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Project Star 2012: Presentation of results

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2 July 2013

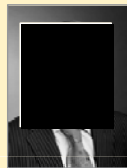
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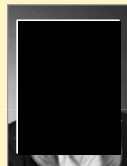
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Introduction

Introduction



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[REDACTED], KPMG

Objectives for today

- Provide an overview of developments in the EU illicit cigarette trade in 2012 identified as a result of Project Star. The presentation will cover;
 - Methodology
 - Market overview
 - C&C levels
 - C&C flows
 - Illicit whites
 - Summary
- A document containing detailed results for each Member State will be available following the presentation
- KPMG is happy to provide clarifications or respond to questions both at the end of the session and on an ongoing basis

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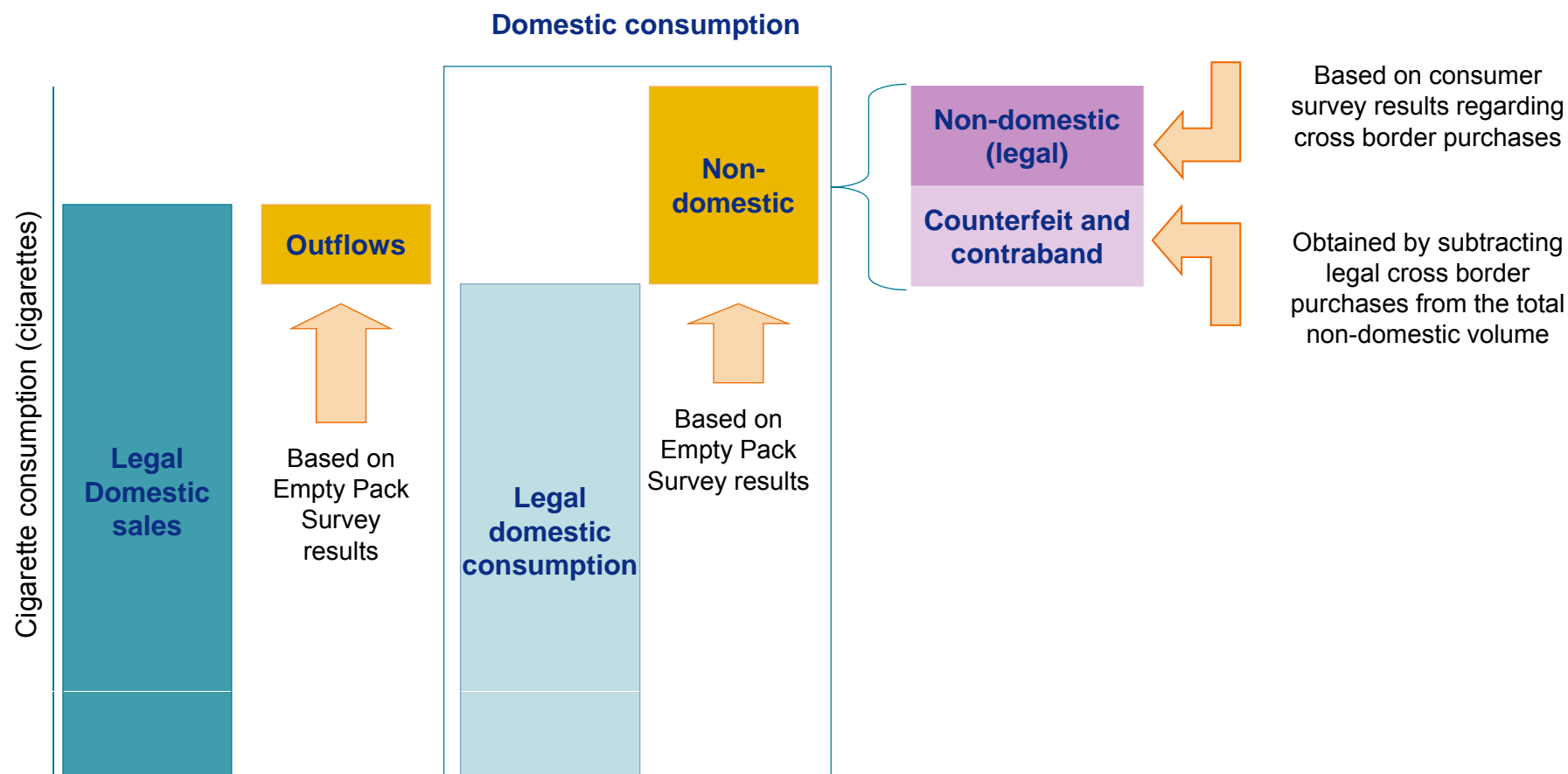
C&C flows

Illicit whites

Summary

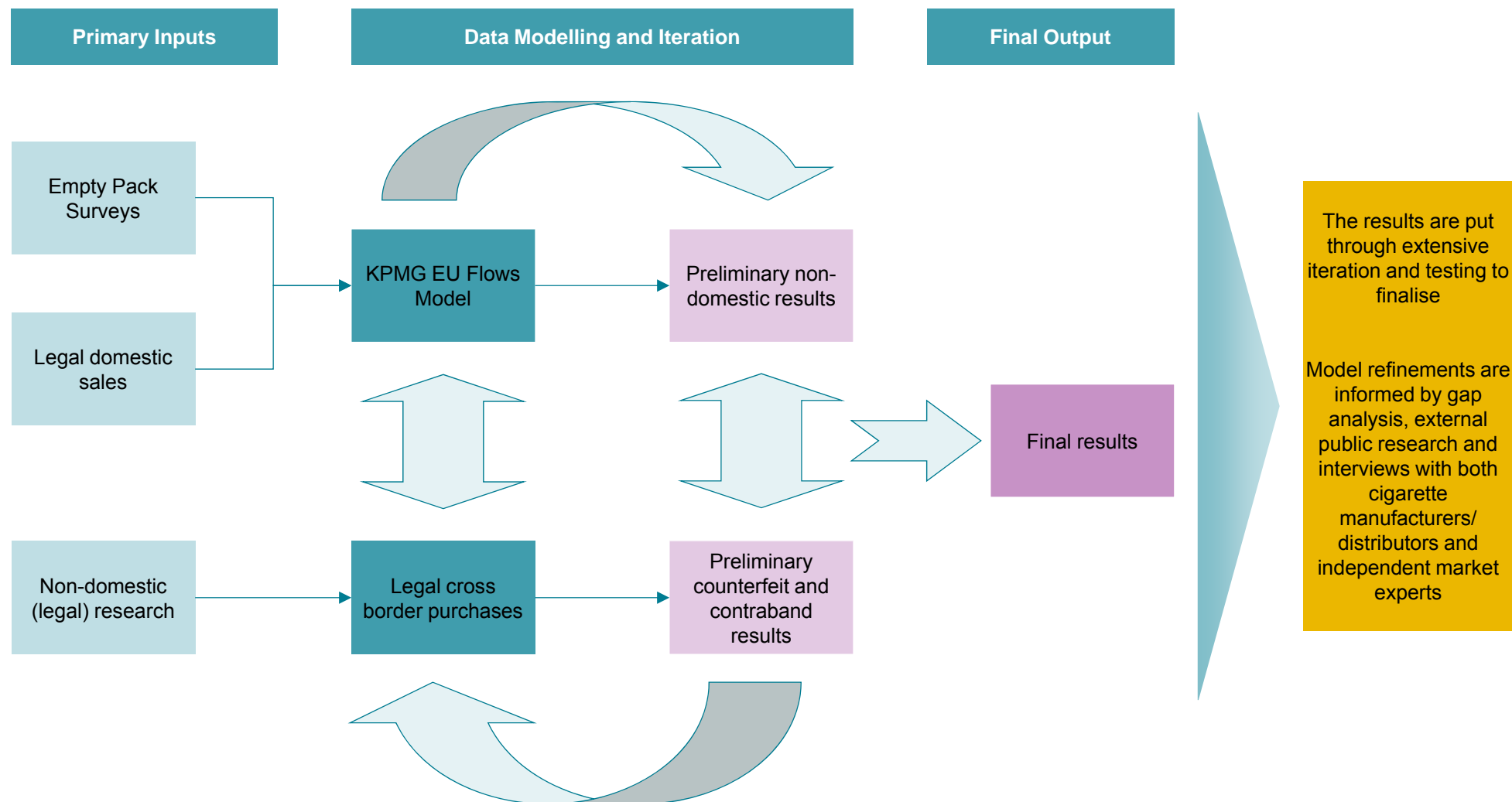
Appendix

Project Star uses legal domestic sales, Empty Pack Survey results and consumer research to quantify the volume of C&C cigarettes consumed in the EU



The Project Star methodology was developed by KPMG and approved by OLAF. It has been deployed on a consistent basis since 2006, enabling comparisons to be made between counterfeit and contraband volumes from year to year

Our approach integrates multiple sources with custom-built analytical tools



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Non-domestic consumption in the EU

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C&C has continued to grow since 2006, reaching 11.1% in 2012. ND(L) also increased in 2012, for the first time since 2006

ND(L) and C&C share of total consumption
2006-2012⁽¹⁾



ND(L) volume (bn cigarettes)	31.0	30.3	29.0	25.0	23.7	23.3	24.8
C&C volume (bn cigarettes)	56.8	60.6	60.5	61.1	64.2	65.3	65.5

Source: (1) EU Flows Model 2006 – 2012

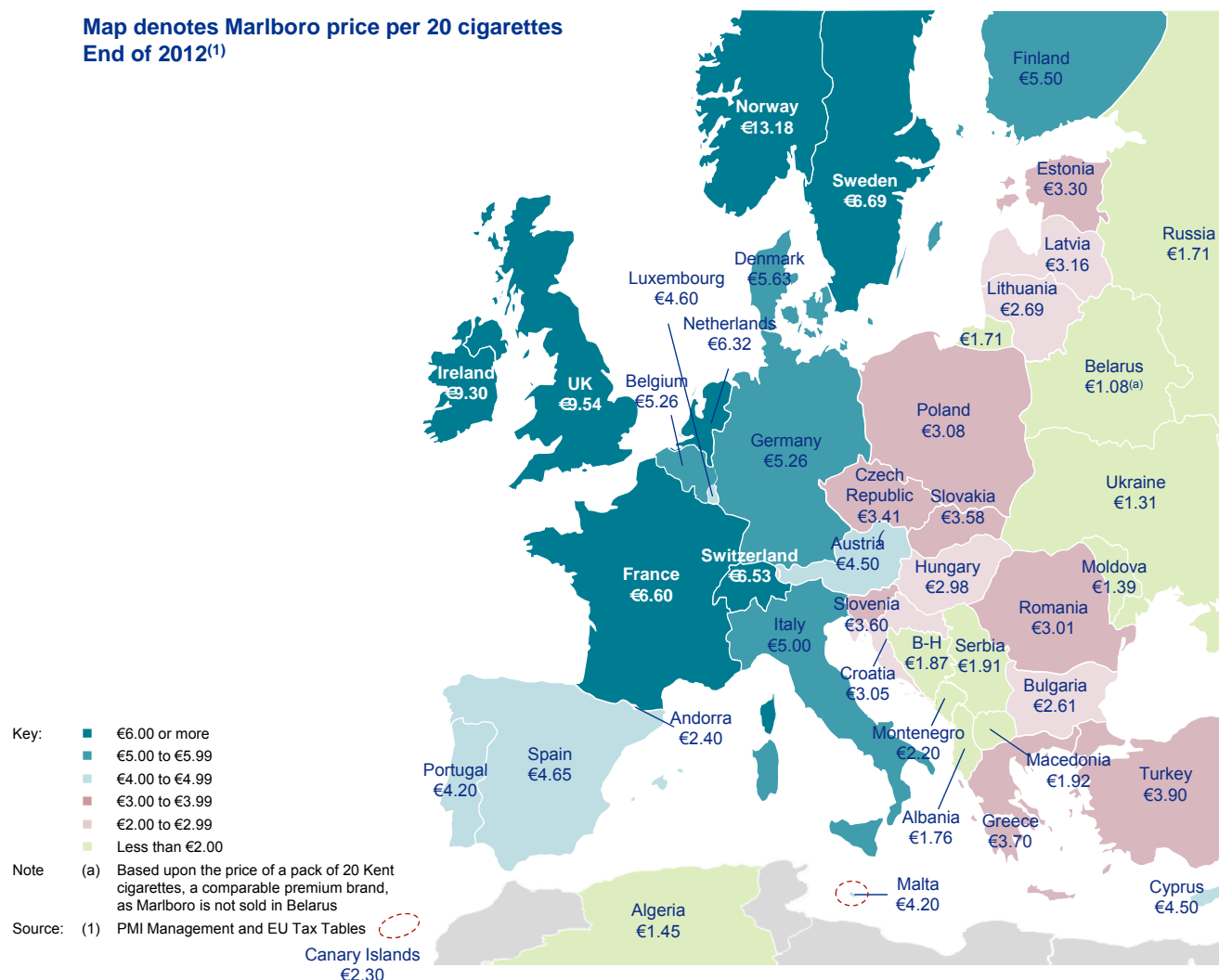
EU Price differentials

Price gaps have narrowed between EU countries; however, prices in countries on the Eastern border remain up to 8 times lower

