



PHILIP MORRIS  
INTERNATIONAL

# 2018 INVESTOR DAY

Designing a Smoke-Free Future

## Investor Day

Lausanne, September 27, 2018

André Calantzopoulos  
*Chief Executive Officer*

# PMI: Strong Business with a Strong Future

- Enormous opportunity from RRP is undiminished
- **Our goal:** convincing people who smoke to switch to better alternatives and governments to help
- **Our future:** highly promising with, at this early stage, less predictability
- **Our strong cigarette business** provides the foundation to accomplish our ambitious goals



**Confidence in our  
growth outlook**



# PMI's Strategic Priorities



- **Convincing men and women who would otherwise continue to smoke to switch to RRP:**
  - Superior science and technology
  - Superior end-to-end consumer experience
  - Understanding, relevance, credibility
- **Demonstrate to regulators, the scientific community and NGOs** that RRP are fundamental to improving public health
- **Significantly improve our internal capabilities:**
  - Technical skills
  - Organizational agility
  - Entrepreneurship, continuous learning
  - Digitalization
  - Operating efficiency
- **Focused approach to our combustible business initiatives to maintain our strong leadership**



# PMI's Strong Combustible Business Enables the Strategy



- From an RRP perspective, our combustible business gives us infrastructure, consumer pathways and scale
- Maintaining our combustible category leadership is essential, but we operate with more focus and efficiency
- Expect robust performance going forward, although category will inevitably decline as RRP's grow

Combustible Price  
Variance as a % of  
Combustible PY Net Revenues

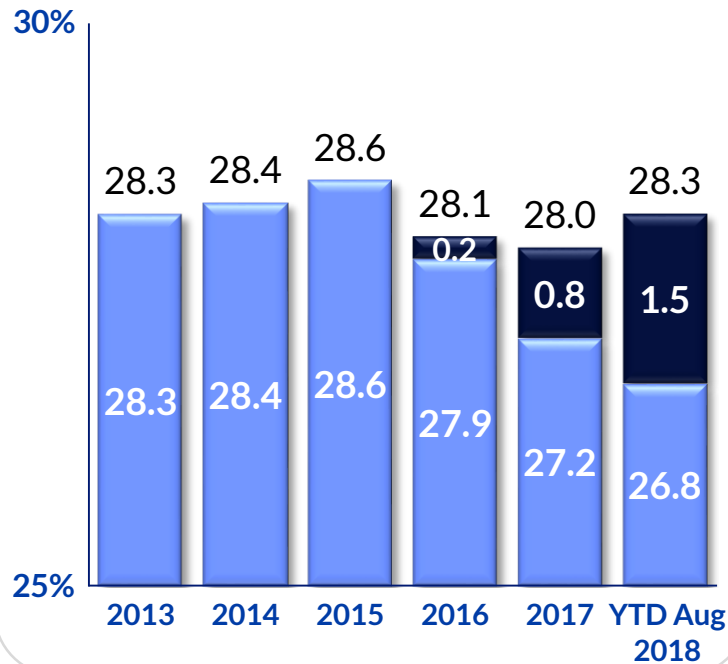
~6.5% (a)

Average Growth  
(2008-2018 Forecast)

