

# Deutsche Bank Global Consumer Conference

Fireside chat  
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## CORPORATE PARTICIPANTS

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*Chief Executive*

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*Finance Director*

## DEUTSCHE BANK MODERATOR

**Gerry Gallagher**  
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**Gerry Gallagher, Deutsche Bank**

Thank you everybody for joining today's presentation by BAT Senior Management at our virtual Paris Global Consumer Conference.

My name is Gerry Gallagher and I'm a member of Deutsche Bank's consumer team in London.

It's my very great pleasure to introduce the Senior Management Team of British American Tobacco, being Jack Bowles the Chief Executive Officer and Tadeu Marroco the Finance Director.

In terms of the format of today's fireside chat, I'll hand over to Jack in a couple of minutes to start with some opening comments. I will then take the floor to ask a series of questions to Jack and Tadeu, which will take us through to maybe 25 minutes.

I'm going to keep my comments relatively high level and strategic. Tadeu has already held a call on today's trading update which some of you I'm sure listened to. And I'm sure when I open to the floor I'm going to get some questions on this morning's release from those of you who are listening in.

On that, as I say after about 25 minutes I will offer the call out to you guys to ask your questions. You can ask your questions via typing into your web link which you are all logged into at present. I'll ask those questions on a non-attributable basis, so please don't be shy in terms of asking the questions.

And finally at the end of the presentation, at the end of our time I will hand back to Jack for some closing comments to finish off our time together.

So before we start, in terms of my questions, I'll hand over to Jack for his opening comments, Jack.

**Jack Bowles, Chief Executive**

Yes, good morning Gerry, how are you? We are there with Tadeu and Tadeu had a call already this morning where we demonstrated that we are resilient and growing. We adapt to the new environment and we invest in our business. So we grow revenue and we grow share.

The business is performing very well and our share performance demonstrates that. We are growing share year to date in every category and in every geographical region that we have.

But for the COVID we would be hitting all the guidance we gave at the beginning of the year.

There is of course coming up a very clear differentiation between developed markets and emerging markets. It is a very good situation to be in when we have 75% of our business that is in developed markets, including the US, where there is far more stability.

The total 3% impact on the top line that we see due to COVID cannot be fully offset. But we are doing a lot to mitigate it, especially on the cost base.

We could have maintained our earnings guidance, but that would have meant doing the wrong thing for the business. We prefer to invest in the business and we do not want to not invest in the business. So we are continuing to spend in the business, combustible and New Categories together, because we want to exit this crisis stronger than we entered.

So our confidence in the future is demonstrated by our maintenance of the dividend moving forward for 2020.

So Gerry, thank you very much for the possibility of the opening.

**Gerry Gallagher, Deutsche Bank**

Thanks very much Jack. So I'm going to start with a very big picture strategic question. Your purpose, and I'm quoting here, 'your purpose is to build a better tomorrow, by reducing the health impact of your business through offering a greater choice of enjoyable and less risky products for your consumers.'

Could you talk a little bit about how that is changing how the business is operating on a daily basis and how the people you employ go about their daily roles?

**Jack Bowles, Chief Executive**

Yeah I think that sense 18 months now we have put a new corporate purpose in the company. I think it has resonated very well, very well with the employees, very well with our consumers and also very well with the financial community.

But the more important thing is about the refreshed strategy and the fact of the sustainability moving forward for the business.

There is a harm side to the products that we sell and this is our key social impact at the moment. And that is why we are aiming for 2030 with very clear goals of 50 million of non-combustible consumers by 2030. We are already at 10 million and that's very important that we continue to do so.

Now in order to do so we had to reengineer, reorganise the company, which we did through the first phase, phase 1 of Project Quantum. But also in bringing new capabilities to the organisation, we hired more than 300 managers in different categories and in different capabilities in order to support that.

So having a clearly purpose is very important for the external world, but also for the company inside. We are able to better recruit and to better continue to deliver.