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Country	End of 2011	End of 2012	Price change
Belarus (a)	0.58	1.08	86.4%
Moldova	1.05	1.39	32.4%
Hungary	2.33	2.98	28.0%
Ukraine	1.09	1.31	20.4%
Turkey	3.25	3.90	20.0%
Russia	1.43	1.71	19.8%
Sweden	5.66	6.69	18.2%
Norway	11.21	13.18	17.6%
UK	8.26	9.54	15.4%
Serbia	1.66	1.91	15.4%
Netherlands	5.47	6.32	15.4%
Slovenia	3.20	3.60	12.5%
Finland	5.00	5.50	10.0%
Estonia	3.00	3.30	10.0%
Spain	4.25	4.65	9.4%
Albania	1.62	1.76	8.4%
Poland	2.86	3.08	7.5%
France	6.20	6.60	6.5%
Slovakia	3.37	3.58	6.3%
Greece	3.50	3.70	5.7%
Latvia	2.99	3.16	5.7%
Romania	2.87	3.01	4.9%
Denmark	5.37	5.63	4.8%
Bosnia	1.79	1.87	4.6%
Luxembourg	4.40	4.60	4.5%
Lithuania	2.58	2.69	4.5%
Croatia	2.93	3.05	4.3%
Belgium	5.05	5.26	4.2%
Switzerland	6.34	6.53	3.0%
Czech Republic	3.32	3.41	2.8%
Cyprus	4.40	4.50	2.3%
Ireland	9.10	9.30	2.2%
Italy	4.90	5.00	2.0%
Germany	5.16	5.26	2.0%
Bulgaria	2.56	2.61	2.0%
Montenegro	2.19	2.20	0.5%
Austria	4.50	4.50	0.0%
Malta	4.20	4.20	0.0%
Portugal	4.20	4.20	0.0%
Algeria	1.46	1.45	-0.7%
Macedonia	1.94	1.92	-0.9%
Canary Islands	2.40	2.30	-4.2%

Map denotes Marlboro price per 20 cigarettes
End of 2012⁽¹⁾

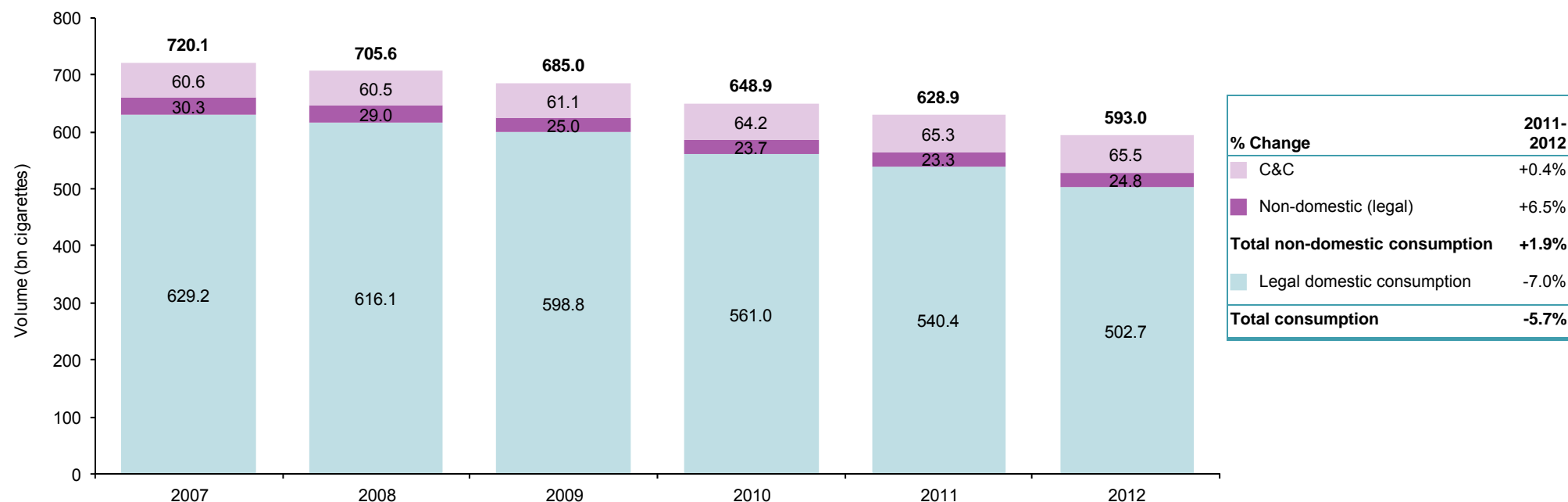


EU total consumption

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Non-domestic volumes increased by 1.9% in 2012, while total cigarette consumption declined by 5.7%

**Total cigarette consumption within the EU by type
2007-2012^{(1)(a)}**



Source: (1) KPMG analysis based on EPS, LDS and ND(L) research

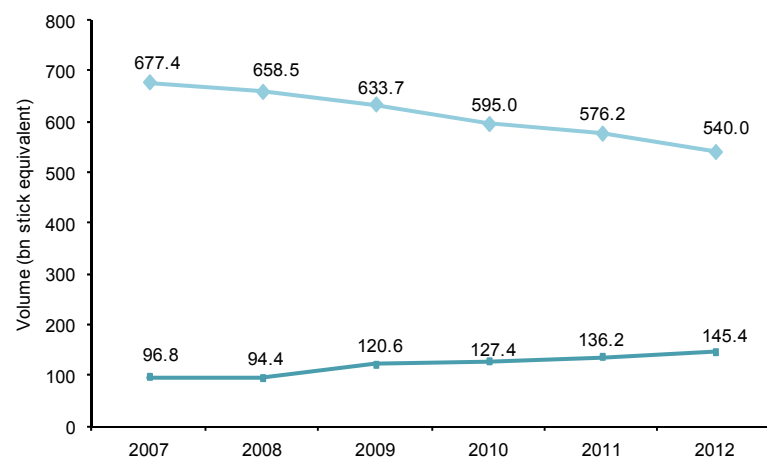
Note: (a) Total cigarette consumption within the EU by type is shown from 2007, as Romania and Bulgaria were not included in the 2006 study.

Total tobacco consumption in the EU

The decline in legal domestic cigarette sales by 6.3% was partly offset by an increase in non-domestic flows and OTP sales

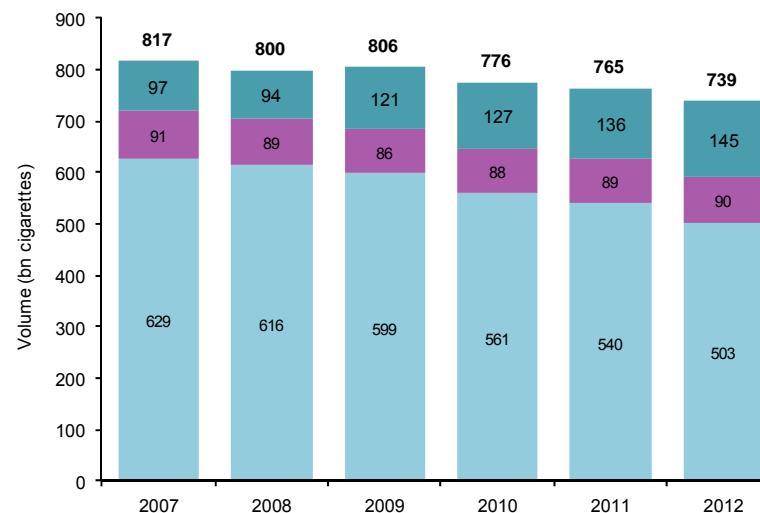
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Legal domestic sales of manufactured cigarettes and OTP
2007-2012^{(1)(a)(b)}



% Change		2011-2012
◆	Cigarettes (Legal Domestic sales)	-6.3%
■	OTP (Legal Domestic sales)	6.8%

European Union total cigarette consumption and OTP LDS (bn sticks)
2006-2012^{(1)(a)(b)}



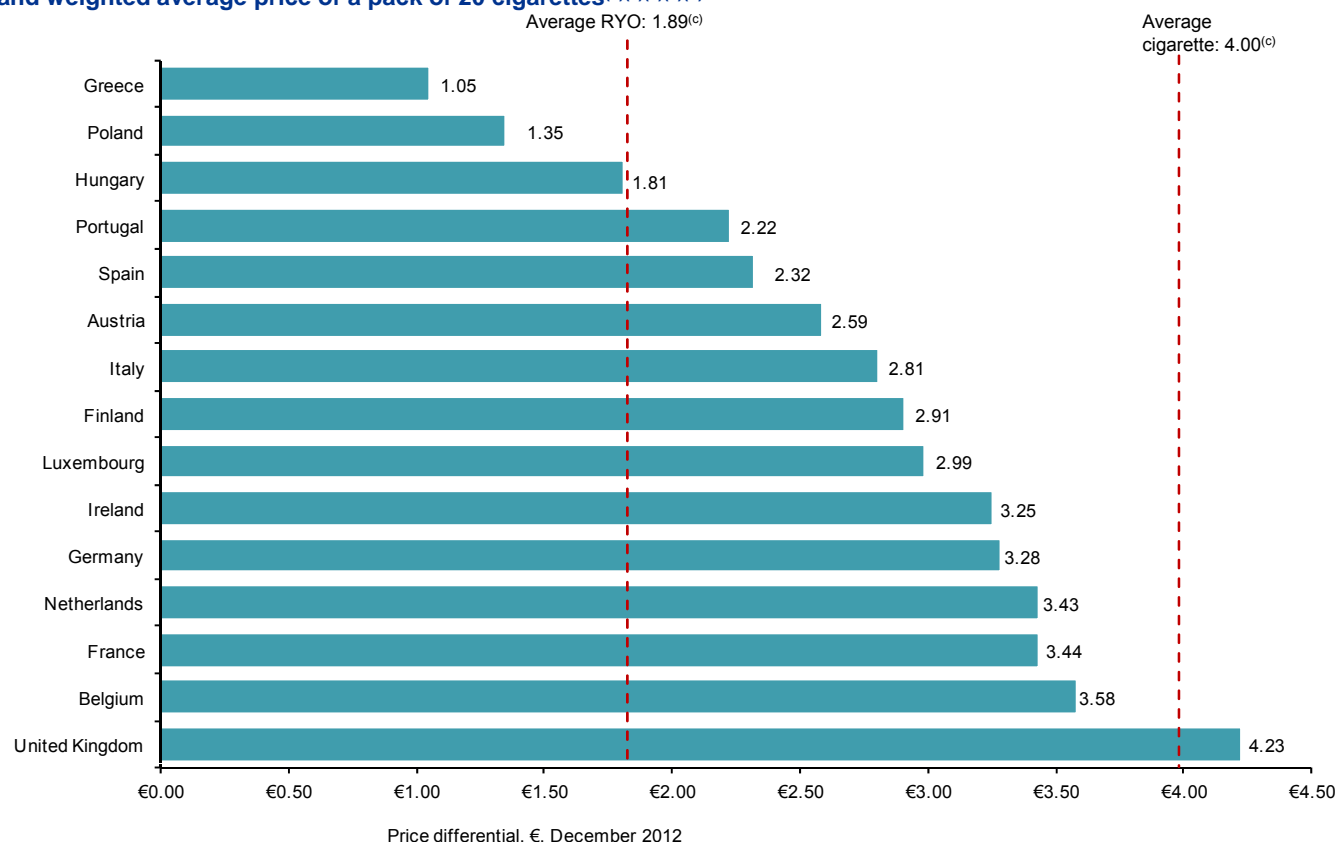
% Change		2011-2012
■	OTP (legal domestic sales)	6.8%
■	Non-domestic consumption	2.0%
■	Legal domestic consumption	-7.0%
Total consumption (including OTP)		-3.4%

