euro and US dollar exchange rates, which are detailed in the table below.

	2021		2020	
Foreign exchange rate versus GBP	**Closing rate**	**Average rate**	Closing rate	Average rate
Euro	**1.1621**	**1.1451**	1.0960	1.1393
US Dollar	**1.3456**	**1.3690**	1.2832	1.2753

REVENUE RECOGNITION

For the Tobacco & Next Generation Products (Tobacco & NGP) business, Revenue comprises the invoiced value for the sale of goods net of sales taxes, rebates and discounts. Revenue is based on the completion of performance obligations that constitute the delivery of goods. The performance obligation is recognised as complete at the point in time when a Group company has delivered products to the customer, the customer has accepted the products and collectability of the related receivables is reasonably assured. The distribution business also recognises revenue associated with logistics services, recognised on the basis of the invoiced value for the provision of these services net of sales taxes, rebates and discounts. The performance obligations associated with distribution services, which include fees for distributing certain third party products, are linked to the successful distribution of products for customers.

The Group recognises income arising from the licensing of intellectual property, occurring in the ordinary course of business, which is treated as revenue. Licensing revenue will be recognised over the period of the licence. The licences granted are distinct from other promises in the contract.

For the Distribution business, revenue comprises the invoiced value for the sale of goods and services net of sales taxes, rebates and discounts when goods have been delivered or distribution services have been provided. The Distribution business only recognises commission revenue on purchase and sale transactions in which it acts as a commission agent. Distribution and marketing commissions are included in revenue. Revenue is recognised on products on consignment when these are sold by the consignee.

Payments are made to both direct and indirect customers for rebates, discounts and other promotional activities. Direct customers are those to which the Group supplies goods or services. Indirect customers are other entities within the supply chain to the end consumer. Rebates and discounts are deducted from Revenue. Where the contract with customers has an entitlement to variable consideration due to the existence of retrospective rebates and discounts, revenue is estimated based on the amount of consideration expected to be received. This estimation is a determination of the most likely amount to be received using all known factors including historic experience. Typically there is a high degree of certainty over the amount of retrospective rebates/discounts paid due to relatively low year on year variations in the volume and pattern of product sales. As the provision of distribution services typically involves product delivery tasks undertaken in a short period of time, revenue and any associated rebates and discounts relating to these services do not normally span an accounting year end.

Payments for promotional activities will also be deducted from Revenue where the payments relate to goods or service that are closely related to or indistinct from associated sales of goods or services to that customer. The calculated costs are accrued and accounted for as incurred and matched as a deduction from the associated revenues (i.e. excluded from revenues reported in the Group's consolidated income statement).

DUTY AND SIMILAR ITEMS

Duty and similar items includes duty and levies having the characteristics of duty. In countries where duty is a production tax, duty is included in Revenue and in Cost of sales in the consolidated income statement. Duty is regarded as a sales tax and excluded from revenue where:

- duty becomes payable to the tax authority when the goods are sold;
- there is an obligation to change the sales price when a change in the rate of duty is imposed; and
- there is a requirement to identify the duty separately on sales information such as invoices.

Payments made in the USA under the Master Settlement Agreement are recognised in other cost of sales, for further disclosure see note 30 contingent liabilities.

TAXES

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustments to tax payable in respect of previous years.

Uncertain tax positions are assessed and measured on an issue by issue basis within the jurisdictions that we operate using management's estimate of the most likely outcome. Where management determines that a greater than 50% probability exists that the tax authorities would accept the position taken in the tax return, amounts are recognised in the consolidated financial statements on that basis. Where the amount of tax payable or recoverable is uncertain, the Group recognises a liability or asset based on either: management's judgement of the most likely outcome; or, when there is a wide range of possible outcomes, a probability weighted average approach. The Group recognises interest on late paid taxes as part of financing costs. The Group recognises penalties, if applicable, as part of administrative and other expenses.

Deferred tax is provided in full on temporary differences between the carrying amount of assets and liabilities in the financial statements and the tax base, except if it arises from the initial recognition of an asset or liability in a transaction, other than a business combination, that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which the assets can be realised. Deferred tax is determined using the tax rates that have been enacted or substantively enacted at the balance sheet date, and are expected to apply when the deferred tax liability is settled or the deferred tax asset is realised.

DIVIDENDS

Final dividends are recognised as a liability in the period in which the dividends are approved by shareholders, whereas interim dividends are recognised in the period in which the dividends are paid.

INTANGIBLE ASSETS – GOODWILL

Goodwill represents the excess of value transferred to the seller in return for control of the acquired business together with the fair value of any previously held equity interest in that business over the Group's share of the fair value of the identifiable net assets.

Goodwill is tested at least annually for impairment and carried at cost less accumulated impairment losses. Any impairment is recognised immediately in the consolidated income statement and cannot be subsequently reversed. If any negative goodwill arises this is recognised immediately in the income statement. For the purpose of impairment testing, goodwill is allocated to groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

INTANGIBLE ASSETS – OTHER

Other intangible assets are initially recognised in the consolidated balance sheet at historical cost unless they are acquired as part of a business combination, in which case they are initially recognised at fair value. They are shown in the balance sheet at historical cost less accumulated amortisation and impairment. The Group does not operate a revaluation model and therefore assets are not subject to ongoing revaluations.

These assets consist mainly of acquired trademarks, intellectual property, product development, concessions and rights, acquired customer relationships and computer software. The Davidoff cigarette trademark and some premium cigar trademarks are considered by the Directors to have indefinite lives based on the fact that they are established international brands with global potential. Trademarks with indefinite lives are not amortised but are reviewed annually for impairment. The carrying value of Davidoff is subject to an annual impairment review under the requirements of IAS 36 as the Group does not currently foresee a limit to the period over which the asset is expected to generate net cash inflows. The most recent assessment indicates that the carrying value is not impaired.

Intellectual property (including trademarks), product development, supply agreements (including customer relationships) and computer software are amortised over their estimated useful lives as follows:

Intellectual property	5 – 30 years	straight line
Supply agreements	3 – 15 years	straight line
Software	3 – 10 years	straight line
Product development	3 – 10 years	straight line

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are recognised in the consolidated balance sheet at historical cost or at their initial fair value where they are acquired as part of an acquisition, subject to depreciation or impairment. The Group does not operate a revaluation model and therefore assets are not subject to ongoing revaluations.

Land is not depreciated. Depreciation is provided on other property, plant and equipment so as to write down the initial cost of each asset to its residual value over its estimated useful life as follows:

Property	up to 50 years	straight line
Plant and equipment	2 – 20 years	straight line/reducing balance
Fixtures and motor vehicles	2 – 15 years	straight line

The assets' residual values and useful lives are reviewed and, if appropriate, adjusted at each balance sheet date.

FINANCIAL INSTRUMENTS AND HEDGING

Receivables held under a hold to collect business model are stated at amortised cost. Receivables held under a hold to sell business model, which are expected to be sold via a non-recourse factoring arrangement are separately classified as fair value through profit or loss, within trade and other receivables.

The calculation of impairment provisions is subject to an expected credit loss model, involving a prediction of future credit losses based on past loss patterns. The revised approach involves the recognition of provisions relating to potential future impairments, in addition to impairments that have already occurred. The expected credit loss approach involves modelling of historic loss rates, and consideration of the level of future credit risk. Expected loss rates are then applied to the gross receivables balance to calculate the impairment provision.

Cash and cash equivalents include cash in hand and deposits held on call, together with other short-term highly liquid investments.

The Group transacts derivative financial instruments to manage the underlying exposure to foreign exchange and interest rate risks. The Group does not transact derivative financial instruments for trading purposes. Derivative financial instruments are initially recorded at fair value plus any directly attributable transaction costs. Derivative financial assets and liabilities are included in the consolidated balance sheet at fair value, and include accrued interest receivable and payable where relevant. However, as the Group has decided (as permitted under IFRS 9) not to cash flow or fair value hedge account for its derivative financial instruments, changes in fair values are recognised in the consolidated income statement in the period in which they arise unless the derivative qualifies and has been designated as a net investment hedging instrument in which case the changes in fair values, attributable to foreign exchange, are recognised in other comprehensive income.

Collateral transferred under the terms and conditions of collateral appendix documents in respect of certain derivatives are netted off the carrying value of those derivatives in the consolidated balance sheet.

RIGHT OF USE ASSETS

The Group has lease contracts relating to property and other assets (which predominantly relates to motor vehicles).

The Group recognises right of use assets, at the commencement date of the lease (i.e. the date the underlying asset is available for use). Right of use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any remeasurement of lease liabilities. The cost of right of use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Unless the Group is reasonably certain to obtain ownership of the leased asset at the end of the lease term, the recognised right of use assets are depreciated on a straight-line basis over the shorter of its estimated useful life and the lease term. Right of use assets are subject to impairment.

LEASE LIABILITIES

At the commencement date of the lease, the Group recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments less any lease incentives receivable, variable lease payments which depend on an index or a rate, and amounts expected to be paid under residual value guarantees. Lease payments include the exercise of purchase options if determined reasonably certain to be exercised and termination payments if the lease term reflects the exercise of an option to terminate.

In calculating the present value of lease payments, the Group uses the incremental borrowing rate, defined as the rate of interest that a lessee would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right of use asset in a similar economic environment, at the lease commencement date if the interest rate implicit in the lease is not readily determinable. After the commencement date, the amount of lease liabilities is increased to reflect the accumulation of interest and reduced

for the lease payments made. In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term, a change in the in-substance fixed lease payments or a change in the assessment to purchase the underlying asset.

Lease payments on short-term leases and leases of low value assets are recognised as expense on a straight line basis over the lease term in cost of sales or distribution, advertising and selling costs.

SHORT TERM LEASES, LEASES OF LOW VALUE ASSETS AND PRACTICAL EXPEDIENTS APPLIED

The Group has applied a number of practical expedients permitted by IFRS 16. These include;

- the exclusion of leases where the lease term ends within 12 months of the commencement of the lease or date of initial application; and
- the exclusion of leases of low value assets, defined as those of less than US$5,000.

IFRS 16 was applied using the modified retrospective method, to contracts that were previously identified as operating leases in accordance with IAS 17 and IFRIC 4. The Group has elected to;

- apply hindsight in determining the lease term if the contract contains options to extend or terminate the lease;
- exclude initial direct costs from the measurement of the right of use asset; and
- use a single discount rate to a portfolio of leases with reasonably similar characteristics

These elections were only applied on transition to IFRS 16 and have not been applied to new leases following adoption of the standard.

INVENTORIES

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the first in first out (FIFO) method. The cost of finished goods and work in progress comprises raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity). Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. Inventory is considered for obsolescence or other impairment issues and an associated provision is booked where necessary.

Leaf tobacco inventory which has an operating cycle that exceeds 12 months is classified as a current asset, consistent with recognised industry practice.

PROVISIONS

A provision is recognised in the consolidated balance sheet when the Group has a legal or constructive obligation as a result of a past event, it is more likely than not that an outflow of resources will be required to settle that obligation, and a reliable estimate of the amount can be made.

A provision for restructuring is recognised when the Group has approved a detailed formal restructuring plan, and the restructuring has either commenced or has been publicly announced, and it is more likely than not that the plan will be implemented, and the amount required to settle any obligations arising can be reliably estimated. Future operating losses are not provided for.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

ASSETS HELD FOR SALE

Assets held for sale arise once a disposal process has advanced sufficiently to meet the requirements of IFRS 5. Assets identified as held for sale are considered for impairment of their carrying value against expected proceeds. The assets and liabilities are presented separately on the balance sheet as assets held for disposal and liabilities held for disposal.

CONTINGENT LIABILITIES

Contingent liabilities are possible obligations that arise from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events, not wholly within the control of the Group. Contingent liabilities are not recognised, only disclosed, unless the possibility of a future outflow of resources is considered remote, or where a disclosure would seriously prejudice the position of the Group.

RETIREMENT BENEFIT SCHEMES

For defined benefit schemes, the amount recognised in the consolidated balance sheet is the difference between the present value of the defined benefit obligation at the balance sheet date and the fair value of the scheme assets to the

extent that they are demonstrably recoverable either by refund or a reduction in future contributions. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash flows using interest rates of high quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligation.

The service cost of providing retirement benefits to employees during the year is charged to operating profit. Past service costs are recognised immediately in operating profit, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time.

All actuarial gains and losses, including differences between actual and expected returns on assets and differences that arise as a result of changes in actuarial assumptions, are recognised immediately in full in the statement of comprehensive income for the period in which they arise. An interest charge is made in the income statement by applying the rate used to discount the defined benefit obligations to the net defined benefit liability of the schemes.

For defined contribution schemes, contributions are recognised as an employee benefit expense when they are due.

SHARE-BASED PAYMENTS

The Group applies the requirements of IFRS 2 Share-Based Payment Transactions to both equity-settled and cash-settled share-based employee compensation schemes. The majority of the Group's schemes are equity-settled.

Equity-settled share-based payments are measured at fair value at the date of grant and are expensed over the vesting period, based on the number of instruments that are expected to vest. For plans where vesting conditions are based on total shareholder returns, the fair value at the date of grant reflects these conditions. Earnings per share and net revenue vesting conditions are reflected in the estimate of awards that will eventually vest. For cash-settled share-based payments, a liability equal to the portion of the services received is recognised at its current fair value at each balance sheet date. Where applicable the Group recognises the impact of revisions to original estimates in the consolidated income statement, with a corresponding adjustment to equity for equity-settled schemes and current liabilities for cash-settled schemes. Fair values are measured using appropriate valuation models, taking into account the terms and conditions of the awards.

The Group funds the purchase of shares to satisfy rights to shares arising under share-based employee compensation schemes. Shares acquired to satisfy those rights are held in Employee Share Ownership Trusts. On consolidation, these shares are accounted for as a deduction from equity attributable to owners of the parent. When the rights are exercised, equity is increased by the amount of any proceeds received by the Employee Share Ownership Trusts.

TREASURY SHARES

When the Company purchases its own equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted on consolidation from equity attributable to owners of the parent until the shares are reissued or disposed of. When such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, increases equity attributable to owners of the parent. When such shares are cancelled they are transferred to the capital redemption reserve.

Where the group enters into a contract with a third party that contains an obligation to re-purchase its own shares for cash or another financial asset; a financial liability is recognised for the present value of the redemption amount. One example is an obligation under a forward contract to re-purchase shares in Imperial Brands PLC for cash. The financial liability is recognised initially at the present value of the redemption amount, and is reclassified from equity. Subsequently, the financial liability is measured in accordance with IFRS 9, and is revalued at subsequent reporting points as appropriate. If the contract expires without delivery, the carrying amount of the financial liability is reclassified to equity.

USE OF ADJUSTED PERFORMANCE MEASURES

Management believes that non-GAAP or adjusted performance measures provide an important comparison of business performance and reflect the way in which the business is controlled. The adjusted performance measures seek to remove the distorting effects of a number of significant gains or losses arising from transactions which are not directly related to the ongoing underlying performance of the business and may be non-recurring events or not directly within the control of management.

Accordingly, adjusted performance measures of operating profit, net finance costs, profit before tax, tax, attributable earnings and earnings per share exclude, where applicable, acquisition and disposal costs, amortisation and impairment of acquired intangibles, restructuring costs, post-employment benefits net financing cost, fair value and

exchange gains and losses on financial instruments, and related tax effects and tax matters. Reconciliations between adjusted and reported operating profit are included within note 6 to the financial statements, adjusted and reported net finance costs in note 6, adjusted and reported tax in note 8, and adjusted and reported earnings per share in note 10. There are also other adjusted reported measures which are defined below.

The adjusted performance measures in this report are not defined terms under IFRS and may not be comparable with similarly titled measures reported by other companies.

The items excluded from adjusted performance results are those which are one-off in nature or items which arose due to acquisitions and are not influenced by the day to day operations of the Group, and the movements in the fair value of financial instruments which are marked to market and not naturally offset. Adjusted net finance costs also excludes all post-employment benefit net finance cost since pension assets and liabilities and redundancy and social plan provisions do not form part of adjusted net debt. This allows comparison of the Group's cost of debt with adjusted net debt. The adjusted performance measures are used by management to assess the Group's financial performance and aid comparability of results year on year.

ADJUSTED OPERATING PROFIT

Adjusted operating profit is calculated as operating profit amended for a number of adjustments, the principal changes are detailed below. This measure is separately calculated and disclosed for Tobacco, NGP and Distribution where appropriate. In addition, adjustments have been made to present this measure on an organic basis to allow year on year comparability (see organic adjustments below). A reconciliation can be found in note 6.

ACQUISITION AND DISPOSAL COSTS / PROFIT ON DISPOSAL OF SUBSIDIARIES

Adjusted performance measures exclude costs and profits or losses associated with major acquisitions and disposals as they do not relate to the day to day operational performance of the Group. Acquisition costs and profits or losses on disposal can be significant in size and are one-off in nature. Exclusion of these items allows a clearer presentation of the day to day underlying income and costs of the business. Where applicable and not reported separately, this includes changes in contingent or deferred consideration.

AMORTISATION AND IMPAIRMENT OF ACQUIRED INTANGIBLES

Acquired intangibles are amortised over their estimated useful economic lives where these are considered to be finite. Acquired intangibles considered to have an indefinite life are not amortised. Any negative goodwill arising is recognised immediately in the income statement. We exclude from our adjusted performance measures the amortisation and impairment of acquired intangibles, other than software and internally generated intangibles, and the deferred tax associated with amortisation of acquired intangibles. Gains and losses on the sale of intellectual property are removed from adjusted operating profit.

It is recognised that there may be some correlation between the amortisation charges derived from the acquisition value of acquired intangibles, and the subsequent future profit streams arising from sales of associated branded products. However, the amortisation of intangibles is not directly related to the operating performance of the business. Conversely, the level of profitability of branded products is directly influenced by day to day commercial actions, with variations in the level of profit derived from branded product sales acting as a clear indicator of performance. Given this, the Group’s view is that amortisation and impairment charges do not clearly correlate to the ongoing variations in the commercial results of the business and are therefore excluded to allow a clearer view of the underlying performance of the organisation. The deferred tax is excluded on the basis that it will only crystallise upon disposal of the intangibles and goodwill. The related current cash tax benefit is retained in the adjusted measure to reflect the ongoing tax benefit to the Group.

PRESENTATION OF AUXLY CANNABIS GROUP INC.

As the movement in the fair value of loan receivables associated with the Auxly Cannabis Group Inc. investment has the potential to be significant the Group has disclosed a fair value movement separately on the face of the income statement.

RESTRUCTURING COSTS

Significant one-off costs incurred in integrating acquired businesses and in major rationalisation and optimisation initiatives together with their related tax effects are excluded from our adjusted earnings measures. These include restructuring costs incurred as part of fundamental multi-year transformational change projects but do not include costs related to ongoing cost reduction activity. These costs are all Board approved, and include impairment of property, plant and equipment which are surplus to requirements due to restructuring activity. These costs are required in order to address structural issues associated with operating within the Tobacco sector that have required action to both modernise and right-size the organisation, ultimately delivering an operating model suitable for the

future of the business. The Group's view is that as these costs are both significant and one-off in nature, excluding them allows a clearer presentation of the underlying costs of the business.

ADJUSTED NET FINANCE COSTS

Adjusted net finance costs excludes the movements in the fair value of financial instruments which are marked to market and not naturally offset. This measure also excludes all post-employment benefit net finance costs since pension assets and liabilities and redundancy and social plan provisions do not form part of adjusted net debt. This allows comparison of the Group's cost of debt with adjusted net debt. A reconciliation can be found in note 6. The detail of these adjustments is given below.

FAIR VALUE GAINS AND LOSSES ON DERIVATIVE FINANCIAL INSTRUMENTS AND EXCHANGE GAINS AND LOSSES ON BORROWINGS

IFRS 9 requires that all derivative financial instruments are recognised in the consolidated balance sheet at fair value, with changes in the fair value being recognised in the consolidated income statement unless the instrument satisfies the hedge accounting rules under IFRS and the Group chooses to designate the derivative financial instrument as a hedge.

The Group hedges underlying exposures in an efficient, commercial and structured manner. However, the strict hedging requirements of IFRS 9 may lead to some commercially effective hedge positions not qualifying for hedge accounting. As a result, and as permitted under IFRS 9, the Group has decided not to apply cash flow or fair value hedge accounting for its derivative financial instruments. However, the Group does apply net investment hedging, designating certain borrowings and derivatives as hedges of the net investment in the Group's foreign operations, as permitted by IFRS 9, in order to reduce income statement volatility.

We exclude fair value gains and losses on derivative financial instruments and exchange gains and losses on borrowings from adjusted net finance costs. Fair value gains and losses on the interest element of derivative financial instruments are excluded as there is no direct natural offset between the movements on derivatives and the interest charge on debt in any one period, as the derivatives and debt instruments may be contracted over different periods, although they will reverse over time or are matched in future periods by interest charges. The fair value gains on derivatives are excluded as they can introduce volatility in the finance charge for any given period.

Fair value gains and losses on the currency element of derivative financial instruments and exchange gains and losses on borrowings are excluded as the relevant foreign exchange gains and losses on the instruments in a net investment hedging relationship are accumulated as a separate component of other comprehensive income in accordance with the Group's policy on foreign currency.

Fair value movements arising from the revaluation of contingent consideration liabilities are adjusted out where they represent one-off acquisition costs that are not linked to the current period underlying performance of the business. Fair value adjustments on loans receivable measured at fair value are excluded as they arise due to counterparty credit risk changes that are not directly related to the underlying commercial performance of the business..

POST-EMPLOYMENT BENEFITS NET FINANCING COST

The net interest on defined benefit assets or liabilities, together with the unwind of discount on redundancy, social plans and other long-term provisions are reported within net finance costs. These items together with their related tax effects are excluded from our adjusted earnings measures, as they primarily represent charges associated with historic employee benefit commitments, rather than the ongoing current period costs of operating the business.

ADJUSTED TAX CHARGE

The adjusted tax charge is calculated by amending the reported tax charge for significant one-off tax charges or credits arising from:

- prior period tax items (including re-measurement of deferred tax balances on a change in tax rates); or
- a provision for uncertain tax items not arising in the normal course of business; or
- newly enacted taxes in the year; or
- tax items that are closely related to previously recognised tax matters, and are excluded from our adjusted tax charge to aid comparability and understanding of the Group's performance.

The recognition and utilisation of deferred tax assets relating to losses not historically generated in the normal course of business are excluded on the same basis.

A reconciliation can be found in note 8.

The adjusted tax rate is calculated as the adjusted tax charge divided by the adjusted profit before tax.

ADJUSTED EARNINGS

Adjusted earnings is calculated by amending the reported basic earnings for all of the adjustments recognised in the calculation of the adjusted operating profit, adjusted finance costs and adjusted tax charge metrics as detailed above. In addition, adjustments have been made to present this measure on an organic basis to allow year on year comparability (see organic adjustments). Adjusted earnings per share and organic earnings per share are calculated by providing adjusted earnings and organic earnings by the weighted average number of shares. A reconciliation is provided in note 10.

OTHER NON-GAAP MEASURES USED BY MANAGEMENT

NET REVENUE

Tobacco & Next Generation Products (NGP) net revenue comprises associated revenue less duty and similar items, excluding peripheral products. Management considers this an important measure in assessing the performance of Tobacco & NGP operations.

