



IMPERIAL
BRANDS

Imperial Brands

Pre-close Trading Update

Thursday, 26th September 2019

Introduction

Alison Cooper

CEO, Imperial Brands

Current Year Revenue and Earnings

Revising expectations

Good morning everyone and thank you for joining at relatively short notice. I am joined this morning by Oliver Tant and Matthew Phillips. We have issued a statement this morning revising our current year revenue and earnings expectations. We are clearly very disappointed that we have needed to do this.

What has changed? In essence, there are two key factors that have impacted our expectations. Firstly, there is NGP, where our delivery is below expectations in the USA. We stepped up our investment in brand and retail contacts and consumer promotions in the second half, and our performance has been improving as a result. However, the highly competitive environment, and a marked slow-down in the growth of the US vapour category in recent weeks following US media reports and increased regulatory uncertainty, has impacted our performance. We now anticipate delivering around 50% growth in overall group NGP revenues. This is not what we wanted for the current year. However, going forward I believe that NGP provides the opportunity for us to deliver additive, profitable growth to complement our tobacco growth.

In tobacco, we are delivering good performances in Europe and the Americas. However, trading conditions have remained tough in our Africa, Asia and Australasia division. Our expectations for the second half have been particularly affected by a timing issue in Australia, where we have re-phased the current year benefit of duty-paid inventory gained. This has resulted in a negative impact on our numbers for 2019, but with the benefit now arising in 2020.

Overall our tobacco businesses continue to perform well, and will deliver modest revenue growth and improved profitability, notwithstanding the revised Australian phasing. Oliver will now provide a bit more detail around this morning's announcement before we open the call for your questions.

Financial Performance

Oliver Tant

CFO, Imperial Brands

Revised Expectations

Challenging trading

Thanks, Alison. From a tobacco perspective, we expect good financial performance across both our Europe and Americas divisions, with the latter also benefiting from US shipment timings. However, our triple-A division has been more challenging, with tougher trading in

Russia, the Middle East, and Australia. As Alison mentioned, the main factor which has driven the need to revise our expectations has been a change in our results phasing in Australia.

To provide a little background, the Australian market has experienced the rapid growth of a highly competitive value segment over recent months. The evolution of what is called the Fifth Price Tier has negatively impacted the industry pull profit this year, with lower margin brands now at around 20% of the overall market. Within this context, we increased our investment behind P&S, which we anticipated would be funded by benefits from duty-paid inventory around the annual excise increase in September.

We overestimated the level of benefit that we would realise in the current year, resulting in a rephasing of profit from FY19 into FY20. Our investment behind P&S has resulted in it achieving over a 6% share in its first year in Australia, which positions us well in a dynamic market going forward. At a group level, we still expect pricing to more than offset volume declines in tobacco, delivering modest revenue growth, albeit at a lower level than originally anticipated.

From an NGP perspective, we now expect revenues to grow by around 50% compared to the FY18 revenue of 187 million. This revised expectation has been driven mainly by the US market. Growing regulatory uncertainty, including individual US state actions, has prompted a marked slow-down in the growth of the vapour category in recent weeks, and an increasing number of wholesalers not ordering or not allowing promotion of vaping products.

Stepped up retail engagement programs

As highlighted in May, we stepped up our retail engagement programs during the second half, allied to more targeted brand investment at both a store level, and through a new media campaign. We also increased consumer promotions, given the substantial competitor discounting and consequently higher levels of consumer churn.

Although our actions have delivered improving consumer off-take for blu, sales have been lower than expected, reflecting the category slowdown and competitor discounting. This has impacted NGP revenues and profitability.

Markets outside the US

We have continued to deliver good year-on-year growth in NGP revenues in markets outside of the US, particularly in Japan where our zero-nicotine variant of *myblu* is now available nationally. We have made good progress with our heated tobacco brand, Pulse, following the city pilot which began in May.

In Europe, we have successfully launched new oral products in several markets, and consolidated strong share positions in vaping following the successful build out of *myblu* distribution in markets like Spain and Germany during the early part of the year.

Consumer offtake has continued to build. Second half NGP sales are expected to be at a broadly similar level to the first half. As mentioned in the statement, given the evolving environment, including factors such as Brexit, tariffs, and regulation, we are currently evaluation the effectiveness of our NGP supply-chain. This may result in contract termination costs which are not yet currently reflected in our revised expectations.

Other Gains

Just a few additional guidance areas I would like to mention before handing back to Alison. As I mentioned at the half-year, we were expecting other gains to be at the lower end of our guidance range of between £50 and £100 million. I now expect our results will benefit from around £30 million of other gains this year, £50 million lower than the £80 million of other gains recognised in FY15.