Note: (a) OTP is defined as MYO, MYO volume tobacco, RYO tobacco and cigarillos as appropriate, whose cigarette equivalents are defined as 0.73g of tobacco per cigarette for MYO and 0.6g per cigarette for RYO and MYO volume tobacco. This definition and conversion rates have been applied for Project Star 2012 and may differ in previous reports.
(b) Significant volumes of green leaf are understood to be consumed in Poland, Czech Republic, Hungary and Bulgaria which are not captured in the LDS data above.

Source: (1) KPMG analysis based on EPS, LDS and ND(L) research

In most European markets, the price differential between OTP and manufactured cigarettes is significant

Price differential between weighted average price of RYO 20 cigarette equivalents and weighted average price of a pack of 20 cigarettes^{(1)(2)(3)(a)(b)}



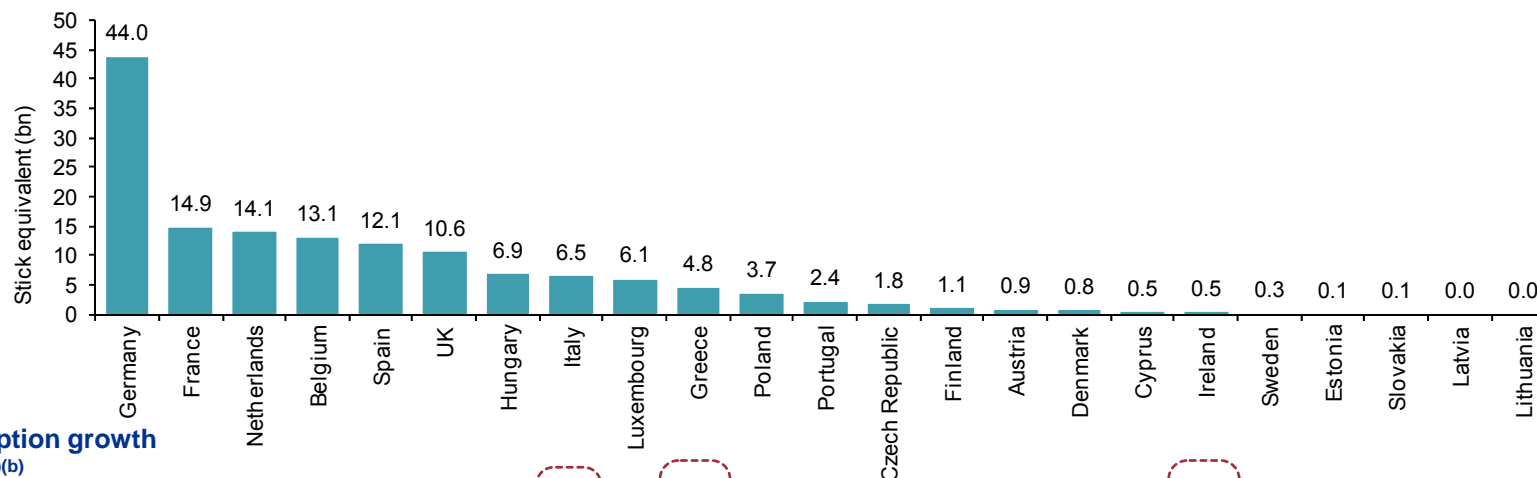
Source: (1) European Commission "Excise Duty tables", January 2013
 (2) Italy, Ireland and Greece – PMI estimates
 (3) UK – KPMG estimate based on Euromonitor sales data

Note: (a) Total tobacco market defined as total legal domestic sales of manufactured cigarettes and RYO cigarette equivalents (0.65 grams cigarette equivalent rate), with the price gap being defined as the cost between the weighted average price of pack of 20 and 20 roll-your-own cigarettes. For Ireland no weighted average price of RYO was available so the cheapest price of 20 cigarettes and cheapest RYO cigarette equivalent was used.
 (b) Weighted average of European Commission excise duty tables.
 (c) Simple average across each country

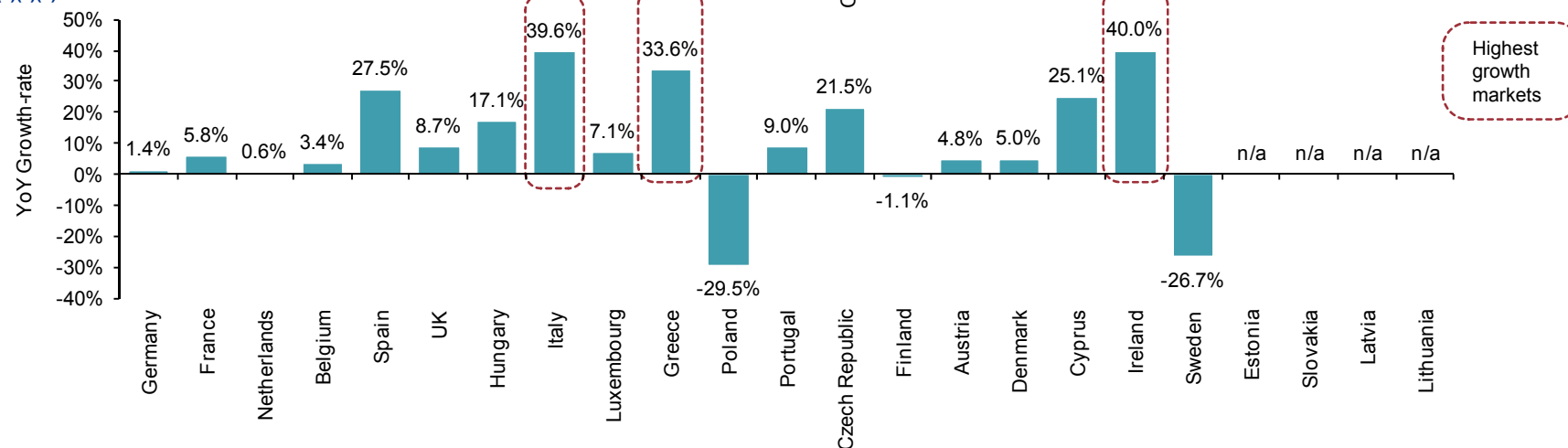
OTP consumption and growth in the EU

Countries with the largest growth vs 2011 were Ireland, Italy and Greece

OTP consumption, cigarette equivalent volumes
2012^{(1)(a)(b)}



OTP consumption growth
2011-2012^{(1)(a)(b)}



Source: (1) KPMG analysis based on EPS, LDS and ND(L) research

Note: (a) OTP is defined as MYO, MYO volume tobacco, RYO tobacco and cigarillos as appropriate, whose cigarette equivalents are defined as 0.73g of tobacco per cigarette for MYO and 0.6g per cigarette for RYO and MYO volume tobacco. This definition and conversion rates have been applied for Project Star 2012 and may differ in previous reports.

(b) Significant volumes of green leaf are understood to be consumed in Poland, Czech Republic, Hungary and Bulgaria which are not captured in the LDS data above

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C&C flows

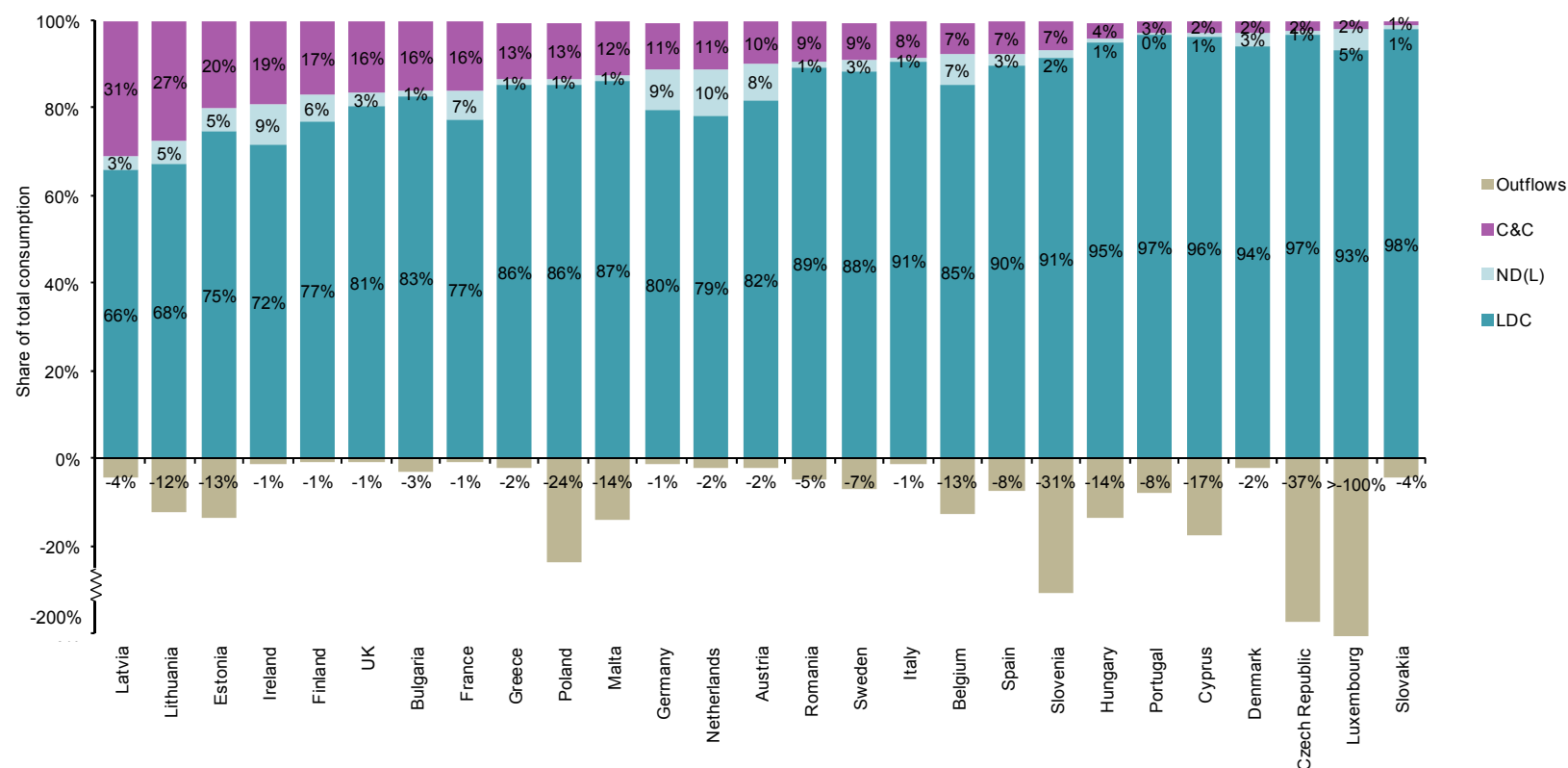
Illicit whites

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The Baltic countries had the highest non-domestic and C&C incidence as a proportion of total cigarette consumption

