



A study of the illicit cigarette market
in the European Union

2013 Results



Important Notice

- This presentation of Project SUN key findings (the 'Report') has been prepared for British American Tobacco plc, Imperial Tobacco Limited, JT International SA and Philip Morris International Management SA, described together in this Important Notice and in this Report as the Beneficiaries, on the basis set out in a private contract dated 20 December 2013 agreed separately with the Beneficiaries (the 'Contract').
- Nothing in this Report constitutes legal advice. Information sources, the scope of our work, and scope and source limitations, are set out in the Appendices to this Report. The scope of our review of the contraband and counterfeit segments of the tobacco market within the 28 EU Member States was fixed by agreement with the Beneficiaries and is set out in the Appendices.
- We have satisfied ourselves, so far as possible, that the information presented in this Report is consistent with our information sources but we have not sought to establish the reliability of the information sources by reference to other evidence.
- This Report has not been designed to benefit anyone except the Beneficiaries. In preparing this Report we have not taken into account the interests, needs or circumstances of anyone apart from the Beneficiaries, even though we have been aware that others might read this Report.
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- The work undertaken and the methodology followed are based on that undertaken in connection with the Project STAR reports which were commissioned by Philip Morris International Management SA between 2006 and 2012. The methodology has been refined to reflect the provision of additional data from British American Tobacco plc, Imperial Tobacco Limited and JT International SA (see Methodology and Appendices section).
- This Report makes reference to 'KPMG Analysis'; this indicates only that we have (where specified) undertaken certain analytical activities on the underlying data to arrive at the information presented.

CIGARETTE INDUSTRY TERMS	
Bootlegging	Also called small-scale smuggling, bootlegging is the purchase of tobacco products in one country for illegal consumption or resale in another country without paying the applicable taxes or duties
Cigarette	Any factory-made product that contains tobacco and is intended to be burned or heated under ordinary conditions of use
Cigarillos	A short, narrow cigar, which, like cigarettes, is often machine-made and sold in packs
Contraband (CB)	Genuine product that has been bought in a low-tax country and which exceeds legal border limits or acquired without taxes for export purposes to be illegally re-sold (for financial profit) in a higher priced market. There are generally two types of contraband: bootlegging and wholesale smuggling/organised crime
Counterfeit (CF)	Cigarettes that are illegally manufactured and sold by a party other than the original trademark owner. For the purposes of this analysis, data relating to Counterfeit is not included within the definition of Contraband. Illicit flows of BAT, ITL, JTI and PMI brands are split into their separate Counterfeit and Contraband components
Duty Free	Purchases made outside the EU that have no state, local or provincial taxes, federal import duties or any other type of taxation added to the cost of the item purchased. Subject to purchase volume restrictions
Green Leaf	Uncut dried tobacco leaf, which smokers cut themselves. Green leaf was not subject to excise tax in Poland until 2013
MPPC	Most popular price category
NMA /TMA	National Manufacturers Association /Tobacco Manufacturers Association
OTP	Other Tobacco Products (RYO/MYO, cigarillos, portions, rolls and cigars; excluding smokeless tobacco and water-pipe tobacco)
Smoking incidence	Daily average consumption by the adult population
Smoking prevalence	The percentage of smokers in the total adult population
Tobacco taxes	The sum of all types of taxes levied on tobacco products. There are two basic methods of tobacco taxation: Normal or specific taxes are based on a set amount of tax per unit (e.g. cigarette); these taxes are differentiated according to the type of tobacco. Ad valorem taxes are assessed as a percentage mark up on a determined value, usually the retail selling price or a wholesale price and includes any value added tax
DATA SOURCES	
EPS	Empty Pack Survey
IMS	In Market Sales (the primary source of legal domestic sales volumes)
CONSUMER RESEARCH	
CAPI	Computer-aided personal interviewing
CATI	Computer-aided telephone interviewing
MEASUREMENTS	
Bn	Billion
Mn	Million



TERMINOLOGY USED IN PROJECT SUN REPORT	
BAT	British American Tobacco plc
C&C	Counterfeit and Contraband
CAGR	Compound Annual Growth Rate
Consumption	Actual total consumption of cigarettes in a market, including legal IMS and illicit products as well as those purchased overseas to be brought back and smoked in market
Country of origin	Country from which the packs collected are deemed to have originated. This is determined by either the tax stamp on the pack or in cases where tax stamp is not shown, on the health warning and packaging characteristics
Domestic Whites	Domestic whites are packs of domestic market variant, but those that are priced below the minimum tax yield. These products are treated as having not been legally sold in the country in question, and have therefore been reclassified as non-domestic
EU	European Union
Illicit Whites	Cigarettes that are usually produced legally in one country/market, primarily for smuggling. While they may also be exported legally from some countries, they are smuggled across borders during their transit to their final destination market where they have limited or no legal distribution and are sold without payment of tax
Inflows/Outflows	Inflows of non-domestic product into a market / outflows of product from a market
ITL	Imperial Tobacco Limited
JTI	JT International SA
KPMG EU Flows Model	The primary methodology which we have used for measuring consumption in a market. The model has been developed by KPMG on a bespoke basis for the specific purpose of measuring inflows and outflows of cigarettes in the scope of this project
LDC	Legal Domestic Consumption is defined as legal domestic sales net of outflows
LDS	Sales of genuine domestic product through legitimate, domestic channels based on In Market Sales (IMS) data
ND	Non-Domestic product – product that originates from a different market than in which it is consumed
ND(L)	Non-Domestic (Legal) – product that is brought into the market legally by consumers, such as during a cross-border trip
PMI	Philip Morris International Management SA
Under Declaration	Tobacco products that are produced and distributed in the same country, a portion of which is not declared to the domestic tax authorities
Unspecified	Unspecified market variant refers to cigarette packs which do not bear specific market labelling or Duty Free labelling
WAP	The weighted average price for cigarettes calculated by reference to the total value of all cigarettes released for consumption, based on the retail selling price including all taxes, divided by the total quantity of cigarettes released for consumption. The WAP is provided by the EC Excise Duty Tables



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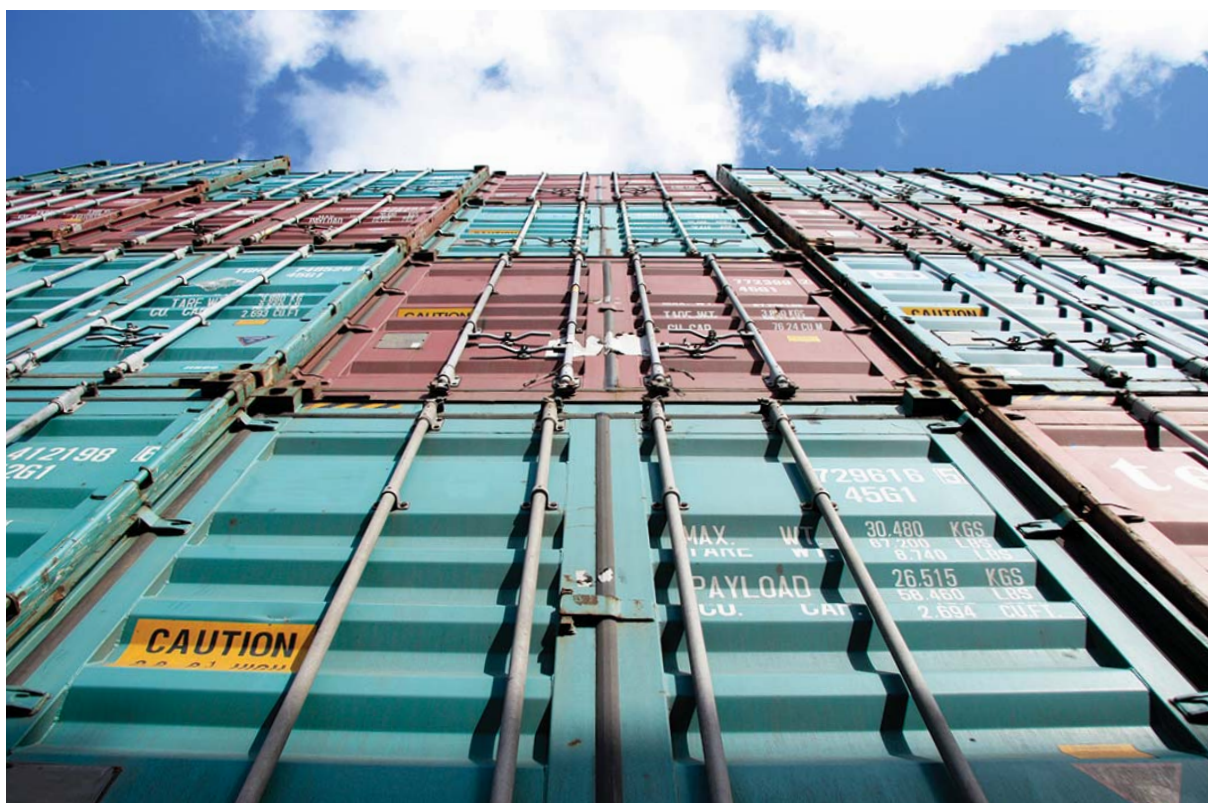
EXECUTIVE SUMMARY

INTRODUCTION

Project SUN is an annual study estimating the scale and development of the illicit cigarette market in Europe.

This report was commissioned jointly by the four major tobacco manufacturers (British American Tobacco plc, Imperial Tobacco Limited, JT International SA and Philip Morris International Management SA) for data covering 2013. KPMG LLP was previously commissioned by Philip Morris International Management SA to produce reports covering 2006 and 2012 ('Project STAR'). The study covers all 28 European Union member states with Croatia included for the first time in 2013.

The methodology used to estimate the size of the illicit cigarette market in connection with the Project STAR reports has continued to be applied consistently in the Project SUN report. The input and provision of data sources from all four major cigarette manufacturers has however provided KPMG LLP with access to a much wider set of data sources, allowing for greater refinement of results and an enhanced level of detail in the report.



Counterfeit and contraband volumes declined as a percentage of overall consumption in 2013

Overall volumes of counterfeit and contraband (C&C) consumption declined from 65.7 billion cigarettes to 58.6 billion cigarettes. The C&C share of overall consumption fell from 11.1% to 10.5%. If these cigarettes had been sold legally in the countries where they were identified, the tax revenue would have been worth approximately €10.9 billion.

The C&C decline reflects a reduction of 3.9 billion cigarettes in the UK and 3.6 billion cigarettes in Italy, whilst in most countries, consumption of C&C products remained broadly static.

Greece experienced an increase in the overall volume of C&C products consumed achieving 17% of overall consumption.

Consumption of Illicit Whites brands grew from 17.1 billion to 19.6 billion cigarettes in 2013, 33% of overall C&C consumption

Illicit Whites brands were identified in every EU country (except Luxembourg), many with unspecified or Duty Free labelling. The majority of Illicit Whites brands are manufactured by six manufacturers and distributed across Europe through sophisticated criminal supply chains.

The largest source of Illicit Whites was Belarus, where a large volume of brands were manufactured by the Grodno Tobacco Company.

Overall consumption of legally manufactured cigarettes in the EU declined by 7%

Legal domestic consumption, the most significant proportion of total consumption in all markets, declined by 7.5%. Legal domestic sales may have been impacted by both the economic environment within Europe and price rises. Unemployment rose in 21 of the 28 EU countries, whilst in over half the EU countries prices increased by more than 5%. In some countries there is evidence of consumers switching to other tobacco products (OTP).

Levels of EU contraband consumption (excluding Illicit Whites) declined significantly, in the main being replaced by non-domestic legal (ND(L)) purchases

Border sales between cheaper and more expensively priced markets grew by 12.0% in 2013. In many areas with high volumes of border sales, prices in cheaper markets increased at a greater level than in more expensive markets, resulting in a lower price gap.

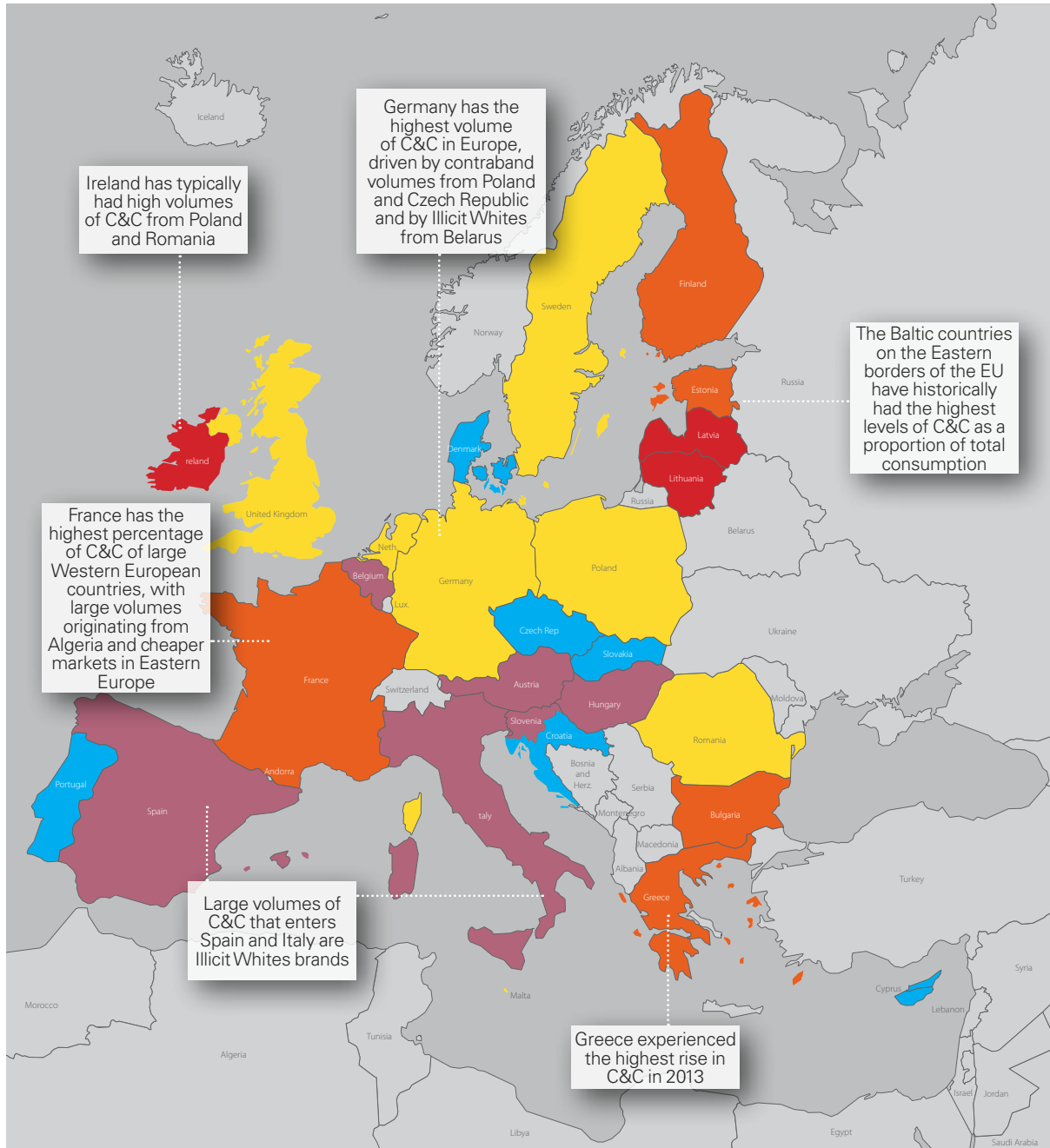
Countries with large populations close to the border with cheaper markets had the highest volume of non-domestic legal consumption. These countries included the Netherlands, Austria, France and Germany.



EUROPEAN MARKET OVERVIEW

There are significant hotspots of C&C consumption across the European Union

Counterfeit and contraband consumption as a percentage of overall consumption 2013⁽¹⁾



EXECUTIVE SUMMARY



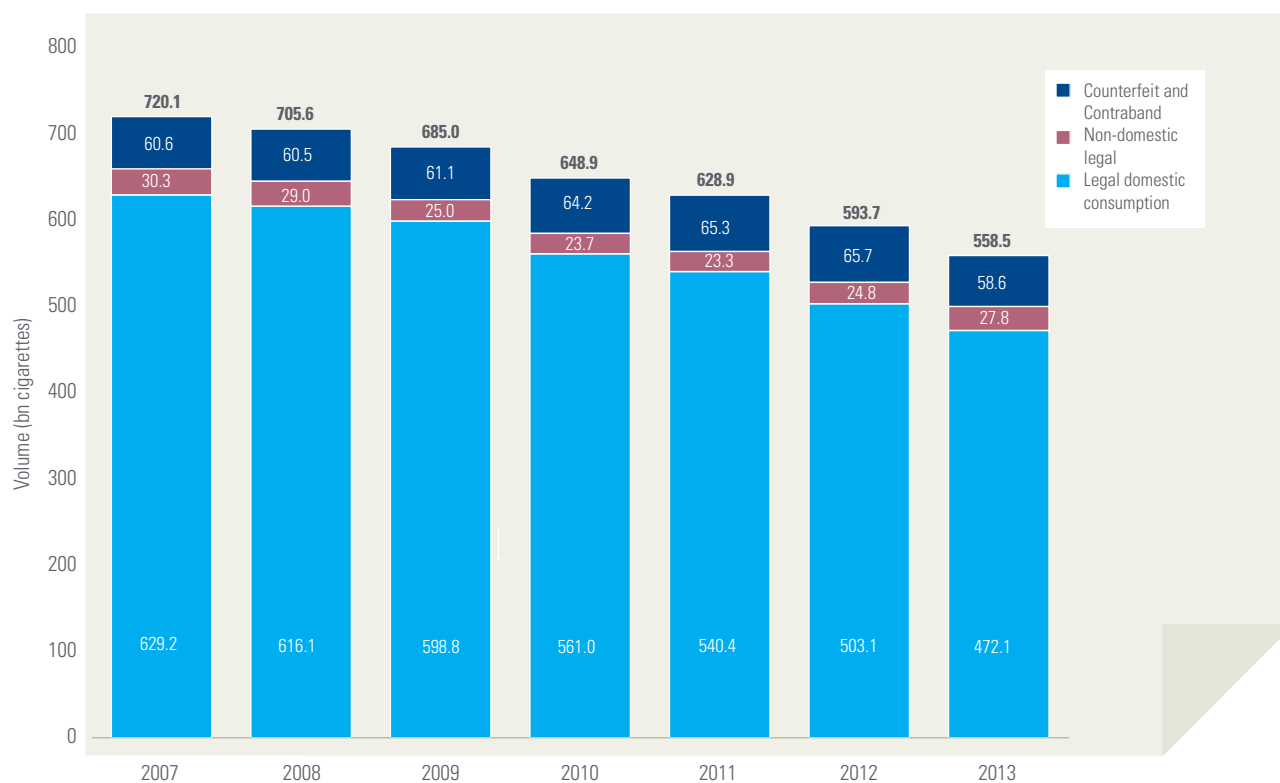
PROJECT SUN

Source: (1) KPMG EU Flows Model calculations, 2013.

EUROPEAN MARKET OVERVIEW

Overall consumption declined by 7% in 2013. For the first time since the start of the study, C&C decreased by 11% in volume terms

Total cigarette consumption within the EU by type 2007-2013^{(1)(a)(b)}



GROWTH RATE OF TOTAL CIGARETTE CONSUMPTION WITHIN THE EU

CAGR (%) ^(a)	2007-2013	2012-13 %
Counterfeit and Contraband	(0.5)%	(10.6)%
Non-domestic legal	(1.4)%	12.0%
Legal domestic consumption	(4.9)%	(7.5)%
Total	(4.3)%	(7.0)%

Note: (a) The percentages above have been calculated without the inclusion of Croatia, however the overall volumes for 2013 include Croatia for the first time. Without Croatia total consumption would have been 551.5 billion, C&C 58.3 billion, ND(L) 27.7 billion and legal domestic consumption 465.6 billion.

(b) The availability of data from all manufacturers for the first time in 2013 has allowed for additional refinement of results in some countries. The net impact of this is to allocate an additional 1 billion to ND(L) from C&C. Without these refinements C&C would be 59.6 billion and ND(L) 26.8 billion.

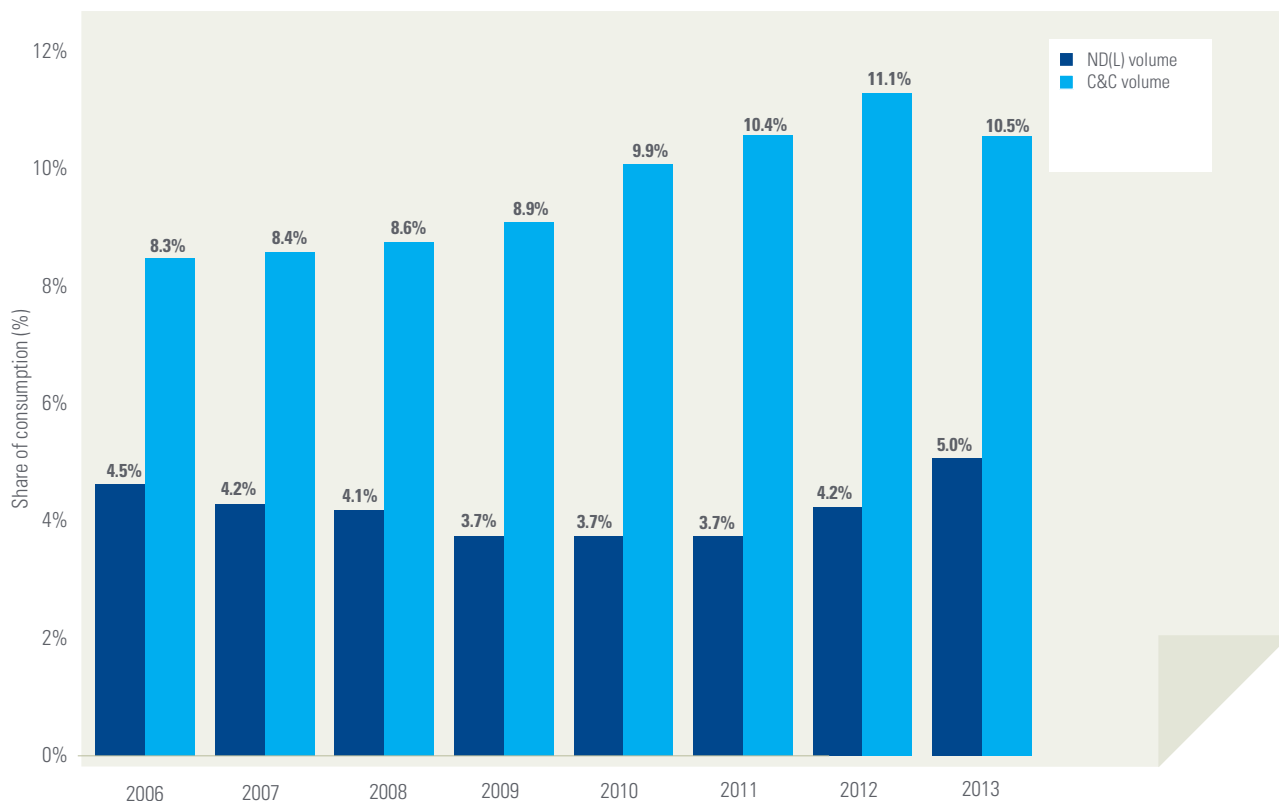
Source: (1) KPMG EU Flows Model 2007 – 2013.



EUROPEAN MARKET OVERVIEW

After years of growth, C&C declined as a share of total consumption in 2013, while ND(L) continued to grow

ND(L) and C&C share of total consumption 2006-2013^{(1)(a)(b)}



EXECUTIVE SUMMARY



PROJECT SUN

ND(L) AND C&C VOLUMES (BN CIGARETTES)								
	2006	2007	2008	2009	2010	2011	2012	2013
ND(L) volume	31.0	30.3	29.0	25.0	23.7	23.3	24.8	27.8
C&C volume	56.8	60.6	60.5	61.1	64.2	65.3	65.7	58.6

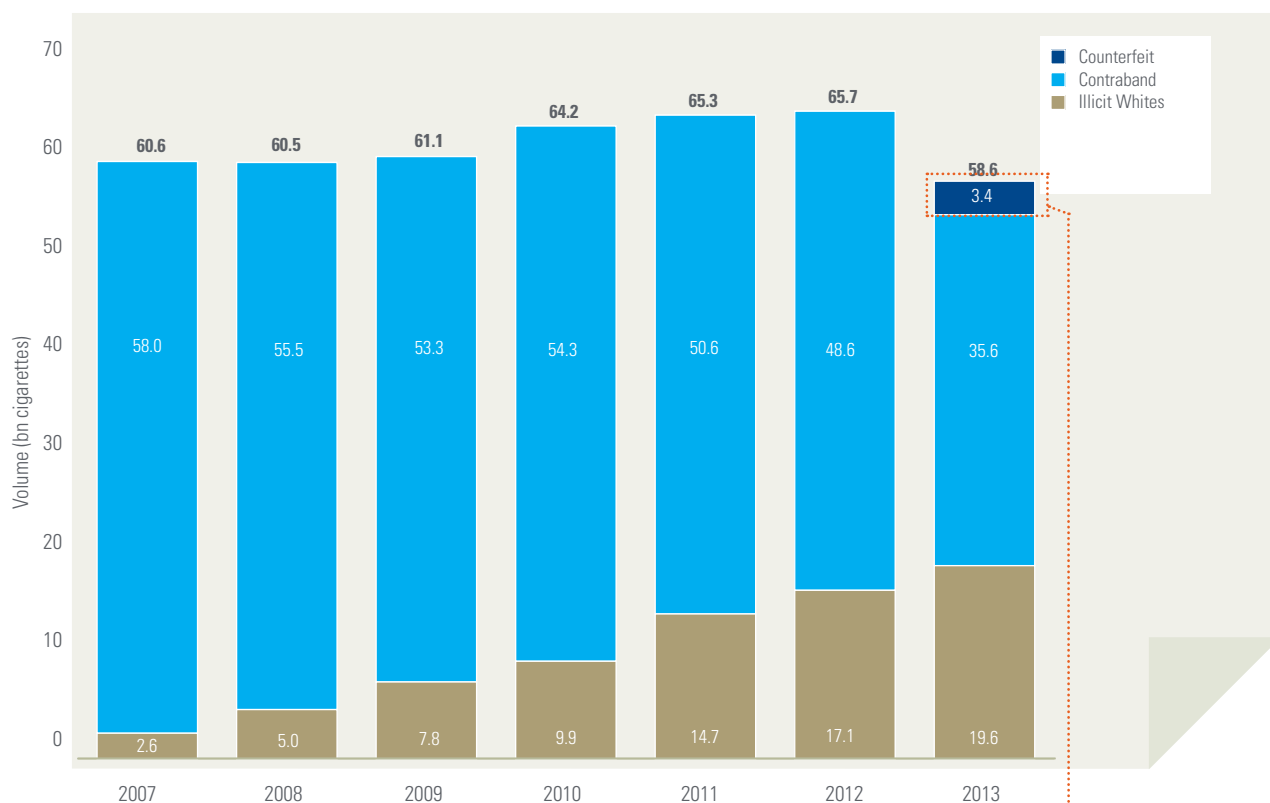
Note: (a) As previously noted, the availability of additional data sources has had a net impact of 1 billion sticks in favour of ND(L). Had this not been available, the overall C&C volume would have been 10.75% of total consumption and ND(L) 4.85%.

(b) 2006 calculation does not include Bulgaria and Romania.

Source: (1) KPMG EU Flows Model calculations 2006 – 2013.

Illicit Whites grew to 33% of overall C&C consumption in 2013

Counterfeit and contraband consumption by type 2007-2013^{(1)(a)}



Conducting Project SUN on a pan-industry basis has allowed for estimation of total counterfeit volumes for the first time in 2013^(b)

Note: (a) Overall decline in C&C includes the effect of availability of additional data sources as stated previously.
 (b) The Counterfeit volume reflects Counterfeit data from BAT, Imperial Tobacco, JTI and PMI, but does not include data from other manufacturers.

Source: (1) KPMG EU Flows Model 2007 – 2013.



EUROPEAN MARKET OVERVIEW

Hungary, Slovenia and Croatia had the highest price increases in the EU in 2013 in order to comply with the minimum EU tax rate

COUNTRY PRICE COMPARISON WEIGHTED AVERAGE PRICE (WAP), PACK OF 20 (€) ^(a)			
Country	End of 2012	End of 2013	Price change
Serbia	1.52	1.79	16.2%
Hungary	2.66	3.00	13.0%
Russia	1.16	1.31	12.7%
Slovenia	2.95	3.27	10.8%
Croatia	2.46	2.70	10.0%
Ukraine	0.80	0.88	9.9%
Albania	1.27	1.39	9.1%
Bosnia	1.57	1.71	9.1%
Finland	4.50	4.89	8.7%
Canary Islands	1.68	1.83	8.6%
UK	7.52	8.15	8.5%
Latvia	2.40	2.60	8.3%
Estonia	2.62	2.82	7.6%
Greece	3.28	3.50	6.8%
Spain	4.03	4.30	6.7%
France	6.10	6.50	6.6%
Romania	2.64	2.81	6.5%
Lithuania	2.25	2.38	5.8%
Austria	3.95	4.18	5.7%
Slovakia	2.72	2.87	5.7%
Poland	2.65	2.80	5.5%
Switzerland	6.00	6.33	5.5%
Ireland	8.47	8.92	5.3%
Netherlands	5.03	5.29	5.1%
Cyprus	3.91	4.08	4.3%
Czech Republic	2.76	2.88	4.2%
Macedonia	1.24	1.29	3.8%
Germany	4.88	5.02	2.8%
Luxembourg	3.84	3.95	2.8%
Belgium	4.77	4.88	2.3%
Denmark	5.26	5.33	1.3%
Portugal	3.85	3.90	1.3%
Bulgaria	2.36	2.38	0.9%
Italy	4.56	4.58	0.4%
Malta	4.14	4.07	(1.6)%
Sweden	6.02	5.91	(1.8)%
Belarus	0.66	0.64	(3.5)%
Norway	12.14	11.66	(3.9)%

Key:
EU countries highlighted

Note: (a) Manufacturer estimates used for countries not included in the EU Tax Tables.

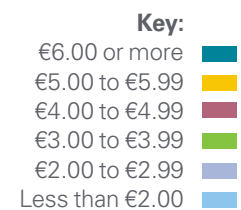
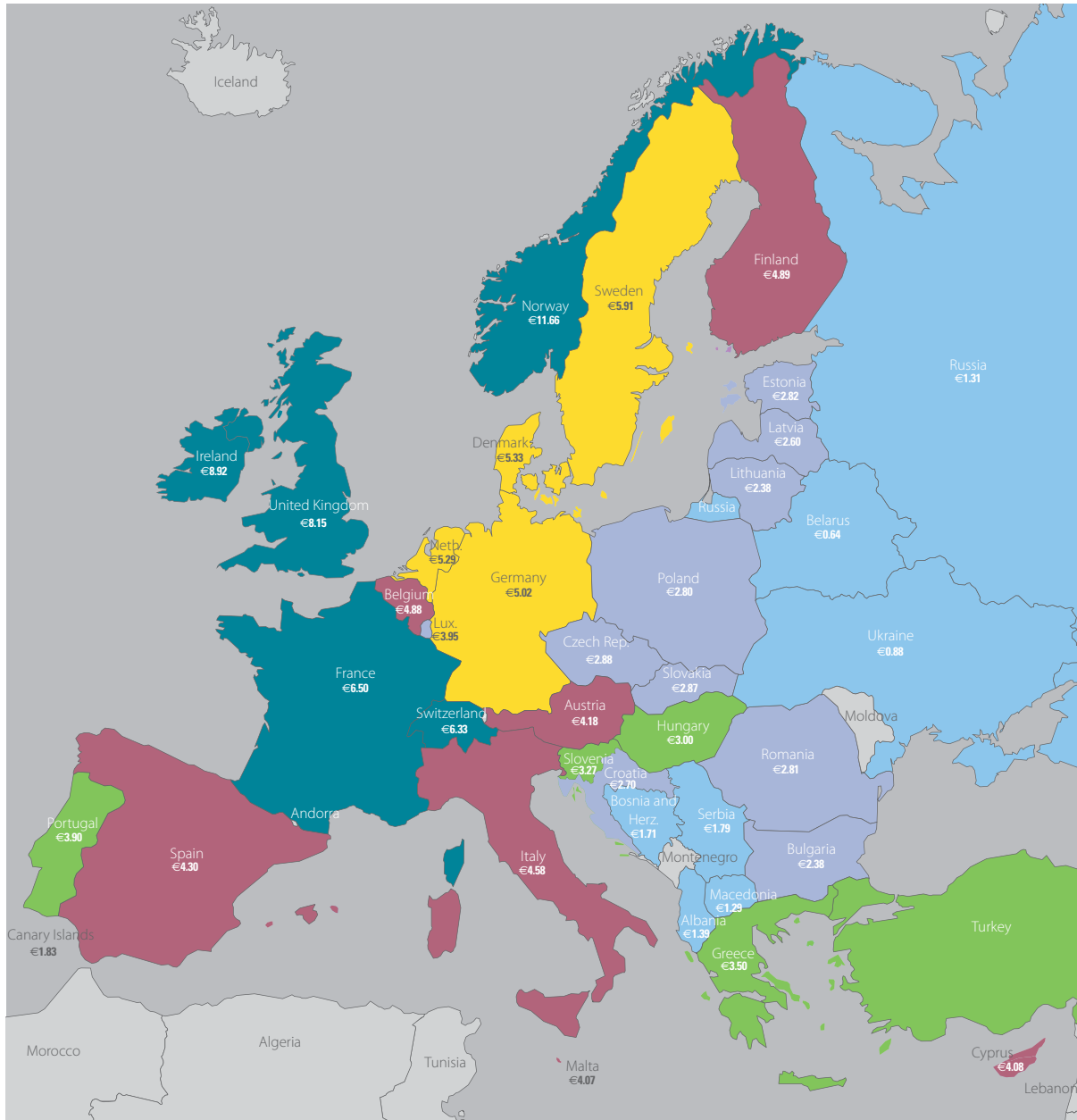
Source: (1) WAP from EC Excise Duty tables (Part III – Manufactured Tobacco) and manufacturer estimates for non-EU countries.



EUROPEAN MARKET OVERVIEW

Price gaps have narrowed between EU countries; however, prices in non-EU countries on the Eastern border remain up to 13 times lower than the EU

Map denotes weighted average prices for a pack of 20 cigarettes - End of 2013⁽¹⁾

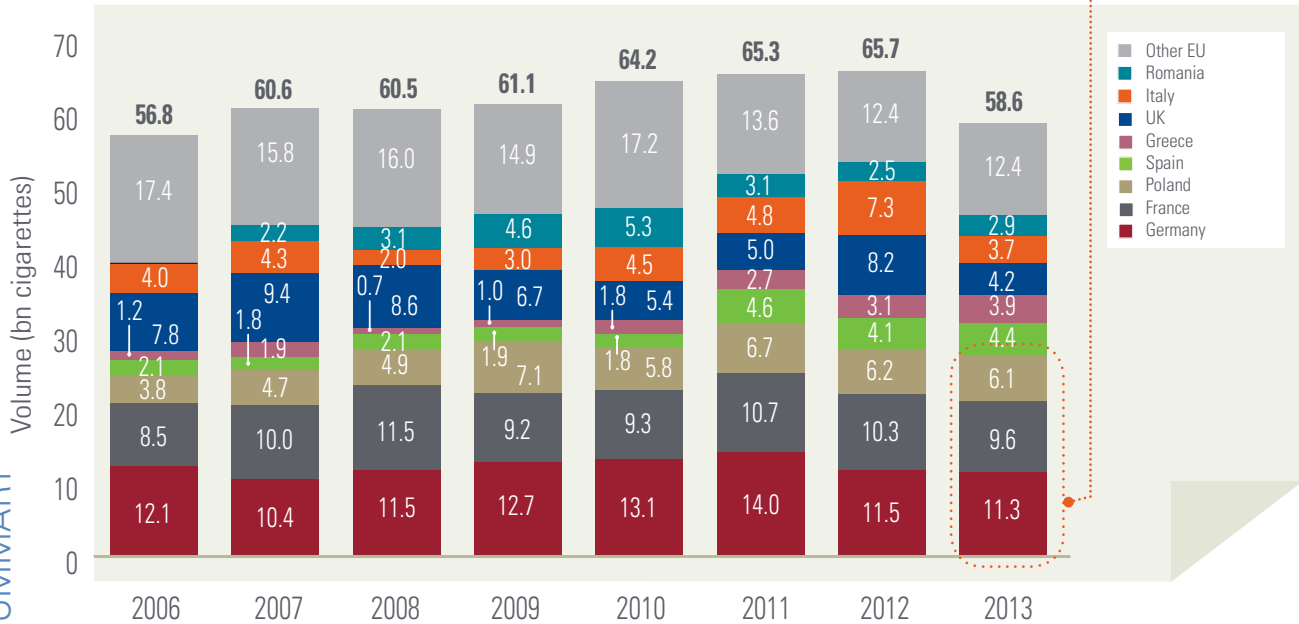


Source: (1) WAP from EC Excise Duty tables (Part III – Manufactured Tobacco) and manufacturer estimates for non-EU countries.

EUROPEAN MARKET OVERVIEW

The key C&C consumption markets of Germany, France and Poland were stable. Whilst there were significant declines in Italy and UK, there were increases in Spain and Greece. The main source country to increase was Belarus

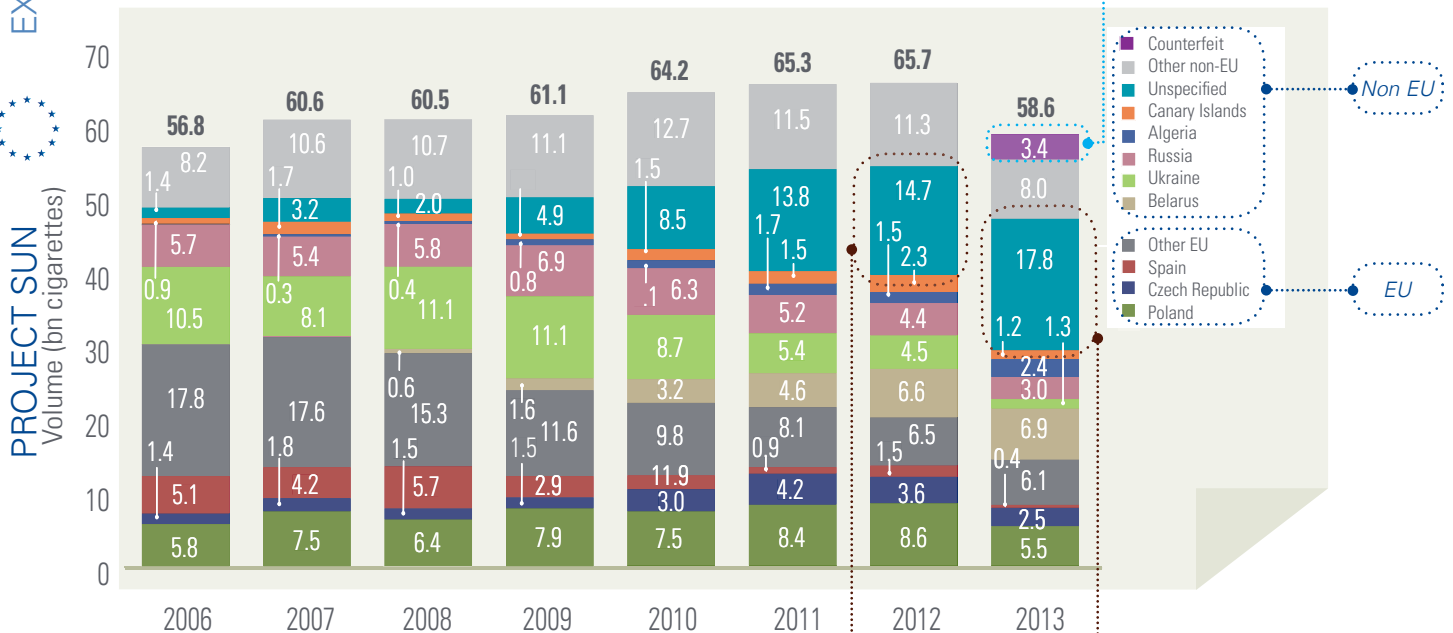
C&C volume by destination country 2006-2013⁽¹⁾



Almost half of C&C manufactured cigarettes are consumed within three countries in Europe

EXECUTIVE SUMMARY

C&C volume by source country 2006-2013⁽¹⁾



Conducting Project SUN on a pan-industry basis has enabled an estimation of total counterfeit volumes for the first time in 2013

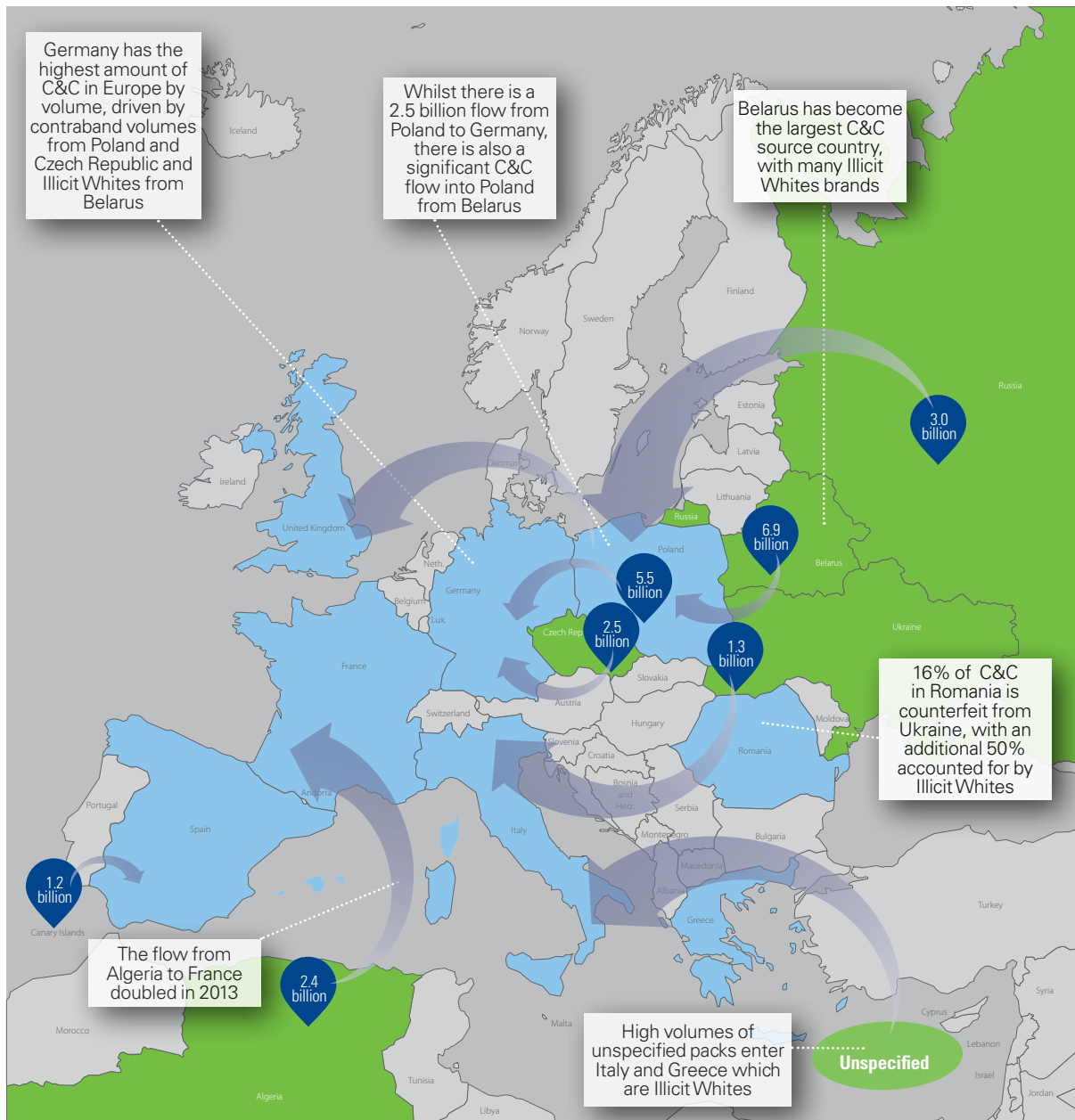
The growth in "unspecified" as a source of C&C is the result of greater volumes being sold with no tax stamps and as Illicit Whites

Source: (1) KPMG EU Flows Model 2006 – 2013.

