



GLOBAL TOBACCO IN TRANSITION

36TH UNITAB CONGRESS

BRUSSELS, 2018

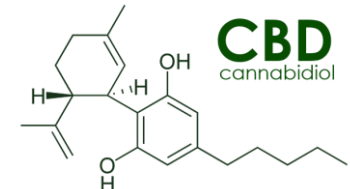
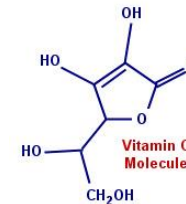
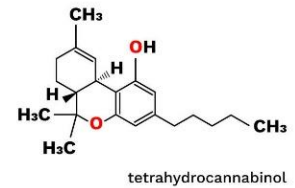
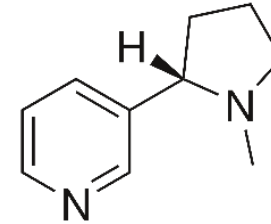
Navigating change, reinvigorating the core mission

2

Consumer and technological shifts disrupt the means but core purpose remain



“Mental wellbeing”



The 2017 global cigarettes market in figures

Volume performance best since 2014 but smoking prevalence drop speeds up



5,420 billion =
cigarettes consumed



2.8% = value growth
in cigarettes
(2.1% exc China)



1.4% = decline in
2017 v 2016
(**3.1%** exc China)



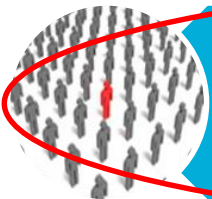
USD699 billion =
value of global
cigarettes market



11% = illicit
penetration of total
sales (exc China)



USD2.58 = average
amount spent per
pack of 20



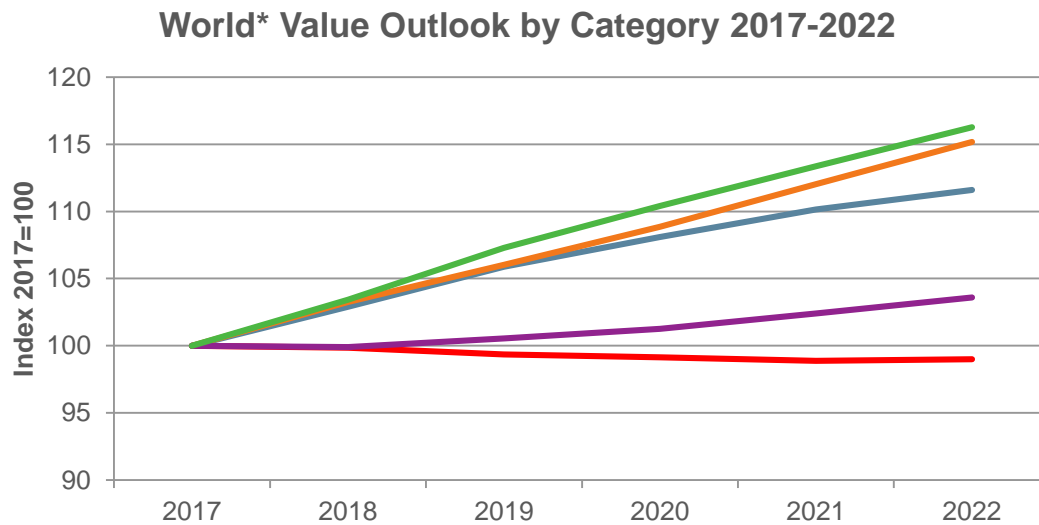
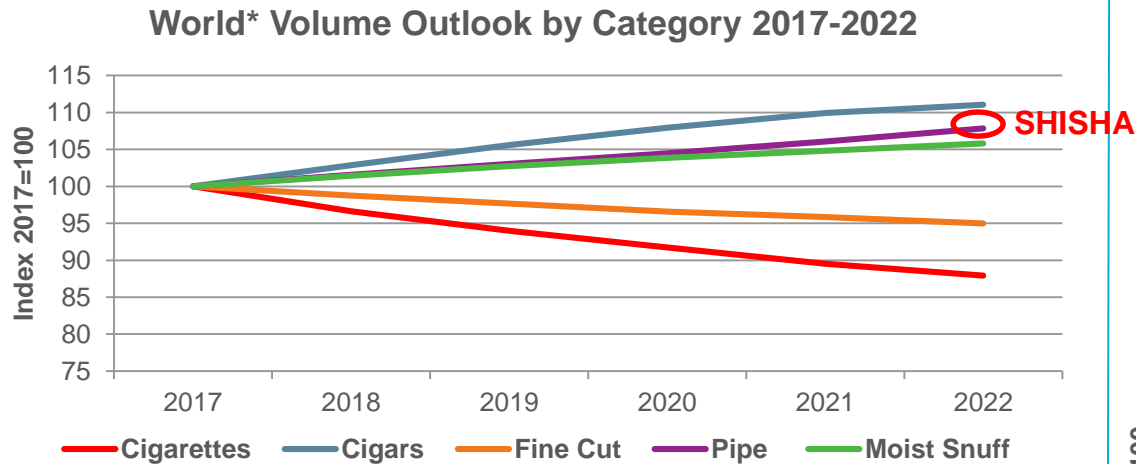
19.8% = proportion of
adults in the world
smoke



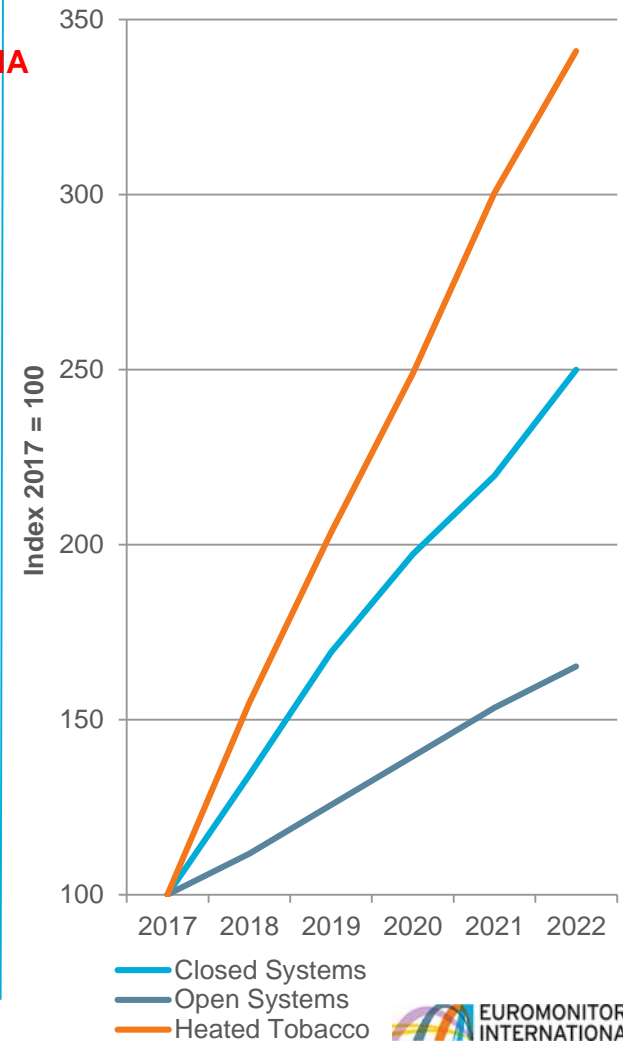
89.4% = cigarettes as
share of total value
sales