# PMI: Robust International Market Share

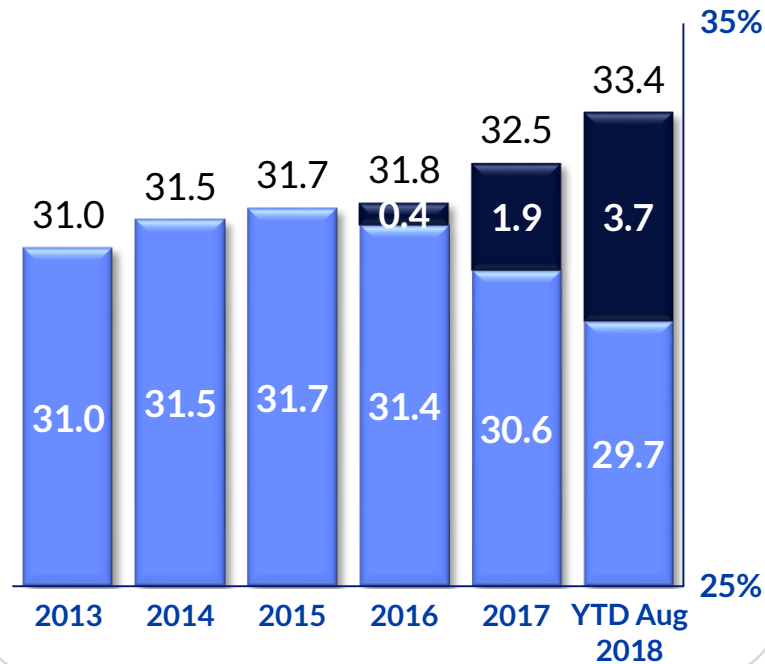


## Total International SoM



## SoM where IQOS is Present

HTUs  
Cigarettes



Note: Status at the end of August 2018. Excludes China and the U.S.  
Source: PMI Financials or estimates

# Strong Combustible Business with a Focused Approach



- Superior brand portfolio
- Targeted investments in combustibles are working, and freeing up resources
- We have more than halved the number of new product launches since 2015 whilst achieving a significantly higher success rate
- We have streamlined our brand portfolio with morphings and SKU rationalization

# Ahead of Plan with Smoke-Free Future

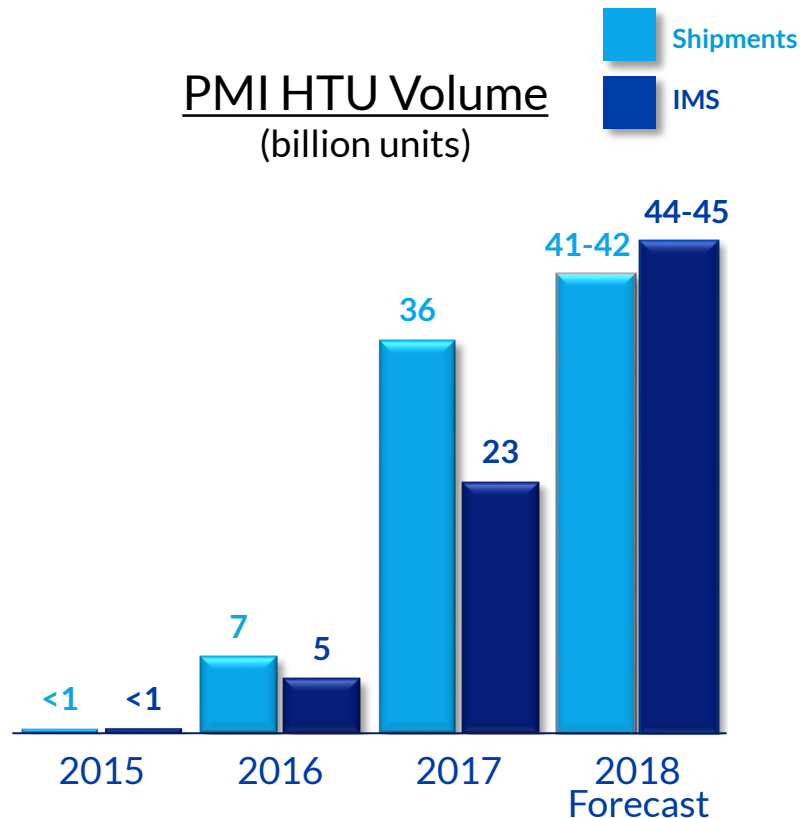


- PMI 2014 Investor Day:
  - Targeted 30 to 50 billion HTUs by 2020<sup>(a)</sup> assuming 3-5% SOM in scope

