2021 Half Year Results

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Jack Bowles – Chief Executive

Good morning everyone, I am Jack Bowles, Chief Executive of BAT, and I am here with, Tadeu Marroco, Group Finance and Transformation Director.

We are very happy to be here this morning, to present our 2021 Interim Results.

I hope everyone listening this morning and your family and friends are well.

Today, I will provide an update on our strong progress towards building A Better Tomorrow and creating the enterprise of the future.

And Tadeu will share more detail on our performance in the first half, and outlook for the full year.

Today's results show our established multi-category strategy is working.

We are energised and committed to reducing the health impact of our business.

To achieve this, we want to encourage smokers who would otherwise continue to smoke, to switch completely to reduced risk alternatives.

We are clear that the greatest contribution we can make to society is to offer smokers a wide range of less risky alternatives to cigarettes.

We are transforming BAT at speed. To a high growth, Multi-category CPG, led by the consumer. Growing New Category volume, revenue and value and reducing our impact on public health.

This puts ESG at the core of our strategy. And alongside our other ESG targets. It means, we are creating value for all our stakeholders.

I am delighted that our established consumer-centric multi-category strategy has delivered excellent growth in the first half of 2021.

New Category revenue was up 40% at current rates and 50% at constant rates.

We added 2.6million New Category consumers in H1, our highest ever increase, to reach 16.1million consumers of our non-combustible products.

This was driven by our powerful global brands, Vuse, glo and Velo, underpinned by strong innovation.

We are leveraging our existing strengths and new digital capabilities in the business, and towards consumers.

ESG is an increasing core focus, building on over 20 years of activity.

In the first half, three of our factories were externally validated as carbon neutral.

We now have on-site solar energy at factories in 9 countries, with additional installations planned later this year.

We are delighted to have received further external recognition:

including, being named as the third highest ESG-rated FTSE 100 company, by Refinitiv.

And the Financial Times has named us both a Diversity, and a Climate Leader.

Our strong New Category revenue growth has been driven by all three brands, with Vuse revenue up 59%, Glo revenue up 38%, and Velo revenue up 63%, at constant rates.

We have clear ambitions for each brand. And we are well on track to achieve our £5 billion New Category revenue target by 2025.

Vuse is fast approaching global value share leadership in vapour. With value share in our Top 5 markets reaching 32% Year to date May, up 6.1 percentage points.

This is driven by value share gains across all top 5 markets, with Vuse now leader in 20 states in the US.

Glo continues to build strong momentum, following the successful launch of glo Hyper in Japan in April 2020, and its fast rollout across ENA.

glo's volume share in our Top 9 markets reached 17% year to date May, up 3.2 percentage points.

And we are accelerating our ambition to become global leaders in Modern Oral with Velo. Volume share in our top 5 markets reached 40% year to date May, up 2.8 percentage points.

Our Modern Oral products are now present in 23 markets globally.

Together, this progress has been driven by our strong growth in New Category consumer numbers.

Consumer acquisition in non-combustibles grew across all three New Categories. With our established multi-category strategy we offer adult tobacco and nicotine consumers a wide range of less risky products, to satisfy their needs during different moods and moments.

This is also reflected in strong Poly-usage growth across our brands.

I am particularly pleased that we added nearly as many consumers in the first half as we did in the whole of 2020.

This shows that our brand building activities and continued investment, with an incremental £350million invested in the first half, is generating tangible results.

And we are confident in achieving our 50million non-combustible consumer target by 2030.

Our increase in consumer numbers is translating into strong volume growth across all three of our brands.

Further accelerating the momentum from the second half of last year:

Vuse has maintained its rapid growth

glo has further accelerated driven by the success of Hyper

And Velo's volume has more than doubled in the period.

We are accelerating our transformation and building strong brands of the future with growing brand power scores.

We are building consumer-relevant brands, across the New Categories with ESG a core focus, as shown by the independent verification of Vuse as the first global carbon neutral vape brand.

This is powered by the continued rapid digitalisation of the whole business.

Which is being applied across all our New Category brands.

We now have more than 12million contactable adult New Category consumers in our databases, and this continues to grow.

As just one example, Vuse is now number one in branded search traffic across the Top 5 vapour markets

And consumer subscription numbers are up 63%, representing nearly 40% of Vuse own e-commerce revenue.

We are leveraging our new digital capabilities and further driving the digital transformation of our business.

While, of course, our focus remains on continued acceleration of our New Category business, we continue to develop further opportunities beyond nicotine.

Led by the consumer, our approach mirrors our established multi-category strategy, and will replicate the same BAT DNA that runs through our whole business.

We are targeting our 3 defined consumer spaces.

Creating an ecosystem of internal and external capabilities taking a collaborative, agile approach, leveraging minority stakes, partnerships and bolt on M&A.

Earlier this year, we also entered a strategic collaboration with Organigram a leading Canadian cannabis licensed producer, acquiring a 19.9% equity stake.

All this will leverage our combined expertise in broader plant-based science while also developing the next generation of adult cannabis products, with an initial focus on CBD.

We are also looking forward to exciting developments from B Tomorrow Ventures which we launched in 2020 it has already completed 13 investments, building an eco system across:

- functional products,
- health and wellness,
- science and IP,
- sustainability and technology.

As we have shown, BAT is changing rapidly, and with Quest, we are further accelerating our transformation to create the Enterprise of the Future.

Led by Tadeu, QUEST is our organisational and business transformation programme, with five pillars, that is transforming BAT into a truly multi-platform CPG, driving change through next generation innovations and new digital capabilities, and enhancing our future sustainability.

Through Quest we will accelerate the delivery of A Better Tomorrow.

Moving onto the financials. Our reported results reflect a translational currency headwind of 8% on EPS, masking strong growth.

To better understand the key drivers of our performance. We will focus on constant currency adjusted results, unless otherwise stated.

We delivered strong results in H1.

Excellent New Category revenue growth and good volume growth, which benefitted from a partial recovery in emerging markets drove Group revenue up over 8%.

We continue to gain volume and value share in combustibles demonstrating the strength of our brands and driving 5.4% profit growth.

EPS was up over 6% and would have been up over 8%, excluding transactional FX.

These results show we are delivering against our three operational priorities.

We are step-changing our New Category growth with a significant acceleration in H1.

Our continued strong Combustible value growth and cost savings are providing the funds to fuel this

And we are simplifying and transforming the organisation.

Tadeu will now provide more detail on this strong momentum in our business.

Tadeu Marroco – Finance and Transformation Director
Thank you Jack. In the first half we have delivered strong progress against the key financial focus areas I set out last year.

We have delivered over £900million of total savings from Quantum to date with the £1billion of annualised savings now expected 12 months early.

Together with the value from combustibles, this has enabled further investment to accelerate New Category revenue growth in H1.

We remain confident in reducing the losses from New Categories by the full year with a clear pathway to profitability by 2025.

This will be driven by maximising our marketing spend effectiveness, alongside scale benefits and a reduction in trade margins.

Cash generation remains a top priority, as we continue to invest in the business and de-lever the balance sheet.

We are on track to reach around 3 times adjusted net debt to adjusted EBITDA by year end.

I am delighted to say we delivered group revenue growth of 8.1% in H1. With Non Combustibles contributing 2.9 percentage points to group revenue growth, up from 1% in 2020. This represents around 1/3 of Group revenue growth in the first half.

Revenue growth from combustibles was strong with emerging market volume partly recovering against COVID impacts in the first half of last year.

Our combustible brands continued to drive both value and volume share gains.

Our price-mix of 4.3% reflected the geographic mix impact of the emerging market recovery.

The FX headwind on both group and New Category revenue was significant at around 9%.

Based on current exchange rates, we would expect a headwind to revenue of around 8% on a full year basis.

Our portfolio transformation is accelerating. 15% of our revenue in developed markets is in non-combustibles.

In emerging markets we have doubled the proportion to 4%, driven by the strength of glo Hyper.

In total, we now have around 12% of group revenue in non-combustibles, up 2 percentage points from 2020.

Vuse is approaching global value share leadership in vapour, with continued strong share growth across all key markets in the first half.