Translation FX

And Translation FX is expected to benefit earnings by around 2%, at current rates of exchange. Underlying cash conversion remains strong, and I expect the full year will be slightly below the 90% number, in line with previous guidance. Alison?

Improving Execution

Alison Cooper

CEO, Imperial Brands

A Challenging Year*Driving stronger delivery*

Thank you, Oliver. While there is no doubt this has turned out to be a challenging year, particularly given the evolving environment, it is also clear there are areas where our execution can be improved, and we are taking on board the learnings of 2019 to drive stronger delivery in 2020.

As we have highlighted, today's announcement is being driven by predominately two factors: profit phasing in Australia and NGP in the US. The impact in Australia is expected to reverse next year, benefiting our 2020 delivery, and overall tobacco is in good shape and delivering in-line with our strategy.

The NGP situation in the US is harder to call. We have improved our execution in the US, focused on sustainable growth. The environment is clearly volatile, and we will need to continue to monitor and adapt. What is needed, in our view, is a clear regulatory framework which supports high product standards and responsible sales and marketing behaviours. We need to be able to freely communicate the potential benefits of NGPs and address any misconceptions among consumers. We must find a way to differentiate between the responsible and irresponsible players in the industry. A faster PMTO process could provide the opportunity to achieve that.

As we move into 2020, we are better placed to deliver additive NGP growth, with a broader portfolio and stronger execution across our markets, all focused on building a sustainable and profitable business. Now I would like to open the call to questions.

Q&A

Gaurav Jain: Hi, thank you for taking my questions. I have a few. First of all, on NGP EBIT, you had earlier guided that exiting FY19 it would be breakeven, where are we right now and how much of the shortfall previously communicated that you expected NGP to exit FY19 and

how much of the shortfall that we have seen in EBIDTA is happening because NGP EBIDTA is running below prior expectations?

The second is that, is £50 million of this happening because of lower one-time gains, which Oliver mentioned that last year it was £80 million and this year it is going to be £30 million, when the earlier expectation was £50 million to £100 million? Then the third is should we just add the miss that is happening because of Australia to FY20 numbers, because that is the message I heard from Alison. Thank you.

Alison Cooper: Thank you. First of all, as you might imagine, given the additional investment we have put into the US and the associated slowdown in our top-line delivery. Well, associated, but the slowdown in our top-line delivery, we aren't reaching a break-even exit rate in 2019 as originally anticipated.

As we look into 2020, we are very much looking to reshape the investments behind NGP across the business, not only in the US. As we go through 2020, we are going to be moving much more towards a break-even position next year as we really look to drive the profitability in vaping as well as clearly the top-line opportunity and that is a very important focus for the business as we are, as we are moving into 2020.

On the one off's, we mentioned them just in terms of making sure the updated guidance was complete in terms of the update, but it is not the driver of the miss. The two recent events that we are communicating today are in relationship to the US NGP and Australia. It is important to note it and I think as Oliver just mentioned, we indicated at the half-year our expectation was at the lower end of that guidance anyway. However, it is not a main element in terms of the earnings miss.

Then Australia, yes, there will be the benefit in 2020 and the opportunity, there for an uptick potentially. However, I think we should take that into the overall shape of our 2020 guidance, which we'll come back to at the end of October. However, yes, there is some good uplift there.

Gaurav Jain: Okay, thank you.

Alison Cooper: Thank you.

Nico von Stackelberg: Hi. Can I please learn more about the error relating to the overestimated stock profit in Australia? Just looking granularity, what was the mistake that was made on your side? When did you learn about it? Thank you.

Oliver Tant: Well, it was a forecasting error that arose as a result of, I guess, an over-optimistic assessment of the level of pre-duty increase stock that we would sell-through by the end of the year. It was, in essence, an assumption that we would be able to sell more of it through before the 30th of September than we have been able to do. We still sit with that stock having been acquired before the excise duty increase and we can sell it at prices that incorporate excise duty in part. Therefore, actually we are sitting with, if you like, a pregnant gain sitting in our balance sheet, which we should be able to realise in a FY20.

Nico von Stackelberg: Okay, great. Secondly, on some of these adjustments that you are putting through, could you tell me what is the nature of some of these one-offs? What do they relate to in particular?

Oliver Tant: In terms of what is in the 30?

Nico von Stackelberg: Yes.

Oliver Tant: Well, we mark to market, we have a number of assets which are financial assets. Essentially under accounting practice we have a series of minority interests which are regarded essentially as financial assets and our requirement is to mark those to market, which is what we do. Those gains come from increases in the value of those assets. The largest component of this at the moment is Auxly.