EUROPEAN MARKET OVERVIEW

A greater proportion of counterfeit and contraband now originates from unspecified sources along with Belarus, Russia and North African countries

Major C&C inflows and source countries 2013⁽¹⁾



Main inflow

Denotes total volume into EU

Source: (1) KPMG EU Flows Model 2013.

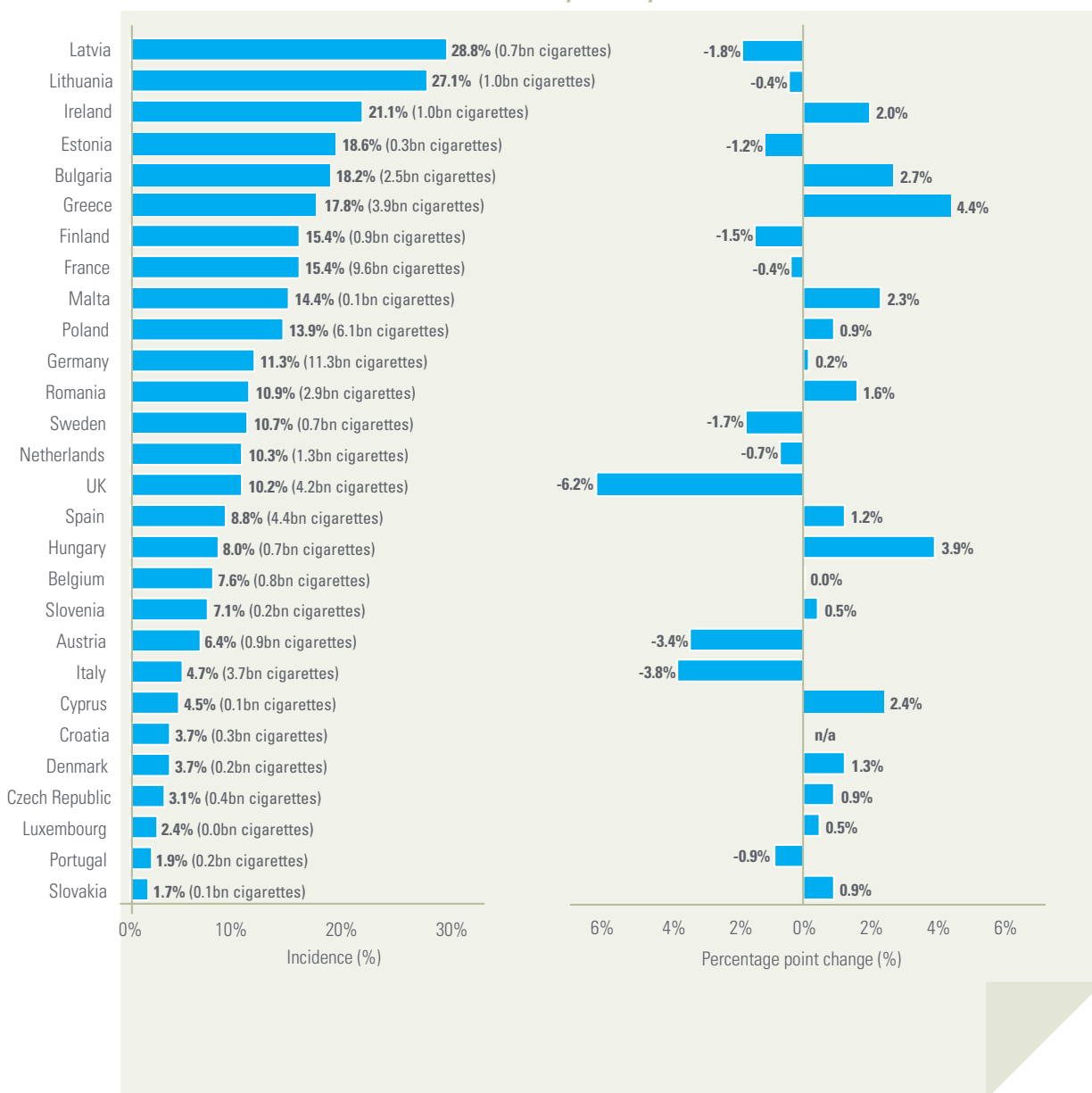


EUROPEAN MARKET OVERVIEW

11 of the 28 EU markets experienced a decline in illicit cigarette consumption as a percentage of overall consumption in 2013

C&C consumption incidence by country 2013⁽¹⁾

Percentage point change in C&C consumption incidence by country 2012 vs 2013⁽¹⁾



Source: (1) KPMG EU Flows Model 2013.

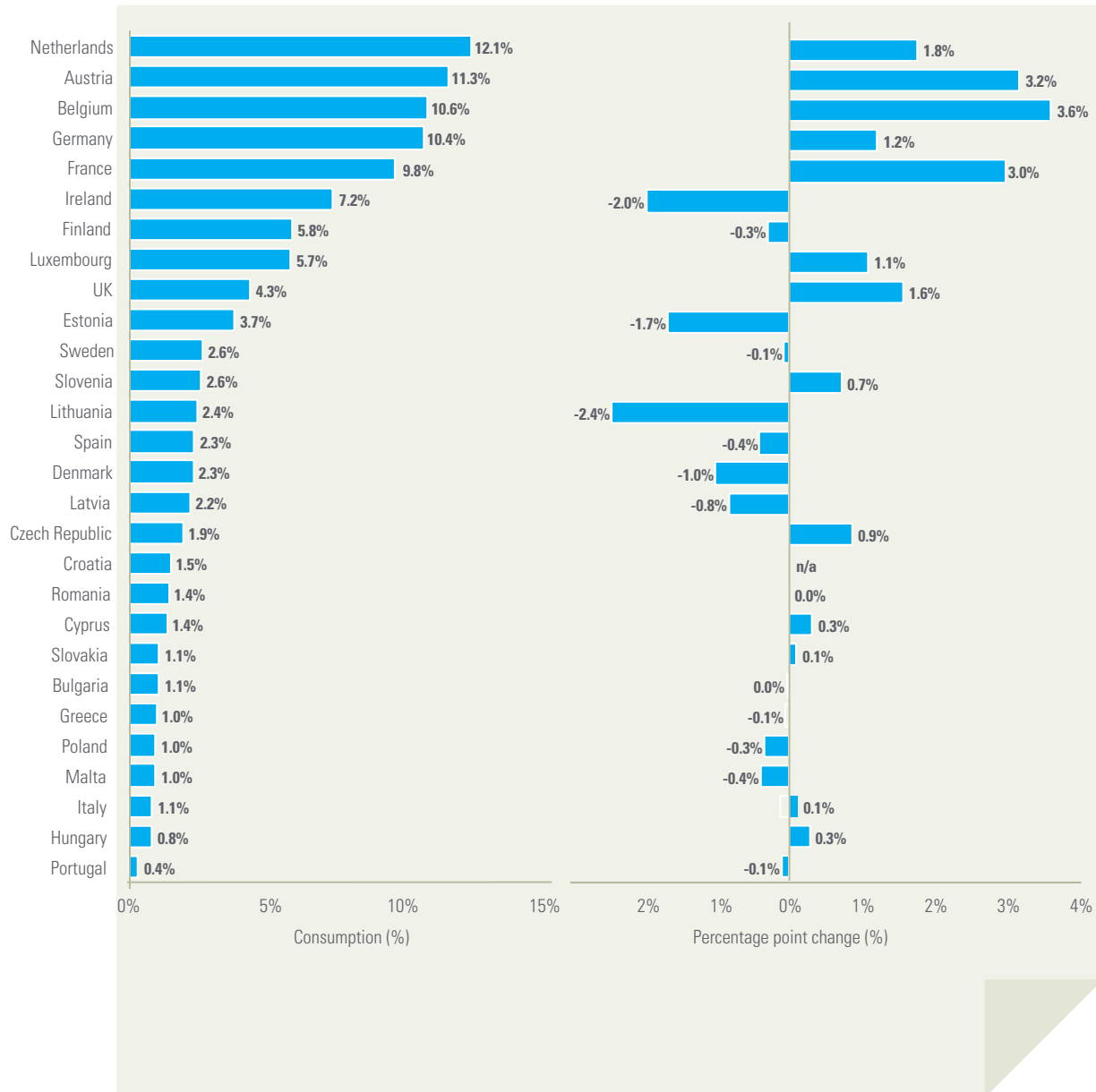


EUROPEAN MARKET OVERVIEW

ND(L) increased as a share of overall consumption in several large markets, including Germany and France

ND(L) consumption incidence by country 2013⁽¹⁾

Percentage point change in ND(L) consumption incidence by country 2013⁽¹⁾

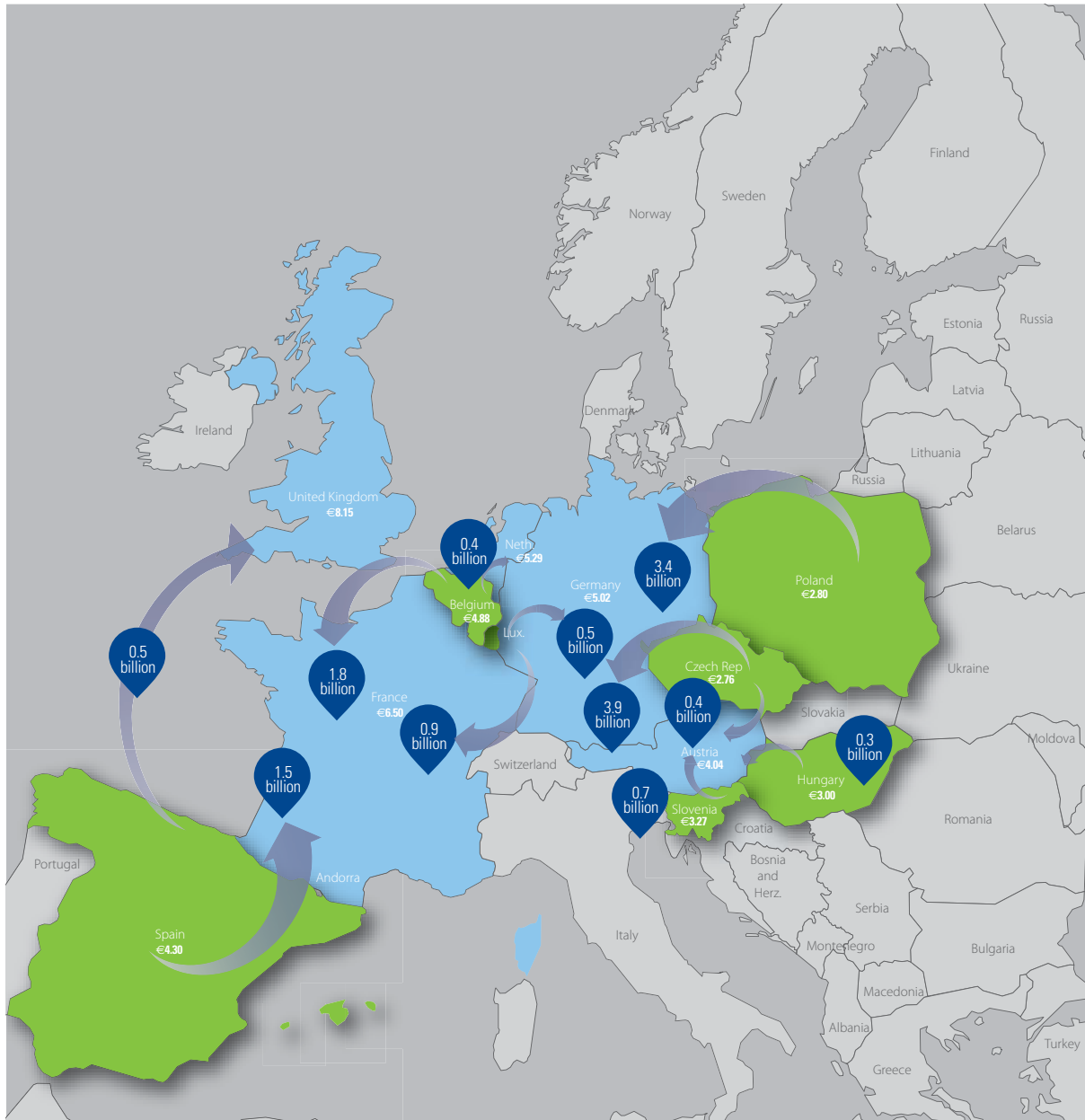


Source: (1) KPMG EU Flows Model 2013.

EUROPEAN MARKET OVERVIEW

Non-domestic legal consumption increased as a result of greater border sales between markets with large price differentials

Major border sales points⁽¹⁾



Key: Border countries

Higher priced country ■

Lower priced country ■

Denotes size of flow ●

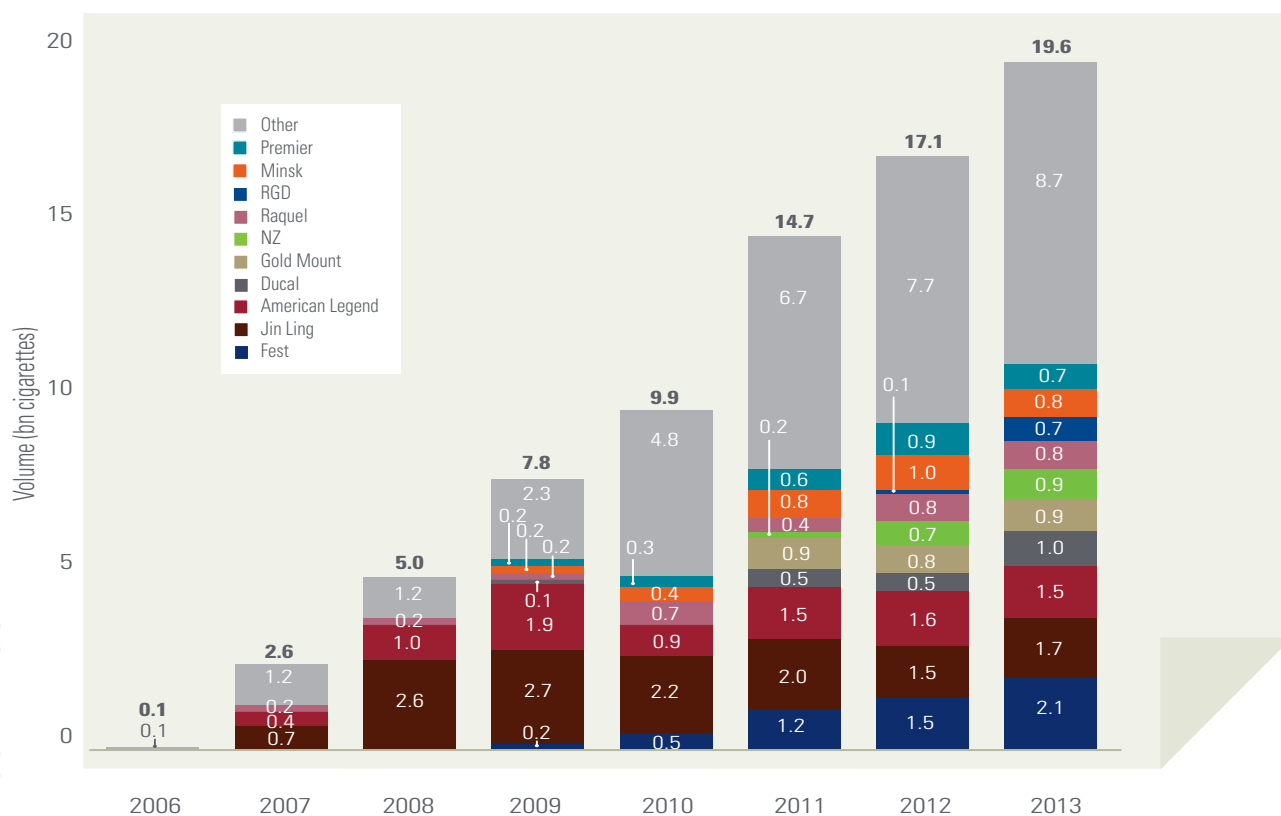
Source: (1) KPMG analysis of Non-domestic legal research.



ILLCIT WHITES

Total consumption of Illicit Whites increased by 15% in 2013, representing 33% of total C&C volumes in the EU. The largest Illicit Whites brand is Fest, which increased its volumes by 44%

Consumption of Illicit Whites brands 2006-2013^{(1)(a)}



ILLCIT WHITES AS A PERCENTAGE OF TOTAL EU C&C

	2006	2007	2008	2009	2010	2011	2012	2013
% of total EU C&C	0.2%	4.3%	8.3%	12.7%	15.5%	22.6%	26.0%	33.5%

GROWTH OF ILLICIT WHITES

CAGR (%)	2007-2013	2012-13 %
Illicit Whites	40%	15%

TOP ILLICIT WHITES BRANDS GROWTH

BRAND	2012-13 %
Fest	44%
Jin Ling	8%
American Legend	(5)%
Ducal	81%
Gold Mount	5%
NZ	32%
Raquel	(11)%
RGD	541%
Minsk	(21)%
Premier	(17)%

Note: (a) Our definition of Illicit Whites has been updated in 2013 to the ITIC definition (shown in the Glossary). We have updated our Illicit Whites analysis from prior years in reflection of this and have applied this definition consistently over the period shown, resulting in some updates to Illicit White volumes from prior years.

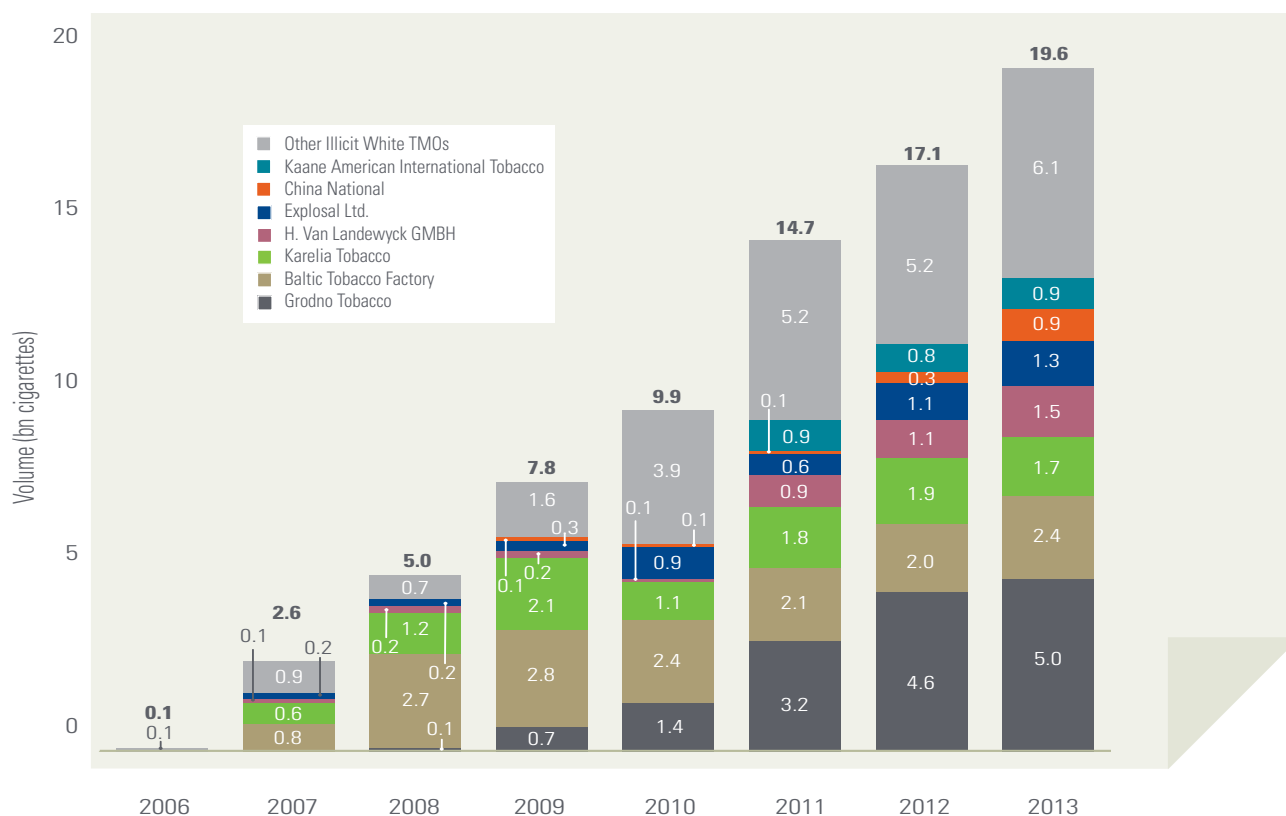
Source: (1) KPMG analysis based on Empty Pack Surveys, legal domestic sales and non-domestic (legal) research.

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ILLICIT WHITES

Grodno Tobacco remained the largest Illicit Whites trademark owner in 2013 whilst Baltic Tobacco increased volumes by 19%

Consumption of Illicit Whites brands by trademark owner 2006-2013^{(1)(a)}



ILLICIT WHITES TRADEMARK OWNER GROWTH	
TRADEMARK OWNER	2012-13 %
Grodno Tobacco	9%
Baltic Tobacco Factory	19%
Karelia Tobacco	(9)%
H. Van Landewyck GMBH	27%
Explosal Ltd.	12%
China National	161%
Kaane American International Tobacco	5%

Note: (a) Our definition of Illicit Whites has been updated in 2013 to the ITIC definition (shown in the Glossary). We have updated our Illicit Whites analysis from prior years in reflection of this and have applied this definition consistently over the period shown, resulting in some updates to Illicit White volumes from prior years.

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

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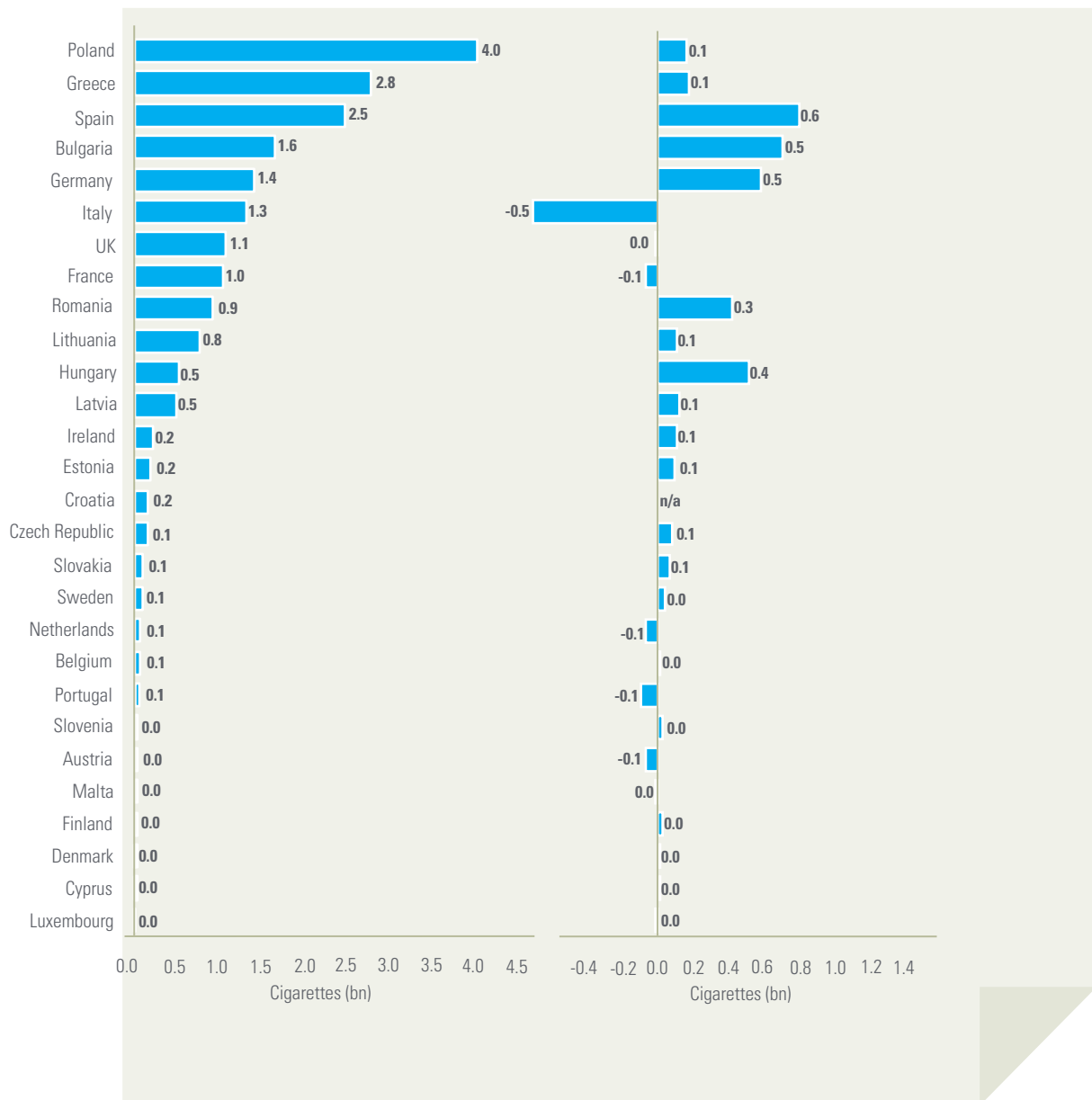


ILLCIT WHITES

Poland had the highest level of Illicit Whites consumption in 2013. 15 out of 28 EU markets experienced a growth in Illicit Whites consumption in 2013

Illicit Whites consumption by country 2013^{(1)(a)}

Volume change in Illicit Whites consumption by country, 2012 vs 2013^{(1)(a)}



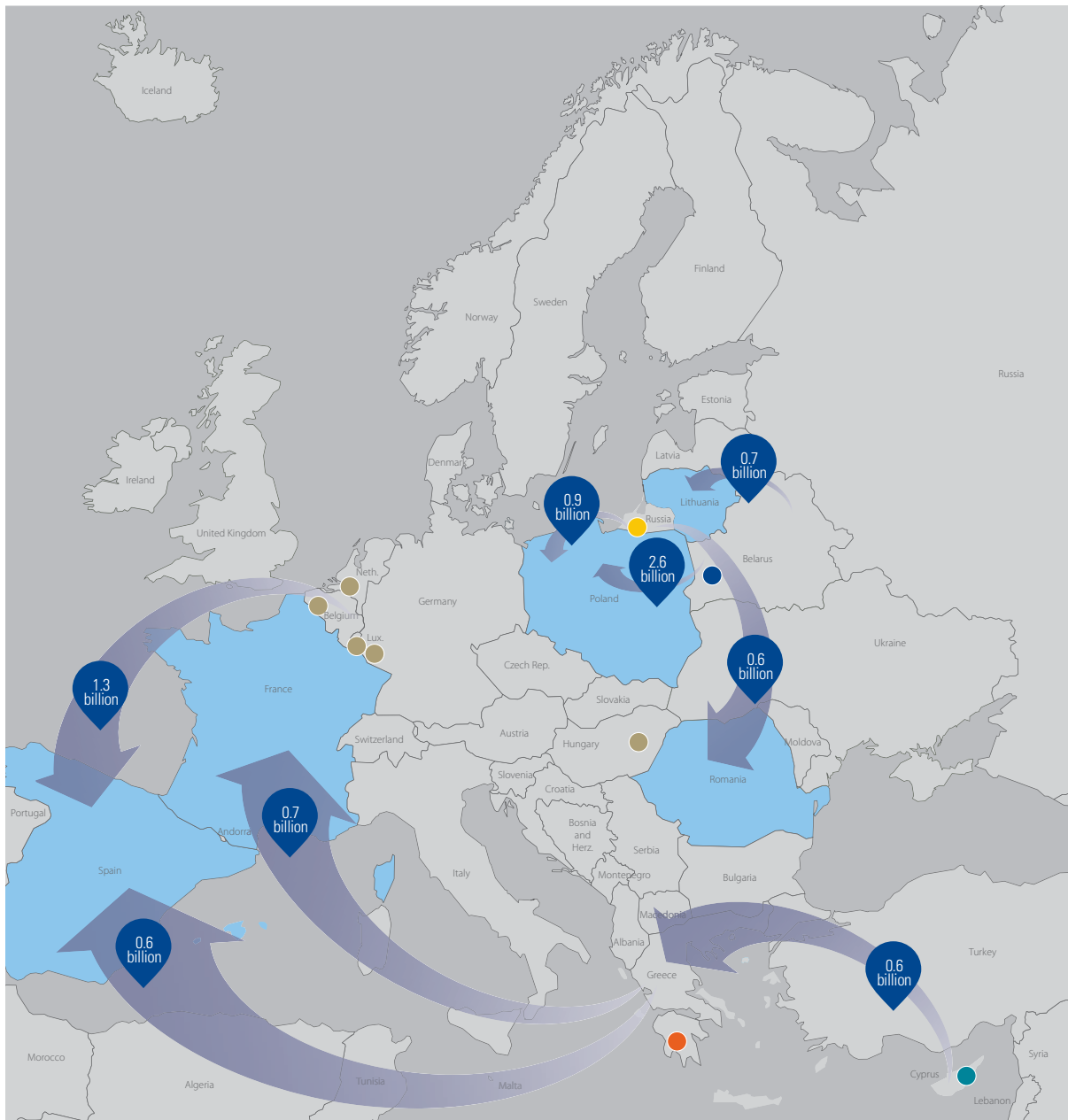
Note: (a) Our definition of Illicit Whites has been updated in 2013 to the ITIC definition (shown in the Glossary). We have updated our Illicit Whites analysis from prior years in reflection of this and have applied this definition consistently over the period shown, resulting in some updates to Illicit White volumes from prior years.

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

ILLCIT WHITES

Belarus continues to be the largest known source country of Illicit Whites brands, which are mainly manufactured by Grodno Tobacco Company

Source country of Top 5 manufacturers 2013^{(1)(a)(b)}



Key:

- Illicit Whites main destination countries
- Flow from manufacturer to destination country
- Grodno Tobacco
- Baltic Tobacco Factory
- Karella Tobacco
- H. Van Landewyck GMBH
- Explosal Ltd.

Note: (a) Analysis represents flows for brands of the top 5 manufacturers and from unspecified markets, representing over 60% of total Illicit Whites volumes in 2013.

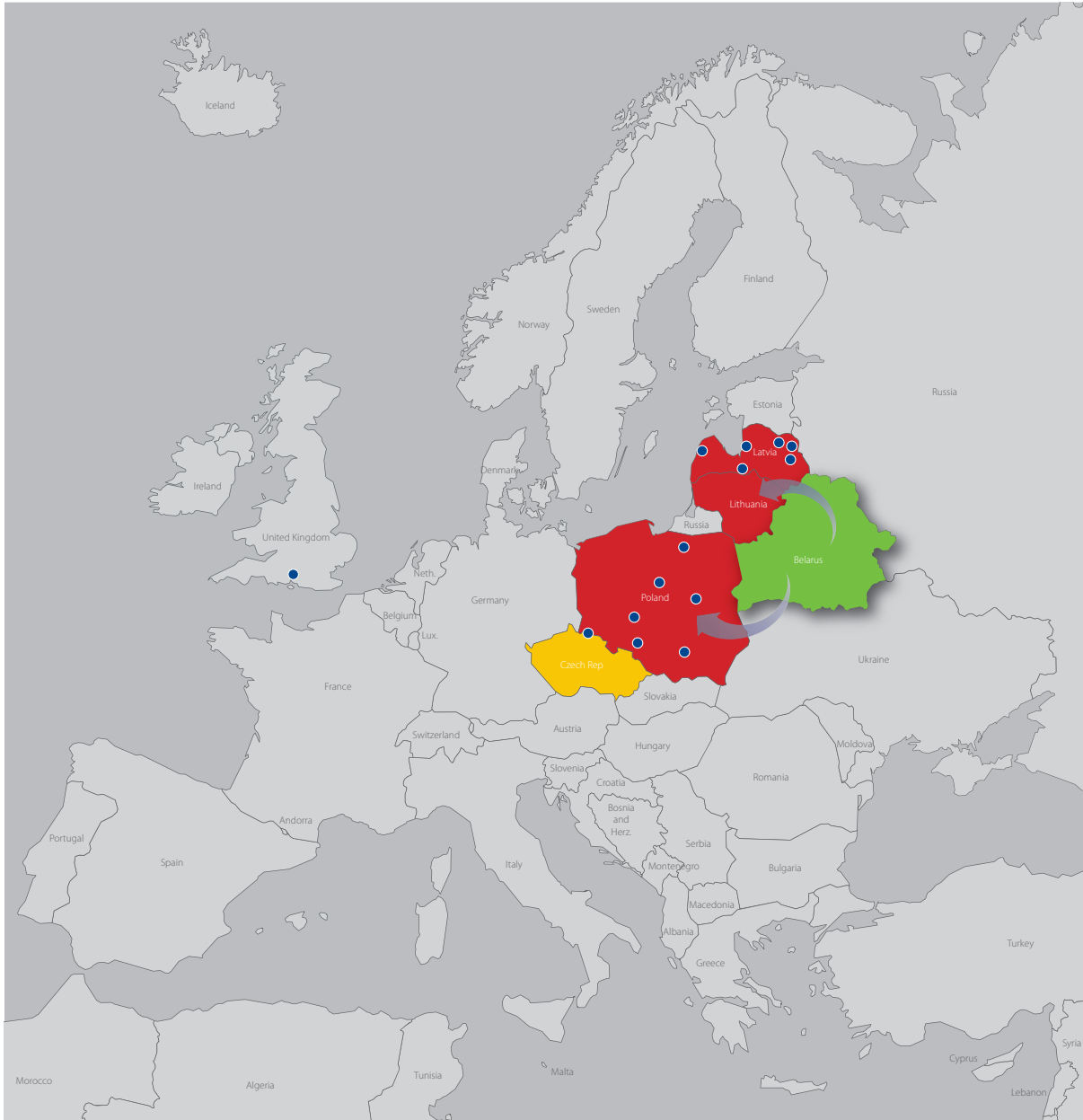
Source: (1) KPMG analysis based on EPS, LDS and ND(L) research.



ILLCIT WHITES

While Grodno Tobacco brands were found in 4 countries in 2009, its brands have become prevalent in 15 countries in 2013

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



Key:

- Grodno tobacco brands comprise greater than 0.5% of total consumption ■
- Grodno tobacco brands comprise between 0.1% and 0.5% of total consumption ■
- Grodno Tobacco brand located ●

Note: (a) The analysis covers Illicit Whites brands found in 2009.
 (b) The number of dots marked represent the varying levels of consumption in each country.
 (c) Grodno brands in the EU consist of Fest, NZ, Minsk, Premier, Queen, Magnat and VIP.

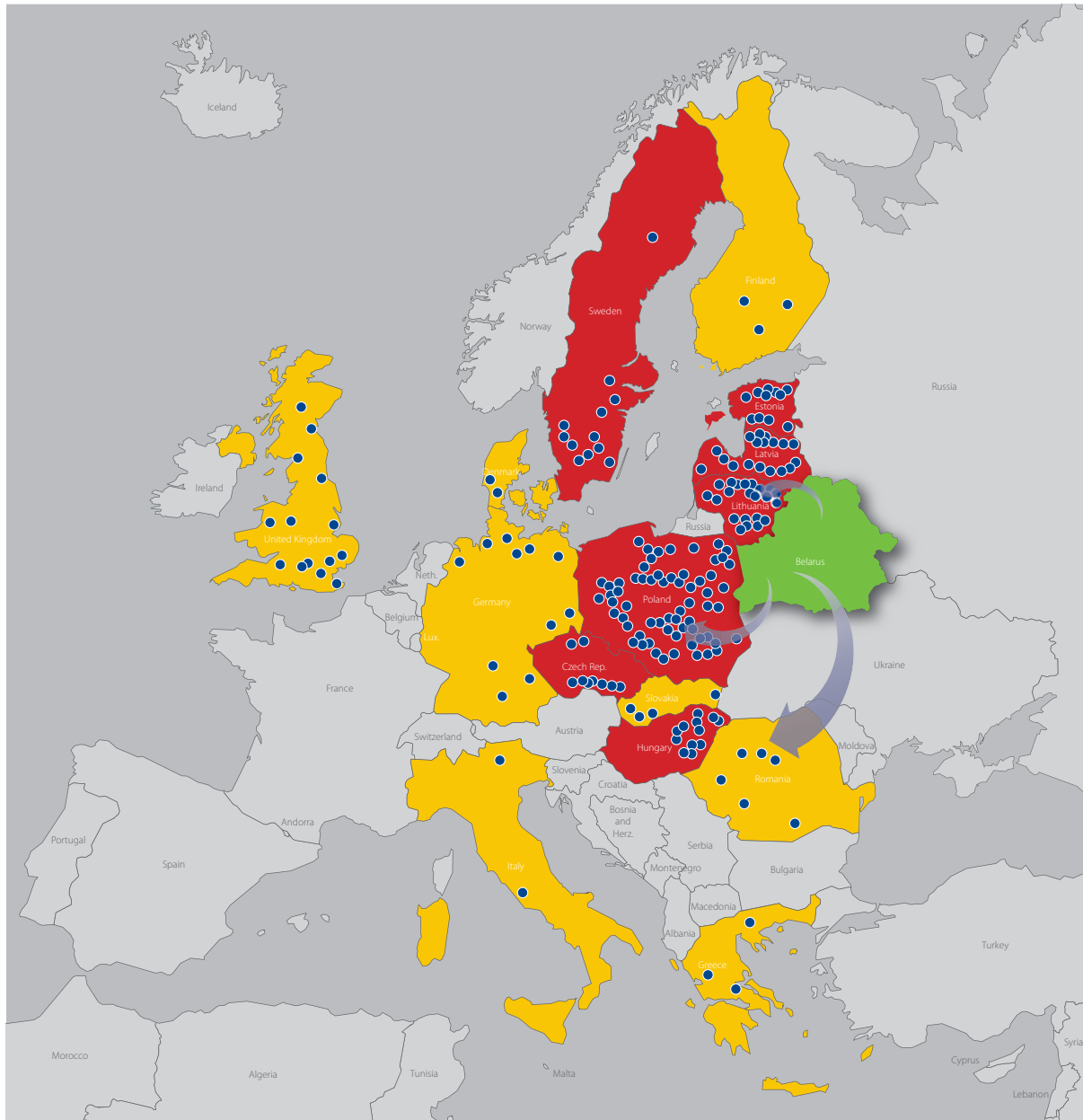
Source: (1) KPMG analysis based on Empty Pack Surveys, legal domestic sales and non-domestic (legal) research.