Total cigarette consumption by type 2012⁽¹⁾



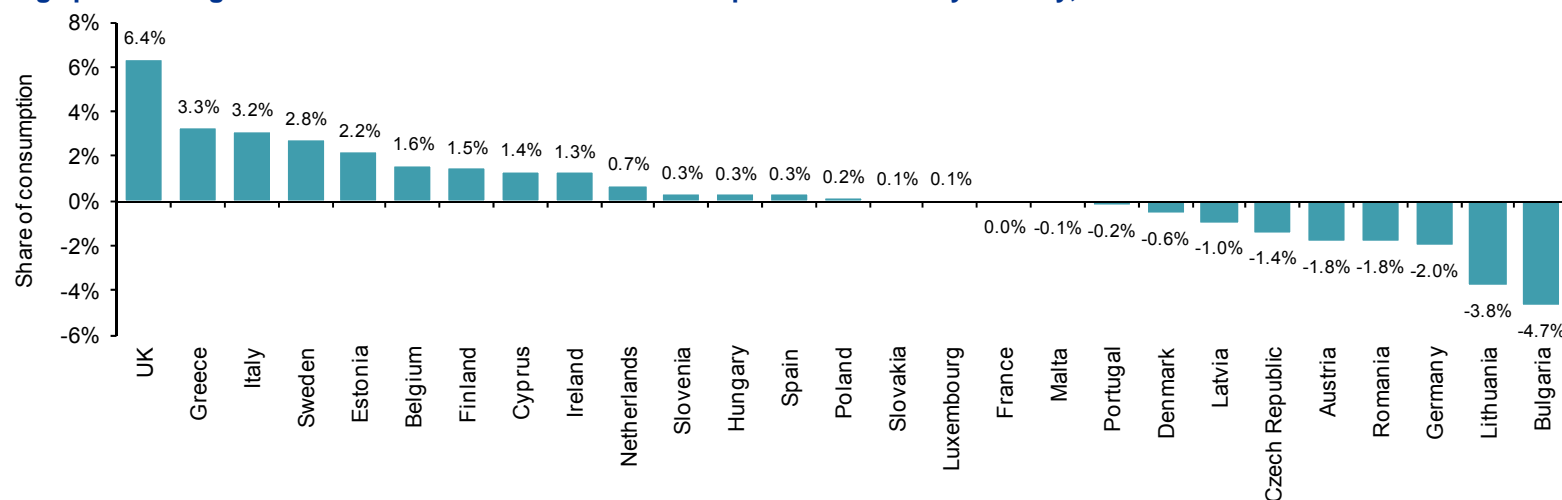
Source: (1) KPMG analysis based on EPS, LDS and ND(L) research

Non-domestic C&C consumption in the EU

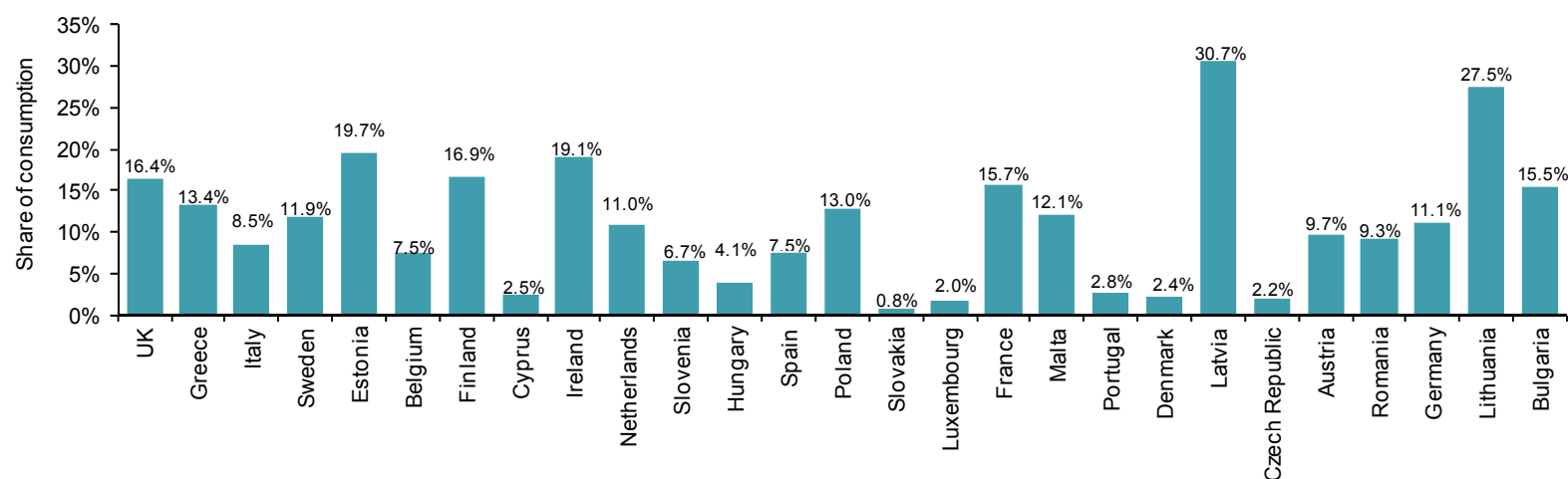
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The UK experienced the highest increase of C&C at 6.4 percentage points, followed by Greece and Italy at +3.3 and +3.2 points respectively

Percentage point change in counterfeit and contraband consumption incidence by country, 2011 vs 2012⁽¹⁾



Counterfeit and Contraband consumption incidence by country, 2012⁽¹⁾



Source: (1) KPMG analysis based on EPS, LDS and ND(L) research

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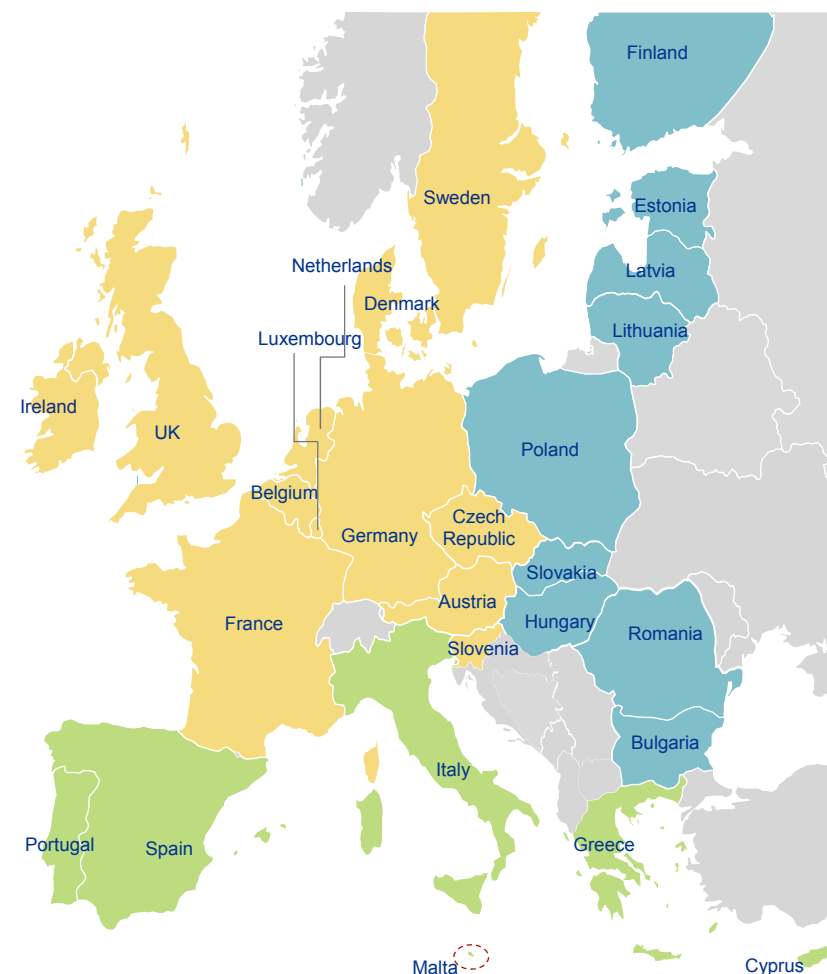
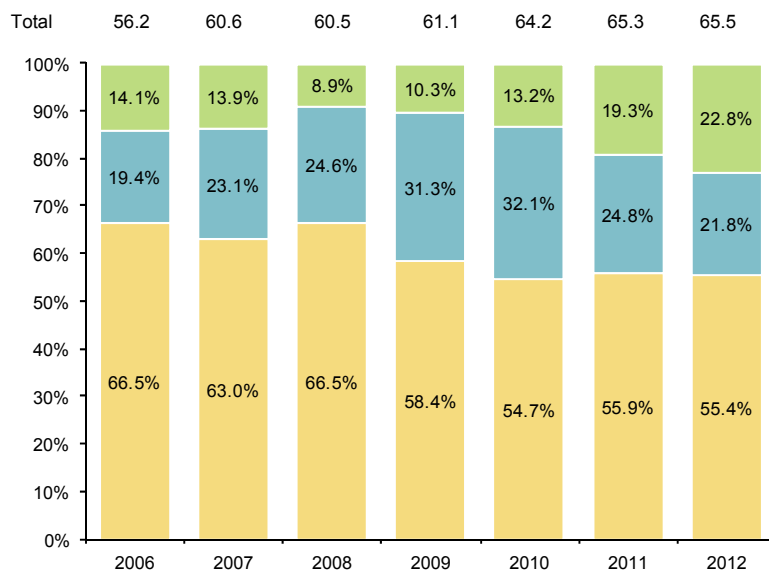
Illicit whites

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The share of EU illicit cigarette consumption accounted for by the Southern European countries continued to rise in 2012