With our number 1 device volume share across all our T5 markets, we expect to continue to grow category share.

We are already category leaders in four of the top five markets and are approaching leadership in the US.

As we continue to build momentum and scale, we are very confident in our pathway to vapour profitability

Focused on three key levers of margin improvement: Trade margin, cost of goods and Marketing Spend Effectiveness

In the US, Vuse is now value share leader in 20 states.

Overall value share was up 5.1 percentage points to 30% year to date May, with an average of 30.9% value share over April and May, the leading share of device volume and consumable volume nearly doubling.

Vuse brand scores are ahead of our main US peer across key consumer attributes.

We are continuing to take share in a category that is back to growth, and represents 7% of total nicotine value share in the US.

glo Hyper, our first to world THP induction heating device, continues to drive share growth.

In Japan, around 60% of glo volume is already in Hyper, with conversion rates nearly double previous levels.

Since January, glo has been the only brand to grow volume share in the THP category, reaching 19.8% year to date May.

eCommerce traffic, revenue and social media mentions all grew strongly, a mark of the increasing digitalisation of our business.

Across these 5 markets together accounting for over 85% of our THP volume our consumables price is on average at an index of over 90 to our main peer.

In ENA, Hyper is driving strong growth across all key markets with glo volume growth outpacing category growth in the region by more than 6 times.

We are now in 23 of around 60 THP markets globally and are continuing our geographic expansion.

As Hyper rapidly generates scale, we can begin to drive down production costs.

In Modern Oral we accelerated volume growth over the first half and further consolidated our leadership position outside the US.

We continue to see share growth in established oral markets in Scandinavia and more broadly across Europe.

In ENA we are already volume share leaders in 16 out of the 18 markets where we are present.

Modern oral is an attractive opportunity in emerging markets offering an affordable reduced risk alternative to cigarettes.

We are gathering insights from our pilots in emerging markets including Pakistan and Indonesia.

In the US, the Modern Oral category continues to account for a small proportion of total nicotine value, at 1.6%.

The acquisition of Dryft has transformed our portfolio.

As has been successful with Vuse and glo, our current focus with Velo is on driving combustible consumer acquisition and building brand awareness, following the launch of the expanded portfolio.

We are pleased that Velo brand awareness is now at parity with the market leader and the brand is resonating with consumers ranking Velo ahead of peers on key brand attributes.

We have increased distribution from 6,000 to around 80,000 outlets nationwide, and we expect further expansion in the second half.

In a highly competitive market, Velo volume share has doubled in 32 states since launch in November.

Our Combustible business continues to perform well, with value growth in the first half.

Combustible revenue was up 5.8% and we grew both our value share and volume share.

Price/mix was robust at 4.3% driven by strong pricing of around 8%, partially offset by geographic mix.

And we have already achieved 90% of planned pricing for the full year.

Cigarette volume grew 1.8%, as emerging markets recovered from the impact of COVID in the prior period, particularly Bangladesh, Pakistan, and Vietnam.

I am pleased with the continued strong value delivery in our Combustible business supported by ongoing efficiencies, including further SKU rationalisation.

And we continue to leverage our scale to drive our transformation.

This year one billion of our cigarette packs worldwide will carry communication to encourage smokers to switch to our New Category products.

Turning now to the regions. All four delivered revenue growth at constant rates above 5% in the first half.

In ENA:
New Category revenue doubled compared to the first half of 2020, supported by further increased investment behind all three categories.

glo Hyper's success has more than tripled our THP revenue, making it the largest of our three categories in the region.

In Vapour and Modern Oral we have delivered over 50% revenue growth.

In APME:
Glo grew volume strongly and volume share was up.

New Category revenue was slightly lower due to: Consumer acquisition investment, and the disproportionate impact of excise harmonisation on our products, leading to a partial absorption of excise increases.

In Combustibles, volume was up as a number of markets lapped the impact of COVID in 2020.

We continued to grow cigarette volume share, which was up 60bps in H1, driven by Bangladesh, Vietnam, Pakistan and Japan.

Value share was down 10 bps, mainly due to Indonesia.

In AMSSA, continued strong growth of Vuse in Canada drove New Category revenue up over 70%.

As with APME, combustible volume grew, driven by the recovery in a number of markets, including South Africa, following the impact of COVID in the prior period.

Combustible share declined 30 bps on both a volume and value basis, driven by South Africa, Brazil, and Canada.

In the US we continued our strong momentum. Revenue was up 9% at constant rates, reflecting the strength of our brand portfolio. New Category revenue, grew 55%

This was led by continued significant value share gains from Vuse, which is approaching value share leadership in the US.

Velo volume share was up strongly, reaching 16% share year to date May, up 8.4 percentage points in a competitive market.

Combustible price/mix was 12.3% driven by good pricing, positive portfolio mix, and Revenue Growth Management.

Our combustible volume was down -4.3% in H1.

We delivered strong combustible value share growth, up 40bps, driven by Newport and Natural American Spirit which continue to take share on both a value and volume basis.

We expect full year US industry volume to be down around -5.5%, given continuing macro-economic uncertainties and a strong second half comparator.

Moving onto Group operating margin. A strong operational improvement of 150 basis points enabled an incremental £350million New Category investment in the first half.

The absorption of a 2% transactional FX headwind, or 60 basis points of margin, resulted in Group margin being down 70 basis points in the first half to 43%.

While we plan further incremental investment in the second half, New Category spend is anticipated to remain first half weighted.

For the full year, we continue to expect, the losses from New Categories to reduce in 2021 and we see a clear pathway to profitability by 2025.

Quantum is continuing to drive further simplification, adding new capabilities and agility to the business and is changing the way we operate.

In addition, the programme has delivered total savings of over £900million to date and we now expect to deliver £1billion annualised savings from Phase 1 and 2, 12 months ahead of plan.

This has been a significant driver of our strong operational margin performance.

Phase 1 of the project, which focused on organisational design, is now largely complete.

Phase 2, has been centred around the optimisation of our end market operating model and route to market together with embedding new commercial capabilities in the organisation.

Phase 3 of Quantum has started, which covers our HQ organisation redesign including a 25% headcount reduction in the Head Office where we are also increasingly moving to more fluid and collaborative ways of working.

And we continue to identify further Supply Chain efficiencies, increasingly related to the New Categories.

As a result, we have increased our target and we now expect to generate a total of £1.5billion of Quantum savings by 2022.

In addition, we continue to drive the roll out of Revenue Growth Management, which now covers more than 75% of group revenue, delivering accelerated value growth, and Marketing Spend Effectiveness, where 75% of total New Category marketing investment is now enabled by our digital tool.

Turning now to EPS, we delivered constant currency adjusted diluted EPS growth of 6.1%, this was driven by strong operating profit growth, up 5.4%.

Current rate reported EPS was down 6%, mainly due to the translational FX of over 8% and charges relating to the proposed sale of our operations in Iran.

Net finance costs were lower and we expect the full year charge to be around £1.6 billion.

Associate income was down, reflecting the inclusion of results from ITC, three months in arrears

The underlying tax rate was 24.8% and we continue to expect a rate of around 25% for the full year.

Extrapolating current spot rates we expect a currency translation headwind of around 7% on adjusted EPS growth for the full year.

We delivered further strong cash flow in the first half, driven by combustibles and releasing cash through new ways of working.

Operating cash flow conversion was impacted by the prior year benefitting from the deferral of excise in the US, due to COVID.

We continue to expect full year gross capex of £700million, broadly in-line with adjusted depreciation and amortisation.

We expect to deliver another year of strong operating cash conversion in excess of 90%.

And, confirm that we are on track to de-lever the balance sheet to around 3 times adjusted net debt to adjusted EBITDA by year end.

So, in summary, we expect Full Year constant currency revenue growth in excess of 5%, driven by continued strong second half momentum in New Categories, albeit against a high comparator.

In combustibles, the emerging market recovery continues, while we will lap a strong prior year performance in the second half, particularly in the US.

Our expected strong top-line performance allows us to further increase investment in New categories and absorb profit impacts including £170million from excise changes in Australia, the impact of COVID on our associate income from ITC, and a -2% transactional FX headwind.