ILLCIT WHITES

Grodno Tobacco brands have spread further west through Europe since 2009

Consumption of Grodno Tobacco brands 2013^{(1)(a)(b)(c)}



Key:

- Grodno tobacco brands comprise greater than 0.5% of total consumption ■
- Grodno tobacco brands comprise between 0.1% and 0.5% of total consumption ■
- Grodno Tobacco brand located ●

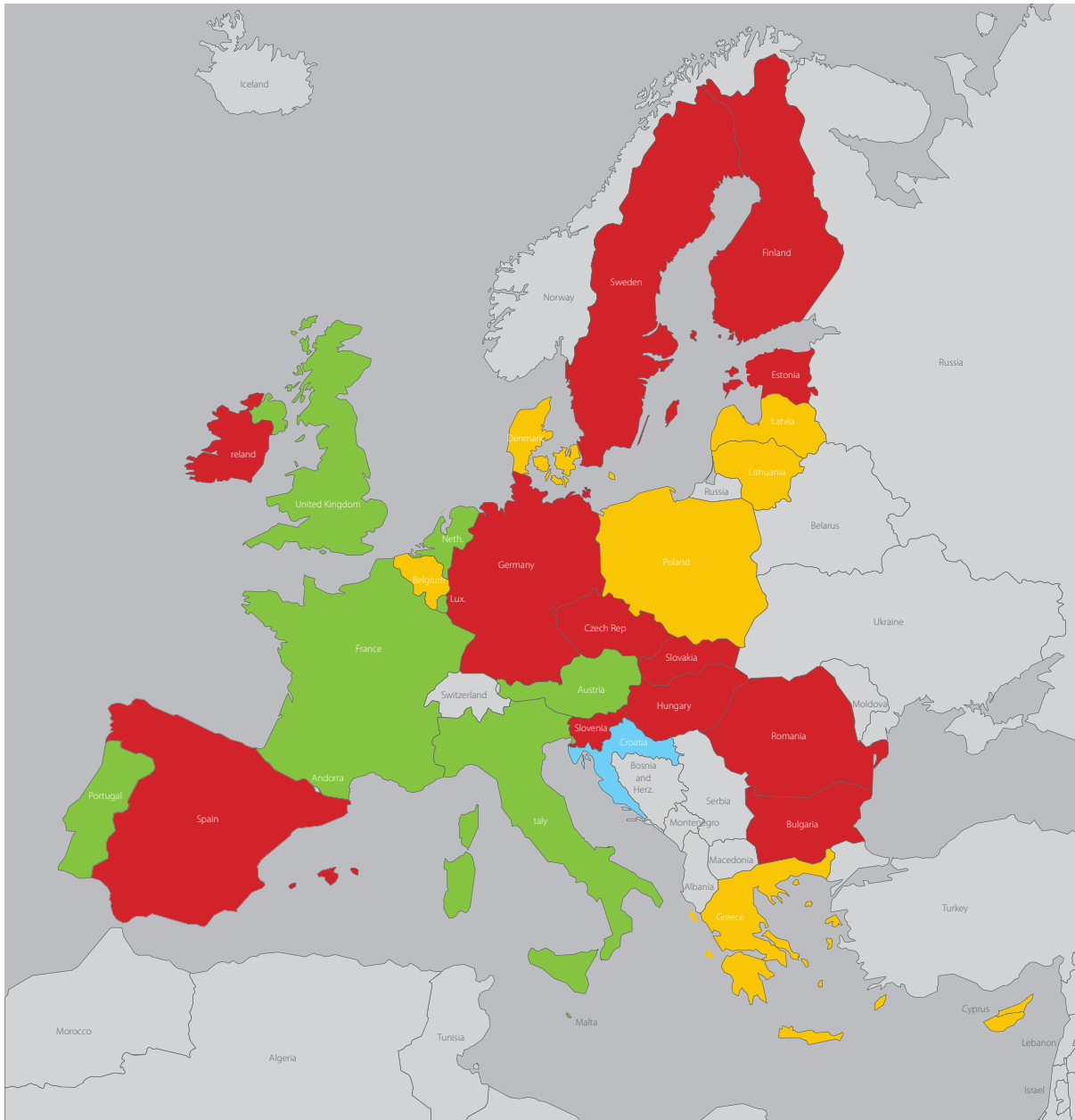
Note: (a) The analysis covers Illicit Whites brands found in 2013.
 (b) The number of dots marked represent the varying levels of consumption in each country.
 (c) Grodno brands in the EU consist of Fest, NZ, Minsk, Premier, Queen, Magnat and VIP.

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

ILLCIT WHITES

Eastern European and Scandinavian countries have seen the fastest growth of Illicit Whites volumes in 2013

Change in Illicit Whites consumption 2012-2013^{(1)(a)(b)}



Key: 2012/2013 % Growth
 >30% ■
 0-30% ■
 <0% ■
 n/a ■

Note: (a) Our definition of Illicit Whites has been updated in 2013 to the ITIC definition (shown in the Glossary). We have updated our Illicit Whites analysis from prior years in reflection of this and have applied this definition consistently over the period shown, resulting in some updates to Illicit White volumes from prior years.

(b) Illicit Whites volumes in Croatia were not identified in 2012, therefore it is not possible to calculate a percentage change year on year; countries where volumes have increased from zero have been coloured red, while countries which remained at zero have been coloured yellow.

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

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ILLICIT WHITES

VOLUME AND GROWTH OF ILLICIT WHITES BRANDS BY COUNTRY				
COUNTRY	2012	2013	CHANGE 2012/13%	Share of consumption
Hungary	0.12	0.52	>100%	5.8%
Finland	0.01	0.03	>100%	0.6%
Slovakia	0.04	0.10	>100%	1.5%
Slovenia	0.02	0.05	>100%	1.5%
Czech Republic	0.09	0.15	70%	1.1%
Estonia	0.12	0.19	64%	10.3%
Ireland	0.15	0.23	57%	5.0%
Romania	0.60	0.93	54%	3.5%
Bulgaria	1.10	1.64	50%	11.9%
Germany	0.93	1.39	49%	1.4%
Sweden	0.07	0.09	40%	1.5%
Spain	1.83	2.45	34%	4.9%
Latvia	0.40	0.50	24%	21.1%
Denmark	0.02	0.02	19%	0.4%
Cyprus	0.01	0.01	18%	0.6%
Lithuania	0.67	0.76	13%	21.2%
Greece	2.63	2.76	5%	12.2%
Belgium	0.05	0.06	3%	0.5%
Poland	3.87	3.99	3%	9.1%
Croatia	n/a	0.17	n/a	2.5%
UK	1.06	1.06	(1)%	2.5%
France	1.08	1.03	(5)%	1.6%
Malta	0.04	0.04	(5)%	7.7%
Italy	1.84	1.30	(30)%	1.7%
Netherlands	0.12	0.06	(48)%	0.5%
Austria	0.09	0.04	(59)%	0.3%
Portugal	0.13	0.05	(60)%	0.5%
Luxembourg	0.01	0.00	(100)%	0.0%
Total	17.11	19.61	15%	

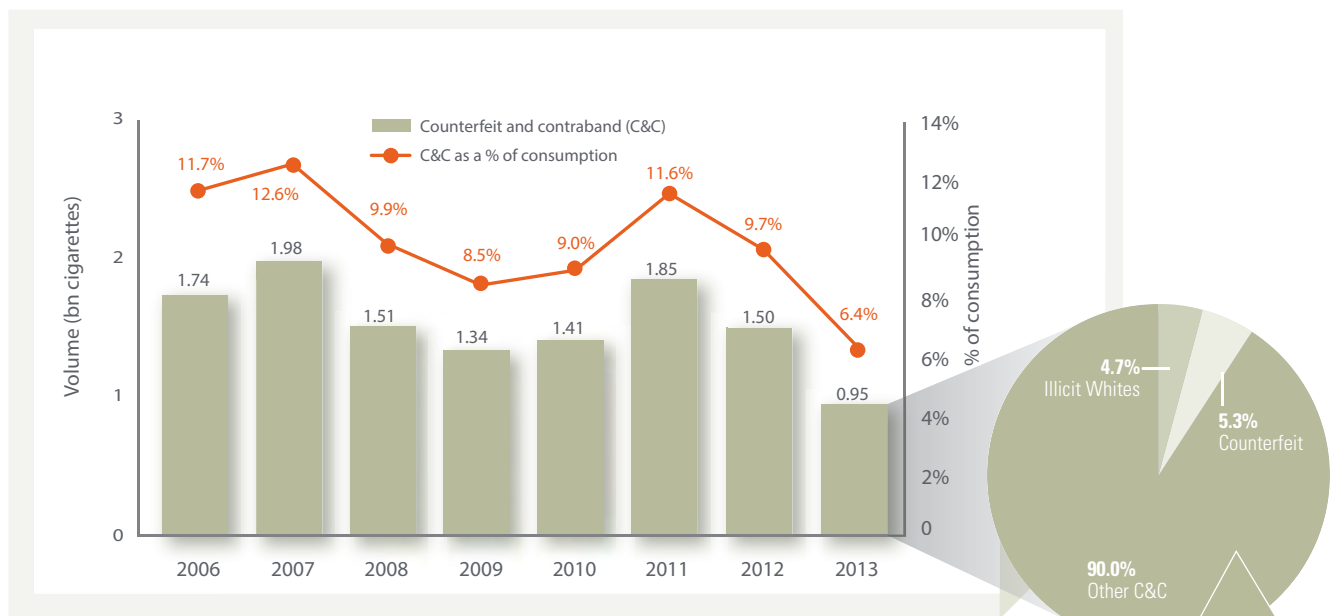


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Consumption declined, driven by decline of the Counterfeit and Contraband volumes

Manufactured cigarette C&C volumes and share of overall consumption 2006-13

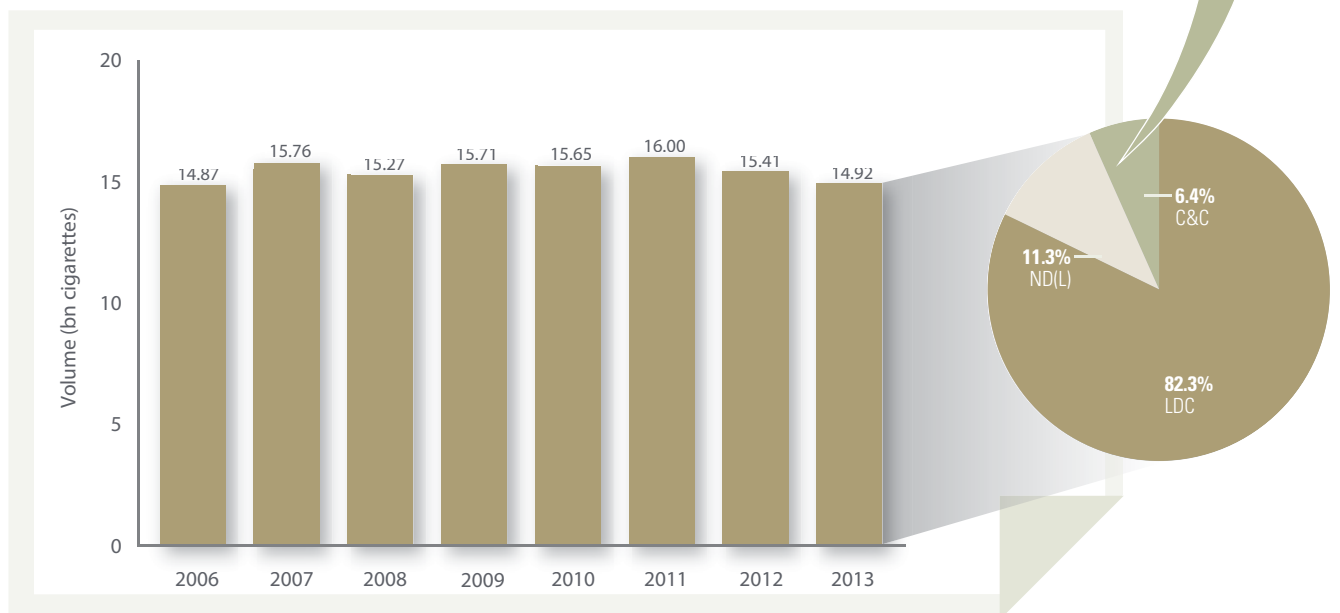


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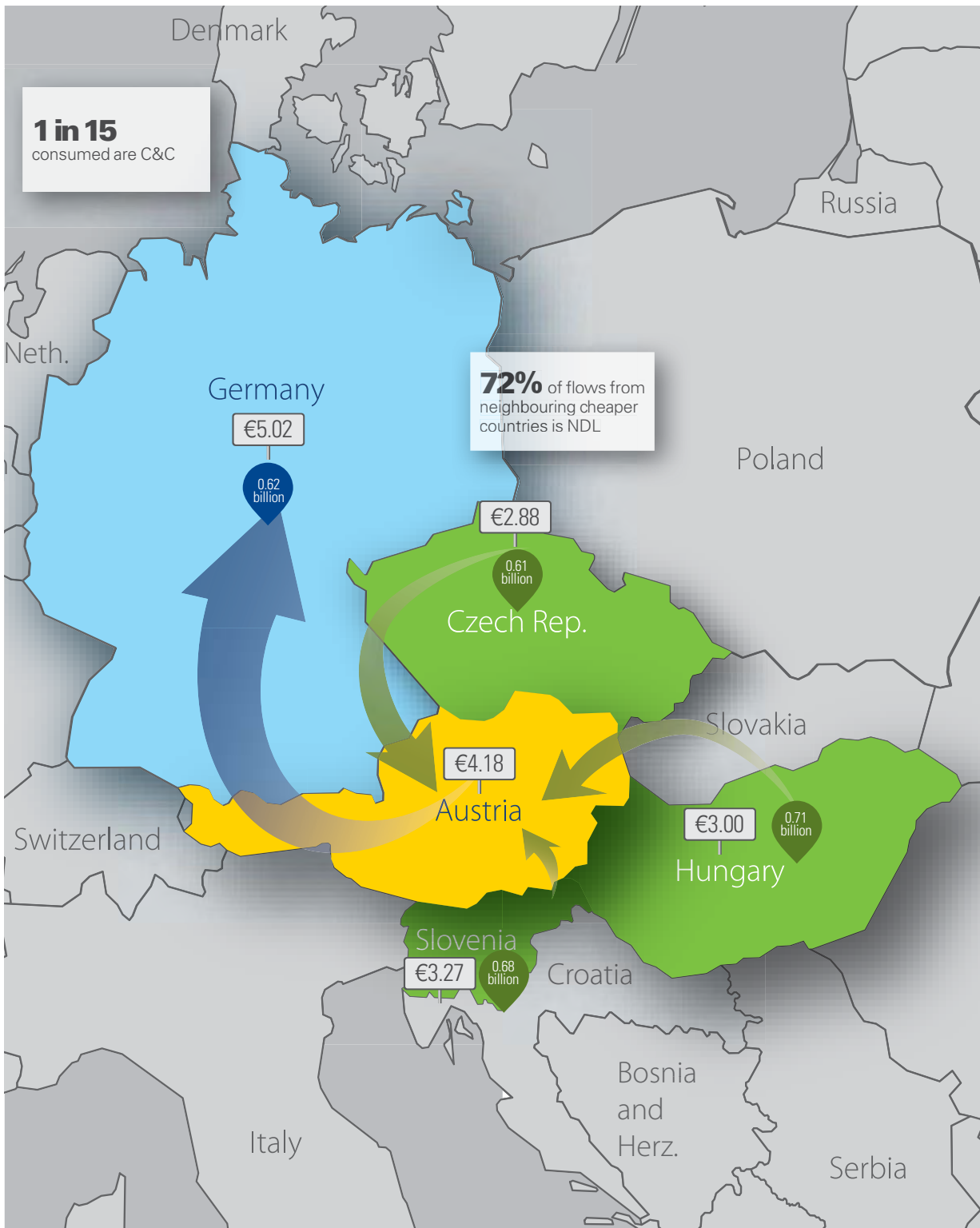


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Manufactured cigarette consumption 2006-13





KEY INFLOWS AND OUTFLOWS



AUSTRIA

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Main outflow 
Main inflow 

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

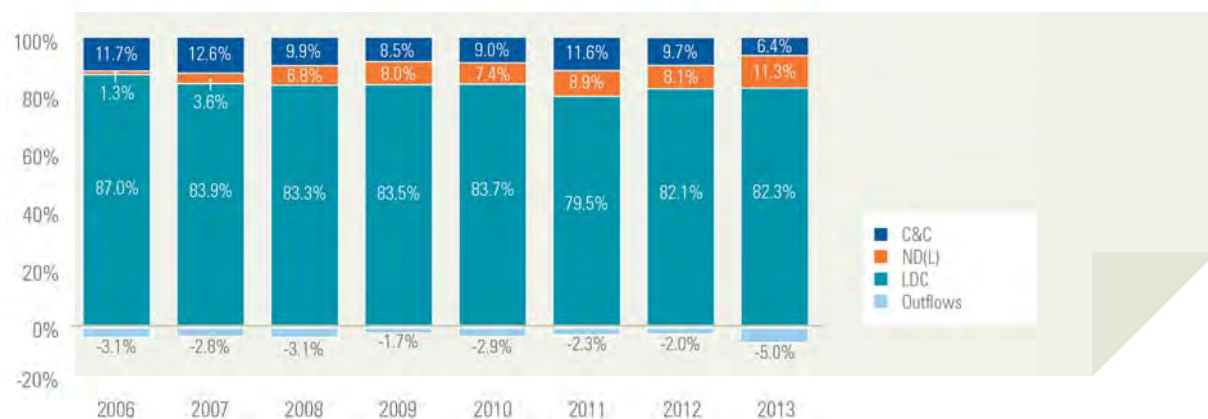
MANUFACTURED CIGARETTE CONSUMPTION

Cigarette consumption in Austria declined in 2013, reflected equally by falls in both domestic and non-domestic consumption

Total manufactured cigarette consumption – Austria⁽¹⁾⁽²⁾

TOTAL AUSTRIA CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	13.40	13.66	13.20	13.39	13.54	13.09	12.96	13.04	1%
Outflows	-0.46	-0.45	-0.48	-0.27	-0.45	-0.36	-0.31	-0.75	>100%
Legal domestic consumption (LDC)	12.94	13.22	12.72	13.12	13.09	12.72	12.65	12.29	(3)%
Non-domestic legal (ND(L))	0.20	0.56	1.04	1.25	1.15	1.43	1.25	1.69	35%
Counterfeit and contraband (C&C)	1.74	1.98	1.51	1.34	1.41	1.85	1.50	0.95	(37)%
Total non-domestic	1.94	2.54	2.55	2.59	2.56	3.28	2.76	2.64	(4)%
Total consumption	14.87	15.76	15.27	15.71	15.65	16.00	15.41	14.92	(3)%

Share of Austria manufactured cigarette consumption by type⁽¹⁾⁽²⁾ - 2006-2013



Total consumption of manufactured cigarettes declined by 3% even in the context of an increase in legal domestic sales (LDS) of 1%

- LDS volumes may have increased slightly due to a larger outflow from Austria to Germany. If the outflow had stayed at a similar level to prior year, legal domestic sales would have fallen at the same pace as overall consumption
- Consumption is unlikely to have been significantly impacted by the economy as Austria experienced strong economic conditions in 2013 compared to other EU countries, with positive growth of personal disposable income and GDP per capita, and with comparatively low levels of unemployment⁽³⁾

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Personal disposable income data from Euromonitor (downloaded March 2013), Unemployment data from Statistik Austria.

Hungary and Slovenia remained the largest non-domestic source countries, though volumes declined following price rises in both countries

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWSTO AUSTRIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Hungary	0.13	0.32	0.45	0.48	0.48	0.99	0.86	0.71	(17)%
Slovenia	0.23	0.53	0.73	0.79	0.85	1.04	0.83	0.68	(18)%
Czech Republic	0.17	0.16	0.20	0.23	0.25	0.47	0.41	0.61	49%
Serbia	0.07	0.05	0.06	0.08	0.10	0.08	0.14	0.10	(32)%
Counterfeit								0.05	n/a
Other	1.34	1.48	1.12	1.01	0.88	0.70	0.51	0.48	(6)%
Total inflows	1.94	2.54	2.55	2.59	2.56	3.28	2.76	2.64	(4)%

The largest inflows into Austria came from Hungary and Slovenia, however the significant decline in volumes from both countries may be the result of the decreasing price differentials

- Whilst the weighted average price in Austria increased by 8%, prices rose in Hungary by 13% and in Slovenia by almost 11%. In 2013, this resulted in the price differential reducing from €1.29 to €1.14 for Hungary and €1.00 to €0.91 for Slovenia
- The price rises may explain the 17% decline in flows from Hungary and 18% decline from Slovenia as changes in the price differential impact the average number of packs that consumers are likely to purchase

Total outflows by destination country – 2006-2013⁽¹⁾

OUTFLOWS FROM AUSTRIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Germany	0.23	0.17	0.20	0.18	0.33	0.28	0.18	0.62	>100%
Netherlands	0.03	0.03	0.07	0.00	0.05	0.02	0.03	0.03	3%

Outflows from Austria more than doubled due to an increase in flows to Germany

- Austria has historically been a lower priced market compared to Germany and outflows have been stable. This year the weighted average price difference between Germany and Austria remained stable, although the average price of a pack of cigarettes in Germany rose above €5 for the first time, potentially making cross border purchases from Austria more likely

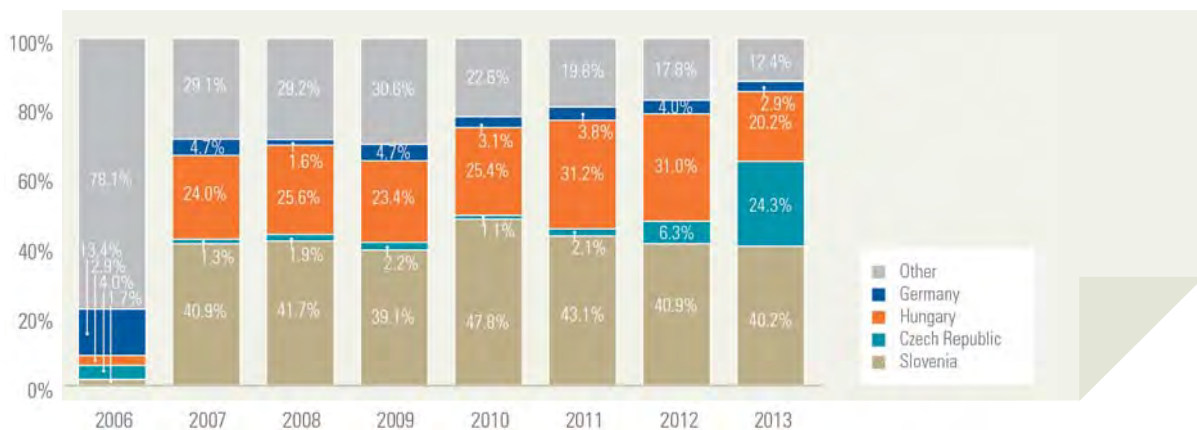
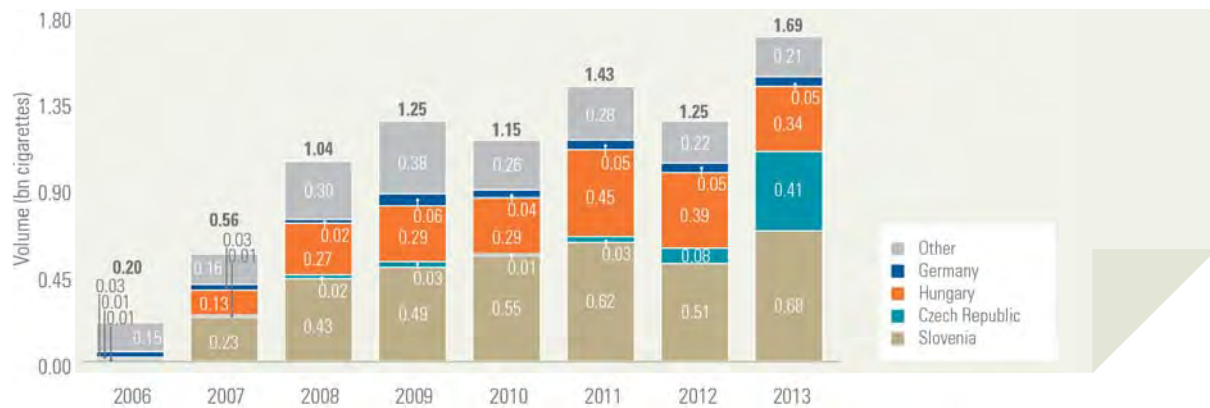
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition

Sources: (1) KPMG EU Flows Model.



Slovenia was the main source of ND(L) with flows increasing significantly from the Czech Republic

ND(L) by origin - 2006-2013^{(1)(2)(3)(a)(b)}



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As price differences between Austria and its surrounding countries have fallen, the proportion of ND(L) inflows compared with counterfeit and contraband has increased

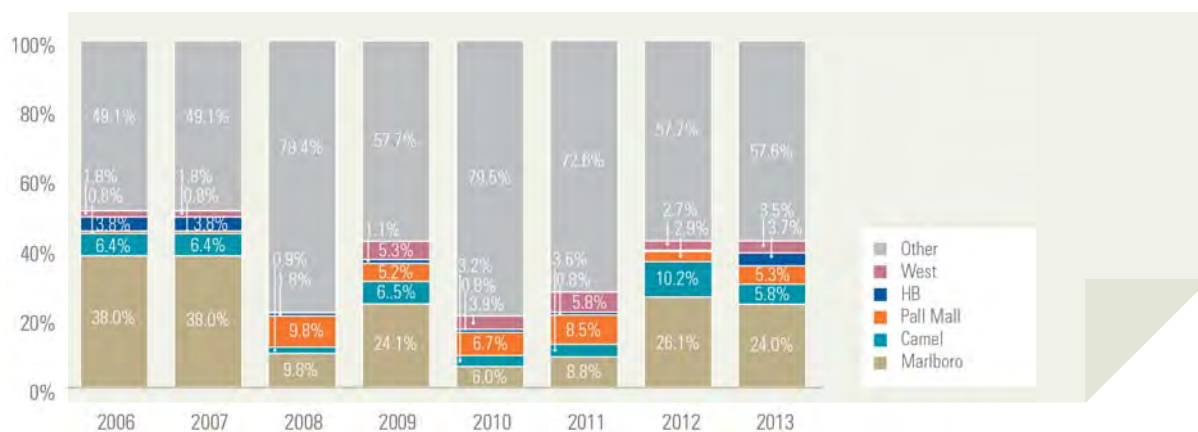
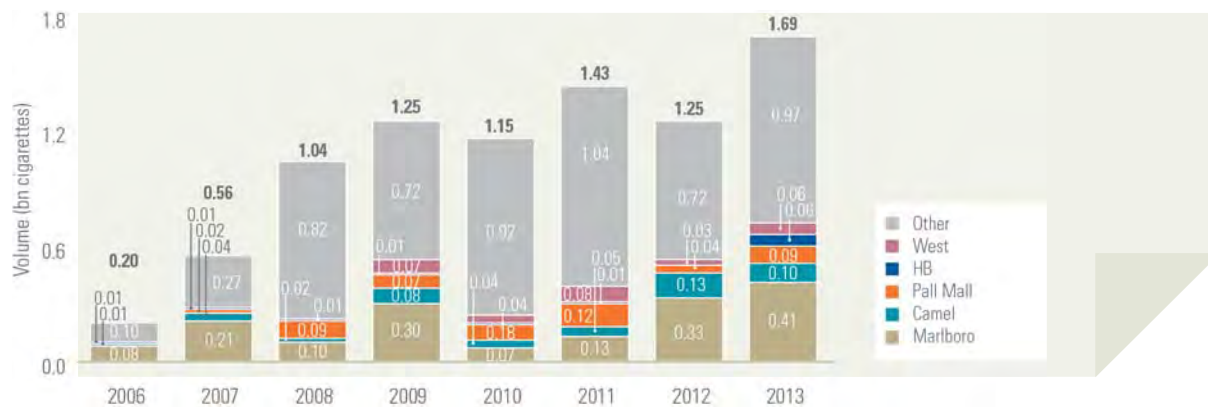
- In 2013 the price difference between Austria and Slovenia fell to €0.91, reducing incentive for smuggling and re-sale⁽⁴⁾
- In the same period, tourist flows from Austria to Slovenia increased by 8%; both the price difference and the high number of tourists supported 100% of the flow from Slovenia to Austria classed as being legal
- For Hungary there was a 4% increase in tourist flows in 2013, however a 12% decrease in the price difference to €1.14 suggests it is unlikely that so many Austrians would travel to Hungary to purchase cigarettes; 48% of these flows were classed as legal
- Consumers do however appear to be purchasing more cigarettes in the Czech Republic where prices rose more slowly in 2013
 - In addition, more favourable exchange rates between the Euro and the Czech Koruna have made shopping visits to the Czech Republic more attractive

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers. (4) KPMG analysis of EU Tax tables to see price increases.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

Total ND(L) by brand - 2006-2013^{(1)(2)(3)(a)}



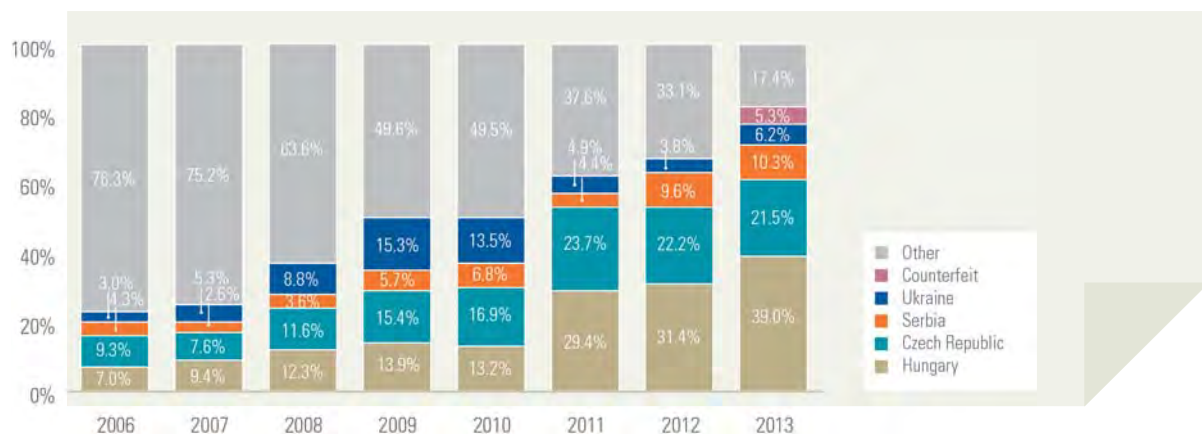
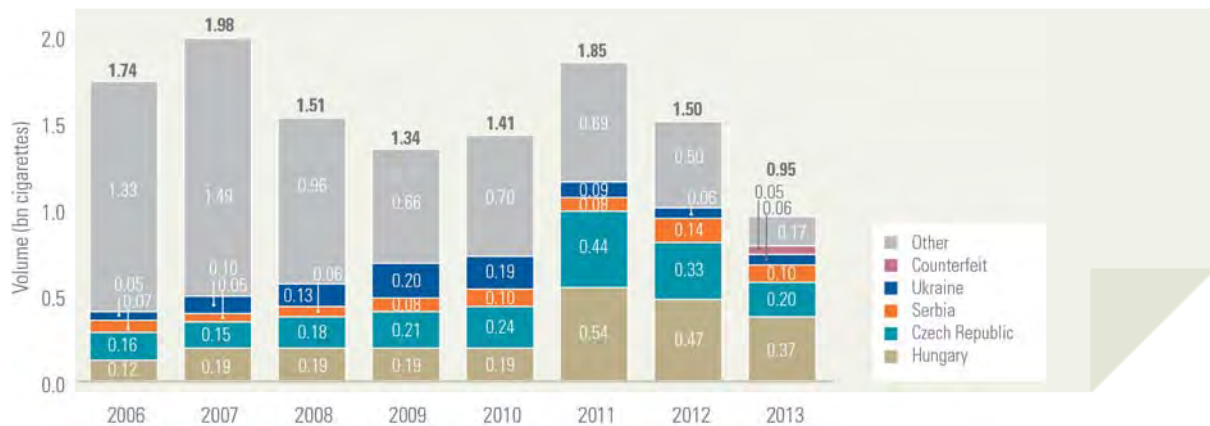
The composition of the most popular ND(L) brands remained fairly consistent, with Marlboro continuing to be the most popular brand purchased abroad

- A large proportion of the Marlboro flow was from Slovenia where all of the flow was legal
- All flows of West and Pall Mall were also classed as legal

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.
Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

C&C flows from Austria's surrounding countries fell significantly

Total C&C by origin - 2006-2013^{(1)(2)(3)(a)(b)}



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The majority of C&C flows still come from the neighbouring countries of Hungary and the Czech Republic

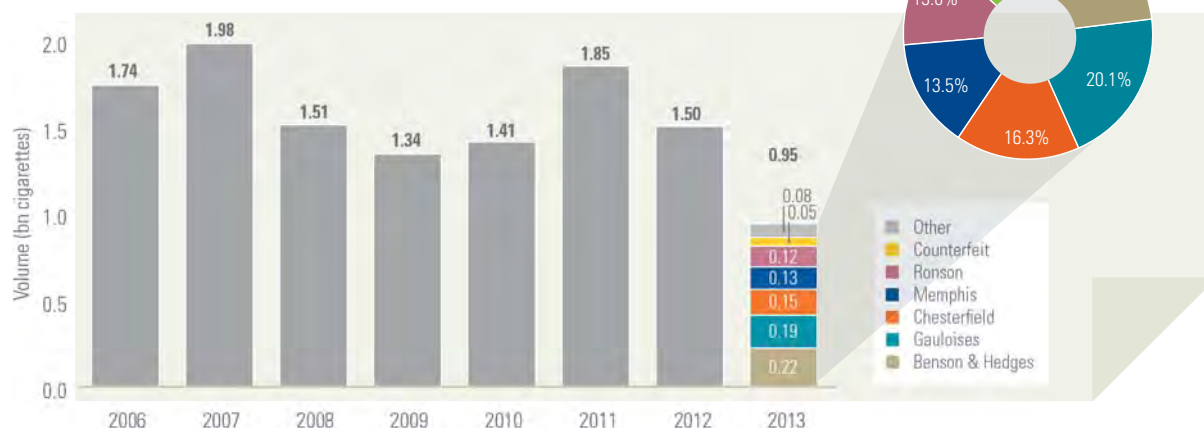
- The lack of one single source country indicates that the majority of C&C into Austria comes in the form of informal bootlegging rather than one specific source or brand
- If the total volume of C&C had been consumed legally within the Austrian market, an additional tax revenue of approximately €146 million would have been raised by the Austrian Treasury

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

C&C INFLOWS BY BRAND

Total C&C by brand - 2006-2013^{(1)(2)(3)(a)(b)}



Composition of Illicit Whites inflows - 2006-2013^{(1)(3)(b)}

LABELLING OF ILLICITWHITES INFLOWS TO AUSTRIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country Specific	0.038	0.014	0.049	0.093	0.150	0.096	0.041	(58)%
Duty Free	0.000	0.001	0.001	0.003	0.000	0.002	0.002	12%
Unspecified	0.000	0.000	0.000	0.000	0.000	0.000	0.002	n/a
Total Illicit Whites	0.038	0.015	0.050	0.095	0.151	0.098	0.044	(55)%

Illicit Whites made up 4% of overall duty free flows

The largest contraband brands were those that came from surrounding countries

- The largest contraband brand was Benson & Hedges which mainly came from the Czech Republic
- Illicit Whites make up less than 10% of the overall C&C volume, one of the lowest in Europe

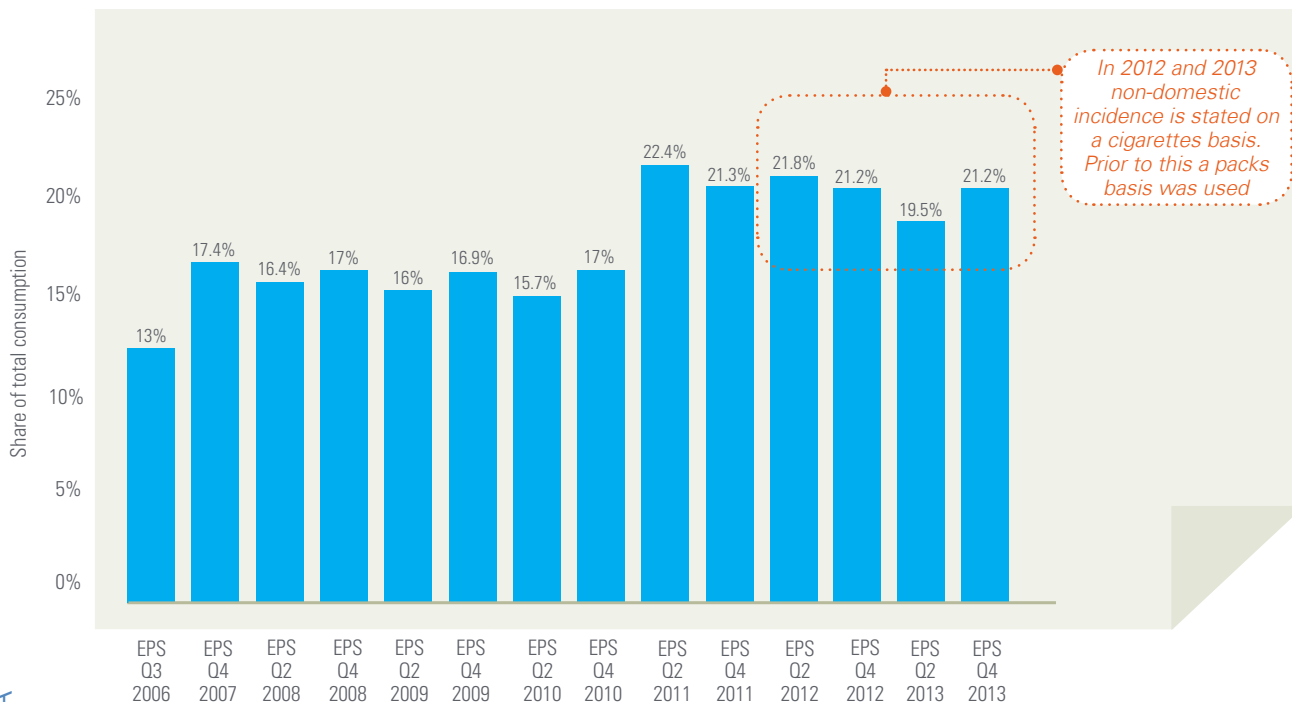
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.

(3) KPMG analysis of data sources provided by manufacturers.

EPS non domestic estimates

Empty Pack Survey non-domestic market estimates - 2006-2013^{(1)(a)}



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- The empty pack survey in Austria is run in two separate quarters and conducted by the National Manufacturer’s Association in Austria. The survey collects over 25,000 packs during the course of the year
- The packs are collected in 621 different locations, sampling both rural and urban population centres
- An adjustment to the weighting of the packs was made in order to reduce the impact of the extra samples collected in areas with high levels of non-domestic incidence
 - Kärnten was the most over-sampled region, and had the highest level of non-domestic incidence; where over three times as many packs were collected compared with the population
 - The adjustment results in the KPMG estimate of non-domestic incidence being 2.2 percentage points below EPS results

Note: (a) The EPS results are conducted before.

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers.

Non-domestic legal volume calculations and explanations

KPMG non domestic legal flows Austria

COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 ⁽¹⁾ (bn sticks)	2013 ND(L) (bn sticks)	% of ND
Slovenia	0.68	0.68	100%

USE OF CONSUMER RESEARCH AND ANY ADJUSTMENTS FOR 2013 DATA							
Country	ND 2013 ⁽¹⁾	Total trips where cigarettes purchased (m) ⁽²⁾⁽³⁾	Number of packs per trip ⁽³⁾⁽⁴⁾	Total packs (m)	Data sources ⁽²⁾⁽³⁾⁽⁴⁾	2013 ND(L) (bn sticks)	% of ND
Hungary	0.71	0.64m	20	99.4	UNWTO, WAP pricing tables	0.34	48%
Czech Republic	0.61	0.9m	22	10.75	UNWTO, WAP pricing tables	0.41	67%

- Total flows from Slovenia are classed as 100% legal as the price difference is less than €1 per packet
- Given the low price difference between Austria and Hungary and the Czech Republic respectively, it is assumed that many of these flows are local border sales. Therefore consumer research is used to calculate the number of trips made by each purchaser and number of packs bought from each country, whilst the local population in the border areas and smoking prevalence is used to calculate the total number of purchasers
- The volume of non-domestic incidence is calculated by assuming that smokers in the states bordering Hungary and the Czech Republic make two trips over the border to purchase cigarettes each year (as stated in the consumer research). It is also assumed that the number of packs purchased from each country is the same as recorded in the consumer research on each trip; 20 for Hungary and 22 for Czech Republic
- This results in assuming that all smokers in Steiermark and Burgenland (a total of 428,000) travel to Hungary twice a year and that all smokers in Niederösterreich travel to the Czech Republic twice a year.

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

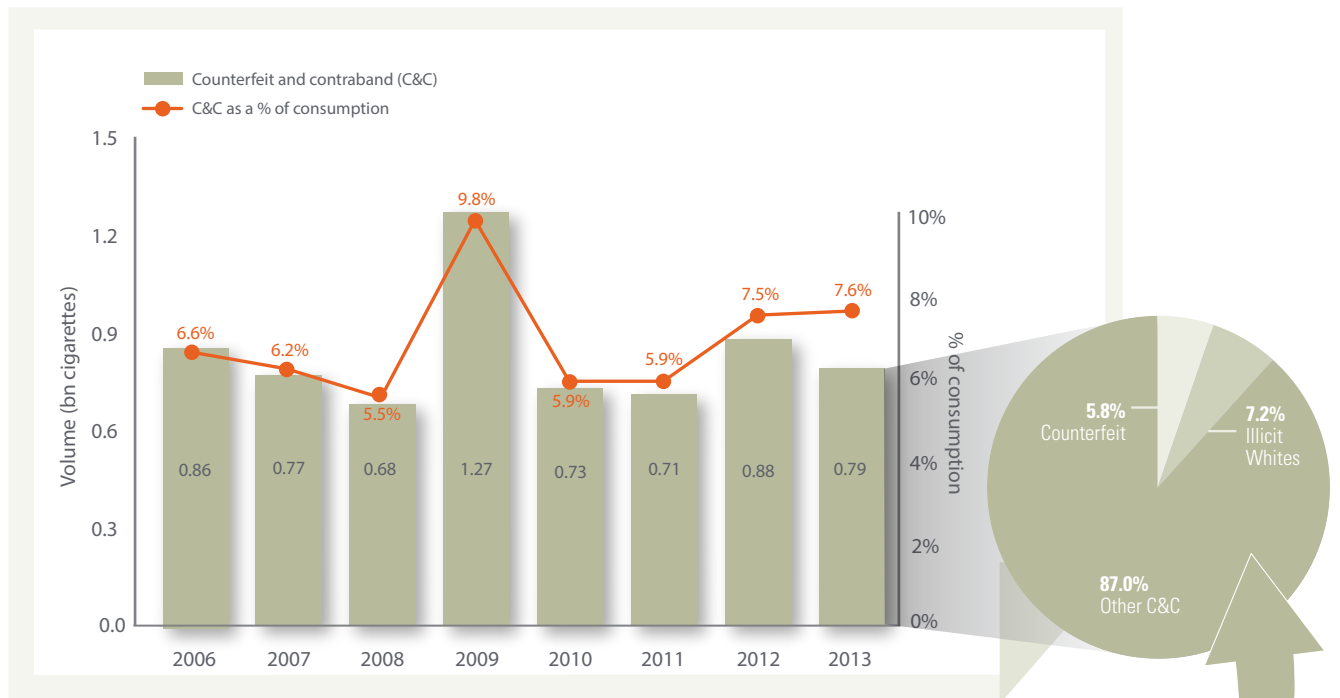
Sources: (1) KPMG EU Flows Model. (2) Synovate/Ipsos ND(L) research 2013. (3) UN WTO Tourism Factbook 2008-2012, UN WTO. (4) EC Excise Duty tables (Part III – Manufactured Tobacco).