The Group recognises revenue on sales to Logista, a Group company, within its reported Tobacco & NGP revenue figure. As the revenue calculation includes sales made to Logista from other Group companies but excludes Logista's external sales, this metric differs from revenue calculated under IFRS accounting standards. For the purposes of Adjusted Performance Measures on Net Revenue we treat Logista as an arms length distributor on the basis that contractual rights are in line with other Third Party suppliers to Logista. Variations in the amount of inventory held by Logista results in a different level of revenue compared to that which is included within the income statement. For tobacco product sales, inventory level variations are normally not significant. A reconciliation can be found in note 3.

DISTRIBUTION NET REVENUE

Distribution net revenue comprises the Distribution segment revenue less the cost of distributed products. Management considers this an important measure in assessing the performance of Distribution operations. The eliminations in note 3 all relate to sales to Distribution. A reconciliation can be found in note 3.

ADJUSTED OPERATING CASH

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

ADJUSTED NET DEBT

Management monitors the Group's borrowing levels using adjusted net debt which excludes interest accruals, lease commitments and the fair value of derivative financial instruments providing commercial hedges of interest rate risk. The adjusted net debt metric is used in monitoring performance against various debt management obligations including covenant compliance. A reconciliation can be found in note 31.

ORGANIC

To aid comparison of performance between years, the Group uses the term ‘organic’ in all years reported to exclude the impact of the Premium Cigar divestment, which completed on 29 October 2020. The organic performance comparison excludes the contribution of the Premium Cigar divestment in all years reported.

CASH CONVERSION

The Group uses cash conversion as a key metric for assessing underlying cash performance. Cash Conversion is calculated as cash flow from operations pre-restructuring and before interest and tax payments, less net capital expenditure relating to property, plant and equipment, software and intellectual property rights as a percentage of adjusted operating profit. A reconciliation can be found in note 6.

ADJUSTED OPERATING PROFIT MARGIN

Adjusted operating profit margin is adjusted operating profit divided by net revenue expressed as a percentage. This measure is separately calculated and disclosed for Tobacco, NGP and Distribution where appropriate. In addition, adjustments have been made to present this measure on an organic basis to allow year on year comparability (see organic adjustments). A reconciliation of adjusted operating profit can be found in note 6 and a reconciliation of net revenue can be found in note 3.

FREE CASH FLOW

Free cash flow is adjusted operating profit (as defined above) adjusted for certain cash and non cash items. The principal adjustments are depreciation, working capital movements, net capex, restructuring cash flows, tax cash flows, cash interest and minority interest dividends.

RETURN ON INVESTED CAPITAL

Return on invested capital measures the effectiveness of capital allocation and is calculated by dividing adjusted operating profit after tax by the annual average of: intangible assets, property, plant and equipment, net assets held for sale, inventories, trade and other receivables and trade payables and other current liabilities.

The annual average is defined as the average of the opening and closing balance sheet values.

NET DEBT TO EBITDA (MULTIPLE)

This is defined as adjusted net debt divided by adjusted EBITDA. Adjusted net debt is measured at balance sheet foreign exchange rates, with a full reconciliation shown in note 30. Adjusted EBITDA is calculated as adjusted operating profit plus amortisation, depreciation and impairments. A reconciliation of adjusted net debt can be found in note 31.

ALL IN COST OF DEBT

This is defined as adjusted net finance costs (defined above) divided by the average net debt in the year (note 31). A reconciliation of adjusted net finance costs can be found in note 6.

CONSTANT CURRENCY

Constant currency removes the effect of exchange rate movements on the translation of the results of our overseas operations. We translate current year results at prior year foreign exchange rates.

NEW ACCOUNTING STANDARDS

For the year ended 30 September 2021 the Group continued to apply international accounting standards in conformity with the requirements of the Companies Act 2006 and IFRS, issued by the International Accounting Standards Board (IASB) and adopted pursuant to Regulation (EC) No. 1606/2002 as it applies in the European Union. From 1 October 2021, as a result of the UK leaving the European Union, the Group will prepare the consolidated financial statements in accordance with applicable international accounting standards, issued by the IASB or International Financial Reporting Interpretations Committee (IFRIC) and endorsed for use in the UK, referred to as 'UK-adopted IFRS'.

The following amendments to the accounting standards, issued by the IASB or IFRIC, have been adopted by the Group from 1 October 2020 with no impact on the group's consolidated results, financial position or disclosures:

- Amendments to References to the Conceptual Framework in IFRS
- Amendments to IFRS 3 – Definition of a Business
- Amendments to IAS 1 and IAS 8 – Definition of Material
- Amendments to IFRS 16 – Covid-19 – Related Rent Concessions
- Amendments to IFRS 9, IAS 39 and IFRS 7 – Interest rate benchmark reform (phase 1)

Derivatives with a notional value of €3,233 million designated in net investment hedges will be impacted by the impending reforms to the calculation of the Interbank Offered Rates (IBOR). However, as discussed in Note 21 Financial Risk Management, only the undiscounted foreign currency spot exposures of these instruments are designated in the hedging relationship and therefore there will be no change to the effectiveness of the hedges due to the reform. Changes in the fair value of these derivatives attributable to changes in interest rates and the effect of discounting are recognised directly in profit or loss within the Finance costs line.

NEW ACCOUNTING STANDARDS AND INTERPRETATIONS NOT YET IN ISSUE

The following standard and amendment, issued by the IASB has not been adopted by the Group:

- Amendments to IFRS 9, IAS 39 and IFRS 7 – Interest rate benchmark reform (phase 2) (effective in the year ending 30 September 2022)

Following the announcement of the discontinuation of GBP LIBOR at the end of 2021 and USD LIBOR discontinuation in 2023, the Company has amended its bank facility agreement to stop referencing GBP and USD LIBOR and instead reference the daily risk free rates of SONIA and SOFR respectively. All current GBP LIBOR derivatives will be changed to reference SONIA instead of GBP LIBOR by the end of 2021, then all USD LIBOR derivatives will be changed to reference SOFR instead of USD LIBOR during the remainder of fiscal year 2022. There are no changes pending for EUR derivatives.

There are also a number of other amendments and clarifications to IFRS, effective in future years. None of which are expected to significantly impact the group's consolidated results or financial position.

2. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The Group makes estimates and judgements associated with accounting entries which will be affected by future events. Estimates and judgements are continually evaluated based on historical experience, and other factors, including current information that helps form a forward-looking view of expected future outcomes.

Estimates involve the determination of the quantum of accounting balances to be recognised. Judgements typically involve decisions such as whether to recognise an asset or liability.

The actual amounts recognised in the future may deviate from these estimates and judgements. The estimates and judgements that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

DETERMINATION OF USEFUL ECONOMIC LIFE OF INTANGIBLE ASSETS

For non-goodwill intangible assets, there are critical judgements required in determining whether the asset has an indefinite useful economic life, or not. The Davidoff trademark has a significant market share and positive cash flow growth expectations. There are no regulatory or contractual restrictions on the use of this trademark, and there are no plans to significantly redirect resources elsewhere which would reduce the value of this asset. Consequently, in the view of management, the Davidoff trademark does not have a foreseeable and definite end to its ability to generate future cash flows and hence it is not amortised. The carrying value of Davidoff is subject to an annual impairment review under the requirements of IAS 36 as Group does not currently foresee a limit to the period over which the asset is expected to generate net cash inflows. The most recent assessment indicates that the carrying value is not impaired.

AMORTISATION AND IMPAIRMENT OF INTANGIBLE ASSETS

For non-indefinite life assets, which are amortised, the useful economic life and recoverable amounts are estimated based upon the expectation of the amount and time period during which an intangible asset will support future cash flows. Due to estimation uncertainties the useful economic lives and associated amortisation rates have to be reviewed and revised where necessary. In addition, where there are indications that the current carrying value of an intangible asset is greater than its recoverable amount, impairment in the carrying value of the asset may be required. Factors considered important that could trigger an impairment review of intangible assets include the following:

- significant underperformance relative to historical or projected future operating results;
- significant changes in the manner of the use of the acquired assets or the strategy for the overall business; and
- significant negative industry or economic trends.

The complexity of the estimation process and issues related to the assumptions, risks and uncertainties inherent in the application of the Group's accounting estimates in relation to intangible assets affect the amounts reported in the financial statements, especially the estimates of the expected useful economic lives and the carrying values of those assets. If business conditions materially change it is likely that materially different amounts could be reported in the Group's financial statements. Indefinite life intangible assets, including goodwill, are subject to annual impairment testing where an assessment of the carrying value of the asset against its recoverable amount is undertaken. There are long term uncertainties associated with estimating the valuation of the recoverable amount, particularly with regard to long term cash flow growth rates which are influenced by the future size and shape of the tobacco sector. While long term growth rates currently used in impairment assessments are based on current best estimates of future performance, there may be changes in these assumptions when conducting impairment tests in subsequent years. Details of goodwill and intangible asset impairment assessments are included in note 12.

INCOME TAXES

Judgement is involved in determining whether the Group is subject to a tax liability or not in line with tax law. Where liabilities exist, estimation is often required to determine the potential future tax payments. The Group is subject to income tax in numerous jurisdictions and significant judgement is required in determining the provision for tax. There are many transactions and calculations for which the ultimate tax determination is uncertain. The Group recognises provisions for tax based on estimates of the taxes that are likely to become due. Where the final tax outcome is different from the amounts that were initially recorded, such differences will impact the current income tax and deferred tax provisions in the period in which such determination is made. Consideration of the judgements surrounding certain tax positions are applicable to the Group and consideration of the valuation estimates related to tax provisions are given in note 8 to these financial statements.

LEGAL PROCEEDINGS AND DISPUTES

The Group reviews outstanding legal cases following developments in the legal proceedings at each balance sheet date, considering the nature of the litigation, claim or assessment; the legal processes and potential level of damages

in the jurisdiction in which the litigation, claim or assessment has been brought; the progress of the case (including progress after the date of the financial statements but before those statements are issued); the opinions or views of legal counsel and other advisers; experience of similar cases; and any decision of the Group's management as to how it will respond to the litigation, claim or assessment. Judgement is required as to whether a liability exists. Where a liability is determined there can be a degree of estimation of the potential level of damages expected. Key areas of judgement include consideration as to whether certain claims associated with the acquisition of certain brands and the likely outcome of a number of product liability claims. More detail as to the considered position on these claims is given in both note 30 of the financial statements and within the Directors' Report – update on Tobacco and e-vapour related litigation. To the extent that the Group's assessments at any time do not reflect subsequent developments or the eventual outcome of any claim, its future financial statements may be materially affected, with a favourable or adverse impact upon the Group's operating profit, financial position and liquidity.

PROVISIONS

Provision accounting involves judgement as to whether a liability should be recognised and requires estimates of the quantum of any such liability. The Group holds provisions where appropriate in respect of estimated future economic outflows, principally for restructuring activity and excise tax, which arise due to past events. Estimates are based on management judgement and information available at the balance sheet date. Actual outflows may not occur as anticipated, and estimates may prove to be incorrect, leading to further charges or releases of provisions as circumstances dictate. The main area of estimation risk relates to the estimation of restructuring provisions associated with various plans to transform the business. These include the cost of factory closures, scaling down of capacity and other structural changes to the business. These programmes are run as discrete projects with controls over the expected costs and the associated accounting impacts. The calculation of restructuring provisions includes estimation challenges relating to asset remediation costs, the valuation of disposals and termination costs. More details relating to the estimates associated with these restructuring programmes can be found in notes 5 and 25.

CONTROL OF LOGISTA

A key judgement relates to whether the Group has effective control of Logista sufficient that the Group can consolidate this entity within its Group accounts in line with the requirements of IFRS 10 Consolidated Financial Statements. The Group holds 50.01 per cent of the voting shares. The Group has reviewed its control of Logista and that it is appropriate to consolidate this entity in line with the requirements of IFRS 10 Consolidated Financial Statements. The Group continues to have Director presence on the Board of Logista, representing 4 out of 10 Directors. The Group has powers to control as set out in the Relationship Framework Agreement which specifies certain areas of operation reserved for shareholder approval and through these measures the Group is able to exercise control of Logista. The Group has therefore concluded that it continues to be appropriate to recognise Logista as a fully consolidated subsidiary.

3. SEGMENT INFORMATION

Imperial Brands comprises two distinct businesses – Tobacco & NGP and Distribution. The Tobacco & NGP business comprises the manufacture, marketing and sale of Tobacco & NGP and Tobacco & NGP-related products, including sales to (but not by) the Distribution business. The Distribution business comprises the distribution of Tobacco & NGP products for Tobacco & NGP product manufacturers, including Imperial Brands, as well as a wide range of non-Tobacco & NGP products and services. The Distribution business is run on an operationally neutral basis ensuring all customers are treated equally, and consequently transactions between the Tobacco & NGP and Distribution businesses are undertaken on an arm's length basis reflecting market prices for comparable goods and services.

The function of Chief Operating Decision Maker (defined in IFRS 8), which is to review performance and allocate resources, is performed by the Board and the Chief Executive, who are regularly provided with information on our segments. This information is used as the basis of the segment revenue and profit disclosures provided below. The main profit measure used by the Board and the Chief Executive is adjusted operating profit. Segment balance sheet information is not provided to the Board or the Chief Executive.

Our reportable segments are Europe, Americas, Africa, Asia & Australasia (AAA) and Distribution. Operating segments are comprised of geographical groupings of business markets. The main Tobacco & NGP business markets within the Europe, Americas and AAA reportable segments are:

Europe – United Kingdom, Germany, Spain, France, Italy, Greece, Sweden, Norway, Belgium, Netherlands, Ukraine and Poland.

Americas – United States

AAA – Australia, Japan, Russia, Saudi Arabia, Taiwan and our African markets including Algeria and Morocco.

TOBACCO & NGP

£ million unless otherwise indicated	2021	2020
Revenue	**23,863**	23,973
Net revenue	**7,610**	7,985
Operating profit	**2,991**	2,587
Adjusted operating profit	**3,308**	3,288
Adjusted operating margin %	**43.5**	41.2

RECONCILIATION FROM OPERATING PROFIT TO ADJUSTED OPERATING PROFIT

£ million	2021	2020
Adjusted operating profit	**3,308**	3,288
Acquisition and disposal costs	**–**	(26)
Profit on disposal of subsidiaries	**281**	–
Amortisation of acquired intangibles	**(365)**	(438)
Excise tax provision	**1**	20
Fair value adjustment of loan receivable	**15**	(62)
Restructuring costs	**(249)**	(195)
Operating profit	**2,991**	2,587

DISTRIBUTION

£ million unless otherwise indicated	2021	2020
Revenue	**9,589**	9,268
Distribution net revenue	**1,069**	1,015
Operating profit	**148**	131
Adjusted operating profit	**258**	226
Adjusted operating margin %	**24.1**	22.3

RECONCILIATION FROM OPERATING PROFIT TO ADJUSTED OPERATING PROFIT

£ million	2021	2020
Adjusted operating profit	**258**	226
Acquisition and disposal costs	**(17)**	–
Amortisation of acquired intangibles	**(85)**	(85)
Restructuring costs	**(8)**	(10)
Operating profit	**148**	131

REVENUE

	2021		2020	
£ million	**Total revenue**	**External revenue**	Total revenue	External revenue
Tobacco & NGP				
Europe	**14,720**	**14,059**	14,395	13,716
Americas	**3,393**	**3,393**	3,371	3,371
Africa, Asia & Australasia	**5,750**	**5,750**	6,207	6,207
Total Tobacco & NGP	**23,863**	**23,202**	23,973	23,294
Distribution	**9,589**	**9,589**	9,268	9,268
Eliminations	**(661)**	**–**	(679)	–
Total Group	**32,791**	**32,791**	32,562	32,562

RECONCILIATION FROM TOBACCO & NGP REVENUE TO TOBACCO & NGP NET REVENUE

	2021			2020		
£ million	**Tobacco**	**NGP**	**Total**	Tobacco	NGP	Total
Revenue	**23,664**	**199**	**23,863**	23,757	216	23,973
Duty and similar items	**(16,218)**	**(11)**	**(16,229)**	(15,947)	(15)	(15,962)
Sale of peripheral products	**(24)**	**–**	**(24)**	(26)	–	(26)
Net Revenue	**7,422**	**188**	**7,610**	7,784	201	7,985

TOBACCO & NGP NET REVENUE

£ million	2021 Tobacco	2021 NGP	2021 Total	2020 Tobacco	2020 NGP	2020 Total
Europe	**3,425**	**126**	**3,551**	3,471	98	3,569
Americas	**2,478**	**56**	**2,534**	2,409	71	2,480
Africa, Asia & Australasia	**1,519**	**6**	**1,525**	1,904	32	1,936
Total Tobacco & NGP	**7,422**	**188**	**7,610**	7,784	201	7,985

PREMIUM CIGAR DIVESTMENT & ORGANIC NET REVENUE

£ million	2021	2020
Organic Net Revenue	**7,589**	7,738
Premium Cigar Divestment Net Revenue	**21**	247
Total Tobacco & NGP	**7,610**	7,985

RECONCILIATION FROM DISTRIBUTION REVENUE TO DISTRIBUTION NET REVENUE

£ million	2021	2020
Revenue	**9,589**	9,268
Cost of sales - Distribution	**(8,520)**	(8,253)
Distribution Net Revenue	**1,069**	1,015

ADJUSTED OPERATING PROFIT AND RECONCILIATION TO PROFIT BEFORE TAX

£ million	2021	2020
Tobacco & NGP		
Europe	**1,670**	1,582
Americas	**1,037**	1,032
Africa, Asia & Australasia	**601**	674
Total Tobacco & NGP	**3,308**	3,288
Distribution	**258**	226
Eliminations	**7**	13
Adjusted operating profit	**3,573**	3,527
Acquisition and disposal costs – Tobacco & NGP	**–**	(26)
Acquisition and disposal costs – Distribution	**(17)**	–
Profit on disposal of subsidiaries – Tobacco & NGP	**281**	–
Amortisation and impairment of acquired intangibles – Tobacco & NGP	**(365)**	(438)
Amortisation of acquired intangibles – Distribution	**(85)**	(85)
Excise tax provision – Tobacco & NGP	**1**	20
Fair value adjustment of loan receivable – Tobacco & NGP	**15**	(62)
Restructuring costs – Tobacco & NGP	**(249)**	(195)
Restructuring costs - Distribution	**(8)**	(10)
Operating profit	**3,146**	2,731
Net finance income/(costs)	**81**	(610)
Share of profit of investments accounted for using the equity method	**11**	45
Profit before tax	**3,238**	2,166

See note 8 for details of the Excise tax provision. See note 12 for details on amortisation and impairment, note 11 for details of acquisition and disposal costs, and note 5 for details of restructuring costs.

OTHER INFORMATION

£ million	2021 Additions to property, plant and equipment	2021 Depreciation and software amortisation	2020 Additions to property, plant and equipment	2020 Depreciation and software amortisation
Tobacco & NGP				
Europe	**87**	**99**	77	101
Americas	**26**	**28**	30	31
Africa, Asia & Australasia	**20**	**27**	46	34
Total Tobacco & NGP	**133**	**154**	153	166
Distribution	**32**	**40**	21	36
Total Group	**165**	**194**	174	202

ADDITONAL GEOGRAPHIC ANALYSIS

External revenue and non-current assets are presented for the UK and for individually significant countries. The geographical analysis is based on country of origin. The Group's products are sold in over 120 countries.

	2021		2020	
£ million	**External revenue**	**Non-current assets**	External revenue	Non-current assets
UK	**4,558**	**102**	4,498	104
Germany	**4,566**	**3,246**	4,637	3,465
France	**3,537**	**2,336**	3,772	2,564
USA	**3,405**	**5,486**	3,575	6,143
Other	**16,725**	**7,307**	16,080	7,900
Total Group	**32,791**	**18,477**	32,562	20,176

Non-current assets comprise intangible assets, property, plant and equipment and investments accounted for using the equity method.

4. PROFIT BEFORE TAX

Profit before tax is stated after charging/(crediting):

£ million	2021	2020
Raw materials and consumables used	**947**	947
Changes in inventories of finished goods – Tobacco & NGP	**2,700**	2,781
Changes in inventories of finished goods – Distribution	**7,009**	6,798
Depreciation and impairment of fixed assets	**170**	205
Amortisation and impairment of intangible assets	**575**	628
Acquisition and disposal costs	**17**	26
Expenses relating to short-term leases	**4**	4
Expenses relating to low value asset leases	**2**	2
Depreciation of Right of use assets	**66**	72
Net foreign exchange (gains)/losses	**(442)**	258
Write down of inventories	**117**	126
Loss/(profit) on disposal of non-current assets	**2**	(2)
(Write back)/impairment of trade receivables	**(10)**	44

ANALYSIS OF FEES PAYABLES TO ERNST AND YOUNG LLP AND ITS ASSOCIATES

£ million	2021	2020
Parent Company and consolidated financial statements	**2.0**	1.9
The Company's subsidiaries	**5.1**	4.7
Audit related assurance services	**0.4**	0.4
Total audit related fees	**7.5**	7.0
Other assurance services	**0.4**	0.2
Total non-audit fees	**0.4**	0.2
Total auditor's remuneration	**7.9**	7.2

Ernst & Young LLP was appointed the Group's auditor for the year ended 30 September 2020.

PwC (the Group's previous auditor) provided services to Logista relating to preparation of their consolidation financial statements amounting to £nil (2020: £0.2m).

5. RESTRUCTURING COSTS

£ million	2021	2020
Employment related	**145**	103
Asset impairments	**92**	58
Other charges	**20**	44
	257	205

Restructuring costs analysed by workstream:

£ million	2021	2020
2021 Strategic review programme	**226**	–
Cost optimisation programmes	**23**	187
Other	**8**	18
	257	205

The charge for the year of £257 million (2020: £205 million) predominantly relates to our 2021 Strategic review programme and Cost optimisation programmes.

Restructuring costs are included within administrative and other expenses in the consolidated income statement. All restructuring costs are treated as adjusting items.

These projects differ from everyday initiatives that are undertaken to improve the efficiency and effectiveness of the ongoing operations business. These costs are required in order to address structural issues involved in operating within the Tobacco sector that require action to both modernise and right-size the organisation, ultimately delivering an operating model suitable for the future of the business.

2021 STRATEGIC REVIEW PROGRAMME

In January 2021, the Group announced the results of a Strategic Review Programme including an associated and specific time-bound restructuring programme. The Group expects the majority of the associated restructuring costs to have been incurred by September 2022. Total restructuring costs in respect of the programme are expected to be in the range of £375 million – £425 million.

Restructuring costs of £226 million (2020: £nil) related to the 2021 Strategic Review Programme have been incurred in the year, representing £153 million costs in respect of the change programme itself and £73 million of impairments associated with NGP assets.

2021 Strategic Review Programme cash spend for the year was £48 million (2020 £nil).

COST OPTIMISATION PROGRAMMES

The cost optimisation programmes (Phase I announced in 2013 and Phase II announced in November 2016) was part of the Group strategy to optimise costs and drive operational efficiencies. The programmes were time bound projects which, given their scale, were delivered over a number of years. Phase I was concluded at the end of 2018 and Phase II was concluded at the end of 2021. Whilst both programmes are concluded there remain some ongoing cash costs.