As a result, we maintain our outlook for mid-single digit adjusted diluted EPS growth for the full year.

We are a highly cash generative business and expect to generate cumulative free cash flow of around £40billion over the next 5 years.

We remain committed to our progressive dividend policy, continuing to invest behind the transformation of the business, and de-leveraging the balance sheet to around 3 times adjusted net debt to adjusted EBITDA by the year end.

At that point, we expect our capital allocation flexibility to increase.

Thank you and with that I will hand back to Jack.

Jack Bowles, Chief Executive

Thank you Tadeu.

So, in the first half, we have generated excellent New Category revenue growth, share gains across all three New Categories, and our fastest growth in consumer numbers, to date, delivering on our 3 operational priorities.

This momentum is giving us increasing scale.

In New Categories we are well on track to reduce full year New Category losses in 2021, with a clear pathway to our £5 billion revenue target, and to profitability, by 2025.

As we reach our leverage target at the end of the year, our capital allocation flexibility increases.

As we said at our preliminary results in February, 2021 will be a pivotal year.

We are committed to transforming BAT to a high growth, Multi-category, Consumer led, CPG; with a reduced impact on public health and ESG at its core; creating value for all our stakeholders.

Our established multi-category strategy is working and our transformation is accelerating, we are building strong global brands with Vuse, glo and Velo. And continue to drive the digitalisation of the whole business, at speed.

BAT is changing rapidly, powered by our ethos. We are creating the Enterprise of the Future

I look forward to the second half, and I am excited about the future for BAT.

Thank you for listening. This presentation is available on our new website, which I am pleased to say has been recently upgraded.

Thank you and I will now open it up to questions.

Questions and Answers

Telephone Operator
And, as a reminder, if you'd like to ask a question or make a contribution on today's call, please press *1 on your telephone keypad. To withdraw your question, please press *2. You'll be advised when to ask your question. So, again, that is *1 on your telephone keypad.
And we do have a few questions in the queue. The first one comes from the line of Richard Felton from Goldman Sachs. Please go ahead.

Richard Felton, Sell-side Analyst, Goldman Sachs
Good morning. Thank you for the question. My first question is on the topic of cash returns. Now, your target leverage range is 2 to 3 times net debt to EBITDA, but, Jack, I think you previously described being at 3 times as removing the straitjacket. So, do you want to clarify how you're thinking about capital allocation, and would you be comfortable with starting in a cash returns programme and running with balance sheet while you're still at the upper end of that 2 to 3 net debt to EBITDA range? That's my first question.

Jack Bowles, Chief Executive
Yeah, thank you very much. First of all, I must say that we are very pleased with the momentum that we're having at the moment and, as we said, the end of the year is the time for these reviews. Of course, we like capital allocation, we'd done it in the past, and we said very clearly that we will do, of course, the de-leverage of the company. We're true to our dividend, and we want to invest in the business.

As you saw, the investment in the business is paying off very well and will continue to do so. So, by the end of the year, we will review again the situation.

Richard Felton, Sell-side Analyst, Goldman Sachs
Thank you. My second question is quite a specific one on Vuse. You mentioned in the presentation that improved trade margin are one element of driving

better profitability for your Vapour category. I was wondering if you could share some numbers around that, please. I think you said the trade margins for Vapour were around about 40% at your CMD in March last year. Have you seen a material improvement in that over the last 18 months?

Jack Bowles, Chief Executive
Yeah, I mean, Tadeu is going to complete the answer, but I think what's very important with Vuse now is that we're scaled. So, we can go to optimisation, we can reduce the trade margin and can accelerate on our goal.

We have been a very strong brand, and that is what is the most important. So, people are coming back to the thing, but Tadeu will want to add something.

Tadeu Marroco, Finance and Transformation Director
Yeah, the margin depends a lot on the country where you are and the channels that we are commercialising.

So, one thing that I would say, Vape stores are very high margins, like 70+, and the trend, moving from open system to closed system, is leading the commercialisation towards more convenience stores where margins are around 40% - that's the number we have quoted in the CMD probably that you have in mind.

Now, what's happening is that, first of all, we are increasing our presence in ecommerce and the margin comes up fantastic, and 40%, like you saw today, with subscriptions, which makes it even more interesting because there you have more loyalty, and the margins are even three times more than what you sell in the convenience stores.

And, on top of that, with the leadership that we are acquiring now in places like France, like the UK, we are able to now to renegotiate margins with some of these key accounts, moving from a specific, for example, percentage of revenue to a margin for Vapour performance, for example, which is also translating into improving margins.

So, that's why we refer to a path to profitability where we include trade margin management as part of this.

Jack Bowles, Chief Executive
So, we have a very clear path to profitability on e-cigarettes.

Richard Felton, Sell-side Analyst, Goldman Sachs
Great. Very clear. Thank you.

Telephone Operator
Thank you. The next question comes from the line of Gaurav Jain from Barclays. Please go ahead.

Gaurav Jain, Sell-side Analyst, Barclays
Hi. Good morning.

Jack Bowles, Chief Executive
Good morning.

Gaurav Jain, Sell-side Analyst, Barclays
Thanks a lot for taking my questions. So, my first question is on the guidance for the year. So, one that you mentioned revenue is about 8% full year guidance as 5% plus, so that will indicate a significant slowdown in 2H, where I think still you would probably have easy coms, especially in the emerging markets, so could you just help us understand where you might see the slowdown?

Jack Bowles, Chief Executive
Well, first of all, I think what's important to consider is that we have strong momentum, and that momentum will continue to build on. Then, the other thing is I prefer to be reasonable and to have the space, as we referred to earlier, a very straitjacket in the past, and we have a bit more space to invest in the business.

You see that there is a very strong reason in terms of Combustible and in terms of New Categories' growth. I think that the second half of the year is going to be comparing with higher comparators of the second half of last year, which was very strong, and we are reaffirming our guidance.

Gaurav Jain, Sell-side Analyst, Barclays
Sure. Thank you.

Jack Bowles, Chief Executive
Thank you very much.

Gaurav Jain, Sell-side Analyst, Barclays
The second question I have is on the US market. So, your pricing right now is ahead of competition and, you know, we are seeing in the recent data that you are beginning to lose share on the US segment side of things. And then, when I look at the amount of investment you are doing in New Categories, if I look at, you know, for instance, your Modern Oral realisation in the US, it's a fraction of your key competitor there.

So, if you keep increasing prices in cigarettes at the level which is ahead of competition to fund these New Category investments, isn't it a risk that you're carrying that, at some point of time, your share losses in the cigarette market and just accelerates?

Jack Bowles, Chief Executive
I think it's a very good question. What you have to consider is available income, and income, in general, in the US, it's quite strong. Price elasticity is 3.4, as it was last year. And what you see is you have a huge resilience of our brands in terms of market share, and we're growing premium share in the US.

So, we are always doing the balance. As I said, it's one of the key priorities of the Group, which is extracting the value of our Combustible business, and that's what we are doing. So, we're taking more pricing than our competition. We are having all the tools that we need in terms of digital to make decisions shop by shop, city by city, state by state, and at the national level and by channels. And we are able to grow our value share.

So, I think that the fact of having these stores that allow us to navigate through all this allows us to take more pricing than competition and continue to grow value share. So, of course, we are reviewing that all the time with the US team, but I must say that the performance in the US has been extremely good.

Gaurav Jain, Sell-side Analyst, Barclays
Thank you.

Jack Bowles, Chief Executive
We're growing share in premium.

Gaurav Jain, Sell-side Analyst, Barclays
Okay. And my last question is just device launches and glo. So, a competitor launches new devices in the next month and, you know, they have laid out a roadmap of, you know, how we should think of device launches that every year, there iteration and every three years there is a major change in platform. How should we think about device launches in glo, you know, this year and over the next few years?

Jack Bowles, Chief Executive
Okay. Well, of course, there will be innovation. Of course, there will be innovation. What I must say is that we were the first ones to launch the new device with Hyper and we think that's - with induction heating. I think that's a testament of the quality of the innovation that we have. I think that we have

improved significantly, the consumables, and we'll continue to do so also in the months to come.