It means a lot of resource allocation, we have invested £500m more last year and we continue to invest normally this year. And it means that we need the money from the combustible business in order to fuel that investment. We are taking some positions, as I said earlier, we grew in all categories, we strongly believe in the multi-category approach and we will continue to develop our business moving forwards.

**Gerry Gallagher, Deutsche Bank**

Okay thank you. I think you've touched on - I've got a follow up to that, but I think you've touched on the answer to my following question which I'll ask anyway in terms of the investment on the combustible side, how your new purpose reconciles with the priority for combustible growth?

**Jack Bowles, Chief Executive**

Yes, thank you for this question because what differentiates us very clearly is that we consider that the combustible business is a very important building block of the company, BAT. We have a new purpose and we are taking the development of New Categories very seriously.

In order to fuel that growth you have to have the resources to invest in the New Categories. And they will not disappear overnight, these combustible products. So it's essential that we manage them responsibly and that we make the organisation accountable for their development.

It's not one size fits all, it's combustible plus New Categories. And we strongly believe and demonstrated that we can get 10 million consumers on top of that. We strongly believe that New Categories is multi-platform approach, because there are different consumer moments and different consumer satisfaction parameters. So they go hand in hand.

**Gerry Gallagher, Deutsche Bank**

Thank you Jack that's very clear.

I'll just move on to looking at New Categories and your Beyond Nicotine strategy. So is there any change in your level of conviction around one size does not fit all markets in terms of New Categories? And where does your Beyond Nicotine strategy fit into your overall strategic thinking? And how does that work in terms of how you look to allocate capital?

**Jack Bowles, Chief Executive**

Yes, it's a very broad question Gerry. To start with we believe in multi-categories because the consumers tell us so, it starts with the insights. And the insights tell us that there are different levels of satisfaction required by consumers. There are different geographies. And we have created some systems, some market typographies, some regulatory regimes,

so excise and other factors systems to put that into our MAPS system, which we call MAPS system. And that allows us to separate the different markets and to separate the different categories.

I must say that if you were not to be in e-cigarettes in the US, then you were not be present in the New Categories. If you were not to be in e-cigarette in Europe, then you would be missing a big part of the development of New Categories. If you were not in Japan in THP, you would miss a big part of the development of the New Categories. If you were not in oral tobacco, Modern Oral, you would not be in Scandinavia and in emerging markets where we're doing some developments.

So I think what is important is that we consider the fullness of the offers that we have to give to the consumer, that we get the right insights and we are the only ones to have insights on the four categories and to get really the understanding of the consumer moments.

I think it is very important to realise also that in the last nine months the New Categories, and it is the right investment for the future, the new categories have slowed down their pace of growth. But that's okay, because we have to build brands; we have to transform our business moving forward. Take the money from the combustible business, investing enough in our combustible business and tuning the investment for New Categories.

And we will explore further in all - in terms of further than nicotine because that is the right thing to do and the way to go for the business moving forward. We have to continue to explore. We were the first one in multi-category; we will be the first one going forwards.

But that is a long time down the track. Let's focus on what we have, a very strong combustible business, we are growing share and value share in all our different regions. We are doing extremely well in the US. And we are growing share in all our four categories. A slower growth rate in 2020, but we are continuing to grow and we will continue to invest.

**Gerry Gallagher, Deutsche Bank**

Thank you, I'll just move tack now a little bit and talk about markets generally, pricing and down trading a little bit. Now it could be the case that in a lot of your markets and not just tobacco, but staples in general, that inflation may be a thing of the past and that was the case prior to COVID and COVID may exacerbate the lack of inflation around the world.

So could you talk a little bit around your thoughts about pricing resilience for the remainder of this year and beyond, and the risk that even if there is pricing, because of the macro backdrop the consumer trades down and the price mix trade off maybe isn't quite as positive in the future as it has been in the past?