Nico von Stackelberg: Okay. Thank you.

Alicia Forry: Hi. Good morning. I was wondering –

Speaker: Hi.

Alicia Forry: Yes, hello. Can you hear me?

Speaker: Yes, I can. Yes.

Alicia Forry: Okay, great. Sorry, the line has been a bit in and out. I was wondering about the run rate of NGP [inaudible] situation persists, which it seems likely to do for at least the near term. Is there a baseline number that you think your business can generate? That would be the first question. What factors, really [inaudible] in light of the health scares and FDA government, etc. That is one.

Alison Cooper: Okay, right.

Alicia Forry: Then two, can you remind us what percent of your US blu sales are in flavours, please?

Alison Cooper: Yes, certainly. The line was going in and out I am afraid with the first question, but I took it broadly as question around the US outlook from a vaping perspective. Is that fair?

Alicia Forry: Yes, that is correct.

Alison Cooper: Okay. All right, fine. Clearly, there are a number of factors here at the moment in terms of the environment, which, as you were mentioning, make this quite volatile in terms of predictions for the market at the moment. Just to look at the overall category and what's gone on. When we announced our half-year results, we were looking at roughly, early teens, 12, 13% growth in the closed system category, and that deteriorated to a mere 2% growth by the time we hit August. The current month is actually running negative. It is affecting clearly the category quite considerably.

I think until we see the regulatory impact starting to kick in in the US as the FDA starts moving, as the PMTA process, which has been accelerated, starts to kick in, I do think it may be a bit bumpy over the coming months. You have seen, I think, news-flow wise, I think I almost hear something every hour out of the US at the moment in terms of a state doing something or something happening with a retailer or wholesaler. It is a volatile environment currently. There may be some short-term pain, but I think as we move forward through into a regulated environment, as the FDA really kicks in in terms of the regulation of this space, we'll come out the other side in an environment that will be about responsible players. There will only be a few of us, I think, who will actually properly get through that FDA process and it

will actually, therefore, be a much better competitive environment from our perspective in the future. However, to be precise on numbers right here, right now, I think is quite difficult to do.

I am confident that we have addressed some of our execution issues in the US, particularly around the brand with the blu investment differentiating *myblu* from that original blu investment and awareness. We have done a lot around the ATL advertising, a lot of work as well as retail that we highlighted at the half-year, which has really moved us forward well. A lot of work too in terms of working on the environment with regulators. But, I think the key thing also is it is just really refocusing our spend, not just behind trial, which is why I don't like the promotion levels in the market and the dollar offers, but really around driving the stickiness and the loyalty of consumers as well in that market.

I think we know what we are doing in that market much better now with the things we have implemented in the second half. However, what we really now need to do is get the environment fixed and that is what we are working on. We have got some people speaking at the Global Tobacco and Nicotine Forum today, really outlining our thoughts around how that needs to work in the US and elsewhere.

Then your other question in terms of blu. We have two sorts of nicotine formulations in the US market. The main one, which is our initial portfolio, is very much focused on freebase. From a freebase perspective, non-flavoured is around three-quarters of our portfolio and actually, our biggest skew is actually our tobacco flavour, which is 45% of our portfolio. We also have some intense products on the market, which is the Nic salts products, that has a higher skew to flavours. Only 30% of that portfolio is non-flavoured. That gives you a feel for the split.

Alicia Forry:: Thanks.

Operator: Your next question comes from the line of [inaudible]. Please ask your question.

Speaker: Thanks. Thanks for the question, guys. Good morning.

Alison Cooper: Hi.

Speaker: Can I also ask two questions, please? Firstly, on NGP, I guess it is quite clear the US environment is challenging, but I also expected Europe to see a bit of a sequential improvement in NGP sales. Are you able to just give us the market dynamics in your key markets in Europe? Be it vaping or modern oral? That would be very helpful. How you are expecting – whether you are seeing sequential improvements in Europe as well? That is my first question.

Second, if you can comment, I would love to hear any further increments on your 2 billion disposals target. I know cigars you are progressing well within the statement. However, you probably still need other disposals assets in the next six months to hit your 2 billion target by May 2020. Some more detail on that would be very helpful. Thank you so much.