Share of total EU C&C inflows by destination regions
2006-2012⁽¹⁾



Key: ■ Southern EU countries – Cyprus, Greece, Italy, Malta, Portugal and Spain

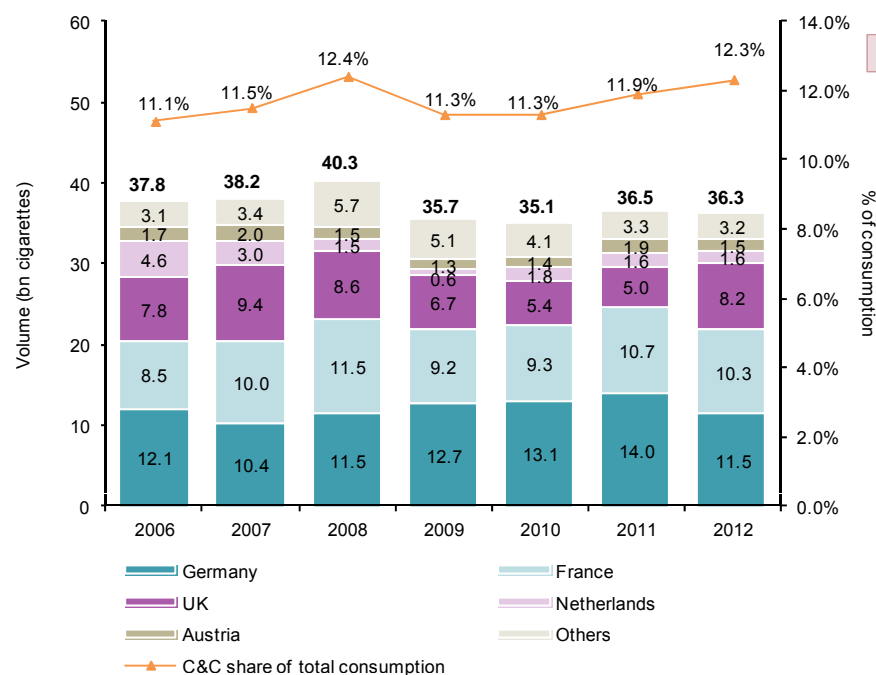
■ Eastern border EU countries – Bulgaria, Estonia, Finland, Hungary, Latvia, Lithuania, Poland, Romania and Slovakia

■ Western and Central EU countries – Austria, Belgium, Czech Republic, Denmark, France, Germany, Ireland, Luxembourg, Netherlands, Slovenia, Sweden and UK

Source: (1) KPMG analysis based on EPS, LDS and ND(L) research

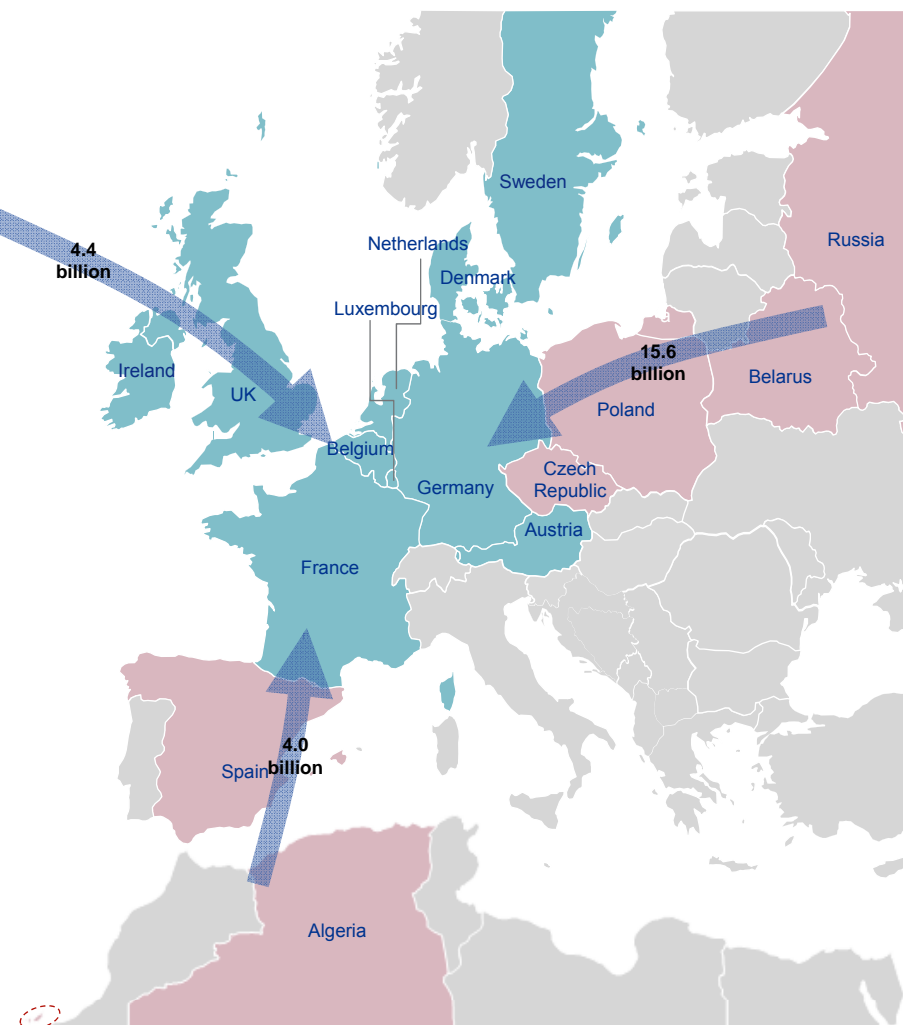
C&C flows to Western EU countries remained stable in volume; however, there was an increase to the UK from Eastern Europe and Spain

C&C inflows to Western EU countries
2006-2012⁽¹⁾



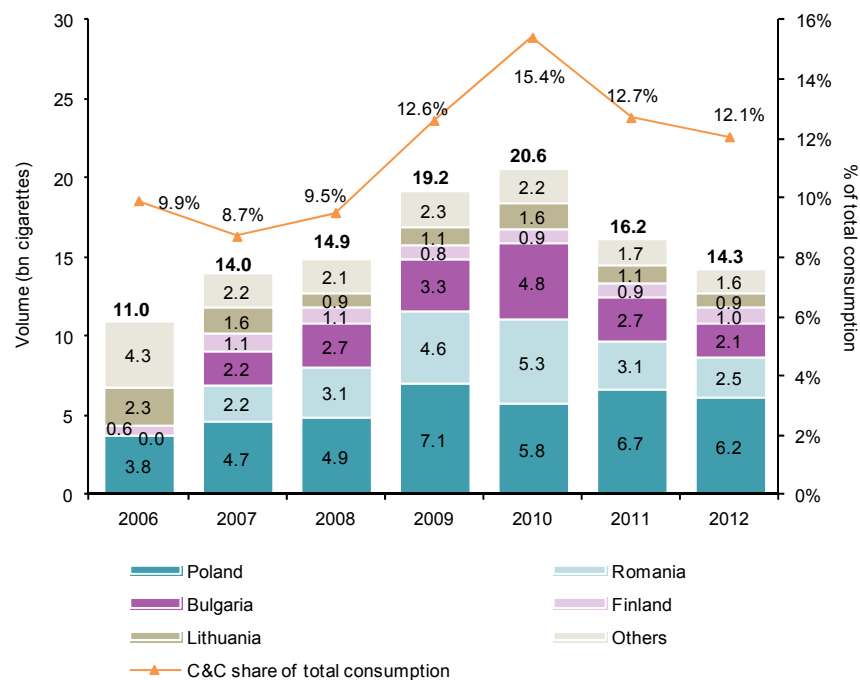
Key: ■ Western EU countries
■ Source countries with inflows of >0.5 billion cigarettes in 2012 – total flows from highlighted source countries to Western Europe

Source: (1) KPMG analysis based on EPS, LDS and ND(L) research



Eastern European countries' C&C inflows declined, mainly as a result of lower flows into Bulgaria and Romania

C&C inflows to Eastern EU countries
2006-2012⁽¹⁾

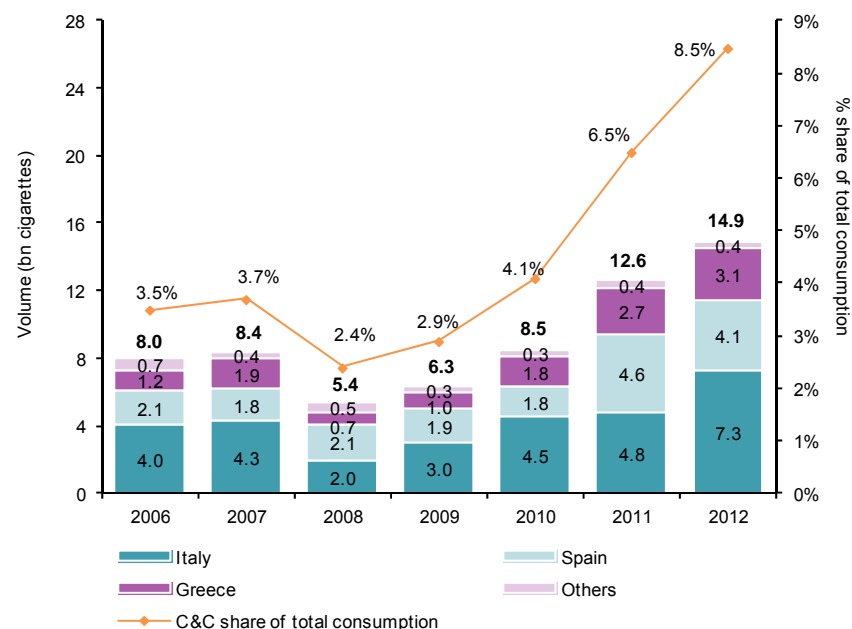


Key: ■ Eastern EU countries
■ Source countries with inflows of >0.5 billion cigarettes in 2012 - total flows from highlighted source countries to Eastern Europe

Source: (1) KPMG analysis based on EPS, LDS and ND(L) research

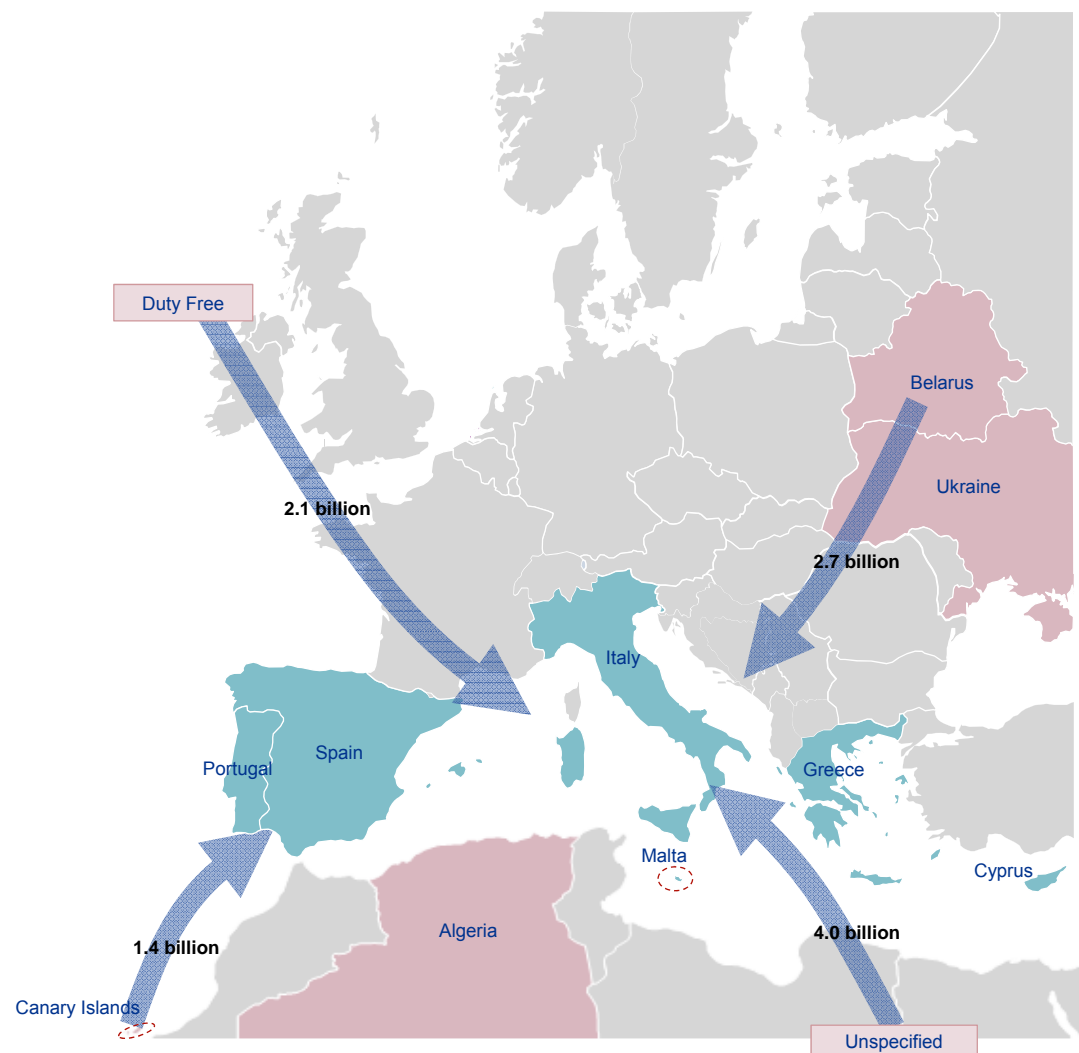
Southern European countries' C&C inflows continued to increase, mainly as a result of a 50% increase in Italy between 2011 and 2012