Tobacco and vapour market outlook 2017-2022

Cigarette value growth looks increasingly under pressure



Vapour Products Value 2017-2022

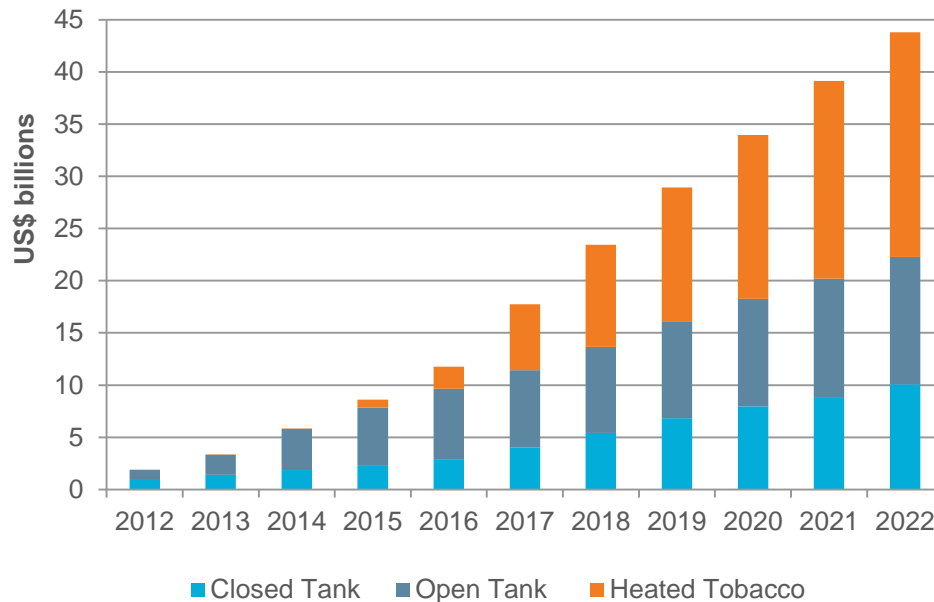


Note: *Excluding China

Vapour products market sizing and user population

Continues to grow but remains almost negligible in total tobacco context

Vapour Products Global Market Size 2012-2022



2011

11



2017

39



2022

64



million vapers



@ 10 sticks per day

=

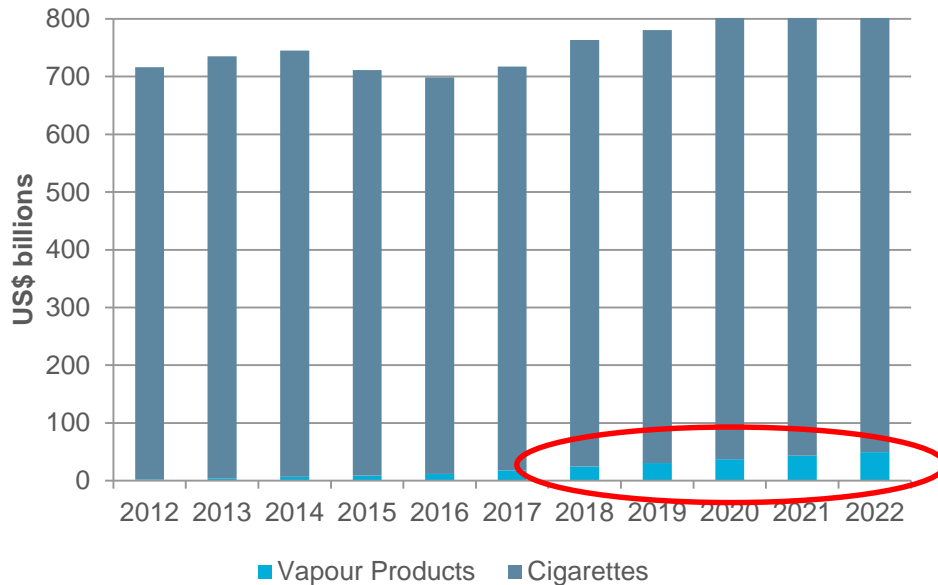
235 billion sticks

impact

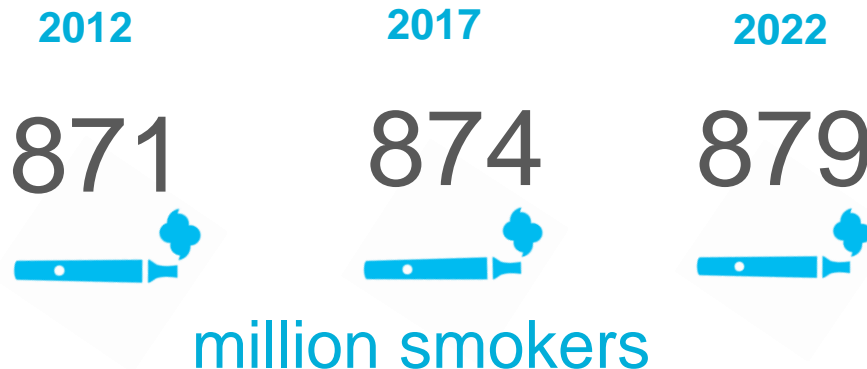
Vapour products market sizing and user population

Continues to grow but remains almost negligible in total tobacco context

Vapour Products V Cigarettes Global Market Size 2012-2022



Selected Tobacco Categories Global Market Size 2017 (US\$ billion)

