IMPERIAL BRANDS PLC
INTERIM RESULTS FOR THE SIX MONTHS ENDED 31 MARCH 2018

9 MAY 2018

H118 Interims Script

Slide 3 - Introduction

Good morning & welcome.

I am joined here today by CFO Oliver Tant, CDO Matthew Phillips and also our Chairman Mark Williamson. We are also joined by Dominic Brisby and Joerg Biebernick, Division Directors for Growth & Returns.

I am pleased to be updating you on our progress in the last 6 months, building on the success of our investments behind our strategy both in tobacco & NGP in 2017 and building on the improving metrics in the second half of 2017.

Slide 4 - Strategy delivering in Tobacco & NGP

Let's start with some headlines…

We have a clear focus on our product, brand & market priorities, and that focus is delivering results.

Our volumes are outperforming the market, reflecting the outperformance of our growth brands, including good organic growth.

And share is up overall and in 7 of our priority markets...

As we previously flagged, price/mix has been weak in the first half but is now strengthening into the second half.

We are stepping up our activity in NGP... and it's exciting to get the early feedback from the *my*blu launches & see the significant progress with our innovation pipeline.

And as we continue to sharpen our strategic focus we are progressing opportunities to divest assets, which will further simplify the business & create additional value.

Slide 5 - Building Momentum

We are delivering against our strategy in a better environment.

Many of the headwinds carried over from FY17 into the beginning of FY18 are ameliorating. We are lapping the EUTPD impacts of last year, particularly the negative mix in the UK from the ban on high margin 10s packs.

We are also lapping some excise increases, although there are continuing negative impacts in Saudi & Taiwan and France continues to be (I think the polite word is) challenging.

If we look at the headline industry declines, they seem high, but stripping out an outlier like Japan, where we have limited exposure, the decline is around 4%, which is more manageable.

And price/mix is improving, at around 4% in the second quarter.

Against this backdrop, as I have already highlighted, our performance is ahead of the market and with improved quality of growth. We are on track target with our NGP launches.

I therefore anticipate a much stronger H2, with tobacco growth driven by our Growth Brands, improved price/mix and NGP growth from market expansion and growth in existing markets, including nicotine salt launches in the next few months.

In addition, profits will benefit from further cost savings which are H2 weighted.

We are on track to deliver in line with our guidance.

Now over to Oliver to cover the financials.

Thank you Alison and good morning everyone.

Slide 6 - Summary H1 Financials

I am going to start with a summary of our results for the Half Year.

The results we have announced this morning are further evidence of our investment initiatives delivering with our volumes outperforming the industry. Volumes were down 2% in the first half, comfortably ahead of the industry footprint declines of 5.7%.

We delivered first half results slightly ahead of our expectations at the time of our February update.

First half net revenue was down 2.1% with flat price/mix due to the carry-over of the tough trading environment from last year – and the impact of a one-off IP settlement in the first half of FY17.

We've seen a much better price/mix performance in our second quarter of around 4% and this improving trend is expected to underpin our second half delivery.

EPS was down 1% reflecting the revenue performance but was partially offset by lower finance costs due to deleverage, a marginally lower tax rate and a better contribution from Logista. At actual rates, EPS was impacted by a 5.2% currency headwind.

Our focus on cash has delivered another strong performance with debt reduction of £1.2bn or £900m excluding FX movements.

Slide 7 - H118 Tobacco Volume

Our volume performance has significantly outperformed the market driven by market share gains. As I have mentioned, our volume performance has been led by our Growth Brands - as these continue to benefit from increased focus and investment.

Growth brands outperformed with volumes up over 6% growing 100bps of market share. Excluding the benefit of our migration programme, they grew 1.6%, demonstrating the benefits of our focused brand strategy in generating quality growth.

We have achieved a strong performance in our Growth Brands in every year since we began this strategy in 2013.

In Specialist Brands, we have delivered strong volume performances with Backwoods and Kool. However, volume was disproportionately impacted by lower volumes of Gitanes in the Middle East, although this had a minimal financial impact.

Growth & Specialist Brands now represent 65.2% of total tobacco revenue, up 3.9% at constant currency.