**Achieved 2020 HTU volume and SOM target two years ahead**

**Expect continued strong growth in 2019 and beyond**

**PMI HTU Volume**  
(billion units)



(a) "initial five years ... for launches," confirmed as 2020 at CAGNY, February 2016  
Source: PMI Financials or estimates

# RRPs: Our Future and Most Promising Growth Opportunity

- **5.8 million** adult smokers have quit smoking and switched to *IQOS*<sup>(a)</sup>, with a further **2.8 million** in conversion<sup>(b)</sup>:
  - Only 4.5% of the 189 million directly addressable in current *IQOS* markets<sup>(c)</sup>
  - 1+ billion worldwide

(a) Exclusive use of HnB with over 70% consumption of *HEETS/Heatsticks*

(b) Status at the end of August 2018

(c) Includes 40 markets. Excluding duty free, Monaco and Réunion

Source: PMI Financials or estimates





# RRPs: Our Future and Most Promising Growth Opportunity (cont.)



- Sizing the opportunity with a **realistic target** for 2021 of 90 to 100 billion HTUs:
  - Each two million new consumers that quit smoking and switch to *IQOS* equate to an annualized 10 billion HTUs:
    - Approximately **\$0.9 billion in revenues and \$0.6 billion in marginal contribution<sup>(a)</sup>**, including devices and impact of cannibalization
  - **10 billion HTUs<sup>(b)</sup> represent approximately 2.9 points of total PMI revenues and 3.4 points of marginal contribution** as compared to 10 billion combustibles (in RRP markets) which would add 1.4 points to net revenues and 1.6 points to marginal contribution
- Our current fixed infrastructure<sup>(c)</sup> can manage this volume
- Variable commercial costs will grow, but at a lower pace than revenues/volumes in the forthcoming years

(a) PMI estimates assuming current pricing and excise tax incidence, existing market footprint