**Jack Bowles, Chief Executive**

Yes. I think it's a very important question and that's more of a forward looking question, but let me tell you where we are since the beginning of the year. More than 70% of the pricing is done now for the year. We still have some important times during the summer, but we see a very strong pricing environment.

The second thing is we see that the most important parameters are in terms of consumption, we see no reduction, no significant reduction, in terms of ADC, average daily consumption, we see no significant reduction, we see no significant down trading. It is more of a new normal which we have to adapt fast to.

The world is changing and it will be more for New Categories and it will be more for new consumer moments. The people, the consumers - it's all starting with the insights - the consumers will live a bit differently.

Now, in terms of the absolute pricing levels, you have to remember that tobacco is a category where the price gaps are extremely small. In the majority, when you have other FMCG it tends to be two or three fold, in cigarettes you have 20%, 25% maximum top to bottom of the price range.

And the consumers are looking for brands, they are looking for their flavours that they know, they are looking for their brands and their satisfaction. And mostly they are sticking to their brands.

Take the example of the US, our premium share is growing, our market share is growing, our ASU 30 share of beyond 21 years old is growing. When we have a record share of 35 share points in the US, we have 45 in consumers above 21 years old, because our brands are strong. When you take Newport for instance, 15 share, it's a record and it is growing and that is creating our value share growth in the US. Our premium share is growing.

So I think that when you have strong brands in an environment where consumers buy their products nearly on a daily basis, I think that with the right marketing, the right capabilities and the right support to the combustible business you are there.

Of course on the mid-term you can never avoid the fact that some governments will have some, I would say, radical approaches in terms of pricing or in terms of taxation. Nonetheless at the end of the day the governments now know that there will be a significant increase in illicit, which will generate a reduction in their revenue. So they know that they have to go step by step and that the regulatory framework has to be discussed with the industry in order to have the right balance.

So I think that all in all as we speak pricing is good, as we speak price mix worldwide is good and as we speak there is more pricing to come for the second half of the year. We

have to be reasonable and expect some skirmishes towards the second half of the year, but we think we can navigate that and all the signs are for the time positive.

**Gerry Gallagher, Deutsche Bank**

Okay, you've touched on the next question I had which was excise shocks. From your answer there Jack, I take it - it sounds like you're of the view that governments understand the potential negative revenue implications for them of being aggressive on excise. Is it your view that although governments may be under fiscal pressure moving forward because of COVID-19 that in general they understand the trade-off they have to work with and the likelihood of excise shocks with the knock on to illicit trade is probably unlikely, is that what you're trying to say?

**Jack Bowles, Chief Executive**

There are two schools of thought on that Gerry. One is when you have an excise increase that is related to a fiscal revenue objective then they do understand that it is by steps that you have to proceed and go progressively because that works well in all the examples we have seen historically.

When it is for another reason, like for instance in Indonesia at the moment, where there has been a 30% increase, then you see a collapse of the market, a very radical inflection point in terms of the market, because it is impacting all the different price tiers in the market. And it is impacting the consumers in a developing market where the available income is not so high. Because when you go back for instance to the US, you see that the pricing elasticity is very good, the absolute prices in terms of cigarettes are low compared to available income, the same that you have in most developed markets. It is more when there are some extreme cases like in Indonesia.

Interestingly enough now if you take another developing market, which is Brazil, where you remember that in the last few years the government has taken very important excise increases, it has made the market collapse by close to 50%, the legal market. But the consumption remains, 50% of the market became illicit.

And by the way now that with COVID the border with some bordering markets like Paraguay are closed suddenly the market of Brazil, which is a very sizable one for us, is growing by 7% volume wise, for the industry, since the beginning of the year.

So illicit is a big factor in all of this and the governments know that.

**Gerry Gallagher, Deutsche Bank**

Thank you. I'm just going to touch on a theme that came out of today's trading update and the call Tadeu hosted earlier on today.