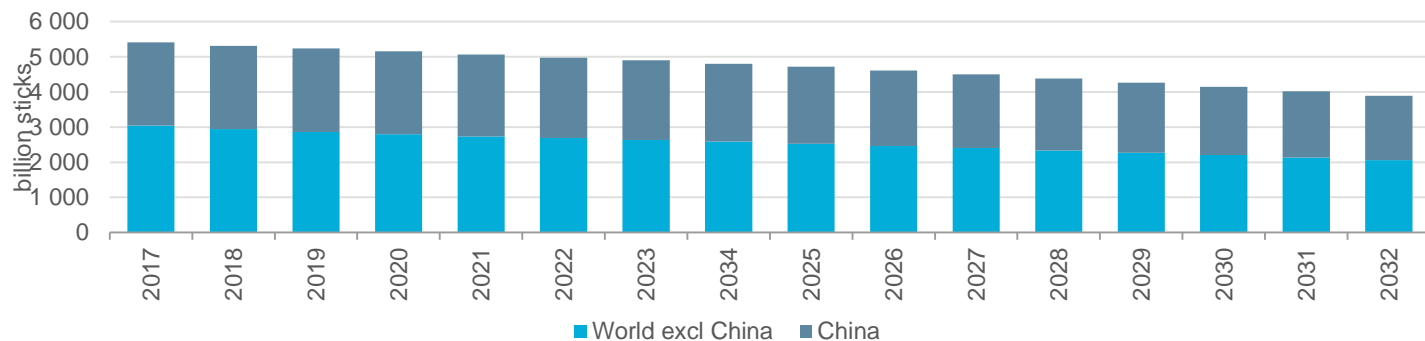


Cigarette retail volume projections 2017–2032

Global decline expected in range of 25% to 40% in next 15 years

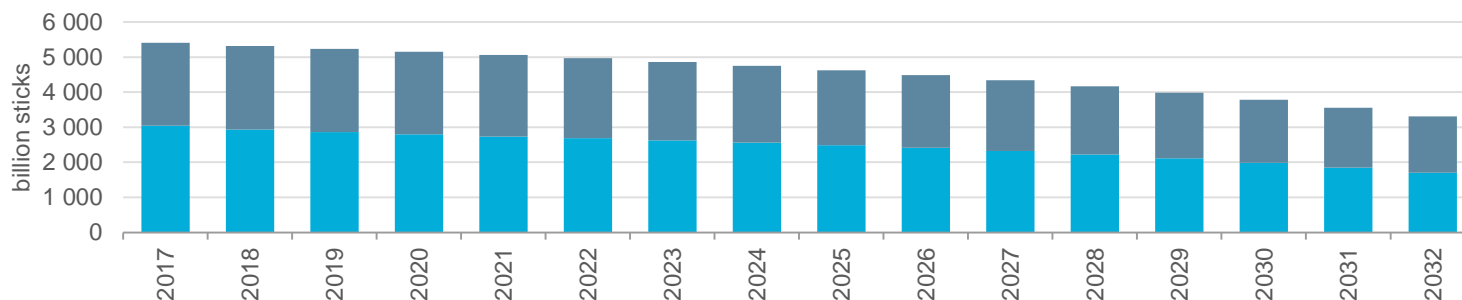
Absolute World Volume Growth 2002-2017: -2.5%

Positive Realist Scenario: Fading status quo; Incrementally stricter excise and regulation; Relatively slow migration to RRP



Absolute:
-33
-22
-28

Pessimistic Realist Scenario: Significant adoption of RRP in dev markets; Substantially enhanced reg and excise in CN



Absolute:
-44
-31
-39

Note: Absolute -39%

Top 20 cigarettes markets by volume 2017-2032

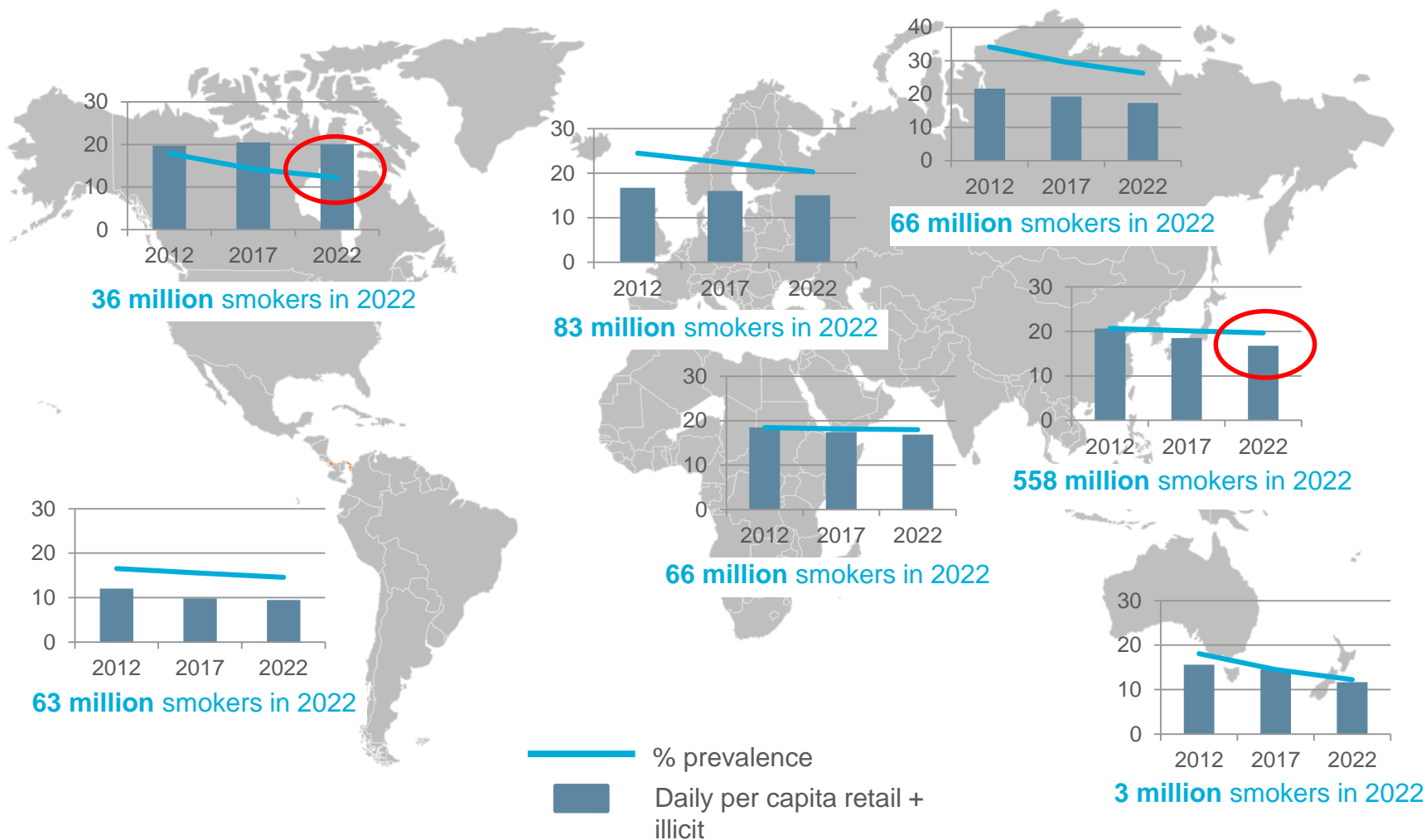
Global leadership will disperse

	2017	2032	
1	China	China	↔
2	Indonesia	Indonesia	↔
3	Russia	USA	↑
4	USA	Egypt	↑
5	Japan	Bangladesh	↑
6	Turkey	Russia	↓
7	Egypt	Turkey	↓
8	Bangladesh	Vietnam	↑
9	India	Iran	↑
10	Germany	Philippines	↑
11	Vietnam	India	↓
12	Italy	Pakistan	↑
13	South Korea	Germany	↓
14	Ukraine	Ukraine	↔
15	Philippines	Algeria	↑
16	Iran	Japan	↓
17	Pakistan	Spain	↑
18	Brazil	Brazil	↔
19	Spain	Saudi Arabia	↑
20	France	Mexico	↑