Alison Cooper: Yes, okay, I will come to the disposals question second. First of all, yes, on the EU, from our perspective, in terms of consumer offtake, we continue to see very good progress in consumer offtake from an EU perspective. In retail, we have effectively got number-one positions in Germany, Italy and Spain. We are joint number one in France. In the UK, we are still I think number three in the UK. So not so good in the UK, but the share

overall for blu is very good in terms of the category position in each of those markets. We are working on those, how that category develops, because the category growth has not been as rapid in recent months as we would like. There are different factors for that, which I will come back to, but we are very much looking at how the category evolves going forward. As I look at it, you have some markets in the EU, that have very big open systems, such as France and the UK, and in those markets I think it is very important that we continue to focus on the benefits of the closed systems and also work on product standards in those markets as well, which will help promote the closed systems over time.

In Germany, I think we have a very different situation. We very much created the category in the market, like Germany and Italy for that matter as well, and we still see opportunities in terms of the category growth, but again, we could do with some better product standards in the market, taking, if you like, the learnings of the US and some of the concerns about an unregulated market. We are going to take the opportunity to really drive better product standards in that market even harder over the coming months as well. From a category perspective, I think there is still a very good opportunity, but we need to see what we can do to actually move the category forward. As I say, our performance within the category continues to be good in Europe and growing. On disposals, Matt?

Matthew Phillips: Yes, on disposals, our target was up to £2 billion by May 2020. You will recall that we have already generated around £300 million from the sale of an OTP business plus also from Logista and the premium cigar process is working well now and we will deliver a very significant chunk of the balance. There is nothing further to update at this stage. We will obviously do so as soon as we can, but the interest in the asset has been very strong.

Alison Cooper: Sorry, just quickly back to the Europe opportunity, I think you asked about oral nicotine as well. It is true, we are now looking at a broader portfolio in terms of the Europe NGP opportunity. We had some fantastic success in terms of initial launch in Austria, clearly small in relation to the overall business, but even so a very important learning environment for us and have launched in Germany as well with some really good initial success too and rapid share growth. It is something we are very much building on and see a good opportunity for us in 2020 and beyond.

Speaker: Thank you so much.

Adam Spielman: Hello. Thank you very much. Now, when I ask the question, please be aware that I have been on an aeroplane and therefore missed frankly the press release and most of this conference call.

Alison Cooper: Okay, all right.

Adam Spielman: I will maybe ask you a question that has already been asked. This time last year, you did a presentation where you effectively said that the world was going to move pretty rapidly to e-vapor and that blu was going to be a very effective competitor, both because it had a very good brand and it was a technically good product. As I think about both the massive turbulence that has hit the US, visible in Juul, but also in what you said today, and the progress or relatively slow progress in Europe, it seems to me that frankly the idea that blu is a really good product that can sail through this new world of tobacco is completely under question. I wonder to what extent you accept that view. Furthermore, if I am right, it seems to me that you have really, quite a profound choice. Do you basically

continue with the portfolio as it is and make the sort of progress that you are currently making, or do you invest, and while doing that, obviously focus on maximising profit and cash from the conventional product? Or do you invest much more heavily to try and create frankly much better products? It is a double-barrel question. Do you accept that the vision that you outlined this time last year has turned out to be wrong, particularly on the capabilities of blu? Secondly, to what extent do you accept that and to what extent do you think you now have a really profound question about whether you double up on investment or quadruple up? I hope that question is straightforward –

Adam Spielman: – and you have not already covered it. Because I literally dialled in two minutes ago.

Alison Cooper: No, it has not been covered, Adam. First of all, around the build-up of the vapor category I think was the first point as well, most of the things we talked about when we talked about it last year was over a longer period of time, but there is no doubt, as I talked about from the EU perspective and then more recently – and very recently, to be honest, in the US, because that has been growing as a category – we have now seen a tip down in that growth. However, we actually globally still do have a very big vaping opportunity, even without extensive additional growth happening in terms of vaping. It is just the shape of it, which I will come onto, that needs thinking about in terms of open and closed systems in particular.

From a blu perspective, I think there are two learnings around blu. One is I think we said last year we had a good product. We do have a good product. It is very competitive with the other products in the market when we test it with consumers. I have to be very clear though, we do not do a product with the nicotine strength of Juul in the US, deliberately, because we do not see that as a product that is for smokers, because it is of a level of nicotine that is beyond the nicotine levels that smokers are looking for. However, that is a deliberate choice. We have a very competitive product, but I think it is fair to say that it sits within a repertoire in terms of consumers and therefore the opportunity to differentiate is something we are very much focused on, which I will come back to. In terms of the brand, blu is a good brand. It is a well-known brand in markets such as the US and the UK and increasingly now where we have launched it and we have invested significantly behind its awareness in markets, for example, such as Germany and Japan. Where we have had blu on the market previously, we have had to do I think some harder yards to actually get *myblu* awareness increased, and that was one of the things we did specifically in the US as we moved into the second half as well, because blu was known, but *myblu* needed some higher awareness.