And I think that, you know, in a competitive environment, you know, competition is going to launch new products. Fine. What we see is that we're getting a huge chunk of the growth of the category everywhere we are present now. And remember, we said in the presentation, we're only in half of the markets where THP is sold at the moment.

So, there is a lot of space for us to continue to grow. I think that the price of our sticks is very competitive and in line with competition - Tadeu referred to above 90 in terms of the index, and I think that we have a very good formula for the consumer.

As you saw in the charts, in every market that we have launched, we are growing shares significantly and at pace, capturing more than our fair share of the growth of the category. We have now 16.1 million consumers in New Categories. Who would have said that two years' ago?

You know, I remember vividly, and sorry for taking the opportunity, but, you know, two years' ago, Tadeu and myself, we stood up and we said we are going to transform the Group, have a new purpose and develop the company to a new pace. I mean, everybody said - Yes, right strategy, but let's see the results.

Now, let me tell you, in the second half of the year, we grew the three categories last year, we grew the three categories in terms of volume by around 50%. We do the same, and even more this time, and we have a record of 2.6 million consumers, additional, in this half of 2021. So, we have the momentum, we have the right products, we have the innovation to come and it's a competitive environment, yes. Let's enjoy the competition.

Remember also that, in terms of e-cigarettes, we are the leaders worldwide and, in the US where we were weak, two years' ago people told me - there is no way you're going to take a position in the US - Okay? Now, we are the leader in 20 states in the US. Out of the Modern Oral now, out of the 18 markets that we're in, we are leaders in 16, and we have a gap in Modern Oral in the US. We acquired the products that we needed, we've put our brand behind it, and we grew 10 share points in the meantime. So, we're in consumer acquisition mode, and we are delivering the revenue at 50% growth.

Gaurav Jain, Sell-side Analyst, Barclays
That's very helpful, Jack. Thanks a lot.

Jack Bowles, Chief Executive
Thank you very much.

Telephone Operator
Thank you. The next question comes from the line of Rey Wium from SBG Securities. Please go ahead.

Rey Wium, Sell-side Analyst, SBG Securities
Hi, Jack, Tadeu. Thank you for the opportunity.

Jack Bowles, Chief Executive
Hi. How are you?

Rey Wium, Sell-side Analyst, SBG Securities
All good, thanks. First, I just want to start off with the Vapour category. I mean, obviously, loss-making and you indicate you were working towards profitability by 2025, but, I mean, is there any colour that you can give us in terms of cost relative to revenue? I mean, to what is the extent of the cost relative to revenue? Are costs, basically, currently double of revenue or it is a little bit less? And, just on that, if you maybe can just give us a sort of, steer which markets do you think will achieve profitability first? So, that is my first question.

Jack Bowles, Chief Executive
Yeah. Thank you very much. Tadeu?

Tadeu Marroco, Finance and Transformation Director
Yeah. Look, when you see the numbers of BAT, the consolidation of different markets in different moments and different stages, we are already in positive territories in the three categories in the specific markets.

If you take, for example, THP in Japan, we are already in a profit position there. If you take Vapour in places like Canada, for example, and we are having profitability very soon as well. In Modern Oral, most of the markets we are already in a positive territory. But what I can tell you is that, in terms of different categories, the Modern Oral category has a very short payback, so it is around 15 months you are already in a positive territory because the margins are very high, even more competitive than the ones that we see today for cigarettes. There is no divisive hold on that.

The Vapour situation is we are progressing very fast in terms of margins. We have spoken before about trade margin. They are biggest levers that we are actioning now, is the cost of goods so we are gaining scale. We are moving from manual lines to automated lines, and this is where it's translating to massive cost reduction for us across the Group.

So, we are very, very pleased with the progress we are making in terms of margins in Vapour. And THP, the margins are attractive. They are compared with cigarettes. We know that there will be some headwinds coming from excise, but we also have opportunities in terms of the cost of the consumable itself.

It's a question of, you know, acquiring consumers, and are in the acquisition mode that Jack was referring to, and the levels of conversion are increasing, and we are quite excited about that because, as we put our device in the hands of consumers, they really enjoy either the liquid on the Vapour side of the consumables on the THP side, and we see more and more loyalty coming along.

So, the numbers of conversion are very high. So, all these losses that we are referring to is actually fiscal driven and consumer driven, and the timelines that we are referring is basically, you know, us moving along the journey of expanding this through different geographies. But surely, we have red markets are coming on the positive side.

Jack Bowles, Chief Executive
You know, always remember we speak about digital, and digital is extremely at the core of BAT and, not only in marketing where we have now the business with 12 million consumers of New Categories, we have three times more than that in terms of Combustible consumers, but it's also going through the whole supply chain. It is also going through the whole way we operate, and that has huge benefits in terms of enabling us to deliver the savings of Quantum, where we have put the £1bn to £1.5bn now, and the acceleration of consumer engagement. And that has allowed us to be far more effective.

So, now that we have scales, we can build the brands to have very strong and very effective brands supported by digitalisation that will, in time, give us the profitability in these New Categories.

We see already that, despite the size of the investments that you saw last year and this year, that we're going to start to reduce the losses this year, which is a very, very good milestone. So, consumer acquisition, start to review the losses, NPO (?) is growing very fast, so revenue up 50%, not a bad score. Of course, the three categorises have a very good score. And we'll continue our road to profitability. The pathway to profitability per category is absolutely clear. [Pause] Question?

Telephone Operator
Thank you.

Jack Bowles, Chief Executive
Thank you very much.

Telephone Operator
The next question comes from the line of Jemima Benstead from Citi. Please go ahead.

Jack Bowles, Chief Executive
Hello.

Jemima Benstead, Sell-side Analyst, Citi
Hi. Good morning.

Jack Bowles, Chief Executive
Good morning.

Jemima Benstead, Sell-side Analyst, Citi
Thank you for the presentation. Most of my questions have been answered so just a couple more. My first one's on Emerging Markets. You obviously saw very good growth in H1 and that contributed to your full year industry volume upgrade. I know you flagged the cost comps in the second half, but can you talk a bit about the ongoing drivers of momentum in the second half and how we should think about price mix developing? Thank you.

Jack Bowles, Chief Executive
Yes. Tadeu will take price mix, but, in terms of, you know, Emerging Markets, as you saw last year, there was very big slowdown related to the pandemic. What we've seen in the first half of the year is recovery in terms of Emerging Markets. And, as you know, you know although it's 25% of our revenue, it's more than 50% of our volume. And what you saw is very strong performance in our businesses across the patch.

Of course, it's a mixed bag because you have countries like South Africa where you still have a lot of issues in terms of lockdowns and in terms of illicit and things there but, overall, in Emerging Markets, much more volume.

So, of course, it comes at a cost of a lower margin, which is very good performance, and that allows us to have a very strong performance in terms of our Combustible business. But, Tadeu, a bit more colour.

Tadeu Marroco, Finance and Transformation Director
Yes. In terms of pricing, we are seeing similar levels of pricing that we saw in the previous year. There is not much excise ad hocs happening. We had one in Russia; we had another one in Indonesia. These are the outliners I would say. We are not seeing these across the patch. And, hence, the price mix is not much different because we are not also seeing much of acceleration in terms of downtrading.

We have seen some punctual movements in terms of Brazil where illicit trade reduced, and we have sold more volume in the low end, hence the mix gets a bit impacted by that. But it is more volume coming from illicit to the more lower end of the market.

Overall, illicit is slightly better in the first half of the year, which is a positive as well, so I would say that these are the major trends.

Jack Bowles, Chief Executive
So, it's more the geographical mix. The pricing is very strong.

Jemima Benstead, Sell-side Analyst, Citi
Thank you. And then just for my second question, it's just a clarify of that around guidance too, you quantify the £170m impact from the excise change in Australia, I just wanted to check, was this magnitude previously included within that mid-single digit constant currency EPS growth guidance that you'd already given or are you facing a greater headwind but you're still able to deliver the EPS guidance? Thank you.