- 2017 top 20 = 10 Asia-Pac, 7 Europe, 2 Americas, 1 MEA
- 2032 top 20 = 9 Asia-Pac, 5 Europe, 3 MEA, 3 Americas
- Growth in absolute terms will come exclusively from countries in the AP and MEA regions. Advancement in rankings elsewhere is only due to moderated rates of decline
- Iran will rise furthest (from 16th to 9th) while Japan will suffer steepest drop (5th to 16th)

Trends in smoking prevalence by region

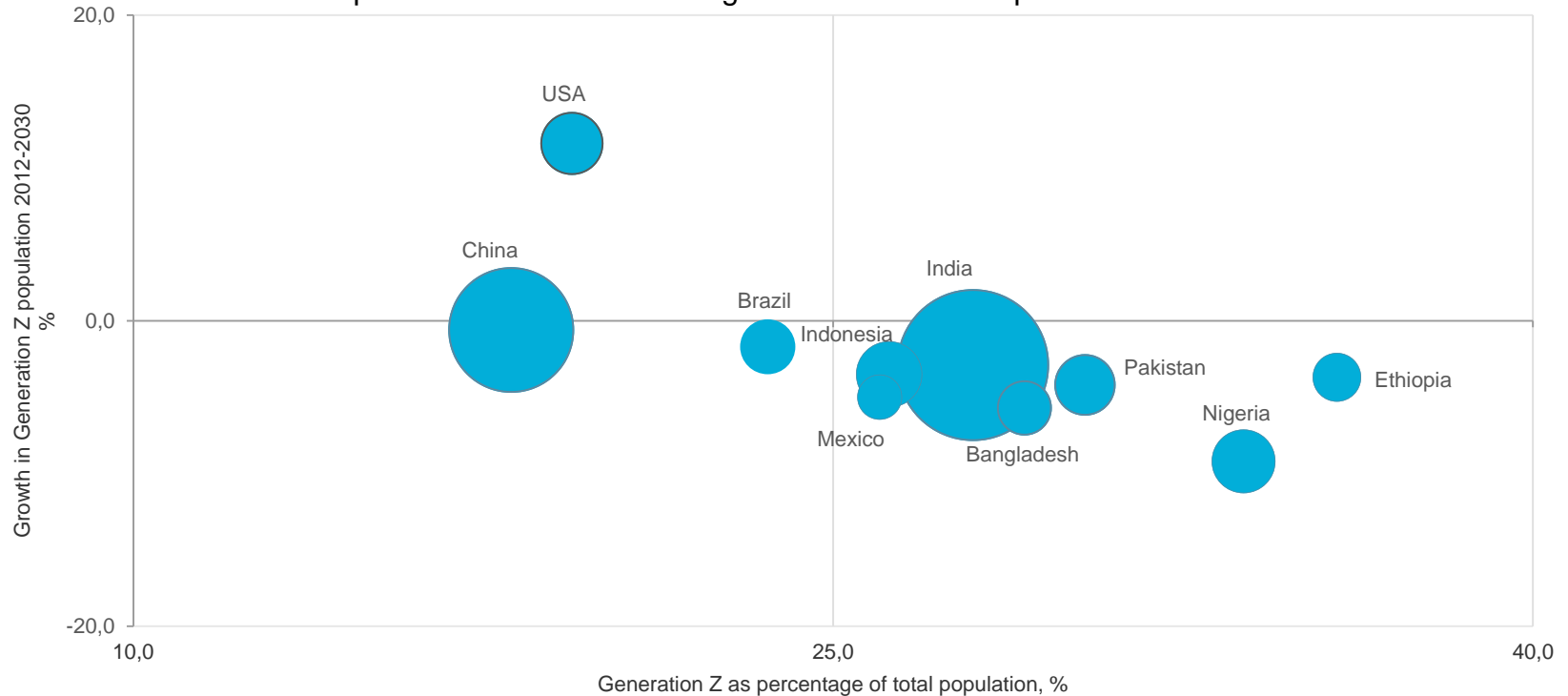
Smoking incidence is under pressure across the universe