(b) HTUs only, not including impact of devices and cannibalization

(c) Includes fixed manufacturing expense, R&D, direct retail and other

Source: PMI Financials or estimates

# RRPs: Public Health at a Pivotal Moment



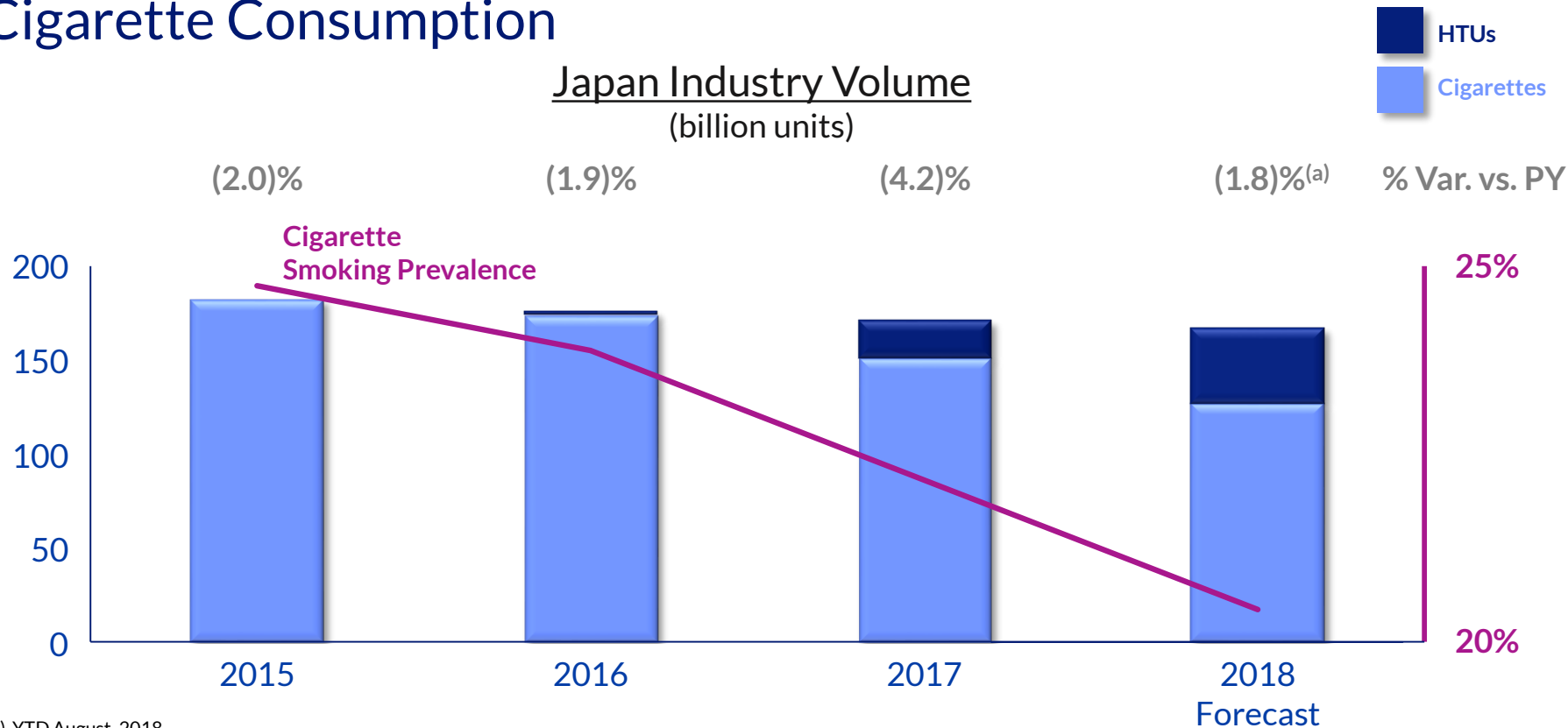
- RRP are an inseparable part of the solution to world's tobacco-related public health goals
- Allowing adult consumers to make informed choices is a critical need
- Consumer knowledge and regulatory frameworks are now being shaped
- The actions of governments, NGOs and the industry in this critical period will reverberate long into the future:
  - Regulatory measures and taxation influence consumer behavior
  - They must differentiate tobacco products according to their risk profiles
  - The discussion should not be whether scientifically substantiated RRP should be made available but how best and how fast
  - Complexity, conservatism or ideology should not be reasons for inaction
  - Regulation and related discussion should be centered on the interests of the people who smoke and avoid misleading statements or research

# RRPs: Public Health at a Pivotal Moment (cont.)



- Skeptics emit hypothetical scenarios that changes in initiation or quitting rates outweigh the benefits to the individual smoker
- Post-market surveillance and regulatory interventions can minimize these unintended outcomes, if any
- We will continue to demonstrate through scientific substantiation our seriousness and transparency
- The in-market results so far on RRP already show a step-change in cigarette smoking prevalence
- Japan post-market data to date shows no change in the areas of concern

# RRPs: The Single Most Impactful Tool in Reducing Cigarette Consumption



(a) YTD August, 2018

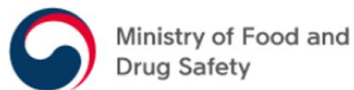
Note: Industry volume reflects cigarettes and heated tobacco units

Source: PMI Financials or estimates, Tobacco Institute of Japan and PMI Market Research

# How is this going to convince people who smoke to change their behavior?



# Korea: Deceptive Statements Mislead Consumers



*"Average tar containment (of IQOS HEETS) is 4.8mg, 9.1mg, 9.3mg. Most sold conventional cigarettes' tar numbers range from 0.1mg ~ 8.0mg".*

–Korean Ministry of Food and Drug Safety



*"Nicotine-Free Dry Particulate Matter (NFDPM), commonly known as 'Tar' is what is left when water and nicotine are subtracted from cigarette smoke. Because IQOS heats tobacco, there is no combustion of tobacco. Instead, the tobacco is heated to generate a vapor with on average 90% lower levels of harmful chemicals. Any comparison of cigarette 'Tar' and the weight of aerosol/vapor produced by HNB products is therefore a deception and misleading".*