Tadeu Marroco, Finance and Transformation Director
No, I mean, before Tadeu gives you a broader answer on that, you know, in the time of COVID and in the time of the business where we're in, where New Categories are developing quite fast and where Combustible business is enjoying a strong pricing environment, there are pros and cons, or there are ins and outs, and the fact of Australia is something that is happening. And, because we have a very strong top line growth, we're able to manage this and to continue to invest very strongly in our business.

I think I was referring earlier to a straitjacket, now we have more space to be able to take care and to cater for these kinds of things and to move on. Tadeu?

Tadeu Marroco, Finance and Transformation Director
Yeah. Jack is absolutely right. The strength in the top line of the business, which is promoted by not just the volume recovering from a lower comparative due to COVID, but, more importantly, the New Categories are accelerating

which, like I mentioned in my presentation, one-third of the revenue growth is where it's coming from New Categories, and plus, the initiatives we are doing in terms of cost saving the problem, we are accelerating Quantum, is giving us the possibility to absorb those shocks.

So, this is one shock of £170m is not a small one, and this is a good thing for the market in the long run, but we have a hit in this particular market that also impacts the revenue in the second half the year, by the way, and related to that excise. And, when we articulate the guidance of mid-single digit, we are considering the absorption of this hit and also the fact that, like we said before, since the beginning of the year, that transaction FX this year is double of what we saw last year.

Some companies in our sector, they prefer to provide constant guidance excluding transaction. We don't do that. In our constant guidance, we have transaction in otherwise I would be here upgrading the guidance for all of you, but we had a shock of 2% equivalent in terms of transaction FX, which is part of our mid-single digit guidance. And also, the fact the, like we said, since the beginning of the year, India's going through a tough time in terms of COVID and, hence, the ITC performance is being impacted by that.

This translated us in a very short kicker between operating profit, I think, particularly this year, for BAT. So, I think that that's the overall story around the mid-single digit target.

Jack Bowles, Chief Executive
Yeah, maybe an additional point. You know, I said very clearly that the three priorities of the Group are including the fact of going for value share. Value when important and adequately with different share the right way. We'll make sure that our business is continuing to prosper because this is delivering the money that we need in order to continue to grow our business. So, this is for the sustainability, that 50% growth in terms of New Categories and that 16.1 million consumers that we have in New Categories. Thank you.

Jemima Benstead, Sell-side Analyst, Citi
Thank you.

Telephone Operator
Thank you. The next question comes from the line of Karim Ladha from Independent Franchise Partners. Please go ahead.

Karim Ladha, Partner, Independent Franchise Partners
Good morning, Jack. Good morning, Tadeu. Thank you for taking my question.

Jack Bowles, Chief Executive
Good morning.

Karim Ladha, Partner, Independent Franchise Partners
So, your operational executions in taking the helm have been strong and as shareholders, we've been impressed with your ability to both invest in your next-gen platforms as well as to deliver solid earnings growth.

Jack Bowles, Chief Executive
Well, thank you.

Karim Ladha, Partner, Independent Franchise Partners
The market though, it's not giving you credit for this. You're trading on just 8 times EBITDA. And, at £28, there is opportunity to create enormous value by buying back stock in size and doing so before your investments in next-gen platforms start to materialise in your financial results. And, of course, you'll be in a position to buy back shares from next year as your leverage comes down, but, given the burden of your dividend, your buyback capacity will be just £2bn to £3bn a year. And we understand that your dividend is important to a portion of your shareholders, but, overall shareholder value creation must be your guiding principle rather than catering to the needs of a specific subset of dividend focused shareholders.

You know, for example, if you halve the dividend in '22, your buyback capacity increases to £5bn a year. You could buy back half your shares in just five years. So, with that concept, our question is under what circumstances can we expect you and the Board to reconsider the dividend in the short term in order to more aggressively pursue buybacks to drive long-term shareholder value?

Jack Bowles, Chief Executive
Yeah. Thank you very much for your question. I think it's an interesting question and we are reviewing this subject on a regular basis.

I think that I said very clearly that capital allocation will be reviewed at the end of the year, and the end of the year's not so far away, in July. Yet, you know, you're always to consider the net debt to EBITDA that we have the investment we're making into the business. So, I think that the long-term sustainability of the company is the first priority that we have.

Of course, it's a very attractive tool to be used. But, as we said, I mean, it's going to be towards the end of the year. Tadeu, do you want to add there?

Tadeu Marroco, Finance and Transformation Director
Yeah, no, we are definitely very committed to delivering shareholder returns.

Jack Bowles, Chief Executive
Yeah.

Tadeu Marroco, Finance and Transformation Director
And we believe that the commitment dividend as a means of shareholder return. But the Board recognised the value of share buyback. That's the reason why we have done that in the past. This is not new for BAT, and over ITC in a broader time horizon, like I said in the presentation, this is a very cash company. We expect to generate £40bn of cash over the next five years. So, there will be plenty of opportunities for us in terms of capital allocation.

But our priority right now is the dividend pay-out of 65%, continuing to invest in the business in the New Category space, like we have just done, you know in Organigram or in the companies we acquired through our corporate venture arm, and we will then pay the debt to get us to the revised corridor between 2 to 3 of leverage on the balance sheet. And then, like Jack said, we will have more flexibility to reassess capital allocation, which is something that we're doing on a constant basis.

Jack Bowles, Chief Executive
So, we really do understand your interest, and it's about, you know, a short timeframe towards the end of the year.

Karim Ladha, Partner, Independent Franchise Partners
Okay. Thanks then.

Jack Bowles, Chief Executive
Thank you very much.

Telephone Operator
Thank you. The next question comes from the line of Alicia Forry from Investec. Please go ahead.

Jack Bowles, Chief Executive
Hello. Good morning.

Alicia Forry, Sell-side Analyst, Investec
Hi. Good morning to you both and thank you for the detail on the New Categories' profitability. That's very helpful.

My first question is on the Modern Oral category, and specifically on the US. I mean, volume's up 450% but revenue up only 29%. I appreciate you're in customer acquisition mode, but is this dynamic primarily actions that you're specifically taking or reflective of the boarder category, and how long do you expect this customer acquisition phase or dynamic to persist for you? Should we expect this category in the US to become profitable within the next 18 months or is it a unique situation that will take longer? That's the first question.

Jack Bowles, Chief Executive
Okay. Thank you very much. I think what you have to be cognisant of is it's a small category in the US. It's 1.6% total nicotine. Then, we have a gap in terms of the portfolio, yeah. So, we had the very limited share of that segment which we didn't like because we are the leaders in the rest of the world in terms of Modern Oral.

So, we acquired the company that we need. And I must say that we it is quite normal now that you have, I would say, three players that are actively pursuing the segment, that you will have, you know, promotions and consumer acquisition.

I think we're doing two things at the same time because we know the categories interesting to the consumer. One is geo-expansion. And, as Tadeu said, we went from 6,000 to 80,000 outlets, and we'll continue to grow the outlets and we'll go more for active distribution further than new American distribution. And, at the same time, we are building the brand and we know already that, in terms of marketing parameters, we are very well rated, and our wellness is already at the level of the leader in the category.

So, we are going up 10 share points in the category. You have to go fast in this category in order to benefit from the geo-expansion and the fact that it's a new category in the market for the consumers.

So, I think that it is playing completely in our hands to make sure that we grow to a sizeable position. When then, you have scale, you have economies of scales, we you have distribution effectiveness, and your brand then is taking over from your consumer acquisition.

So, it's a very normal journey. How long will it last? That’s a good question. Let me grow my share for a few more periods and then I will tell you where we stand on moving forward. That can be a profitable category but, again, it's 1.6% of the total nicotine market in the US.

Alicia Forry, Sell-side Analyst, Investec

Thank you. If I could follow up on Modern Oral in APME where volumes were up 500%, I appreciate off a very small base, but it's a region where we perhaps a bit less visibility on that category. Can you discuss, as far as you're able to, your strategy for expanding Modern Oral in that region, perhaps some markets that you're targeting and government attitudes, etc?