BELGIUM



Counterfeit and contraband represents a smaller share of total consumption than non-domestic legal flows; other C&C is the largest part of this

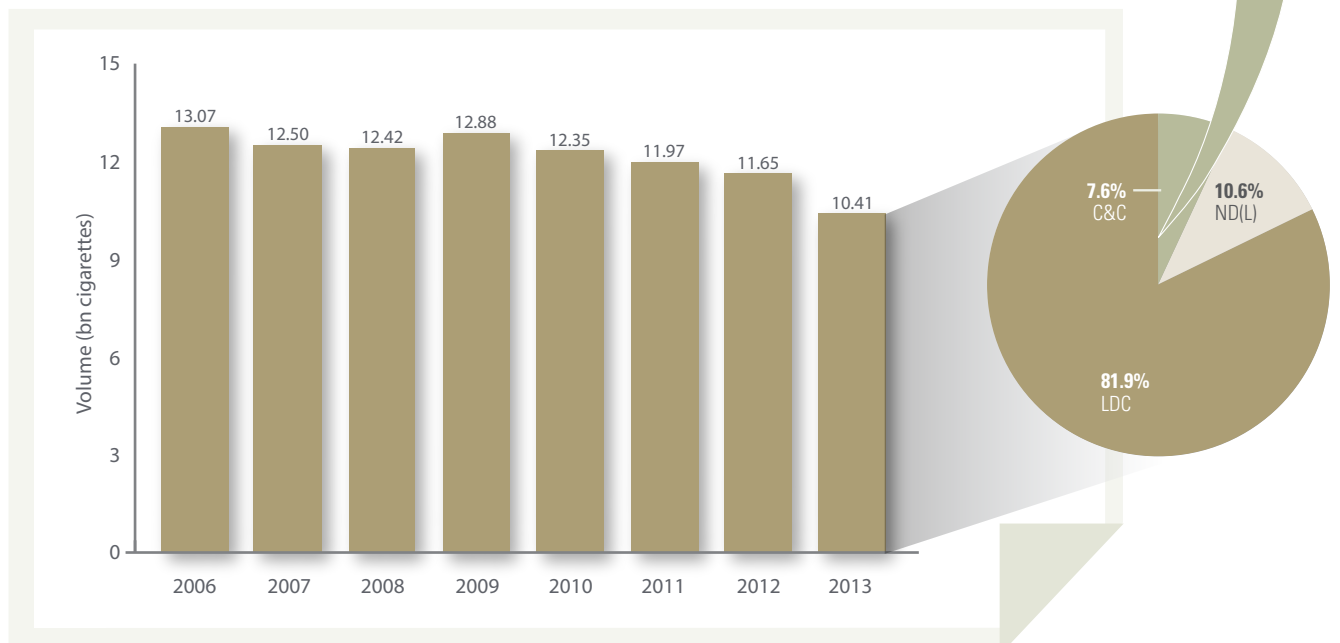
Manufactured cigarette C&C volumes and share of overall consumption 2006-13



BELGIUM

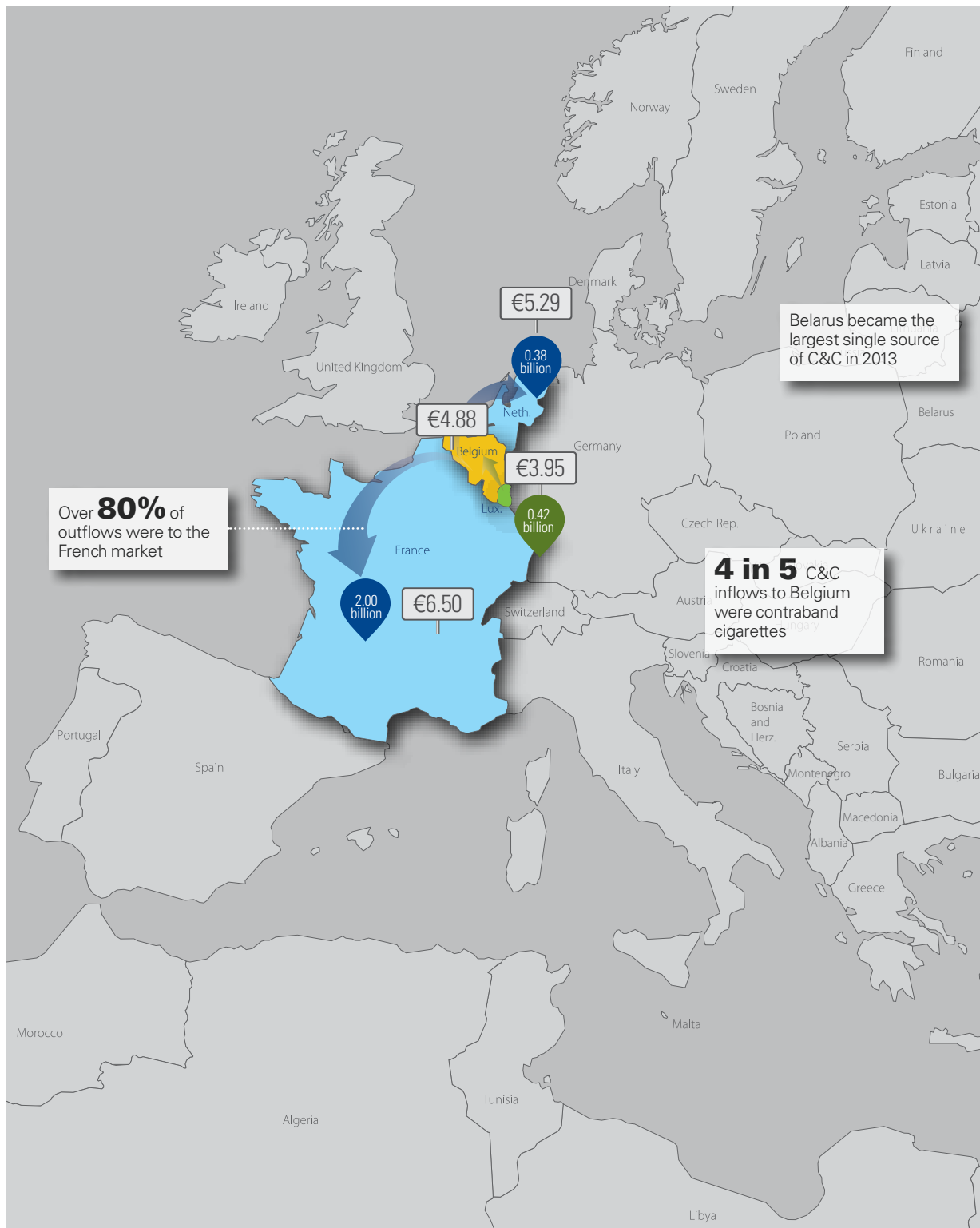


Manufactured cigarette consumption 2006-13



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KEY INFLOWS AND OUTFLOWS





Over **80%** of outflows were to the French market

4 in 5 C&C inflows to Belgium were contraband cigarettes

BELGIUM

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Main outflow 
Main inflow 

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

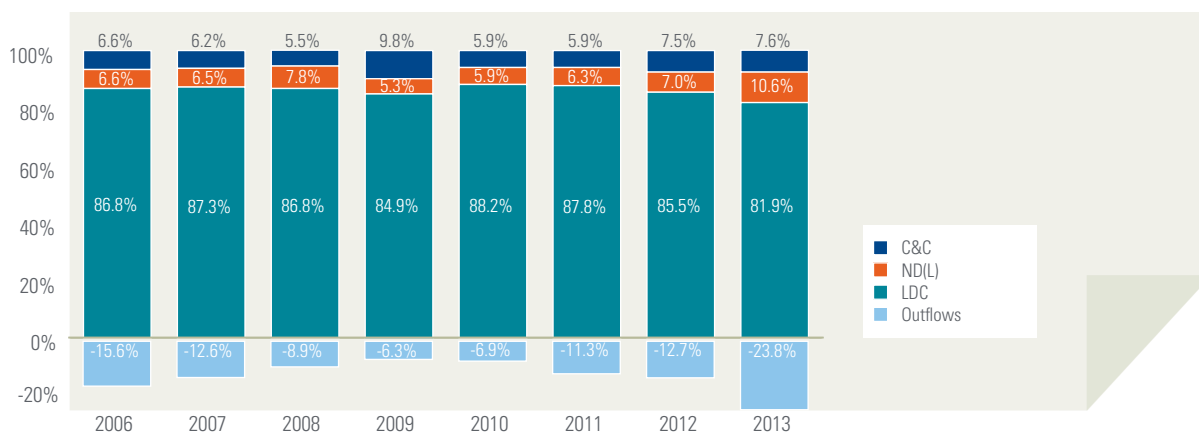
MANUFACTURED CIGARETTE CONSUMPTION

Overall consumption declined, reflected in lower legal domestic consumption, partially offset by an increase in non-domestic inflows

Total manufactured cigarette consumption - Belgium^{(1)(2)(a)}

TOTAL BELGIUM CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	13.39	12.49	11.89	11.74	11.73	11.86	11.44	11.00	(4)%
Outflows	-2.04	-1.58	-1.10	-0.81	-0.85	-1.35	-1.48	-2.48	68%
Legal domestic consumption (LDC)	11.35	10.92	10.78	10.93	10.89	10.50	9.96	8.52	(14)%
Non-domestic legal (ND(L))	0.86	0.81	0.96	0.68	0.73	0.76	0.81	1.10	35%
Counterfeit and contraband (C&C)	0.86	0.77	0.68	1.27	0.73	0.71	0.88	0.79	(10)%
Total non-domestic	1.73	1.58	1.64	1.95	1.46	1.46	1.69	1.89	12%
Total consumption	13.07	12.50	12.42	12.88	12.35	11.97	11.65	10.41	(11)%

Share of Belgium cigarette consumption by type - 2006-2013⁽¹⁾⁽²⁾



Overall consumption of manufactured cigarettes in Belgium fell 10.6% in the year. This follows a declining trend from 2010, however the decline in 2013 was greater

- Continued economic difficulties are likely to have depressed legal domestic sales, which fell 3.8% this year. Unemployment has risen from 7.6% to 8.4%⁽³⁾, however there have been marginal increases in both GDP per capita and PDI⁽⁴⁾
- WAP however has remained relatively stable, increasing only 2.3% in the year from €4.67 per pack of 20 cigarettes to €4.77⁽⁶⁾
- Legal sales volumes of fine cut tobacco have continued to increase in recent years⁽⁵⁾, which suggests that some consumers are switching from manufactured cigarettes to OTP, which are considerably cheaper

Notes: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) 2014 Economist Intelligence Unit. (4) Euromonitor, downloaded January 2014. (5) European Commission releases for consumption of fine cut tobacco, 2002-2012. (6) EC Excise Duty tables (Part III – Manufactured Tobacco).

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Belgium became a net outflow country to the EU in 2013, largely due to greater outflows to France

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWSTO BELGIUM									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Luxembourg	0.47	0.25	0.31	0.12	0.23	0.47	0.51	0.42	(18)%
France	0.07	0.15	0.03	0.16	0.07	0.06	0.09	0.29	>100%
Duty Free	0.45	0.21	0.47	0.37	0.27	0.18	0.20	0.22	8%
Netherlands	0.09	0.05	0.02	0.11	0.13	0.06	0.04	0.17	>100%
Belarus	0.00	0.00	0.00	0.01	0.03	0.04	0.11	0.09	(18)%
Counterfeit								0.05	n/a
Other	0.65	0.92	0.82	1.17	0.73	0.66	0.73	0.65	(11)%
Total inflows	1.73	1.58	1.64	1.95	1.46	1.46	1.69	1.89	12%

Inflow volumes have grown in 2013 and represent a greater share of total consumption

- Greater inflows are largely the result of French and Dutch origin cigarettes picked up during the Empty Pack Survey (EPS). Due to the wide distribution of these packs throughout Belgium, this is likely to be due to general travel patterns to these nearby markets
- These flows offset the decline from Luxembourg. This may be because the 'basket' of goods from Luxembourg is not as cheap as the prior year, evidenced by lower diesel and petrol price differentials with Belgium and a higher rate of inflation in Luxembourg⁽²⁾⁽³⁾
- Other inflows include Poland (0.09bn), Russia (0.08bn), Germany (0.07bn) and Spain (0.05bn)
- Duty Free inflows increased marginally this year, however Illicit Whites with Duty Free labelling represent only 3.0% of Duty Free volumes. The main brands sold as an Illicit Whites appear to be Karelia and Yun Yan

Total outflows by destination country – 2006-2013⁽¹⁾

OUTFLOWS FROM BELGIUM									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
France	0.53	0.73	0.71	0.48	0.43	0.90	1.01	2.00	99%
Netherlands	0.54	0.73	0.13	0.15	0.24	0.29	0.32	0.38	18%
UK	0.36	0.00	0.14	0.09	0.04	0.08	0.08	0.04	(53)%
Other	0.59	0.12	0.13	0.09	0.15	0.08	0.08	0.06	(22)%
Total outflows	2.04	1.58	1.10	0.81	0.85	1.35	1.48	2.48	68%

Increased outflows are almost entirely due to greater flows into France

- The North-East regions of Nord-Picardie and Alsace-Lorraine-Champagne-Ardenne have seen particularly large increases. As a result of further excise increases in France, the price differential with Belgium increased 22%, from €1.33 to €1.62 per pack of 20 cigarettes⁽⁴⁾. The relatively low GDP per capita in North East France versus the country average may also be a contributing factor
- Outflows to the Netherlands have also increased marginally versus 2012. This is again likely to be driven by a rise in the price differential between the markets, up over 50% to €0.41 per 20 cigarettes⁽⁴⁾, and also the proximity of large Dutch cities to the Belgian border
- Prices in Belgium have tended to increase at a slower rate than the key bordering markets of France and the Netherlands, largely due to an unchanging excise tax environment. Cigarette taxation remained constant between 2009 and July 2012 and since then there has been a marginal reduction in the ad valorem %, offset by a small increase in the specific tax⁽⁴⁾

Notes: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

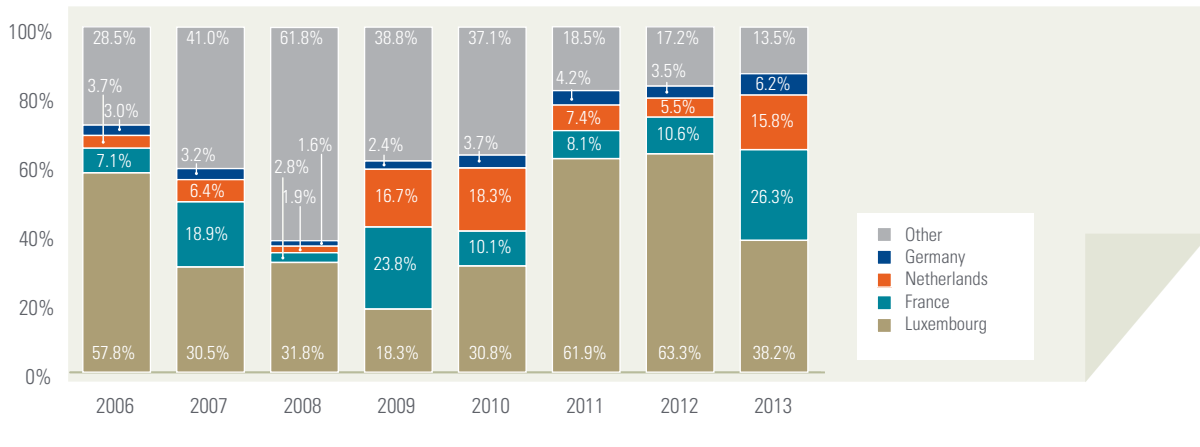
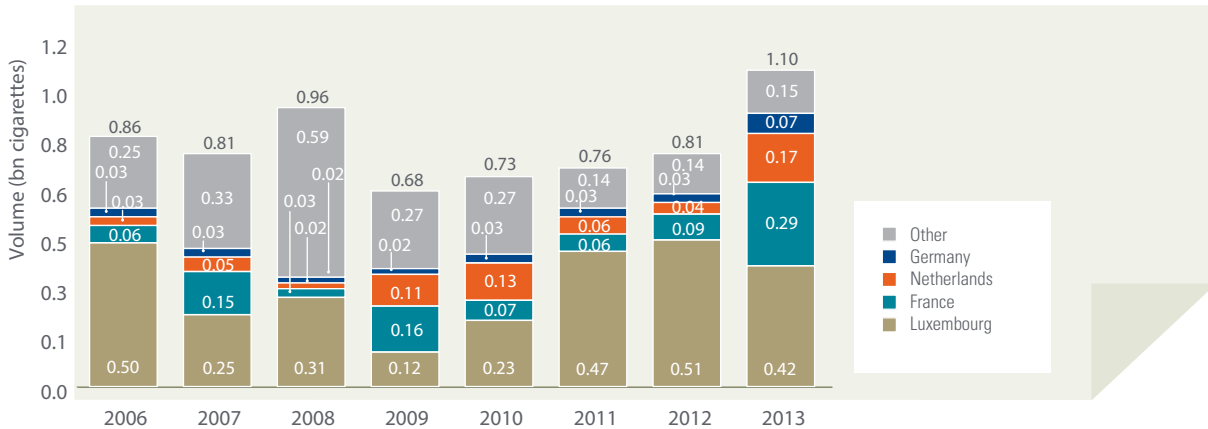
Sources: (1) KPMG EU Flows Model. (2) Euromonitor, downloaded April 2014. (3) Eurostat. (4) EC Excise Duty tables (Part III – Manufactured Tobacco).

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ND(L) inflows continued to increase

ND(L) by origin - 2006-2013^{(1)(2)(a)(b)}



BELGIUM



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Non-domestic ND(L) legal inflows of manufactured cigarettes have increased by 35.4% in 2013

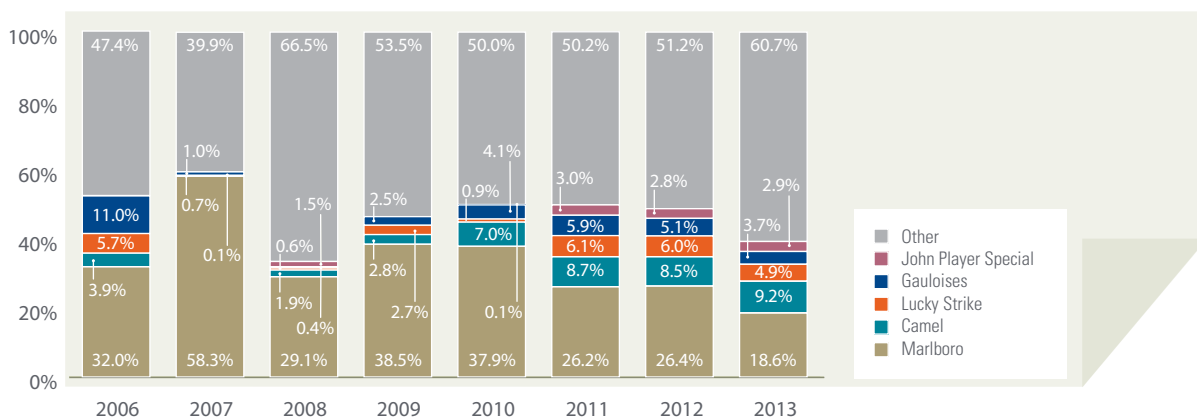
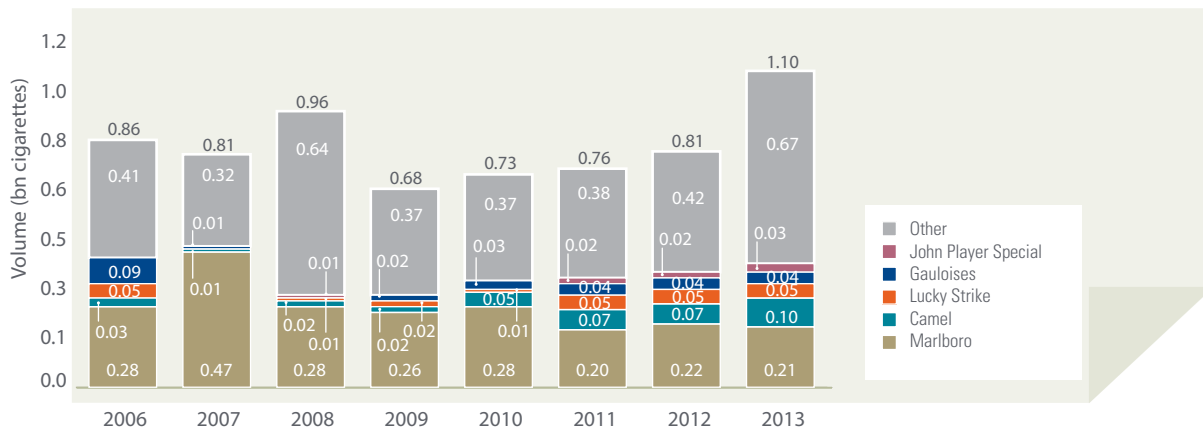
- ND(L) from Luxembourg declined by 18.3% in 2013, the only major decline. Although outbound tourism to Luxembourg was steady over this period⁽³⁾ and there was a marginal increase in commuter flows to 40,000 people, increases in fuel prices and inflation in general may have dissuaded smokers who traditionally travelled to Luxembourg to buy a 'bundle' of goods. The price differential per pack of 20 cigarettes stayed constant during the year at €0.94
- Incidence of French origin cigarettes increased from 0.09bn to 0.29bn. This was true in both larger Belgian cities (i.e. Antwerp) and in smaller towns sampled. As prices in France are above those in Belgium, all inflows from France are classed as ND(L). Inflows from the Netherlands also increased, which is likely for similar reasons to France

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-12, UN WTO.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013^{(1)(2)(a)}



The ND(L) brand share is largely driven by the change in volumes from the three largest inflow countries

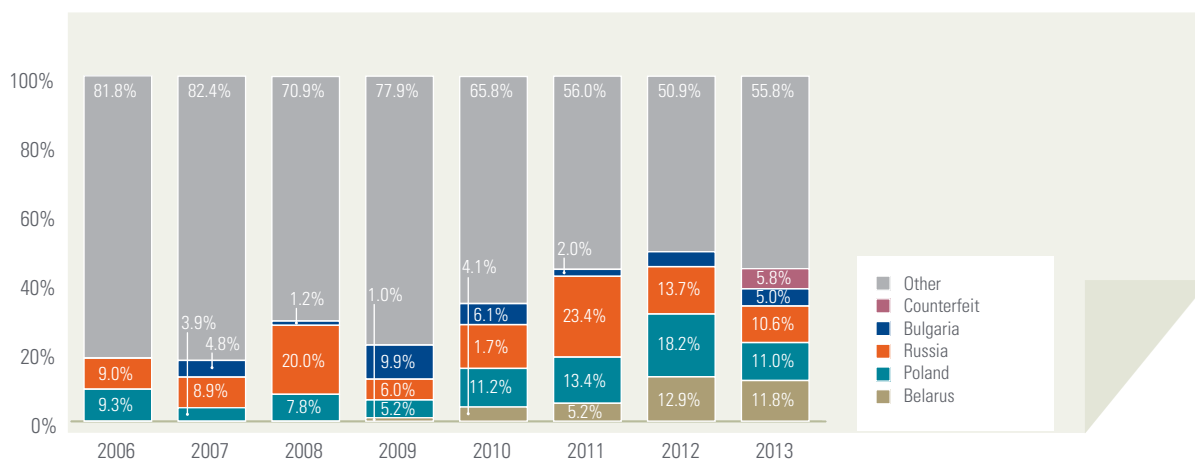
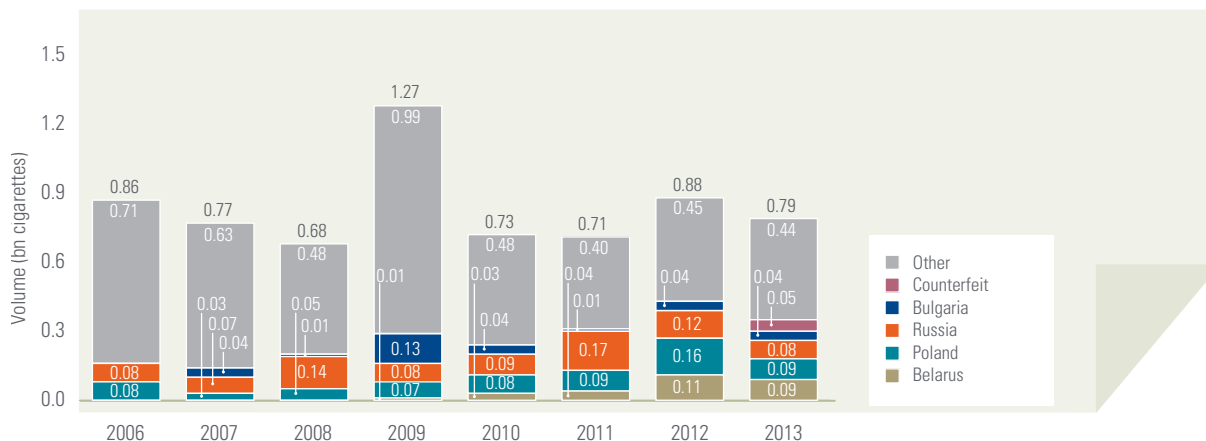
- The marginal decline in Marlboro arises due to the offsetting effects of greater French and Dutch inflows, but lower volumes from Luxembourg
- Due to oversampling of the Marlboro brand, a second methodology was used to determine inflow volumes, as explained on page 10
- Growth in non-domestic Camel largely resulted from greater French and Netherlands inflows, whilst volumes from Luxembourg fell
- Inflows of Gauloises also declined due to smaller inflows from Luxembourg
- "Other" inflows comprises smaller volumes of around 20 brands, such as L&M, Pall Mall and Chesterfield

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

C&C declined, driven by a decrease in Belarusian, Polish and Russian volumes

C&C by origin - 2006-2013^{(1)(2)(a)(b)}



Counterfeit and contraband (C&C) consumption represents a smaller share of consumption than ND(L) volumes in 2013 following a 10.4% decline

- The main flows of C&C arise from Eastern European markets where manufactured cigarette prices are significantly cheaper than domestic product
- Consumer research did not identify trips made to Belarus in the year and therefore inflows from Belarus are allocated to C&C
- Inflows from both Poland and Russia fell in 2013, which may have been driven by a €0.04 decline in the price differential with these markets⁽³⁾. There have also been declines in outbound tourism to Poland⁽⁴⁾
- “Other” C&C flows mainly represent other non-EU volumes (0.18bn), further Eastern European inflows (such as Romania) and some Duty Free flows
- Counterfeit cigarettes do not appear to be a significant issue in Belgium, making up only 5.8% of C&C volumes in 2013
- If these cigarettes had been legally purchased in Belgium, the tax revenue gained would have been approximately €145m

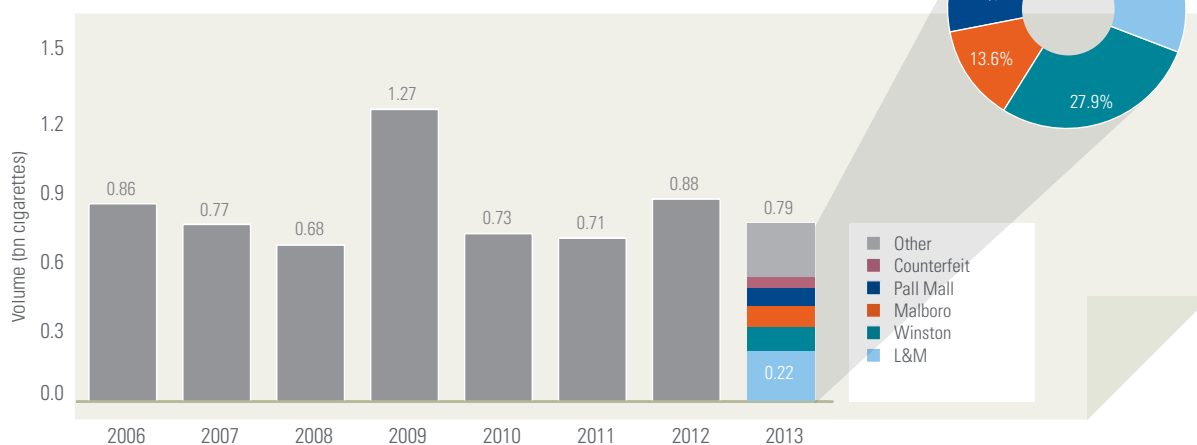
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Source: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) EC Excise Duty tables (Part III – Manufactured Tobacco). (4) UN WTO Tourism Factbook 2008-12, UN WTO.



C&C INFLOWS BY BRAND

C&C by brand - 2006-2013^{(1)(2)(a)}



Inflows of contraband cigarettes account for over four fifths of total C&C volumes

- The largest C&C brand is L&M, with inflows from Poland and Russia accounting for this. Winston is another brand with high C&C incidence; Belarus, Moldova, Russia and Ukraine drive these flows
- Marlboro C&C flows have a relatively high share, though inflows from Poland fell this year

Breakdown of Illicit Whites by type - 2007-2013^{(1)(2)(a)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO BELGIUM								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.00	0.00	0.00	0.00	0.06	0.05	0.04	(19)%
Duty Free	0.00	0.00	0.00	0.00	0.00	0.00	0.01	n/a
Unspecified	0.00	0.00	0.00	0.00	0.00	0.00	0.01	n/a
Total Illicit Whites	0.00	0.13	0.02	0.03	0.07	0.05	0.06	3%

- Illicit Whites represent 7.2% of total C&C inflows in 2013 and country Illicit Whites are the most common type. The main Illicit Whites brands appear to be Karelia, Austin and Ducal

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows

(b) A methodology and definition of Illicit Whites is provided in the methodology section.

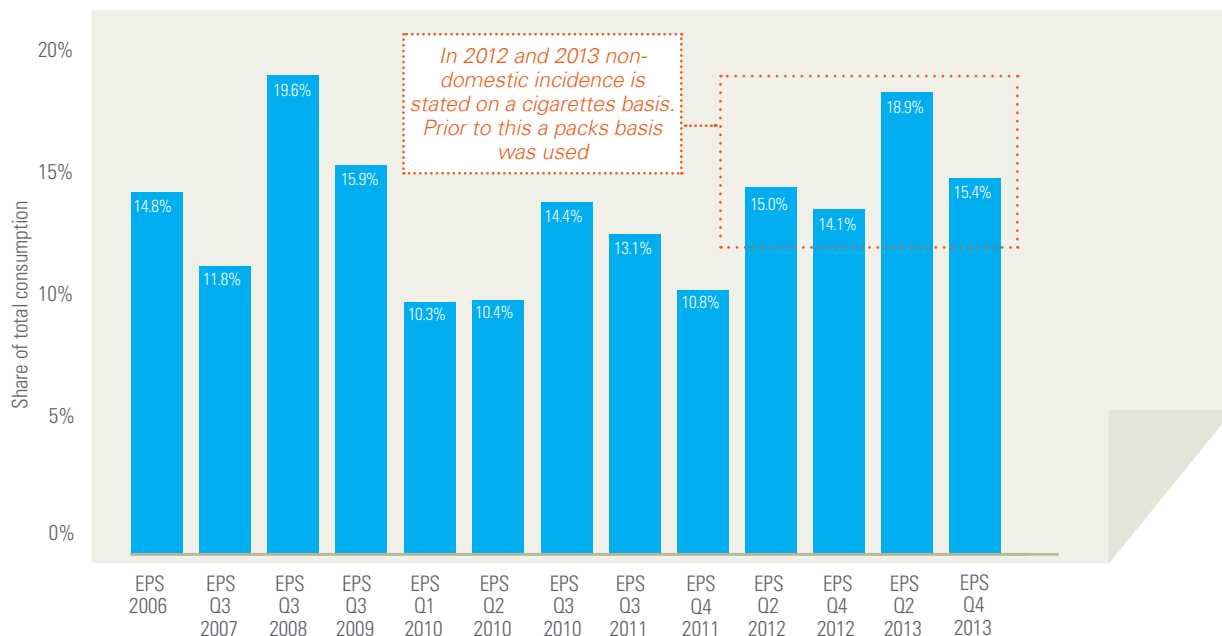
Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.

(3) KPMG analysis of data sources provided by manufacturers.



EPS results and EU Flows Model

Empty Pack Survey non-domestic estimates - 2006-2013⁽¹⁾



BELGIUM



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- The EPS in Belgium collected 5,600 packs during the course of the year. This was undertaken as two waves – one conducted in Q2 (April/May) and one in Q4 (October / November). Each wave collected 2,800 packs across the largest 18 towns and cities. The number of packs collected in each city is weighted by the city population
- Analysis of the EPS data highlighted that the region of Luxembourg (and the city of Arlon specifically) had been underrepresented in the sample. The regions were re-weighted to help ensure that the EPS share of each region aligned with the regional share of the country’s population. This had the effect of uplifting inflows from Luxembourg and overall ND incidence from 17.2% to 17.8%
- (Non-domestic) Marlboro packs appeared to be overstated in the EPS results when compared to Marlboro’s share of legal domestic sales in the country. A second methodology has therefore been used to model ND Marlboro which is more in line with ND(L) results and domestic brand share. The balance has been allocated to other brands. This is further explained in the methodology section of the appendices

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

ND(L) volume calculations and explanations

KPMG non domestic legal flows Belgium

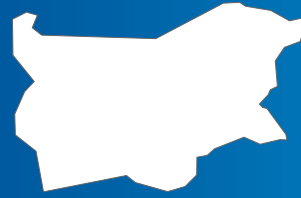
COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 (bn sticks) ⁽¹⁾	2013 ND(L) (bn sticks)	% of ND
Luxembourg	0.42	0.42	100%
France	0.29	0.29	100%
Netherlands	0.17	0.17	100%

- Owing to outbound travel of around 0.18m in the year (a relatively large volume considering the size and population of Luxembourg), 40,000 daily outbound commuters to Luxembourg and a number of large towns and cities in close proximity to the border (meaning significant border shopper and commuter flows), 100% of non-domestic inflows from Luxembourg have been classed as legal flows
- Based on higher prices for manufactured cigarettes in France and the Netherlands, inflows from these two markets have been classed as legal



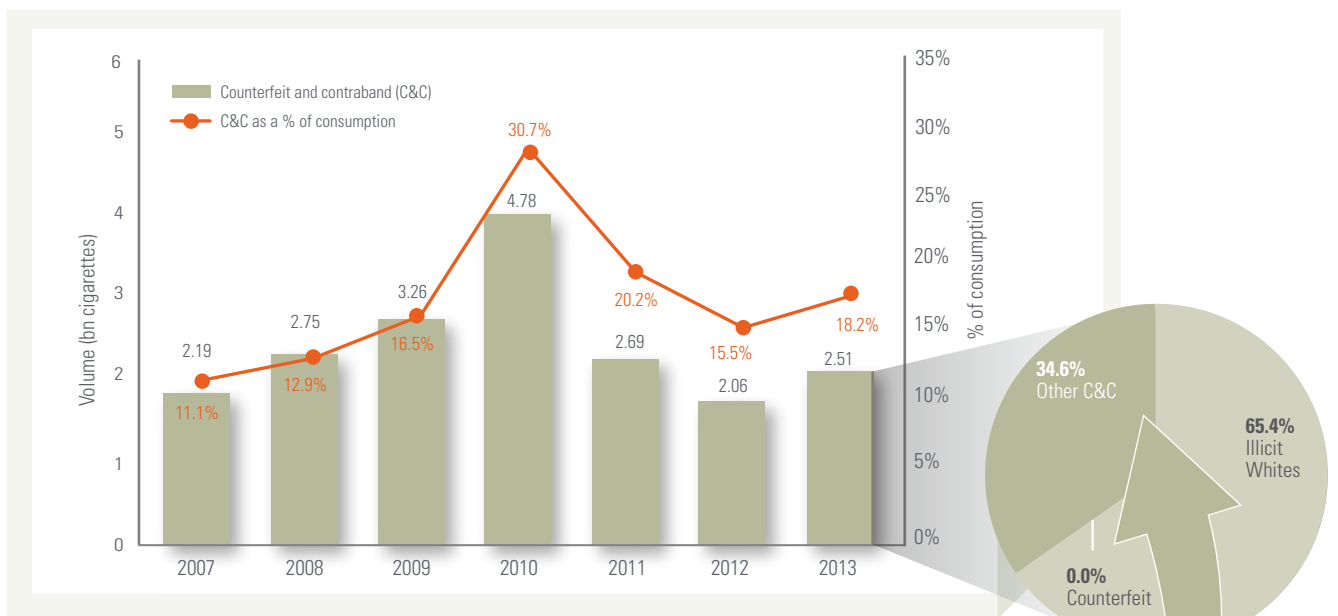
Sources: (1) KPMG EU Flows Model.