Can you talk a little bit about the different impacts that COVID-19 is having on developed markets and emerging markets, the differences there and maybe the outlook for some of

your key emerging market businesses operationally given the potential macroeconomic legacy of COVID-19 maybe greater in emerging markets than developed markets?

**Jack Bowles, Chief Executive**

Yes I think it's - and maybe Tadeu can complete the question later. What is very important is that 75% of our revenue is in developed markets. As I said earlier in developed markets we do not see down trading acceleration. We do not see a reduction of average daily consumption. And we see more of the new normal. Mostly the outlets are open and the access to the product by the consumer is there.

In emerging market representing 25% of our brands, you know - it's the laws of the average that works. There are countries like South Africa where the sales - the ban is remaining in place and the consumption is down 29%. But even though the consumption is down 29%, 100% of what is consumed is illegal.

So the illegal players in South Africa are really owning the market. It is very strange to see that in South Africa there is a total ban on tobacco sales for more than six weeks now. And apart from a production that has been recently partly reopened for export only, it has driven down completely the legal market.

Products are there everywhere, our products, in the factory, in the retailers and in the wholesalers, but they are not allowed to sell them - six weeks. So we have sued the government in South Africa in order to change that situation. So that's one case in terms of implementation of the ban that is in South Africa.

On the other side there are countries of course like Brazil, as I just said, where you see that the volume is increasing because the borders are closed and the illicit is now possible.

In other markets like Argentina for instance we have taken the option to reorganise our portfolio completely and to shrink our portfolio and to make sure that the supply chain is working full blast.

And by the way I would like to take the opportunity to say that by utilising all our supply chain it has allowed us to be much more reactive and much more efficient in the delivery of our products worldwide, moving even products from country to country, or even shops to shops in order to make sure that demand and the supply were met.

So I think that there are different cases in emerging markets. What we have to see is at which phase they come back online and it has impacted our total volume; but far less our revenue, because as I said, 75% of our revenue is coming from mature markets. So a plus and a minus in the emerging markets, but I think a strong position and a strong development thanks to the great capabilities that we have in more than 180 markets.

Tadeu, would you like to add something?



**Tadeu Marroco, Finance Director**

Yeah, the point - and I made it in the morning as well, that is important to bear in mind is that the volume drop that we see in emerging markets is not driven by recession; it's basically driven by the lockdown.

When you go to markets like Bangladesh for example, Malaysia, stick sales are very important. And then you have curfews and you have a very stringent enforcement in terms of lockdown. So the consumers they just cannot buy the product.

And then you go to Vietnam - and in a number of those markets it is a very social event the consumption of cigarette. And all of a sudden you have all the pubs, HoReCa, which is the big channel of consumption completely shut down. This impacts that.

So what we are doing is we are gaining share in all those emerging markets, we are trying to be as agile as possible whenever this lockdown eases and that's the reason why we are gaining share. But overall the impact is in the volume declines that we are seeing.

**Jack Bowles, Chief Executive**

Emerging markets, you know I mean they represent 25% of our revenue, but they represent more than 50% of our volume. And we are growing share, as we said this morning, we are growing share significantly, close to 50 basis points, it's massive, it's the best share growth that we had in a long time. And at the same time we are growing value share.

So we are taking the opportunities where they are, we are investing in the business and we are driving our business out with the right balance between us, cutting costs and investing our money and balancing the investments within combustible and our New Categories.

Always remember what we said earlier, which is the emerging markets it not about recession, it is about the lockdown effects in terms of limitation of distribution. That is where we stand today.

**Gerry Gallagher, Deutsche Bank**

Okay, understood, thanks very much. I'm going to move tack to the US; I'm going to ask a general question here. And I'm conscious that today's trading update and the very positive comments you made around the US market and more importantly your position within it, maybe makes this questions redundant, but I'm going to ask it anyway.

Immediately after you acquired Reynolds American within a matter of days the proposed - the proposed - I used the word proposed deliberately, the regulatory environment changed potentially quite a bit. So with that in mind and ongoing debates around regulation in the US I'll ask a simple question. Was the Reynolds American a good deal - the Reynolds American acquisition a good deal in your view?