Jack Bowles, Chief Executive
Yeah. I've always said, you know, Modern Oral, in terms of consumers, makes a lot of sense for Emerging Markets because you don't have a device. The return on investment, as Tadeu said, is very quick. You need to have local manufacturing because that's not a product that travels extremely well with the level of moisture and everything.

But the reality is, we have a very strong base in terms of Emerging Markets, and we see that, in terms of consumer affinity, there are lots of markets between Africa and Southeast Asia where you have a lot of permeability and receptibility from the consumers. So, we are doing pilots and tests and launching in some markets in order to learn more.

The thing also is you have to craft, and you have to sit at the table with the regulators in order to have a regulatory framework that allows us to have a sustainability in the establishment of that category. So, I think that there's a huge benefit for the consumers because most of the time they cannot afford devices before they get into buying consumables or buying pods, and it is a strong adequation with the palate of the consumer, and the ritual is well accepted. So, it's a question of, you know, pursuing the development of these places. So, you will have places like Southeast Asia and some places in Africa where it will grow very fast.

We have to set the frame and establish as we go along. Always, in all the new categories, what we've done is there's a difference between speed and rush. I want high speed; I don't want rush. I want the possibility to establish to and to learn, and then make the investment because I want to have a rational approach in terms of resource allocation in terms of the three categories and in terms of the different geographies.

Alicia Forry, Sell-side Analyst, Investec
Thank you. I'll past it on.

Jack Bowles, Chief Executive
Thank you.

Telephone Operator
The next question comes from the line of Jon Leinster from Societe Generale. Please go ahead.

Jonathan Leinster, Sell-side Analyst, Societe Generale
Hi, good morning gentlemen and thanks.

Jack Bowles, Chief Executive
Good morning.

Jonathan Leinster, Sell-side Analyst, Societe Generale
Morning. A couple of questions. First of all in terms of Japan, obviously there was a tax increase in October last year which you've absorbed. There's another tax increase in October this year. Given the changes are you expecting another significant tax absorption on heated tobacco, or is it now fairly equalised?

Jack Bowles, Chief Executive
Are you referring to our pricing position in Japan or …?

Jonathan Leinster, Sell-side Analyst, Societe Generale
Yeah, a mix. I mean clearly, you've absorbed the tax increase in October as they've moved the sort of weight-based system towards sort of …

Jack Bowles, Chief Executive
I think the situation that, Tadeu, you can complete on that one. The situation in Japan is very simple, you know. Glo has grown segment share, glo has grown a total nicotine share and glo is taking a very big part of the growth of the segment in Japan, so we're very happy with the results in Japan.

We are present in multiple price points in Japan, like the competitors are, and we'll continue to do so. So, I think that our pricing at the moment is competitive and if there are some tax increases then we'll take the decision at this time. But I think the momentum that we have does not need us to be overly aggressive in terms of this environment.

It's not about giving you pricing guidance, I'm just saying we have a very strong brand that is growing very fast and that is acquiring a lot of consumers.

We're taking more than our fair share in terms of the growth of the segment, and we'll continue to do so. So, we are very present in multi-price points already and we'll continue to do so.

Jonathan Leinster, Sell-side Analyst, Societe Generale
Okay. I guess that really the point of the question was whether the tax situation in October this year would be unfavourable to glo vis-a-vis the other competitors perhaps the way it was in the last year.

Tadeu Marroco, Finance and Transformation Director
Yeah, in the past, you're absolutely right. The characteristics of our product means that the equalisation of tax hit us disproportionally because we had a lower level of incidents of excise, we were before in a super-slim product and the difference between weight bases shows the way that they changed their way to calculate the tax means that the hit in terms of incidents for us was higher than competitors. So, we had to absorb some of that excise otherwise we'd be out of their market in terms of price competitiveness.

Our decisions moving forward around, will be you know, the tax that we know how we will then turn out, but also competitive landscapes.

So, we haven't made the full decision yet, we still have some months to go, and we'll be analysing where we stand in terms of competitors and making a final call on that.

Jonathan Leinster, Sell-side Analyst, Societe Generale
Okay, thanks. Secondly, a general question. You've outlined in terms of NGP the sort of cost reductions that are possible in marketing and then trade margins and also costs for goods sold, could you outline sort of in broad terms which of those areas is the most important?

Jack Bowles, Chief Executive

Well, I would say that the three areas are extremely important, you know. And the most important one is scale. And scale drives the three elements that we spoke about.

But Tadeu, do you want to say something more?

Tadeu Marroco, Finance and Transformation Director
Which category is this? Sorry, I missed the whole question.

Jack Bowles, Chief Executive
New Category in general.

Tadeu Marroco, Finance and Transformation Director
New Category in general?

Jack Bowles, Chief Executive
Yes.

Tadeu Marroco, Finance and Transformation Director
Well look, yeah, the trade margins are more relevant in the Vape space for sure and it's not that much in the other things, in the THP or the Modern Oral space. But the comps like Jack said, is permeating everything. And the level of savings that we are making, being able to make when you move from more niche towards a more global player is massive, and this is a big driver for us moving forward.

Jack Bowles, Chief Executive
We have now the scale that we need as a foundation, as a bedrock in order to continue to accelerate the development of New Categories, and we will do so. Scale is critical. Now we have the bedrock, then we'll continue to build on that foundation.

Jonathan Leinster, Sell-side Analyst, Societe Generale
Just to follow up on that, I mean you've talked in the past about automation, particularly from the supply base, is that now starting to come in particularly in Vaping or is that still handmade?

Jack Bowles, Chief Executive
No, no, it is coming now, and we've already started that, and we're building the lines accordingly for automation.

And automation, as I said, scale is the most important. That's what I was missing in the equation a year ago. Now, I have the scale that I need in order, in the three categories to do automation to do rationalisation, to do digitalisation of the supply chain.

Then on the side of the product itself, I can do now RGM. As Tadeu was saying, now 75% of the business is on RGM, and that's extremely important for us. So then it becomes a self-fulfilling prophecy of a business that is growing at pace. And we'll continue to invest because, as I said, we will invest a lot of money this year. As you saw, we invested £350m in the first half of the year, which is more than the increase that we did last year, so that comes on top, and we continue to accelerate. And at the same time, we'll have a reduction of our losses at the end of the year in New Category.

So, I think that's why I'm speaking always about the pivotal year. This plus the three net debt to EBITDA gives us the possibility really to charge ahead in terms of our development. And we're very proud of the results.

Jonathan Leinster, Sell-side Analyst, Societe Generale
Yeah, thank you. And lastly, currency transaction I think you said is 2% off EPS this year. As you look forward into you know, particularly into 2022 given the hedging policies are we likely to see a sort of similar currency transactional impact in 2022 or is it more favourable?

Jack Bowles, Chief Executive
Well, this is a …

Tadeu Marroco, Finance and Transformation Director
Your question is a difficult question. At the end of the day we are seeing a lot of the weakness coming mainly on those Emerging Markets where we have to import goods, for example, for our imports for our product costs in hard currency and where it's mostly why we see the transaction. They are badly hit now because of the COVID.

So, your guess is as good as ours, but at the end of the day the large goods say, if you have an improvement situation in COVID who knows what will happen with COVID. Maybe there will be some recovery in those markets, hence less impact. But actually, this is a tough one for us to forecast.

Jonathan Leinster, Sell-side Analyst, Societe Generale
Okay, well thank you very much for that.

Jack Bowles, Chief Executive
Thank you very much for your question, very good. Thank you.

Telephone Operator
Thank you. The next question comes from the line of Jared Dinges from JP Morgan. Please go ahead.

Jack Bowles, Chief Executive
Good morning.

Jared Dinges, Sell-side Analyst, JP Morgan
Sorry, morning. Hi, guys. I know you've done very well in terms of THP volumes …

Jack Bowles, Chief Executive

Thank you.

Jared Dinges, Sell-side Analyst, JP Morgan
... compared to your peers, you know, the volume share gains are definitely positive to see. But I want to ask about your THP revenues. So, in the first half actually your constant growth to revenue growth in THP, it was just in line with your key peer, which implies that you guys aren't actually gaining any value share in the category despite the launch of glo Hyper. Can you maybe talk about when you'll be out of investment mode on devices and maybe when we can expect a price mix in general in THP to turn positive? Thanks.