BULGARIA



Illicit Whites were the main driver for Counterfeit & Contraband increase

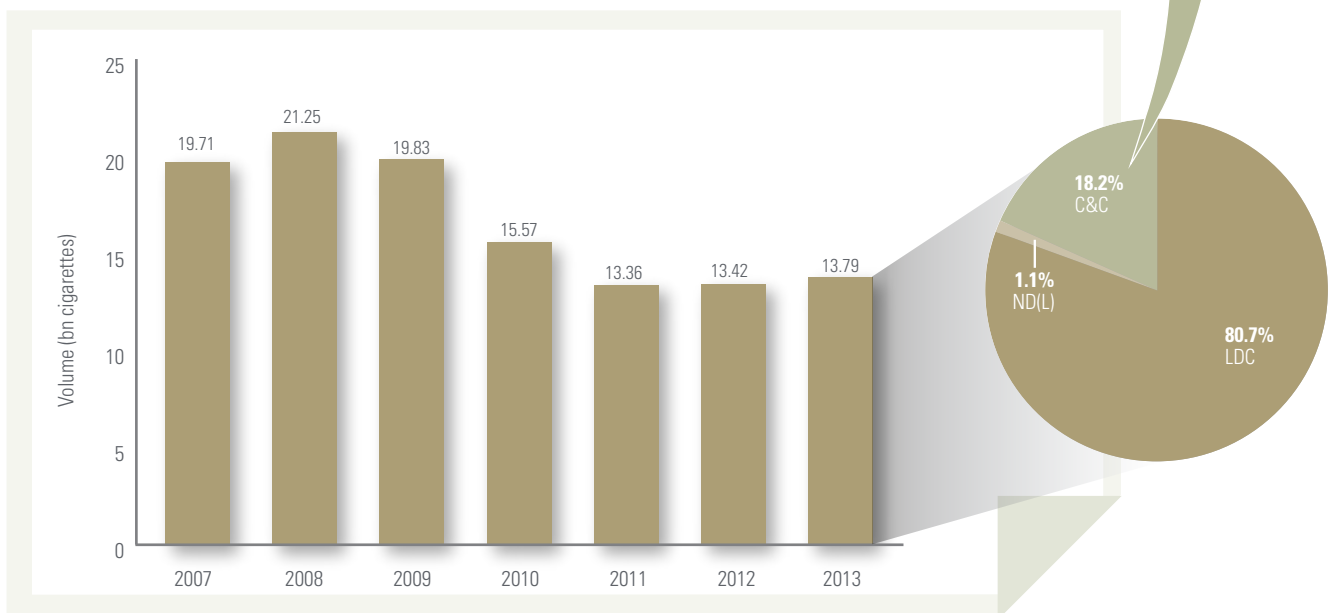
Manufactured cigarette C&C volumes and share of overall consumption 2007-13



BULGARIA

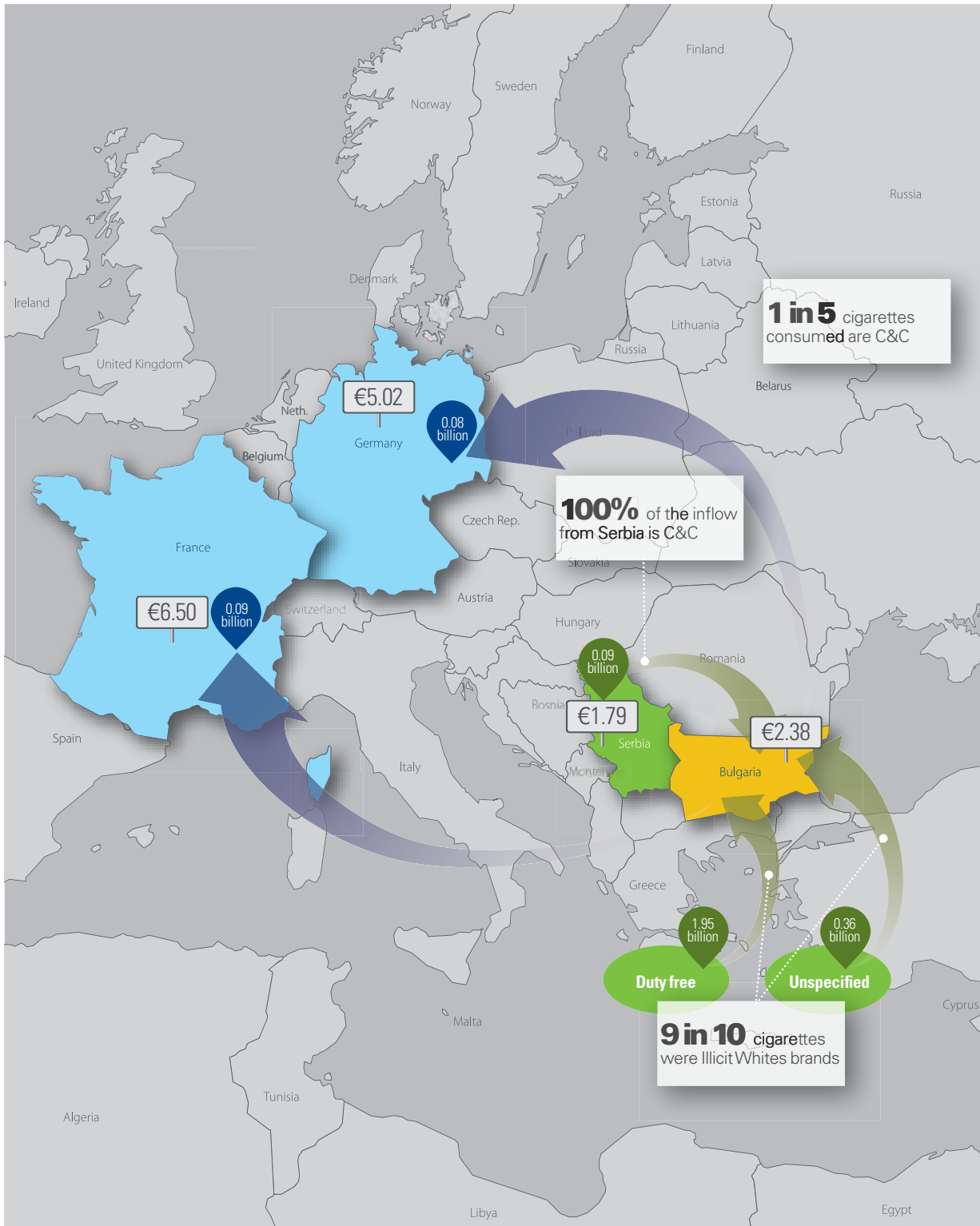


Manufactured cigarette consumption 2007-13



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KEY INFLOWS AND OUTFLOWS



BULGARIA



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Main outflow █
Main inflow █

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

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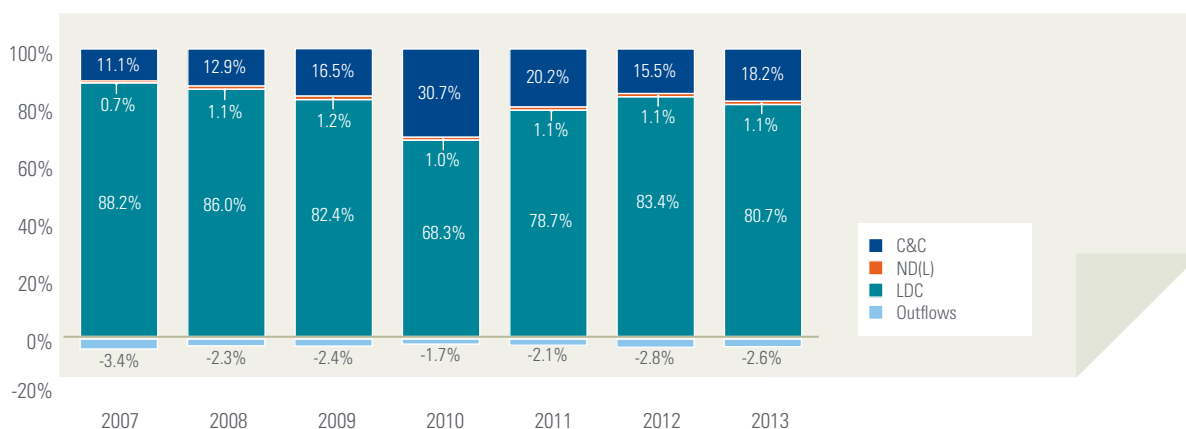
Total consumption grew slightly, with stable legal domestic sales and increased C&C

Total manufactured cigarette consumption - Bulgaria^{(1)(2)(3)(4)(a)}

Legal domestic sales as per Bulgarian Customs Agency data

TOTAL BULGARIA CONSUMPTION								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	18.06	18.77	16.80	10.91	10.80	11.57	11.50	(1)%
Outflows	-0.67	-0.49	-0.47	-0.27	-0.29	-0.38	-0.36	(5)%
Legal domestic consumption (LDC)	17.38	18.28	16.33	10.64	10.51	11.19	11.14	(0)%
Non-domestic legal (ND(L))	0.14	0.22	0.23	0.15	0.15	0.15	0.15	0%
Counterfeit and contraband (C&C)	2.19	2.75	3.26	4.78	2.69	2.08	2.51	21%
Total non-domestic	2.33	2.97	3.50	4.93	2.84	2.23	2.66	19%
Total consumption	19.71	21.25	19.83	15.57	13.36	13.42	13.79	3%

Share of Bulgaria cigarette consumption by type 2007-2013⁽¹⁾⁽²⁾⁽³⁾



Total manufactured cigarette consumption in Bulgaria rose by 3% in 2013, with greater levels of non-domestic product contributing to the increase

- Legal domestic sales (LDS) remained largely flat, despite unemployment increasing slightly from 11.1% to 11.3% and average personal disposable income declining by 2.9%⁽⁵⁾⁽⁶⁾
- Price changes have remained stable with WAP increasing by 0.7% in 2013⁽⁷⁾

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section)

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011) (3) Independent agency Empty Pack Surveys, 2006 – 2013 (4) Bulgarian Customs Agency data for legal domestic sales volumes in 2012 and 2013 (5) The Economist Intelligence Unit (6) Euromonitor Passport (7) EU Commission WAP tables



Inflows increased, mainly driven by a higher presence of Illicit Whites

65% of Duty Free inflows were Illicit Whites brands

Total inflows by country of origin 2007-2013^{(1)(a)}

ND INFLOWSTO BULGARIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	1.90	2.56	2.07	2.19	1.23	1.28	1.95	52%
Unspecified	0.00	0.00	0.77	1.68	1.05	0.47	0.36	(23)%
Serbia	0.24	0.10	0.25	0.29	0.20	0.17	0.09	(49)%
Spain	0.00	0.01	0.00	0.00	0.00	0.00	0.02	>100%
Ukraine	0.08	0.18	0.13	0.11	0.05	0.01	0.01	27%
Counterfeit							0.00	n/a
Other	0.10	0.13	0.28	0.66	0.31	0.29	0.23	(23)%
Total inflows	2.33	2.97	3.50	4.93	2.84	2.23	2.66	19%

Non-domestic inflows to Bulgaria rose by 19% in 2013. This increase is due to an increase in Illicit Whites brands

- Corsair, My Way and Palladium are the most prevalent Illicit Whites brands with Duty Free labelling. These brands comprise over 29% of the 1.95bn Duty Free inflow
- Packs of unspecified market variant are also Illicit Whites brands, with Raquel the most prevalent, accounting for 30% of the inflow
- An increase in the WAP of Serbian cigarettes of 16.2% in 2013 may be a contributing factor in the 49% volume decline⁽²⁾

Total outflows by destination country – 2007-2013⁽¹⁾

OUTFLOWS FROM BULGARIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
France	0.17	0.08	0.04	0.02	0.03	0.05	0.09	71%
Germany	0.05	0.04	0.04	0.03	0.07	0.06	0.08	27%
Belgium	0.04	0.01	0.13	0.05	0.01	0.04	0.04	4%
UK	0.09	0.13	0.09	0.03	0.06	0.08	0.03	(58)%
Greece	0.15	0.07	0.04	0.02	0.03	0.03	0.03	12%
Netherlands	0.02	0.02	0.00	0.04	0.03	0.03	0.03	(14)%
Other	0.16	0.15	0.13	0.08	0.05	0.09	0.07	(25)%
Total outflows	0.67	0.49	0.47	0.27	0.29	0.38	0.36	(5)%

Outflows from Bulgaria have declined by 5% in 2013, with France and Germany the major destination markets

- Outflows continue to be of low volumes

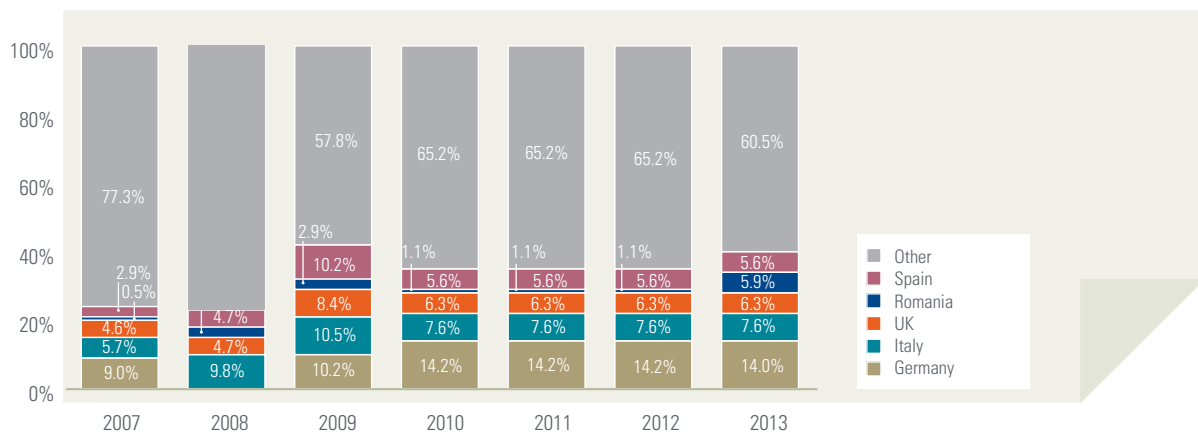
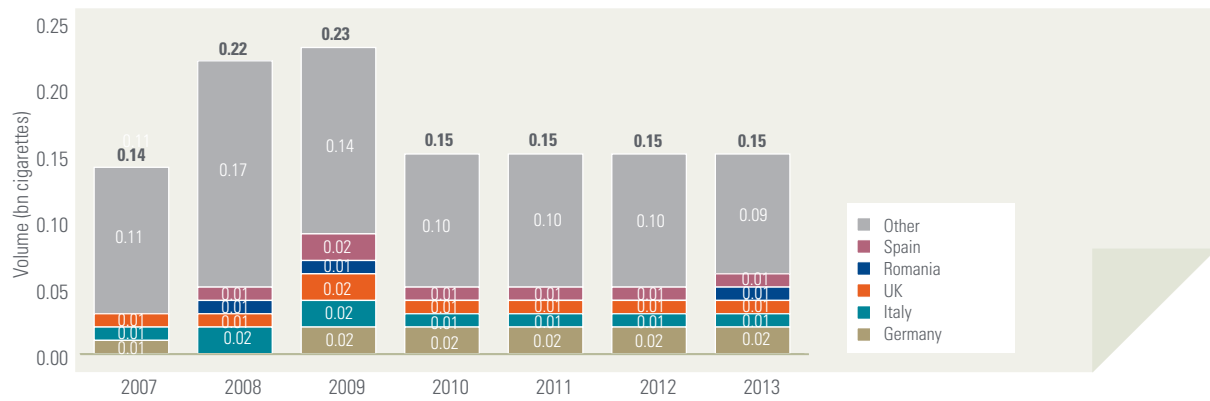
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Source: (1) KPMG EU Flows Model. (2) EU Commission WAP tables.



ND(L) volumes were stable and account for a low level of consumption

ND(L) by origin 2007-2013^{(1)(2)(3)(a)(b)}



BULGARIA



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Germany, Greece, Italy and Turkey remained popular travel destinations for Bulgarians, with all inflows from these countries therefore assumed to be legal

- As a neighbouring higher priced market, all flows from Romania were assumed to be legal

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand 2007-2013^{(1)(2)(3)(a)}



Most brands have shown a decline in ND(L) inflows, with the exception of Karelia

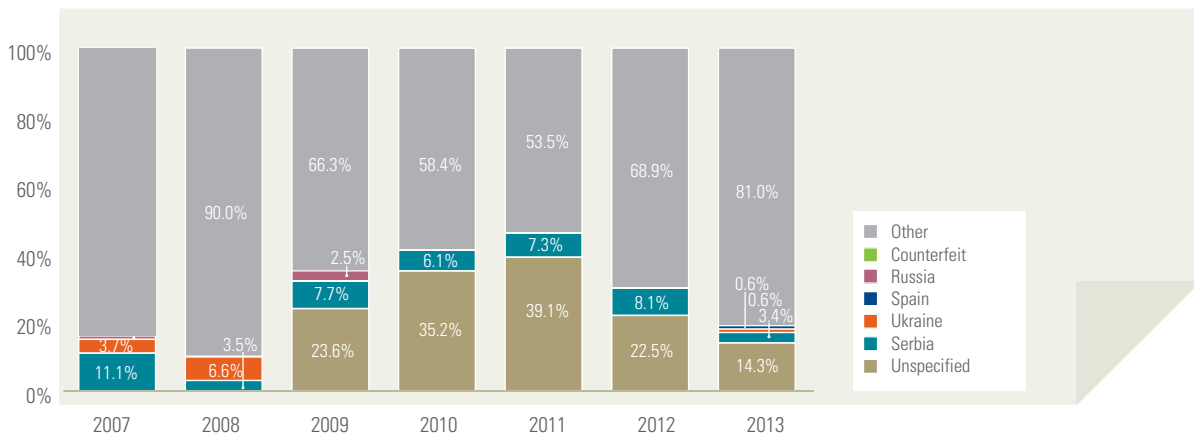
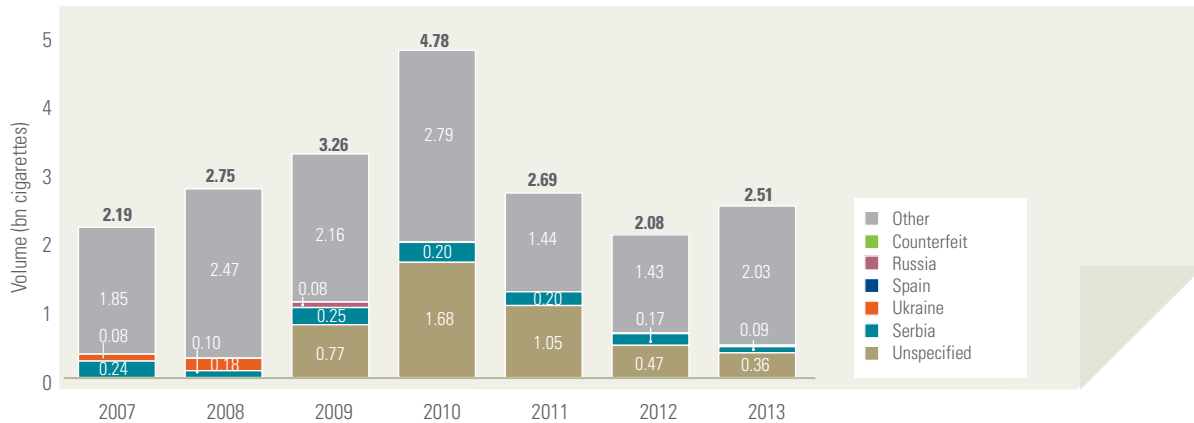
- The most popular ND(L) brand is Marlboro. Germany, Greece, Italy, Turkey and the UK comprise 74% of the Marlboro ND(L) balance
- 65% of Karelia branded cigarettes are from Greece and Turkey

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

Illicit Whites brands are driving increased C&C in 2013

C&C by origin 2007-2013^{(1)(2)(3)(a)}



BULGARIA



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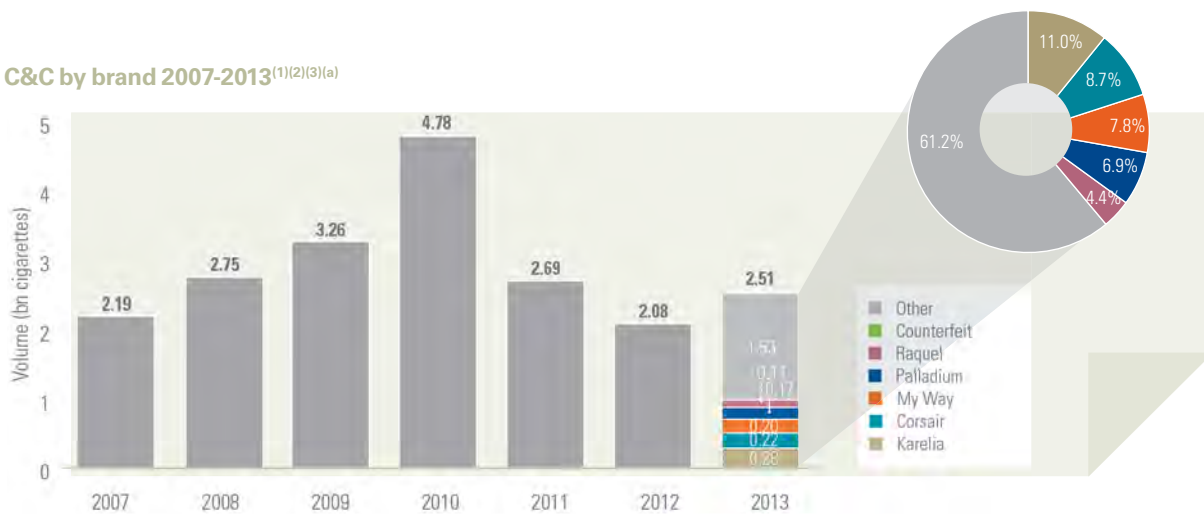
Total C&C in Bulgaria increased by 21% between 2012 and 2013, driven by an increase in Illicit White brands

- If the 2.51bn C&C cigarettes in 2013 had been legally purchased in Bulgaria the tax revenue gained would have been approximately €247m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.
 Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.
 (3) KPMG analysis of data sources provided by manufacturers.

C&C INFLOWS BY BRAND

C&C by brand 2007-2013^{(1)(2)(3)(a)}



The increase in C&C has been driven by Illicit White brands such as Corsair, MyWay and Palladium

- Counterfeit volumes remain low in Bulgaria in 2013, with C&C dominated by Illicit Whites brands

Composition of Illicit Whites inflows 2007-2013^{(1)(3)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO BULGARIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	0.09	0.14	0.26	0.52	0.57	0.64	1.27	98%
Country specific	0.00	0.00	0.04	0.10	0.10	0.05	0.08	64%
Unspecified	0.00	0.00	0.28	1.11	0.82	0.40	0.29	(29)%
Total Illicit Whites	0.09	0.14	0.58	1.73	1.49	1.10	1.64	50%

65% of Duty Free inflows were Illicit Whites brands

Illicit Whites are an increasing part of illicit trade in Bulgaria, accounting for 65% of C&C volumes in 2013

- The majority of Illicit Whites in 2013 with Duty Free labelling, with Corsair, MyWay and Palladium accounting for 46% of the Duty Free Illicit Whites balance

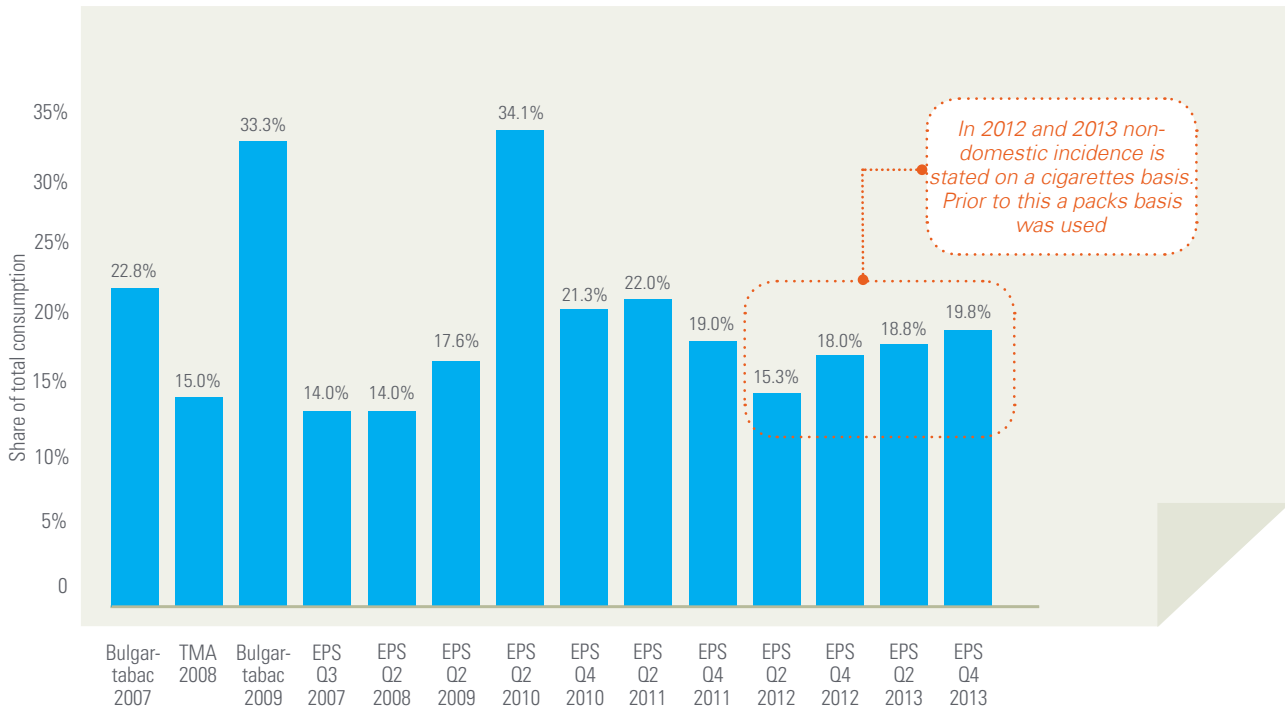
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



EPS results and EU Flows Model

Empty Pack Survey non-domestic estimates 2007-2013⁽¹⁾



BULGARIA

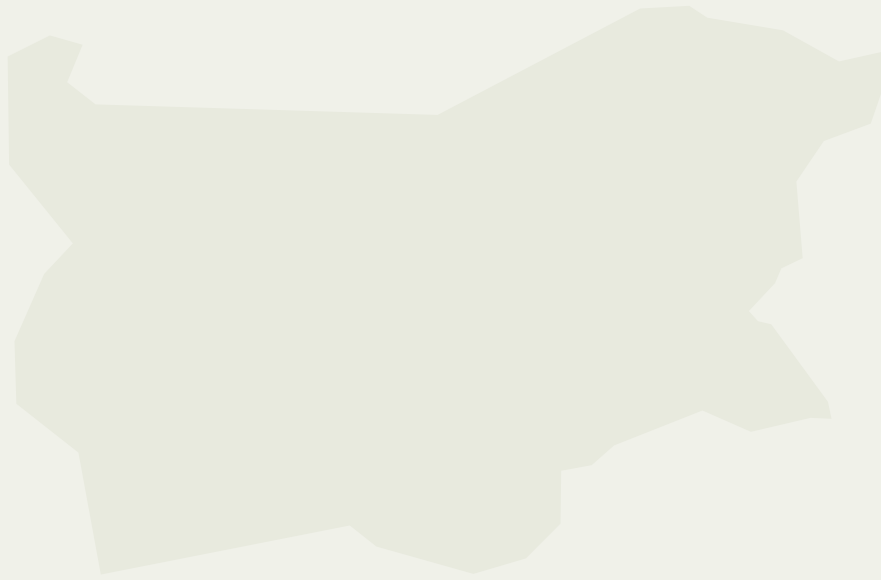


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EPS has shown an increase in non-domestic incidence since 2012

- The empty pack survey in Bulgaria collected 10,000 packs during the second and fourth quarters of the year. These packs were collected across 14 towns and cities. The number of packs collected in the town or city is weighted by its population

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013.



BULGARIA



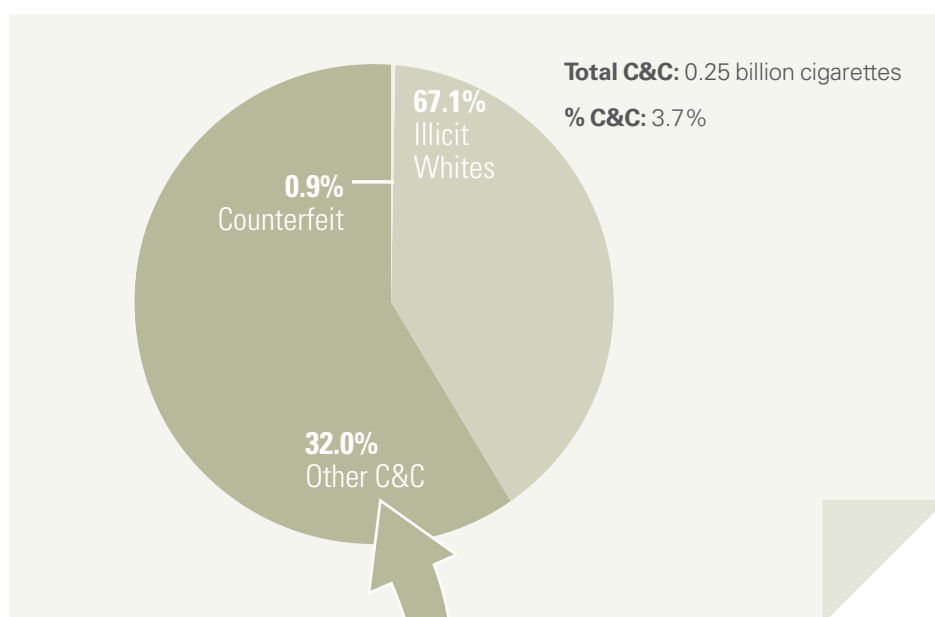
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CROATIA



Croatia has low volumes of counterfeit and contraband but high levels of Illicit Whites

Manufactured cigarette C&C consumption 2013

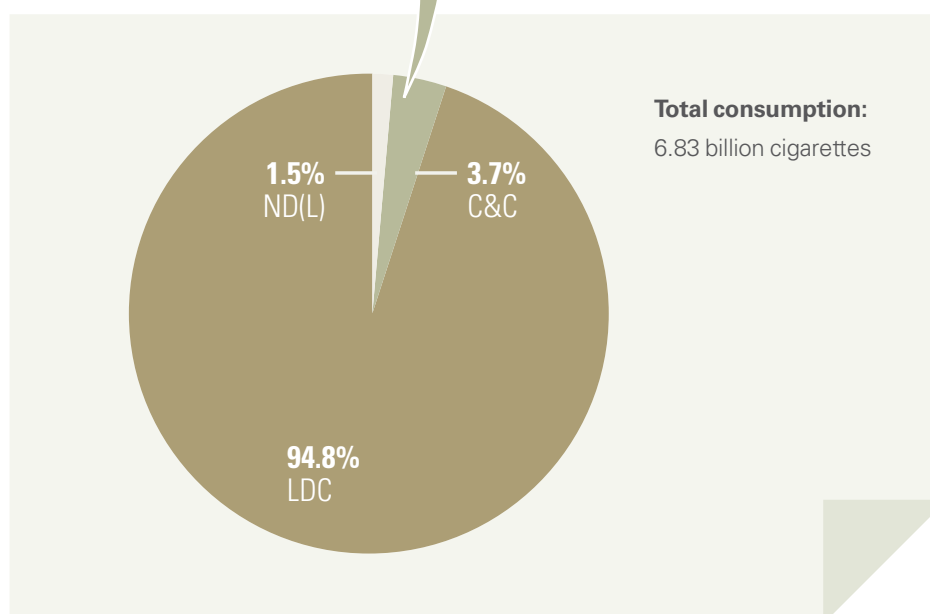


CROATIA

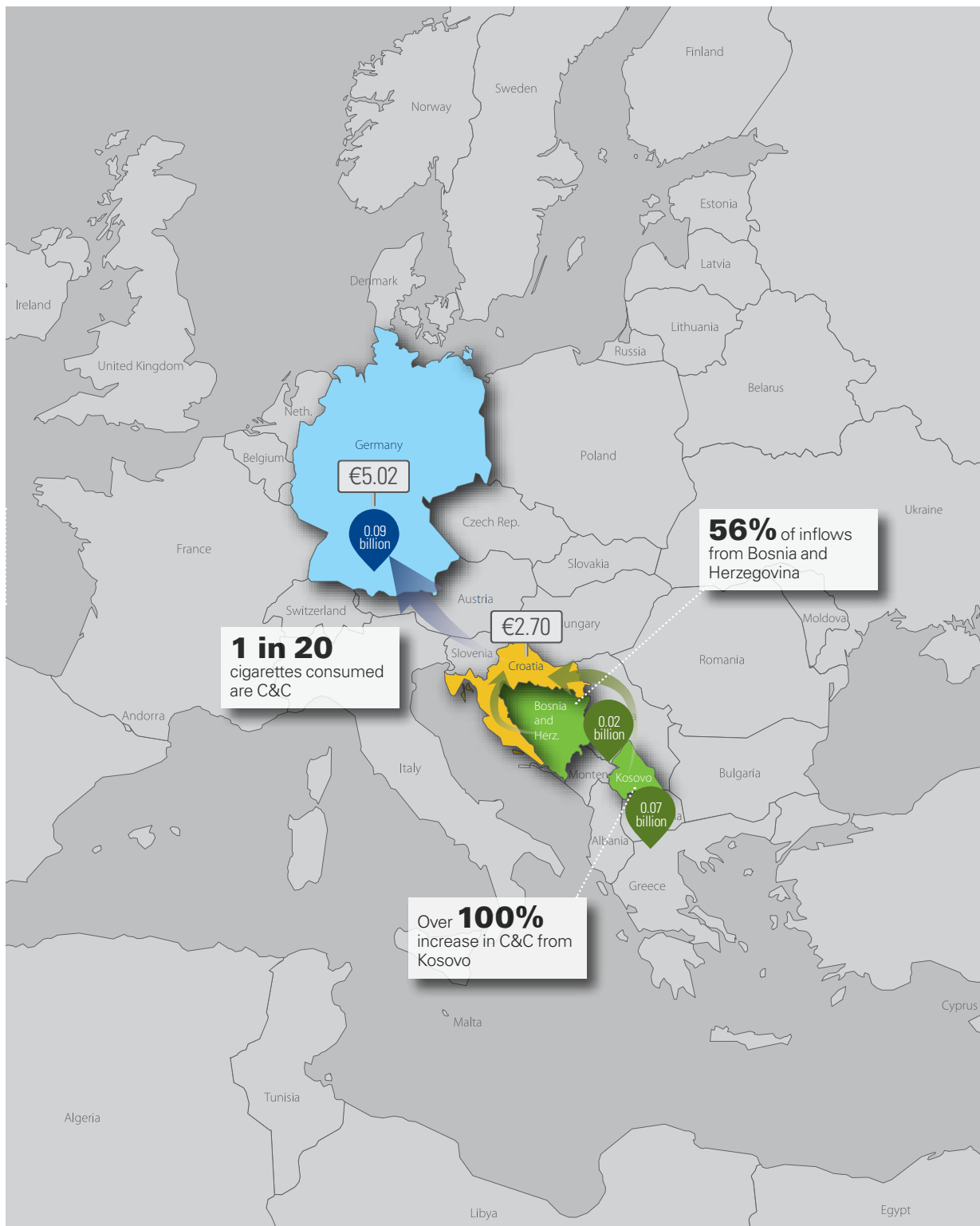


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Manufactured cigarette share of consumption 2013



KEY INFLOWS AND OUTFLOWS



CROATIA



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Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

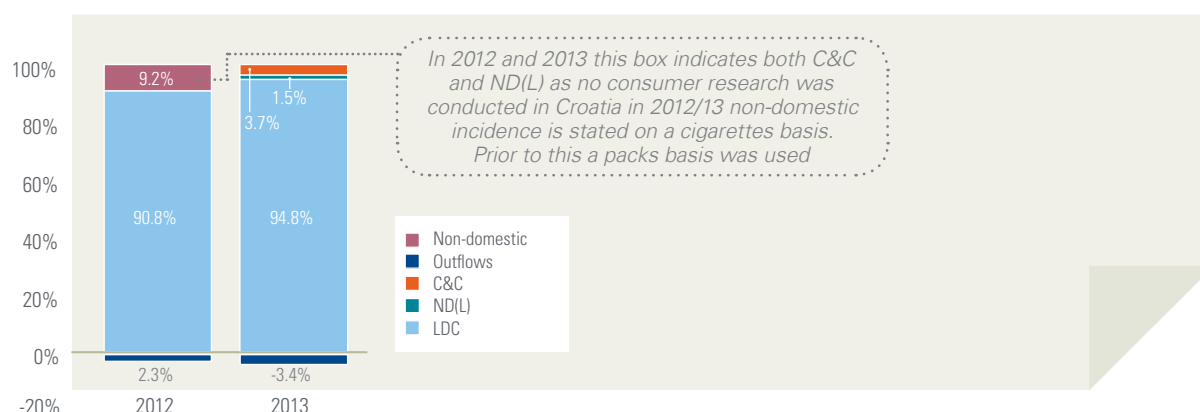
Source: (1) KPMG EU Flows Model.

The first year of analysis suggested a decline in overall consumption and the majority of inflows being C&C

Total manufactured cigarette consumption – Croatia⁽¹⁾⁽²⁾⁽³⁾

TOTAL CROATIA CONSUMPTION				
Billion cigarettes	2012	2013	% change 2012-13	% incidence 2013
Legal domestic sales (LDS)	7.22	6.71	(7)%	
Outflows	-0.18	-0.23	31%	3%
Legal domestic consumption (LDC)	7.04	6.47	(8)%	95%
Non-domestic legal (ND(L))	n/a	0.10	n/a	2%
Counterfeit and contraband (C&C)	n/a	0.25	n/a	4%
Total non-domestic	0.71	0.35	(50)%	5%
Total consumption	7.76	6.83	(12)%	

Share of Croatia cigarette consumption by type - 2012-2013^{(1)(2) (3)(a)(b)}



CROATIA



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Both legal domestic sales (LDS) and non-domestic consumption appear to have fallen in 2013 as a result of reduced overall consumption, which may have been impacted by Croatia’s membership of the EU

- Overall non-domestic incidence fell from 9.2% to 5.2% between 2012 and 2013 (Croatia was not part of the EU for the 2012 study and hence a comparative split of non-domestic into ND(L) and C&C is not available)
- Assuming that outflows remained the same between 2012 and 2013, the results imply that overall consumption has fallen by around 12%
- Price rises of 10% of the WAP may have contributed to the significant decline in consumption
- The economic environment was mixed; despite high unemployment in Croatia of 20%⁽⁴⁾ Personal Disposable Income grew by 2% in 2013⁽⁵⁾

Note: (a) As Croatia was not in the EU in 2012 KPMG has used historic legal domestic sales data but did not report on 2012 volumes. Therefore the volumes reported for 2012 is an estimate based on historic data and not generated by the 2012 EU flows model. (b) Non-domestic incidence for 2012 is given as no consumer research was undertaken for Croatia before 2013.

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Independent agency Empty Pack Surveys, 2012 – 2013. (4) Croatian Statistical Office, 2013. (5) Euromonitor, Personal Disposable Income, 2013, downloaded March 2014.

Inflows almost halved between 2012 and 2013, with the main sources coming from neighbouring non-EU countries

Total inflows by country of origin - 2012-2013^{(1) (a)(b)}

INFLOWSTO CROATIA			
Billion cigarettes	2012	2013	2012-13 %
Bosnia and Herzegovina	0.46	0.20	(56)%
Kosovo	0.01	0.07	>100%
Serbia	0.07	0.05	(34)%
Duty Free	0.02	0.02	15%
Counterfeit		0.00	n/a
Other	0.16	0.01	(93)%
Total inflows	0.71	0.35	(50)%

All Duty Free labelled packs were Illicit Whites brands

Based on analysis of the 2012 and 2013 empty pack survey results in Croatia, inflows from Bosnia & Herzegovina make up over half of the overall inflow

- Whilst cigarette prices in Croatia are some of the lowest in the EU, prices in Bosnia & Herzegovina are on average €0.99 cheaper, which may create incentive for smuggling of contraband product
- However, the tightening of border security and reduction of the legal allowance since Croatia's accession to the EU may also have driven the lower flows
- Kosovo became a more significant inflow market in 2013

Total outflows by destination country - 2006-2013^{(1) (a)}

OUTFLOWS FROM CROATIA			
Billion cigarettes	2012	2013	2012-13 %
Germany	0.07	0.09	25%
Austria	0.03	0.03	0%
Slovenia	0.01	0.03	<100%
Other	0.07	0.09	28%
Total outflows	0.18	0.23	31%

Outflows appear to be generated by tourists purchasing cheaper cigarettes before returning from holidays as opposed to cross-border sales

- Prior to joining the EU land border limits would have been just 40 cigarettes from Croatia, resulting in low outflows to the EU, which now appear to be increasing
- The largest outflow in 2013 was to Germany, a major source of tourism for Croatia

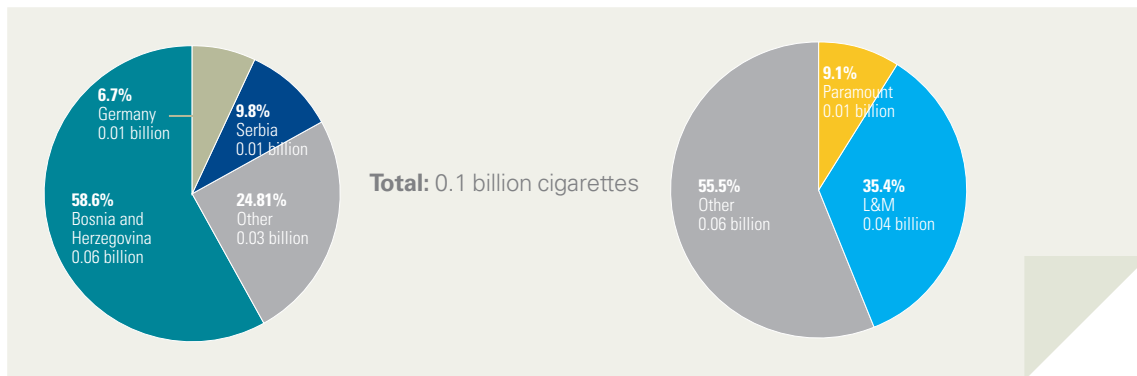
Note: (a) As Croatia was not in the EU in 2012 KPMG has used historic legal domestic sales data but did not report on 2012 volumes. Therefore the number is an estimate based on historic data and not generated by the EU flows model.
 (b) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Source: (1) KPMG EU Flows Model.



Low import allowances from Bosnia & Herzegovina mean that overall ND(L) volumes are low

ND(L) by origin and brand - 2013 ^{(1)(2)(a)(b)}



ND(L) volumes represent 1.5% of total consumption

- Consumer research in Croatia indicated that 60% of consumers that travelled and purchased cigarettes in 2013 travelled to Bosnia & Herzegovina
- The low legal limit of 40 cigarettes per land crossing resulted in 37% of the total flow from Bosnia coming from legal purchases
- Consumer research also showed that a small number of trips were made to Serbia, where once again the low legal limit of 40 cigarettes resulted in these trips only accounting for 26% of the total flow
- Consumer research indicated that L&M was the most popular brand purchased. Other brands purchased included Paramount, Vogue, Multifilter and Winston

CROATIA



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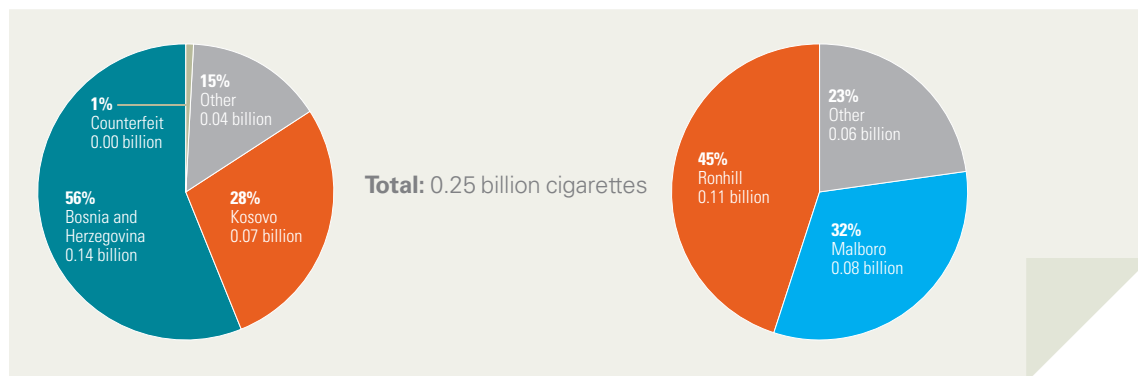
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.

(3) KPMG analysis of data sources provided by manufacturers.

60% of counterfeit and contraband in Croatia comes from Illicit Whites brands manufactured in non-EU countries

ND(L) by origin and brand 2013^{(1)(2)(a)(b)}



LABELLING OF ILLICIT WHITES INFLOWS TO CROATIA	
Billion cigarettes	2013
Country Specific	0.15
Duty Free	0.02
Unspecified	0.00
Total Illicit Whites	0.17

All Duty Free labelled packs were Illicit Whites brands

63% of the flow from Bosnia & Herzegovina and the majority of the flow from Kosovo make up most of the C&C consumed within Croatia

- The consumer research indicated that travel from Croatia to Kosovo was limited, indicating that almost all of this flow is likely to be C&C
- All of the flow from Kosovo was from the brand Ronhill, whilst a large proportion of the flows from Bosnia & Herzegovina came from Marlboro
- Ronhill was also the only brand with Duty Free and Unspecified markings on it, as well as being widely available across Croatia and neighbouring countries
- If the total volume of counterfeit and contraband had been consumed legally within the Croatian market, an additional tax revenue of approximately €25 million would have been raised by the Croatian Treasury

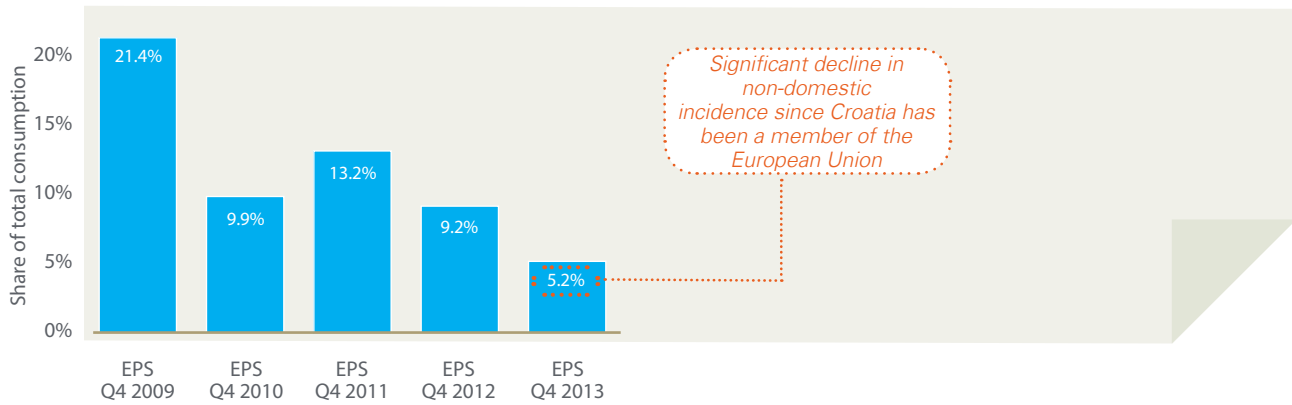
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.



EPS non domestic estimates

Empty Pack Survey non-domestic estimates 2009-2013^{(1)(a)}



- The empty pack survey in Croatia collected 3,000 in 2013. This was undertaken as a single wave conducted in Q4 (October). The sample focused on 8 cities and the number of packs collected in each city was weighted by the city population
- No adjustments were made to the data in our analysis

CROATIA



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Note: (a) For many countries the project methodology changed in 2012 when the non-domestic incidence was reported by the number of cigarettes rather than the number of packs. For Croatia all data is presented by the number of cigarettes.

Source: (1) Independent agency Empty Pack Surveys, 2009 – 2013.