Phase II of the programme focused on reducing product costs and overheads. Phase II cash spend for the year was £41 million (2020: £107 million), bringing the cumulative cash cost of the programme to £548 million as at September 2021. Phase II is currently delivering savings of c. £320 million per annum as at September 2021.

Phase I cash spend for the year was £12 million (2020: £16 million), bringing the cumulative cash cost of the programme to £571 million as at September 2021. Phase I has delivered savings of c. £305 million per annum from September 2018.

Restructuring costs of £23 million (2020: £187 million) related to the Cost optimisation programmes includes £19 million of impairments associated with tangible assets.

OTHER RESTRUCTURING ACTIVITIES

In the year £8 million (2020: £10 million) of restructuring costs related to Logista.

There are £nil (2020: £8 million) Other restructuring costs that do not relate to Logista.

In the year other restructuring cash spend was £11 million.

6. ALTERNATIVE PERFORMANCE MEASURES

RECONCILIATION FROM OPERATING PROFIT TO ADJUSTED OPERATING PROFIT

£ million	Notes	2021	2020
Operating profit		**3,146**	2,731
Acquisition and disposal costs	11	**17**	26
Amortisation and impairment of acquired intangibles	12/15	**450**	523
Excise tax provision		**(1)**	(20)
Fair value adjustment of loan receivable	21	**(15)**	62
Profit on disposal of subsidiaries		**(281)**	–
Restructuring costs	5	**257**	205
Adjusted operating profit		**3,573**	3,527
Organic adjusted operating profit		**3,570**	3,496
Premium cigar divestment adjusted operating profit		**3**	31
Adjusted operating profit		**3,573**	3,527

Amortisation and impairment of acquired intangibles, acquisition and disposal costs and restructuring costs are discussed in further detail in the above referenced notes.

RECONCILIATION FROM REPORTED NET FINANCE COSTS TO ADJUSTED NET FINANCE COSTS

£ million	2021	2020
Reported net finance (income)/costs	**(81)**	610
Fair value gains on derivative financial instruments	**508**	661
Fair value losses on derivative financial instruments	**(457)**	(581)
Exchange (gains)/losses on financing activities	**445**	(256)
Net fair value and exchange losses on financial instruments	**496**	(176)
Interest income on net defined benefit assets	**89**	99
Interest cost on net defined benefit liabilities	**(87)**	(104)
Post-employment benefits net financing cost	**2**	(5)
Adjusted net finance costs	**417**	429
Comprising		
Interest income on bank deposits	**(18)**	(10)
Interest cost on lease liabilities	**7**	7
Interest cost on bank and other loans	**428**	432
Adjusted net finance costs	**417**	429

CASH CONVERSION CALCULATION

£ million unless otherwise indicated	2021	2020
Net cash flow from operating activities	**2,167**	4,030
Tax	**820**	568
Net capital expenditure	**(150)**	(274)
Restructuring spend	**112**	145
Cash flow post capital expenditure pre interest and tax	**2,949**	4,469
Adjusted operating profit	**3,573**	3,527
Cash Conversion %	**83%**	127%

7. DIRECTORS AND EMPLOYEES

EMPLOYMENT COSTS

£ million	2021	2020
Wages and salaries	**775**	812
Social security costs	**177**	184
Other pension costs (note 24)	**75**	68
Share-based payments (note 27)	**25**	20
	1,052	1,084

OPERATING EXECUTIVE (EXCLUDING EXECUTIVE DIRECTORS)

£ million	2021	2020
Base salary	**3.0**	2.0
Benefits	**0.7**	–
Pension salary supplement	**0.3**	–
Bonus	**2.9**	1.6
Termination payments	**–**	–
LTIP annual vesting[1]	**0.8**	–
SMS annual vesting[1]	**–**	0.1
	7.7	3.7

1. Share plans vesting represent the value of SMS and LTIP awards where the performance periods ends in the year. The SMS has no performance conditions and is valued at the time of vesting being 15 February at a share price of £15.0657

Note: aggregate remuneration paid to or receivable by Executive directors, Non-Executive Directors and members of the Operating Executive for qualifying services in accordance with IAS 24, which includes National Insurance and similar charges was £16,422,230 (2020: £9,239,049).

KEY MANAGEMENT COMPENSATION[1]

£ million	2021	2020
Short term employee benefits	**12.7**	9.2
Post-employment benefits	**0.5**	2.0
Other long-term benefits	**–**	–
Termination payments	**–**	–
Share based payments (in accordance with IAS 24)	**0.9**	0.2
	14.1	11.4

1. Key management includes Directors, members of the Executive Committee and the Company Secretary

Details of Directors' emoluments and interests, and of key management compensation which represent related party transactions requiring disclosure under IAS 24, are provided within the Directors' Remuneration Report.

NUMBER OF PEOPLE EMPLOYED BY THE GROUP DURING THE YEAR

	2021		2020	
	At 30 September	**Average**	At 30 September	Average
Tobacco & NGP	**24,100**	**24,000**	26,300	25,900
Distribution	**6,200**	**6,200**	6,200	6,200
	30,300	**30,200**	32,500	32,100

NUMBER OF PEOPLE EMPLOYED BY THE GROUP BY LOCATION DURING THE YEAR

	2021		2020	
	At 30 September	**Average**	At 30 September	Average
UK and European Union	**14,600**	**14,700**	14,900	15,100
Americas	**8,300**	**8,000**	8,900	8,400
Rest of the World	**7,400**	**7,500**	8,700	8,600
	30,300	**30,200**	32,500	32,100

The average number of employees includes 2,500 La Romana employees that are expected to leave the Group in 2022 as part of the final part of the Premium Cigar Division disposal. Excluding these employees, the average number of employees was 27,700 on a pro-forma basis.

8. TAX

The major components of income tax expense for the years ended 30 September 2021 and 2020 are:

£ million	**2021**	2020
UK Current tax		
Current year charged to the consolidated income statement	**21**	97
Current year charged to consolidated other comprehensive income	**105**	10
Total current year UK current tax	**126**	107
Adjustments in respect of prior years charged to the consolidated income statement	**(38)**	26
Total UK current tax	**88**	133
Overseas current tax		
Current year charged to the consolidated income statement	**458**	458
Current year charged to consolidated other comprehensive income	**(2)**	–
Total current year overseas current tax	**456**	458
Adjustments in respect of prior years charged to the consolidated income statement	**46**	12
Total overseas current tax	**502**	470
Total current tax charged to the consolidated statement of other comprehensive income	**590**	603

£ million	**2021**	2020
UK Current tax		
Current year	**21**	97
Adjustments in respect of prior years	**(38)**	26
Overseas current tax		
Current year	**458**	458
Adjustments in respect of prior years	**46**	12
Total current tax	**487**	593
Deferred tax		
Relating to origination and reversal of temporary differences	**(156)**	15
Total tax charged to the consolidated income statement	**331**	608

£ million	2021	2020
Tax related to items recognised in consolidated other comprehensive income during the year:		
Current tax on hedge of net investment	**105**	10
Current tax on actuarial gains and losses	**(2)**	–
Total current tax	**103**	10
Deferred tax on hedge of net investment	**12**	80
Deferred tax on actuarial gains and losses	**21**	53
Total deferred tax	**33**	133
Total tax charged to consolidated other comprehensive income	**136**	143

RECONCILIATION FROM REPORTED TAX TO ADJUSTED TAX

The table below shows the tax impact of the adjustments made to reported profit before tax in order to arrive at the adjusted measure of earnings disclosed in note 10.

£ million	2021	2020
Reported tax	**331**	608
Deferred tax on amortisation of acquired intangibles	**31**	57
Current tax on excise tax provision	**–**	(4)
Tax on net foreign exchange and fair value gains and losses on financial instruments	**78**	(63)
Tax on post-employment benefits net financing cost	**1**	1
Tax on restructuring costs	**72**	31
Tax on disposal of premium cigar division	**11**	(19)
Recognition of tax credits	**239**	67
Uncertain tax positions	**–**	(77)
Tax on unrecognised losses	**(47)**	41
Adjusted tax charge	**716**	642

The use of adjusted performance measures is explained in note 1, Accounting Policies (Use of Adjusted Performance Measures).

FACTORS AFFECTING THE TAX CHARGE FOR THE YEAR

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the average UK corporation tax rate of 19.0 per cent (2020: 19.0 per cent) as follows:

£ million	2021	2020
Profit before tax	**3,238**	2,166
Tax at the UK corporation tax rate of 19.0% (2020: 19.0%)	**615**	411
Tax effects of:		
Differences in effective tax rates on overseas earnings	**107**	100
Movement in provision for uncertain tax positions	**49**	61
Remeasurement of deferred tax balances arising from changes in tax rates	**15**	9
Recognition of deferred tax assets for tax credits	**(239)**	–
Remeasurement of previously recognised deferred tax assets	**(5)**	(81)
Increase in unrecognised deferred tax assets	**12**	30
Deferred tax on unremitted earnings	**(4)**	(19)
Share of profit of investments accounted for using the equity method	**(2)**	(8)
Non-deductible expenses/(non-taxable income)	**35**	(4)
(Non-taxable gains)/non-deductible losses on net foreign exchange on financial instruments	**(169)**	80
Non-taxable gain on Premium Cigar Division disposal	**(81)**	–
Adjustments in respect of prior years	**(2)**	29
Total tax charged to the consolidated income statement	**331**	608

Differences in effective tax rates on overseas earnings represents the impact of worldwide profits being taxed at rates different from 19.0 per cent. The effective tax rate benefits from internal financing arrangements between group subsidiaries in different countries which are subject to differing tax rates and legislation and the application of double taxation treaties.

Recognition of deferred tax assets for credits includes £239 million (2020: £nil) in the Group's Spanish business arising from an internal reorganisation during the year.

Remeasurement of previously recognised deferred tax assets includes £8 million recognition (2020: £18 million) in relation to deferred tax assets for tax losses in the Group's Dutch business, £nil recognition (2020:£15 million) in relation to deferred tax assets for tax credits and losses in the Group's Spanish business and £nil recognition (2020: £45 million) in relation to deferred tax assets for tax losses in the Group's US business. The Group's assessment of the recoverability of deferred tax assets is based on a review of underlying performance of subsidiaries, changes in tax legislation and the interpretation thereof and changes in the group structure.

The remeasurement of deferred tax balances arising from changes in tax rates for the year is £15 million (2020: £9 million).

During the year the Group has decreased the provision for deferred tax on unremitted earnings by £4 million (2020: £19 million decrease). The tax will arise on the distribution of profits through the group and on planned group simplification.

MOVEMENT ON THE CURRENT TAX ACCOUNT

£ million	2021	2020
At 1 October	**(144)**	(118)
Charged to the consolidated income statement	**(487)**	(593)
(Charged)/credited to other comprehensive income	**(103)**	10
Credited to equity	**–**	1
Cash paid	**820**	568
Exchange movements	**3**	(13)
Other movements	**(7)**	1
At 30 September	**82**	(144)

The cash tax paid in the year is £333 million higher than the current tax charge (2020: £25 million lower). This arises as a result of timing differences between the accrual of income taxes and the actual payment of cash and the movement in the provision for uncertain tax positions.

ANALYSIS OF CURRENT TAX ACCOUNT

£ million	2021	2020
State aid tax recoverable	**101**	–
Current tax assets	**234**	206
Current tax liabilities	**(253)**	(350)
	82	(144)

UNCERTAIN TAX POSITIONS

As an international business the Group is exposed to uncertain tax positions and changes in legislation in the jurisdictions in which it operates. The Group's uncertain tax positions principally include cross border transfer pricing, interpretation of new or complex tax legislation and tax arising on the valuation of assets.

Provisions arising from uncertain tax positions taken in the calculation of tax assets and liabilities are included within current tax liabilities. At 30 September 2021 the total value of these provisions, including foreign exchange movements, was £306 million (2020: £273 million). The assessment of uncertain tax positions is subjective and significant management judgement is required. This judgement is based on current interpretation of legislation, management experience and professional advice. Until matters are finally concluded it is possible that amounts ultimately paid will be different from the amounts provided.

Management have assessed the Group's provision for uncertain tax positions and have concluded that apart from the matters referred to below the provisions in place are not material individually or in aggregate, and that a reasonably possible change in the next financial year would not have a material impact to the results of the Group.

FRENCH TAX LITIGATION

In November 2015 the Group received a challenge from the French tax authorities that could lead to additional tax liabilities of up to £234 million. The challenge concerns the valuation placed on the shares of Altadis Distribution France (now known as Logista France) following an intragroup transfer of shares in October 2012 and the tax consequences flowing from a potentially higher value that is argued for by the tax authorities. In October 2018 the Commission Nationale, an independent adjudication body, whose decision is advisory only, issued a report supportive of the Group's arguments for no adjustment. In December 2018 the French tax authorities issued their final assessments seeking the full amount of additional tax assessed of £234 million (2020: £248 million). In January 2019 the Group appealed against the assessment. In August 2020, the French tax authorities rejected the Group's appeal and the matter will now proceed to litigation. As of September 2021, all submissions have been made to the court and we await a hearing date. The Group believes it is appropriate to maintain a £41 million (2020: £44 million) provision for uncertain tax positions in respect of this matter.

STATE AID UK CFC

The Group continues to monitor developments in relation to EU State Aid investigations. On 25 April 2019, the EU Commission's final decision regarding its investigation into the UK's Controlled Foreign Company regime was published. It concludes that the legislation up until December 2018 does partially represent State Aid. The UK Government has appealed to the European Court seeking annulment of the EU Commission's decision. The Group, along with a number of UK corporates, has made a similar application to the European Court. The UK Government is obliged to collect any State Aid granted pending the outcome of the European Court process.

Based on advice, the Group's position remains that no State Aid has been received, but following HMRC guidance an assessment of potential State Aid was submitted to HMRC in July 2020. In February 2021 a charging notice for £101 million, in line with the Group's assessment, was issued to the Group by HMRC and has since been paid. Advice to date is that our appeal and that of the UK government against the Commission's decision should ultimately be successful so a current tax receivable of £101 million has been recognised as a non-current asset.

Based upon current advice the Group does not consider any provision is required in relation to any other EU State Aid investigation.

TRANSFER PRICING

The Group has tax audits in progress, relating to transfer pricing matters in a number of jurisdictions, principally UK, France and Germany. The Group estimates the potential gross level of exposure relating to transfer pricing issues is approximately £900 million (2020: £800 million). The Group holds a provision of £260 million (2020: £207 million) in respect of these items.

In August 2020 the Group notified HMRC of a potential Diverted Profits Tax (DPT) issue relating to brand rewards. In September 2020, HMRC issued a preliminary notice under the DPT regime in respect of the year ended 30 September 2016 indicating a potential liability of c. £6 million. Collaborative discussions on the issue continue and it is the Group's belief the issue is a transfer pricing one, and will be resolved as such. In November 2020, HMRC issued a final DPT notice, which has now been paid. In September 2021, further preliminary DPT notices were received in respect of the year ended 30 September 2017 indicating a potential liability of c. £4 million. Based on advice, the Group continues to believe this is a transfer pricing matter, but if a settlement is not reached before December 2021 the c. £4 million DPT notice will be payable. On conclusion of the transfer pricing discussions, an appropriate refund is anticipated for all DPT payments.

The Group believe the transfer pricing provision held above appropriately provides for this and other transfer pricing issues.

9. DIVIDENDS

DISTRIBUTIONS TO ORDINARY EQUITY HOLDERS

£ million	2021	2020	2019
Paid interim of 42.12 pence per share (2020: 41.70 pence, 2019: 62.56 pence)			
– Paid June 2019	**–**	–	298
– Paid September 2019	**–**	–	298
– Paid December 2019	**–**	–	679
– Paid June 2020	**–**	197	–
– Paid September 2020	**–**	197	–
– Paid December 2020	**–**	453	–
– Paid June 2021	**199**	–	–
– Paid September 2021	**199**	–	–
Interim dividend paid	**398**	847	1,275
Proposed interim of 48.48 pence per share (2020: 48.00 pence, 2019: 72.00 pence)			
– To be paid December 2021	**458**	–	–
Interim dividend proposed	**458**	–	–
Proposed final of 48.48 pence per share (2020: 48.01 pence, 2019: 72.01 pence)			
– Paid March 2020	**–**	–	680
– Paid March 2021	**–**	454	–
– To be paid March 2022	**458**	–	–
Final dividend	**458**	454	680
Total ordinary share dividends of 139.08 pence per share (2020: 137.71 pence, 2019: 206.57 pence)	**1,314**	1,301	1,955

The third interim dividend for the year ended 30 September 2021 of 48.48 pence per share amounts to a proposed dividend of £458 million, which will be paid in December 2021.

The proposed final dividend for the year ended 30 September 2021 of 48.48 pence per share amounts to a proposed dividend payment of £458 million in March 2022 based on the number of shares ranking for dividend at 30 September 2021, and is subject to shareholder approval. If approved, the total dividend paid in respect of 2021 will be £1,314 million (2020: £1,301 million). The dividend paid during 2021 is £1,305 million (2020: £1,753 million).

10. EARNINGS PER ORDINARY SHARE

Basic earnings per share is based on the profit for the period attributable to the owners of the parent and the weighted average number of ordinary shares in issue during the period excluding shares held to satisfy the Group's employee share schemes and shares purchased by the Company and held as treasury shares. Diluted earnings per share have been calculated by taking into account the weighted average number of shares that would be issued if rights held under the employee share schemes were exercised. No instruments have been excluded from the calculation for any period on the grounds that they are anti-dilutive.

£ million	2021	2020
Earnings: basic and diluted – attributable to owners of the Parent Company	**2,834**	1,495

Millions of shares	2021	2020
Weighted average number of shares:		
Shares for basic earnings per share	**945.0**	944.4
Potentially dilutive share options	**2.5**	1.4
Shares for diluted earnings per share	**947.5**	945.8

Pence	2021	2020
Basic earnings per share	**299.9**	158.3
Diluted earnings per share	**299.1**	158.1

RECONCILIATION FROM REPORTED TO ADJUSTED EARNINGS AND EARNINGS PER SHARE

	2021		2020	
£ million unless otherwise indicated	Earnings per share (pence)	Earnings	Earnings per share (pence)	Earnings
Reported basic	**299.9**	**2,834**	158.3	1,495
Acquisition and disposal costs	**1.8**	**17**	2.8	26
Amortisation and impairment of acquired intangibles	**44.3**	**419**	49.2	466
Profit on disposal of subsidiaries	**(29.7)**	**(281)**	–	–
Excise tax provision	**(0.1)**	**(1)**	(1.7)	(16)
Fair value adjustment of loan receivable	**(1.6)**	**(15)**	6.6	62
Net fair value and exchange movements on financial instruments	**(60.7)**	**(574)**	25.3	239
Post-employment benefits net financing cost	**(0.3)**	**(3)**	0.4	4
Restructuring costs	**19.6**	**185**	18.4	174
Tax on disposal of premium cigar division	**(1.2)**	**(11)**	2.0	19
Recognition of tax credits	**(25.3)**	**(239)**	(7.1)	(67)
Uncertain tax positions	**–**	**–**	8.2	77
Tax on unrecognised losses	**5.0**	**47**	(4.3)	(41)
Adjustments above attributable to non-controlling interests	**(4.6)**	**(43)**	(3.7)	(35)
Adjusted	**247.1**	**2,335**	254.4	2,403
Adjusted diluted	**246.4**	**2,335**	254.1	2,403
Organic adjusted	**246.5**	**2,330**	247.2	2,335
Premium Cigar divestment adjusted	**0.6**	**5**	7.2	68
Adjusted	**247.1**	**2,335**	254.4	2,403
Organic adjusted diluted	**245.8**	**2,330**	246.9	2,335
Premium Cigar divestment adjusted diluted	**0.6**	**5**	7.2	68
Adjusted diluted	**246.4**	**2,335**	254.1	2,403

11. DISPOSAL OF SUBSIDIARIES

On 27 April 2020 the Group announced that it had agreed the sale of the Premium Cigar Division ("the Division"). The total cash receipts expected for the transaction are €1,198 million (including the La Romana disposal - see below). The share sale element of the sale of the Division completed on 29 October 2020 and to date €1,041 million (£845 million) of consideration has been received. A further €88 million of deferred consideration relating to the share sale was received on 26 October 2021.

The profit arising on disposal of the Division was £281 million and includes £337 million of foreign exchange gains that had previously been recognised in the foreign exchange reserve and that were recycled to the income statement on completion of the transaction.

The sale of the La Romana factory in the Dominican Republic is due to complete during the Group's 2022 financial year when it is expected that €69 million of sales consideration will be received subject to a true up in respect of inventory values. The carrying value of the net assets of the La Romana factory total $64 million. This sale of the La Romana factory does not meet the recognition criteria for an asset held for sale as there is ongoing work to separate the factory for disposal.

On 18 June 2021 a letter of intent to sell Supergroup S.A.S. was agreed. At 30 September 2021, the Group has assessed the IFRS 5 criteria for presentation of the business as held for disposal. Given the progress made on the sale the Group considers the IFRS 5 criteria to have been met and therefore it is highly probable that a disposal will be completed. The Group has therefore presented the net assets of Supergroup S.A.S. as current assets and liabilities held for sale. A fair value adjustment of £3 million and a reclassification of an associated provision of £9 million has resulted in the non-current assets being written down to nil.

In addition to the above, certain assets within the Distribution business have also been reclassified to assets held for sale due to the existence of purchase offers from third parties. The value of these assets on 30 September 2021 was £8 million.