–Philip Morris International

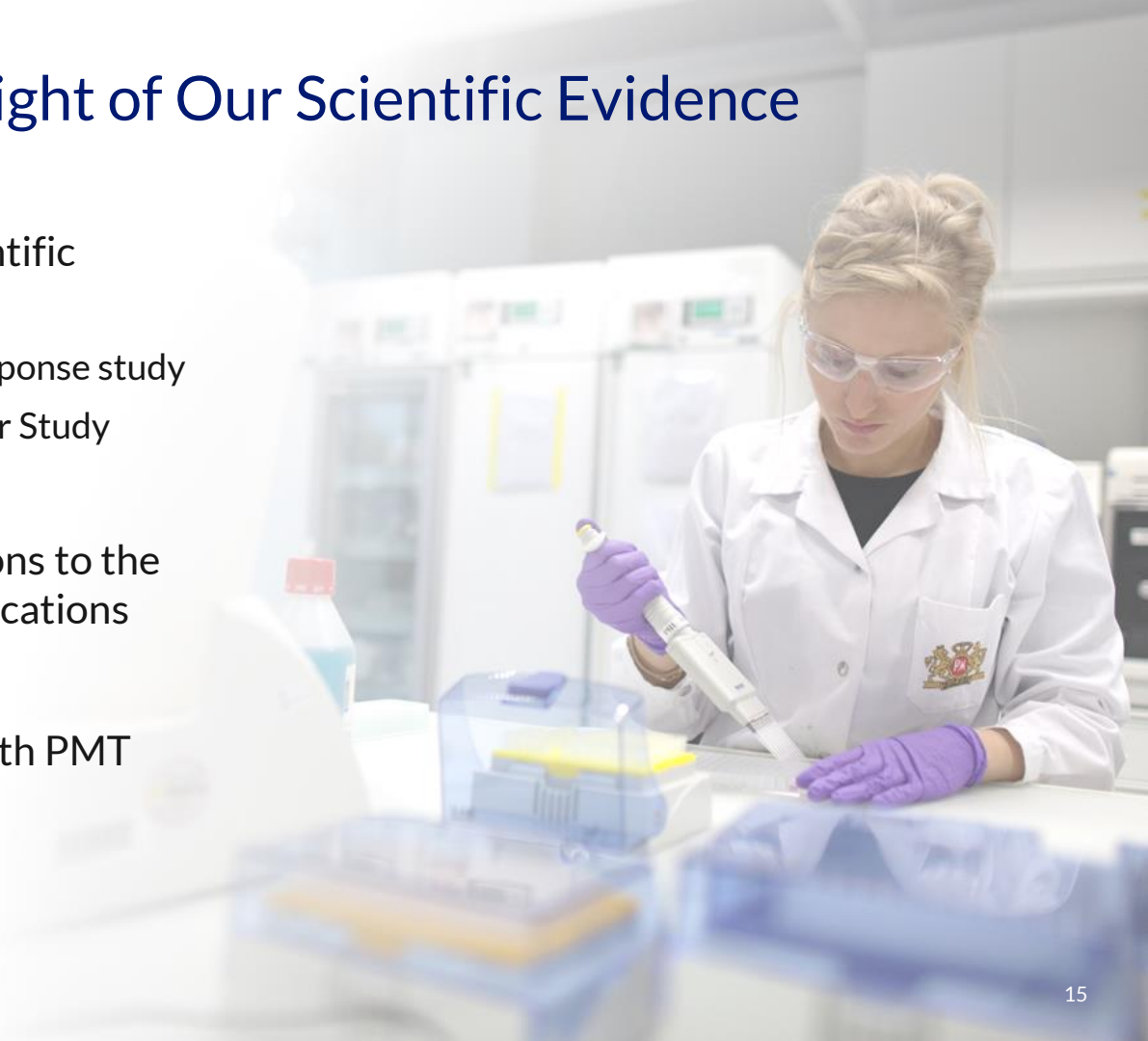


*"Although the NFDPM value for HNB products can be formally calculated as for the conventional cigarettes, direct comparisons would be misleading".*