**Jack Bowles, Chief Executive**

It's a very key answer and the answer is yes. I mean of course the US market, I mean you cannot be a truly international company if you're not on the US to start with. Two, there is a lot of consumer spend in the US and the affordability of products in the US is good. The price elasticity is good in the US.

We see that there is a regulatory framework that people maybe misunderstood some time ago with the FDA. Remember the FDA has to have an impact in terms of the health of the population, so they will go step by step and they will go scientific evidenced based. So it takes some time.

So it is a very, very strong market and a market where if you want to be truly international you have to have your presence. We have a strong company in the US, we are growing share since the acquisition, we have just hit 35% share, which is the record ever for our company in the US. We have 10 share points in ASU 30, which we consider above 21 years old. We see that the pricing environment is doing well, we grow share, 10 bps, we grow value share and we have a very strong portfolio.

We are the only ones that do not see down trading, which is good. And of course we see strong potential for the future the US market.

Will there be some skirmishes? Yes. But even on the regulatory framework, you know, even when the FDA speaks about pictorial involvement they tell you one year before because they want to have the time to get the engagement right and to make sure that everything is okay.

We are speaking about PMTAs for e-cigarettes; it has been in the pipe for two years and more. And we will have the right discussion and the right possibility for the companies to put the full spectrum for scientific data, consumer data, marketing data that will allow the FDA to the case here.

So I think that I like the environment in the US because the environment in the US is consumer centric, it is with a positive regulatory engagement environment and it is with a very strong prospect for the future. And the market has been very strong since the beginning of the year.

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**Gerry Gallagher, Deutsche Bank**

Thanks Jack. I'm going to follow that up with an additional question on the US given that we're there and relating to today's trading update. The H2 comps in the US are getting easier, it just makes me think - is your revised guidance for the US market volumes being

down 4%, against you previously saying 5%, may be a little bit too conservative on your part given, you know, easier comps in the second half and the market being down 2% to May?

And in addition to that, if I think about you guys specifically, now you talk about, you know your share being at 35% now and very importantly your share growth being driven by, you know, very high margin and Newport and Natural American Spirit. So to what extent perhaps on the spectrum of conservatism to bullishness that maybe you're leaning a little bit towards the conservative side for the outlook for the US business?

**Jack Bowles, Chief Executive**

You know Gerry it is very important and it's a very good question. What we want to make sure is that we have the possibility to look at the US market, with all the different parameters. And what we have seen in Q1 in the US market is a very strong market, because there was, of course, some activities related to the price increase.

Then of course in Q2 you see some positions that are taken in terms of stock build for potential price increases. So - plus you have a slowdown that has been since Q4 of last year in terms of the growth of the New Categories which has taken less away from the combustible business.

So I think that these three parameters put together gives us a better outlook than what we said a few months ago. Yet, you always have to consider in the US that changes are quite radical and quite - as you said the margins are very high, quite impactful. So I prefer, like the overall approach that we have for our guidance and few companies are giving guidance at the moment, but I want to give guidance in order to be able to help you guys to better navigate that market. And that guidance is prudent.

And we should do that because what we want to do is both at the same time give some clarity in terms of our business, but also give us some space to invest in our business because we think that it is a big opportunity at the moment. And as you saw in our results this morning, we are growing share 50 bps, that's the record for BAT, we are growing share in the US also and we have a record share of 35%. We are growing value share worldwide and in the US. And we are not impacted by down trading.

Apart from lockdowns we do not see for the time being some recession. But there might be some skirmishes in terms of taxation and things like that. And I prefer to be on the prudent side. My objective is to drive the business; it's to be able to invest in the business without chasing numbers. And I want to make sure that after the good year that we had in 2019 we can continue to invest in 2020.