The assets and liabilities classified as held for disposal are as follows:

£ million	2021	2020
Non-current assets		
Intangible assets	**–**	101
Property, plant and equipment	**8**	17
Investments accounted for using the equity method	**–**	584
Trade and other receivables	**–**	35
Right of use leased assets	**–**	7
Deferred tax assets	**–**	10
	8	754
Current assets		
Inventories	**9**	166
Trade and other receivables	**18**	67
Cash and cash equivalents	**–**	75
	27	308
Total assets	**35**	1,062
Current liabilities		
Trade and other payables	**(13)**	(35)
Tax liabilities	**(4)**	–
Provisions	**(18)**	(3)
	(35)	(38)
Total liabilities	**(35)**	(38)
Net assets	**–**	1,024

12. INTANGIBLE ASSETS

£ million	Goodwill	Intellectual property and product development	Supply agreements	Software	Total
					2021
Cost					
At 1 October 2020	**14,435**	**12,994**	**1,463**	**465**	**29,357**
Additions	**–**	**9**	**–**	**28**	**37**
Disposals	**(260)**	**5**	**(2)**	**(22)**	**(279)**
Exchange movements	**(758)**	**(649)**	**(74)**	**(20)**	**(1,501)**
At 30 September 2021	**13,417**	**12,359**	**1,387**	**451**	**27,614**
Amortisation and impairment					
At 1 October 2020	**1,895**	**7,663**	**1,341**	**298**	**11,197**
Amortisation charge for the year	**–**	**333**	**85**	**37**	**455**
Impairment	**–**	**118**	**–**	**2**	**120**
Disposals	**(260)**	**–**	**(1)**	**(15)**	**(276)**
Exchange movements	**(93)**	**(379)**	**(70)**	**(14)**	**(556)**
Accumulated amortisation	**–**	**7,196**	**1,355**	**304**	**8,855**
Accumulated impairment	**1,542**	**539**	**–**	**4**	**2,085**
At 30 September 2021	**1,542**	**7,735**	**1,355**	**308**	**10,940**
Net book value					
At 30 September 2021	**11,875**	**4,624**	**32**	**143**	**16,674**

£ million	Goodwill	Intellectual property and product development	Supply agreements	Software	Total
					2020
Cost					
At 1 October 2019	14,232	13,021	1,423	421	29,097
Additions	–	74	–	38	112
Disposals	–	(1)	–	(7)	(8)
Reclassifications	(1)	–	–	7	6
Transferred to held for disposal (note 11)	–	7	2	–	9
Exchange movements	204	(107)	38	6	141
At 30 September 2020	14,435	12,994	1,463	465	29,357
Amortisation and impairment					
At 1 October 2019	1,847	7,169	1,220	265	10,501
Amortisation charge for the year	–	466	85	33	584
Impairment	12	29	–	2	43
Disposals	–	–	–	(6)	(6)
Reclassifications	(1)	–	–	–	(1)
Exchange movements	37	(1)	36	4	76
Accumulated amortisation	–	7,242	1,341	296	8,879
Accumulated impairment	1,895	421	–	2	2,318
At 30 September 2020	1,895	7,663	1,341	298	11,197
Net book value					
At 30 September 2020	12,540	5,331	122	167	18,160

Amortisation and impairment of acquired intangibles excluded from adjusted operating profit amounted to £450 million (2020: £523 million), this comprises amortisation on intellectual property of £320 million (2020: £466 million), impairment on intellectual property of £45 million (2020: £14 million) and amortisation on supply agreements of £85 million (2020: £85 million).

A further £73 million (2020: £nil) impairment of intellectual property and product development assets has also been recognised in restructuring costs and therefore excluded from adjusted operating profits.

Intellectual property mainly comprises brands acquired in the USA in 2015 and through the purchases of Altadis in 2008 and Commonwealth Brands in 2007.

Supply agreements include Distribution customer relationships. All were acquired as part of the Altadis purchase.

Intangible amortisation and impairment are included within administrative and other expenses in the consolidated income statement.

Amortisation and impairment in respect of intangible assets other than software and internally generated intellectual property are treated as reconciling items between reported operating profit and adjusted operating profit, except to the extent these have been treated as restructuring costs.

ACQUISITIONS

NERUDIA

On 23 October 2017, the Group acquired 100 per cent of the share capital of Nerudia Limited. As previously disclosed, a portion of the consideration remained contingent and was tied to certain contractual pre-conditions. The matter is expected to conclude in the near future.

GOODWILL AND INTANGIBLE ASSET IMPAIRMENT REVIEW

Goodwill is allocated to groups of cash-generating units (CGUs) that are expected to benefit from the business combination in which the goodwill arose. For the Tobacco & NGP business CGUs are based on the markets where the business operates and are grouped in line with the divisional structure in operation during the year. The groupings represent the lowest level at which goodwill is monitored for internal management purposes. A summary of the carrying value of goodwill and intangible assets with indefinite lives is set out below.

	2021		2020	
£ million	**Goodwill**	**Intangible assets with indefinite lives**	Goodwill	Intangible assets with indefinite lives
Europe	**4,402**	**334**	4,645	353
Americas	**4,042**	**–**	4,265	–
Africa, Asia & Australasia	**1,740**	**132**	1,836	140
Tobacco & NGP	**10,184**	**466**	10,746	493
Distribution	**1,691**	**–**	1,794	–
	11,875	**466**	12,540	493

Goodwill has arisen principally on the acquisitions of Reemtsma in 2002 (all CGU groupings), Commonwealth Brands in 2007 (USA), Altadis in 2008 (all CGU groupings) and ITG Brands in 2015 (USA). Intangible assets with indefinite lives relate to the tobacco trademark, Davidoff, which was purchased as part of the acquisition of Reemtsma in 2002.

The Group tests goodwill and intangible assets with indefinite lives for impairment annually, or more frequently if there are any indications that impairment may have arisen. The value of a Cash Generating Unit Grouping (CGUG) is based on value-in-use calculations. These calculations use cash flow projections derived from financial plans of our Tobacco business which are based on detailed bottom-up market-by-market forecasts of projected sales volumes for each product line. These forecasts reflect, on an individual market basis, numerous assumptions and estimates regarding anticipated changes in market size, prices and duty regimes, consumer uptrading and downtrading, consumer preferences and other changes in product mix, based on long-term market trends, market data, anticipated regulatory developments, and management experience and expectations. We consider that pricing, market size, market shares and cost inflation are the key assumptions used in our plans.

GROWTH RATES AND DISCOUNT RATES USED

The compound annual growth rates implicit in these value-in-use calculations are shown below.

			2021			2020
%	**Pre-tax discount rate**	**Initial growth rate**	**Long-term growth rate**	Pre-tax discount rate	Initial growth rate	Long-term growth rate
Europe	**9.9**	**2.7**	**0.1**	9.6	2.6	1.0
Americas	**9.8**	**5.7**	**1.6**	8.8	1.3	1.9
Africa, Asia & Australasia	**12.1**	**1.7**	**0.3**	12.9	0.4	2.1
Distribution	**11.2**	**1.5**	**1.4**	13.0	0.8	1.6

Cash flows from the business plan period are used for year one, two and three, then extrapolated out to year five using the implicit growth rate, shown in the table above as the initial growth rate. In certain markets, the extrapolated growth rate can exceed the long term growth rate based on the business plan being a better reflection of the anticipated initial growth. Estimated long term weighted average compound growth rates are used beyond year five.

Long term growth rates are determined as the lower of:

- the nominal GDP growth rates for the country of operation; and
- the extrapolation of the initial growth rates as estimated by management for years one to five

Long-term growth rates are based on management's long-term expectations, taking account of industry specific factors such as the nature of our products, the role of excise in government fiscal policy, and relatively stable and predictable long-term macro trends in the Tobacco industry. Year on year variations in initial growth rates may result in consequential changes to estimated long term rates.

Discount rates used are based on the Group's weighted average cost of capital adjusted for the different risk profiles of the CGUs. Our impairment projections are prepared under the basis set out in IAS 36 which can differ from our internal plans.

Europe's initial growth rate is broadly consistent with the prior year, and the long term growth rate has reduced reflecting the alignment of outer year rates to reductions in initial growth rates for certain markets.

Americas shows an increased initial growth rate driven by the mass market cigar growth (improved sales and benefits from manufacturing and investment in leaf supply), reduced one-off costs for NGP & litigation settlements. The reduction in the long term growth rates is based on changes in the macroeconomic outlook.

Africa, Asia & Australasia (AAA) increases in the initial growth rates are driven by improved medium term forecasts, which are heavily influenced by changes in the Australian market. The long term growth rate reduction reflects changes in certain assumptions associated with the extrapolation of the initial growth rate for a number of individual markets.

The Distribution discount rate reflects reductions in the country risk premium driven by macroeconomic factors. The initial growth rates reflects improved medium term forecasts.

Our impairment testing confirms there are sufficient cash flows to support the current carrying values of the goodwill held at 30 September 2021. Any reasonable movement in the assumptions used in the impairment tests would not result in an impairment. The complexity of the estimation process and issues related to the assumptions, risks and uncertainties inherent in the application of the Group's accounting estimates in relation to intangible assets affect the amounts reported in the financial statements, especially the estimates of the expected useful economic lives and the carrying values of those assets. If business conditions materially change it is likely that materially different amounts could be reported in the Group's financial statements. There are uncertainties associated with estimating the valuation of the recoverable amount.

At the present time the recoverable amount is significantly in excess of the carrying value of goodwill and other intangible assets. However, given the uncertainties mentioned above this could change in the future.

Consideration of the impact of climate change

In terms of the possible impacts of climate change, the two key metrics that could be sensitive to this are the initial and the long-term growth rate. If climate change has a negative impact on product sales revenues and/or the operating costs of the Group there could be a potential impact on the discounted cash flow growth rates used within the valuation model. Lower future growth rates would reduce the level of the discounted cash flow valuation and hence the amount of headroom available to the Group above an impairment trigger. At present, the material short to medium term risks presented by possible climate change impacts will be factored into the initial growth rates where they are known and can be quantified. For example, government regulatory changes which impact operating costs will be recognised where they are known.

However, the current level of headroom for goodwill is substantial for the Group. Using the current growth rate assumptions, on a CGUG basis, the total value of assets will be recovered via the discounted cash flows within a maximum of 9 years. Therefore, at present, changes in the long-term growth rates beyond this period due to the impact of climate change would not be expected to trigger an impairment.

OTHER INTANGIBLE ASSETS

Other intangible assets are considered for impairment risk. The carrying values of brand intangibles are reviewed against expected future cash flows of associated products. Impairment will only be recognised where there is evidence that the carrying value of the brand cannot be recovered through those cash flows. No impairments have been recognised for brand intangibles.

Intellectual property and product development intangible assets have also been reviewed to identify potential impairment triggers. The impact of the 2021 strategic review programme, which was announced in the current

financial year, has been identified as an impairment trigger. The change in commercial plans has resulted in the exit of NGP product offerings in certain markets and the implementation of a different approach to future product development, which focuses on achieving the best potential for sustainable growth and is being led by consumer needs. The change in strategy has meant that certain previously acquired intangible assets and internally generated development assets are now no longer required to support the business. As a result of this, these assets have been determined to have a nil residual value. This has resulted in an impairment of £118 million relating to NGP intangible assets (intellectual property and product development) in the year (2020: £29 million). Of this impairment charge £73 million related to internally generated intangible assets and has been taken as a restructuring cost and the remaining £45 million has been recognised as an impairment charge within amortisation and impairment of acquired intangible assets, both of which are excluded from adjusted operating profit. The impairment of £118 million is split between Europe (£96 million) and Americas (£22 million) operating segments.

A further £2 million (2020: £2 million) impairment charge was incurred in the year relating to software.

13. PROPERTY, PLANT AND EQUIPMENT

				2021
£ million	Property	Plant and equipment	Fixtures and motor vehicles	Total
Cost				
At 1 October 2020	905	2,216	438	3,559
Additions	13	99	53	165
Disposals	(78)	(114)	(43)	(235)
Reclassifications	4	1	(4)	1
Transfer to current assets held for disposal	(8)	–	(12)	(20)
Exchange movements	(39)	(116)	(21)	(176)
At 30 September 2021	797	2,086	411	3,294
Depreciation and impairment				
At 1 October 2020	188	1,190	282	1,660
Depreciation charge for the year	20	104	33	157
Impairment	2	11	–	13
Disposals	(40)	(93)	(30)	(163)
Reclassifications	4	(6)	(2)	(4)
Exchange movements	(12)	(60)	(12)	(84)
At 30 September 2021	162	1,146	271	1,579
Net book value				
At 30 September 2021	635	940	140	1,715

£ million	Property	Plant and equipment	Fixtures and motor vehicles	2020 Total
Cost				
At 1 October 2019	909	2,193	440	3,542
Additions	11	122	41	174
Disposals	(16)	(65)	(30)	(111)
Reclassifications	3	1	(13)	(9)
Exchange movements	(2)	(35)	–	(37)
At 30 September 2020	905	2,216	438	3,559
Depreciation and impairment				
At 1 October 2019	181	1,104	278	1,563
Depreciation charge for the year	18	117	34	169
(Impairment write back)/impairment	(2)	38	–	36
Disposals	(6)	(49)	(28)	(83)
Reclassifications	(1)	(2)	(2)	(5)
Exchange movements	(2)	(18)	–	(20)
At 30 September 2020	188	1,190	282	1,660
Net book value				
At 30 September 2020	717	1,026	156	1,899

14. RIGHT OF USE ASSETS AND LEASE LIABILITY

The movements in Right of Use Assets in the year were as follows:

£ million	Property	Plant and equipment	Fixtures and motor vehicles	2021 Total
Net book value				
At 1 October 2020	**254**	**8**	**31**	**293**
Additions	**29**	**2**	**22**	**53**
Terminations & modifications	**(21)**	**(2)**	**(3)**	**(26)**
Depreciation	**(49)**	**(2)**	**(15)**	**(66)**
Exchange movements	**(11)**	**–**	**(1)**	**(12)**
At 30 September 2021	**202**	**6**	**34**	**242**

The movements in lease liabilities in the year were as follows:

£ million	Lease Liabilities
At 1 October 2020	**299**
Cash flow	**(69)**
Accretion of interest	**7**
New leases, terminations & modifications	**26**
Exchange movements	**(12)**
At 30 September 2021	**251**

The maturity profile of the carrying amount of the Group's lease liabilities and the contractual cash flows as at 30 September 2021 is as follows:

£ million	Lease liabilities	Effect of discounting	2021 Contractual cash flows
Amounts maturing:			
Within one year	**57**	**7**	**64**
Between one and five years	**124**	**17**	**141**
In five years or more	**70**	**8**	**78**
	251	**32**	**283**

Future minimum lease payments liabilities are analysed as below:

				2021
	Property	**Plant and equipment**	**Fixtures and motor vehicles**	**Total**
Due in less than one year	**47**	**2**	**15**	**64**
Due between one and five years	**116**	**3**	**22**	**141**
Due in more than five years	**78**	**–**	**–**	**78**
Total future minimum lease payments payable	**241**	**5**	**37**	**283**
Effect of discounting				**(32)**
Lease liability				**251**

The following are the amounts recognised in the Consolidated Income statement:

	2021	2020
Expenses relating to short-term leases	**4**	4
Expenses relating to low value asset leases	**2**	2
Depreciation expense of Right of Use Assets	**66**	72
Interest on lease liabilities	**7**	7

The movements in Right of Use Assets in the year ending 30 September 2020 were as follows:

				2020
£ million	Property	Plant and equipment	Fixtures and motor vehicles	Total
Net book value				
At 1 October 2019	279	7	41	327
Additions	24	4	11	39
Terminations & modifications	(2)	–	(4)	(6)
Depreciation	(52)	(3)	(17)	(72)
Exchange movements	5	–	–	5
At 30 September 2020	254	8	31	293

The movements in lease liabilities in the year ending 30 September 2020 were as follows:

£ million	Lease Liabilities
At 1 October 2019	326
Cash flow	(72)
Accretion of interest	7
New leases, terminations & modifications	32
Exchange movements	6
At 30 September 2020	299

The maturity profile of the carrying amount of the Group's lease liabilities and the contractual cash flows as at 30 September 2020 is as follows:

			2020
£ million	Lease liabilities	Effect of discounting	Contractual cash flows
Amounts maturing:			
Within one year	64	6	70
Between one and five years	160	15	175
In five years or more	75	12	87
	299	33	332

Future minimum lease payments liabilities as at 30 September 2020 are analysed as below:

				2020
	Property	Plant and equipment	Fixtures and motor vehicles	Total
Due in less than one year	53	3	14	70
Due between one and five years	151	5	19	175
Due in more than five years	87	–	–	87
Total future minimum lease payments payable	291	8	33	332
Effect of discounting				(33)
Lease liability				299

15. INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD

The principal joint ventures during the year were Corporación Habanos SA, Cuba, Altabana SL, Spain and Global Horizon Ventures Limited. Corporación Habanos SA, Cuba and Altabana SL, Spain were disposed of on 29 October 2020 as part of the Premium Cigar Division. Summarised financial information for the Group's joint ventures, which are accounted for under the equity method, is shown below:

					2021
£ million	**Corporación Habanos**	**Altabana**	**Global Horizon Ventures**	**Others**	**Total**
Revenue	**15**	**30**	**18**	**27**	**90**
Profit after tax	**5**	**5**	**13**	**5**	**28**
Non-current assets	**–**	**–**	**24**	**3**	**27**
Current assets	**–**	**–**	**47**	**49**	**96**
Total assets	**–**	**–**	**71**	**52**	**123**
Current liabilities	**–**	**–**	**(3)**	**(43)**	**(46)**
Non-current liabilities	**–**	**–**	**–**	**(9)**	**(9)**
Total liabilities	**–**	**–**	**(3)**	**(52)**	**(55)**
Net assets	**–**	**–**	**68**	**–**	**68**

					2020
£ million	Corporación Habanos	Altabana	Global Horizon Ventures	Others	Total
Revenue	188	322	10	61	581
Profit after tax	43	52	1	10	106
Non-current assets	458	27	–	11	496
Current assets	99	233	41	82	455
Total assets	557	260	41	93	951
Current liabilities	(147)	(40)	(2)	(16)	(205)
Non-current liabilities	(28)	(5)	–	(45)	(78)
Total liabilities	(175)	(45)	(2)	(61)	(283)
Net assets	382	215	39	32	668

TRANSACTIONS AND BALANCES WITH JOINT VENTURES

£ million	**2021**	2020
Sales to	**6**	163
Purchases from	**19**	111
Accounts receivable from	**–**	–
Accounts payable to	**(3)**	(24)

MOVEMENT ON INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD

£ million	2021	2020
At 1 October	**117**	81
Share of profit for the year from joint ventures and associates	**11**	45
Increase in investment in associates	**3**	5
Impairment of investment in joint ventures	**–**	(1)
Dividends	**(9)**	(27)
Classification (to)/from held for disposal and disposals of business	**(32)**	50
Foreign exchange losses	**(2)**	(36)
At 30 September	**88**	117

16. INVENTORIES

£ million	2021	2020
Raw materials	**839**	1,001
Work in progress	**58**	74
Finished inventories	**2,765**	2,781
Other inventories	**172**	209
	3,834	4,065

Other inventories mainly comprise duty-paid tax stamps.

Within finished inventories of £2,765 million (2020: £2,781 million) there is excise duty of £1,282 million (2020: £1,312 million).

It is generally recognised industry practice to classify leaf tobacco inventory as a current asset, although part of such inventory, because of the duration of the processing cycle ordinarily would not be consumed within one year. We estimate that around £115 million (2020: £179 million) of leaf tobacco held within raw materials will not be utilised within a year of the balance sheet date.

17. TRADE AND OTHER RECEIVABLES

	2021		2020	
£ million	Current	Non-current	Current	Non-current
Trade receivables	**2,431**	**3**	2,410	4
Less: loss allowance	**(68)**	**(3)**	(112)	(4)
Net trade receivables	**2,363**	**–**	2,298	–
Other receivables	**227**	**58**	178	48
Prepayments	**159**	**4**	162	9
	2,749	**62**	2,638	57

Trade receivables may be analysed as follows:

	2021		2020	
£ million	Current	Non-current	Current	Non-current
Within credit terms	**2,271**	**–**	2,138	–
Past due by less than 3 months	**85**	**–**	77	–
Past due by more than 3 months	**7**	**–**	83	–
Amounts that are impaired	**68**	**3**	112	4
	2,431	**3**	2,410	4

The movements in the total loss allowance for receivables can analysed as follows:

£ million	2021	2020
At 1 October	**116**	77
Net (decrease) / increase in provision	**(45)**	39
At 30 September	**71**	116

Trade receivables are reviewed by their risk profiles and loss patterns to assess credit risk. Historical and forward-looking information is considered to determine the appropriate expected credit loss allowance. Provision levels are calculated on the residual credit risk after consideration of any credit protection which is used by the Group. Expected credit losses (ECLs) are applied to net trade receivables which are measured reflecting lifetime ECLs using the simplified approach. Trade receivables are all repayable within 12 months and therefore the ECL provision represents all expected losses within this term.

18. CASH AND CASH EQUIVALENTS

£ million	2021	2020
Cash at bank and in hand	**673**	791
Short-term deposits and other liquid assets	**614**	835
	1,287	1,626

£152 million (2020: £154 million) of total cash and cash equivalents is held in countries in which prior approval is required to transfer the funds abroad. Nevertheless, if the Group complies with these requirements, such liquid funds are at its disposition within a reasonable period of time which in all cases is 3 months or less from the date the transfer is requested.

19. TRADE AND OTHER PAYABLES

	2021		2020	
£ million	Current	Non-current	Current	Non-current
Trade payables	**1,018**	**–**	1,191	–
Duties payable	**5,507**	**–**	6,129	–
Other taxes and social security contributions	**1,399**	**–**	1,603	–
Other payables	**449**	**–**	464	–
Accruals	**733**	**7**	783	5
	9,106	**7**	10,170	5

20. BORROWINGS

The Group's borrowings held at amortised cost, are as follows:

£ million	2021	2020
Current borrowings		
Bank loans and overdrafts	**51**	61
Capital market issuance:		
€1,000m 2.25% notes due February 2021	**–**	925
€500m 0.5% notes due July 2021	**–**	456
£1,000m 9.0% notes due February 2022	**1,056**	–
Total current borrowings	**1,107**	1,442
Non-current borrowings		
Bank loans	**1**	1
Capital market issuance:		
£1,000m 9.0% notes due February 2022	**–**	1,056
$1,250m 3.75% notes due July 2022	**–**	980
$1,000m 3.5% notes due February 2023	**746**	782
€750m 1.25% notes due August 2023	**646**	684
£600m 8.125% notes due March 2024	**626**	626
$1,000m 3.125% notes due July 2024	**745**	782
€500m 1.375% notes due January 2025	**434**	460
$1,500m 4.25% notes due July 2025	**1,119**	1,172
€650m 3.375% notes due February 2026	**570**	604
$750m 3.5% notes due July 2026	**559**	586
£500m 5.5% notes due September 2026	**500**	500
€750m 2.125% notes due February 2027	**653**	692
$1,000m 3.875% notes due July 2029	**745**	781
£500m 4.875% notes due June 2032	**505**	504
€1,000m 1.75% notes due March 2033	**866**	–
Total non-current borrowings	**8,715**	10,210
Total borrowings	**9,822**	11,652
Analysed as:		
Capital market issuance	**9,770**	11,590
Bank loans and overdrafts	**52**	62

Current and non-current borrowings include interest payable of £56 million (2020: £13 million) and £93 million (2020: £151 million) respectively as at the balance sheet date.

Interest payable on capital market issuances are at fixed rates of interest and interest payable on bank loans and overdrafts are at floating rates of interest.

On 30 November 2020, €1,000 million 2.25 per cent notes were repaid. On 18 March 2021, €1,000 million 1.75 per cent notes due March 2033 were issued. On 27 April 2021, €500 million 0.5 per cent notes were repaid. On 29 September 2021, $1,250 million 3.75 per cent notes were repaid.

All borrowings are unsecured and the Group has not defaulted on any borrowings during the year (2020: no defaults).