As I look forward in terms of the opportunity, I have mentioned blu and how we are thinking about the brand, but when it comes to the experience and the offering, it is absolutely something that we have actions that are being significantly progressed to build more differentiation into the product. By product, I do not just mean the device, and I think this is something that is missing in the thinking in the category. It has got to be about the total experience around blu and that is partly why we are now shifting our focus not only behind retail but also increasingly behind the blu.com channel. The reason for that is not just to drive e-commerce. It is actually to drive the stronger relationship and build the blu experience with consumers as well. That is a very important aspect of the work we have been doing over recent months and will be very much part of the focus. To be honest, it is

more effective from an investment perspective going into 2020. That will be also linked with a better product, which we are targeting for launch during next year and we are very actively progressing at the moment all aspects of the design of that product in terms of its functionality, but also in terms of its look and feel, in terms of the device. Now I think the other aspect to mention is we have already clearly taken a step to have optionality in other NGP products, so we have optionality in heated tobacco. We have an excellent product there. We are getting great feedback from the trial in Fukuoka. We will be building on that next year. I have already mentioned OND, again, where we have innovation behind the oral nicotine delivery products, the tobacco-free products in particular, and those are starting to pick up for us quite nicely as well.

Overall, I think there are a lot of learnings to take into 2020, but as I look at our portfolio and our execution of that portfolio moving into 2020, I feel that we have something there that can really work for us.

Adam Spielman: I suppose the implication of that answer is that you do not... Well, previously you were guiding obviously to sort of margin inflation at this end of this year, but I was implying in my question that you are going to have to really step up your investment in next-generation products, reduced-risk products, but I think the implication from that answer is actually you are pretty happy with the progress –

Alison Cooper: Yes.

Adam Spielman: – you are making and therefore investment plans are not going to need to change dramatically, even if results were slightly disappointing in fiscal 2019.

Alison Cooper: Yes. I think the point that I would make is that we are optimising investment behind the level of spend we are making. I will give you an example. I have a huge frustration with the level of trade take on vapour products because of the history of their evolution and that is something we are actively addressing. We have been actively addressing, but we are tackling even harder now because it is not money that works for us.

Therefore, I see a significant reduction in those trade margins going into 2020, which we can reapply to some of our more consumer-facing activities and, particularly, around some of the online engagement and work with consumers. There is definitely a reshaping of that investment, but it is not that I am sitting here, thinking we need to increase that investment. It is substantial already.

Adam Spielman: You equally said – I mean, I am just repeating what you said – that anyone who argues that blu just is not good enough is thinking about it in the wrong way and that would just be the wrong takeaway from this morning.

Alison Cooper: It would be the wrong takeaway from this morning. I think, particularly, you need to look at our leading position in the European vaping market in Germany, in Spain, in Italy, in France that indicate that we have a good product. It is definitely a competitive product. What I wanted to do is to move ahead and be more differentiated.

Adam Spielman: Okay. Thank you.

Robert Rampton: Good morning. I have three questions.

Alison Cooper: Yes.

Robert Rampton: Firstly, you say good progress on consumer off-take update. Could you give us a bit more detail on that? What kind of sequential monthly growth are talking about and how has that changed? I feel like every update we get, it is good progress on consumer off-take.

Then, my second question is you previously stated that 1H US NGP revenue of £60 million was a clean base. How do we get from that to the kind of 2H implied sequential decline? The gap seems very large, then, to expectations. At the end of the day, September is just one of six months.

Then, my third question is can you give an update on how US volumes are trending versus your previous update? You said that – I think it is MSAi data four weeks to May 2019 were down 6.4%. Those are my questions. Thanks.

Alison Cooper: Okay. From a consumer off-take perspective, I think the best data we have is the shares that we quote and how they are evolving. I mentioned those earlier. Germany, in terms of the market share, up at around 29% in Germany. Italy, we are off a little bit just because we have established the market effectively, but we are still in the mid-50s, in terms of share. The category continues to move forward. Spain, we are around three-quarter of the market. We have very big share positions and that consumer off-take is continuing to evolve. Those are the numbers that we quote from the market data. In the USA also, you can see our off-take is increasing and our share is increasing in the US through the IRI data.

Of the £60 million in the first half of the year, if you compare it to H2, you have to remember that in the US in H2 last year, we had quite a significant IP settlement. There is still progress in H2 from the US perspective. However, it is not evident at the top line numbers because of the significant IP settlement, which we talked at the end of last year and at the half-year as well.

Robert Rampton: Just on that point –

Alison Cooper: Yes.