–German Federal Institute for Risk Assessment

# RRPs: The Growing Weight of Our Scientific Evidence

- Robust *IQOS* pre-market scientific package complemented by:
  - 6-month clinical exposure response study
  - 18-month Mouse Lung Cancer Study
- These complete our submissions to the U.S. FDA for *IQOS* MRTP applications
- Awaiting FDA decisions on both PMT and MRTP applications



# Evidence-based Conclusions on RRP's are Encouraging



- A number of key regulatory bodies and scientists have taken a more dispassionate and evidence-based view of RRP's:

***"There is conclusive evidence that completely substituting e-cigarettes for combustible tobacco cigarettes reduces users' exposure to numerous toxicants and carcinogens present in combustible tobacco cigarettes".***

– National Academies of Science, Engineering and Medicine (US). The Public Health Consequences of E-cigarettes. Washington DC. January 2018. Conclusion 18-1

***"The available evidence suggests that heated tobacco products may be considerably less harmful than tobacco cigarettes and more harmful than e-cigarettes".***

– McNeill A, Brose LS, Calder R, Bauld L & Robson D (2018). Evidence review of e-cigarettes and heated tobacco products 2018. A report commissioned by Public Health England. London: Public Health England

***"The use of heatsticks with IQOS is harmful to health, but probably less harmful than smoking tobacco cigarettes".***

– Dutch National Institute for Public Health and the Environment, August 2018

***"We need to envision a world where cigarettes lose their addictive potential through reduced nicotine levels. And a world where less harmful alternative forms, efficiently delivering satisfying levels of nicotine, are available for those adults who need or want them".***

– FDA Commissioner Gottlieb, S., Protecting American Families: Comprehensive Approach to Nicotine and Tobacco, July 28, 2017

- Confident that the growing weight of our scientific evidence will validate our strategy:
  - Also supporting risk-based fiscal & regulatory frameworks



# IQOS Portfolio Brand Architecture



THE SCIENCE

*"IQOS HeatControl Technology"*

BRAND

IQOS

PLATFORMS

1



2



3



4



CONSUMABLES

HEETS™

TEEPS™

STREM™

VEEV™

# RRPs: Key Innovation Corridors

- Heating / vaporization technologies across all platforms
- Product design, consumer interface, extended ecosystem, consumer care
- Convergence of platforms to allow use with different IQOS consumables
- Life sciences
- Digital assets to increasingly replace legacy operations
- Data science at the center

**World class technical expertise, strong partnerships, promising technology / start-up acquisitions. New working methods for speed and efficiency**

**Intellectual Property is the base, superior user experience know-how is a key competitive advantage**

# RRPs: Our Strategic Focus



- We lead the way in RRP with determination but our strategy is designed to be flexible and pragmatic, as befits the less predictive nature of a new category
- While other platforms have a significant role to play, the evidence continues to support the highest potential for *IQOS* heated tobacco:
  - Taste and satisfaction
  - Scientific substantiation
  - High conversion rates demonstrate unique ability to switch people who smoke
  - Growing brand equity and continuously improving user experience
  - Superior unit margins over combustibles
  - Low appeal to youth and non-smokers

# RRPs: Our Strategic Focus (cont.)



- Upfront investments, both centrally and at market level, pay back quickly and substantially
- Fixed infrastructure can carry vastly higher numbers of *IQOS* users and HTU volumes than today, and will service all RRP platforms
- A converted *IQOS* HTU consumer is significantly more valuable vs. a combustible smoker in comparable price segments
  - Amplified by HTU share gains
- High retention means profit uplift is sustainable
- The organizational transformation will increase our capabilities in everything we do. We are learning and improving ahead of all others
- Significant efficiency and cost improvement initiatives over the next 3 years

