



# Half-Yearly Results 2014

Nicandro Durante, Chief Executive

## Performance

**Q: Half way through the year, are you satisfied with these results?**

A: Yes, I am. We had a very good first half of the year. We had some currency headwinds, of course, in the first half of the year. Around 12%, 13%. But if you look at it in constant terms, it was a very good result. Revenue is up 3%, we have operating profit going up 4% and we are reaching the high single EPS growth target that we have in the long term. Volume is performing better than previous years and we have now 0.4% volume decline in an industry that should be declining this year around 2% to 3%. This is mainly due to our share growth. We are growing share overall, mainly driven by our GDBs that are performing very well. So I'm very happy with the first half of the year. It's set us quite well for the full year.

**Q: As you say, volumes are improving but price mix is lower. Why is this and how do you see this developing throughout the year?**

A: Well in the first half of the year, we had 75% of the price mix that we expect for the full year. That's - I think that the percentage is lower than we had in the same period of last year. But it's because in 2014, pricing's moving towards more the second half of the year. So we have some price increases going through now in May, June and July that improve our performance in terms of price mix for the second half. Also, we are growing very fast in developing countries I which the margins are lower. That's why we have a bigger impact in the mix element. But we are still confident that we'll get the price mix that we estimated for the full year.

## Markets

**Q: Are you pleased with the performance from each of your regions?**

A: Yes, I am. We had a very good performance in BAT in the first half. If you look across the regions, the performance was - were very good. Let me start with Asia, for example. Asia was growing volume around 4% and profitability

was up 6% in the first half. So very, very solid numbers and we are growing across the region in places like Indonesia, Japan, and Malaysia. So fantastic performance - Philippines as well. Very good performance in Asia, GDBs are growing very well, Kent is performing extremely well in Japan. So it's set us quite well for the second half as well.

You look at Americas, for example, also a very good performance overall in Americas. Growing share in most of our markets. GDBs are growing 14% in the first half of the year. Quite an outstanding rate of growth. You go to Western Europe, volumes declined in the first half of the year, mainly due to the economic conditions in Western Europe. Of course, the market is declining less than in the past. I said in the full year's result at the beginning of the year that Western Europe was declining around 7% to 8% in terms of the industry decline. Now we see the industry declining around 5% to 6%. So it's better.

Our numbers in the first half were 8% down. But if you excluded the one-off in Denmark in which we have a trade loading, volumes are 6% down. You have a good performance in places like in Poland, UK, among other markets. In EEMEA, very good all round performance, very good profit growth, 7%. Good growth in places like Russia, Ukraine, South Africa, Middle East. So very good results overall.

**Q: But as you say, Western Europe is proving to be challenging. Are you seeing any signs of improvement from this market?**

A: As I said, we are declining a little bit less in the first half of the year. But if you look at the fundamentals for the region, in terms of unemployment and disposable income, it's a little bit better. But we will have to wait another six months, 12 months to confirm this improvement.

**Q: Last year, we saw big excise-driven price increases in Russia and Brazil. How do you see these markets performing and are there likely to be further big excise increases in your view?**

A: Let me start with Russia. Yes, we have significant industry volume decline in Russia. Around 9% to 10% because of the size of the price, the excise driven price increase at the beginning of the year and another one, second price increase that we had at the middle of the year. I expect that next year, we still have a significant excise increase in Russia. But the profit pool is moving to the right direction. We are taking prices there, our competitors as well, and the profit pool is moving quite well. We are growing share in Russia quite strongly through Rothmans and through the whole portfolio that we have there. So very happy with Russia in spite of the overall industry decline.

If we look at Brazil, Brazil last year we came with a double digit decline in terms of volume. Look at the first half of this year and the market is declining around 4% to 4.5%, much better than it was before. As I explained before, excise increases in Brazil, and it happened at the beginning of each year, the

level, the size of the excise increase is coming down. So next year, excise will move up according to inflation. So it's much more manageable.

For 2015, as far as I'm aware, there are two significant excise increases. One in Russia, as I mentioned, and the second in Australia, part of the four years program of 12.5% excise increase every year. Apart from that, I think that excise environment is quite rational.

## **Global Drive Brands**

**Q: Now, as you say, the GDBs performed strongly in the first half. Is that likely to continue in the second half?**

A: Well our objective with the GDBs is that they grow faster than overall market. It happened again. The GDBs grew in the first half of the year, 5.7%. If you include the GDBs plus international brands, they are already 60% of BAT portfolio. Which is a much better position than we were four to five years ago. All the brands have performed well and this has driven a growth in terms of share of the GDBs of 60 basis points and helped us to have a growth in the premium segment of 40 basis points. Kent is doing very well across the world but I think that if we look at the big markets of Kent, good performance through the development of the tube innovation is doing quite well.

You look at Dunhill in places like Indonesia and Brazil, outstanding performance beating all the records in terms of share growth in those markets that are quite important for the brand. The same I can say about Rothmans in Russia and in some other markets that have been launched recently, is doing very well. The same with Lucky Strike and the same with Pall Mall. So very happy with the performance of the GDBs.

## **Reynolds American**

**Q: Why do you think the investment that you've announced Reynolds American is a good deal for BAT?**

A: Well Reynolds American decided to go for the acquisition of Lorillard, of course subject to anti-trust regulators that we think that will go through. I think that they have a bigger and stronger business than Reynolds by itself. We had 42% in Reynolds and we think that having 42% in this enlarged company was a good investment. I think that they have a very good portfolio of brands in the biggest profit pool in the world outside China. It's a place that you want to participate and keep our shareholding there.

On top of it, I am very glad that we have been able to work together in terms of sharing technologies to develop in the NGP category, in the heat-not-burn and the e-cigarette category as well. So it's quite an important development for both companies.

## **Plain packaging**

**Q: Now following on from your comments at the prelims that plain packaging is not having any effect in Australia, is this still proving to be the case?**

A: Well if you look at the numbers, it's very difficult to talk about the impact of plain packaging when you look at four to five years. You have to look at the impact of plain packaging after the introduction of plain packaging. It was at the beginning of last year, end of 2012 to be precise, in December 2012. You look at the numbers in 2013. For example, the average daily consumption has declined last year at a lower rate than it was before. Volumes were up last year 0.3%. So I don't see any impact in plain packaging.

This year, we see a higher rate of decline in terms of volume but this is driven by the significant excise driven price increase that you had at the beginning of the year. That is the only reason for that. So the rates of decline of volume in the past was around the 3%, 4%, to 5% and last year we grew 0.3%. So I don't think that is bringing the benefits that the Government was expecting.

**Q: What's the outlook for the rest of the year?**

A: We are very confident for the second half of the year because we have a very good first half. If you look at the shape of the business, I don't think that BAT could be in a better form. We have share growth, we have share growth in big markets, we have GDB growth, we have growth in the premium segment. We are delivering our financial metrics in the long term. I'm confident that the second half will be the same. So very confident for 2014.

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