Non-domestic legal volume calculations and explanations

KPMG non domestic legal flows Croatia

COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 ⁽¹⁾	2013 ND(L) (bn sticks)	% of ND
Germany	0.01	0.01	100%

USE OF CONSUMER RESEARCH AND ANY ADJUSTMENTS FOR 2013 DATA							
Country	ND 2013 ⁽¹⁾	Total trips where cigarettes purchased (m) ^{(2) (3)}	Number of packets per trip ⁽³⁾	Total packs (m)	Data sources ^{(2) (3)}	2013 ND(L) (bn sticks)	% of ND
Bosnia and Herzegovina	1.9m	2	3.71	1.9m	Consumer research, Excise allowances	0.06	37%
Serbia	0.04	0.3m	2	0.62	Consumer research, Excise allowances	0.01	26%

- Consumer research was used in order to estimate the level of non-domestic legal inflows to Croatia
- Whilst this represents 1.85 million trips, the majority day trips, the legal limit of 40 cigarettes per trip resulted in 37% of the total flow from Bosnia coming from legal purchases
- Consumer research also showed that a small number of trips were made to Serbia, where once again the low legal limit of 40 cigarettes resulted in these trips only accounting for 26% of the total flow
- For Germany, as it is a higher priced country, it is assumed that 100% of the flow is legal

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

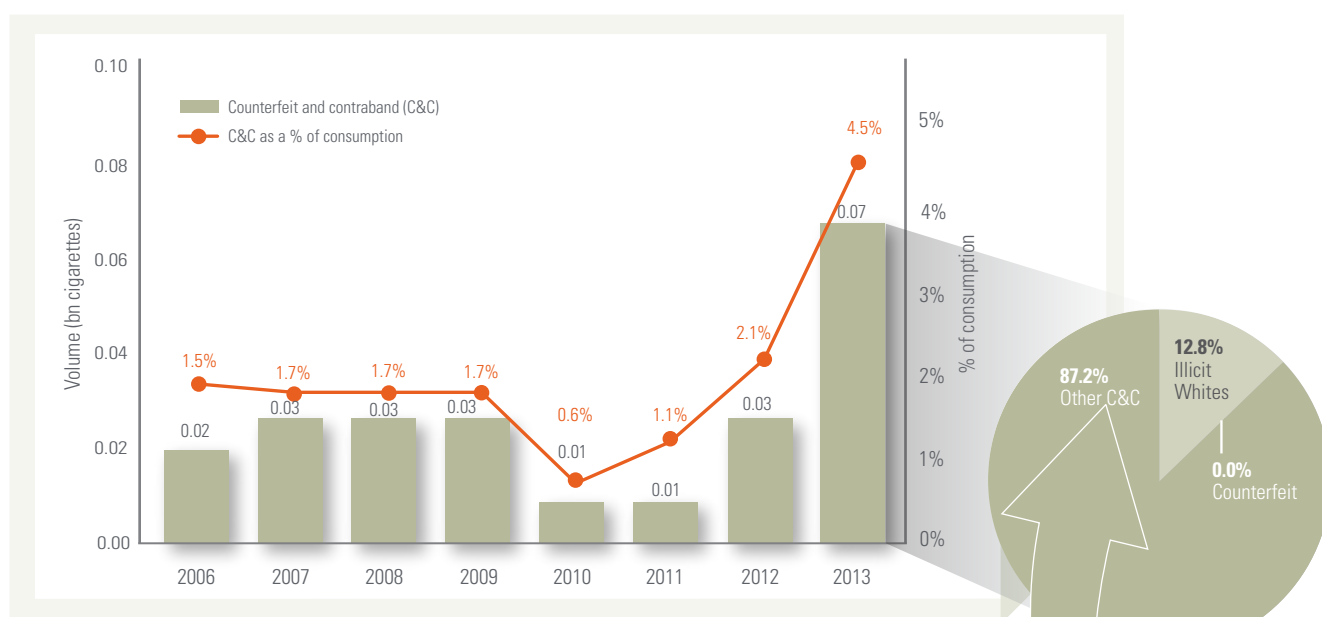


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Overall consumption was stable

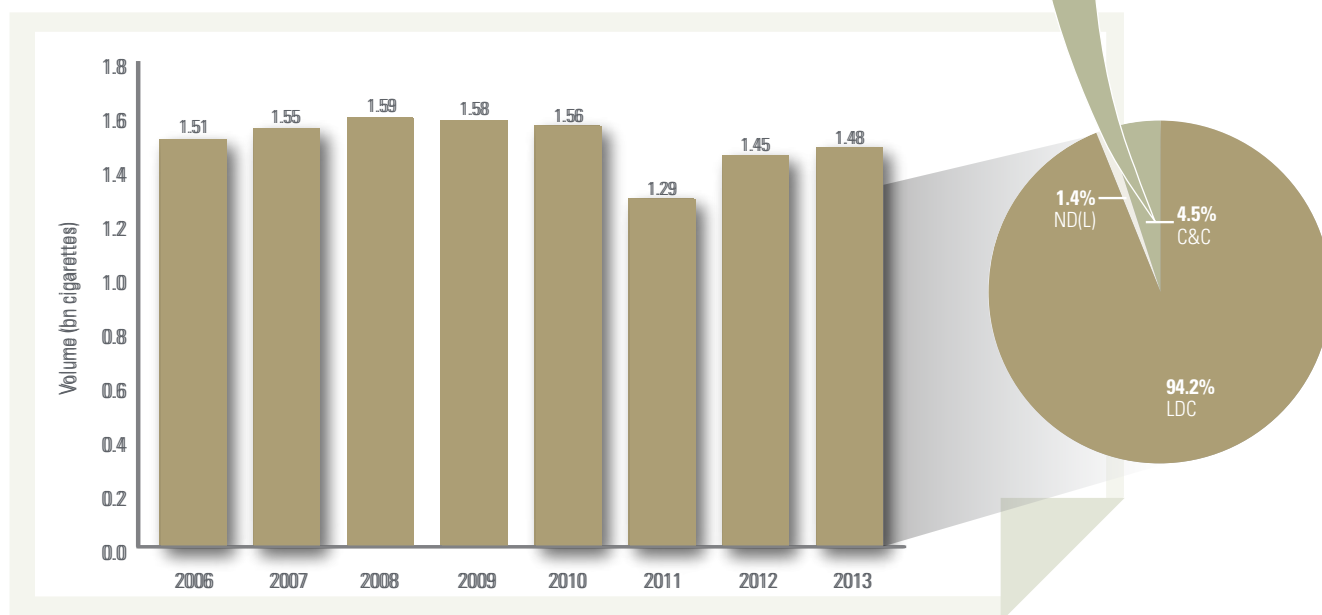
Manufactured cigarette C&C volumes and share of overall consumption 2006-13



CYPRUS

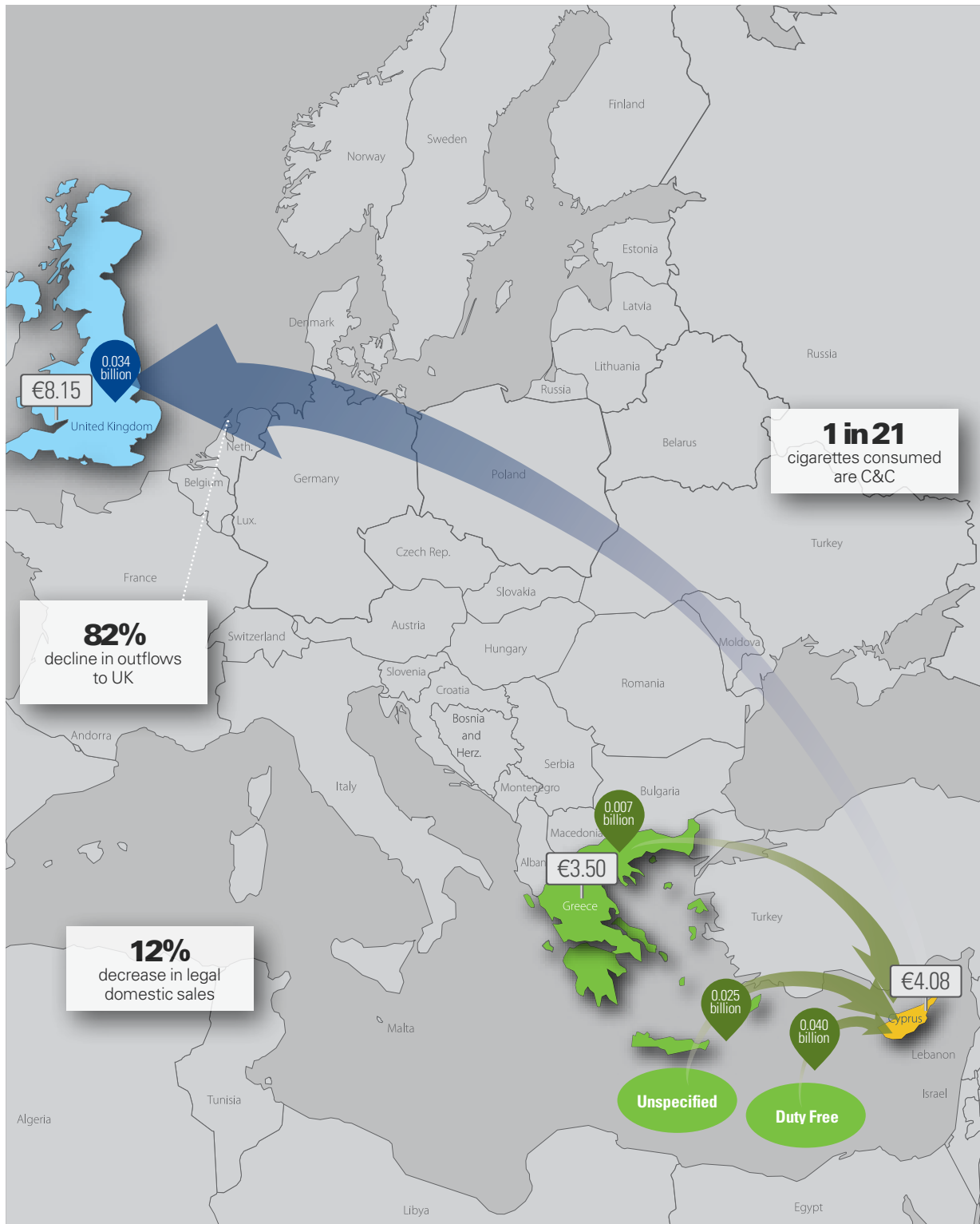


Manufactured cigarette consumption 2006-13



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KEY INFLOWS AND OUTFLOWS



CYPRUS



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Main outflow

Main inflow

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

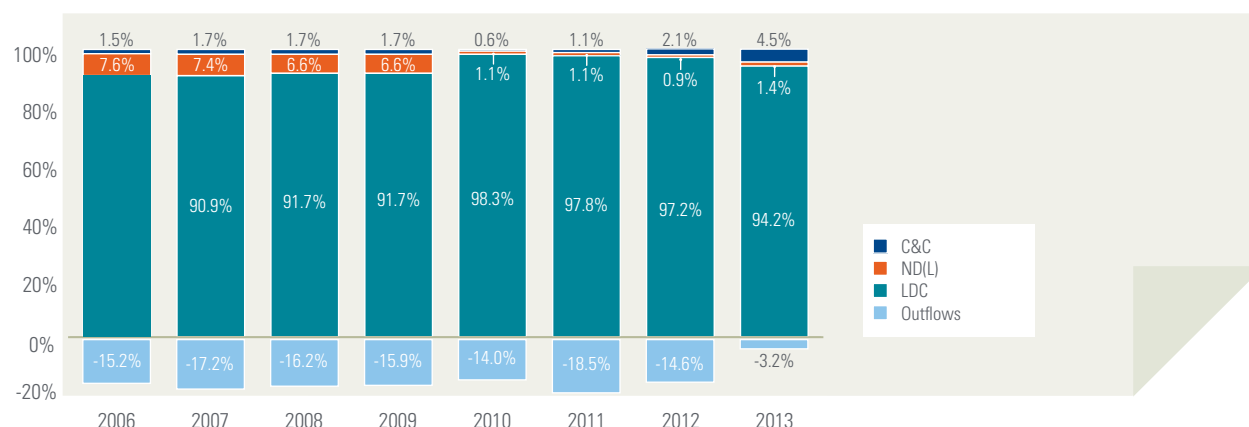
Overall consumption increased as outflows declined significantly whilst non-domestic flows grew

Updated figures from 2012 report revised after tax stickers were released to the EU after publication

Total manufactured cigarette consumption – Cyprus^{(1)(2)(a)}

TOTAL CYPRUS CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	1.60	1.67	1.72	1.71	1.75	1.51	1.63	1.45	(12)%
Outflows	-0.23	-0.27	-0.26	-0.25	-0.22	-0.24	-0.21	-0.05	(77)%
Legal domestic consumption (LDC)	1.38	1.40	1.46	1.45	1.53	1.27	1.42	1.40	(2)%
Non-domestic legal (ND(L))	0.12	0.11	0.10	0.10	0.02	0.01	0.01	0.02	59%
Counterfeit and contraband (C&C)	0.02	0.03	0.03	0.03	0.01	0.01	0.03	0.07	>100%
Total non-domestic	0.14	0.14	0.13	0.13	0.03	0.03	0.04	0.09	>100%
Total consumption	1.51	1.55	1.59	1.58	1.56	1.29	1.45	1.48	2%

Share of Cyprus cigarette consumption by type 2006-2013⁽¹⁾⁽²⁾



CYPRUS



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A 2% increase in total manufactured cigarette consumption was caused by an increase in non-domestic consumption as well as a decrease in outflows

- The biggest impact on legal domestic consumption has been the decline in outflows, mainly to the UK
- Tax increases consisted of a 0.72% increase in VAT⁽³⁾ resulting in the overall weighted average price increasing by 4.3%
- The financial crises in Europe since 2008 and further crisis in Cyprus since 2012 may have impacted manufactured cigarette consumption as unemployment grew significantly from 3.7% in 2008 to 17.4% in 2013 while GDP per capita declined by 7%⁽⁴⁾ over the same period

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used.
 Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2012 (Ipsos acquired Synovate in 2011). (3) EC Excise Duty tables (Part III – Manufactured Tobacco) as at January 2013/ January 2014. (4) The Economist Intelligence Unit.

Main non-domestic sources were from Duty Free or unspecified markets

5% of Duty Free flows were Illicit Whites

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWS TO CYPRUS									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	0.014	0.017	0.061	0.060	0.009	0.014	0.023	0.040	77%
Unspecified	0.000	0.000	0.000	0.000	0.000	0.003	0.004	0.025	>100%
Greece	0.006	0.006	0.014	0.014	0.005	0.001	0.001	0.007	>100%
Bulgaria	0.000	0.000	0.000	0.000	0.003	0.000	0.000	0.005	n/a
Russia	0.000	0.000	0.008	0.008	0.005	0.000	0.004	0.002	(56)%
Counterfeit								0.000	n/a
Other	0.118	0.117	0.049	0.049	0.005	0.010	0.011	0.008	(31)%
Total inflows	0.138	0.141	0.132	0.131	0.027	0.028	0.043	0.087	>100%

Total non-domestic inflows more than doubled as both non-domestic legal (ND(L)) and counterfeit and contraband (C&C) flows increased

- The majority of non-domestic cigarettes had either Duty Free or Unspecified labelling, accounting for approximately 70% of total non-domestic flows
- The largest inflow country was Greece where inflows increased significantly from 1 million to 7 million cigarettes

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM CYPRUS									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
UK	0.213	0.250	0.241	0.214	0.200	0.205	0.193	0.034	(82)%
Greece	0.013	0.000	0.000	0.000	0.003	0.005	0.002	0.004	>100%
Germany	0.002	0.004	0.003	0.003	0.004	0.000	0.003	0.004	28%
Netherlands	0.000	0.000	0.000	0.000	0.000	0.006	0.004	0.003	(36)%
Other	0.002	0.005	0.007	0.029	0.012	0.023	0.003	0.000	(100)%
Total outflows	0.230	0.266	0.258	0.252	0.218	0.239	0.211	0.048	(77)%

Total outflows decreased by 77% in 2013 as flows to Cyprus' main outflow country, the UK, fell significantly

- Outflows to the UK, a higher priced market which historically accounted for 70% of total outflows reduced
 - This may have been partially caused by a 7% decline in tourist flows from the UK to Cyprus⁽²⁾⁽³⁾
- The decrease in outflows was partially offset by increased outflows to Greece and Germany

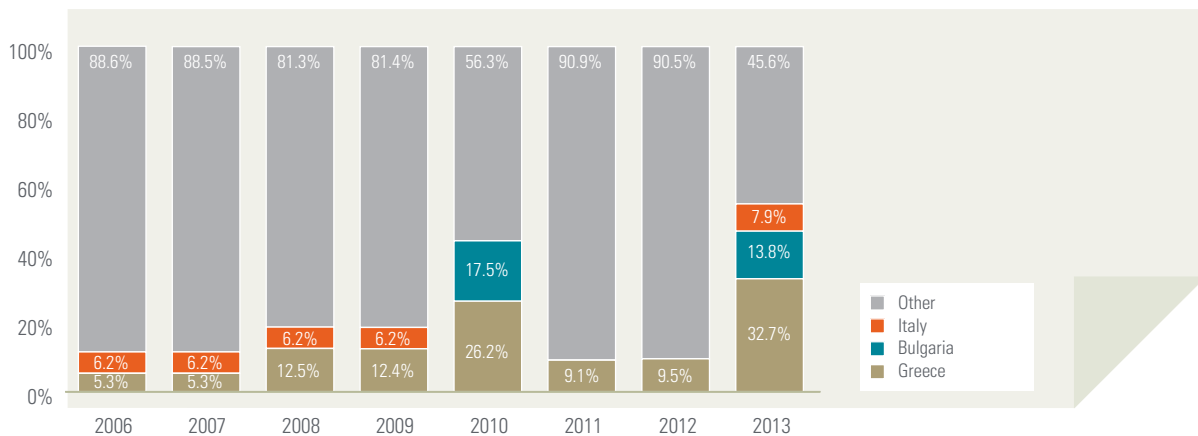
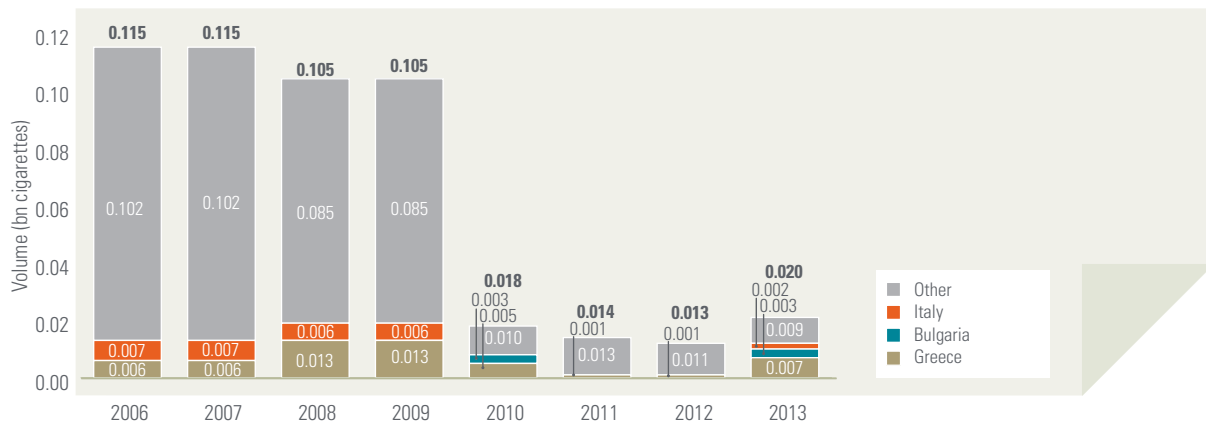
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model. (2) Arrivals of tourists by country of usual residence, 1980-2012, Republic of Cyprus, Statistical Service; downloaded April 2014. (3) Tourism statistics, January- December 2013, Republic of Cyprus, Statistical Service; downloaded April 2014.



Mediterranean markets close to Cyprus account for the majority of non-domestic inflows

ND(L) by origin - 2006-2013^{(1)(2)(a)(b)}



CYPRUS



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ND(L) volumes increased as a share of total consumption

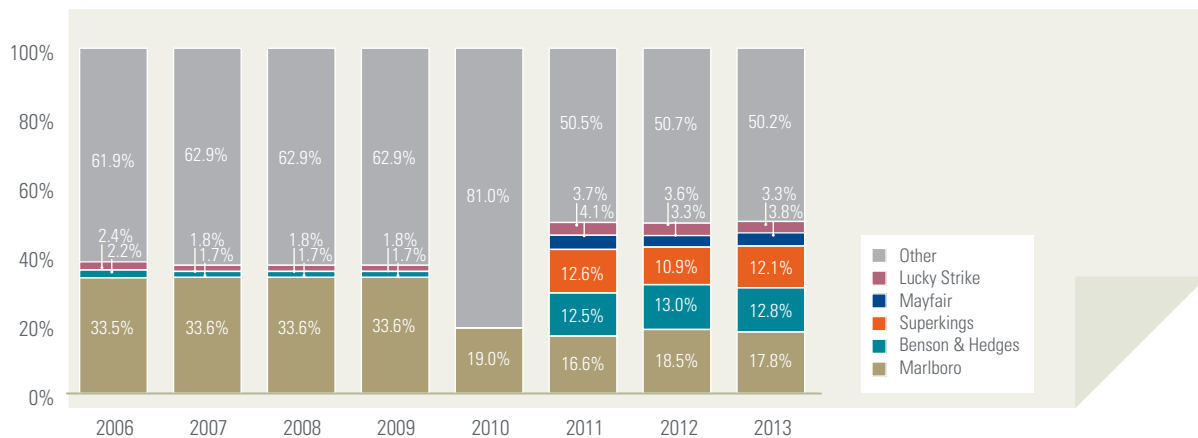
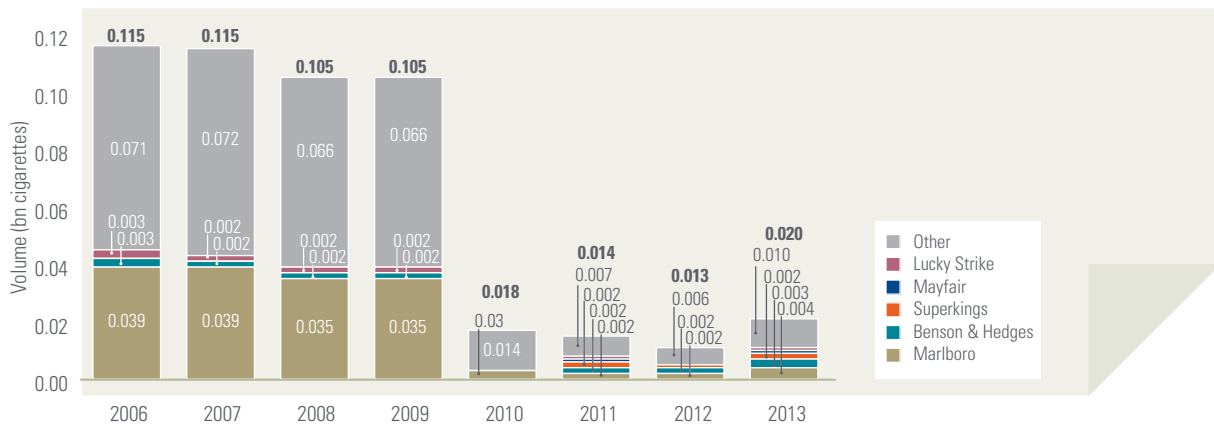
- All inflows from Greece were categorised as non-domestic legal consumption as the price difference between Greece and Cyprus was only €0.58⁽³⁾ in 2013
- Inflows from Bulgaria, where the average price difference was €1.70 per pack, totalled 5 million cigarettes in 2013. Analysis of the consumer research and travel and purchasing patterns showed that 58% of Bulgarian flows were legal
 - An analysis of historic consumer research, updated to reflect travel trends in 2013 resulted in the number of trips made to purchase cigarettes being 14,000⁽¹⁾
 - An average of 10 packs per trip were brought per trip

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) EC Excise Duty tables (Part III – Manufactured Tobacco) as at January 2013/ January 2014.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand 2006-2013^{(1)(2)(a)}



The increase in ND(L) showed a consistent level of growth between the main brands

- Marlboro, Benson & Hedges and Superkings together accounted for 45% of total ND(L) inflows
- “Other” legal inflows consisted of smaller volumes of just over 35 other brands

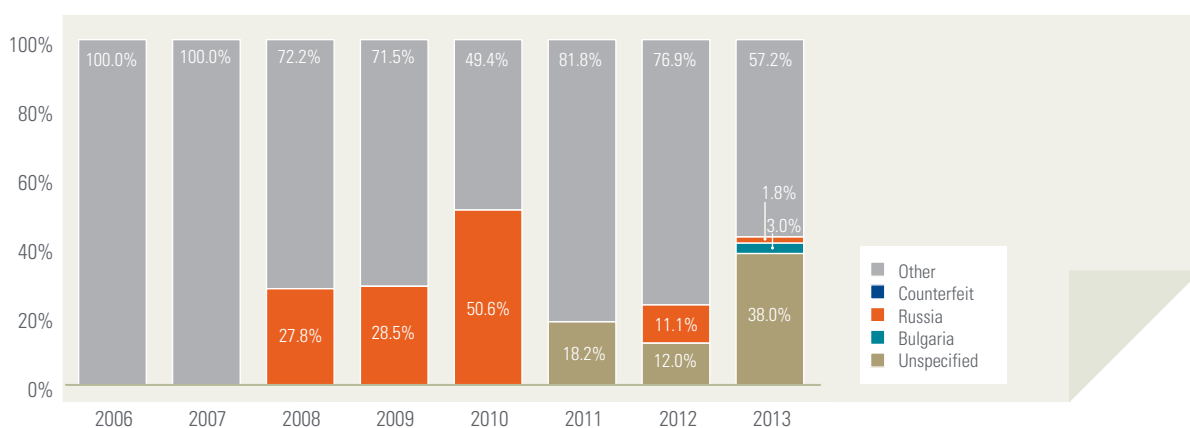
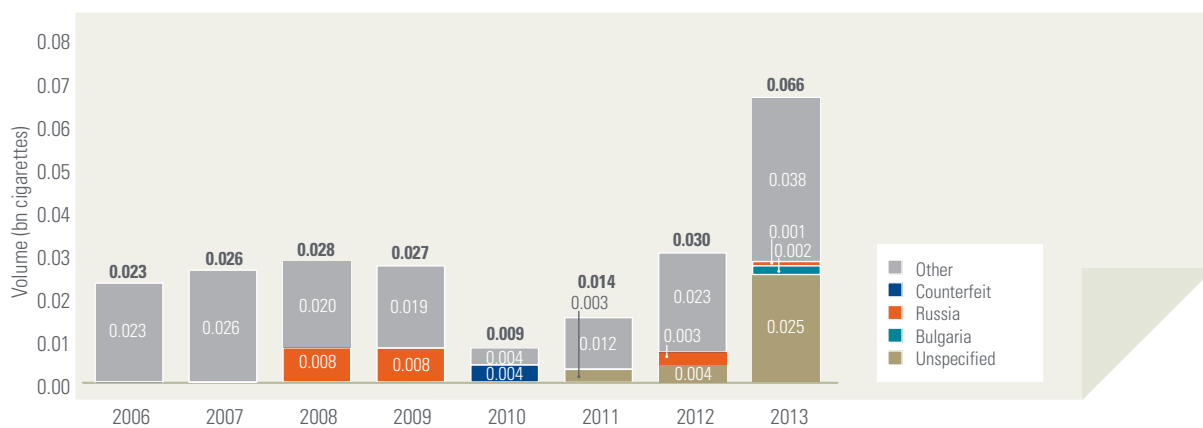
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



Contraband volumes increased significantly in 2013

C&C by origin 2006-2013^{(1)(2)(a)}



CYPRUS



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C&C more than doubled in 2013, largely due to a significant increase in cigarettes with unspecified labelling

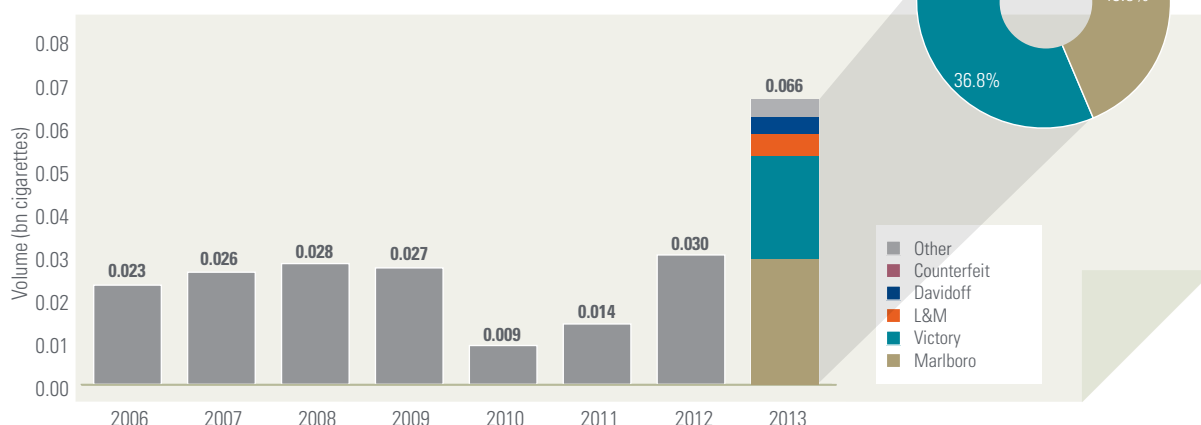
- Almost 40% of C&C flows were unspecified cigarettes, classified as Illicit Whites
- In Russia, relatively few tourist flows were identified in the consumer research and the price difference was high at over €2.77⁽³⁾, therefore 75% of inflows were categorised as C&C flows

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) EC Excise Duty tables (Part III – Manufactured Tobacco) as at January 2013/ January 2014.

C&C INFLOWS BY BRAND

C&C by brand - 2006-2013^{(1)(2)(a)}



Illicit Whites made up of 5% of overall Duty Free flows

Composition of Illicit Whites inflows - 2006-2013^{(1)(2)(a)(b)}

LABELLING OF ILLICITWHITES INFLOWS TO CYPRUS								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country Specific	0.000	0.002	0.000	0.002	0.005	0.006	0.006	7%
Duty Free	0.000	0.000	0.000	0.000	0.000	0.001	0.000	(68)%
Unspecified	0.000	0.000	0.000	0.000	0.000	0.000	0.002	n/a
Total Illicit Whites	0.000	0.002	0.002	0.002	0.005	0.007	0.009	18%

All C&C consumption in Cyprus consisted of contraband and Illicit Whites inflows as no counterfeit cigarettes were identified in the EPS

- The largest contraband brand was Marlboro, followed by Victory, manufactured by Bulgartabac
- If the total volume of C&C had been consumed legally within Cyprus, an additional tax revenue of approximately €10 million would have been raised by the Cypriot Treasury

Consumption of Illicit Whites brands is increasing

- This was partly due to an increase of Illicit Whites brands such as Super Sunday and President with unspecified labelling

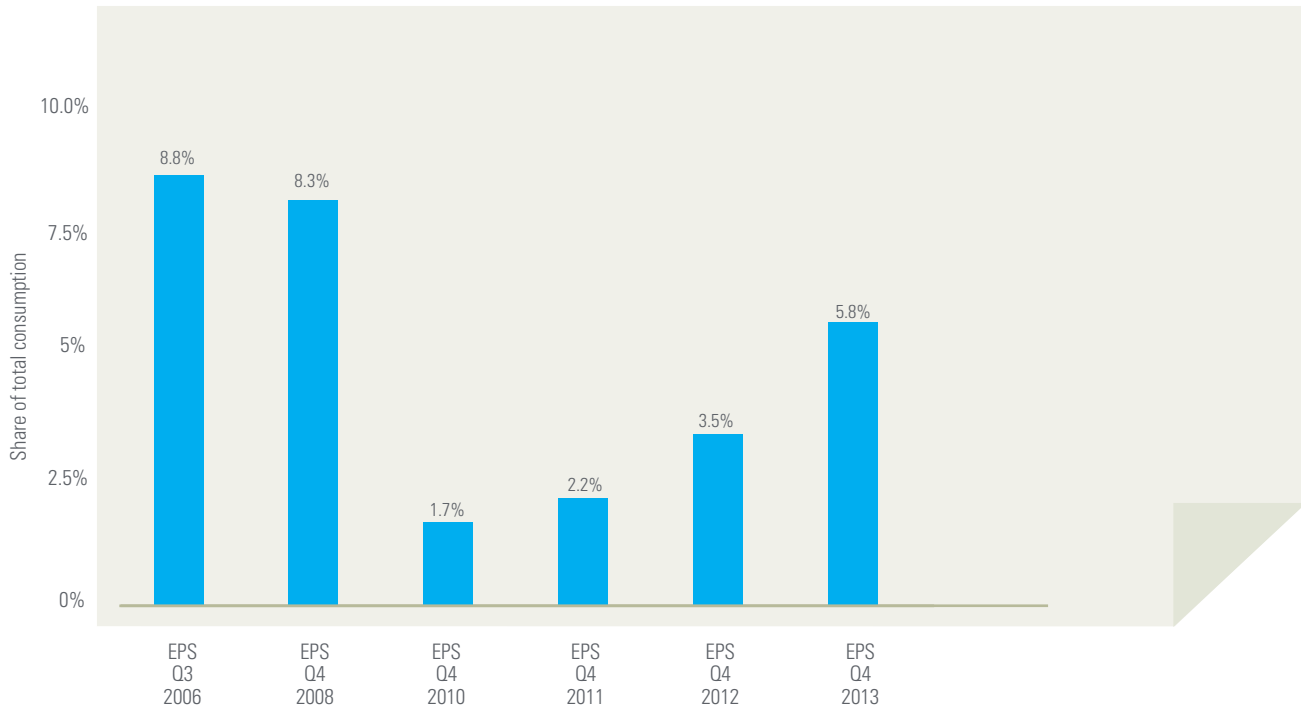
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



EPS results & EU Flow Model

Empty Pack Survey non-domestic estimates - 2006-2013 ⁽¹⁾



CYPRUS



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- The empty pack survey (EPS) in Cyprus collected 1,000 packs during the course of the year. This was undertaken in 1 wave conducted in Q4 (October)
- The sample focused on the top 4 cities in Cyprus, which covered 67.4% of the total population. The number of packs collected in each city is weighted by the city population
- No adjustments were made to the data in our analysis

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013.



CYPRUS



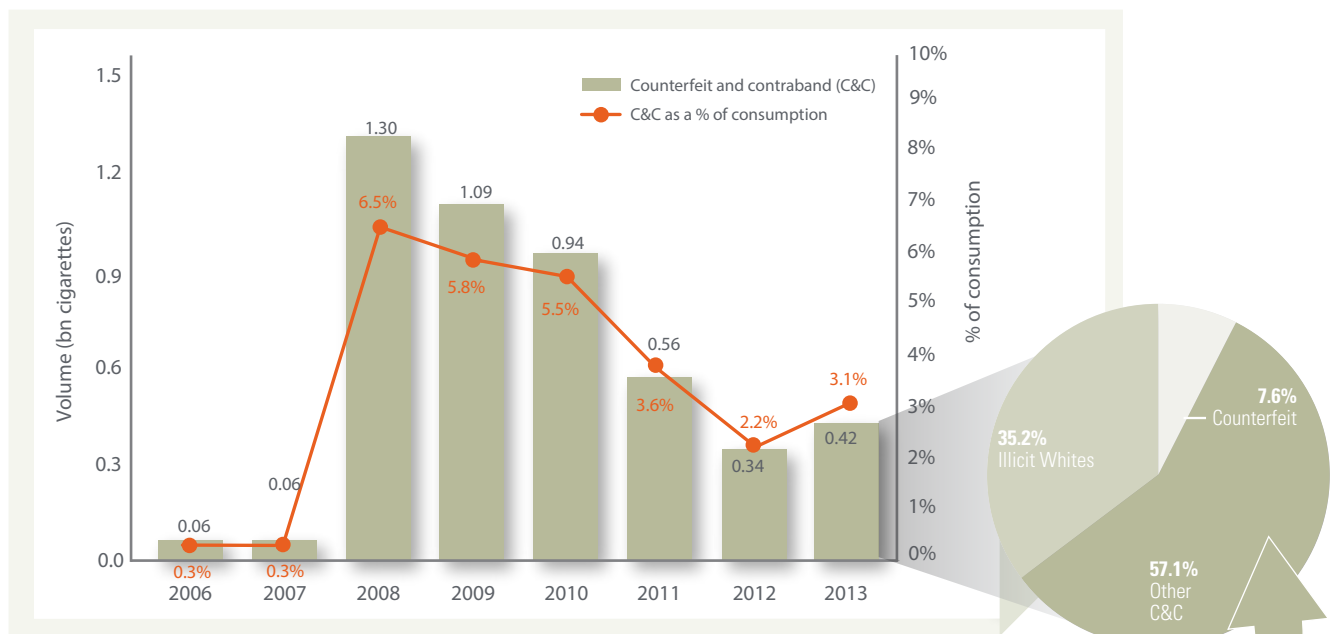
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CZECH REPUBLIC



Counterfeit & Contraband increased, partially driven by growth in Illicit Whites

Manufactured cigarette C&C volumes and share of overall consumption 2006-13

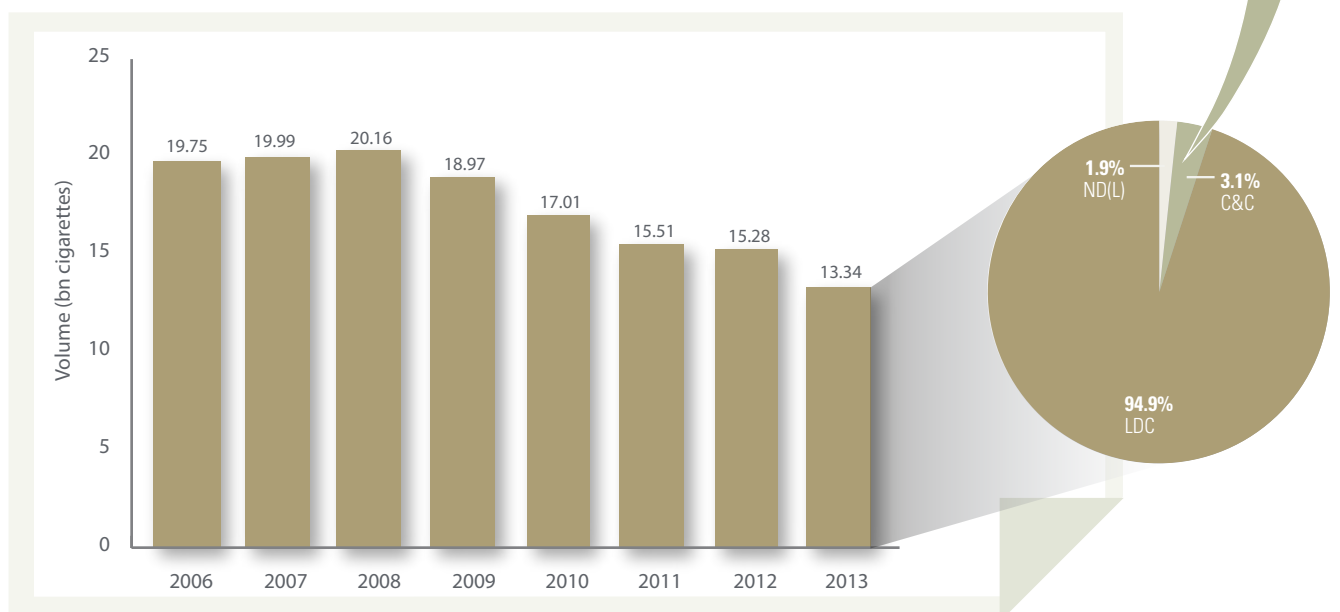


CZECH REPUBLIC

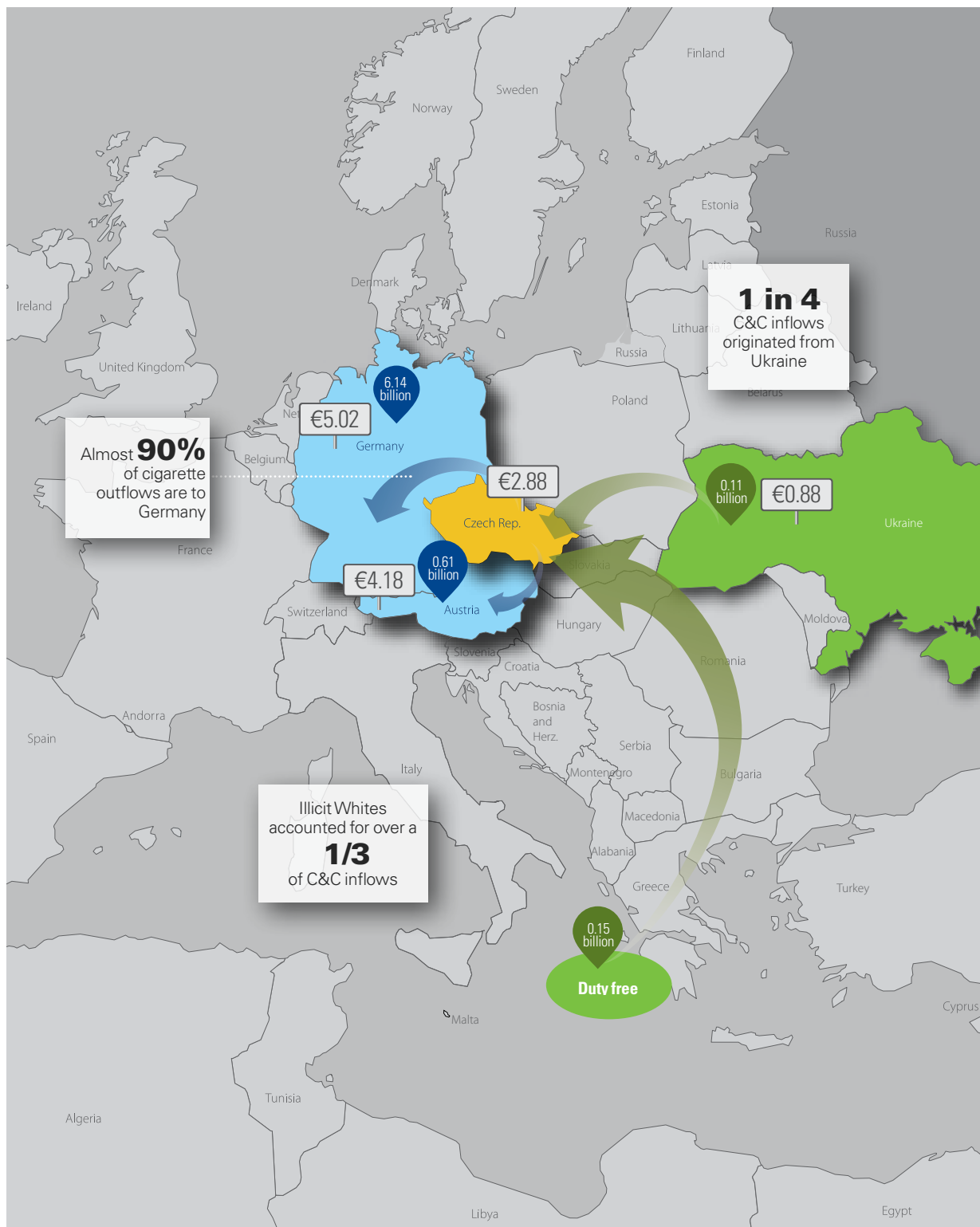


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Manufactured cigarette consumption 2006-13



KEY INFLOWS AND OUTFLOWS



CZECH REPUBLIC



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Main outflow

Main inflow

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

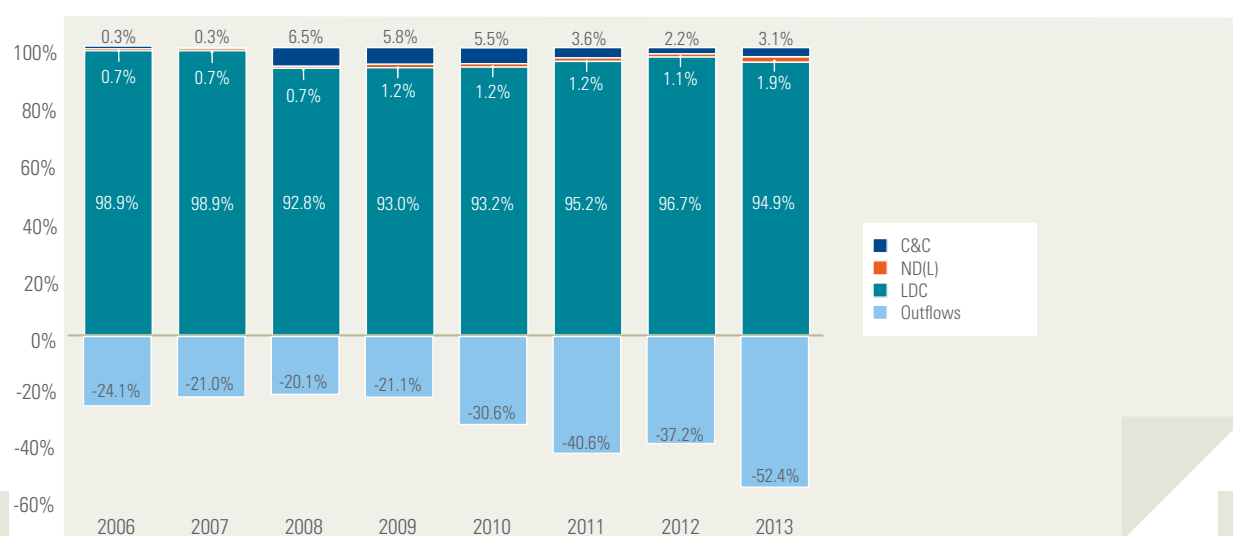
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Total consumption declined in the Czech Republic, while outflow volumes increased substantially

Total manufactured cigarette consumption – Czech Republic^{(1)(2)(a)}

TOTAL CZECH REPUBLIC CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	24.31	23.97	22.77	21.65	21.06	21.06	20.46	19.65	(4)%
Outflows	-4.76	-4.19	-4.06	-4.00	-5.21	-6.30	-5.68	-6.99	23%
Legal domestic consumption (LDC)	19.54	19.78	18.71	17.65	15.85	14.76	14.78	12.67	(14)%
Non-domestic legal (ND(L))	0.15	0.15	0.15	0.23	0.21	0.19	0.16	0.26	57%
Counterfeit and contraband (C&C)	0.06	0.06	1.30	1.09	0.94	0.56	0.34	0.42	25%
Total non-domestic	0.21	0.21	1.45	1.32	1.15	0.75	0.50	0.68	35%
Total consumption	19.75	19.99	20.16	18.97	17.01	15.51	15.28	13.34	(13)%

Share of Czech Republic cigarette consumption by type - 2006-2013⁽¹⁾⁽²⁾



Total consumption of manufactured cigarettes fell by 12.7% in the year in comparison to only a 4.0% decline in legal domestic sales (LDS); an increase in outflows is the major reason for this difference

- The overall economic environment remained challenging
 - The level of unemployment increased, growing almost 1% in the year to 7.7%⁽³⁾
 - GDP per capita may remain depressed until approximately 2016, despite a marginal increase in 2013. There was also a decline in PDI, following a prior year fall⁽⁴⁾
- Legal OTP volumes have increased in recent years⁽⁵⁾, suggesting there may have been some switching by consumers

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) 2014 Economist Intelligence Unit. (4) Euromonitor, downloaded January 2014. (5) European Commission releases for consumption of fine cut tobacco, 2002-2012.