I'm increasing my marketing spend in 2020, it is different in terms of allocation, we do a lot of resource allocation, but it is the right way to go. I have a more agile organisation because of Quantum that we've done and I saved £300m, that gives me flex, and I think

that is the right thing to do in order to continue to accelerate, both on combustible and on New Categories.

**Gerry Gallagher, Deutsche Bank**

Great thanks very clear. You mentioned Quantum there and I'm conscious Tadeu is on the line and I want to make sure that we have a chance to engage with Tadeu, so maybe this is one for you Tadeu.

Could you just expand a little bit on Quantum for us and its aims to make the business simpler? And what opportunities a simpler business provides in terms of top line and bottom line? And can you talk us through maybe one or two examples of what you mean by making the business simpler through Quantum?

**Tadeu Marroco, Finance Director**

Yes sure. The backdrop for all that is the fact that we need to be closer to the markets and have to be more agile, faster and more empowered because have new competitors that didn't even exist five years ago. So the environment is much more dynamic right now.

So Quantum was created to address that need of BAT. So the phase 1 of Quantum was all about our organisational design, it was about delayering the company, creating the empowerment that is necessary, easier - the decision maker. And as a consequence we reduced the numbers of direct business units, we used to have in the past 36 business units, today we have 18. And this creates clearly more agility, more decisions closer to the action in the markets and more empowerment.

We moved a lot of activities out from the end markets, leverage in the investments that did years ago in how, rolling out SAP across the Group, in a manner for them to really be focused on customers, in terms of consumers and not doing transactional activities at that market level.

We were able to move 2300 people out of the organisation, but we also hired 300 new managers, bringing new capabilities that are needed, new capabilities to support the digital journey that we are going through, like e-commerce, but also science, IPs, innovation in general. And as a consequence of that phase 1 basically brought £300m that will be very helpful in a tough year like the one that we are living through.

The Quantum 2 phase is about operational efficiencies, route to market focus, the leverage on technology as well and a lot of supply chain productivity initiatives. And this will guarantee that we continue with the cost agenda programme, not just in 2020, but also in 2021 and 2022. By then we aim to achieve £1bn, like announced in the CMD back in March.

**Gerry Gallagher, Deutsche Bank**

Thanks very much for that. Tadeu maybe sticking with you for the next one and I'm going apologise, I've got a bee in my bonnet about this, so forgive me, and forgive me because I may be completely down the wrong track, but I'd just like your insights on the following question. And it's about how as the business develops and moves towards New Categories and perhaps more towards vaping being increasingly important and dominant in the business over time, the question is how should we think about dollar per customer and percentage margin per customer in vaping compared to combustibles?

Now the question I am asking is there will be an impact from device sales on the maths I assume on the basis of maybe devices being sold at or near zero gross margin. So could we be in a position one day where BAT and for that matter other players in the industry on a per customer basis have percentage margins downwards, but on a dollar margin per customer margins are actually improving, and although the makeup of the percentage margin structure of the P&L may change, optically to the negative the actual quality of the business has improved?

**Jack Bowles, Chief Executive**

Maybe before Tadeu takes the second side of the question, I mean I think that what you have to remember always is that consumers are spending money today on combustible products and they are paying within that price 60% on average in terms of tax. So these taxes do not exist in these New Categories. They are there, but on the lower percentage.

Then the second thing is the margins for New Categories, trade margins are very high because it's very often specialised outlets. So it can go up to 70% in terms of trade margins. These margins for normal distribution are more around 10, or 15% depending on the different countries.

So although the consumer has to pay more taxes when he uses combustibles, he still pays the price and the disposable income is there.

So I think there is a lot of space for margin in New Categories. You will have more platforming, you will have more volume, you will have more volumes going from open systems to closed systems and you will have normal distribution channels and you will have internet sales that will grow. And by the way since the beginning of the year we have doubled our internet sales on New Categories.

So I think that there is a lot of opportunity for margin improvement in our business. But Tadeu I'm sure you'll want to add words on that.