Portfolio Brands were down partly as we migrate volumes into our Growth Brands. As compared to the industry volumes in our footprint, these brands underperformed by 1.7%, a really good performance given the focus and investment is directed elsewhere. We continue to optimise the Portfolio Brands for profit and cash, which has an impact on volumes.

Slide 8 - H118 Tobacco Net Revenue

Revenue reflects our volume outperformance and a price/mix that was broadly flat, in line with our year end guidance. This has been driven by some adverse mix in certain markets. Price/mix was also affected by the benefit of the Fontem IP royalties we received in the first quarter last year.

These royalty payments are an ongoing revenue stream for Imperial although their timing is irregular. Price/mix was up 1% excluding the Fontem IP and up 4% in the second quarter.

A weaker Dollar resulted in a FX translation headwind of 2.9% and resulted in a 5% decline in net revenues in the period.

Slide 9 - H118 Adjusted Operating Profit

The adjusted operating profit reflects the lower revenue and the additional investment in NGP.

It was also impacted by £13m of transactional FX, which we expect to be circa £30m for the full year in line with guidance, this is primarily due to increased input costs of leaf.

We also achieved other gains in operating profit with the net benefit of £7m - comprising £40m profit from the sale of other tobacco assets in the US offset by last year's £33m of gains on sale of Logista bank shares and the benefits arising on post-retirement benefit schemes in the US.

We undertook to provide greater clarity and transparency on these gains in future.

As a result and in-line with our full year guidance of £50-100m, we expect further one-off gains in the second half.

Logista improved profits by £16m by further developing their non-tobacco business and continued cost discipline.

Slide 10 - Divisional Performance

Growth Market volumes were up with the growth of West in Saudi Arabia and improved share performance in other priority markets.

The net revenue movement reflects mix pressures in Saudi as a result of excise duty changes as well as the Fontem IP income we received in FY17 which I have referred to already.

The US had another positive performance with strong net revenue reflecting price/mix and continued growth in our mass market cigar business.

Profits in the US were helped by the sale of other tobacco assets although stripping these out underlying profits were still up over 12%.

Returns markets saw volume down broadly in-line with market declines in the footprint. Revenues were affected by the carry-over of last year's trading conditions particularly with the tough trading in France and the mix impact from EUTPD in the UK.

As you can see, our portfolio simplification and investment focus has delivered Growth Brand share gains across all of our divisions.

Slide 11 - Cash & Balance Sheet

Overall the business continues to generate strong cash-flows with cash conversion of 111% in the half – benefiting from better working capital with a £700m inflow over the 12-month period.

Of this, around £250m came from the timing of duty payments at Logista and around £350m was from lower finished goods levels in the UK and Russia due to the changes in timing of excise increases. Without these, the cash conversion would have been just over 90%.

None of these are expected to benefit the full year cash conversion, which we expect to be around 95%.

We have also seen another £0.9bn of debt pay-down at constant currency over the last 12 months, and £1.2bn at actual rates.

I should remind you that full year cash flows will be affected by £160m due to P&H entering administration and a step up in restructuring spend of c. £200m this year, as previously guided.

Given the strong track record on cash generation and debt pay-down our credit metrics continue to improve… and you will have seen two of our credit rating agencies recently reaffirmed our ratings.

Slide 12 - Outlook

In summary, these results are further evidence of continued delivery against our strategy.

We are targeting to deliver full year constant currency revenue and earnings growth in line with our medium-term guidance.

This will be driven by a far stronger price/mix delivery and will build on the improved volume and share performances we have achieved over the last six months.

It will also be supported by the rollout of *my*blu, which we expect to enhance our top line growth.

The improving top-line will drive a better margin performance in the second half as will the cost savings, which will be second half weighted.

We expect that full year earnings will additionally benefit from the lower tax charge although FX will remain a headwind of around 4-5% at current rates.

Our view on full year finance charge, capex, etc. are unchanged and more detail is provided in the appendices.

So to finish, we are delivering through our focus on Growth Brands and priority markets with improving performance metrics that will drive results.

On NGP we are well placed with the roll-out of *my*blu benefiting the second half.

Our focus on capital discipline and our strong balance sheet supports our strategic agenda as well as growing returns for shareholders and enabling debt repayment.