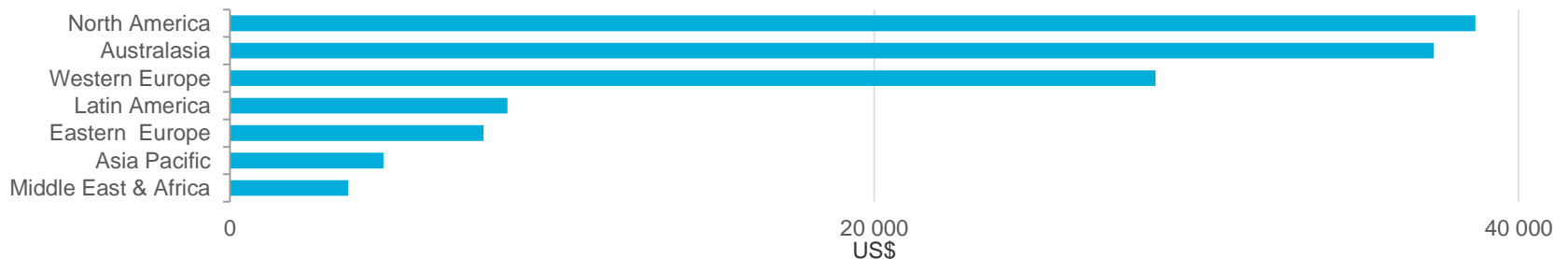
Generation Z: future market driver

World's largest demographic begins to enter the adult consumer equation

Top 10 Countries with the Largest Generation Z Population 2017



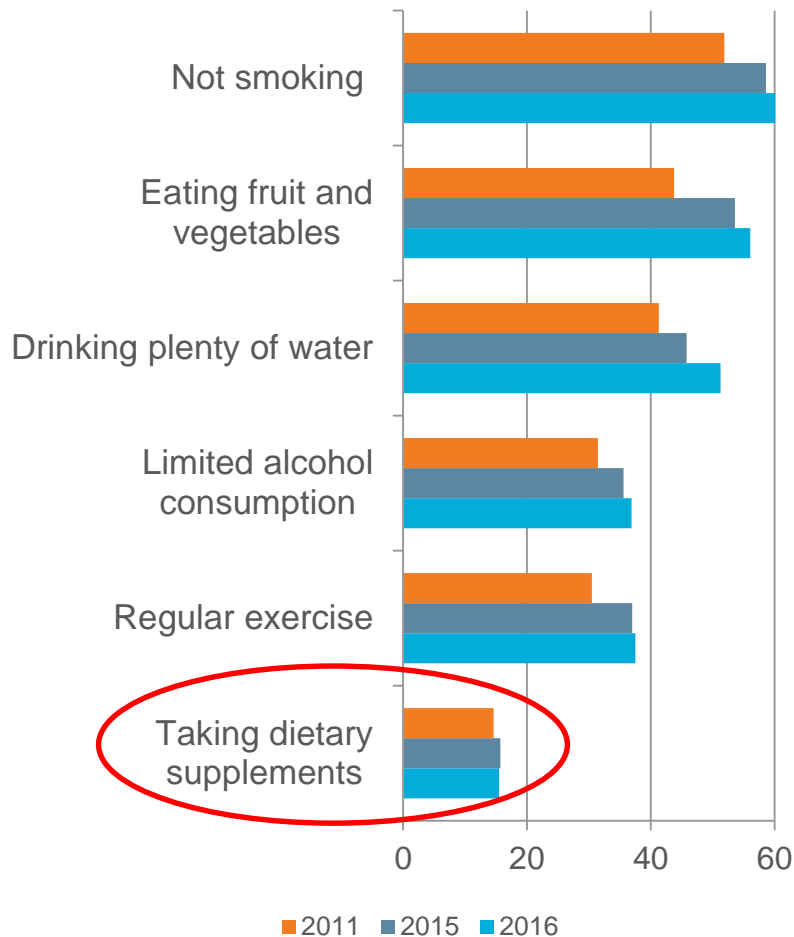
Average Gross Income of Population Aged 20-24 by Region 2017



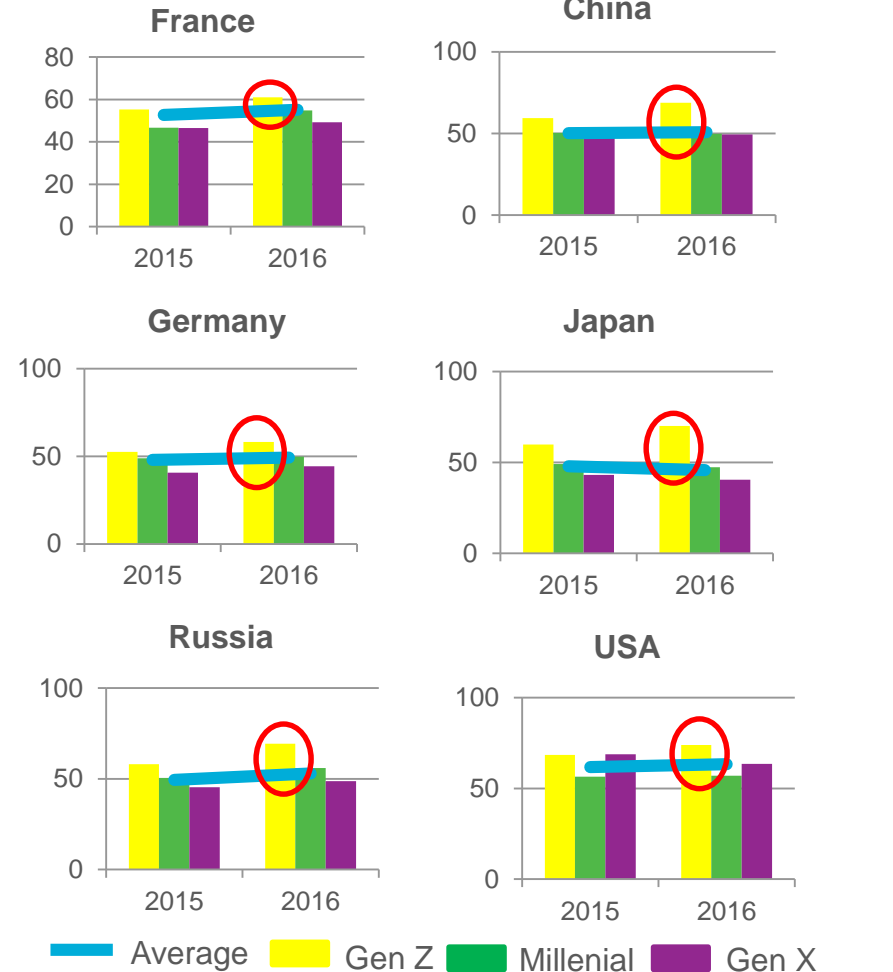
Changing attitudes driven by Generation Z

Generational differentials clear on tobacco

Factors Described as Extremely Important For Health Globally



“Not Smoking is Extremely Important to Health” % by Generation 2015 and 2016



Standardised packaging = standardised product

In the medium to long term plain packaging is the thinner end of a wedge

Standardisation requirements for tobacco products and packages

Subpart 1—Colour and smell of tobacco

29 Colour of tobacco

30 Smell of tobacco

Subpart 2—Text and other markings that may appear on tobacco packages

31 Text or alphanumeric marking on tobacco packages

32 Brand name and variant name

33 Company name

34 Bar code

35 Details of manufacturer or importer

Subpart 3—Wrapper and outer surface of tobacco packages

36 Tobacco package wrapper

37 Tear strip of tobacco package wrapper

38 Outer surfaces of tobacco package

Subpart 4—Prohibited features

39 Tobacco package must not have scent or noise making feature to promote tobacco product

40 Tobacco package must not have feature designed to alter package after sale

41 Tobacco package must not contain inserts

Subpart 5—Individual cigarettes

42 Dimensions and features of cigarette

Detaching nicotine from the sins of its delivery platforms

Accurate perception of nicotine is central to industry evolution



The JUUL phenomenon

Disrupting the emerging harm reduction consensus

Inside Juul: The Most Promising, and Controversial, Vape Company in America

How the San Francisco nicotine delivery startup, now valued at \$15 billion, set out to make cigarettes obsolete and inherited the tobacco industry's baggage along the way.



A wall of pod mods (from left to right): Bo by Jwells, myblu by Imperial Brands, Phix by MLV, Myle by ?, Vuse Alto by BAT, Mate 1 by Vapecinno, MarkTen Elite by Altria, iQ Air by Hangsen, Hexa by Hexa Vapor, Mylo by Mylo Vape, Rubi by Kandy Pens, Infinix and Fit by Smok, Kilo by Kilo E-liquids, Uboat by Kangertech

What shape will the endgame for combustible tobacco take?