**Tadeu Marroco, Finance Director**

I think I would just add to what Jack said in terms of margin improvement opportunities the cost of goods sold as well. There are a lot of opportunities to automate what we have today and take a lot of cost out.

But independent of the margins because we get very obsessed when you compare with specific margins, but just on your question around the dollar per customer. If we were to migrate all our cigarette consumers in some markets that we had today, take for example the UK, where we have a portfolio which represents 10% more or less of the market in a very more low base, low price base and if we migrate them all to our vapour products, actually we make more money out of that.

So the key point is about how you keep the loyalty of these new consumers in your system. And that is why it's so important to invest in terms of differentiation, in terms of brand building. And that is why we are migrating now from Vype to Vuse in a number of markets. We have just started in Canada; we have clearly you know all this ambition to create powerful brands, not just in vapour but in other categories, in New Categories as well, like we did in cigarettes. And this together with a very powerful pipeline will create the ground for us to work on the margins and have a very profitable business moving forwards.

#### **Gerry Gallagher, Deutsche Bank**

Understood.

#### **Jack Bowles, Chief Executive**

Gerry if I may, it always starts with the consumer and if you understand the consumer logic and the consumer segmentation then you're getting much closer. The satisfaction index study we showed at the Investor Day is a clear example of that. Different products cover different needs for consumers. So you have to have a multi-product, a multi-platform offer to the consumers. They are spending the money on the combustible business as we speak and we can improve our margins on the New Categories and we can create some strong brands.

Even if you look at today, you know you have more e-cigarette smokers in the US than any other category. Even the Modern Oral category that we were all excited about, you see that it is only 0.8% of total nicotine in the US. So it's not that dramatic, so let's give it some time, get it going in the right way.

In Europe for instance you see that e-cigarette is the number one category of the industry by far in terms of the number of consumers.

And in some countries like in Japan, which is - Japan and Korea still are 60% of the THP business worldwide, you see that THP because of regulatory reasons and very, very low tar and nic products in cigarettes THP is the winning category.

And I would like to take the opportunity to speak about our new launched products which is the Hyper product that we've just launched, which is bigger in diameter, which is with 33% more tobacco for satisfaction, which has capsules and which allows us to be present in 91% of the market. Despite all the COVID and the limitations of distribution we

launched six weeks ago and we have already 50 bps in terms of market share. And we are going to do some slow launches in Russia and in Italy and in other markets, you know, to test the waters.

You know my way is taking the time to understand the consumer, testing the different profiles and the different platforms and then going there. So I think that there are very clear examples around the world that you need different platforms in order to be successful.

It is taking more energy and more time, but it is the right way to go for the future. That's what we think. And we are growing share in our combustible business because we focus on it. We are growing value share in our combustible business because we focus on it.

And we are growing market share on our New Categories because we put the right focus and we investing in building brands and having the right consumer offer. Then we do a pilot, then we launch, then we accelerate.

#### **Gerry Gallagher, Deutsche Bank**

Great thank you. I'm conscious of time, I'm going to ask one question and then I'm going to leave it for you to make some closing comments Jack.

Just on today's trading update and the move of the £5bn New Category revenue target to 2025 from '23/'24. Now a lot of that I presume is down to activation being on hold because of COVID and that may last for some time, but could you just talk a little bit about that and put some flesh on the bones around the influence of the US market on that changing guidance, as well as COVID? And also whether we should be thinking about any shifts between Vapour, THP, and Modern Oral within that £5bn?

#### **Jack Bowles, Chief Executive Officer**

Tadeu will add to my comments. I think what is important is you're speaking about the proportionalities between THP, Vapour and Modern Oral, I think what's important is to keep our minds open to the fact that there are regulatory frameworks that are different in different places. There are taxation systems that are different in different places. There are consumers that are used to high tar and nic products, definitely Japan is 3, the US is 16 and Europe is 10 now. So you need different products to satisfy the consumer.