Robert Rampton: – I was talking about in reference to the 1H £60 million number rather than the year-on-year.

Alison Cooper: Oh, the £60 million? Versus which number then, sorry? The £60 million versus...?

Robert Rampton: The 2H 2019 US NGP number versus the 1H 2019 number.

Alison Cooper: Yes. Okay.

Oliver Tant: Robert, just to understand the question, so what you are asking is that you are implying H2 US NGP, based on the overall guidance, must be down on H1. I think your question was to what extent was all that in September because it seems implied to be quite a large number. I think that was the question, Robert. Yes?

Robert Rampton: Yes. I'm trying to understand if there is a sequential decline, what is driving that. I may be wrong in my application – in my implied number.

Alison Cooper: Yes. We are looking at similar numbers in H2 to H1 for the US. What you saw was a pick-up through the half but we did anticipate a significant ramp-up towards the

backend of the half because that is when all the different investment activities were coming onstream.

As I mentioned earlier, there was a slowdown in the growth of the category that was quite marked in August, which already impacted that, but then the lion's share of this impact has come through in September where it is not just market dynamics, in terms of the category and the share position that are impacting, but also, clearly, we have wholesalers and retailers who are just not taking stock either, which is a very significant part of that because as we are ramping up our share, we would expect, clearly, to be selling that through and it is not happening.

The last question was on the US share. Again, on the US share data, I think we have some improving data when it comes to the total market size, when you look at Nielsen. However, when it comes to our market share, it is still way off. Our share is increasing year-on-year contrary to the externally disclosed data. We estimate roughly about ten basis points.

Robert Rampton: Apologies, if you could give us some more colour on US industry volumes? If your share is up ten bps, the US industry is –

Alison Cooper: Yes. The US industry volumes are down just over 5%, we estimate, for the year.

Robert Rampton: Okay. Thank you very much.

James Edward Jones: Yes. Good morning. I would like to understand your previous expectations a bit better. The sales shortfall for the Group is going to be something like £150 million. As the previous question said, you did £61 million of sales of NGPs in the US in the first half. If NGPs are the only real reason of the sales shortfall, what were you budgeting to do in the second half because on that evidence, you must have been budgeting for your sales to go up sort of three or four times in the US in the second half compared to the first half.

Oliver Tant: James, I do not think it was that much. If you look at our guidance – the guidance we gave – we said at the upper end of our 1% to 4% range, about 1% of which was going to be Tobacco. If you sort of roughly derive a number – you were talking about something around the £400 million – 50%, as I think some people have already latched on to, would imply that we are closer to £300 million. You have a chunk of it which relates to that.

Then, the other element, obviously, is the rephasing of Australia. Now, Australia is sort of a high-value market for us and the volume, therefore, in terms of net revenue, can be quite substantial if we see rephasing elements to it. We did have quite a sizeable, given the change in regime that happened in Australia over revenue opportunity. The balance of it is principally Australia.

James Edward Jones: I am just – while I was trying to think about this philosophically with high tide, obviously, your expectations were over optimistic. Are you going through any sort of thought processes to how you set your guidance in future and whether it would be appropriate to take more sort of a prudent stance?

Oliver Tate: We are looking at the basis for our guidance and we will give you a little more colour around this when we get to the prelims.

James Edward Jones: Thank you.

Mark Howden: Yes. Good morning. Two questions. In September, you talked about the US vape being quite negative. I think that was an Imperial point, not an industry point, but forgive me if I have misunderstood. I am curious as to what share is doing sequentially. You talked a little bit about the 99-cent devices – I assume that is NJOY. Then, some competitors reacted. Did you react and recover share sequentially or is there a sequential issue here?

Alison Cooper: Okay. The negative piece in September is around the overall category development. It is IRI data. It is only – clearly, we do not have all of September in yet because we have done some extrapolation, clearly, from how we see this happening. Yes, that was actually for the overall category. It was not our data, in terms of the blu performance.

In terms of blu, we are seeing a growth in share. It's continued to make progress in terms of share because ultimately, we did respond with a device offer of \$1. However, it is only what we call a dry kit with no pod associated with it. Therefore, the consumer has to buy the pods with it as well. The out-of-pocket was nearer at the minimum \$10 depending on the outlet. In other outlets, it was around the \$18 mark. We made sure that we had a sufficient out-of-pocket from the consumer in terms of driving repeat purchase, because our history when we trialled a \$1 offer with a full wet kit historically was that we just did not drive that consumer loyalty. It was too cheap in terms of them sticking with the device going forward. We have done the dollar offer and that has helped from a dry kit perspective the overall progress of our share in the market.

Mark Howden: Extremely clear, thank you very much.