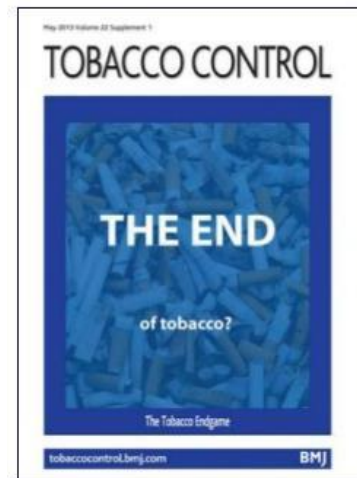
A mixed picture likely globally but a decisive model could emerge

Fading status quo



- Regulation or excise continues to increase, but not radically in most markets
- Smoking prevalence and denormalisation gradually declines as some consumers exit, others slowly migrate to reduced risk products occurs

Coercive



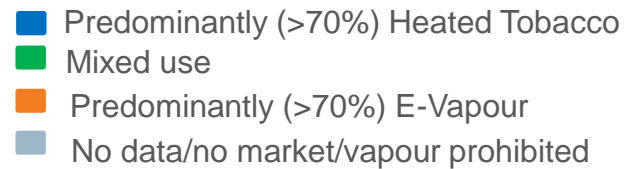
- Becoming a policy framework
- Potentially involves
 - Reducing nic content
 - Sinking lid production cap
 - Birth year bans
 - State ownership of tobacco companies
 - Price control/profit caps

Incentivised



- Along with consumer preference, maintenance of shareholder value has the potential to slow migration to reduced risk products
- Governments could intervene positively (through excise and regulation) to incentivise and accelerate this shift

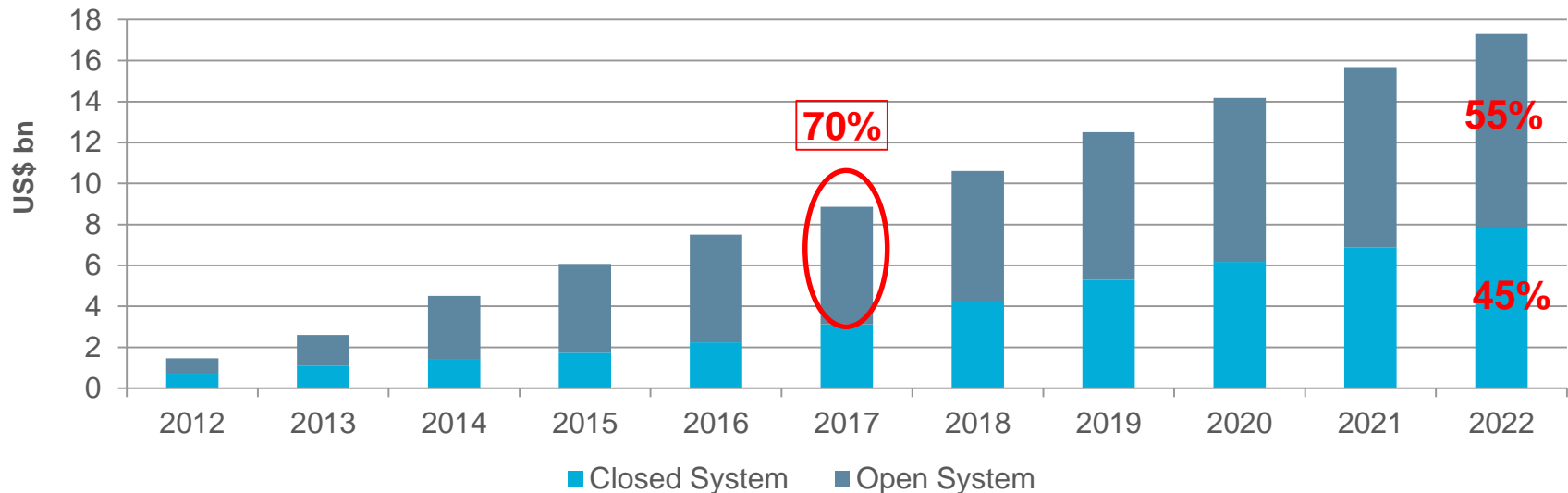
E-liquid will dominate in the majority of markets



Liquid consumption set to shift back to closed systems

E-liquid will dominate in the majority of markets

Retail Value Sales of Closed and Open Vapour Systems 2012- 2022



© Euromonitor International

- Key markets but projected to expand
- Regulatory concerns
- Ease of product use for mainstream consumer
- Involvement of tobacco and large independent organisations

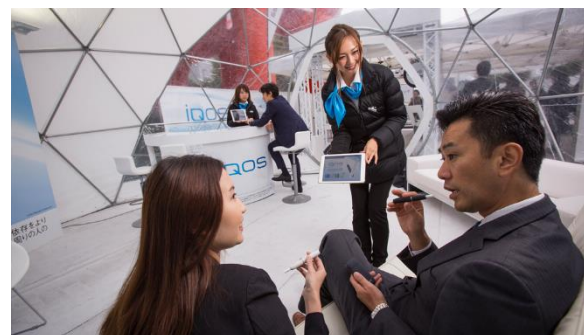


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What Japan can tell us about HT growth elsewhere

