BAT Preliminary Results 2013

Ben Stevens, Financial Director

Financials

Q: Can you run through the financial highlights for the full year?

A: Yes. I think this has been a really strong year for British American Tobacco. On a constant currency basis we've met or exceeded all of our financial targets in 2013. We did see the appreciation of sterling in the second half of the year and that meant we had a 4% adverse FX headwind on translation on exchange during the course of the year. Overall, I am very pleased with the growth we've had in operating margin, we grew operating margin right at the top of our guidance at 100 basis points. And we are still very cash generative. Our free cash flow is very strong and that's meant that we can carry on the buyback at £1.5bn during the course of 2014, so overall very pleased with the results in 2013.

Q: You mentioned the impacts of the strength of sterling; can you just give me a little bit more detail on how that's affected these results?

A: Yes. This time last year we were expecting a tailwind of about 3% in terms of exchange rates, but as you know sterling strengthened substantially in the second half of the year and that's affected our exchange rates with some of our bigger end markets so markets like South Africa, Australia, Brazil all saw fairly substantial depreciations in their currencies against sterling, along with the Indian rupee as well and that's meant that we face a 4% FX headwind during the course of 2013.

I'm often asked for guidance in terms of FX on 2014 and obviously it's very early days yet, but if we had to translate 2014 results at today's exchange rates that would give us something like an 11% headwind in 2014.

Q: Over the last few years you've either exceeded or been at the top end of guidance on margin improvement, this without the benefits of the SAP programme. Now that the SAP programme is rolling out across the world are you going to increase guidance?

A: Well you're right, we delivered at the top of guidance in terms of operating margin growth for the last few years. It gets tougher to deliver cost reductions every year of course and the growth in operating margin is not just from the

SAP roll out, we've been doing factory rationalisations, we've been gathering people together in shared service centres, we've been building centres of expertise and we've been rolling out our target operating model all the bits that aren't dependant on SAP so the benefits of the new operating model have already been coming through in terms of operating margin over the last few years.

But we have a very successful roll out of SAP in Australasia and in South Asia this year and we do expect to complete the majority of Asia during 2014, so I'm confident that we can continue to deliver our 50 to 100 basis points operating margin growth year on year. And I have said that when we reach 40% then we'll pause and think about giving more guidance to the market.

Q: With foreign exchange being such an important factor behind earnings growth will your dividend policy stay the same?

A: Yes, we've always said that the 65% payout ratio is a floor and not a ceiling and you can see that this year in the sense that if we follow strictly the 65% payout ratio our dividend would only have gone up 4%. But we like to keep our dividend ticking ahead in sterling terms. We've increased the dividend 6% in 2013. And I think if we ever got to a situation where adverse translational FX rates overwhelmed a strong business performance then we'd look at the payout ratio and we'd keep the dividend moving ahead in sterling terms.

Q: If we turn to capital expenditure this was well below rates previously indicate, why was this and will spending remain at 2013 levels?

A: Yes, we had some factory sales and assets sales in 2013 so we sold a property in Russia and a property in Australia and that reduced the net CapEx figure. But I've already given the guidance that net CapEx will be in the £750m to £800m range for the next few years as we continue to roll out SAP and as we invest in new areas like Next Generation Products as well.

Q: What are your plans for the share buyback programme given recent share price movement?

A: We've announced that the share buyback will be £1.5bn in 2014. And that will take the total share buyback programme since it started in 2011 to £5bn.

Q: Are you still confident that you can deliver on your high single figure EPS promise in 2014?

A: Yes. I think the business is performing extremely well. Not only are we delivering results today we are investing in tomorrow. So despite the 10% constant currency EPS growth in 2013 we've been investing in Next Generation Products, in the Philippines, in Indonesia, in North Africa and China and these investments will repay us in future years, so I'm very confident that we can continue to deliver high single digit earnings growth going forward because we are not only delivering today but we are investing in tomorrow.