C&C inflows to Southern EU countries
2006-2012⁽¹⁾



Key:
■ Southern EU countries
■ Source countries with inflows of > 0.5 billion cigarettes in 2012 - total flows from highlighted source countries to Southern Europe

Source: (1) KPMG analysis based on EPS, LDS and ND(L) research

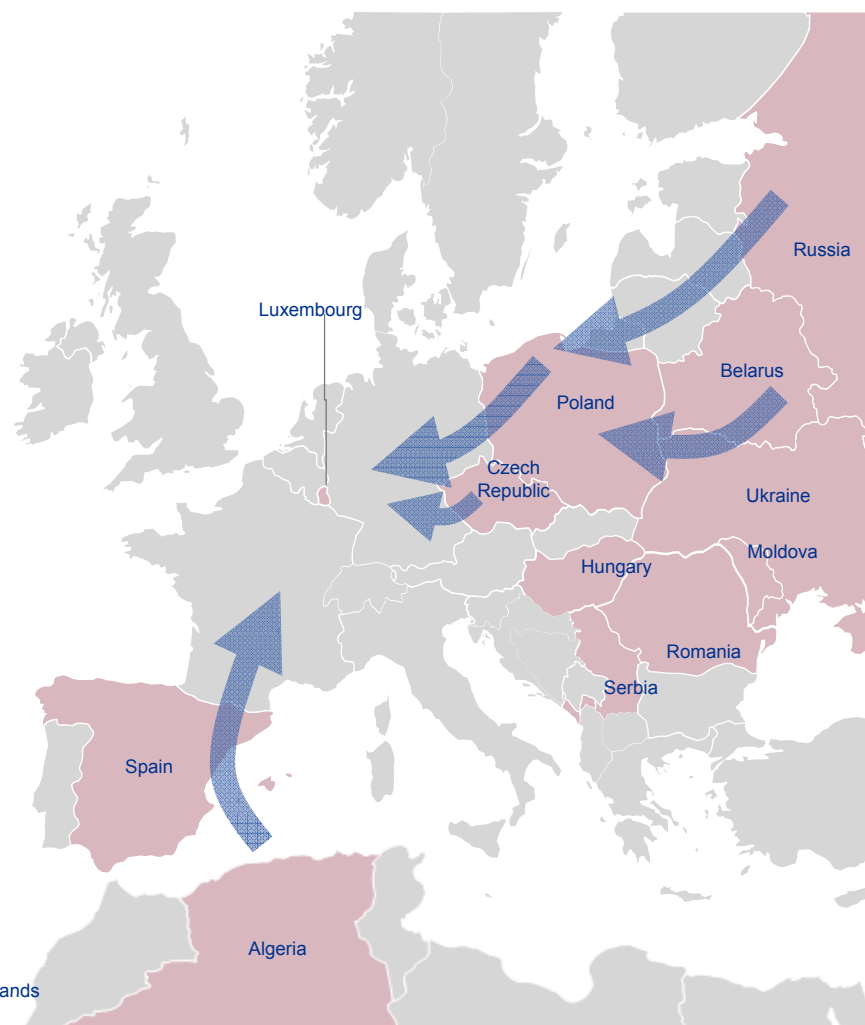
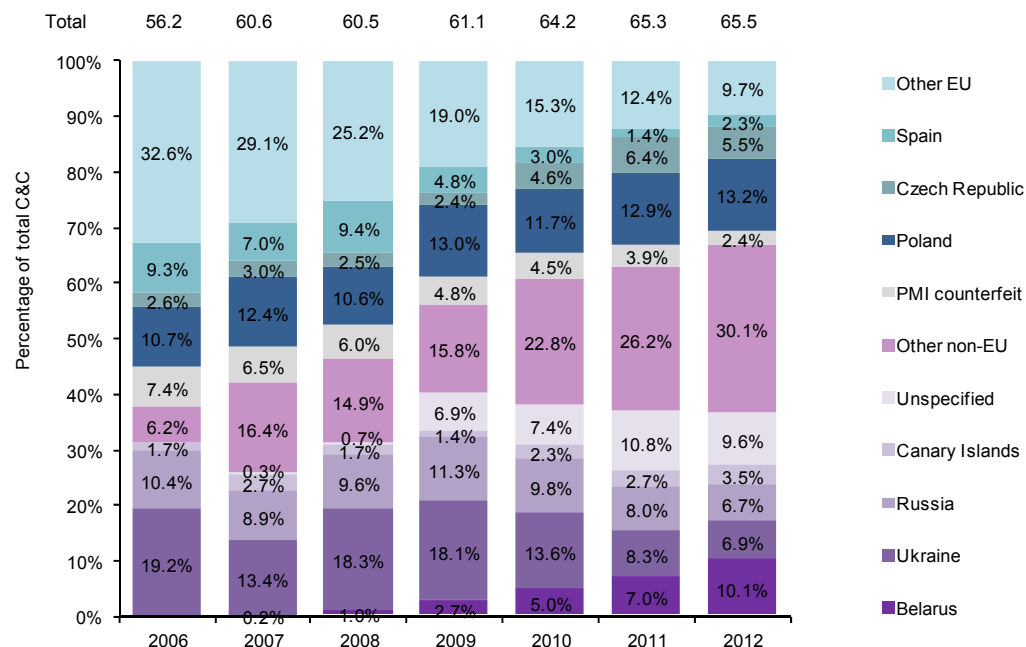


C&C source countries

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The largest source countries of C&C are from outside the EU, predominantly Belarus, which grew by 3.1 percentage points vs 2011. Within the EU Poland, the Czech Republic and Spain continue to be major source countries

Main non-domestic outflow countries and outflows
2012⁽¹⁾

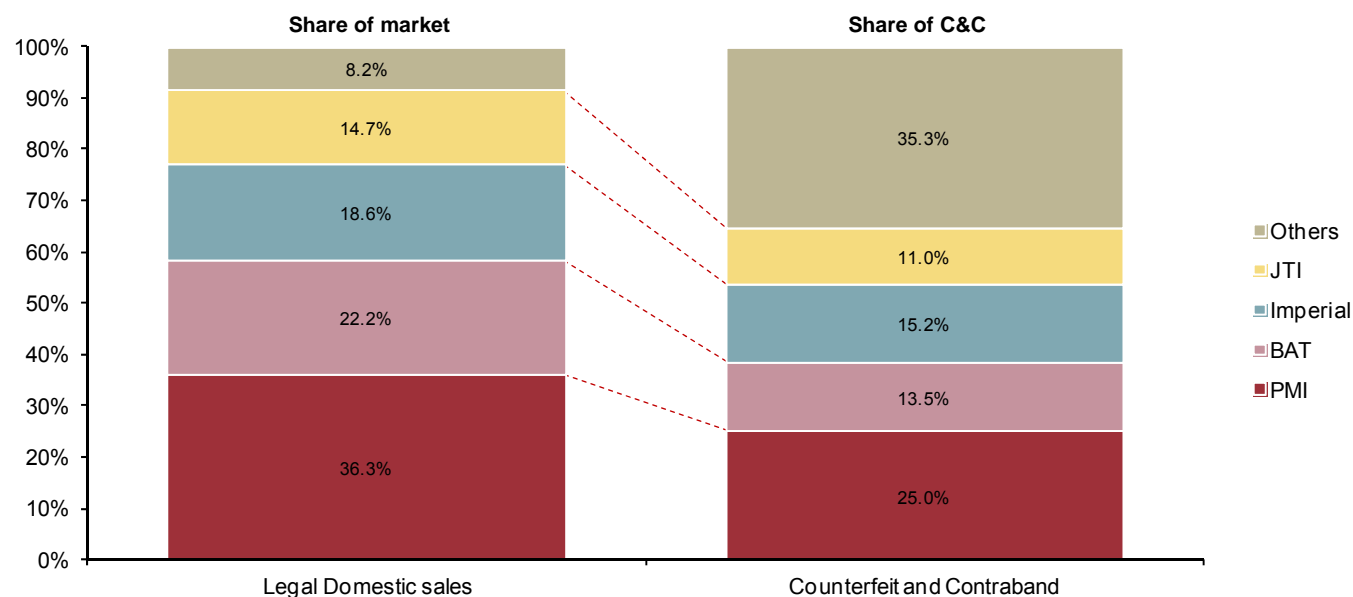


Key: ■ Source countries with outflows of > 0.5 billion cigarettes in 2012

Source: (1) KPMG analysis based on EPS, LDS and ND(L) research

The share of C&C accounted for by the big four manufacturers is significantly lower than their market share of legal domestic sales

EU27 share of manufacturers by consumption type (LDS, C&C)
2012^{(1)(a)}



Source: (1) KPMG analysis based on EPS, LDS and ND(L) research

Note: (a) The counterfeit and contraband calculations are made on a brand basis with brands allocated to each manufacturer. This creates limitations where there are non-EU brands manufactured by the big four manufacturers which are included in "others". In addition, there may be minor changes between the big 4 manufacturers where brands have been allocated to the manufacturer with the largest share and may exclude incidences where another manufacturer produces the same brand in a different territory.