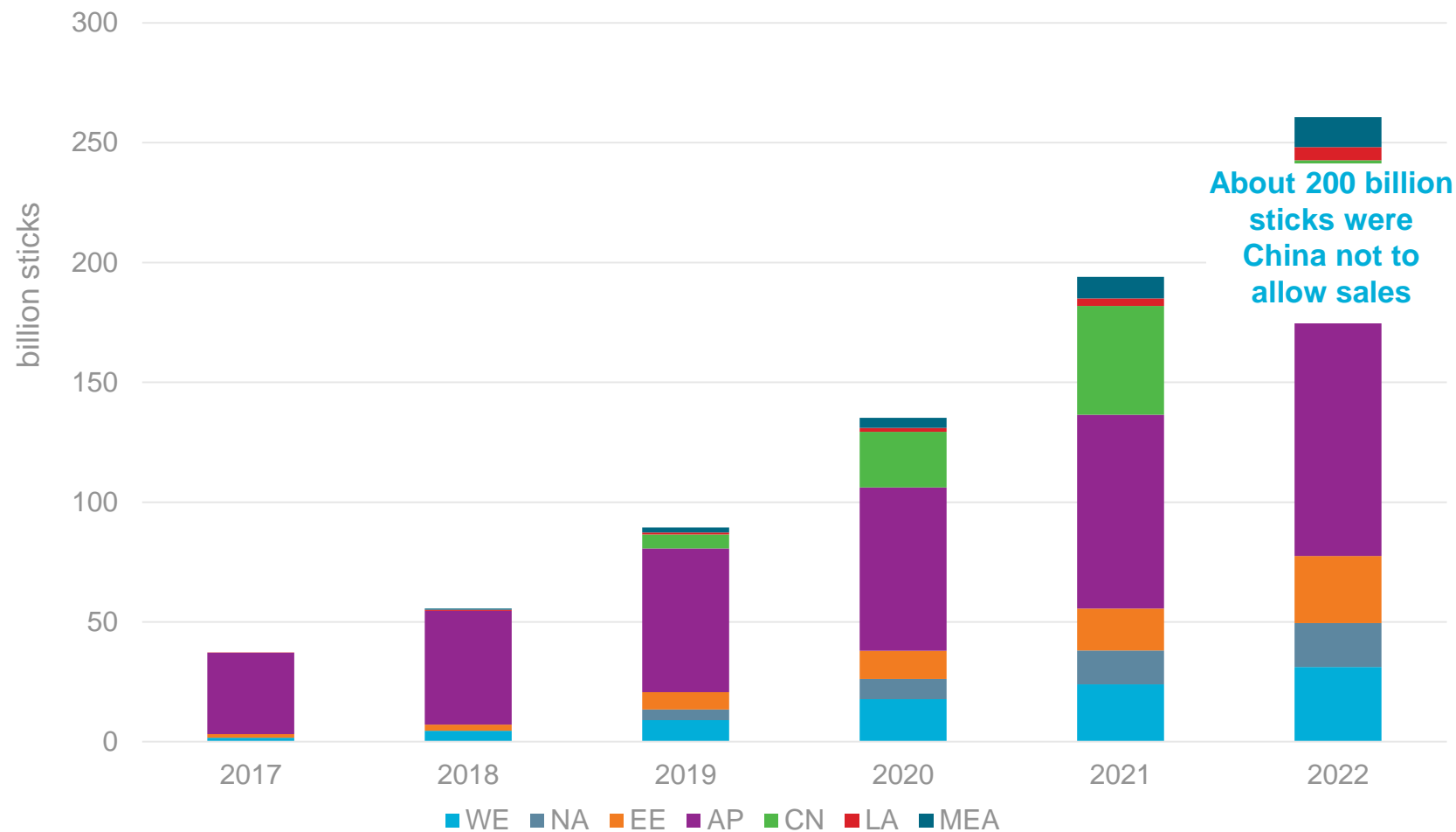
Transferrable drivers of rapid uptake

- Collective, per-oriented mindset
- Predisposed to novelty/innovation
- Relatively low competition from other alternative products
- High cultural affinity with tobacco use and strong identity relationships at the individual smoker level
- Ability to communicate with consumer relatively freely
- Favourable tax treatment
- High levels of disposable income



Estimated heated tobacco volume by region

Were sales in China to be licensed it would become the 2nd largest market



Significant next gen innovations emerging

If successful could appeal to different demographics enhancing migration

Heated Tobacco



Nicotine Liquid



Alternative Platforms



3d Flavour™ Innovating the flavour experience

flavour is a key
consumer driver

Vapers are looking for true flavour

THE MARKET TODAY:

- > Only 10% of flavour is delivered to the mouth
- > Flavour quality diminished through heating
- > Flavour experienced as scent, not taste