Sanath Sudarsan: Hello, good morning. Thanks for the questions, two from me. One, you have actually reiterated on the call quite a few times that your pace of growth has actually been better than most categories or markets. Does this imply that you are saying or suggesting that the overall nicotine market has actually slowed versus your expectations earlier? The second question basically is on your confidence on the outlook you initially provided on NGP growth of 35 to 150% medium term and also on the tobacco growth algorithm on revenues and profits over the medium term. How do you see this evolving, or are you still confident of maintaining this over the medium term? Thank you.

Alison Cooper: Okay. In terms of the nicotine market overall, there is a number of dynamics we are seeing. I think one of the things that we talked about, and I talked about in various presentations earlier in the year, was in the research we did with consumers there is no doubt the consumers are now using a repertoire of nicotine products. That is very often two, if not three, products. Depending on those products, they may be substituted, or they may be additive in terms of consumption. As we know, heated tobacco tends to be a substitutive experience. You either have a heat stick or you have a cigarette, whereas vaping or oral nicotine tend to provide opportunities for additional occasions of using nicotine because you can use them when you cannot smoke. Clearly, vaping, you have more opportunities than oral nicotine. There are really no constraints at all as to when you can use oral nicotine, which is one of the attractions of the product for consumers.

Overall, nicotine marketwise, there are various areas that are growing currently and we do still see nicotine markets in growth overall. I would say that the specific point I was making was around the closed system vaping category. That particular category has not grown as

fast as we anticipated. Some of the reasons for that are around the presence of open systems in markets, sometimes it is around affordability. Therefore, there are actions we are looking at in terms of shaping that environment going forward, particularly in relation to product standards and regulation, which we are working with governments on and will clearly get picked up as well, we believe, in the next EU TPD round as well. That is how we are seeing the nicotine market overall. However, I would say if you are looking at that now versus just looking at combustible tobacco markets a couple of years ago, there were a lot more opportunities in terms of growth products within that.

From an NGP outlook in terms of growth, I have been very clear all along that the LTIP guidance that we gave around compound growth rates was just our LTIP. They are not baked into our plans in terms of the upper end of that actual target range for the LTIP. That was just the LTIP guidance; and the LTIP guidance was set with clearly a huge ambition behind it at 150% compound end, but also recognising the volatility in this space in terms of delivery at the lower end. With the result for this year, we are clearly going to be within that overall range. However, clearly not at the upper end of it next year unless something very significantly different happens.

Finally, on tobacco growth, we are still very much seeing a tobacco market that is very resilient from an Imperial perspective. I have been talking about modest top line growth, which then multiplies down into better operating profit growth lower down the P&L; and that is still the model we are very much looking at going out over the next few years.

Sanath Sudarsan: Thanks, Alison. Just one follow-up on that, on the first part if it. From what I understand is it is actually for Imperial the problem currently is the mix of the brands in the portfolio you have in NGP rather than actually doing better within the categories you are already exposed in. Is that a fair comment?

Alison Cooper: A couple of things there: yes, we are actually looking at driving the optionality we created in heated tobacco and in oral nicotine. We are seeing, as I mentioned earlier on in the call, some success particularly with oral nicotine at the moment in Europe, the beginnings of, I think, a quite nice category for us, and we are getting the learnings out of Japan at the moment as we look at how we take heated tobacco forward. However, from a vaping perspective, we have still got some really good shares in terms of our progress with the closed category. We just need to work, as I say, on moving that forward more in terms of the category growth, which I think we can do.

Sanath Sudarsan: Thank you very much.

Gaurav Jain: Thank you. We had some estimates about NGP revenues and costs. The NGP net revenue shortfall will fall directly to the bottom line. In 1H 2019, you had 100 million extra investment on NGP. We know that the e-cigarette market in US is going to slow down. Is it fair to say that you are going to reduce your investment in NGP in US next year, which should actually then improve your profitability?

Alison Cooper: Yes, I think it is a good point around the US at the moment. In total, in the plans, we are maintaining but reallocating the investment. However, I think at the moment in the US, we are having to just be very much on top of what is going on and making those investment calls as we see the market evolving. We currently have some ATL running in the US. We clearly have investment in retail programs and promotions; but those are being

regularly reviewed to see whether or not they still make sense in the current environment. It is a very active situation in the US currently. However, clearly, the PMTA process itself is absolutely critical. We are confident in terms of our position in terms of getting through PMTA. As we get to the latter part of 2020, it may well be that we have a much clearer situation to invest behind. However, we will reallocate funds and optimise investment as appropriate at that point in time.