NON-CURRENT FINANCIAL LIABILITIES

The maturity profile of the carrying amount of the Group's non-current liabilities as at 30 September 2021 (including lease liabilities detailed in note 14 and net derivative financial instruments detailed in note 22) is as follows:

				2021
£ million	**Borrowings**	**Lease liabilities**	**Net derivative financial liabilities/ (assets)**	**Total**
Amounts maturing:				
Between one and two years	**1,393**	**49**	**(6)**	**1,436**
Between two and five years	**4,553**	**75**	**(9)**	**4,619**
In five years or more	**2,769**	**70**	**608**	**3,447**
	8,715	**194**	**593**	**9,502**

				2020
£ million	Borrowings	Lease liabilities	Net derivative financial liabilities/ (assets)	Total
Amounts maturing:				
Between one and two years	2,037	54	17	2,108
Between two and five years	4,506	106	(37)	4,575
In five years or more	3,667	75	848	4,590
	10,210	235	828	11,273

FAIR VALUE OF BORROWINGS

The fair value of borrowings as at 30 September 2021 is estimated to be £10,386 million (2020: £12,496 million). £10,334 million (2020: £12,434 million) relates to capital market issuance and has been determined by reference to market prices as at the balance sheet date. A comparison of the carrying amount and fair value of capital market issuance by currency is provided below. The fair value of all other borrowings is considered to equal their carrying amount.

	2021		2020	
£ million	**Balance sheet amount**	**Fair value**	Balance sheet amount	Fair value
GBP	**2,686**	**2,894**	2,686	3,054
EUR	**3,168**	**3,278**	3,821	3,943
USD	**3,916**	**4,162**	5,083	5,437
Total capital market issuance	**9,770**	**10,334**	11,590	12,434

UNDRAWN REVOLVING CREDIT FACILITIES

At 30 September the Group had the following undrawn committed facilities:

£ million	**2021**	2020
Amounts maturing:		
Between one and two years	**–**	1,551
Between two and five years	**3,012**	3,193
	3,012	4,744

During the year the maturity date of the Group's existing syndicated multicurrency facility for €3,500 was extended to 30 September 2024.

During the year six bilateral facilities for a total of €1,700 million were cancelled.

21. FINANCIAL RISK FACTORS

FINANCIAL RISK MANAGEMENT

OVERVIEW

In the normal course of business, the Group is exposed to financial risks including, but not limited to, market, credit and liquidity risk. This note explains the Group's exposure to these risks, how they are measured and assessed, and summarises the policies and processes used to manage them, including those related to the management of capital.

The Group operates a centralised treasury function which is responsible for the management of the financial risks of the Group, together with its financing and liquidity requirements. Financial risks comprise, but are not limited to, exposures to funding and liquidity, interest rate, foreign exchange and counterparty credit risk. The treasury function is also responsible for the financial risk management of the Group's global defined benefit pension schemes and management of Group wide insurance programs. The treasury function does not operate as a profit centre, nor does it enter into speculative transactions.

The Group's treasury activities are overseen by the Treasury Committee, which meets when required and comprises the Chief Financial Officer, the Company Secretary, and the Director of Treasury. The Treasury Committee operates in accordance with the terms of reference set out by the Board and a framework (the Treasury Committee framework) which sets out the expectations and boundaries to assist in the effective oversight of treasury activities. The Director of Treasury reports on a regular basis to the Treasury Committee.

The Board reviews and approves all major treasury decisions.

The Group's management of financial risks cover the following:

(A) MARKET RISK

PRICE RISK

The Group is not exposed to equity securities price risk other than assets held by its pension funds disclosed in note 24 and the investment in convertible debentures issued by Auxly Cannabis Group Inc. The Group is exposed to commodity price risk in that there may be fluctuations in the price of tobacco leaf. As with other agricultural commodities, the price of tobacco leaf tends to be cyclical as supply and demand considerations influence tobacco plantings in those countries where tobacco is grown. Also, different regions may experience variations in weather patterns that may affect crop quality or supply and so lead to changes in price. The Group seeks to reduce this price risk by sourcing tobacco leaf from a number of different countries and counterparties and by varying the levels of tobacco leaf held. Currently, these techniques reduce the expected exposure to this risk over the short to medium term to levels considered not material and accordingly, no sensitivity analysis has been presented.

FOREIGN EXCHANGE RISK

The Group is exposed to movements in foreign exchange rates due to its commercial trading transactions and profits denominated in foreign currencies, as well as the translation of cash, borrowings and derivatives held in non-functional currencies.

The Group's financial results are principally exposed to fluctuations in Euro and US dollar exchange rates. Management of the Group's foreign exchange transaction and translation risk is addressed below.

TRANSACTION RISK

The Group's material transaction exposures arise on costs denominated in currencies other than the functional currencies of subsidiaries, including the purchase of tobacco leaf, which is sourced from various countries but purchased principally in US dollars, and packaging materials which are sourced from various countries and purchased in a number of currencies. The Group is also exposed to transaction foreign exchange risk on the conversion of foreign subsidiary earnings into sterling to fund the external dividends to shareholders. This is managed by selling Euros and US dollars monthly throughout the year. Other foreign currency flows are matched where possible and remaining foreign currency transaction exposures are not hedged.

TRANSLATION RISK

The Group seeks to broadly match the currency of borrowings to the currency of its underlying investments in overseas subsidiaries, which are primarily Euros and US dollars. The Group issues debt in the most appropriate market or markets at the time of raising new finance and has a policy of using derivative financial instruments, cross-currency swaps, to change the currency of debt as required. Borrowings denominated in, or swapped into foreign currencies to match the Group's investments in overseas subsidiaries are treated as a hedge against the net investment where appropriate.

FOREIGN EXCHANGE SENSITIVITY ANALYSIS

The Group's sensitivity to foreign exchange rate movements, which impacts the translation of monetary items held by subsidiary companies in currencies other than their functional currencies, is illustrated on an indicative basis below. The sensitivity analysis has been prepared on the basis that net debt and the proportion of financial instruments in foreign currencies remain constant, and that there is no change to the net investment hedge designations in place at 30 September 2021. The sensitivity analysis does not reflect any change to revenue or non-finance costs that may result from changing exchange rates, and ignores any taxation implications and offsetting effects of movements in the fair value of derivative financial instruments.

£ million	**2021 Increase in income**	2020 Increase in income
Income statement impact of non-functional currency foreign exchange exposures:		
10% appreciation of Sterling against Euro (2020: 10%)	**378**	544
10% appreciation of Sterling against US dollar (2020: 10%)	**7**	8

An equivalent depreciation of Sterling against the above currencies would cause a decrease in income of £462 million and £9 million for Euro and US dollar exchange rates respectively (2020: £665 million and £10 million).

Movements in equity in the table below relate to intercompany loans treated as quasi-equity under IAS 21 and hedging instruments designated as net investment hedges of the Group's Euro and US Dollar denominated assets.

£ million	**2021 Change in equity**	2020 Change in equity
Equity impact of non-functional currency foreign exchange exposures:		
10% appreciation of Sterling against Euro (2020: 10%)	**264**	405
10% appreciation of Sterling against US dollar (2020: 10%)	**270**	(134)

An equivalent depreciation of Sterling against the above currencies would result in a change in equity of £(323) million and £(330) million for euro and US dollar exchange rates respectively (2020: £(494) million and £163 million).

At 30 September 2021, after the effect of derivative financial instruments, approximately 78 per cent of the Group's net debt was denominated in Euro and non US Dollar currencies (2020: 70 per cent), 22 per cent in US dollars (2020: 30 per cent).

INTEREST RATE RISK

The Group's interest rate risk arises from its borrowings net of cash and cash equivalents, with the primary exposures arising from fluctuations in Euro and US dollar interest rates. Borrowings at variable rates expose the Group to cash flow interest rate risk. Borrowings at fixed rates expose the Group to fair value interest rate risk.

The Group manages its exposure to interest rate risk on its borrowings by entering into derivative financial instruments, interest rate swaps, to achieve an appropriate mix of fixed and floating interest rate debt in accordance with the Treasury Committee framework and Treasury Committee discussions.

As at 30 September 2021, after adjusting for the effect of derivative financial instruments detailed in note 22, approximately 68 per cent (2020: 71 per cent) of net debt was at fixed rates of interest and 32 per cent (2020: 29 per cent) was at floating rates of interest.

INTEREST RATE SENSITIVITY ANALYSIS

The Group's sensitivity to interest rates on its Euro and US dollar monetary items which are primarily external borrowings, cash and cash equivalents, is illustrated on an indicative basis below. The impact in the Group's Income Statement reflects the effect on net finance costs in respect of the Group's net debt and the fixed to floating rate debt ratio prevailing at 30 September 2021, ignoring any taxation implications and offsetting effects of movements in the fair value of derivative financial instruments.

The sensitivity analysis has been prepared on the basis that net debt and the derivatives portfolio remain constant and that there is no net impact on other comprehensive income (2020: £nil).

£ million	**2021 Change in income**	2020 Change in income
Income statement impact of interest rate movements:		
+/- 1% increase in Euro interest rates (2020: 1%)	**28**	28
+/- 1% increase in US dollar interest rates (2020: 1%)	**6**	8

(B) CREDIT RISK

IFRS 9 requires an expected credit loss (ECL) model to be applied to financial assets. The expected credit loss model requires the Group to account for expected losses as a result of credit risk on initial recognition of financial assets and to recognise changes in those expected credit losses at each reporting date. Allowances are measured at an amount equal to the lifetime expected credit losses where the credit risk on the receivables increases significantly after initial recognition. The Group is primarily exposed to credit risk arising from the extension of credit to its customers, on cash deposits and derivatives. The maximum aggregate credit risk to these sources was £4,177 million at 30 September 2021 (2020: £4,902 million).

TRADE AND OTHER RECEIVABLES

Policies are in place to manage the risk associated with the extension of credit to third parties to ensure that commercial intent is balanced effectively with credit risk management. Subsidiaries have policies in place that require appropriate credit checks on customers and credit is extended with consideration to financial risk and creditworthiness. If a customer requires credit beyond an acceptable limit, security may be put in place to minimise the financial impact in the event of a payment default. Instruments that may typically be used as security include non-recourse receivables factoring and bank guarantees. At 30 September 2021 the level of trade receivables that were sold to a financial institution under a non-recourse factoring arrangement totalled £627 million (2020: £686 million). The total value of trade receivables reclassified as fair value was £69 million at 30 September 2021 (2020: £22 million). There was no valuation difference between amortised cost and fair value. Analysis of trade and other receivables is provided in note 17.

FINANCIAL INSTRUMENTS

In order to manage its credit risk to any one counterparty, the Group places cash deposits and enters into derivative financial instruments with a diversified group of financial institutions carrying suitable credit ratings in line with the Treasury Committee framework. Utilisation of counterparty credit limits is regularly monitored by treasury and ISDA agreements are in place to permit the net settlement of assets and liabilities in certain circumstances. In connection with one ISDA Credit Support Annex the Group had placed £37 million as at 30 September 2021 (2020: £47 million) as collateral with a third party in order to manage their counterparty risk on the Group under derivative financial instruments.

The table below summarises the Group's largest exposures to financial counterparties as at 30 September 2021. At the balance sheet date management does not expect these counterparties to default on their current obligations.

	2021		2020	
Counterparty exposure	**S&P credit rating**	**Maximum exposure to credit risk £ million**	S&P credit rating	Maximum exposure to credit risk £ million
Highest	**A+**	**35**	A+	14
2nd highest	**–**	**–**	A	11
3rd highest	**–**	**–**	A+	5
4th highest	**–**	**–**	A+	2
5th highest	**–**	**–**	–	–

(C) LIQUIDITY RISK

The Group is exposed to liquidity risk, which represents the risk of having insufficient funds to meet its financing needs in any particular location when needed. To manage this risk the Group has a policy of actively maintaining a mixture of short, medium and long-term committed facilities that are structured to ensure that the Group has sufficient available funds to meet the forecast requirements of the Group over the short to medium term. To prevent over-reliance on individual sources of liquidity, funding is provided across a range of instruments including debt capital market issuance, bank term loans, bank revolving credit facilities and European commercial paper.

The Group primarily borrows centrally in order to meet forecast funding requirements, and the treasury function is in regular dialogue with subsidiary companies to ensure their liquidity needs are met. Subsidiary companies are funded by a combination of share capital and retained earnings, intercompany loans, and in very limited cases through external local borrowings. Cash pooling processes are used to centralise surplus cash held by subsidiaries where possible in order to minimise external borrowing requirements and interest costs. Treasury invests surplus cash in bank deposits and uses foreign exchange contracts to manage short term liquidity requirements in line with short term cash flow forecasts. As at 30 September 2021, the Group held liquid assets of £1,287 million (2020: £1,626 million).

The table below summarises the Group's non derivative financial liabilities by maturity based on their contractual cash flows as at 30 September 2021. The amounts disclosed are undiscounted cash flows calculated using spot rates of exchange prevailing at the relevant balance sheet date. Contractual cash flows in respect of the Group's derivative financial instruments are detailed in note 22.

£ million	Balance sheet amount	Contractual cash flows total	<1 year	Between 1 and 2 years	Between 2 and 5 years	> 5 years
						2021
Non-derivative financial liabilities:						
Bank loans	**52**	**52**	**51**	**1**	**–**	**–**
Capital market issuance	**9,770**	**11,158**	**1,341**	**1,678**	**5,068**	**3,071**
Trade payables	**1,018**	**1,018**	**1,018**	**–**	**–**	**–**
Lease liabilities	**251**	**283**	**64**	**55**	**86**	**78**
Total non-derivative financial liabilities	**11,091**	**12,511**	**2,474**	**1,734**	**5,154**	**3,149**

£ million	Balance sheet amount	Contractual cash flows total	<1 year	Between 1 and 2 years	Between 2 and 5 years	> 5 years
						2020
Non-derivative financial liabilities:						
Bank loans	62	62	61	1	–	–
Capital market issuance	11,590	13,302	1,806	2,339	5,165	3,992
Trade payables	1,191	1,191	1,191	–	–	–
Lease liabilities	299	332	70	65	110	87
Total non-derivative financial liabilities	13,142	14,887	3,128	2,405	5,275	4,079

CAPITAL MANAGEMENT

The Group defines capital as adjusted net debt and equity and manages its capital structure through an appropriate balance of debt and equity in order to drive an efficient mix for the Group. Besides the minimum capitalisation rules that may apply to subsidiaries in certain countries, the Group's only externally imposed capital requirements are interest cover and gearing covenants contained within its core external bank debt facilities, with which the Group was fully compliant during the current and prior periods and expects to be so going forward.

The Group continues to manage its capital structure to maintain investment grade credit rating which it monitors by reference to a number of key financial ratios, including ongoing consideration of the return of capital to shareholders via regular dividend payments and in on-going discussions with the relevant rating agencies.

As at 30 September 2021 the Group was rated Baa3/stable outlook by Moody's Investor Service Ltd, BBB/A-2/stable outlook by Standard and Poor's Credit Market Services Europe Limited and BBB/F3/stable outlook by Fitch Ratings Limited.

The Group regards its total capital as follows:

£ million	2021	2020
Adjusted net debt (note 31)	**8,615**	10,299
Equity attributable to the owners of the parent	**5,352**	4,871
Total capital	**13,967**	15,170

HEDGE ACCOUNTING

The Group has investments in foreign operations which are consolidated in its financial statements and whose functional currencies are Euros or US dollars. Where it is practicable and cost effective to do so, the foreign exchange rate exposures arising from these investments are hedged through the use of cross currency swaps and foreign currency denominated debt.

The Group only designates the undiscounted spot element of the cross currency swaps and foreign currency debt as hedging instruments. Changes in the fair value of the cross currency swaps attributable to changes in interest rates and the effect of discounting are recognised directly in profit or loss within the "Finance Costs" line – These amounts are, therefore, not included in the hedge effectiveness assessment.

Net investment gains and losses are reported in exchange movements within other comprehensive income and the hedging instrument foreign currency gains deferred to the foreign currency revaluation reserve are detailed in the statement of changes in equity.

The Group establishes the hedging ratio by matching the notional balance of the hedging instruments with an equal notional balance of the net assets of the foreign operation. Given that only the undiscounted spot element of hedging instruments is designated in the hedging relationship, no ineffectiveness is expected unless the notional balance of the designated hedging instruments exceeds the total balance of the foreign operation's net assets during the reporting period. The foreign currency risk component is determined as the change in the carrying amount of designated net assets of the foreign operation arising solely from changes in spot foreign currency exchange rates.

All net investment hedges were fully effective at 30 September 2021.

The following table sets out the maturity profile of the hedging instruments used in the Group's net investment hedging strategies:

		2021			
		Maturity			
£ million	**Total notional balance**	**<1 year**	**Between 1 and 2 years**	**Between 2 and 5 years**	**> 5 years**
Bonds	**(5,253)**	**–**	**(1,389)**	**(3,219)**	**(645)**
Cross-currency swaps	**(2,782)**	**(1,026)**	**–**	**(1,218)**	**(538)**
	(8,035)	**(1,026)**	**(1,389)**	**(4,437)**	**(1,183)**

		2020			
		Maturity			
£ million	Total notional balance	<1 year	Between 1 and 2 years	Between 2 and 5 years	> 5 years
Bonds	(6,709)	(1,369)	(974)	(3,089)	(1,277)
Cross-currency swaps	(2,950)	–	(1,088)	(704)	(1,158)
	(9,659)	(1,369)	(2,062)	(3,793)	(2,435)

The following table contains details of the hedging instruments and hedged items used in the Group's net investment hedging strategies:

			2021		
		Carrying amount			
£ million	**Notional balance**	**Assets**	**Liabilities**	**Balance sheet line item**	**Changes in fair value used for calculating hedge in effectiveness**
Hedging instrument:					
Bonds	**5,253**	**–**	**5,286**	**Borrowings**	**308**
Cross-currency swaps	**2,782**	**–**	**214**	**Derivative financial instruments**	**168**
Hedged item:					
Investment in a foreign operation	**n/a**	**8,035**			**476**

			2020		
		Carrying amount			
£ million	Notional balance	Assets	Liabilities	Balance sheet line item	Changes in fair value used for calculating hedge in effectiveness
Hedging instrument:					
Bonds	6,709	–	6,755	Borrowings	75
Cross-currency swaps	2,950	–	410	Derivative financial instruments	(86)
Hedged item:					
Investment in a foreign operation	n/a	9,659			(11)

Reconciliation of changes in the value of net investment hedges:

£ million	At the beginning of the year	Income Statement	Other Comprehensive Income	Repayments/ (Borrowings)	At the end of the year
2021					
Derivatives in net investment hedges of foreign operations	**(410)**	**28**	**168**	**–**	**(214)**
Bonds in net investment hedges of foreign operations	**(6,755)**	**13**	**308**	**1,148**	**(5,286)**
Total	**(7,165)**	**41**	**476**	**1,148**	**(5,500)**
2020					
Derivatives in net investment hedges of foreign operations	(341)	17	(86)	–	(410)
Bonds in net investment hedges of foreign operations	(8,482)	87	17	1,623	(6,755)
Total	(8,823)	104	(69)	1,623	(7,165)

The Group also treats certain permanent intragroup loans that meet relevant qualifying criteria under IAS 21 as part of its net investment in foreign operations where appropriate. Intragroup loans with a notional value of €2,506 million (2020 €2,506 million) and US dollar loans with a notional value of $nil (2020: $5,636 million) were treated as part of the Group's net investment in foreign operations at the balance sheet date.

FAIR VALUE ESTIMATION AND HIERARCHY

All financial assets and liabilities are carried on the balance sheet at amortised cost, other than derivative financial instruments and the investment in Auxly Cannabis Group Inc. which are carried at fair value. Derivative fair values are determined based on observable market data such as yield curves, foreign exchange rates and credit default swap prices to calculate the present value of future cash flows associated with each derivative at the balance sheet date (Level 2 classification hierarchy per IFRS 7). Market data is sourced through Bloomberg and valuations are validated by reference to counterparty valuations where appropriate. Some of the Group's derivative financial instruments contain early termination options and these have been considered when assessing the element of the fair value related to credit risk. On this basis the reduction in reported net derivative liabilities due to credit risk is £19 million (2020: £27 million) and would have been a £49 million (2020: £75 million) reduction without considering the early termination options. There were no changes to the valuation methods or transfers between hierarchies during the year. With the exception of capital market issuance and the Auxly investment, the fair value of all financial assets and financial liabilities is considered approximate to their carrying amount as outlined in note 20.

AUXLY CANNABIS GROUP INC.

The Group has invested CAD 123 million into Auxly Cannabis Group Inc. by way of a debenture convertible into 19.9 per cent ownership at a conversion price of $0.81 per share. Repayment of the debenture was due on 25 September 2022, but on 19 April 2021 the debenture agreement was varied and it is now repayable on 25 September 2024. The debenture is valued as a loan receivable measured on the basis of discounting future cash flows at a rate of 14 per cent (2020: 14 per cent) plus the application of an expected credit loss provision. At 30 September 2021 the loan was held at a fair value of £37 million (30 September 2020: £22 million), net of an expected credit loss provision of £16 million (30 September 2020: £36 million).

NETTING ARRANGEMENTS OF FINANCIAL INSTRUMENTS

The following tables set out the Group's financial assets and financial liabilities that are subject to netting and set-off arrangements. Financial assets and liabilities that are subject to set-off arrangements and disclosed on a net basis in the Group's Balance Sheet primarily relate to collateral in respect of one derivative financial instrument under an ISDA Credit Support Annex.

					2021
£ million	**Gross financial assets/ liabilities**	**Gross collateral assets/ liabilities set-off**	**Net financial assets/ liabilities per balance sheet**	**Related amounts not set-off in the balance sheet**	**Net**
Assets					
Derivative financial instruments	**496**	**(37)**	**459**	**(435)**	**24**
Liabilities					
Derivative financial instruments	**(1,083)**	**37**	**(1,046)**	**435**	**(611)**

					2020
£ million	Gross financial assets/ liabilities	Gross collateral assets/ liabilities set-off	Net financial assets/ liabilities per balance sheet	Related amounts not set-off in the balance sheet	Net
Assets					
Derivative financial instruments	913	(47)	866	(858)	8
Liabilities					
Derivative financial instruments	(1,729)	47	(1,682)	858	(824)

The table below sets out the Group's accounting classification of each class of financial assets and liabilities:

						2021
£ million	**Fair value through income statement**	**Fair value through other comprehensive income**	**Assets and liabilities at amortised cost**	**Total**	**Current**	**Non-Current**
Trade and other receivables	**37**	**–**	**2,611**	**2,648**	**2,590**	**58**
Cash and cash equivalents	**–**	**–**	**1,287**	**1,287**	**1,287**	**–**
Derivatives	**459**	**–**	**–**	**459**	**68**	**391**
Total financial assets	**496**	**–**	**3,898**	**4,394**	**3,945**	**449**
Borrowings	**–**	**–**	**(9,822)**	**(9,822)**	**(1,107)**	**(8,715)**
Trade and other payables	**–**	**–**	**(8,373)**	**(8,373)**	**(8,373)**	**–**
Derivatives	**(832)**	**(214)**	**–**	**(1,046)**	**(62)**	**(984)**
Lease liabilities	**–**	**–**	**(251)**	**(251)**	**(57)**	**(194)**
Total financial liabilities	**(832)**	**(214)**	**(18,446)**	**(19,492)**	**(9,599)**	**(9,893)**
Total net financial (liabilities)	**(336)**	**(214)**	**(14,548)**	**(15,098)**	**(5,654)**	**(9,444)**

						2020
£ million	Fair value through income statement	Fair value through other comprehensive income	Assets and liabilities at amortised cost	Total	Current	Non-Current
Trade and other receivables	22	–	2,502	2,524	2,476	48
Cash and cash equivalents	–	–	1,626	1,626	1,626	–
Derivatives	866	–	–	866	53	813
Total financial assets	888	–	4,128	5,016	4,155	861
Borrowings	–	–	(11,652)	(11,652)	(1,442)	(10,210)
Trade and other payables	–	–	(9,387)	(9,387)	(9,387)	–
Derivatives	(1,272)	(410)	–	(1,682)	(41)	(1,641)
Lease liabilities	–	–	(299)	(299)	(64)	(235)
Total financial liabilities	(1,272)	(410)	(21,338)	(23,020)	(10,934)	(12,086)
Total net financial (liabilities)	(384)	(410)	(17,210)	(18,004)	(6,779)	(11,225)

Derivatives classified as fair value through other comprehensive income relate to cross currency swaps designated as hedges of foreign currency denominated net investments. The Group only designates the undiscounted foreign exchange spot element of the cross currency swaps and the changes in fair value related to this element are posted

to other comprehensive income. Changes in the fair value of the cross currency swaps attributable to changes in interest rates and the effect of discounting are recognised in the income statement. The Group also designates certain bonds as hedges of foreign currency denominated net investments and the foreign exchange revaluation of those bonds is recognised in other comprehensive income. The carrying value at 30 September 2021 of those bonds included in the above table is £5,286 million (2020: £6,755 million). All of the Group's net investment hedges remain effective.