What I think is important is that we have the possibility to serve the different consumers and it takes a bit more time. Because what we learn in our business that is the industry that we are in for decades is that the regulatory framework has an influence, or that small aggressive competitors that want to do shortcuts in terms of regulation or product stewardship. They slow down the industry.

So in some cases it is some companies that are doing, you know, excessive loading in terms of nicotine in their products like in Russia for instance where we stopped selling because we wanted to have the right level of nicotine in the products, so we are a reasonable company. In some places like the US it means the underage usage. And in

some other places it is about having first the right regulatory framework in place so that that category can develop on the mid to long term in a more consequent and consistent way.

So we have learnt in the last nine months that it is taking time to have all these stars aligned. There has been crisis in the US, there has been crisis in Europe, there has been crisis in Japan and phases of development of the different categories. It is better to do the right job and to take our time.

COVID is clearly impacting the engagement capabilities that we have with the consumers at the moment. We will grow our New Categories in 2020, yet it will take a bit more time. So I prefer to be in the safer side of £5bn in 2025 in order to focus on the delivery of the business and to make the right calls for the business.

Tadeu do you want to add something?

**Tadeu Marroco, Finance Director**

Yeah and to speculate around the size of each by then is not very helpful at this moment. A lot can change. So for example we are now piloting Modern Oral in emerging markets in a different way of delivery, through sachets for example that could make it very affordable and competitive in terms of pricing, with no comparison between the other categories. And if we are able to reach the virtual barrier this can be massive. And all of a sudden all of the projections could change dramatically in the future.

So more important is the context, the space is right there today, there are 70 million already using these products like Jack alluded to, we have 10, 11 million out of those, so there is a still a lot of space to grow today and we will continue to grow in the future.

**Gerry Gallagher, Deutsche Bank**

Right, thanks very much. So I'm conscious of time, Jack I just want to hand back to you before any closing comments before I wrap up, Jack?

**Jack Bowles, Chief Executive**

Yes thank you very much Gerry. I think what's important to remember is that we're a strong business, we're a resilient business and we're a strong business. You know, not many companies give guidance at the moment and I find it important in order to help everybody to navigate in all these waters.

As I said earlier in the call, we could have delivered the guidance, but I prefer to have the flexibility to invest in the business and to make sure that we see the opportunities. We are both a company that is known in the combustible business and that is doing New Categories. In the combustible business, frankly speaking we are doing extremely well. We are growing share 50 bps and we're growing value share and that is a very good performance.



75% of our business is in mature markets and that is where the money is and that is where the money is going to be in the next two or three years. And the emerging markets - it is more due to lockdowns rather than recession. We don't see significant down trading at the moment, or significant problems in terms of the ADC, average daily consumption, or in terms of the consumption. It is mostly related to lockdowns and the recession. So we are a very, very strong company.

Now the environment is very unpredictable, but yet the business is performing very well. We continue to invest and that is the key of the call today - we continue to invest in our growth, both in combustible and in New Categories.

You'll remember a year and a half ago I gave three clear priorities and we are delivering on them; delivering value for combustibles, driving a step change in New Categories and transforming the business. That gives us the agility that we benefit from in the combustible business and also the agility and the possibility through our insights to operate in four categories in today's business.

So despite the challenges that we all face with COVID-19 I'm very excited by the future opportunities for BAT. We are clearly building a better tomorrow, we didn't speak about the vaccines, these are something that is very important to me. And also our confidence is reflected in our continued commitment to our 65% dividend payout policy.

So thank you very much and stay safe and stay well. Thank you very much Gerry, thank you very much to all of you.

**Tadeu Marroco, Finance Director**

Thank you Gerry.

**Gerry Gallagher, Deutsche Bank**

Thank you very much Jack, thank you Tadeu and thank you all for dialling in and listening to today's very insightful commentary from Jack and Tadeu. Thank you everybody and with that we will sign off. Thank you.

\*\*\*END\*\*\*