Jack Bowles, Chief Executive
You know, two years ago everybody said that I didn't have a chance in hell to get the position in terms of THP. Now we're speaking about what is the pace of the growth that we're having.

I think it's a much better situation to be in for BAT. And I must say that the performance that we have in terms of THP where we have, as we said, a pricing index of 92% or even above that in terms of the price of the consumable. These are a very good performance. We are growing share everywhere; we're growing share everywhere. And we're only present in half of the total number of markets where THP is selling. So, I think we're doing extremely well.

Now of course, we're doing some investments because we're in consumer acquisition mode in terms of the devices, but everybody does. And depending on the geographies, everybody does. So I'm not going to go through a very long and exhaustive list, but there is a lot of space for us grasp in terms of THP.

And as I said, two years ago everybody that we won't be there where we're now having a very strong acceleration in terms of THP in volume, more than 50% in the second half of last year, more than 50%, more close to 100% in this half of 2021. And we'll continue to accelerate.

So it's a question of the right balancing or growing the brand. And as you saw in the marketing indicators, the brand indicators that we're having, we're doing very well and our ONS is growing very fast.

So we're in acquisition mode and we'll continue to do so. But we have also the final part to profitability for THP.

But Tadeu?

Tadeu Marroco, Finance and Transformation Director
Yeah, I just want you to have a look on the Vaping side, for the Vaping we had this type of gap a couple of years ago and as you see now, they are getting much closer because it's working. And you would expect this because at the end of the day glo Hyper is in the market a bit more than a year just?

Jack Bowles, Chief Executive
Yeah.

Tadeu Marroco, Finance and Transformation Director
So, we are in a very emerging phase of our level of investment, different from Vape where we have been for some time. In the dynamic of vaping is probably what we'll be mirroring what we'll be seeing in the THP side.

The good thing is, like I mentioned before, we are increasing conversion. And that's the most important indicator for us. So, we are making investments and the investment is paying back. It's not that difficult, if we take it out, we'll lose it because the conversion is there, and this translates into loyalty and then we have a business that is sustainable over time.

Jared Dinges, Sell-side Analyst, JP Morgan
Okay, so just to be clear, you're not going to, so there's no exact kind of timeframe on how long the investment mode will last on devices, but you'll continue to do so as long as you're expanding. Is that fair?

Tadeu Marroco, Finance and Transformation Director
Yes, but at the end of the day we are in expansion mode as well. We are in half of the markets where THP is present, so there is still a lot to come as well. And then whenever you see a number, our numbers will always have consolidation in different stages of investment.

Jack Bowles, Chief Executive
Yeah, that's the point, different stages, which means that in different geographies you will see different things. But we're growing the category and growing our share of that category, which we are doing strongly in the first half of the year.

Jared Dinges, Sell-side Analyst, JP Morgan
Got it, thanks guys.

Jack Bowles, Chief Executive
Thank you.

Telephone Operator
Thank you. The next question comes from the line of Sanath Sudarsan from Morgan Stanley. Please go ahead.

Jack Bowles, Chief Executive
Good morning,

Sanath Sudarsan, Sell-side Analyst, Morgan Stanley
Good morning, good morning. A couple of questions from my side. First of all, can you just give us some more colour on the NGP investments made this year and how do these differ from investments made last year?

And can you also clarify whether the NGP business or losses in the first half were lower than last year?

And then secondly …

Jack Bowles, Chief Executive
Now as you know, remember always, I'm French so I'm a bit slow so I can go only question by question. And even that question I will speak between the first half for me and the second half. So the first half of the question was, sorry?

Sanath Sudarsan, Sell-side Analyst, Morgan Stanley
Just more colour on the NGP investments you made this year and how do they differ versus what you made last year.

Jack Bowles, Chief Executive
Okay, we said in the previous periods that first we were in an initial phase two years ago of building the capabilities and building the R&D. Now we are in the phase of acquisition of consumers and building the brands, so we're really in the phase of building the brands. And I must say that we've done a lot of investment in terms of THP.

So what has changed if you want compared to last year, full year, is that there is more on THP at the moment than there was before. But you saw that the total number has increased by £360m. So, we are putting the money where we need to put it in terms of consumer acquisition and brand building because consumer acquisition alone is not enough. Now we are in the phase of building the brands and having the right levels of awareness and having the right level of brand content.

You want to …

Tadeu Marroco, Finance and Transformation Director
Yeah, one of the different stages from one year to another is more on the listing fees. As we are expanding into new markets you have to pay listing fees when you get into for example, new key accounts and so on, so this is a natural movement when you do.

But the bulk of these extra investments are the traditional market investments, building the brands like Jack referred to. This is the digital base, there's the social side of it, the social media side of it and so on. So that's more or less there.

Sanath Sudarsan, Sell-side Analyst, Morgan Stanley
That's clear. And also just, I hear about the guidance being for the losses to reduce in the full year for NGP, has that happened in the first half also?

Tadeu Marroco, Finance and Transformation Director
No, it didn't happen in the first half because we have been weighted in the first half of the year. And hence you'll see the operating margin is a very big drag coming from New Categories. This is a consequence of that. And …

Jack Bowles, Chief Executive
And I'm guessing the consumers we will build in the second half.

Tadeu Marroco, Finance and Transformation Director
Yes, you'll probably see this drag to reduce in the second half as a consequence of that. But the fact that has been weighted in the first half means that our reduction loss we must realise in the full year.

Sanath Sudarsan, Sell-side Analyst, Morgan Stanley
Okay, thank you.

Jack Bowles, Chief Executive
We have a very clear pathway for per category and for total New Categories in terms of the road to profitability.

Now that we start to have scale and we start to have a very strong momentum in consecutive two halves of years, now we can really pan out all this. And I must say that digital is helping us a lot in terms of the brand building and in terms of modernising all this.

So we do resource allocation every month. It takes Tadeu and myself a lot of time every month to make sure that we do the resource allocation and that we navigate all this. And we're very happy with the progress that we're making.

Tadeu Marroco, Finance and Transformation Director
Just one more comment on this because it's important for you to notice that some of this growth investment is reducing the revenue side. It's not that it's all related to below revenue.

So when you see our revenue numbers, they are at net of some of these investments that we are referring to.

Sanath Sudarsan, Sell-side Analyst, Morgan Stanley
Got it, yes. Thank you

And the second question is just trying to understand, I mean you've done an incredible job, an incredible job with the cost savings and delivery of that a year earlier.

Jack Bowles, Chief Executive
Thank you.

Sanath Sudarsan, Sell-side Analyst, Morgan Stanley
You've now guided for a higher number of cost savings, but what have you seen over the last two years of these cost savings basically being absorbed into NGP investments? Is that something we should continue to expect probably for these incremental cost savings that you're going to now deliver? And probably there's even more to come.

And then you know, in terms of how or when should we think about NGP business becoming self-sufficient in terms of funding for its own promotions, etc, along with reducing the losses?

Jack Bowles, Chief Executive
Yeah, first of all, I mean these cost savings, you have to see them in two ways. First, it's increasing the efficiency and adding new capabilities to the business, hiring people. We've hired more than now, to date, since we started that journey a year ago, a bit more than a year ago 500 new managers joined the company in capabilities that we didn't have before.

So it is simplifying and increasing the efficiency of our business giving us the new capabilities, and at the same time saving a lot of money.

Now, that saving of a lot of money, I'm very adamant on the fact that we're going to continue to accelerate. And that's now £1.5bn instead of £1bn.

This gives me the flexibility to invest in the business or to allocate where I need to allocate that money. So, we start from the genesis of the financial allegories we will deliver. Yeah? That's kind of the line in the sand.

Then we look at New Categories and we see all the money we need to invest. And I don't think, Tadeu, in 2021 once we said no to a valid acceleration plan in terms of investment, and we do resource allocation every month. So that's kind of the waterline.