22. DERIVATIVE FINANCIAL INSTRUMENTS

The Group's derivative financial instruments held at fair value, are as follows:

	2021			2020		
£ million	**Assets**	**Liabilities**	**Net Fair Value**	Assets	Liabilities	Net Fair Value
Current derivative financial instruments						
Interest rate swaps	**60**	**(33)**	**27**	41	(31)	10
Foreign exchange contracts	**4**	**(4)**	**–**	9	(10)	(1)
Cross-currency swaps	**4**	**(25)**	**(21)**	3	–	3
Total current derivatives	**68**	**(62)**	**6**	53	(41)	12
Collateral[1]	**–**	**–**	**–**	–	–	–
	68	**(62)**	**6**	53	(41)	12
Non-current derivative financial instruments						
Interest rate swaps	**391**	**(780)**	**(389)**	813	(1,204)	(391)
Cross-currency swaps	**–**	**(241)**	**(241)**	–	(484)	(484)
Total non-current derivatives	**391**	**(1,021)**	**(630)**	813	(1,688)	(875)
Collateral[1]	**–**	**37**	**37**	–	47	47
	391	**(984)**	**(593)**	813	(1,641)	(828)
Total carrying value of derivative financial instruments	**459**	**(1,046)**	**(587)**	866	(1,682)	(816)
Analysed as:						
Interest rate swaps	**451**	**(813)**	**(362)**	854	(1,235)	(381)
Foreign exchange contracts	**4**	**(4)**	**–**	9	(10)	(1)
Cross-currency swaps	**4**	**(266)**	**(262)**	3	(484)	(481)
Collateral[1]	**–**	**37**	**37**	–	47	47
Total carrying value of derivative financial instruments	**459**	**(1,046)**	**(587)**	866	(1,682)	(816)

2. Collateral deposited against derivative financial liabilities under the terms and conditions of collateral appendices.

Fair values are determined based on observable market data such as yield curves, foreign exchange rates and credit default swap prices to calculate the present value of future cash flows associated with each derivative at the balance sheet date. Market data is sourced from a well known financial data company and valuations are validated by reference to counterparty valuations where appropriate. Some of the Group's derivative financial instruments contain early termination options and these have been considered when assessing the element of the fair value related to credit risk. On this basis the reduction in reported net derivative liabilities due to credit risk is £19 million (2020: £27 million) and would have been a £49 million (2020: £75 million) reduction without considering the early termination options. The classification of these derivative assets and liabilities under the IFRS 7 fair value hierarchy is provided in note 21.

MATURITY OF OBLIGATIONS UNDER DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments have been classified in the balance sheet as current or non-current on an undiscounted contractual basis based on spot rates as at the balance sheet date. For the purposes of the above and following analysis, maturity dates have been based on the likelihood of any early termination options being exercised with consideration to counterparty expectations and market conditions prevailing as at 30 September 2021. Any collateral transferred to counterparties in respect of derivative financial liabilities has been classified consistently with the related underlying derivative.

The table below summarises the Group's derivative financial instruments by maturity based on their remaining contractual cash flows as at 30 September 2021. The amounts disclosed are the undiscounted cash flows calculated using spot rates of exchange prevailing at the relevant balance sheet date. Contractual cash flows in respect of the Group's non derivative financial instruments are detailed in note 21.

£ million	Balance sheet amount	Contractual cash flows total	<1 year	Between 1 and 2 years	Between 2 and 5 years	>5 years
						2021
Net settled derivatives	(325)	(480)	16	(1)	(157)	(338)
Gross settled derivatives	(262)	-	-	-	-	-
– receipts	-	5,667	2,516	66	2,522	563
– payments	-	(5,818)	(2,521)	(48)	(2,661)	(588)
	(587)	(631)	11	17	(296)	(363)

£ million	Balance sheet amount	Contractual cash flows total	<1 year	Between 1 and 2 years	Between 2 and 5 years	>5 years
						2020
Net settled derivatives	(335)	(479)	62	19	(104)	(456)
Gross settled derivatives	(481)	-	-	-	-	-
– receipts	-	6,530	2,240	1,084	1,528	1,678
– payments	-	(6,858)	(2,221)	(1,153)	(1,633)	(1,851)
	(816)	(807)	81	(50)	(209)	(629)

DERIVATIVES AS HEDGING INSTRUMENTS

As outlined in note 21, the Group hedges its underlying interest rate exposure and foreign currency translation exposures in an efficient, commercial and structured manner, primarily using interest rate swaps and cross currency swaps. Foreign exchange contracts are used to manage the Group's short term liquidity requirements in line with short term cash flow forecasts as appropriate.

The Group does not apply cash flow or fair value hedge accounting, as permitted under IFRS9, which results in fair value gains and losses attributable to derivative financial instruments being recognised in net finance costs unless they are designated as hedges of a net investment in foreign operations, in which case they are recognised in other comprehensive income.

The group has considered the impending requirements to re-base LIBOR based interest rates to new risk-free based rates. The group is currently undertaking an exercise to re-base to risk-free rates all its affected interest rate derivative contracts that mature after the end of September 2021. GBP LIBOR contracts will be rebased to SONIA in the last quarter of the 2021 calendar year with USD LIBOR contracts to be rebased later in the 2022 fiscal year. At present, it is not anticipated that these changes will impact the Group's commercial hedging strategy, nor should they have a material financial impact.

INTEREST RATE SWAPS

To manage interest rate risk on its borrowings, the Group issues debt in the market or markets that are most appropriate at the time of raising new finance with regard to currency, interest denomination or duration, and then uses interest rate swaps to re-base the debt into the appropriate proportions of fixed and floating interest rates. Interest rate swaps are also transacted to manage and re-profile the Group's interest rate risk over the short, medium and long term in accordance with the Treasury Committee framework and Treasury Committee discussions. Fair value movements are recognised in net finance costs in the relevant reporting period.

As at 30 September 2021, the notional amount of interest rate swaps outstanding that were entered into to convert fixed rate borrowings into floating rates of interest at the time of raising new finance were £10,775 million equivalent (2020: £11,656 million equivalent) with a fair value of £425 million asset (2020: £854 million asset). The fixed interest rates vary from 1.1 per cent to 8.7 per cent (2020: 0.5 per cent to 8.7 per cent), and the floating rates are EURIBOR, GBP LIBOR and USD LIBOR.

As at 30 September 2021, the notional amount of interest rate swaps outstanding that were entered into to convert the Group's debt into the appropriate proportion of fixed and floating rates to manage and re-profile the Group's interest rate risk were £8,806 million equivalent (2020: £10,311 million equivalent) with a fair value of £750 million liability (2020: £1,189 million liability). The fixed interest rates vary from 0.5 per cent to 4.4 per cent (2020: 0.5 per cent to 4.4 per cent), and the floating rates are EURIBOR, GBP LIBOR and USD LIBOR. This includes forward starting interest rate swaps with a total notional amount of £1,531 million equivalent (2020: £2,519 million equivalent) with tenors between 3.5 and 6 years, starting between May 2022 and October 2024.

All of the Group's GBP and USD interest rate swaps will be impacted by the changes to the use of LIBOR interest rates. However, the impact of the changes is not expected to be material.

CROSS-CURRENCY SWAPS

The Group enters into cross currency swaps to convert the currency of debt into the appropriate currency with consideration to the underlying assets of the Group as appropriate. Fair value movements are recognised in net finance costs in the relevant reporting period unless the swaps are designated as hedges of a net investment in foreign operations, in which case the fair value movement attributable to changes in foreign exchange rates are recognised in other comprehensive income.

As at 30 September 2021, the notional amount of cross currency swaps entered into to convert floating rate sterling debt into the desired currency at floating rates of interest was £2,600 million (2020: £2,600 million) and the fair value of these swaps was £214 million net liability (2020: £409 million net liability); the notional amount of cross currency swaps entered into to convert floating rate US dollar debt into the desired currency at floating rates of interest was $1,750 million (2020: $1,750 million) and the fair value of these swaps was £48 million net liability (2020: £71 million net liability).

HEDGES OF NET INVESTMENTS IN FOREIGN OPERATIONS

As at 30 September 2021, cross currency swaps with a notional amount of €3,233 million (2020: €3,233 million) were designated as hedges of net investments in foreign operations. During the year, foreign exchange translation gains amounting to £168 million (2020: £87 million losses) were recognised within exchange movements in other comprehensive income in respect of cross currency swaps that had been designated as hedges of a net investment in foreign operations. No hedging ineffectiveness occurred during the year (2020: £nil).

The movements in Other Comprehensive Income due to net investment hedging in the period were as follows:

£ million	**2021**	2020
Foreign exchange gains/(losses) on borrowings	**308**	(75)
Foreign exchange gains on derivative financial instruments	**168**	87
Reclassification to the Income Statement	**117**	–
	593	12

All of the Group's cross currency swaps will be impacted by the changes to the use of LIBOR interest rates. However, this will not impact the effectiveness of the contracts in their net investment hedge relationship and the calculation of the amounts recognised in other comprehensive income will be unaffected.

FOREIGN EXCHANGE CONTRACTS

The Group enters into foreign exchange contracts to manage short term liquidity requirements in line with cash flow forecasts. As at 30 September 2021, the notional amount of these contracts was £1,430 million equivalent (2020: £2,126 million equivalent) and the fair value of these contracts was a net liability of £0.6 million (2020: £0.7 million net liability).

23. DEFERRED TAX ASSETS AND LIABILITIES

DEFERRED TAX ASSETS

£ million	**Consolidated income statement 2021**	Consolidated income statement 2020	**Consolidated balance sheet 2021**	Consolidated balance sheet 2020
Accelerated depreciation and amortisation	**(7)**	34	**(864)**	(871)
Retirement benefits	**(38)**	(17)	**(23)**	88
Other temporary differences	**201**	(32)	**414**	240
Deferred tax expense	**156**	(15)		
Net deferred tax liabilities			**(473)**	(543)

REFLECTED IN THE CONSOLIDATED BALANCE SHEET AS FOLLOWS

£ million	**2021**	2020
Deferred tax assets	**564**	381
Deferred tax liabilities	**(1,037)**	(924)
	(473)	(543)

RECONCILIATION OF NET DEFERRED TAX LIABILITIES

£ million	2021	2020
As at 1 October	**(543)**	(561)
Charged to the income statement	**156**	(15)
(Charged)/credited to other comprehensive income	**(33)**	27
Transferred to held for disposal	**–**	1
Exchange movements	**(55)**	10
Other movements	**2**	(5)
As at 30 September	**(473)**	(543)

Included within net deferred tax liabilities are deferred tax assets recognised of £267million (2020: £42 million) for tax credits arising in the Group's Spanish business. The majority (£239 million) of these tax credits were recognised in the current year following an internal reorganisation of the Spanish business. These tax credits have no time expiry. Utilisation of these tax credits is restricted to 50% of the Spanish business' taxable profits arising in any given year; those tax law restrictions extend the period over which the deferred tax assets would otherwise be recovered. The Group considers there to be forecast future taxable profits which support the recognition of these long term deferred tax assets. The period over which these deferred tax assets are utilised is sensitive to forecasting assumptions about future growth rates (which may be influenced by the future effects of climate change) and regulatory changes. Any material effects of climate change in the long term could extend the period over which the deferred tax asset will be recovered but as the tax credits do not expire, the Group considers there is positive evidence that sufficient future taxable profits would still be available. Based on a range of forecast scenarios modelling sensitivities these deferred tax assets are expected to be utilised over a period of 20-25 years. Deferred tax assets of £57 million (2020: £63 million) for tax credits have not been recognised due to the potential uncertainty of the utilisation of the credits. Of these unrecognised deferred tax assets £57 million (2020: £63 million) are expected to expire between 2022 and 2027.

Included within net deferred tax liabilities are deferred tax assets recognised for retirement benefits of £157 million (2020: £176 million) arising in the Group's German business. These deferred tax assets are expected to be recovered both by way of utilisation against the reversal of deferred tax liabilities of £33 million (2020: £7 million) arising in the Group's German business and by way of utilisation against future taxable profits. The Group considers there to be forecast future taxable profits which support the recognition of these long term deferred tax assets. These deferred tax assets are expected to be recovered over a period of 20-40 years corresponding to the life of the pension scheme.

Within Other temporary differences, deferred tax assets of £25 million (2020: £84 million) are recognised for tax losses carried forward to the extent that the realisation of the related tax benefit through future taxable profits is probable.

As at the balance sheet date, deferred tax assets of £130 million (2020: £152 million) for tax losses, and £13 million (2020: £17 million) for other temporary differences, have not been recognised due to the potential uncertainty of the utilisation of the tax losses and other temporary differences in certain jurisdictions. Of these unrecognised deferred tax assets for tax losses £1 million (2020: £30 million) are expected to expire within 1 year and £8 million (2020: £9 million) are expected to expire within 5 years and the remaining £121 million (2020: £113 million) has no time expiry. The deferred tax assets for other temporary differences of £13 million (2020: £17 million) have no time expiry.

We have reviewed the recoverability of deferred tax assets in overseas territories in the light of forecast business performance. In 2021 we recognised deferred tax assets of £8 million that were previously unrecognised (2020: derecognised deferred tax assets of £51 million that were previously recognised) on the basis that it is more likely than not that these are recoverable (2020: irrecoverable).

A deferred tax liability of £101 million (2020: £111 million) is recognised in respect of taxation expected to arise on the future distribution of unremitted earnings totalling £5 billion (2020: £7 billion).

The temporary differences associated with investments in the Group's subsidiaries, associates and joint ventures for which a deferred tax liability has not been recognised in the periods presented, aggregate to £29 million (2020: £16 million). No liability has been recognised because the Group is in a position to control the timing of the reversal of those temporary differences and it is probable that such differences will not reverse in the foreseeable future.

The UK government announced in its budget on 3 March 2021 that it would increase the main rate of corporation tax by 6% to 25% with effect from 1 April 2023. This change was substantively enacted on 24 May 2021 and, as a result, the effect has been reflected in the closing deferred tax position included in these financial statements.

24. RETIREMENT BENEFIT SCHEMES

The Group operates a number of retirement benefit schemes for its employees, including both defined benefit and defined contribution schemes. The Group's three principal schemes are defined benefit schemes and are operated by Imperial Tobacco Limited (ITL) in the UK, Reemtsma Cigarettenfabriken GmbH in Germany and ITG Brands in the USA; these schemes represent 64 per cent, 14 per cent and 8 per cent of the Group's total defined benefit obligations and 35 per cent, 33 per cent and 7 per cent of the current service cost respectively.

IMPERIAL TOBACCO PENSION FUND

The UK scheme, the Imperial Tobacco Pension Fund (or 'ITPF' or 'Fund'), is a voluntary final salary pension scheme with a normal retirement age of 60 for most members. The ITPF was offered to employees who joined the company before 1 October 2010 and has a weighted average maturity of 17 years. Effective from 1 September 2017, members' pensionable pay was capped at the higher of £75,000 or their pensionable pay at 1 September 2017. By number, the population as at the most recent funding valuation comprises 72 per cent in respect of pensioners and dependants, 26 per cent in respect of deferred members and 2 per cent in respect of current employees. New employees in the UK are now offered a defined contribution scheme. In certain circumstances, surplus funds in the defined benefit section, may be used to finance defined contribution section contributions on ITL's behalf with company contributions reduced accordingly.

The ITPF operates under trust law and is managed and administered by the Trustees on behalf of the members in accordance with the terms of the Trust Deed and Rules and relevant legislation. The ITPF's assets are held by the trust.

The main risk for the Group in respect of the ITPF is that additional contributions are required if the assets are not expected to be sufficient to pay for the benefits. The investment portfolio is subject to a range of risks typical of the asset classes held, such as credit risk on bonds, and exposure to the property market.

Annual increases in benefits in payment are dependent on inflation so the main uncertainties affecting the level of benefits payable under the ITPF are future inflation levels (including the impact of inflation on future salary increases below the pensionable pay cap) and the actual longevity of the membership.

The contributions paid to the ITPF are set by the ITPF Scheme Actuary every three years. The Scheme Actuary is an external consultant, appointed by the Trustees. Principal factors that the Scheme Actuary will have regard to include the covenant offered by the Group, the level of risk in the ITPF, the expected returns on the ITPF's assets, the results of the funding assessment on an ongoing basis and the expected cost of securing benefits if the Fund were to be wound up.

The latest valuation of the ITPF was carried out as at 31 March 2019 when the market value of the invested assets was £4,137 million. Based on the ongoing funding target the total assets were sufficient to cover 110 per cent of the benefits that had accrued to members for past service, after allowing for expected future pay increases. The total assets were sufficient to cover 106 per cent of the total benefits that had accrued to members for past service and future service benefits for current members. In compliance with the Pensions Act 2004, ITL and the Trustee agreed a scheme-specific funding target, a statement of funding principles and a schedule of contributions accordingly.

Following the valuation, a dynamic contribution schedule has been agreed such that ITL's annual contributions will reduce or increase depending on the Fund's valuation going forward. The level of the ITL's annual contribution to the Fund is £65 million per year for the year to 31 March 2022. Further contributions were agreed to be paid by ITL in the event of a downgrade of the Group's credit rating to non-investment grade by either Standard & Poor's or Moody's. In addition, surety guarantees that were provided with a total value of £600 million have been reduced to £225 million following the latest valuation and a parental guarantee from Imperial Brands PLC remains in place.

The IAS 19 liability measurement of the defined benefit obligation (DBO) and the current service cost are sensitive to the assumptions made about future inflation and salary growth levels, as well as the assumptions made about life expectancy. They are also sensitive to the discount rate, which depends on market yields on sterling denominated AA corporate bonds. The main differences between the funding and IAS 19 assumptions are a more prudent longevity assumption for funding and a different approach to setting the discount rate. A consequence of the ITPF's investment strategy, with a proportion of the assets invested in return-seeking assets, is that the difference between the market value of the assets and the IAS 19 liabilities may be relatively volatile.

The ITPF has a pension surplus on the IAS 19 measure, in line with IFRIC 14, recognition of the net asset on the fund is only appropriate where it can be recovered. The ITPF trust deed gives the Group an ability to receive a refund of surplus assets assuming the full settlement of plan liabilities in the event of a plan wind-up. Furthermore, in the ordinary course of business the Trustee has no rights to unilaterally wind up the Fund or otherwise augment the

benefits due to the Fund's members. Based on these circumstances, any net surplus in this scheme is recognised in full.

THE REEMTSMA CIGARETTENFABRIKEN PENSION PLAN

"The German scheme, the Reemtsma Cigarettenfabriken Pension Plan (RCPP), is primarily a career average pension plan, though a small group of members has final salary benefits. It has a weighted average maturity of 19 years. The scheme population comprises 51 per cent in respect of pensioners, 19 per cent in respect of deferred members and 30 per cent in respect of current employees. It was closed to new members from 1 January 2020, but existing active members at that date continue to accrue benefits in the plan.

The plan is unfunded and the company pays benefits as they arise. The plan's obligations arise under a works council agreement and are subject to standard German legal requirements around such matters as the benefits to be provided to employees who leave service, and pension increases in payment. Over the next year Reemtsma Cigarettenfabriken GmbH expects to pay £23 million in respect of benefits.

Annual increases in benefits in payment are dependent on inflation so the main uncertainties affecting the level of benefits payable under the plan are future inflation levels and the actual longevity of the membership.

The IAS 19 liability measurement of the DBO and the current service cost are sensitive to the assumptions made about the above variables, as well as the discount rate, which depends on market yields on euro denominated AA corporate bonds.

ITG SCHEME

The main USA pension scheme, held by ITG Brands is the ITG Scheme, is a defined benefit pension plan that is closed to new entrants. It has a weighted average maturity of 11 years. The population comprises 77 per cent in respect of pensioners, 10 per cent in respect of deferred members and 13 per cent in respect of current employees.

The plan is funded and benefits are paid from the plan assets. Contributions to the plan are determined based on US regulatory requirements and ITG Brands is not expected to make any contributions in the next year.

Annual benefits in payment are assumed not to increase from current levels. The main uncertainty affecting the level of benefits payable under the plan is the actual longevity of the membership. Other key uncertainties impacting the plan include investment risk and potential past service benefit changes from future negotiations.

The IAS 19 liability measurement of the DBO and the service cost are sensitive to the assumptions made about the above variables, as well as the discount rate, which depends on market yields on US dollar denominated AA corporate bonds.

OTHER PLANS

Other plans of the Group include various pension plans, other post-employment and long-term employee benefit plans in several countries of operation. Many of the plans are funded, with assets backing the obligations held in separate legal vehicles such as trusts, others are operated on an unfunded basis. The benefits provided, the approach to funding and the legal basis of the plans reflect their local territories. IAS 19 requires that the discount rate for calculating the DBO and service cost is set according to the level of relevant market yields on corporate bonds where the market is considered ""deep"", or government bonds where it is not.

For the year ended 30 September 2021 the group included four new schemes associated with operations in the Dominican Republic, Poland and Australia in the IAS19 position following a review of the pension schemes in the group.

