



## British American Tobacco – Interim results 2016

### Interview with Ben Stevens, FD

#### Earnings

**Q: What are the financial highlights to these half-year results and how do they compare to the same period last year?**

A: Yes, these are an extremely good set of results. Not only is volume up, share up, the Global Drive Brands up, but our revenue has increased at constant currency rates by 8%. Our operating profit, if you take out the effect of transactional FX, has also increased by 8%, and our earnings per share will be up by 11%. So we're very, very pleased by the first half of this year.

**Q: How much of an impact has the volatility in the FX markets had post-Brexit, and will this alter your guidance for the FX over the full year?**

A: We had a 6% transactional headwind on operating profit in the first half of the year, and our major currencies haven't moved that much against the dollar and against the euro, plus the impact of hedges of course rolling off. So it looks like we'll have something like a 6% headwind from transactional FX on operating profit for the full year in 2016.

Things are a little bit different in terms of translation, where sterling is important. So because of the recent weakness in sterling, where we faced a 4% headwind on translation in the first half of the year, it looks like this will turn into a tailwind for the full year on operating profit of about 4% and at earnings level, probably around 6% tailwind for the full year 2016.

#### Margin

**Q: How much of an impact has transactional ForEx had on margins and what's the outlook there?**

A: Obviously, if you're facing a transactional FX headwind, then that's very difficult to grow operating margin, and we've seen that in the first half of this year. But the good news is that the underlying operating margin continues to grow, so we expect that by the time you've taken out differences in the nature of the business from the mergers and acquisitions that we've done during the course of the year and taken out the impact of transactional FX rates, our underlying operating margin has grown by about 50 basis points in the first half of this year.

**Q: Now you've largely completed the rollout of your SAP system. What's left that will still drive margins then going forward.**

A: Yes. We've still got to deploy SAP in Indonesia and in the new acquisitions in the Balkans. There's still a little bit more deployment of SAP to come, and we expect to go live in those markets on the 1st of January next year. Then of course, having deployed SAP, there's a lot of value we can then build into our shared service centres. So we're just starting, for example, building HR shared services on top of our financial shared service centres. So quite a lot to come in terms of the rule-based activity in BAT that we can put into our shared service centres.

And of course, there are other areas where we're looking to improve margin, as well. For example, in our factory footprint, where we've made some announcements recently.

#### Balance Sheet

**Q: Now the dividend payout ratio is creeping up. Will that continue?**

A: Yes, we've always said that the priority for us in terms of balance sheet usage is the dividend. We like to keep the dividend ticking ahead, even when we're facing a big FX headwind, which we have done for the last few years, and that's led the payout ratio to grow over the years. Now, as we see an FX tailwind coming, we've always said that we expect to pull back slightly on the payout ratio and return to what we see as a long-term sustainable payout ratio for the dividend, which is 65%.

#### Outlook

**Q: Given the strength of the business and the volatility within the currency markets, how do you view the financial outlook?**

A: Well, of course we delivered a very good set of results in the first half of the year, despite facing a 6% transactional FX headwind. That FX headwind will continue in the second half. But despite that, the business is performing extremely well, volume is growing, share is up and the Global Drive Brands are really driving the performance of the business.

Now, we've got some quite difficult markets, places like Brazil, Malaysia, pricing in Australia, so it's still a tough external environment out there, but I am confident that we will have a good set of results in 2016.