Gaurav Jain: Okay. You had mentioned that in August or September the vaping market has slowed down in the US. I do not know, but I would think that it will be certain states, like Massachusetts, New York, Michigan, where the governors are talking about implementing flavour bans or outright e-cigarette bans. In those states or those cities where e-cigarette bans are coming in, are you seeing any improvement in cigarette volumes?

Alison Cooper: I think it is too hard to call at this point in time. I have seen and we have talked about this as a hypothesis. It could have some impact on the cigarette volumes, and I think maybe not so much because of bans necessarily, although clearly that would have an impact. I think what is concerning me is there is a lot of consumer misinformation out there at the moment that consumers are now thinking that e-cigarettes are a really bad thing, e-vapour is a really bad thing for them. We drew some conclusions out of these recent respiratory disease and deaths coming out to reassure consumers around vaping products made by responsible companies; because otherwise, we would really be missing out on a potential public health benefit here.

Gaurav Jain: Sure, thank you.

Faham Bain: Thanks, guys, thanks for the follow-up. Two very quick questions: just to understand the magnitude of the decline in earnings, so I guess 2% is coming from your top line and 2% is coming from profitability, which works out to be about 70 million. Am I right in assuming that half of it is related to Australia, that 70 million, and the other half is related to incremental NGP investment that you spoke about in the second half with regards to advertising, promoting, etc.? That is the first quick question. The second quick question is to Oliver's earlier point around evaluating the effectiveness of the NGP supply chain. What sort of number could we potentially be looking at that could potentially hit your P&L and cash flows?

Alison Cooper: Okay, yes. I am going to get Oliver to answer both of these. However, the first one I think is better looked at in terms of just discussing what is gone on with the 4%, the 4% EPS rather than assuming the 2% from revenue, if you see what I mean? Now, it is easier to explain that way.

Oliver Tant: Well, like I said, the answer pretty simplistically is the majority of it is NGP, a smaller proportion is tobacco-related and Australia-related basically. In answer to your question, that is the simple high-level answer.

In answer to the second question, there is a whole lot going on in the context of regulation, in the context of macro-economic trading relationships between different parties that basically is influencing our judgement around what is the best supply train structure to have. We are building this business. We should not forget we have seen 50% growth in it and as it builds, we are getting the opportunity to drive effectiveness by developing new relationships with

people who are able to perform better on our behalf. That is what we are doing in this particular area. We are talking tens; we are not talking much more than that.

Alison Cooper: Yes, lower tens of millions, yes.

Oliver Tant: However, still, we feel we should flag it because it is relevant. The timing will depend on when we conclude on some of these arrangements, it is a combination of things that are impacting those judgements.

Speaker: Thank you.

Robert Rampton: Thank you for taking my follow-up. Are you profitable with NGPs in any market? Or close? i.e. those EU markets where you are number one.

Alison Cooper: Yes.

Robert Rampton: Are you close. I am asking as I am trying to understand the basis for your comments that you will break even in 2020. Thank you.

Alison Cooper: Yes, we are and particularly in markets where we have not gotten the trade margin issue to the same extent as we have for example in the UK and in the US. Germany for example, Japan. We have profitable models in those markets.

Robert Rampton: Great, thank you.

Nico von Stackelberg: Well, a previous follow-up did ask the question, but I just want to dig in a bit more detail. With the vapour bans coming through, you are a tobacco manufacturer and you need to be monitoring quite closely how volumes will uptick in light of vapour bans. I am just wondering, surely you have a number that you are thinking about in terms of consumers switching back into tobacco and what that means for your own volume. I am just confused that it is too early to call. Surely you guys are looking at this very closely and have some sort of a clue about how consumers are going to respond to this ban? I saw a number in the sixties from Reuters. I think it was 62% of people said that they think that vapour is more harmful than tobacco now. Could you just explain why is it too early to call? How are you thinking about it right now?

Alison Cooper: Well, we can hypothesise but there is no decent data as yet on it basically is what I am saying. I will go back to the comment I made earlier as well, which you have to bear in mind, which is vaping is very often part of a repertoire that a dualist uses, or they have more than two products. I am not sure what we will call them, but anyway. However, it is something that they use very often on occasions when they can't smoke. Even though I think, yes, there may be a small uptick in terms of the cigarette market, I do not think it is going to be that significant. If you look at the data that disaggregates the market size declines in the US currently, just over a percent of that is related to the vapour effect on the market. Maximum is probably that sort of percent in terms of decline. However, I think it is going to be way off that.

Nico von Stackelberg: Okay, thank you.

Operator: There are no further questions at this time. Please continue.

Alison Cooper: I will just say thank you for joining us today and for the questions.