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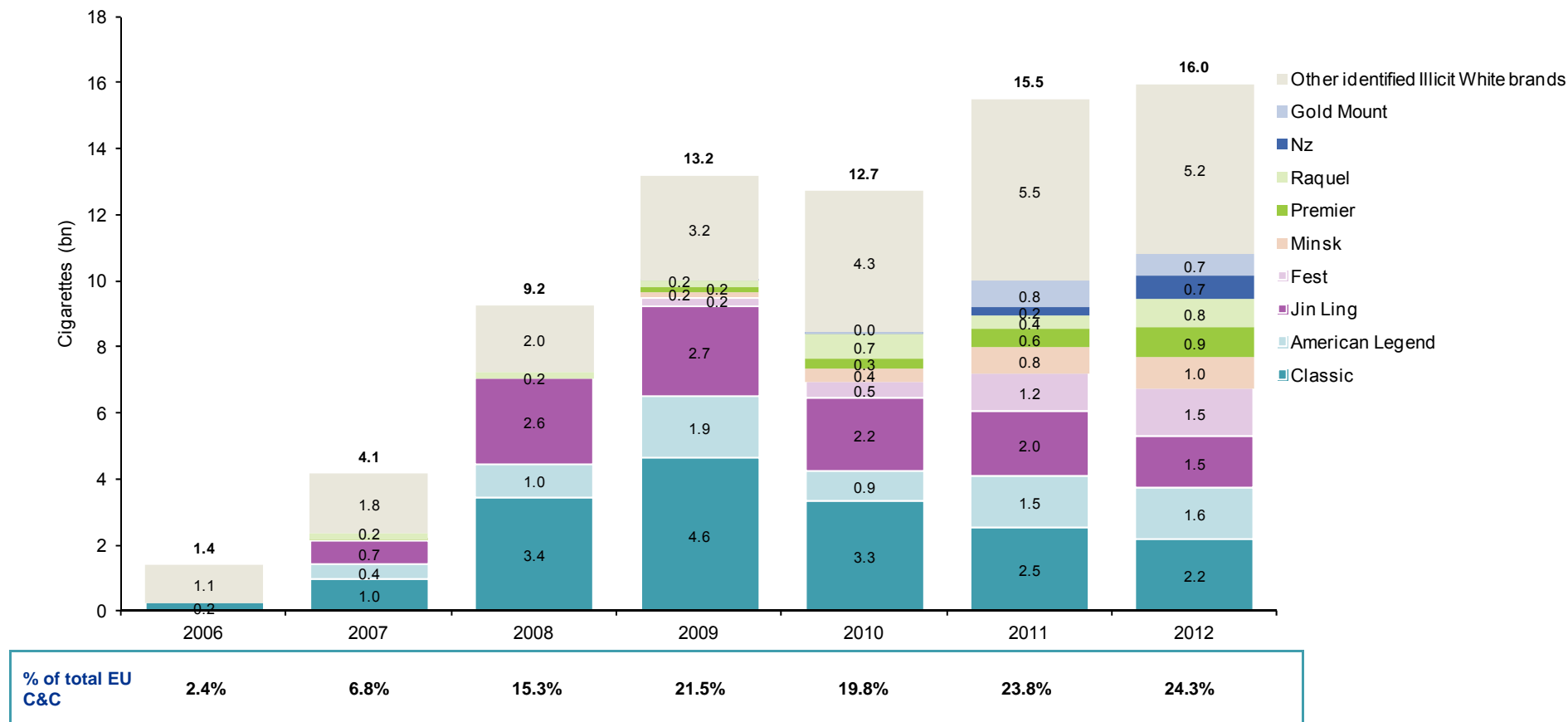
Appendix

Illicit whites

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Consumption of Illicit Whites increased by 3% in 2012, representing over 24% of total C&C volumes in the EU

Consumption of Illicit White brands 2006-2012^{(1)(a)}

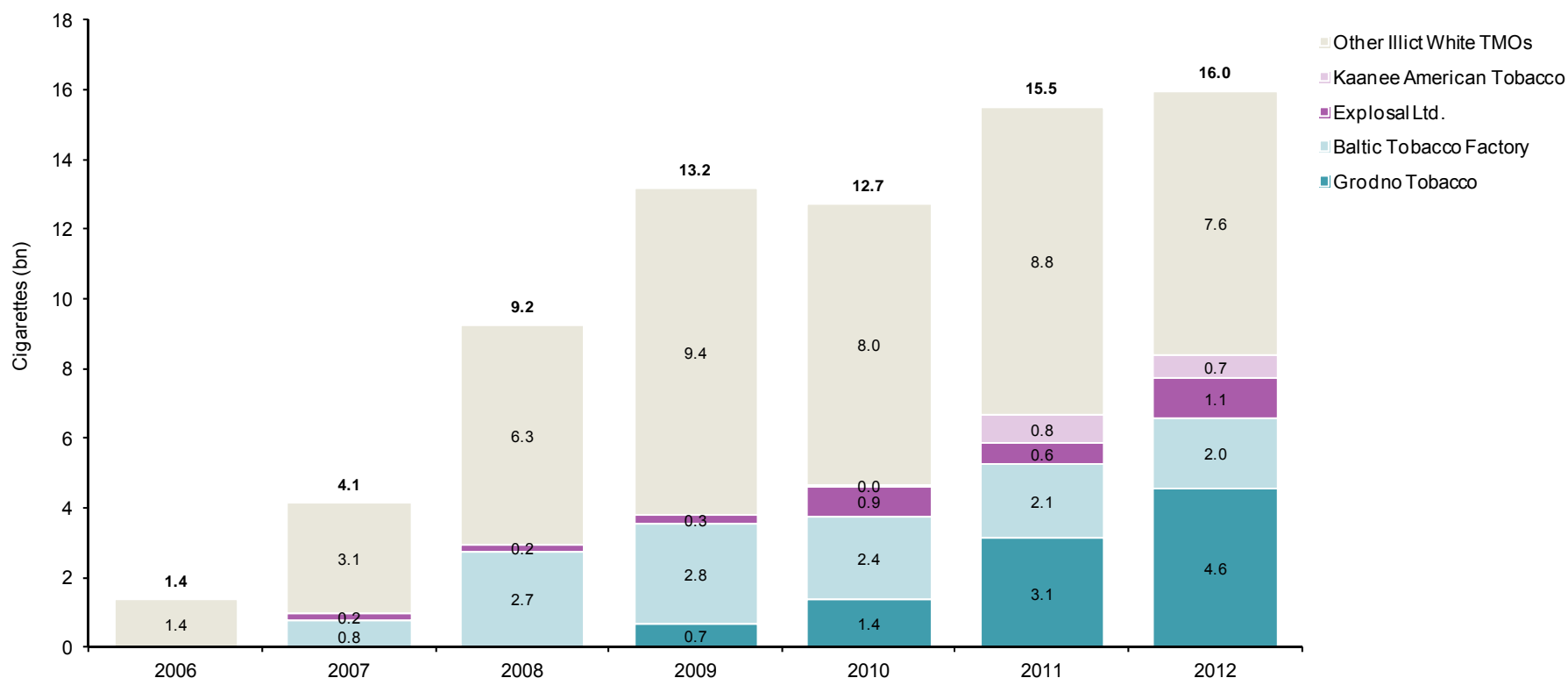


Note: (a) The analysis covers Illicit Whites brands as defined by PMI with at least 10 packs found in 2012.

Source: (1) KPMG analysis based on Empty Pack Surveys, legal domestic sales and non-domestic (legal) research.

Grodno tobacco is the fastest growing Illicit White manufacturer, with volumes increasing by 47% in 2012

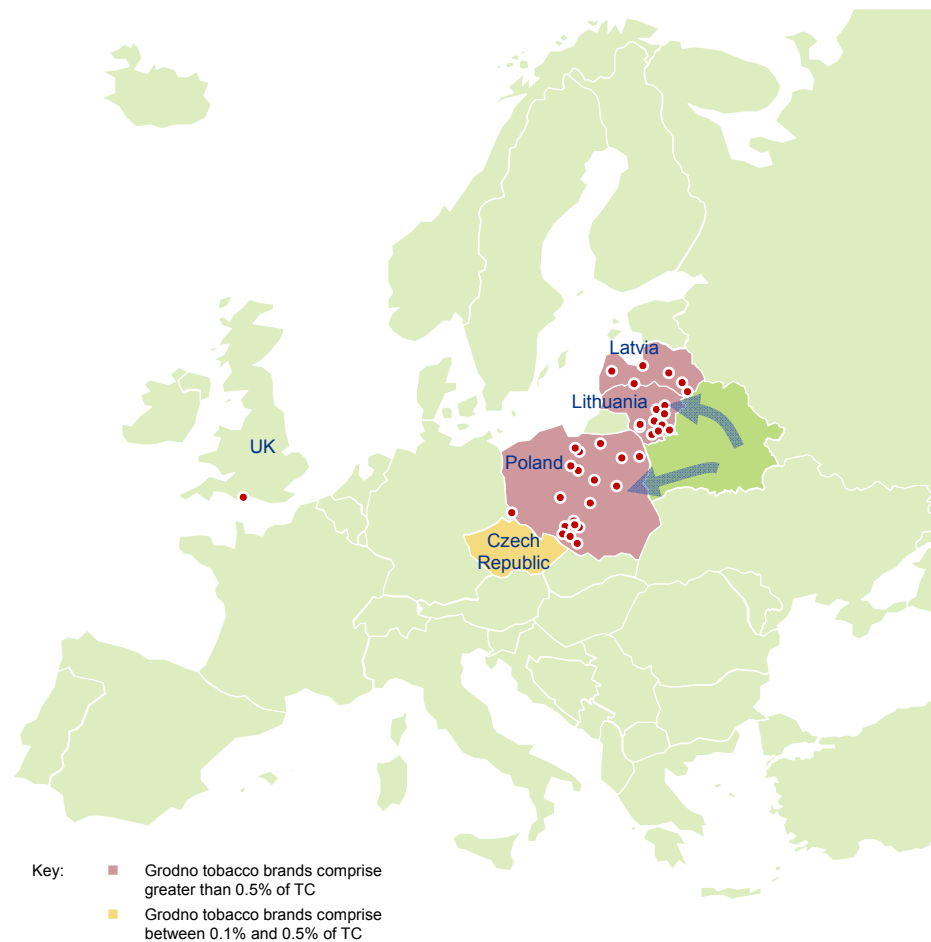
Consumption of Illicit White brands by manufacturer 2006-2012^{(1)(a)(b)(c)}



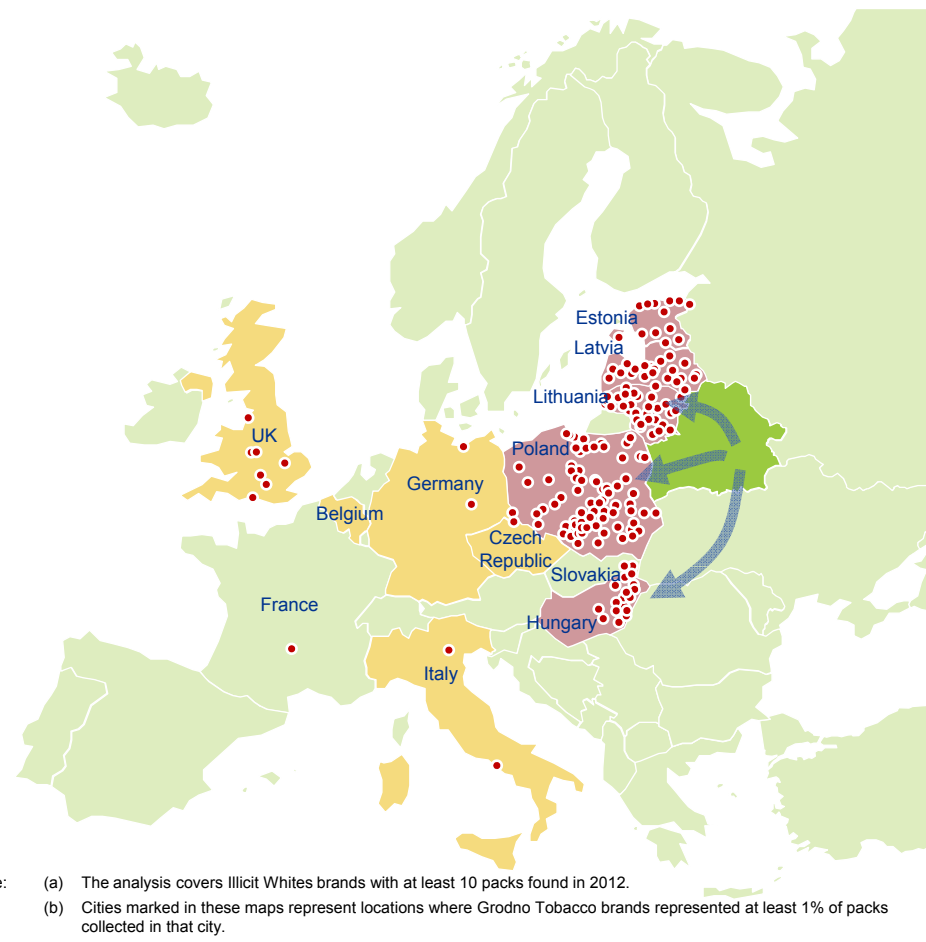
Note: (a) The analysis covers Illicit Whites brands as defined by PMI with at least 10 packs found in 2012.
 (b) Consumption represents the total consumption of each of the company's main brands, which may include packs labelled as Unspecified or immaterial volumes from packs labelled with another TMO.
 (c) Illicit White Manufacturers represent manufacturers of Illicit White brands as indicated by PMI.
 Source: (1) KPMG analysis based on Empty Pack Surveys, legal domestic sales and non-domestic (legal) research.