# RRPs: We Hold a Strong Interest in the E-Vapor Category

- Currently a rather undifferentiated category for both products and brands
- PMI focused on genuine differentiation of consumer experience across all key parameters
- Ability to scale at speed via our *IQOS* sales infrastructure and consumer pathways



***IQOS MESH***

# Improving Our Internal Capabilities

- As our execution improves, so do our results
- We are learning more every day
- Transforming our organization to be fit for purpose is fundamental
- We are building a more agile, responsive, pro-active and **consumer-centric** organization that will **serve all of our business** in the new landscape:
  - Significant infusion of **subject matter expertise** at all levels
  - Organizational structure aligned with the **consumer journey**
  - **Project-based, lean** techniques, **fast** experimentation
  - Digital and data **analytics**
  - **Zero-based budgeting** to optimize resource allocation
- **Strong motivation behind our RRP strategy with the right focus on maintaining our combustible business competitiveness**

# Sustainability at PMI



- Improved performance or above average performance in key ESG ratings in 2018:

- Dow Jones Sustainability Index
- Sustainalytics

Ambition to achieve sector sustainability leadership by 2020

- Environment:

- CDP Climate A-List
- CDP Water A-List
- CDP Supplier Engagement Leadership



- Social:

- Comprehensive program to eliminate child labor in tobacco growing
- Crop diversification
- Equipping our people to successfully transform our business
- >34% women in management, EQUAL-SALARY certified

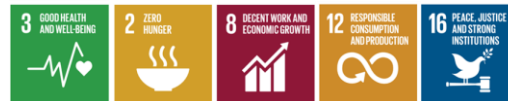
- Sustainability Report 2017:  
(Publication in May 2018)

- Sustainability Strategy towards smoke-free future
- Business Transformation Metrics

- Governance:

- Strengthened Sustainable Governance (BoD, Functions, Markets)
- Formalized our Environmental Commitment
- Continuous improvement in supply chain risk management:
  - Responsible Sourcing Principles roll-out
  - Assessment of main Electronic Manufacturing Services suppliers
  - Update Agricultural Labor Practice (ALP) program

We remain committed to the SDGs and particularly focus our efforts on the following:



# Mid-Term Performance Expectations



- Total industry volume expected to decline at 2% to 3% CAGR
- Our cigarette business is in robust shape with an unrivalled competitive position and a broadly rational excise tax environment
- RRP strong growth will continue but the pace is subject to greater fluctuation:
  - Diffusion curves vary based on culture, consumer readiness, word-of-mouth, experimentation with competitive offerings
  - Timing of positive regulatory interventions
  - Our growing organizational capabilities to scale up at lower marginal cost and much higher speed
  - Device sales have a significant impact on revenue growth (minimal on EPS) and are the most difficult to predict
- Our new mid-term growth targets reflect this volatility, setting realistic thresholds of performance with upside potential. We expect significant improvement in our underlying business as of 2019



# 2019-2021: PMI Compound Annual Growth Targets



Net  
Revenues

$\geq 5\%$

CAGR  
ex-Currency

Adjusted  
Diluted EPS

$\geq 8\%$

CAGR  
ex-Currency

# Our Confident Outlook



- We are still in the early stages of the RRP category's development and of our transformation
- As the category expands, there will be periods of acceleration and periods of slower growth:
  - RRP growth potential is enormous, and will be for many years
  - We are transforming to remain at the forefront of science, innovation and user experience with efficiency and speed
- We will retain strong leadership in our cigarette business, although the category will decline over time as consumers switch to RRP
- Our investments are commensurate to the potential of smoke-free products but also flexible and pragmatic
- All of the above is driven by our unfailing commitment to generously rewarding shareholders
- Positive regulatory developments would be a significant additional accelerator



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