



British American Tobacco

Half-year results 2015

Nicandro Durante, Chief Executive

Performance

Q: You indicated at the full year that this year would be second-half weighted in terms of profit growth. How are these first-half results? Are they as you expected?

A: Yes, they are. We had a very good first half considering the strong comparator coming from 2014, and considering as well that we are in a very challenging environment. But look at the numbers. We had volume decline of 2.9% in an industry that is down around 3.5% to 4%, because you are growing market share, and we keep growing market share year after year. So we have a very good share performance driven by the GDBs. So this is quite good.

In terms of the financial profit on a constant basis was up 1.3% and EPS almost 4%. If you eliminate transactional costs would be 5.5% to around 8% EPS growth. So I think that those numbers are quite sound. I'm very happy with the performance in the first half

Q: And the GDBs are 44% of your overall portfolio and rising. Did all five contribute to this performance?

A: Yes. One of the main reasons that we have had a good performance in the first half is the performance of the GDBs. As you know, we keep talking that our strategies should drive our premium portfolio through the GDBs. And it is working. The GDBs' share was up 80 basis points in the first half of the year with volume 6% up. If you consider that the industry is declining around 3.5%, 4%, as I said before, is an outstanding performance.

And all the brands are contributing to that. Dunhill, for example, if we look at Dunhill performance in places like Brazil, in places like Indonesia: fantastic. If you look at Lucky Strike is doing very well in Americas, Western Europe. You look at Pall Mall, doing very well in Americas, in places like Pakistan. The same is happening with Rothmans. Kent is the only brand that has a slight decline in volume because the industry has declined - the markets which Kent is in are very strong like in Russia and Ukraine. As I said, the GDBs and the overall market share is a good indicator of the underlying strength of the business. So I think that we are doing quite well.

Q: How would you describe the pricing environment?

A: The price environment in the first half of this year has been solid, has been better than last year. We had the price mix of the first half around 5.3%. And if you compare to the first half of last year, that was 3.1%. It just shows how strong it is. We still have some competitive pricing in some places in the world, such as Australia, driven mainly by the growth of low price segments. There are several reasons for that. First, the industries launched some brands there, and second, we see a widening of the price gaps in the market because of huge excise and price increases in the markets. But overall, I think that we have a very solid environment. I'm very confident for the second half of the year as well.

Markets

Q: And how did you perform across your markets?

A: We have done well across the patch. Let me talk a little bit about the four regions. I think that you'd be better to give an in-depth explanation. Asia-Pacific, we have grown share. If you take the 11 top markets in Asia, we have grown share in 10 out of the 11. And the other one, we are stable. So a fantastic performance - , good growth from a region that has been affected by the devaluation of currencies as well. But very good performance overall, very happy with the investments that we have made in Indonesia and Philippines and Indonesia. Dunhill has been growing quite strongly, volume growth, share growth and good profit delivery for the brand in Indonesia. So very happy with that.

We go to Americas, good performance across the region. Take Brazil, for example, Dunhill now has 12.8% market share. It's a record market share for Dunhill with a premium proposition in a market that you see a polarisation, we see a decline in terms of consumers trading down, but at the same time driven by our innovation we see consumers trading up. So we are doing quite well. Mexico, fantastic performance in terms of volume, in terms of share, in terms of profit. So the region has done quite well, very good, strong, very good and strong pricing.

You go to EMEA, has been affected by the devaluation of the currency in Eastern Europe, but the business is in a good shape. Turkey is doing very well. Russia: we are growing share as well. Ukraine: we are doing very well. So across the region, we have some very good performances.

And finally, Western Europe, which I said at the end of – at the beginning of this year, when we were reporting full year's results, share wasn't stable. Yes, share isn't stable in Western Europe. I think that you are setting the basis for very good growth in the second half. Price is strong in Western Europe as well; that has helped to deliver the profitability for the region. So overall, I think there has been quite a good performance across the patch.

Q: You talked a little bit about down-trading there. Is the down-trading that you saw last year still continuing?

A: We see some down trading in the world, yes. Overall, I think that we've seen some down trading. I think that the low-price segment is growing a little bit faster than the premium. But what we saw as well, we see growth in the premium segment for BAT, and the reason for that is that our leadership in innovation is helping us to give a reason why for consumers to trade up. So in several places in the world, we see the premium segment growing, in places like Romania, in places like Brazil, in places like Indonesia through our Dunhill brand. So we see some markets with polarisation, some markets down trading, some marks up trading. But I think overall, of course, the value for money segment, the low price segment, have grown faster than premium.

Acquisitions

Q: Now, there's been a spate of M&A activity. Can you give me the rationale behind your recently announced deals? And shall we expect more over the next 12 months?

A: Well, we have been very active, because, you know, these deals, they'll take a long time to come to fruition. And I always said that we are keeping a conservative balance sheet in order to be able to make some acquisitions in the market. And they happen. We had the Reynolds America announcing that they had approval from FDC. We invested \$4.7bn in Reynolds America to keep up. We've got a 42% share. And we have 42% share in a much stronger company. We've an outstanding brand portfolio. So I'm very happy with that.

We have Brazil, we are going through with CVM, with the documentation to formally launch our offer in the second half of August for the remaining 24.7% shares that we don't own. So let's see how it goes. We have the TDR deal that we announced recently, which gives us very good position in markets that we are not so strong.

We have leadership in markets such as Croatia, such as Bosnia, and very good share position in some other markets, such as Serbia. So very happy with those deals. So I think that, as I said, if you have an opportunity out there, you'd be competing for that, and you have been successful so far, and I see some good opportunities out there. We need to see how things are going to evolve, but you'll be competitive.

Regulation

Q: The plain packaging is being considered across a number of markets. Do you think it's had any effect in Australia?

A: Well, I have said this before, the plain package in Australia was implemented in December 2012. If you look at the results of 2013 and 2014 and the first half of 2015, you'll see it has not achieved the public health goals that the government set for themselves. What we saw in Australia is some down trading, but I don't think that it was caused by plain packaging. This was caused by significant excise increases that demanded that we increased prices at the same proportion. And you look at the significant price increase that you have in 2012 and the decline in volumes similar to the one that you are seeing in 2014. But look at average daily consumption, and smoking rates in Australia. We have no evidence that has accelerated after the introduction of plain packaging. I keep saying that it's an ill thought regulation and we're going to fight it.

Outlook

Q: What's the outlook for the second half?

A: Well, I think that you're going to have, as I said as well, a better second half than the first half. One of the reasons is that the price environment is solid, but also the comparison against the 2014, second half 2014 is more like the like. So I expect a much stronger second half on top of very good H1. So we are on course to deliver very, very good results for our shareholders on a constant basis. I'm very confident of that. I think that the market share gains that we have shown, the growth of GDBs and the operating margin delivery, because operating margin for BAT in the first half has been stable despite the significant transactional forex that we have in our numbers, it just shows the strength of the model that we have. So I'm very confident for the second half of the year.

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