While Grodno Tobacco brands were present in 4 countries in 2009, they have become prevalent in 10 countries in 2012

Consumption of Grodno Tobacco brands
2009^{(1)(a)(b)}

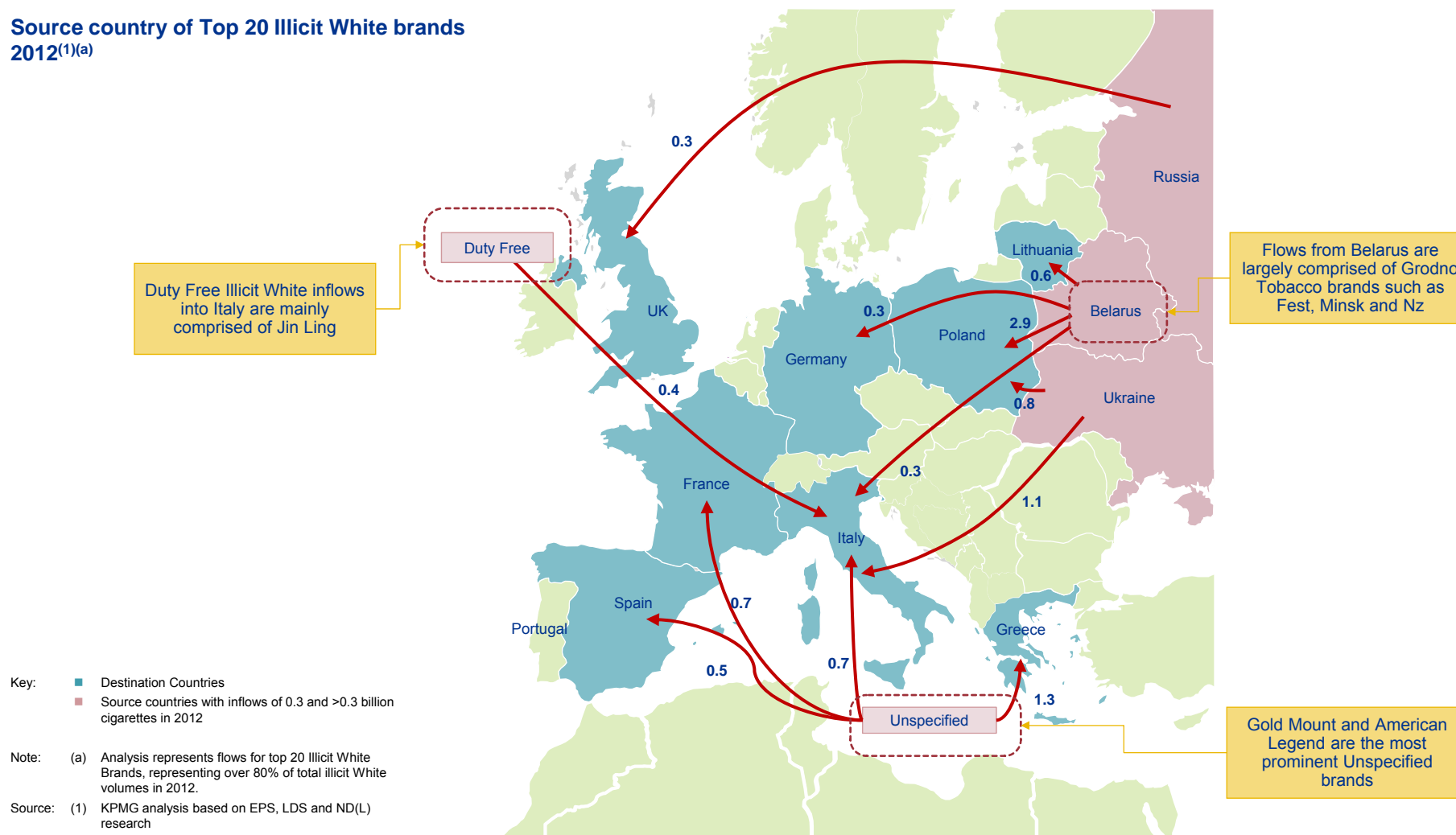


Consumption of Grodno Tobacco brands
2012^{(1)(a)(b)}



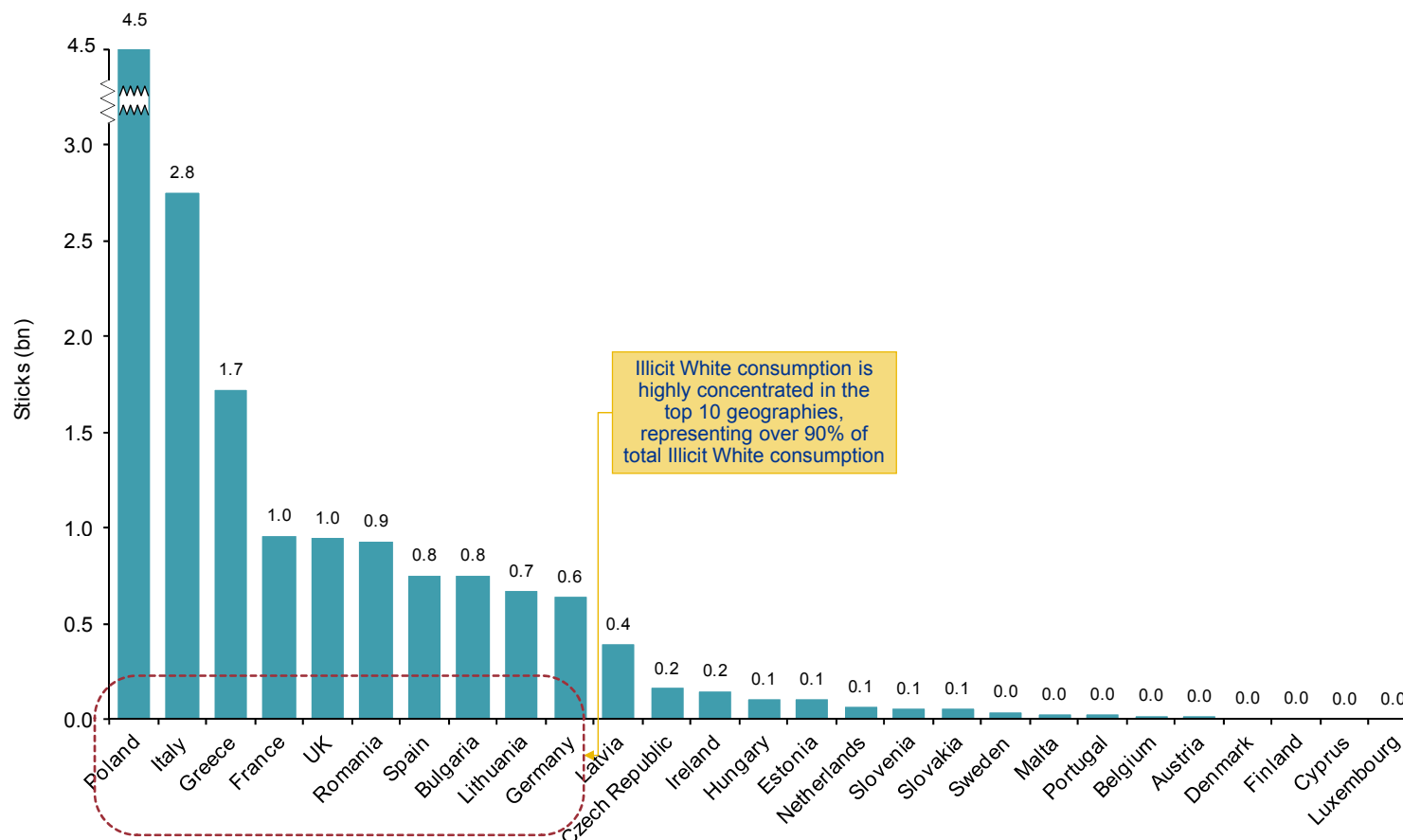
Belarus has become the largest source of Illicit White brands, particularly in Eastern Europe; Unspecified brands remain significant in Southern Europe

Source country of Top 20 Illicit White brands
2012^{(1)(a)}



Poland has the largest Illicit White consumption levels in Europe at 4.5 bn cigarettes; Italy and Greece have the next highest levels at 2.8 bn cigarettes and 1.7 bn cigarettes respectively

Illicit White consumption by country
2012^{(1)(a)}



Note: (a) The analysis covers Illicit Whites brands as defined by PMI with at least 10 packs found in 2012.

Source: (1) KPMG analysis based on Empty Pack Surveys, legal domestic sales and non-domestic (legal) research.

Italy and Greece have seen among the fastest growth rates of Illicit White volumes in 2012

Change in Illicit White consumption 2011/2012^{(1)(a)(b)}

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Project Star 2012: summary of key findings

- Although manufactured cigarette consumption declined in the EU in 2012, Counterfeit & Contraband (C&C) and Non Domestic Legal (ND(L)) increased
 - Cigarette consumption declined by 5.7% to 593 billion cigarettes in the EU 27
 - C&C and ND(L) both increased in 2012, both in absolute terms and as a proportion of consumption
- C&C inflows to Western EU countries remained stable in volume, however there was an increase in flows to the UK from Eastern Europe and Spain
- C&C inflows to Eastern European countries declined, mainly as a result of lower flows into Bulgaria and Romania
- C&C inflows to Southern European countries increased, mainly as a result of a 50% increase in flows to Italy between 2011 and 2012
- The largest source countries of C&C are from outside the EU
- Growth in Illicit White brands has predominantly been driven by emerging brands originating in Belarus
 - Consumption of Illicit White brands increased by 3% to 16 billion sticks in 2012, representing over 24% of total C&C volumes in the EU

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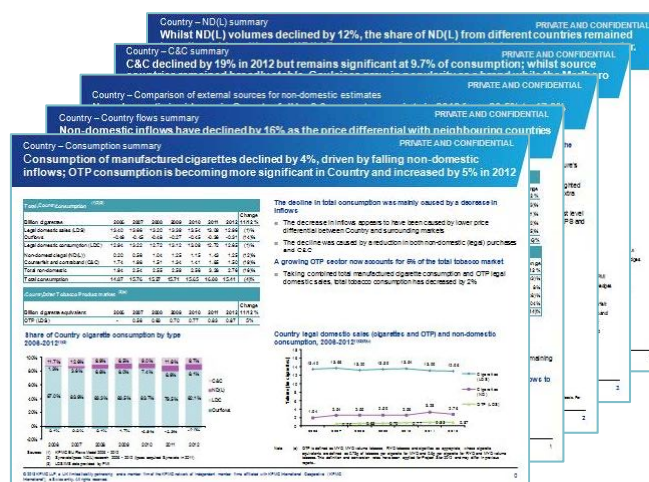
Illicit whites

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Appendix

Individual country results

Copies of both this presentation and individual country results for 2012 are available for your collection after this meeting





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