53 | Half Year Results | 9 May 2018

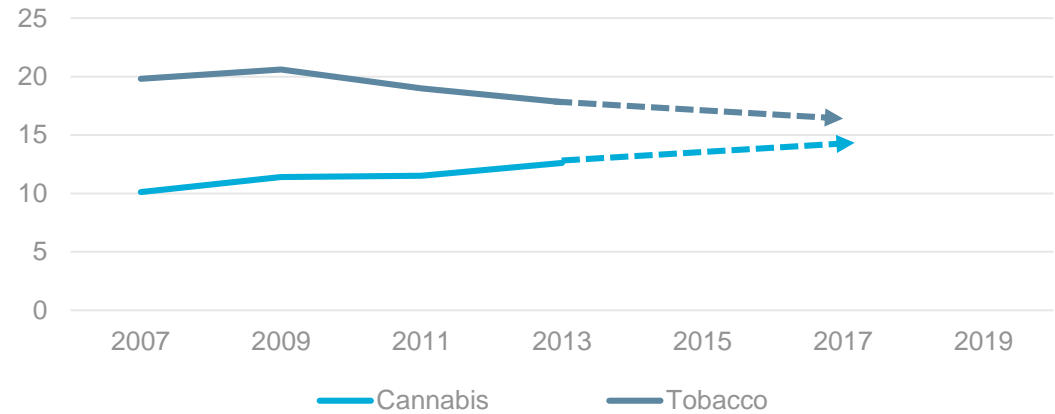


Cannabis presents an opportunity throughout the value chain

But shifts in delivery format and distribution mirror those in tobacco/nicotine

c. 200m
global
cannabis
consumers

US Cannabis Use & Smoking Prevalence 2007-2019*

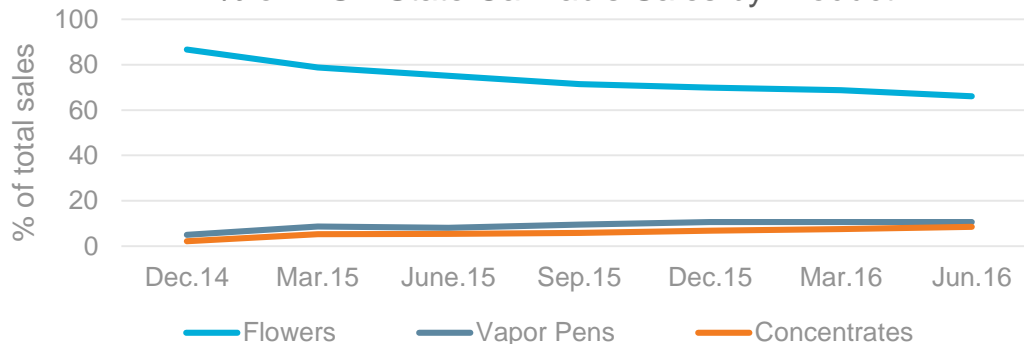


QUARTZ

SMÖKÄSBORD

Nobody smokes their weed any more

% of WSH State Cannabis Sales by Product**



© Euromonitor International

*Sources: SAMHSA & Euromonitor

**Source: Headset

Key delivery formats for cannabis

INHALATION

Flower



Vape Pen



Pre-Roll



Concentrate



ORAL CONSUMPTION

Beverage



Tincture



Edibles



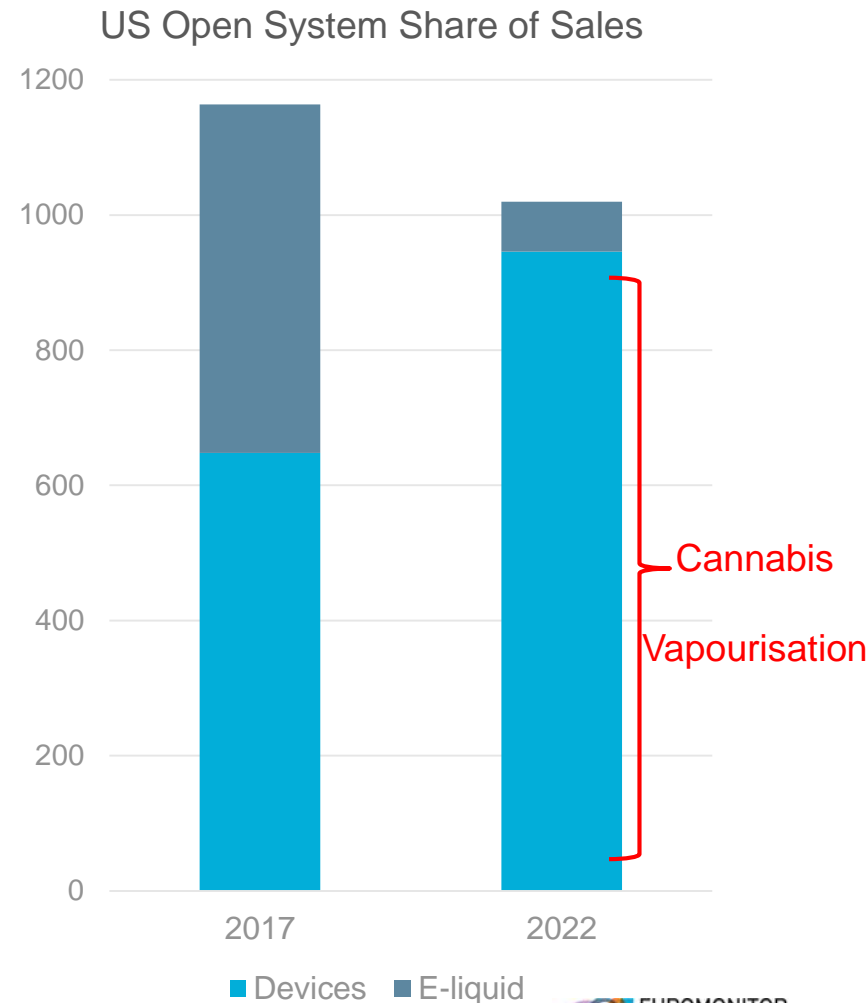
Capsule



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The growth – especially in vapourisation – is on now ...

CBD is already a viable alternative to nicotine



So, platform and substance agnosticism is the future

The industry is only just beginning to metabolise these elements



Reflected in an increasingly diverse range of competitive activity
From an industry castigated for internal pollution to one addressing external fug

AYR

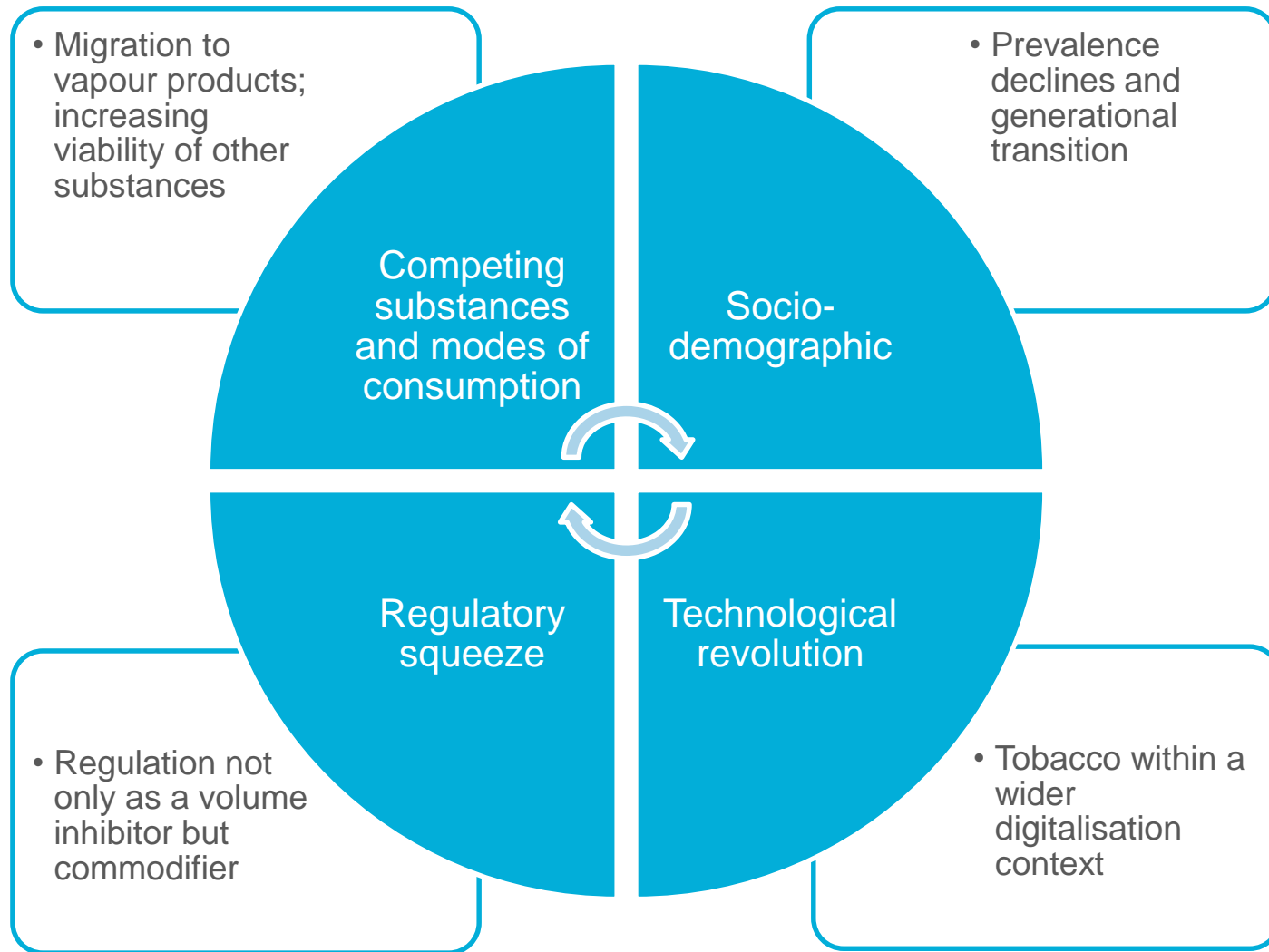
h Canadian pot

‘We’re not just thinking of challenging and possibly disrupting the traditional tobacco industry,’ says Memari, ‘but about our mission of wellness using connected devices in relation to breathing.’ Smiling, he referred to the potential as AYR 2.0, when the company will deliver ‘nicotine, medicines and even better air to customers and patients alike’. ✱ vapeayr.com

British tobacco company Imperial Brands has appointed the chairman of a Canadian medicinal cannabis group to its board.

Key drivers of a changing industry

Explanatory factors (and open issues) in shift to post-combustible era



Thank you ... questions

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