Outflows grew as a share of total consumption, largely accounted for by increased flows to Germany and Austria

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWS TO CZECH REPUBLIC									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	0.08	0.08	0.18	0.12	0.21	0.14	0.12	0.15	26%
Ukraine	0.06	0.06	0.69	0.71	0.51	0.25	0.16	0.11	(334)%
Belarus	0.00	0.00	0.00	0.03	0.04	0.11	0.05	0.10	>100%
Poland	0.01	0.01	0.12	0.09	0.06	0.03	0.01	0.05	>100%
Russia	0.01	0.01	0.05	0.12	0.07	0.06	0.05	0.03	(25)%
Counterfeit								0.08	n/a
Other	0.05	0.06	0.41	0.25	0.27	0.16	0.12	0.15	27%
Total inflows	0.21	0.21	1.45	1.32	1.15	0.75	0.50	0.68	35%

Total inflows remain low as a share of total consumption, although volumes increased this year

- Having declined between 2008 and 2012, there was an upturn in total inflows in 2013, with the largest volumes originating from cheaper Eastern European markets
- The relative importance of these Eastern European flows continued to evolve this year, as inflows from Poland and Belarus grew, whilst Ukrainian and Russian inflows fell again
- "Other" inflows reflect smaller volumes from EU markets such as Slovakia and Italy as well as inflows from non-EU markets such as Serbia
- Total Duty Free inflows grew in the year, with the Illicit Whites with Duty Free labelling increasing as a proportion of this total and now representing almost two fifths of total Duty Free flows. The main brand sold as an Illicit Whites appears to be Jin Ling, with smaller volumes of Esse and 821

Total outflows by destination country – 2006-2013⁽¹⁾

OUTFLOWS FROM CZECH REPUBLIC									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Germany	3.77	3.28	3.53	3.53	4.66	5.69	5.01	6.14	23%
Austria	0.17	0.16	0.20	0.23	0.25	0.47	0.47	0.61	31%
UK	0.21	0.29	0.11	0.07	0.03	0.04	0.06	0.06	5%
Other	0.61	0.47	0.22	0.17	0.27	0.10	0.15	0.17	16%
Total outflows	4.76	4.19	4.06	4.00	5.21	6.30	5.68	6.99	23%

Having declined in 2012, total cigarette outflows increased this year to almost 7.0bn cigarettes

- This was largely a result of greater outflows to Germany, as well as larger flows to Austria
- In January 2013, excise changes drove an 8.9% increase in WAP in Poland (up from €2.28 per 20 cigarettes to €2.65) compared to a 4.2% increase in WAP in Czech Republic, resulting in a change in WAP from €2.73 to €2.88 per 20 cigarettes⁽²⁾
- As such, in markets such as Germany and Austria, the saving from purchasing Polish cigarettes compared to Czech cigarettes decreased significantly and may have contributed to the increase in outflows from Czech Republic, while those from Poland declined
- In addition, foreign exchange movements towards the end of 2013 also made the Czech origin product comparatively cheaper, encouraging outflows into more expensive neighbouring markets

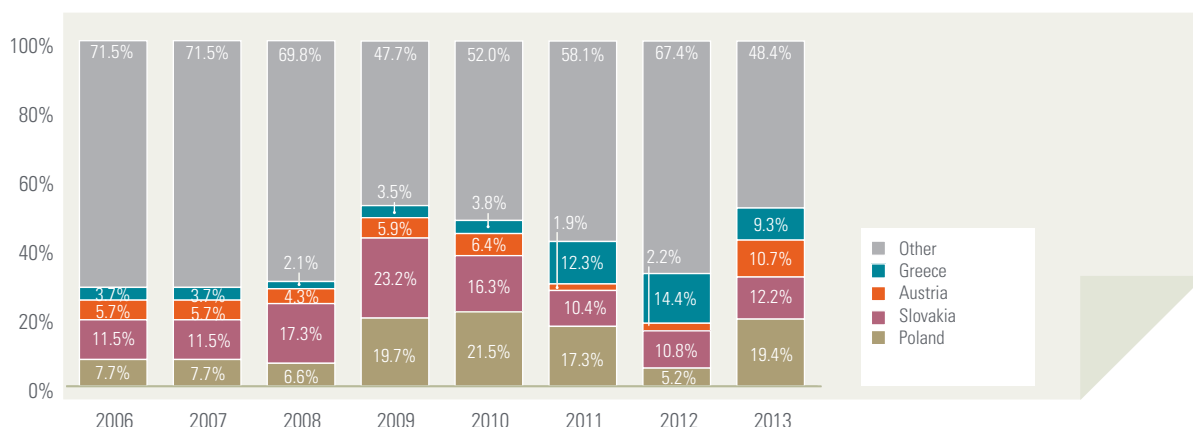
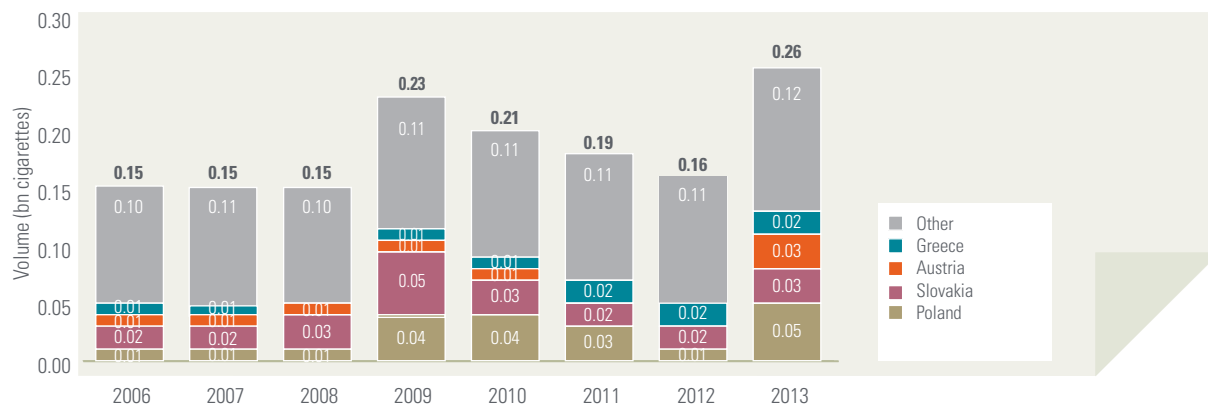
Notes: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model. (2) EC Excise Duty tables (Part III – Manufactured Tobacco).



ND(L) flows remain low, likely due to comparable or higher prices for cigarettes in bordering markets

ND(L) by origin - 2006-2013^{(1)(2)(a)(b)}



CZECH REPUBLIC



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Non-domestic legal (ND(L)) volumes increased by 57.2% in 2013, largely due to greater inflows from neighbouring markets, but remained small as a proportion of total consumption

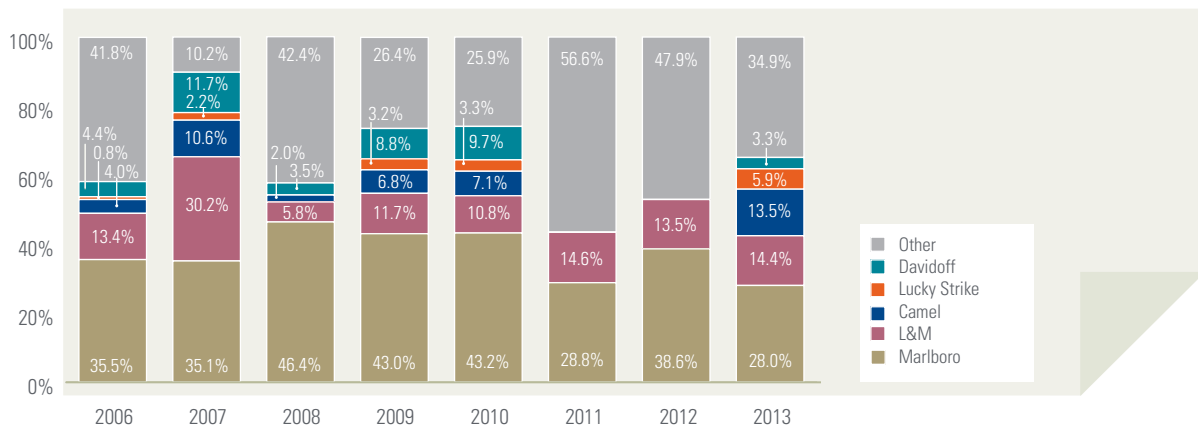
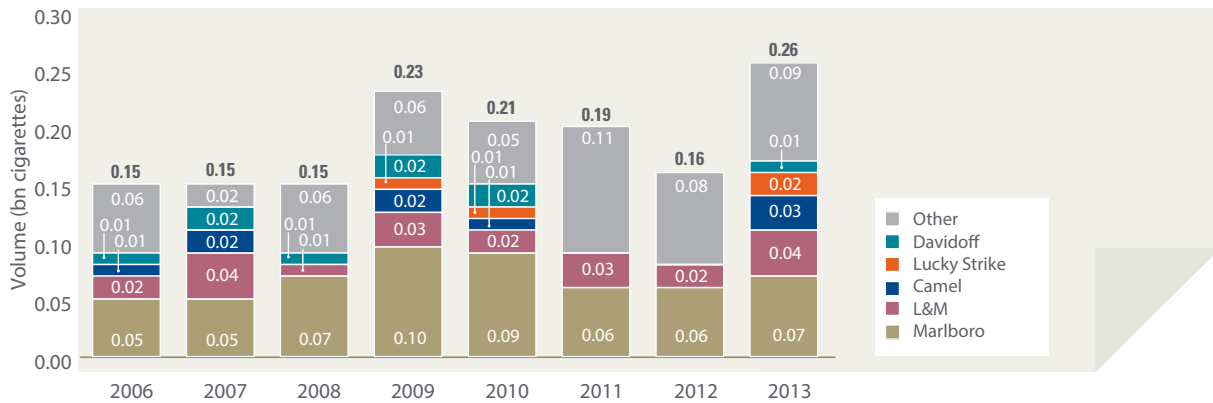
- Legal volumes from Poland increased considerably. Based on growth in outbound tourism to Poland and the fact that prices between the two markets broadly equalised this year (based on WAP⁽³⁾), all of these flows were assumed to be legal
- Legal inflows of Slovakian cigarettes also grew, and based on significant and growing outbound tourism (c. 1.5m trips⁽⁴⁾) and a marginally higher price in the Slovakian market, all of these flows were assumed to be legal
- Other legal flows of manufactured cigarettes arose from Austria and Greece, both of which are higher priced than Czech Republic and see large inbound tourist flows from the country⁽⁴⁾

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) EC Excise Duty tables (Part III – Manufactured Tobacco). (4) UN WTO Tourism Factbook 2008-2012, UN WTO.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013^{(1)(2)(a)}



Flows from bordering markets such as Slovakia, Germany and Poland, account for most of the inflows of the largest brands such as Marlboro and L&M

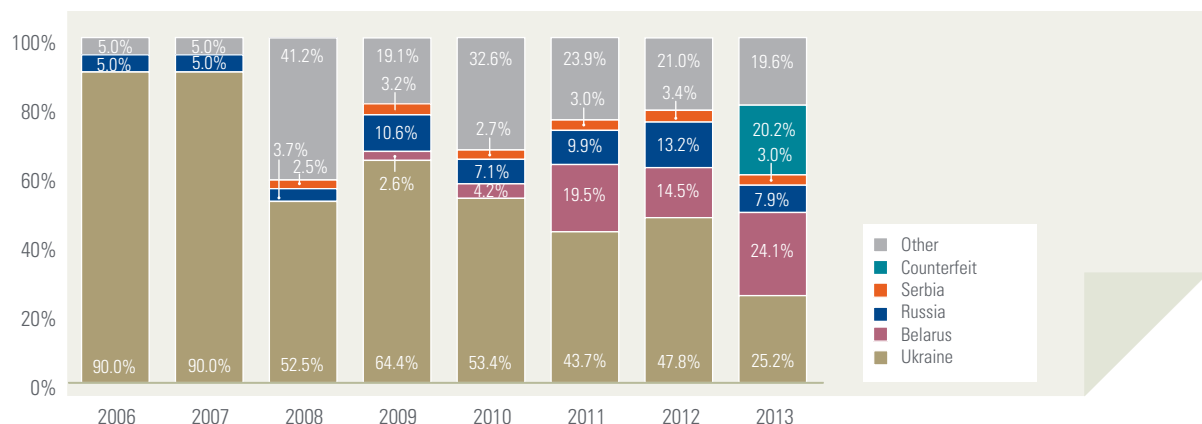
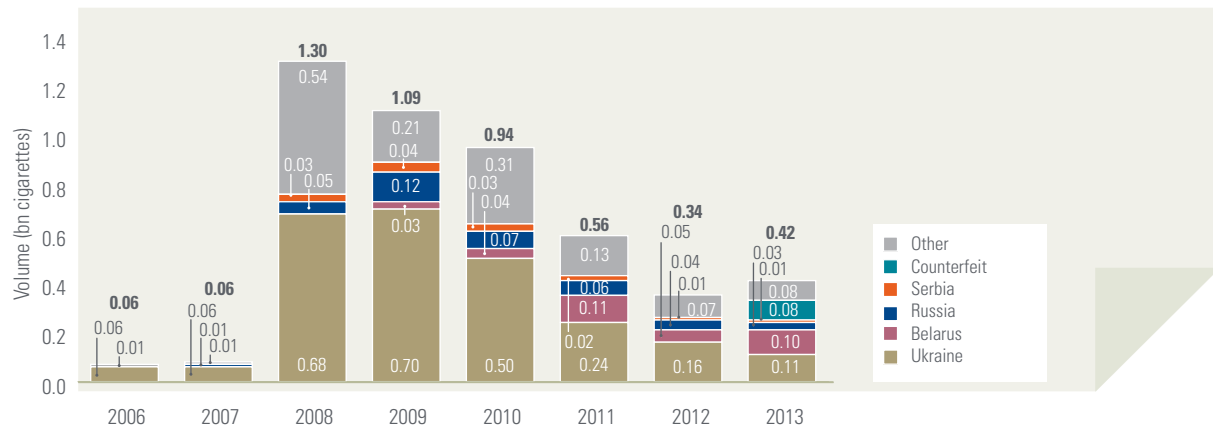
- Marlboro has the highest legal inflow volume and this is likely as a result of it being the most available brand
- “Other” inflows comprise smaller volumes of around 40 other brands

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

C&C inflows increased, mainly driven by the Grodno Tobacco brands from Belarus

C&C by origin - 2006-2013^{(1)(2)(a)(b)}



CZECH REPUBLIC



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Counterfeit and contraband (C&C) inflows increased this year, both in terms of volumes and share of consumption

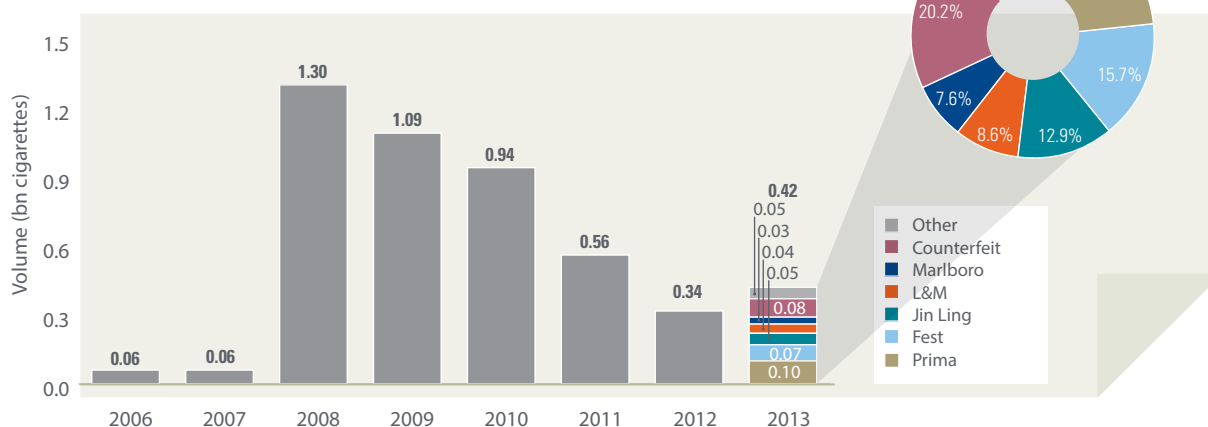
- As a result of consumer research and tourist data highlighting low outbound tourism to countries such as Ukraine and Belarus⁽³⁾, almost all of the inflows from these markets are allocated to C&C
- The Empty Pack Survey (EPS) results highlighted a greater incidence of cigarettes from Belarus (especially into Brno and Ostrava in the East and into the capital, Prague); the majority of the inflows were products manufactured by the Grodno Tobacco Company
- Seizures of manufactured cigarettes also increased versus prior year. The Czech Customs Annual Report details seizures up from 6m cigarettes in 2012 to 35m cigarettes in 2013, which is the highest level reported since 2009⁽²⁾
- Counterfeit cigarette volumes are a relatively large issue in the Czech Republic, representing 20.2% of total C&C flows this year
- If these cigarettes had been legally purchased in the Czech Republic the tax revenue gained would have been approximately €45m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-2012, UN WTO.

C&C INFLOWS BY BRAND

C&C by brand - 2006-2013^{(1)(2)(a)}



The overall incidence of Grodno Tobacco brands grew in the year

- Illicit Whites appear to be a relatively significant issue in the Czech Republic, with consumption this year accounting for 35.2% of total C&C volumes. The largest Illicit Whites brand consumed were Fest (an Illicit Whites with Belarusian health warning) and Jin Ling (an Illicit Whites with Duty Free labelling)
- The Fest brand recorded the highest incidence in the Czech EPS
- Inflows of Jin Ling with Duty Free labelling increased
- Consumption of as many as 25 other Illicit Whites brands was evident, in much smaller volumes

Breakdown of Illicit Whites by type - 2007-2013^{(1)(2)(a)(b)}

LABELLING OF ILLICITWHITES INFLOWS TO CZECH REPUBLIC								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.00	0.02	0.11	0.07	0.12	0.05	0.09	73%
Duty Free	0.00	0.00	0.00	0.01	0.02	0.04	0.05	56%
Unspecified	0.00	0.00	0.00	0.00	0.00	0.00	0.00	n/a
Total Illicit Whites	0.00	0.03	0.12	0.08	0.14	0.09	0.15	70%

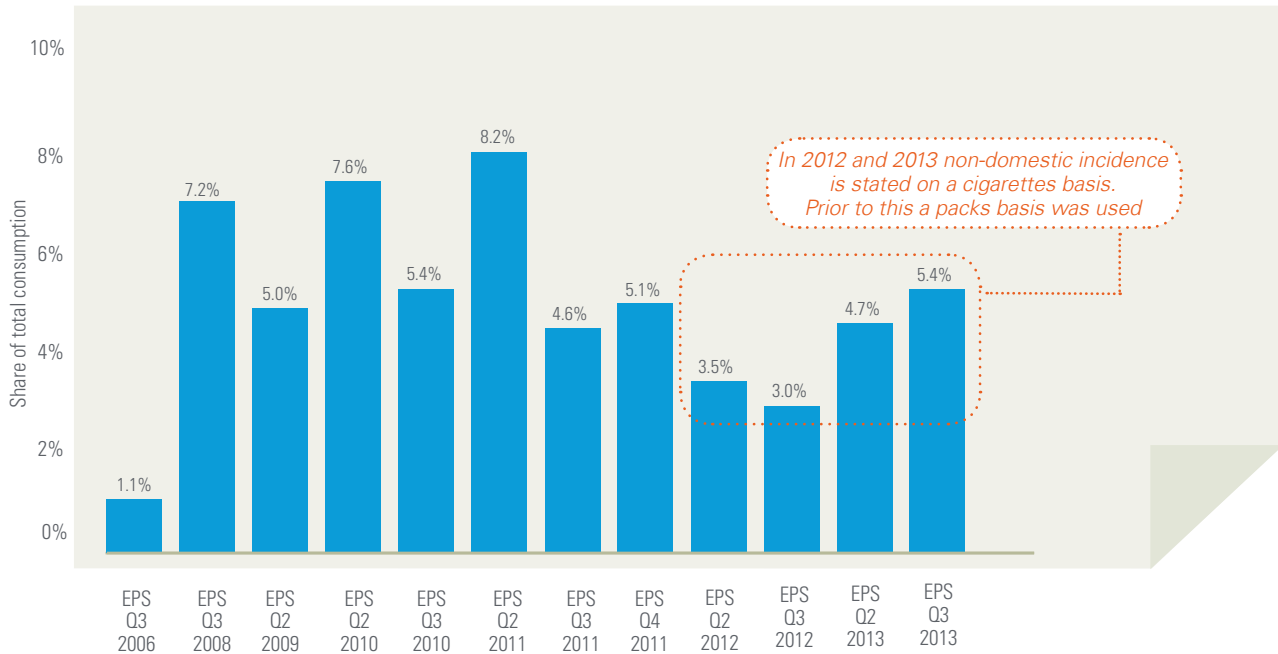
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



EPS results and EU Flows Model

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



CZECH REPUBLIC



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- The empty pack survey in the Czech Republic collected 21,004 packs during the course of the year. This was undertaken through two waves, one conducted in Q2 (April) and one in Q3 (September / October). Each wave collected 10,502 packs across the 30 largest cities. The number of packs collected in each city is weighted by the city population

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

ND(L) volume calculations and explanations

KPMG non domestic legal flows Czech Republic

USE OF CONSUMER RESEARCH AND ANY ADJUSTMENTS FOR 2013 DATA							
Country	ND 2013 (bn sticks) ⁽¹⁾	Total trips where cigarettes purchased (m) ⁽²⁾⁽³⁾	Number of packs per trip (m)	Total packs (m)	Data sources ⁽²⁾⁽³⁾⁽⁴⁾	2013 ND(L) (bn sticks)	% of ND
Poland	0.05	0.45	7	3.02	Consumer research, WTO, WAP pricing tables	0.05	>100%
Slovakia	0.02	0.72	2	1.57	Consumer research, WTO, WAP pricing tables	0.03	>100%

- To estimate the legal element of inflows from Poland, consumer research formed the basis of the calculation for the legal component of flows. This was then updated for a decline in outbound tourism⁽³⁾ and relative price changes (to adjust the average number of packs brought back per trip). On this basis, the legal element was estimated as 0.05bn cigarettes, which is marginally above 100% of the total non-domestic inflow
- In the case of Slovakia, consumer research has also been used. This consumer research implies legal volumes exceed total non-domestic incidence however as the flow is considered immaterial, no capping is applied

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

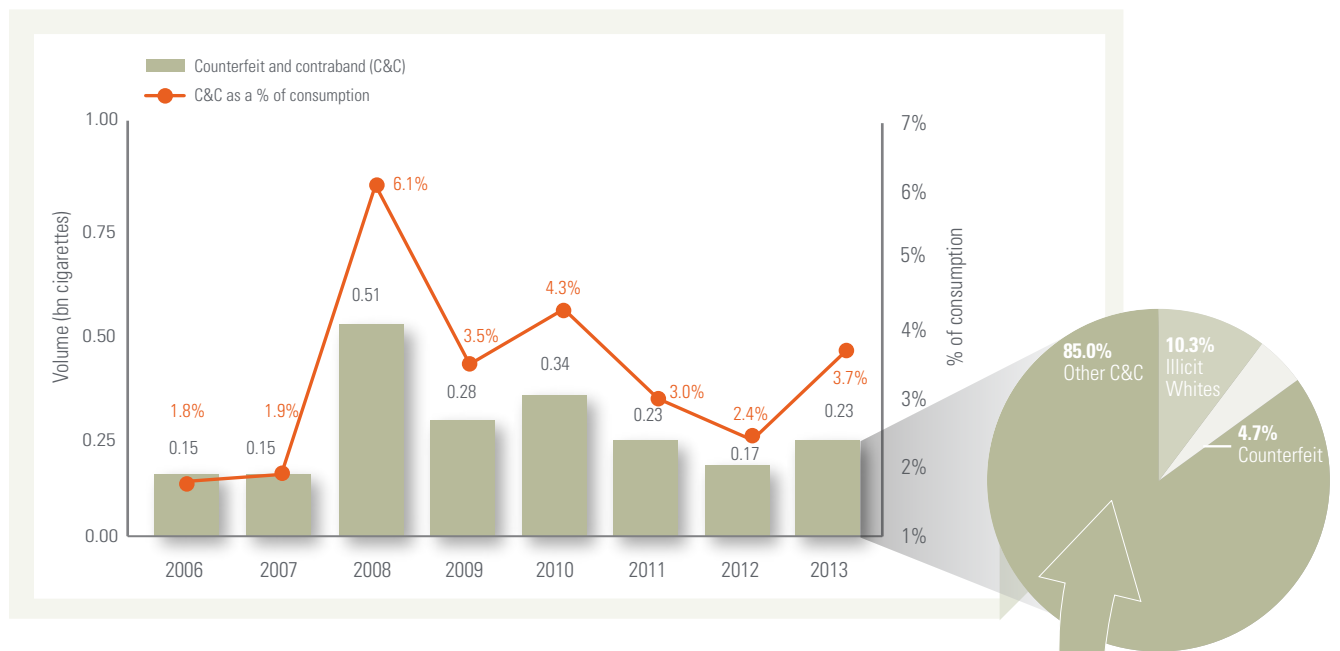
Sources: (1) KPMG EU Flows Model. (2) Synovate/Ipsos ND(L) research 2013. (3) UN WTO Tourism Factbook 2008-2012, UN WTO. (4) EC Excise Duty tables (Part III – Manufactured Tobacco).





Counterfeit and contraband is a relatively small share of total consumption

Manufactured cigarette C&C volumes and share of overall consumption 2006-13

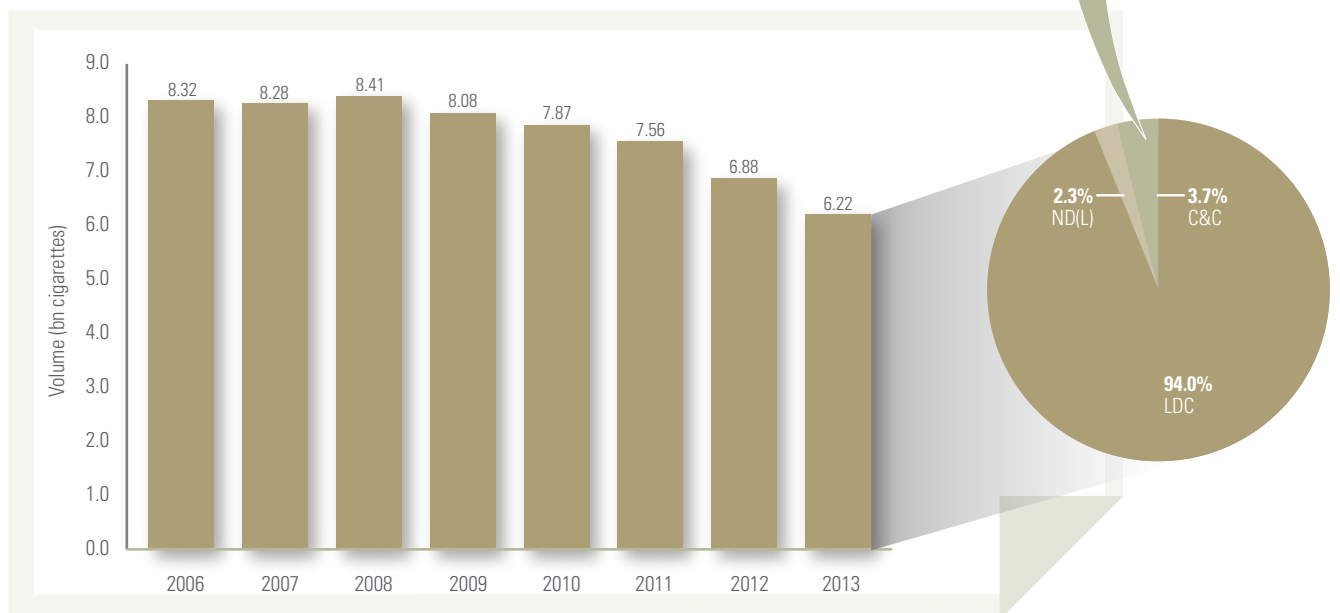


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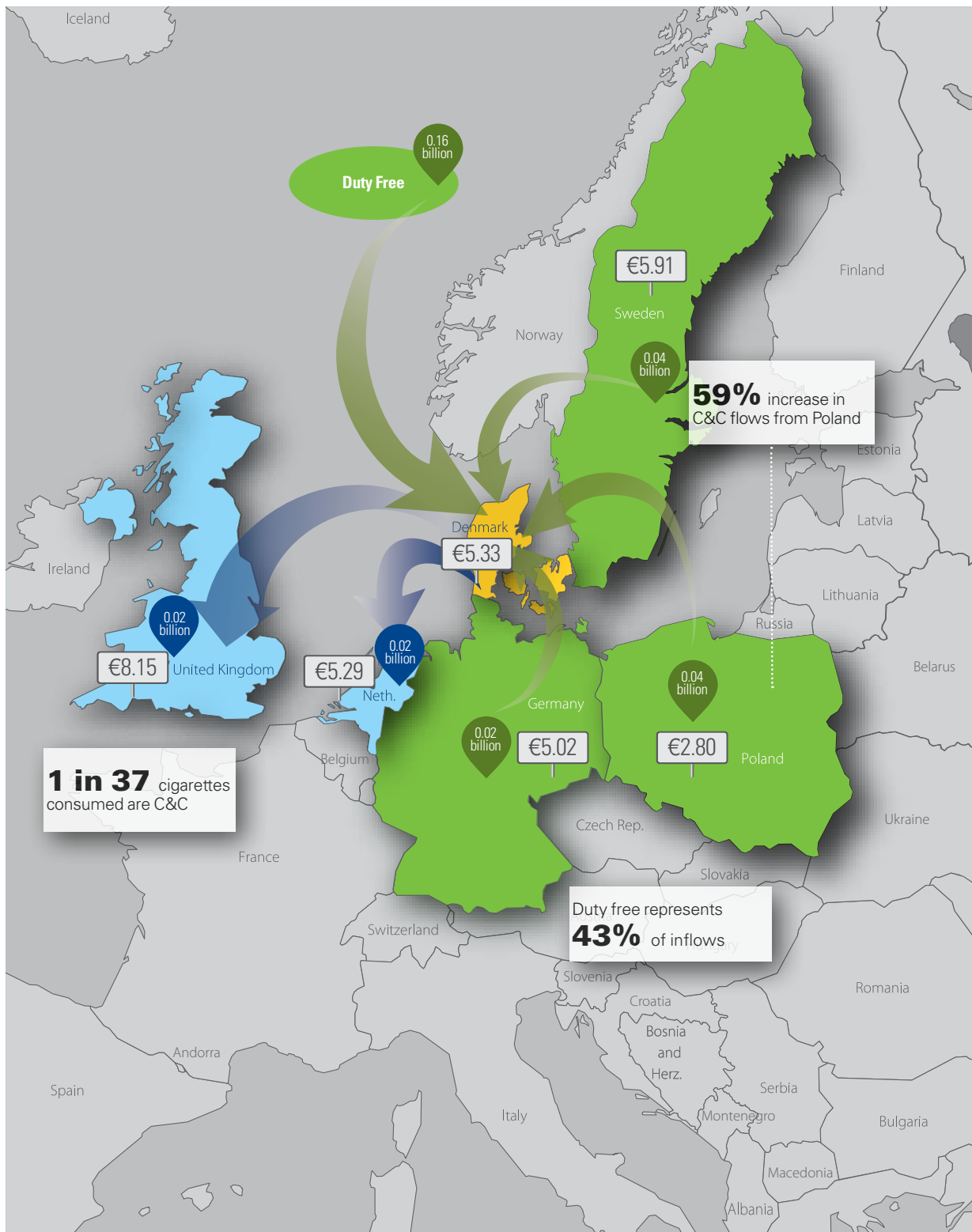


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Manufactured cigarette consumption 2006-13



KEY INFLOWS AND OUTFLOWS



DENMARK



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Main outflow

Main inflow

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

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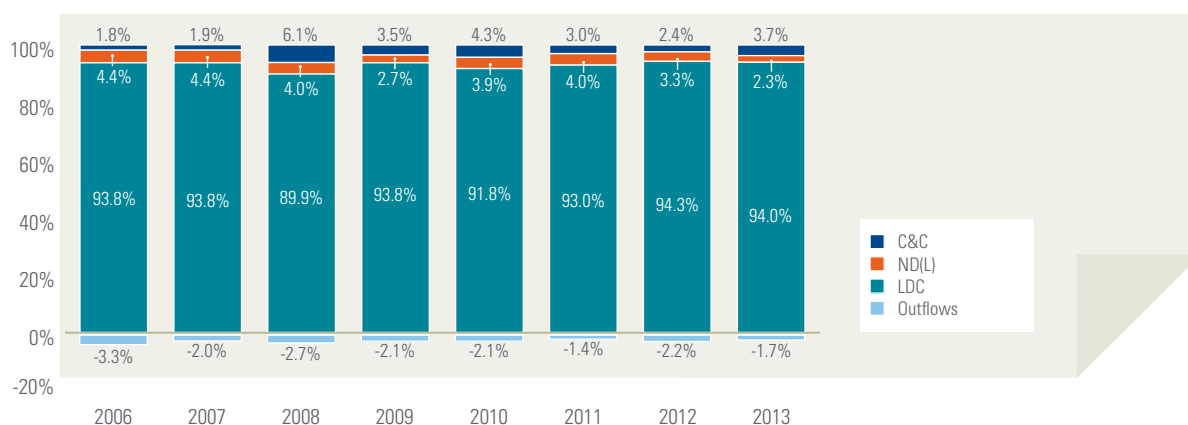
Total consumption declined, despite a sharp increase in counterfeit and contraband volumes

Increase in C&C driven by increased packs collected from lower priced countries such as Poland and Lithuania

Total manufactured cigarette consumption – Denmark⁽¹⁾⁽²⁾

TOTAL DENMARK CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	8.08	7.93	7.79	7.75	7.39	7.13	6.64	5.95	(10)%
Outflows	-0.28	-0.17	-0.23	-0.17	-0.17	-0.10	-0.15	-0.10	(33)%
Legal domestic consumption (LDC)	7.80	7.76	7.56	7.58	7.22	7.03	6.48	5.85	(10)%
Non-domestic legal (ND(L))	0.36	0.36	0.34	0.22	0.31	0.30	0.23	0.14	(37)%
Counterfeit and contraband (C&C)	0.15	0.15	0.51	0.28	0.34	0.23	0.17	0.23	37%
Total non-domestic	0.52	0.51	0.85	0.50	0.65	0.53	0.39	0.37	(6)%
Total consumption	8.32	8.28	8.41	8.08	7.87	7.56	6.88	6.22	(10)%

Share of Denmark cigarette consumption by type 2006-2013⁽¹⁾⁽²⁾



Overall consumption of manufactured cigarettes declined by 10% as both legal domestic sales (LDS) and overall non-domestic consumption declined by 10% and 6% respectively

- The decline of non-domestic legal consumption appears to have been offset by growth in counterfeit and contraband, as flows from neighbouring countries appear to have been offset by flows from countries where counterfeit and contraband (C&C) is more prevalent
- During 2013 the WAP rose by 1.4%⁽³⁾, although taxes remained the same throughout

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) EC Excise Duty tables (Part III – Manufactured Tobacco) as at January 2013/ January 2014.