The results of the most recent available actuarial valuations for the various plans have been updated to 30 September 2021 in order to determine the amounts to be included in the Group's consolidated financial statements. The aggregate IAS 19 position is as follows:

DEFINED BENEFIT PLANS

£ million	2021 DBO	2021 Assets	2021 Total	2020 DBO	2020 Assets	2020 Total
At 1 October	**(5,498)**	**5,182**	**(316)**	(5,877)	5,223	(654)
Consolidated income statement expense						
Current service cost	**(47)**	**–**	**(47)**	(49)	–	(49)
Settlements gains/(losses)	**13**	**(13)**	**–**	–	–	–
Past service costs	**9**	**–**	**9**	–	–	–
Cost of termination benefits	**(18)**	**–**	**(18)**	(2)	–	(2)
Net interest (expense)/income on net defined benefit (liability)/asset	**(87)**	**89**	**2**	(104)	99	(5)
Administration costs paid from plan assets	**–**	**(5)**	**(5)**	–	(6)	(6)
Cost recognised in the income statement			**(59)**			(62)
Remeasurements						
Actuarial gain due to liability experience	**64**	**–**	**64**	36	–	36
Actuarial (loss)/gain due to financial assumption changes	**(114)**	**–**	**(114)**	22	–	22
Actuarial gain/(loss) due to demographic assumption changes	**4**	**–**	**4**	228	–	228
Return on plan assets excluding amounts included in net interest income/(expense) above	**–**	**87**	**87**	–	(9)	(9)
Remeasurement effects recognised in other comprehensive income			**41**			277
Cash						
Employer contributions	**–**	**126**	**126**	–	145	145
Employee contributions	**(1)**	**1**	**–**	(1)	1	–
Benefits paid directly by the company	**264**	**(264)**	**–**	266	(266)	–
Net cash			**126**			145
Schemes brought into scope of IAS19	**(13)**	**–**	**(13)**	–	–	–
Exchange movements	**105**	**(37)**	**68**	(17)	(5)	(22)
Total other			**55**			(22)
At 30 September	**(5,319)**	**5,166**	**(153)**	(5,498)	5,182	(316)

The cost of termination benefits in the year ended 30 September 2021 and 30 September 2020 mainly relate to restructuring activity in Germany.

RETIREMENT BENEFIT SCHEME COSTS CHARGED TO OPERATING PROFIT

£ million	2021	2020
Defined benefit expense in operating profit	**61**	57
Defined contribution expense in operating profit	**19**	17
Total retirement benefit scheme cost in operating profit	**80**	74

Split as follows in the consolidated income statement:

£ million	2021	2020
Cost of sales	**26**	24
Distribution, advertising and selling costs	**33**	31
Administrative and other expenses	**21**	19
Total retirement benefit scheme costs in operating profit	**80**	74

ASSETS AND LIABILITIES RECOGNISED IN THE CONSOLIDATED BALANCE SHEET

£ million	2021	2020
Retirement benefit assets	**1,046**	940
Retirement benefit liabilities	**(1,199)**	(1,256)
Net retirement benefit liability	**(153)**	(316)

KEY FIGURES AND ASSUMPTIONS USED FOR MAJOR PLANS

			2021			2020
£ million unless otherwise indicated	**ITPF**	**RCPP**	**ITGBH**	ITPF	RCPP	ITGBH
Defined benefit obligation (DBO)	**3,404**	**765**	**403**	3,516	764	434
Fair value of scheme assets	**(4,386)**	**–**	**(396)**	(4,395)	–	(398)
Net defined benefit (asset)/liability	**(982)**	**765**	**7**	(879)	764	36
Current service cost	**17**	**15**	**3**	18	16	4
Employer contributions	**65**	**–**	**–**	85	–	–
Principal actuarial assumptions used (% per annum)						
Discount rate	**2.1**	**1.1**	**2.7**	1.7	0.9	2.8
Future salary increases	**3.4**	**3.1**	**n/a**	2.9	2.4	n/a
Future pension increases	**3.4**	**2.0**	**n/a**	2.9	1.3	n/a
Inflation	**3.4**	**2.0**	**2.3**	2.9	1.3	2.5

						2021
	ITPF		**RCPP**		**ITGBH**	
	Male	**Female**	**Male**	**Female**	**Male**	**Female**
Life expectancy at age 65 years:						
Member currently aged 65	**21.1**	**22.7**	**20.5**	**23.9**	**19.7**	**21.7**
Member currently aged 50	**22.1**	**23.9**	**22.6**	**25.6**	**20.9**	**22.9**

						2020
	ITPF		RCPP		ITGBH	
	Male	Female	Male	Female	Male	Female
Life expectancy at age 65 years:						
Member currently aged 65	21.1	22.7	20.3	23.8	19.7	21.7
Member currently aged 50	22.0	23.8	22.4	25.5	20.9	22.9

Assumptions regarding future mortality experience are set based on advice that uses published statistics and experience in each territory. In particular for the ITPF, SAPS S3 (2020: SAPS S3) tables are used with various adjustments for different groups of members, reflecting observed experience. The largest group of members uses the SAPS S3 All Pensioner Male Amounts table with a 101 per cent multiplier. An allowance for improvements in longevity is made using the 2018 (2021: 2018) CMI improvement rates with a long-term trend of 1.25 per cent per annum.

SENSITIVITY ANALYSIS FOR KEY ASSUMPTIONS AT THE END OF THE YEAR

Sensitivity analysis is illustrative only and is provided to demonstrate the degree of sensitivity of results to key assumptions. Generally, estimates are made by re-performing calculations with one assumption modified and all others held constant.

			2021			2020
% increase in DBO	**ITPF**	**RCPP**	**ITGBH**	ITPF	RCPP	ITGBH
Discount rate: 0.5% decrease	**8.6**	**10.8**	**5.8**	8.7	10.3	6.0
Rate of inflation: 0.5% decrease	**6.9**	**7.0**	**n/a**	7.0	6.7	n/a
One year increase in longevity for a member currently age 65, corresponding changes at other ages	**5.1**	**5.1**	**5.1**	4.9	4.8	5.0

The sensitivity to the inflation assumption change includes corresponding changes to the future salary increases and future pension increases assumptions, but is assumed to be independent of any change to discount rate.

We estimate that a 0.5 per cent decrease in the discount rate at the start of the year would have increased the consolidated income statement pension expense by approximately £14 million.

An approximate split of the major categories of ITPF scheme assets is as follows:

£ million unless otherwise indicated	2021 Fair value	2021 Percentage of ITPF scheme assets	2020 Fair value	2020 Percentage of ITPF scheme assets
Equities	**–**	**–**	1	–
Bonds – index linked government	**2,115**	**48**	2,344	53
Bonds – corporate and other	**815**	**19**	693	16
Property	**592**	**14**	533	12
Absolute return	**849**	**19**	809	18
Other – including derivatives, commodities and cash	**15**	**–**	15	1
	4,386	**100**	4,395	100

The primary investment objective is to invest the ITPF's assets in an appropriate and secure manner such that members' benefit entitlements can be paid as they fall due. Specifically the ITPF targets an expected return in excess of the growth in the liabilities, which in conjunction with the contributions paid is consistent to achieve and maintain an ongoing funding level of at least 100 per cent on a buy-out basis by 2028.

The majority of the assets are quoted. The ITPF holds £nil of self-invested assets (2020: £nil). As in previous years, the value of ground leases have been allocated to the property asset class.

An approximate split of the major categories of ITGBH scheme assets is as follows:

£ million unless otherwise indicated	2021 Fair value	2021 Percentage of ITGBH scheme assets	2020 Fair value	2020 Percentage of ITGBH scheme assets
Investment funds	**279**	**70**	224	56
Bonds – fixed government	**20**	**5**	45	11
Bonds – corporate and other	**63**	**16**	121	31
Other – including derivatives, commodities and cash	**34**	**9**	8	2
	396	**100**	398	100

The majority of the assets are non-quoted.

25. PROVISIONS

£ million	Restructuring	Other	2021 Total
At 1 October 2020	**253**	**163**	**416**
Additional provisions charged to the consolidated income statement	**141**	**50**	**191**
Amounts used	**(63)**	**(39)**	**(102)**
Unused amounts reversed	**(66)**	**(24)**	**(90)**
Exchange movements	**(14)**	**(7)**	**(21)**
At 30 September 2021	**251**	**143**	**394**

Analysed as:

£ million	2021	2020
Current	**188**	220
Non-current	**206**	196
	394	416

Restructuring provisions relate mainly to our 2021 Strategic Review Programme and Cost optimisation programmes (see note 5).

The restructuring provision is split between 2021 Strategic Review Programme of £86 million, Cost Optimisation Programmes of £155 million and other programmes of £10 million.

Within the Cost optimisation programme provisions there is £73 million related to costs of consolidating the manufacturing capacity within the Group. It is expected that the Cost optimisation programmes restructuring provisions will be predominantly utilised over the next 2 years.

Other provisions include £41 million relating to local employment requirements including holiday pay, £58 million relating to various local tax or duty requirements and £23 million of employment and duty provisions associated

with distribution. The provisions are spread throughout the Group and payment will be dependent on local statutory requirements.

26. SHARE CAPITAL

£ million	2021	2020
Authorised, issued and fully paid		
1,020,697,238 ordinary shares of 10p each (2020: 1,020,697,238)	**103**	103

During the year nil shares (2020: 5,098,508 shares) were repurchased and immediately cancelled, increasing the Capital Redemption reserve.

On 6 March 2014, 31,942,881 shares held in Treasury were cancelled creating the Capital Redemption reserve, and between September 2017 and December 2017, 4,973,916 shares were cancelled increasing this reserve.

27. SHARE SCHEMES

The Group operates four types of share-based incentive programmes, designed to incentivise staff and to encourage them to build a stake in the Group.

SHARE MATCHING SCHEME

Awards are made to eligible employees who are invited to invest a proportion of their eligible bonus in shares for a period of three years, after which matching shares are awarded on a 1:1 ratio, plus dividend equivalents.

LONG TERM INCENTIVE PLAN (LTIP)

Awards of shares under the LTIP are made to the Executive Directors and senior executives at the discretion of the Remuneration Committee. They vest three years after grant and are subject to performance criteria. Dividend equivalents accrue on vested shares.

SHARESAVE PLAN

Options are granted to eligible employees who participate in a designated savings scheme for a three year period. Historically they were also granted for a five year period.

DISCRETIONARY SHARE AWARDS PLAN (DSAP)

Under the DSAP, one-off conditional awards are made to individuals to recognise exceptional contributions within the business. Awards, which are not subject to performance conditions and under which vested shares do not attract dividend roll-up, will normally vest on the third anniversary of the date of grant subject to the participant's continued employment. The limit of an award under the DSAP is capped at 25 per cent of the participant's salary at the date of grant. Shares used to settle awards under the DSAP will be market purchased.

Further details of the schemes including additional criteria applying to Directors and some senior executives are set out in the Directors' Remuneration Report.

ANALYSIS OF CHARGE TO THE CONSOLIDATED INCOME STATEMENT

£ million	2021	2020
Share Matching Scheme	**3**	4
Long Term Incentive Plan	**20**	13
Sharesave Plan	**1**	2
Discretionary Share Awards Plan	**1**	1
	25	20

The awards are predominantly equity settled. The balance sheet liability in respect of cash settled schemes at 30 September 2021 was £1.8 million (2020 £1.2 million).

RECONCILIATION OF MOVEMENTS IN AWARDS/OPTIONS

					2021
Thousands of shares unless otherwise indicated	Share matching scheme awards	LTIP awards	Sharesave options	DSAP awards	Sharesave weighted average exercise price £
Outstanding at 1 October 2020	**461**	**6,595**	**2,006**	**70**	**15.31**
Granted	**253**	**3,763**	**371**	**17**	**13.09**
Lapsed/cancelled	**(25)**	**(2,003)**	**(323)**	**(3)**	**21.74**
Exercised	**(207)**	**(943)**	**(1)**	**(24)**	**5.45**
Outstanding at 30 September 2021	**482**	**7,412**	**2,053**	**60**	**13.89**
Exercisable at 30 September 2021	**–**	**–**	**170**	**–**	**22.24**

Thousands of shares unless otherwise indicated	Share matching scheme awards	LTIP awards	Sharesave options	DSAP awards	Sharesave weighted average exercise price £
					2020
Outstanding at 1 October 2019	783	4,313	1,559	94	21.21
Granted	297	3,187	1,386	2	12.39
Lapsed/cancelled	(19)	(782)	(939)	(5)	20.81
Exercised	(600)	(123)	–	(21)	25.01
Outstanding at 30 September 2020	461	6,595	2,006	70	15.31
Exercisable at 30 September 2020	–	–	147	–	29.62

The weighted average Imperial Brands PLC share price at the date of exercise of awards and options was £14.96 (2020: £19.34). The weighted average fair value of Sharesave options granted during the year was £2.35 (2020: £2.37).

SUMMARY OF AWARDS/OPTIONS OUTSTANDING AT 30 SEPTEMBER 2021

Thousands of shares unless otherwise indicated	Number of awards/ options outstanding	Vesting period remaining in months	Exercise price of options outstanding £
Share Matching Scheme			
2019	**114**	**5**	**n/a**
2020	**156**	**17**	**n/a**
2021	**212**	**29**	**n/a**
Total awards outstanding	**482**		
Long Term Incentive Plan			
2019	**1,512**	**5**	**n/a**
2020	**2,526**	**18**	**n/a**
2021	**3,374**	**30**	**n/a**
Total awards outstanding	**7,412**		
Sharesave Plan			
2018	**170**	**–**	**22.24**
2019	**231**	**11**	**17.45**
2020	**1,279**	**23**	**12.37**
2021	**373**	**35**	**13.09**
Total options outstanding	**2,053**		
Discretionary Share Awards Plan			
2018	**–**	**–**	**n/a**
2019	**42**	**5**	**n/a**
2020	**–**	**–**	**n/a**
2021	**18**	**29**	**n/a**
Total options outstanding	**60**		

The vesting period is the period between the grant of awards or options and the earliest date on which they are exercisable. The vesting period remaining and the exercise price of options outstanding are weighted averages. Participants in the Sharesave Plan have six months from the maturity date to exercise their option. Participants in the LTIP generally have seven years from the end of the vesting period to exercise their option. The exercise price of the options is fixed over the life of each option.

PRICING

For the purposes of valuing options to calculate the share-based payment charge, the Black-Scholes option pricing model has been used for the Share Matching Scheme, Sharesave Plan, Discretionary Shares Awards Plan and one Long Term Incentive Plan with no market conditions. A summary of the assumptions used in the Black-Scholes model for 2021 and 2020 is as follows:

		2021	
	Share matching	**Sharesave**	**DSAP**
Risk-free interest rate %	**0.7**	**0.2-(0.4)**	**0.7**
Volatility (based on 3 or 5 year history) %	**36.0**	**33.9-33.9**	**26.3**
Expected lives of options granted years	**3.00**	**3.00**	**3.00**
Dividend yield %	**8.85**	**8.86**	**6.7**
Fair value £	**12.37**	**2.31-2.56**	**12.86**
Share price used to determine exercise price £	**16.00**	**16**	**15.27**
Exercise price £	**n/a**	**13.09**	**n/a**

	2020	
	Share matching	Sharesave
Risk-free interest rate %	0.7	0.2-(0.4)
Volatility (based on 3 or 5 year history) %	29.0	33.8-33.9
Expected lives of options granted years	3.00	3.00
Dividend yield %	8.85	8.84
Fair value £	14.00	2.39-2.45
Share price used to determine exercise price £	18.25	15.20-15.26
Exercise price £	n/a	12.37

Market conditions were incorporated into the Monte Carlo method used in determining the fair value of LTIP awards at grant date. Assumptions in 2021 and 2020 are given in the following table:

%	**2021**	2020
Future Imperial Brands share price volatility	**31.2**	20.0
Future Imperial Brands dividend yield	**–**	–
Share price volatility of the tobacco and alcohol comparator group	**17.4-40.9**	14.7-28.3
Correlation between Imperial Tobacco and the alcohol and tobacco comparator group	**26.7**	22.1

EMPLOYEE SHARE OWNERSHIP TRUSTS

The Imperial Tobacco Group PLC Employee and Executive Benefit Trust and the Imperial Tobacco Group PLC 2001 Employee Benefit Trust (the Trusts) have been established to acquire ordinary shares in the Company to satisfy rights to shares arising on the exercise and vesting of options and awards. The purchase of shares by the Trusts has been financed by a gift of £19.2 million and an interest free loan of £147.5 million. In addition the Group has gifted treasury shares to the Trusts. None of the Trusts' shares has been allocated to employees or Executive Directors as at 30 September 2021. All finance costs and administration expenses connected with the Trusts are charged to the consolidated income statement as they accrue. The Trusts have waived their rights to dividends and the shares held by the Trusts are excluded from the calculation of basic earnings per share.

SHARES HELD BY EMPLOYEE SHARE OWNERSHIP TRUSTS

Millions of shares	**2021**	2020
At 1 October	**2.1**	2.8
Gift of shares from Treasury	**–**	–
Distribution of shares held by Employee Share Ownership Trusts	**(1.2)**	(0.7)
At 30 September	**0.9**	2.1

The shares in the Trusts are accounted for on a first in first out basis and comprise nil shares acquired in the open market (2020: nil) and 0.9 million (2020: 2.1 million) treasury shares gifted to the Trusts by the Group. There were nil (2020: nil) shares gifted in the financial year 2021.

28. TREASURY SHARES

Shares purchased under the Group's buyback programme represent a deduction from equity shareholders' funds, and are only cancelled if the number of treasury shares approaches 10 percent of issued share capital. During the year the Group purchased nil shares at a cost of £nil million (2020: 5,098,508 shares at a cost of £92 million) which were immediately cancelled. Shares held in treasury do not qualify for dividends.

	2021		2020	
£ million unless otherwise indicated	**Millions of shares (number)**	**Value**	Millions of shares (number)	Value
At 1 October	**74.3**	**2,183**	74.3	2,183
Purchase of shares	**–**	**–**	5.1	92
Cancellation of shares	**–**	**–**	(5.1)	(92)
Gifted to Employee Share Ownership Trusts	**–**	**–**	–	–
At 30 September	**74.3**	**2,183**	74.3	2,183
Percentage of issued share capital	**7.3**	**n/a**	7.3	n/a

29. COMMITMENTS

CAPITAL COMMITMENTS

£ million	**2021**	2020
Contracted but not provided for:		
Property, plant and equipment and software	**86**	187

30. CONTINGENT LIABILITIES

Where contingent liabilities are disclosed and not quantified this is because it is not practicable to do so.

USA STATE SETTLEMENT AGREEMENTS

In November 1998, the major US cigarette manufacturers, including Reynolds and Philip Morris, entered into the Master Settlement Agreement (MSA) with 52 US states and territories and possessions. These cigarette manufacturers previously settled four other cases, brought by Mississippi, Florida, Texas and Minnesota, by separate agreements with each state (collectively with the MSA, the State Settlement Agreements). These State Settlement Agreements settled all health care cost recovery actions brought by, or on behalf of, the settling jurisdictions against the defendants (the major US cigarette manufacturers); released the defendants from various additional present and potential future claims; imposed future payment obligations based on market share in the US; and significantly restricted their ability to market and sell cigarettes.

ITG Brands (ITGB) and its affiliates were not defendants in the litigations that led to the State Settlement Agreements. However, the MSA contained a provision allowing manufacturers that were not defendants to become parties. Under that provision ITGB and certain affiliates (including its US affiliate Commonwealth Brands, Inc.) became parties to the MSA. They make substantial annual MSA payments based on market share in the US and other factors, and are subject to the MSA's restrictions on their ability to market and sell cigarettes.

On 12 June 2015, ITGB acquired four cigarette brands (Winston, Salem, Kool and Maverick, referred to as the Acquired Brands) from Reynolds and Lorillard Tobacco, in connection with Reynolds' parent's acquisition of the stock of Lorillard Tobacco's parent. Because the MSA requires a purchaser of a brand to assume settlement liability, the Asset Purchase Agreement (APA) between Reynolds and ITGB required ITGB to assume MSA settlement payments on the Acquired Brands. There is no similar mechanism permitting companies that were not defendants to join the settlements with the four states that are not parties to the MSA (Florida, Minnesota, Mississippi, and Texas, collectively called the Previously Settled States or PSS). For those settlements, the APA required ITGB to use reasonable best efforts, with the assistance and cooperation of Reynolds and Lorillard Tobacco, to reach agreement with the PSS to make settlement payments on the Acquired Brands on certain terms and conditions.

Effective 12 June 2015, the date of closing of the transaction, ITGB became a party to the Mississippi settlement as to the Acquired Brands. ITGB had not become a party to the settlements with Florida, Minnesota, or Texas by the date of closing. Two of those states, Minnesota, and Texas, have statutes imposing fees on distributors' sales of products manufactured by companies that are not parties to the settlements, and post-closing fees were paid on sales of ITGB and affiliates' products in those states under those statutes from and after 12 June 2015.

Claims have been made against ITGB in connection with the acquisition of the Acquired Brands:

FLORIDA

On 18 January 2017 Florida and Philip Morris filed motions with the Florida court with jurisdiction over the settlement claiming that Reynolds and/or ITGB must make payments on the Acquired Brands under the Florida settlement. Florida and Philip Morris alleged that ITGB was a "successor" or "assign" to Reynolds' settlement obligations. On 27 December 2017 the court ruled that Reynolds was liable for settlement payments on the Acquired Brands, but ITGB was not because it was not a "successor" or "assign" to Reynolds. On 29 July 2020 the intermediate Florida appellate court affirmed. Reynolds asked that court for reconsideration and for permission to appeal to the Florida Supreme Court. On 18 September 2020, the intermediate appellate court denied that motion. On 18 October 2020, Reynolds asked the Florida Supreme Court directly to permit it to appeal. On 18 December 2020, the Florida Supreme Court denied Reynolds' petition for a further appeal.

Florida sought settlement payments on the Acquired Brands of approximately $127 million plus interest, plus future annual payments based on market share of approximately $26 million. The Florida court's decision that Reynolds, not ITGB, must make these settlement payments to Florida is now final and unappealable and Reynold is making the payments. Reynolds has asked the Delaware court to order the Group to indemnify it for those obligations, in the proceeding described below .

MINNESOTA

On 23 March 2018 Minnesota filed a complaint and motion and Philip Morris filed a motion with the Minnesota state court with jurisdiction over the settlement claiming that Reynolds and/or ITGB must make payments on the Acquired Brands under the Minnesota settlement. Minnesota and Philip Morris alleged that ITGB was a "successor" or "assign" to Reynolds' settlement obligations. On 24 September 2019 the court ruled that Reynolds was liable for settlement payments on the Acquired Brands. The court held that whether ITGB was a "successor" or "assign" under the Minnesota settlement would be determined by whether ITGB had breached its duty under the APA with Reynolds to use reasonable best efforts to reach agreement with Minnesota to join that settlement. On 19 February 2020 the Minnesota court denied ITGB's motion seeking an immediate interlocutory appeal. The Minnesota court held a trial on whether ITG used its reasonable best efforts to reach agreement with Minnesota to join the settlement on 31 August and 1-2 and 9 September 2020. Post-trial briefing and proposed findings of fact and conclusions of law were submitted on 13 November 2020, but the case was resolved before any decision was entered.

The parties have resolved the litigation in Minnesota, with the Court ordering dismissal of the claims with prejudice on 17 March 2021. Minnesota sought settlement payments on the Acquired Brands of approximately $58 million plus interest from 12 June 2015 forward, plus future annual payments of approximately $13 million, and Philip Morris sought additional amounts related to a portion of the payment calculation affecting Philip Morris. In the settlement, ITG paid $28 million (£22 million) with respect to the claims from 12 June 2015 forward, and Reynolds paid $52 million. ITG will pay an estimated $13 million on 31 December 2021 and each year thereafter.