But first it is about developing the business and making sure that we have the resources that we need. So we use that money either for additional investment in New Categories or for the things that we need, or headwinds that we can face as spoke about earlier this morning. Tadeu?

Tadeu Marroco, Finance and Transformation Director
That's absolutely right. So these savings will be primarily to invest and to deliver our financial commitments. That's what you expect.

In terms of the journey, we said 2025 this will be the self-sufficient position that you are referring to. This gives us the space for us to make the geographical rollout investments that we need to up to that point. But more importantly is that the losses that we had in 2020 last year start reducing from this year.

So from now until 2025 when you get the self-sufficiency situations including all levels of costs that are involved within the category, including R&D for example. They will be earnings that are created for the group because we'll be reducing loss over time.

So there will be two drivers for us to benefit from in terms of allowing us to deliver the financial commitments. One is the savings agenda, like you rightly point out, so even after Quantum, you're going to have some levels of continuous modes of savings, continuous improvement moving forwards but also the reduction in losses in New Categories coming forwards.

Sanath Sudarsan, Sell-side Analyst, Morgan Stanley
Thank you. So just to understand this in a simplistic manner, the line in the sand on your financial algorithm can actually move ahead and move higher?

Jack Bowles, Chief Executive
We will take decisions as we go along. You know? I think that we have reached a point now where we're getting close to that pivotal year that I was speaking about before which is net debt to EBITDA around three and delivering our financial algorithm and growing the New Categories in terms of consumer

acquisition and revenue with the path to profitability. And we'll make the calls as we go along.

You know, I'm a long-term person, but I like a lot very speedy growth and not at the detriment of the financial algorithm. So, I'm balancing all the different elements. We spoke about the very straitjacket two years ago, and now I have a bit more space so I can accelerate and do the right things, have the right products.

I'm having a very, very good performance in terms of value creation in our Combustible business. I'm doing very well in the US, Emerging Markets are benefiting from it though it has some impact in terms of you know, the margin per 1000 slower in Emerging Markets. But altogether the whole thing is going in the right direction. So from a position of strength, I can continue to power forward.

There will be some headwinds, there will be some things that are happening, but I will have more defence mechanism if you want, in order to handle that. And the fact that our base in terms of New Categories now is a bedrock solid foundation with 16 million consumers and growing revenue by 50% gives me the ability to continue to power forward.

Sanath Sudarsan, Sell-side Analyst, Morgan Stanley
This is great, thank you very much.

Jack Bowles, Chief Executive
Thank you.

Telephone Operator
Thank you. Our last question for today comes from the line of Patrick Folan from Redburn. Please go ahead.

Jack Bowles, Chief Executive
Good morning.

Patrick Folan, Sell-side Analyst, Redburn
Yeah hi, good morning. Thanks for taking my questions.

Jack Bowles, Chief Executive
Pleasure.

Patrick Folan, Sell-side Analyst, Redburn
My first question is on the B Tomorrow Ventures which is quite interesting, especially being part of the Beyond Nicotine ...

Jack Bowles, Chief Executive
Thank you. That's something that we've created, Tadeu and myself, I think the day we arrived. We said we want to have a venture capital capability in the company in order to be able to acquire capabilities that we don't have.

You don't have to do everything inside, you know. Acquiring capabilities, acquiring technology, and acquiring the different pieces of the puzzle that creates your ecosystem to be able to continue to grow, and especially related to R&D and to brands and products.

Patrick Folan, Sell-side Analyst, Redburn
And is this the main focus for pushing the Beyond Nicotine strategy or should we expect potential M&A investments outside of this venture unit?

Jack Bowles, Chief Executive
Sorry, I didn't get the last part of your question. The line was not ...

Patrick Folan, Sell-side Analyst, Redburn
Is this the main focus we can expect for the Beyond Nicotine strategy or will there be potential M&A outside of the actual venture unit?

Jack Bowles, Chief Executive
Yeah, I mean what you have to consider is there's a lot of internal capabilities that we have. You know, we have very competent people like David O'Reilly that is driving our science in the company, very capable people like Paul Lageweg and all his team that are driving our New Categories. And I think that in R&D in science and in marketing, we have the capabilities that we need.

So it's an accelerating mechanism, that venture capital arm in order to get the missing pieces of the jigsaw.

So, we have a lot of internal pieces of the jigsaw. We do a lot of investment in BAT in terms of Beyond Nicotine, and we acquire what we need to complete the full puzzle.

We have defined three clear consumer spaces that we want to be in. We have a framework reference in which we want to operate. By the way, I gave that framework reference in terms of where we want to be in terms of Beyond

Nicotine two years ago in the Investor Day, so I'll go back to the deck. Yeah? And you will see that we are extremely consistent in what we are doing.

So, I think that we are in the right space really to do that. First of course, we have an established business in New Categories that is working very well and we're doing the tests and we're doing the development that we need.

As I said in my presentation, it covers the whole gamut of the capabilities that we have to have, and we do pilot tests as we go, and we have a lot of knowledge further and beyond only nicotine. We have given in the full year last year results a lot of understanding in terms of the areas in which we are working.

Patrick Folan, Sell-side Analyst, Redburn

Okay, great. Thanks. My second question is I believe you mentioned that 1 billion cigarette packs will be carrying messaging to switch your consumers to your NGP portfolio. Can you elaborate more on that?

Jack Bowles, Chief Executive

Well, I find it very important, you have to be consequent, you know, and there to transform with the team, you know, and there to transform BAT and reduce the risk for the consumers.

So very clearly when you're selling cigarettes, you have the, I would say the obligation to communicate to the consumers that you're adding Non-Combustibles, that there are other products that are now available. Yeah? It's not by forcing consumers to go somewhere, that you would have the right attitude and behaviour. Everybody that has done five minutes of marketing will tell you that.

You have to inform the consumers and to attract them into these New Categories with the right understanding of these reduced-risk products. And I think that's the way it works.

So we are putting in 1 billion of our packs, because you have a lot of limitations related to geographies where you can put something. There's lots of countries where you cannot put anything on the pack or you cannot promote, even if it's New Categories, nothing, you cannot promote anything from the pack.

So, all the countries where we can and all the countries where we have the capabilities, we put inserts or in code or everything that we can in order to bring the consumers to an informative website or even to the product directly if we can. Because I strongly believe that we will in time transfer the consumers from Combustible to these New Categories.

And the development of these New Categories will improve as we go along. We have a strong pipeline of innovation, and I'm very proud of that.

Did I answer your question?

Patrick Folan, Sell-side Analyst, Redburn
Yeah. And I was just wondering is there any target markets you have for that messaging on the brand cigarettes?

Jack Bowles, Chief Executive
Yeah, I would say first the blanket approach is the right way to go. You have to inform as many consumers as you can. After that there's the capabilities that we have and there's the regulation in the different countries, but as a default mechanism everywhere because I think it is important to transfer the consumers from Combustible to New Categories. Yes?

Patrick Folan, Sell-side Analyst, Redburn
Okay, yeah, thank you.

Jack Bowles, Chief Executive
And until everybody has migrated, I'm going to extract value on Combustibles until there are smokers that are legally paying taxes in the different countries. Okay?

Patrick Folan, Sell-side Analyst, Redburn
Thank you.

Telephone Operator
There are no further questions in the queue, so I'll hand you back to your host, Jack Bowles, to conclude today's conference. Thank you.

Jack Bowles, Chief Executive
Well, thank you very much. I think that we are very proud of our results in the is first half of the year as we were proud of the results last year. But really this time it is about, you know, growing the revenue on our New Category. So we're very pleased with our first-half results.

Our multi-category, this is multi-category, yeah? Multi-category strategy is working, and our transformation is accelerating.

We are building strong global brands and embracing digital across the group. BAT is changing at high pace powered by our ethos. And I'm excited about the future of BAT.

Thank you for listening and I hope you will have a safe and enjoyable summer, better than what we have in the UK at the moment.

Thank you very much, bye-bye.

Thank you, Tadeu.

Telephone Operator
Thank you for joining today’s call, you may now disconnect. Host, please stay on the line and await further instruction.

END