Thank you and I will now hand you to Matt….

Slide 13 - Strategy Delivering

Thanks Oliver and good morning.

For the next few minutes I would to update you on our progress in next generation products before handing over to Alison to give you some more colour on the progress in our tobacco business.

As you know, we see a meaningful opportunity with next generation products, namely e-vapour, oral products and heated tobacco, to generate additive revenues and profits.

As a reminder, over 85% of the world's smokers are not currently consumers of Imperial Brand's products & downtrading within tobacco remains a really important dynamic globally – being able to offer affordable yet highly profitable experiences to smokers in such an environment is vital.

We are investing for growth.

In 2018, in e-vapour we are continuing to build the blu brand and are in the early stages of the international roll-out of *my*blu & blu ACE; in oral products we are expanding our existing successful offerings with the introduction later this month of tobacco-free pouches. In heated tobacco we have second stage consumer trials planned for the next few months.

For all 3 areas we have of course been investing in production capacity too.

We are focused on building great brands.

Great brands require great consumer experiences & our innovation pipeline remains totally focused on delivering these experiences across the NGP spectrum.

Slide 14 - Significant NGP Ambition

To repeat, we see a meaningful & additive opportunity for Imperial Brands in next generation products.

None more so than in e-vapour which is by far the biggest NGP experience in terms of numbers of consumers, even more so in our markets.

Whilst the e-vapour market today is fragmented in certain countries, we see this as a fantastic opportunity – everything starts with the consumer – simplistically what has been missing to date are standout consumer experiences. The marrying of a fantastic brand with a drumbeat of new innovations that continually improve the experience with a consumer engagement strategy that is seamless across channels.

The more we enhance the experience, the more the consumer base grows & the more the consumer spend grows;

As we scale the more we can leverage overheads & normalise marketing spend more effectively and as we innovate, our cost of goods falls dramatically – all driving our profitability.

You will recall from a recent presentation by Oliver that we are targeting gross margins of circa 70% and operating profit margins of circa 45% over the next few years.

All underpinned by the increasing levels of scientific & regulatory know-how required to bring innovative new products to market, an area in which few have the requisite capabilities.

Slide 15 - Building blu equity

Before talking a bit more about some of the innovations coming over the next 12 months, a reminder about *my*blu and blu ACE – both platforms are simple to use & therefore of wide consumer appeal.

*my*blu is a simple to use pod-based platform that genuinely provides smoker satisfaction.

Over the next couple of months we will be enhancing the platform further with the introduction of nicotine salt liquids under the name "*my*blu intense" – all targeting adult smoker conversion.

Building on the success of our blu pro platform we are also launching a simple to use & powerful open system platform called blu ACE, enhanced by adult-focused juice ranges.

Slide 16 - Building Growth in Distribution

In terms of the international roll-out of *my*blu, we are currently in the early launch stages in 5 markets with a further 5 to follow in the second half of the year.

We aim to be in 20 markets during FY19.

By the end of 2020 we are aiming to have at least 8m blu consumers.

As I said earlier, the consumer engagement strategy has to be seamless across channels.

You can see on the slide examples of activations, in this case in partnership with vape-channel players & on-line retailers.

We are already receiving good consumer feedback & seeing positive early traction & re-order in retail, the vape channel & on-line.

The approaches we are testing have different biases in different markets.
By way of example, over the next few months we expect to be in more than 50,000 retail outlets in the USA, 6,000 outlets in Russia and 12,000 outlets in France, reflecting the different approaches being tested in the different countries.

Slide 17 - blu Innovation Pipeline

As I said earlier, we are focused on building great brands.

Great brands require great consumer experiences & our innovation pipeline remains totally focused on delivering these experiences across the NGP spectrum.

Finally, therefore here is a reminder of blu's proprietary innovation pipeline for the next 12 months.

I have touched on many of these already this morning and many of you here have experienced some of them.

Of course in oral products we are also expanding our existing successful offerings with the introduction later this month of tobacco-free pouches and in heated tobacco we have second stage consumer trials planned for the next few months.

There are also one or two other exciting opportunities we hope to be able to talk about over the coming months.