TEXAS

On 28 January 2019 Texas and Philip Morris filed motions with the Texas court with jurisdiction over the settlement claiming that Reynolds and/or ITGB must make payments with respect to the Acquired Brands under the Texas settlement. Texas and Philip Morris alleged that ITGB was a "successor" or "assign" to Reynolds' obligations under the settlement. On 25 February 2020 the court determined that Reynolds was liable for settlement payments on the Acquired Brands. The court held that ITGB was as "assign" under the settlement but was not directly liable for settlement payments as a successor or assign, and referred further questions regarding ITGB's liability to Reynolds or Texas to the Delaware litigation described below.

On 5 May 2020, the court entered a judgment. The judgment further held that Reynolds' settlement payments on the Acquired Brands would be reduced by an offset for statutory fees under TEX. HEALTH & SAFETY CODE § 161.601, et seq. paid by or for ITGB. The statutory fee had been collected from ITGB's distributors since June 2015 when ITGB acquired the Brands, with ITGB reimbursing distributors for most of the fees paid. Effective 1 April 2019, Texas increased the fee amount from the lower rate paid for brands sold by Subsequent Participating Manufacturers to the MSA to the higher rate paid on other brands. Texas further demanded payment of the fee at the higher rate for the period between June 2015 and April 2019 plus penalties and interest, in the total amount of $173 million.

Both Texas and ITGB asked the court to remove the portion of its judgment reducing Reynolds' settlement payments by the statutory payments. The court denied those motions on 14 August 2020. The court further held that the judgment regarding Reynolds was final and appealable, but that the holding regarding ITGB's liability was not yet final until further actions from the Delaware and/or Texas courts. Reynolds appealed the judgment against it. ITGB and Texas both also appealed, noting disagreement with the offset for statutory fees. On 5 October 2020, Reynolds moved to dismiss ITGB's appeal (but not Texas') on the basis that the judgment is not final as to ITGB and does not injure it. ITGB opposed the motion on 15 October 2020. On 22 December 2020, the Court ordered the motion "carried with the case" to be decided along with the merits. Initial briefs on the merits were filed on 2 November 2020.

The Texas case was resolved in May 2021 and the state and Philip Morris' claims have been dismissed, while a separate claim brought by ITGB regarding the equity tax rate is awaiting dismissal. Texas sought settlement payments on the Acquired Brands from and after 12 June 2015 of approximately $167 million plus interest, plus future annual payments based on market share of approximately $36 million, and alternatively sought approximately $173 million (including penalties and interest) in statutory fees. In the settlement, ITG paid $13.5m in settlement payments (net of amounts accrued and statutory fees already paid) for 12 June 2015 and thereafter and Reynolds paid $190m, and ITG will pay about $3m in addition to amounts already accrued on 31 December 2021 and each year thereafter.

DELAWARE

ITGB and Reynolds are also engaged in litigation in the Delaware court with respect to whether ITGB has satisfied its obligations to use "reasonable best efforts" to join the settlements with Florida, Minnesota and Texas under the APA through which ITGB purchased the Acquired Brands and whether ITGB is required to indemnify Reynolds for amounts other courts may require Reynolds to pay. On 30 November 2017, on cross-motions by Reynolds and ITGB, the Delaware court held that the "reasonable best efforts" provision did not automatically terminate due to the transaction closing, but determined further that the duty of reasonable best efforts was not perpetual and that whether ITGB complied with that obligation is a question of fact that the court has not decided. On 23 September 2019, the Delaware court denied a motion by Reynolds to hold ITGB liable under other indemnity provisions of the APA for Reynolds' liability under the Florida decision irrespective of whether ITGB breached a duty of reasonable best efforts, finding a fact question on that argument, and granted Reynolds' motion that one of the conditions to reaching agreement on joinder related to equity taxes did not apply in Florida. On 31 October 2019, the trial court denied ITGB's motion for immediate appeal, with the Delaware Supreme Court denying the same motion on 7 November 2019. At present the parties are engaged in discovery. On 1 October 2021, Reynolds filed a motion to set a case schedule. On 15 October 2021, ITGB opposed the motion and proposed an alternative schedule. No schedule has yet been entered.

Reynolds originally sought indemnification for all amounts it might be required to pay in settlement for the Acquired Brands in the Florida, Minnesota, and Texas litigations, described above. The portions of the Delaware dispute that related to Minnesota and Texas have been settled and dismissed, however, so Reynolds' claim for indemnification in Delaware is now limited to the amounts it has been required to pay under the Florida determination described above, plus interest and attorney's fees. ITGB denies that indemnity is appropriate, and further contends that if Reynolds were to be granted indemnity, any amounts due to it should be substantially reduced by the amount by which Reynolds' settlement payments have been reduced through operation of the "profit adjustment" by reason of ITG not becoming a party to the Florida settlement.

MISSISSIPPI

Effective 12 June 2015, ITGB joined the Mississippi settlement with respect to the Acquired Brands. On 18 June 2015, the Mississippi court administering the settlement approved the joinder. On 2 July 2015, Philip Morris filed a motion to vacate the joinder, but the trial court denied that motion on 4 December 2015. Philip Morris appealed, but then dismissed its appeal under a settlement with Mississippi on 2 June 2017. On 26 December 2018, Philip Morris filed a new motion in Mississippi, challenging the basis on which Reynolds and ITGB had allocated the "base year" profit for the Acquired Brands between them on the basis that it adversely affects Philip Morris. The base year affects a calculation for a downward "profit adjustment" to payments under the Mississippi (and other) State Settlements. Philip Morris claims that adjustment of the base year should lower its payments under the profit adjustment and increase Reynolds' payments. A trial was set for 3-6 May 2021. ITGB is indemnified by Reynolds for profit adjustment payments to the extent that its annual profits do not exceed a specified amount. In June 2021, the parties resolved the Mississippi litigation with an agreement to set the base year amount at $860 million (plus inflation), and the Court dismissed Philip Morris' motion on 11 June 2021. ITG also received agreed-upon attorney's fees from Reynolds as part of the settlement.

MSA PREVIOUSLY SETTLED STATES REDUCTION

The MSA contains a downward adjustment, called the Previously Settled States Reduction, which reduces aggregate payments made by Philip Morris, Reynolds, and ITGB by a specified percentage each year. The State of California, later joined by the remainder of the MSA states and by Philip Morris, challenged the application of that Reduction to ITGB for every year from 2016 forward, claiming that it cannot apply to ITGB since it is not making settlement payments to Florida, Minnesota, or Texas under their settlements. The Independent Auditor to the MSA, which initially addresses disputes related to payments, has rejected that challenge every year. It is possible that one of the parties making the challenge may seek to arbitrate the claim under the MSA. The PSS Reduction provides annual MSA payment reductions of about $65 million.

The parties have resolved Philip Morris' related claim under the MSA, challenging ITG's right to receive a "Previously Settled States Reduction" worth about $65 million a year, as such claim relates to Minnesota and Texas.

OVERALL SUMMARY OF LIABILITY POSITION ASSOCIATED WITH USA STATE SETTLEMENT AGREEMENTS

The Group's legal advice is that it has a strong position on pending claims related to the Acquired Brands and the Group therefore considers that no provision is required for these matters.

PRODUCT LIABILITY INVESTIGATIONS

The Group is currently involved in a number of legal cases in which claimants are seeking damages for alleged smoking and health related effects. In the opinion of the Group's lawyers, the Group has meritorious defences to these actions, all of which are being vigorously contested. Although it is not possible to predict the outcome of the pending litigation, the Directors believe that the pending actions will not have a material adverse effect upon the results of the operations, cash flow or financial condition of the Group. This assessment of the probability of economic outflows at the year-end is a judgement which has been taken by management. Consequently, the Group has not provided for any amounts in respect of these cases in the financial statements. Details of these cases are given below.

ARGENTINA

Our subsidiary, Société Nationale d'Exploitation Industrielle des Tabacs et Allumettes SAS (SEITA), has been notified of a claim filed in the Court of Buenos Aires against Nobleza Piccardo, a subsidiary of British American Tobacco (BAT) by an individual smoker. SEITA is not a party to the court claim. BAT has denied liability. Historically, BAT manufactured and distributed two brands of cigarettes owned by SEITA in Argentina under the terms of a Licence Agreement. BAT has sought to invoke an indemnity contained in the Licence Agreement, pursuant to which SEITA is responsible for any product liability to third parties. The amount claimed is AR$8,980,200.

An adverse first instance judgment was received in December 2020. Both parties appealed the first instance judgment and the Court of Appeal decision is currently pending.

FRANCE

On 16 January 2018, the French National Committee against Tobacco (the CNCT) filed a criminal complaint against the four main tobacco manufacturers, including a French subsidiary of the Company named Imperial Brand Finance France (the Subsidiary), on grounds of 'reckless life endangerment'. Neither the Subsidiary nor any of its employees or managers have been charged or placed under formal investigation in any ongoing proceedings, as a result of such a complaint. The Group strongly denies the allegations made by the CNCT and is monitoring developments.

UNITED STATES

ITG Brands

A number of smoking and health-related claims have been brought against ITGB in the state courts of Massachusetts. ITGB has the benefit of an indemnity from another manufacturer in respect of each of these claims. As a result, ITGB either has been dismissed, or is expected to be dismissed, without prejudice from each of the claims. To date, no action has been successful or settled in favour of any individual claimant in any tobacco-related litigation against the Company or any of its subsidiaries.

Fontem US

Fontem US is named as a defendant in a case filed in the Superior Court of the State of California for the County of Los Angeles, Central District. The original and amended complaints in this case name 17 defendants, in addition to Fontem US. The claimants seek recovery of money damages, including punitive damages, against all defendants based on the claim that the principal claimant developed a lung condition as a result of her use of e-cigarette and other vaping devices, including those manufactured by Fontem US. The original complaint asserted claims against all defendants styled as eight causes of action as follows: (1) negligence; (2) strict liability—failure to warn; (3) strict liability—design defect; (4) fraudulent concealment; (5) intentional misrepresentation; (6) negligent misrepresentation; (7) breach of implied warranties; and (8) loss of consortium (asserted on behalf of the claimants spouse).

Fontem US has agreed to provide representation and indemnity to defendant Costco Wholesale Corporation ("Costco"), the retailer from which the claimant allegedly purchased blu products. Costco has also filed an answer to the second amended complaint. The Court set a trial date of 1 November 2021.

A mediation took place on 7 December, 2020 but did not resolve the matter. Since the mediation, Fontem US and other defendants continued to conduct fact discovery in anticipation of trial, while also continuing to negotiate with the claimants to resolve the matter prior to trial. In August, these continued negotiations resulted in an agreement by Fontem US and the claimants to settle this matter (which will include dismissal of the claims against Costco). The terms of the settlement agreement will be confidential. At a status conference before the Court on 15 October 2021 the claimants informed the Court that all remaining defendants have settled and later that day filed a conditional Notice of Settlement of Entire Case contingent upon the final execution of the pending settlement documents.

COMPETITION AUTHORITY INVESTIGATIONS

BELGIUM

On 29 May 2017, the National Competition Authority in Belgium (the BCA) conducted raids at the premises of several manufacturers and wholesalers of tobacco products. On 1 October 2021 the BCA announced that it had issued a Proposal for Decision which alleges the existence of anticompetitive practices in the tobacco industry that lasted for several years and consisted in repeated indirect exchanges of information on manufacturers' prices through wholesalers. The BCA states that such conduct may be contrary to Article IV.1 CEL and Article 101 TFEU. This case will now be examined by the Competition College, before which the parties will have the opportunity to defend themselves against these allegations. The parties will be able to submit written comments to the Competition College and will be heard at a hearing. The Competition College will either state that there exists an infringement of competition or make a finding of no infringement.

SPAIN

On 12 April 2019 the Spanish National Commission on Markets and Competition (CNMC) announced penalties against Philip Morris Spain, Altadis, JT International Iberia and Logista. Altadis and Logista received fines of €11.4 million and €20.9 million, respectively, from the CNMC. According to the decision, Altadis and Logista are alleged to have infringed competition law by participating in an exchange of sales volume data between 2008 and February 2017. CNMC considers that this conduct had the effect of restricting competition in the Spanish tobacco market. Both companies believe that the arguments made by CNMC that define this conduct as anti-competitive are flawed. In June 2019, both Altadis and Logista commenced appeals to the CNMC's Decision and the fines imposed in the Spanish High Court where they believe they will be successful, a decision supported by external legal counsel. In September 2019 Altadis and, separately, Logista arranged bank guarantees for the full amount of the fines with the result that payment of the fines had been suspended pending the outcome of the appeals. Therefore, provision for these amounts is not considered appropriate. In the Altadis appeal, both parties have concluded their submissions to the Court and a judgment is awaited. A judgment is unlikely to be received before the end of 2021.

In the Logista appeal, Logista submitted their pleadings before the High Spanish Court in February 2021. A judgment is also unlikely to be received before the end of 2021.

OTHER LITIGATION

US HELMS-BURTON LITIGATION

Imperial has been named as a defendant in a civil action in federal court in Miami, Florida under Title III of the Cuban Liberty and Democratic Solidarity Act of 1996 ("Helms-Burton") filed on 6 August 2020. Title III provides US nationals with a cause of action and a claim for treble damages against persons who have "trafficked" in property expropriated by the Cuban government. Title III is largely untested because it did not come into effect until May 2019. Treble damages are automatically available under Helms Burton. Although the filed claim is for unquantified damages, we understand the claim could potentially reach approximately $365 million, based on the claimants' claim to own 90% of the property, which they value at $135 million (and then treble). The claim is based on allegations that Imperial, through Corporación Habanos S.A. (a joint venture between one of Imperial's now former subsidiaries and the Cuban government), has "trafficked" in a factory in Havana, Cuba that the Cuban government confiscated from the claimants' ancestor in the early 1960s, by using the factory to manufacture, market, sell, and distribute Habanos cigars.

At the time the claim was filed against Imperial and up until the conclusion of the Brexit "transition period" on 31 December 2020, Imperial was subject to an EU law known as the EU Blocking Statute (Regulation (EC) No. 2271/96), which conflicts with Helms-Burton, protected Imperial against the impact of Title III, and impacted how Imperial might respond to the threatened litigation. On 23 September 2020 the US court granted Imperial's motion for a stay of the action until 9 February 2021 or until further order of the court, while Imperial awaited the European Commission's response to its request for authorisation to defend the action or, at a minimum, to file and litigate a motion to dismiss the action.

On 31 December 2020, the Brexit "transition period" concluded without action from the European Commission on Imperial's request for authorization. As of 1 January 2021, the EU Blocking Statute has been transposed into domestic law with only minimal changes. Accordingly, on 10 January 2021, Imperial submitted an application to the UK Department for International Trade for authorisation from the Secretary of State for International Trade to defend the action or, at a minimum, to file and litigate a motion to dismiss the action. On 8 February 2021, the UK Secretary of State for International Trade authorized Imperial to file and litigate a motion to dismiss the action.

On 26 February 2021, Imperial filed a motion to dismiss the action. In response, on 22 March 2021, the claimants amended their claim. On 28 April 2021, Imperial filed a motion to dismiss the amended action. Briefing on the motion to dismiss was completed on 20 July 2021. In August 2021, the parties filed supplemental briefs addressing the impact of a decision in another Helms-Burton case. A hearing on the motion to dismiss is scheduled for 15 December 2021.

Separately, two other groups of prospective claimants have indicated that they intend to file a lawsuit against Imperial in federal court in Miami, Florida. Neither claim has been filed. The threatened claims relate to other properties in Cuba, which the prospective claimants claim were confiscated from their ancestors by the Cuban government in the 1960s and which they claim are now used by Corporación Habanos S.A for commercial activities. The prospective claimants claim to be entitled to treble damages from Imperial.

No provision has been made for potential liabilities related to Helms-Burton claims.

UK

In June 2020, the Group responded to a claimant law firm's allegations of human rights issues in the Malawian tobacco supply chain, which included allegations relating to child and forced labour. In December 2020, a claim was filed in the UK High Court against Imperial Brands plc, Imperial Tobacco Limited and four of its subsidiaries (the Imperial Defendants) and two entities in the BAT group by a group of tobacco farm workers. The Imperial Defendents have acknowledged service and confirmed to the claimants that they intend to defend the claim in full. The Imperial Defendants have not yet been required to file their Defence. A procedural hearing has been scheduled for November/December 2021. The claim is unquantified, and given the early stage of the litigation a provision would not be appropriate.

MOROCCO

A number of cases have been raised against Société Marocaine des Tabacs SA (SMT) disputing a reduction to retirees' pensions. These cases have been in the courts for several years and SMT has successfully defended many of them in the lower courts. During the year 36 cases have been reviewed by the Cour de Cassation (Supreme Court) in Morocco, and it is understood that they have been decided against SMT and in favour of retirees.

The written reasoned judgment of the Cour de Cassation has not been received by SMT at the time of signing these accounts. Furthermore, the judgments in favour of the retirees reportedly relate to unquantified claims. Because of this it is not possible to assess the impact of the decided cases on the remaining cases within the Moroccan courts. SMT continues to rigorously defend its position.

The Company has reassessed its previously disclosed estimate of exposure to the potential liability following improved clarity of the legal position. Considering the number of cases currently filed by retirees, and allowing for the uncertainty in the calculation of the amount of any future payment, it now considers any outflow, if required, to be significantly lower than that previously disclosed.

31. NET DEBT

The movements in cash and cash equivalents, borrowings, and derivative financial instruments in the year were as follows:

£ million	Current borrowings	Lease liabilities	Non-current borrowings	Derivative financial instruments	Liabilities from financing activities	Cash and cash equivalents	Total
At 1 October 2020	(1,442)	(299)	(10,210)	(816)	(12,767)	1,626	(11,141)
Reallocation of current borrowings from non-current borrowings	(1,055)	–	1,055	–	–	–	–
Cash flow	1,294	69	72	(41)	1,394	(330)	1,064
Accretion of interest	13	(7)	1	1	8	–	8
Change in fair values	–	–	–	51	51	–	51
New leases, terminations & modifications	–	(26)	–	–	(26)	–	(26)
Exchange movements	83	12	367	218	680	(9)	671
At 30 September 2021	(1,107)	(251)	(8,715)	(587)	(10,660)	1,287	(9,373)

£ million	Current borrowings	Lease liabilities	Non-current borrowings	Derivative financial instruments	Liabilities from financing activities	Cash and cash equivalents	Total
At 1 October 2019	(1,937)	(326)	(11,697)	(622)	(14,582)	2,286	(12,296)
Reallocation of current borrowings from non-current borrowings	(1,340)	–	1,340	–	–	–	–
Cash flow	1,857	72	(1)	23	1,951	(611)	1,340
Accretion of interest	32	(7)	–	(28)	(3)	–	(3)
Change in fair values	–	–	–	80	80	–	80
New leases, terminations & modifications	–	(32)	–	–	(32)	–	(32)
Exchange movements	(54)	(6)	148	(269)	(181)	13	(168)
Transferred to held for disposal (note 11)	–	–	–	–	–	(62)	(62)
At 30 September 2020	(1,442)	(299)	(10,210)	(816)	(12,767)	1,626	(11,141)

ANALYSIS BY DENOMINATION CURRENCY

£ million	GBP	EUR	USD	Other	2021 Total
Cash and cash equivalents	**190**	**188**	**505**	**404**	**1,287**
Total borrowings	**(2,696)**	**(3,179)**	**(3,917)**	**(30)**	**(9,822)**
	(2,506)	**(2,991)**	**(3,412)**	**374**	**(8,535)**
Effect of cross currency swaps	**2,580**	**(4,147)**	**1,305**	**–**	**(262)**
	74	**(7,138)**	**(2,107)**	**374**	**(8,797)**
Lease liabilities	**(37)**	**(153)**	**(23)**	**(38)**	**(251)**
Derivative financial instruments					**(325)**
Net debt					**(9,373)**

Average reported net debt during the year was £11,148 million (2020: £13,564 million).

£ million	GBP	EUR	USD	Other	2020 Total
Cash and cash equivalents	412	556	407	251	1,626
Total borrowings	(2,694)	(3,852)	(5,083)	(23)	(11,652)
	(2,282)	(3,296)	(4,676)	228	(10,026)
Effect of cross currency swaps	2,666	(4,515)	1,368	–	(481)
	384	(7,811)	(3,308)	228	(10,507)
Lease liabilities	(39)	(190)	(27)	(43)	(299)
Derivative financial instruments					(335)
Net debt					(11,141)

ADJUSTED NET DEBT

Management monitors the Group's borrowing levels using adjusted net debt which excludes interest accruals, the fair value of derivative financial instruments providing commercial cash flow hedges and lease liabilities.

£ million	2021	2020
Reported net debt	**(9,373)**	(11,141)
Accrued interest	**140**	156
Lease liabilities	**251**	299
Fair value of interest rate derivatives	**367**	387
Adjusted net debt	**(8,615)**	(10,299)

Average adjusted net debt during the year was £10,361 million (2020: £12,765 million).

32. RECONCILIATION OF CASH FLOW TO MOVEMENT IN NET DEBT

£ million	2021	2020
Decrease in cash and cash equivalents	**(330)**	(611)
Cash flows relating to derivative financial instruments	**(41)**	23
Repayment of lease liabilities	**69**	72
Increase in borrowings	**(858)**	(1,240)
Repayment of borrowings	**2,224**	3,096
Change in net debt resulting from cash flows	**1,064**	1,340
Other non-cash movements including revaluation of derivative financial instruments	**59**	77
Transferred to held for disposal (note 11)	**–**	(62)
Lease liabilities	**(26)**	(358)
Exchange movements	**671**	(168)
Movement in net debt during the year	**1,768**	829
Opening net debt	**(11,141)**	(11,970)
Closing net debt	**(9,373)**	(11,141)

The increase in borrowings and repayment of borrowings reflect the cash flow movements relating to borrowings outstanding at the start and at the end of each financial year; cash flows relating to short term borrowings drawn down and repaid within the year are not included in this analysis.

33. NON-CONTROLLING INTERESTS

MATERIAL NON-CONTROLLING INTERESTS

Detailed below is the summarised financial information of Logista, being a subsidiary where the non-controlling interest of 49.99 per cent is considered material to the Group.

SUMMARISED BALANCE SHEET

at 30 September

Euro million	2021	2020
Current assets	**5,958**	6,106
Current liabilities	**(6,687)**	(6,909)
Current net assets	**(729)**	(803)
Non-current assets	**1,630**	1,740
Non-current liabilities	**(376)**	(421)
Non-current net assets	**1,254**	1,319
Net assets	**525**	516

SUMMARISED STATEMENT OF COMPREHENSIVE INCOME

for the year ended 30 September

Euro million	2021	2020
Revenue	**10,817**	10,559
Profit for the year	**174**	157
Other comprehensive income	**–**	1
Total comprehensive income	**174**	158

SUMMARISED CASH FLOW STATEMENT

for the year ended 30 September

Euro million	2021	2020
Cash flows from operating activities	**(302)**	830
Cash flows from investing activities	**505**	(640)
Cash flows from financing activities	**(194)**	(188)
Net increase in cash and cash equivalents	**9**	2

34. POST BALANCE SHEET EVENTS

Sale of the Premium Cigar Division

On 26 October 2021 deferred consideration of €88 million was received in relation to the sale of the Premium Cigar Division.