In summary, we are delivering the significant step-up we outlined at the end of last year with revenue momentum expected to build in H2 as the various roll-outs continue.

I'd now like to handover to Alison to give you some more colour on the progress in our tobacco business.

Slide 18 - Strategy Delivering

Thank you Matt…

NGP momentum is building through focused investment and we have also recently restructured our NGP business to leverage the strengths of the tobacco business even more effectively.

And in tobacco, momentum is also building through focused investment behind our priority markets & behind our Growth Brands, to deliver quality growth.

Slide 19 - Tobacco Max: Portfolio Focus

Our Growth Brand success, builds on our successful portfolio simplification work of the last few years, boosted by the step up in investment last year behind our Market Repeatable Model, or MRM.

All key metrics are significantly improving with volumes up 6.3%, including organic growth (ex migrations) of 1.6%. A 100 basis point increase in share and an increased proportion of Net Revenue from our asset brands - now at 65%.

Slide 20 - Tobacco Max: Leverage Market Repeatable Model

And this investment behind our MRM is also reflected in our overall share performances in priority markets.

We have a clear portfolio focus and have continued investment in equity building, distribution & customer relationships this year. This brand and customer focus has been integral to our share success.

Share is up in Germany, UK, France, Russia, Italy & Japan, driven by our Growth brands & the disciplined implementation of the MRM.

Russia has been a notable success following some tough calls on portfolio simplification and our subsequent investment, particularly in key accounts.

And the UK turnaround continues; again, a clear portfolio focus and investments in activation and customer relationships underpinning our share growth.

In France, share is up with a great performance from News - benefitting from increased focus within a simplified portfolio, although share will come under pressure in H2 as we balance share & profitability in a difficult trading environment.

Share is up significantly in Saudi where our portfolio is well positioned given the market dynamics but mix is significantly negative given the decline in the Premium segment post the excise increase last year.

Share is down temporarily in Australia due to a price disadvantage around an excise increase towards the end of last year, but the spot share has since recovered.

In Spain, share continues to be impacted by the dark segment but our blonde share is on an improving trend.

And in the US we delivered a strong financial performance. Our cigarette share decline is ameliorating. Winston, Kool & Maverick are all doing well, as is MMC where share was up to 14%. Overall some good share performances to build on in the second half…

Slide 21 - Tobacco Max: Always on Price Strategy

So, volumes are good in the first half but the overall top line performance was held back by the carry-over of some 2017 headwinds as we anticipated.

For clarity, there has been no investment in 2018 behind the "always on price strategy" element of the MRM - you will remember that the focus here is about price parity with relevant competitor brands.

Price/mix pressures are environment driven, not the result of aggressive price positioning which merely "borrows" share.

And I mentioned at the beginning, price mix is improving as we lap the 2017 headwinds… up 4% in Q2 as the trading environment improves.

Our volume performance combined with improving price/mix plus additional cost savings underpins our confidence in the second half... whilst recognising that markets like France & Saudi will continue to be a headwind…

Slide 22 - Strategic Focus: Right Markets, Brands & Products

A clear strategic focus sits behind our 2018 delivery.

We are prioritising the brands, products & markets that are central to our strategy.

We are driving continued portfolio simplification and active market prioritization and realising NGP growth opportunities through targeted investment.

All supported by a lean operating model and a continued focus on cost & manufacturing optimisation.

As we further focus the business behind our priorities we are also evaluating opportunities for assets that are not central to our growth agenda, a recent small example was the disposal of our US OTP brands.

There is more that we are doing & today we have announced the initial scale of our thinking, looking to realise up to £2bn of proceeds within the next 12-24 months.

As you will understand, I am not going to be able to provide further details at this stage.

There are clear strategic benefits for the business. It drives an even sharper execution focus & facilitates further simplification and agility and it delivers efficiencies in costs & cash & unlocks capital to redeploy to maximise value for shareholders.

Slide 23 - Improving Momentum into H2

So to conclude.

I am pleased with our progress in H1, reflecting a continued focus on our priority markets & strongest equities and we have improving momentum into H2.

It’s exciting times in NGP with launches & progress on new initiatives & that will also add to our H2 revenue growth.

Thank you.