InfloWS to Denmark from neighbouring countries were replaced by Duty Free and Poland flows

Total inflows by country of origin 2006-2013^{(1)(a)}

No Duty Free flows were Illicit Whites brand

ND INFLOWSTO DENMARK									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	0.20	0.20	0.24	0.21	0.20	0.14	0.13	0.16	20%
Poland	0.04	0.04	0.07	0.03	0.03	0.03	0.02	0.04	59%
Sweden	0.10	0.10	0.10	0.05	0.17	0.11	0.04	0.04	(5)%
Germany	0.03	0.02	0.06	0.04	0.03	0.05	0.06	0.02	(61)%
Lithuania	0.00	0.00	0.00	0.02	0.01	0.01	0.01	0.01	>100%
Counterfeit								0.01	n/a
Other	0.15	0.15	0.38	0.15	0.22	0.19	0.13	0.09	(35)%
Total inflows	0.52	0.51	0.85	0.50	0.65	0.53	0.39	0.37	(6)%

Whilst non-domestic inflows decreased by 6% between 2012 and 2013, flows increased from Poland and Lithuania, along with a slightly higher Duty Free flow

- The increase in Duty Free cigarettes mainly came from the brand Prince
- Poland became the largest inflow country in 2013 as volumes increased by over 50%; inflows from Sweden were broadly stable
 - Both the increase in Polish visitors to Denmark for work and tourism along with a price difference of €2.53 (based on WAP)² are likely to have had an impact on the increase in flows
- Flows from Germany have declined as prices in both countries are €0.31⁽²⁾ different, resulting in little incentive to buy over the border

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM DENMARK									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Netherlands	0.05	0.02	0.02	0.01	0.05	0.02	0.02	0.02	27%
UK	0.03	0.01	0.03	0.05	0.00	0.01	0.02	0.02	(7)%
Sweden	0.17	0.07	0.08	0.03	0.05	0.01	0.03	0.01	(53)%
Germany	0.03	0.02	0.04	0.04	0.04	0.03	0.03	0.01	(61)%
Other	0.00	0.04	0.06	0.04	0.04	0.03	0.05	0.03	(41)%
Total outflows	0.28	0.17	0.23	0.17	0.17	0.10	0.15	0.10	(33)%

Outflows decreased by 33% in 2013 as flows to neighbouring countries with similar prices fell

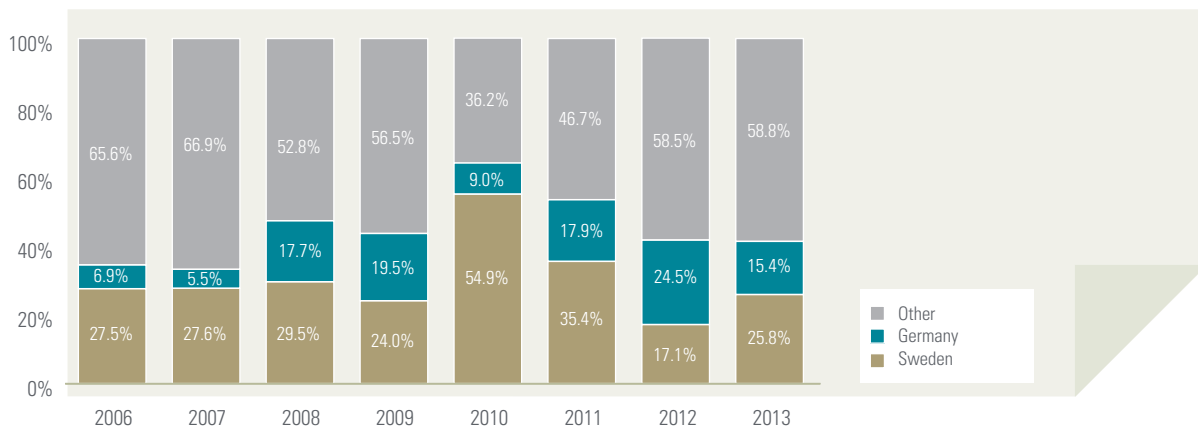
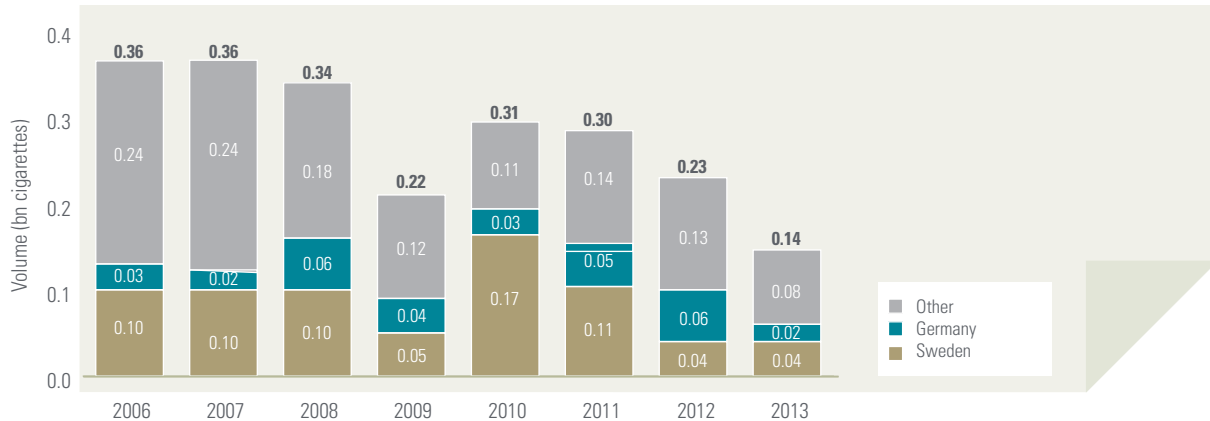
- Outflows to Sweden and Germany, which previously represented the greater shares of outflows from Denmark, declined over 50% in 2013
- This may be explained by the limited price differences between each country, and by lower levels of cigarette consumption in both countries

Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Source: (1) KPMG EU Flows Model. (2) EC Excise Duty tables (Part III – Manufactured Tobacco) as at January 2013/ January 2014 Duty tables (Part III – Manufactured Tobacco).

Markets bordering Denmark represent the main sources of non-domestic legal consumption

ND(L) by origin - 2006-2013^{(1)(2)(a)(b)}



DENMARK



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Non-domestic legal consumption (ND(L)) declined as a share of total consumption 2013

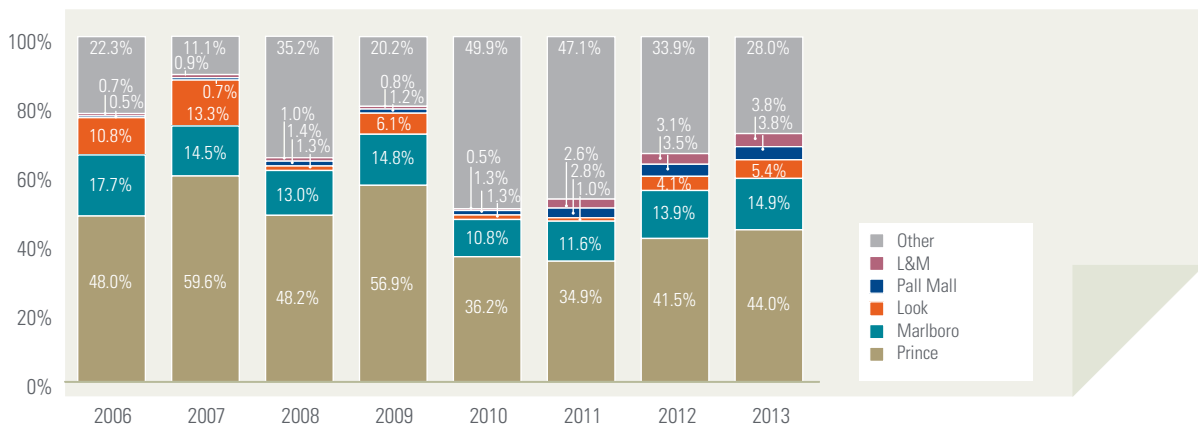
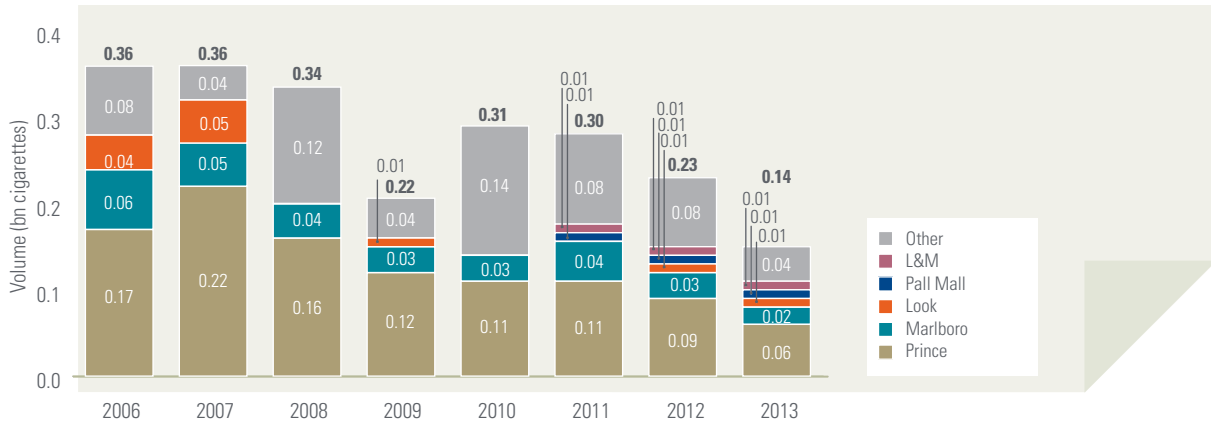
- Flows from Sweden, typically generated by Swedish tourists visiting Denmark, continued to decline
- Flows from Germany also declined as prices between each country are similar
- Being similar or higher priced markets⁽³⁾, all flows from Germany and Sweden are considered as ND(L)

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) EC Excise Duty tables (Part III – Manufactured Tobacco) as at January 2013/January 2014.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand 2006-2013^{(1)(2)(a)}



The percentage decline in ND(L) inflows was relatively consistent between the top 5 brands, although the most popular brands historically continued to represent a relatively high share of volumes

- Prince and Marlboro continued to account for over 50% of total ND(L) inflows in Denmark
- “Other” legal inflows consist of smaller volumes of 34 other brands

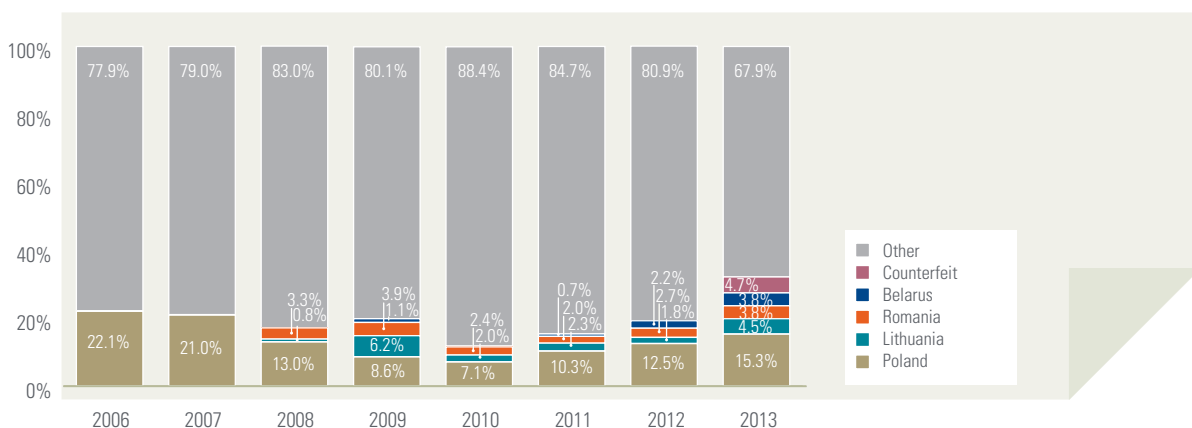
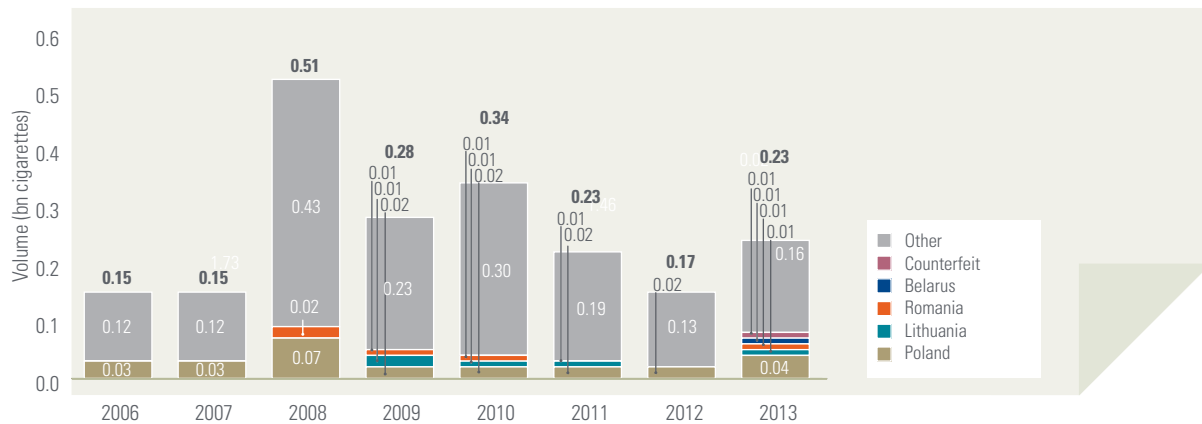
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



Counterfeit and contraband volumes increased, mainly driven by higher volumes from Poland

C&C by origin 2006-2013^{(1)(2)(a)}



DENMARK



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C&C consumption increased as a share of total consumption in 2013

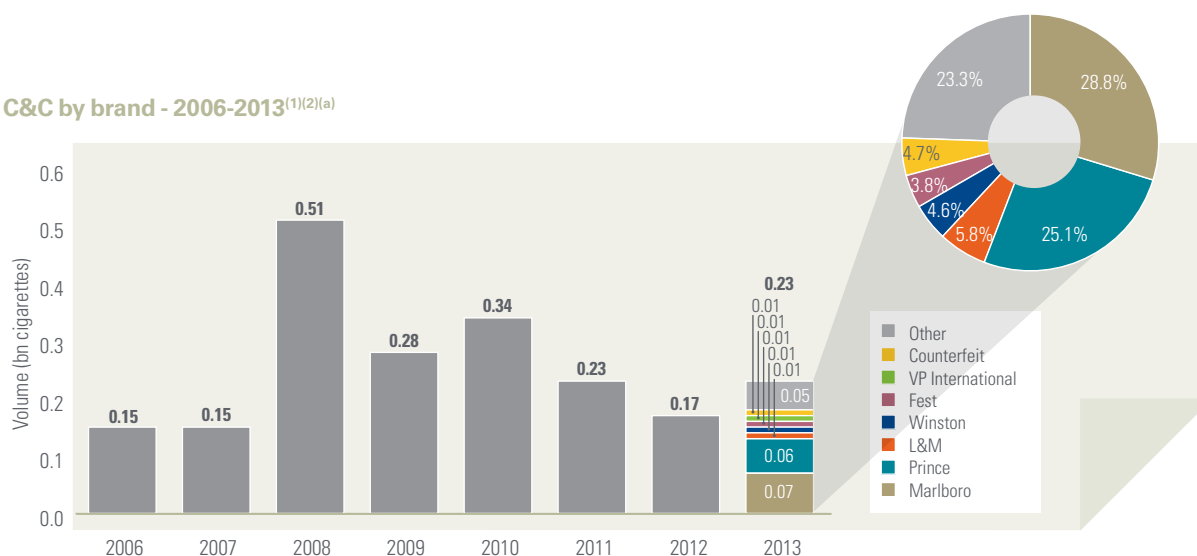
- Poland became the largest non-domestic inflow country in 2013, with 89% of total flows allocated as and C&C
 - Whilst consumer research historically showed that those who travel to Poland do bring back cigarettes, both the number of trips and number of packs brought back were low compared with the total number of cigarettes
 - The number of reported trips in the consumer research was 14,185, which was the equivalent of 15% of total trips made from Denmark to Poland⁽³⁾
 - Analysis of the consumer research and travel data showed that 11% of the flows into Poland were legal purchases, thus the remaining was classified as C&C
- Travel data showed very few trips were made to Lithuania and Romania, meaning that the majority of flows were categorised as C&C
- The consumer research did not identify any trips to Belarus, thus all inflows were classified as C&C

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UNWTO Tourism Factbook 2008-2012, UNWTO.

C&C INFLOWS BY BRAND

C&C by brand - 2006-2013^{(1)(2)(a)}



Contraband inflows accounted for the majority of C&C consumption in Denmark

- The largest contraband brand was Marlboro which came from many locations, followed by Prince
- Winston predominantly originated from Lithuania and Poland
- Counterfeit cigarettes represented 4% of total C&C consumption
- If the total volume of C&C had been consumed legally within the Danish market, an additional tax revenue of approximately €49 million would have been raised by the Danish Treasury

Breakdown of Illicit Whites by type 2006-2013^{(1)(2)(a)(b)}

COMPOSITION OF ILLICIT WHITES INFLOWS TO DENMARK								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country Specific	0.000	0.023	0.029	0.009	0.019	0.013	0.022	69%
Duty Free	0.000	0.000	0.000	0.002	0.001	0.006	0.000	(100%)
Unspecified	0.000	0.000	0.000	0.004	0.000	0.001	0.001	88%
Total Illicit Whites	0.000	0.023	0.029	0.014	0.020	0.020	0.024	19%

Consumption of Illicit Whites brands increased by 57% in 2013 but still only accounted for 10% of C&C

- Major Illicit Whites brands were Fest and VP International, which originated from Belarus and Romania respectively
- There were also some brands with unspecified labelling such as Manchester

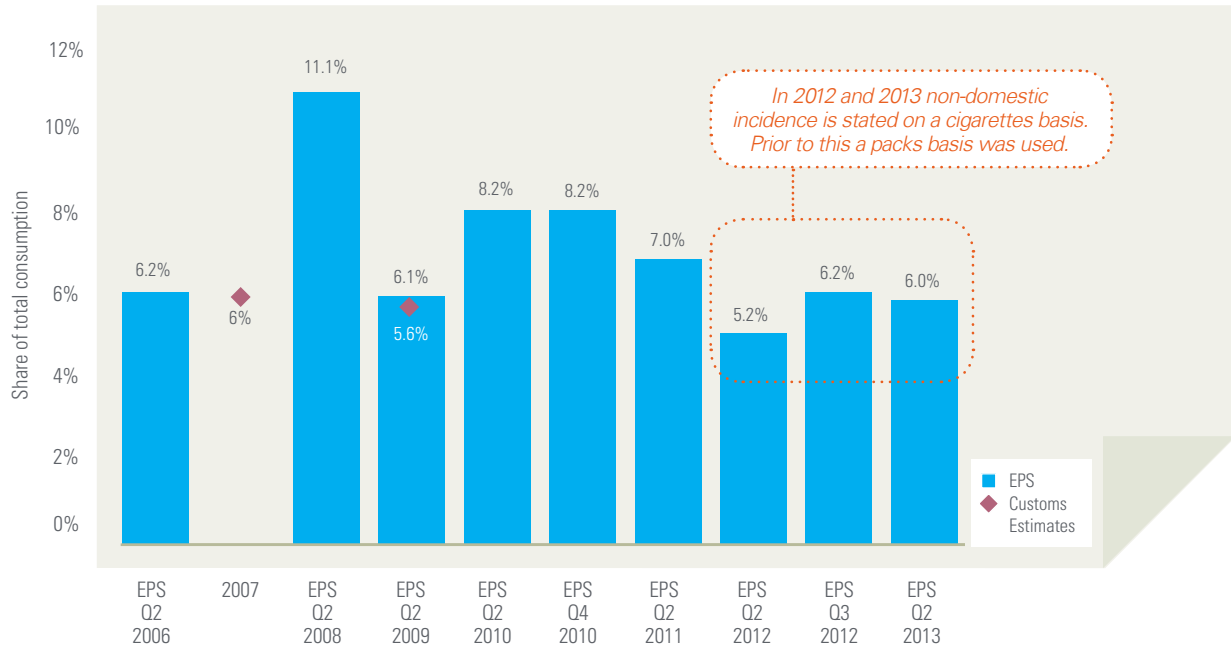
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



EPS results & EU Flow Model

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



DENMARK



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The empty pack survey (EPS) in Denmark collected 5,300 packs during the course of the year. This included an additional focus collection of 300 packs.

- The EPS was undertaken in 1 wave conducted in Q2 (June). The sample focused on 6 principal cities and 2 focus cities. The number of packs collected in each city is weighted by the city population
- No adjustments were made to the data

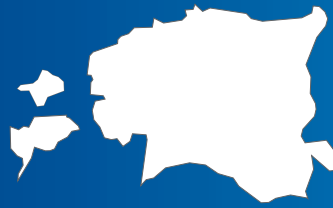
Sources: (1) MSIIntelligence Empty Pack Surveys, 2006 – 2013.



DENMARK

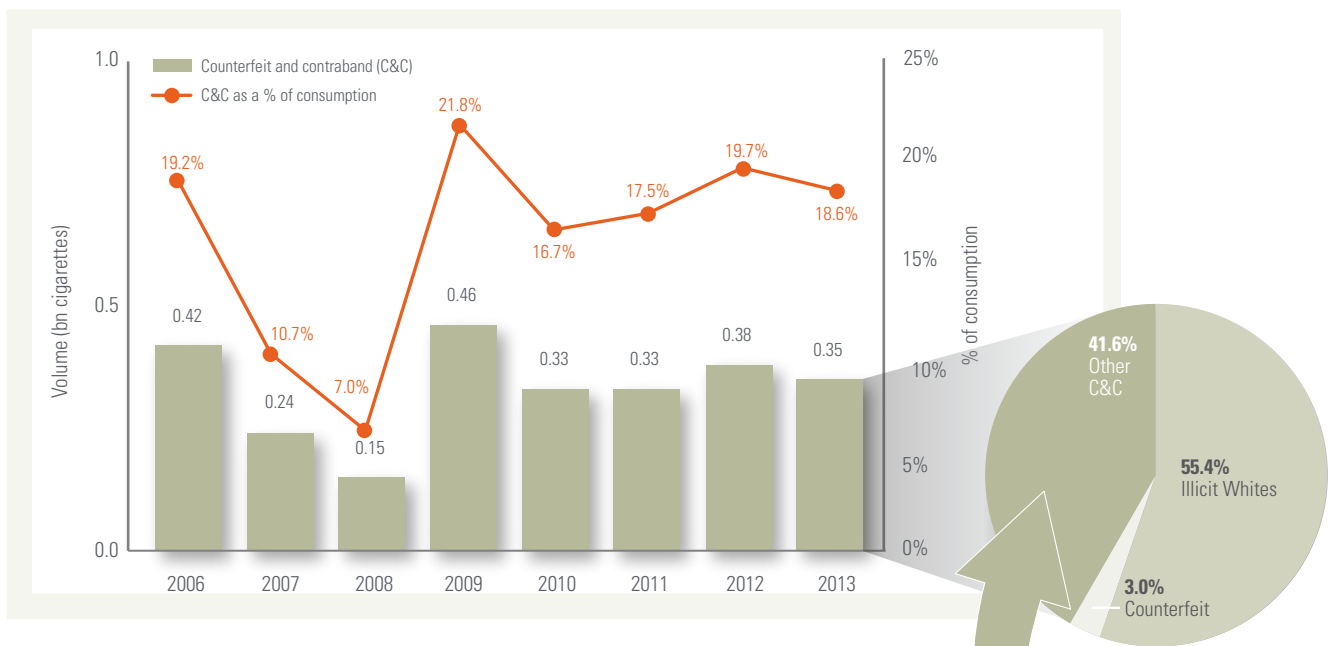


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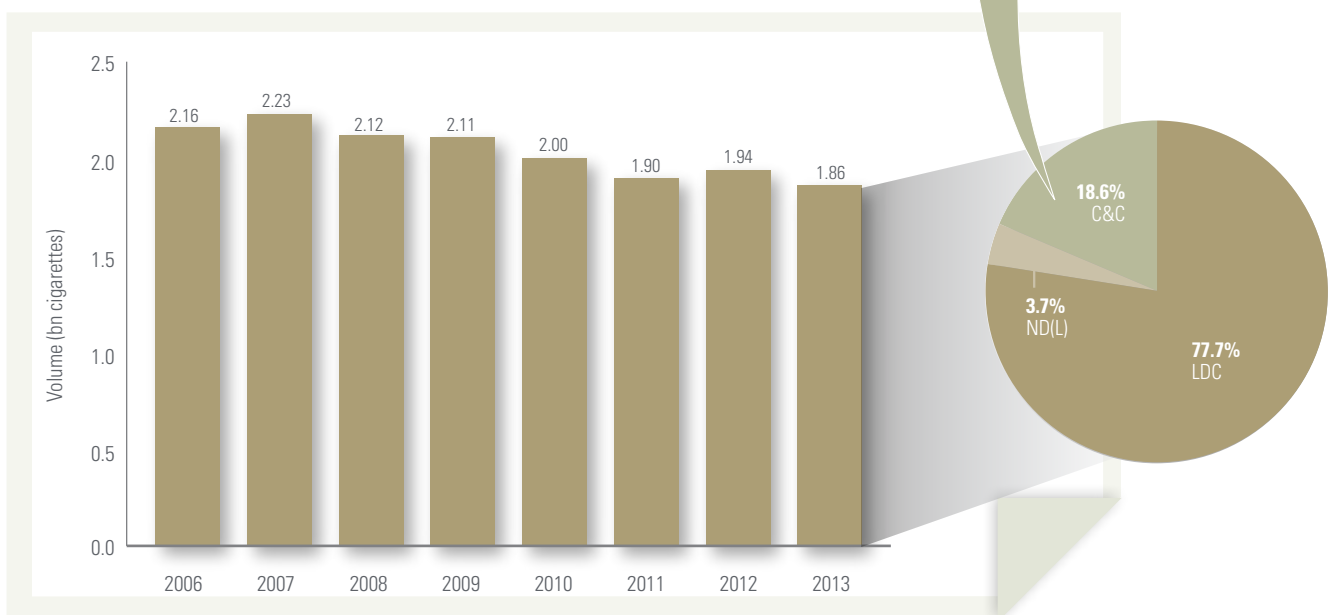


Illicit Whites were the largest component of Counterfeit & Contraband volumes

Manufactured cigarette C&C volumes and share of overall consumption 2006-13



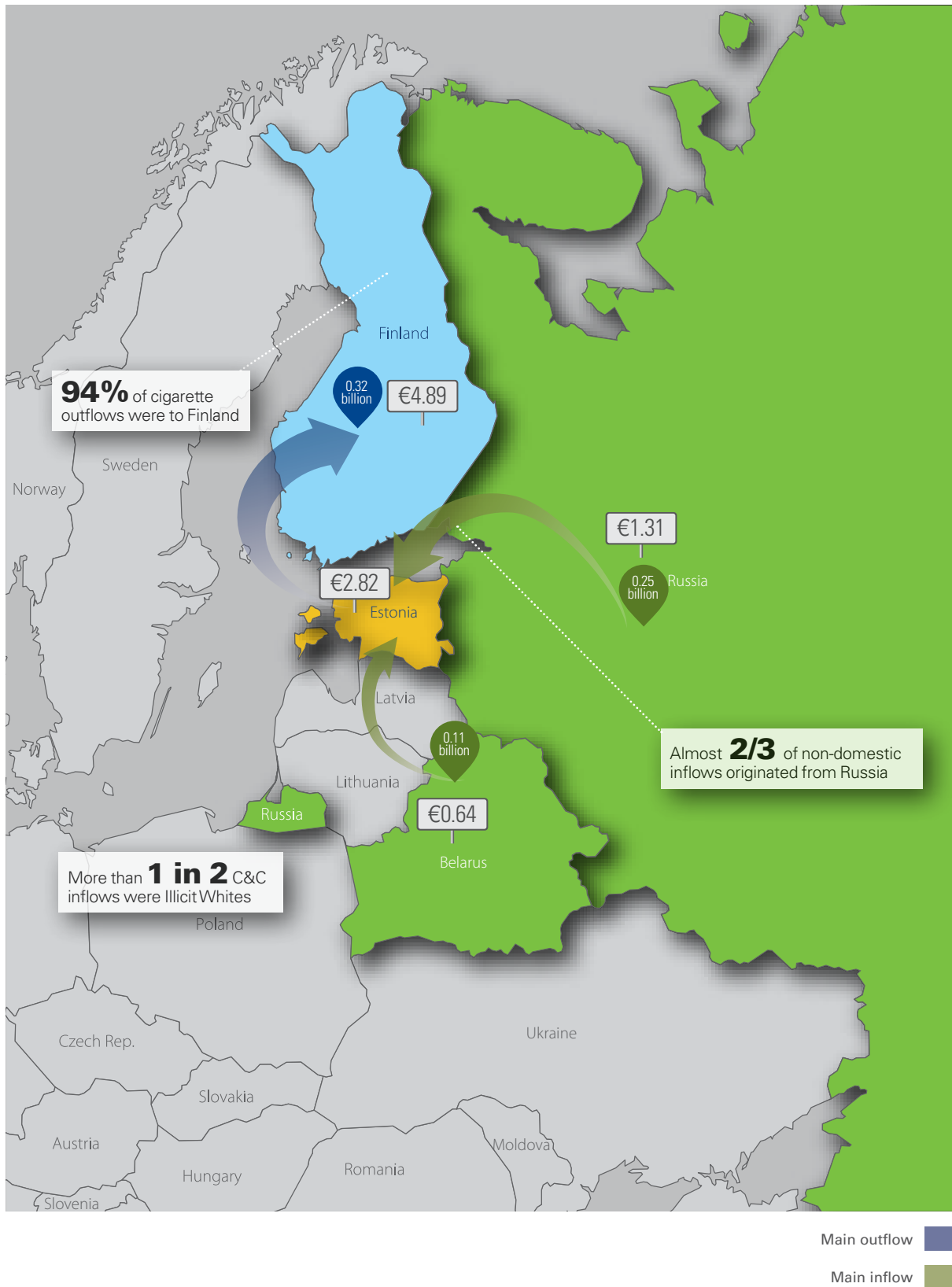
Manufactured cigarette consumption 2006-13



ESTONIA

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KEY INFLOWS AND OUTFLOWS



ESTONIA

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Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

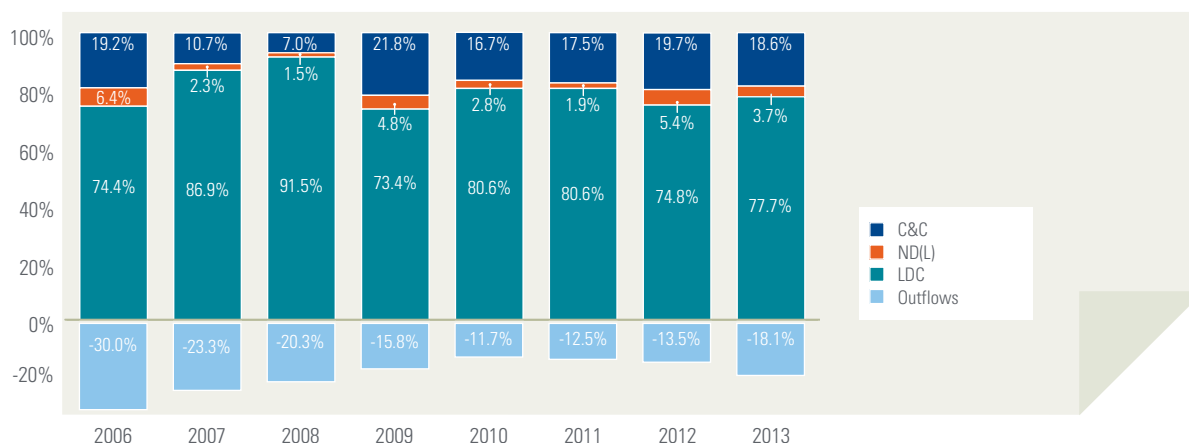
Source: (1) KPMG EU Flows Model.

Total cigarette consumption fell as inflows declined and outflows increased significantly

Total manufactured cigarette consumption – Estonia^{(1)(2)(a)}

TOTAL ESTONIA CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	2.26	2.46	2.37	1.89	1.85	1.77	1.71	1.78	4%
Outflows	-0.65	-0.52	-0.43	-0.33	-0.24	-0.24	-0.26	-0.34	29%
Legal domestic consumption (LDC)	1.61	1.94	1.94	1.55	1.61	1.53	1.45	1.44	(1)%
Non-domestic legal (ND(L))	0.14	0.05	0.03	0.10	0.06	0.04	0.10	0.07	(34)%
Counterfeit and contraband (C&C)	0.42	0.24	0.15	0.46	0.33	0.33	0.38	0.35	(10)%
Total non-domestic	0.55	0.29	0.18	0.56	0.39	0.37	0.49	0.41	(15)%
Total consumption	2.16	2.23	2.12	2.11	2.00	1.90	1.94	1.86	(4)%

Share of Estonia cigarette consumption by type 2006-2013⁽¹⁾⁽²⁾



Total consumption of manufactured cigarettes declined marginally in 2013. Legal domestic sales (LDS) volumes for the period however were greater than prior year

- Sales are likely to have been supported by growth in GDP per capita in the year, up almost €1,000⁽³⁾, whilst PDI per capita also grew by 7.8% in 2013⁽⁴⁾
- Unemployment however increased marginally to 10.9%, despite having fallen in the two previous years⁽³⁾

Notes: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research (3) EIU, GDP per capita, Unemployment, 2013. (4) Euromonitor, PDI, January 2014

InfloWS are largely from neighbouring cheaper non-EU markets of Russia and Belarus; outflows to Finland grew

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWS TO ESTONIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Russia	0.22	0.23	0.14	0.51	0.36	0.30	0.38	0.25	(33)%
Belarus	0.00	0.00	0.00	0.00	0.00	0.03	0.05	0.11	>100%
Duty Free	0.05	0.01	0.02	0.02	0.01	0.02	0.04	0.03	(30)%
Latvia	0.18	0.02	0.00	0.00	0.00	0.00	0.00	0.00	52%
Finland	0.01	0.00	0.00	0.00	0.00	0.00	0.00	0.00	(40)%
Counterfeit								0.01	n/a
Other	0.09	0.02	0.01	0.03	0.01	0.01	0.01	0.01	(44)%
Total inflows	0.55	0.29	0.18	0.56	0.39	0.37	0.49	0.41	(15)%

Non-domestic (ND) inflows declined during the year and also fell as a share of total consumption

- Typically inflows originate from cheaper neighbouring market of Russia and more recently Belarus in the South. Inflows from Belarus more than doubled in the year, up from 0.05bn cigarettes in 2012 to 0.11bn in 2013. This may be due to the widening of the price differential, which increased to €1.96 per 20 cigarettes in January 2013 (from €1.85 in 2012) and remained higher throughout the year⁽²⁾
- Despite an increase in the price differential with Russia in 2013, inflows declined 33.1% to 0.25bn cigarettes. Inflows have been significant in the past, partly due to the long border between the two markets. Lower Russian inflows this year may have been the result of the increased availability of comparatively cheaper cigarettes from Belarus
- The Empty Pack Survey (EPS) showed greatest declines in Russian incidence close to the border, such as Narva and Kohtla-Järve. The highest growth in Belarusian cigarettes was also to be found in these cities. In July 2013, the WAP in Russia was €1.16 for 20 products, compared to €0.66 in Belarus⁽²⁾
- Duty Free volumes have typically been low and declined in 2013. Illicit Whites with Duty Free labelling account for only 1.9% of total Duty Free volumes and the main brand sold as Illicit Whites appears to be Jin Ling

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM ESTONIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Finland	0.43	0.25	0.25	0.27	0.21	0.20	0.21	0.32	51%
UK	0.02	0.03	0.05	0.00	0.00	0.01	0.02	0.00	(73)%
Netherlands	0.00	0.01	0.00	0.00	0.00	0.01	0.01	0.00	(71)%
Other	0.20	0.23	0.13	0.06	0.03	0.02	0.02	0.01	(53)%
Total outflows	0.65	0.52	0.43	0.33	0.24	0.24	0.26	0.34	29%

The decline in total consumption, despite growth of LDS, is in part due to greater outflows in the year

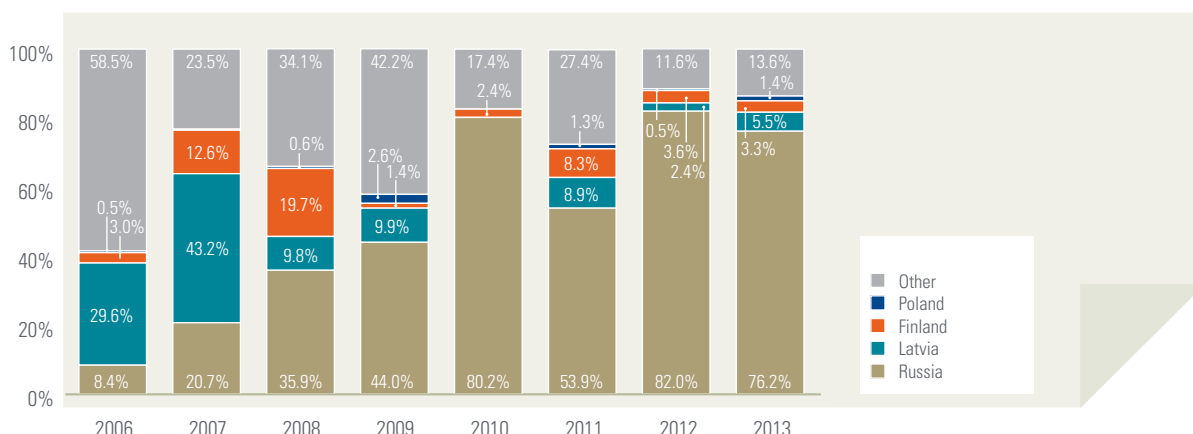
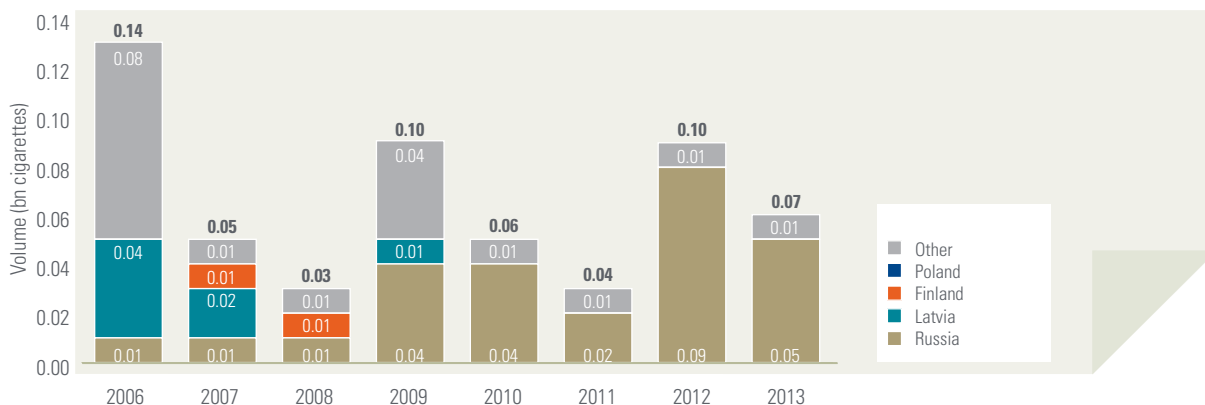
- This was almost entirely driven by greater flows to Finland. Estonian cigarette packs are almost half the price of those sold in Finland, based on the WAP. Despite a small decrease in the price differential in January 2013 (down from €2.07 per 20 cigarettes to €1.88), this then grew in July 2013, up to a high of €2.27 per 20 cigarettes⁽²⁾. The geographical proximity of the markets and the ongoing price differential means these flows continue to be relatively significant

Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model. (2) EC Excise Duty tables (Part III – Manufactured Tobacco).

ND(L) inflows declined in 2013, driven predominantly by a fall in legal inflows from Russia

ND(L) by origin 2006 - 2013^{(1)(2)(a)(b)}



ESTONIA

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Non-domestic legal ND(L) volumes in Estonia represent a relatively small share of total ND

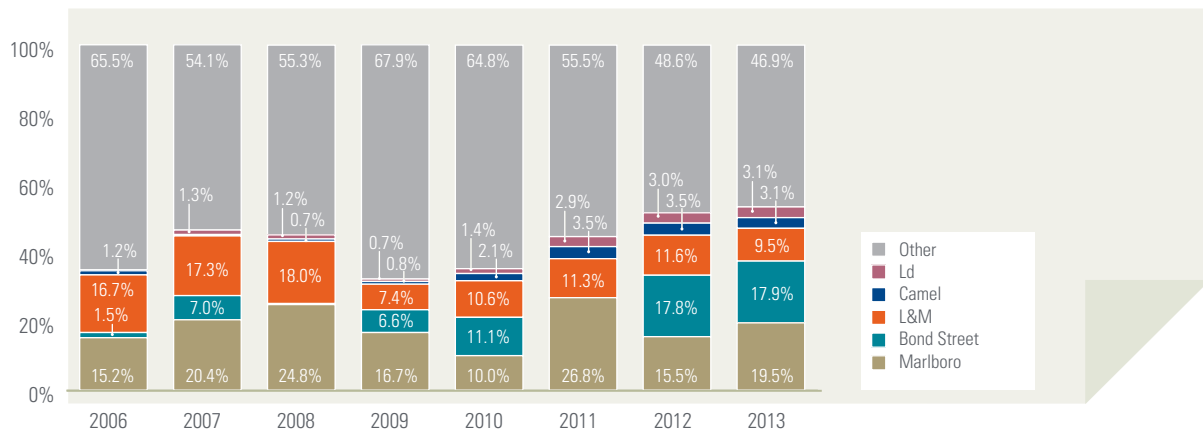
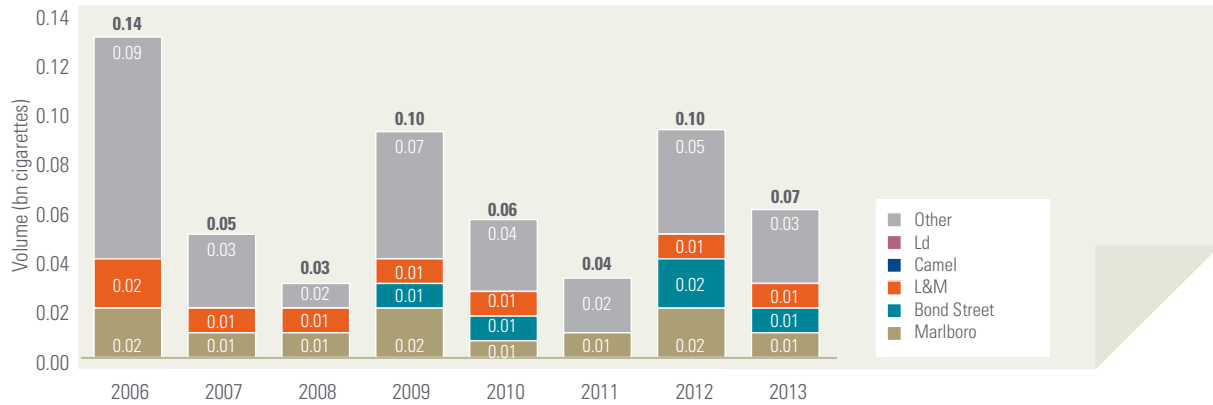
- Cigarette inflows from the bordering Latvian market and nearby Lithuania are minimal and this is likely due to low price differentials for cigarettes between these three countries
- Most inflows originate from Russia and Belarus. Consumer research indicates that travellers to Russia bring back relatively few packs per trip on average. As such, only about a fifth of inflows from Russia are allocated to ND(L)
- In contrast, there are minimal outbound tourism to Belarus⁽³⁾ and as such all of the Belarusian inflows are classed as counterfeit and contraband (C&C)
- In addition, tighter laws were introduced in 2013 which limited inflows from outside the EU. This may have had the effect of reducing non-domestic legal flows

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-2012, UN WTO.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013 ^{(1)(2)(3)(a)}



Marlboro remains the largest ND(L) flow by brand, likely due to its ease of availability in other markets

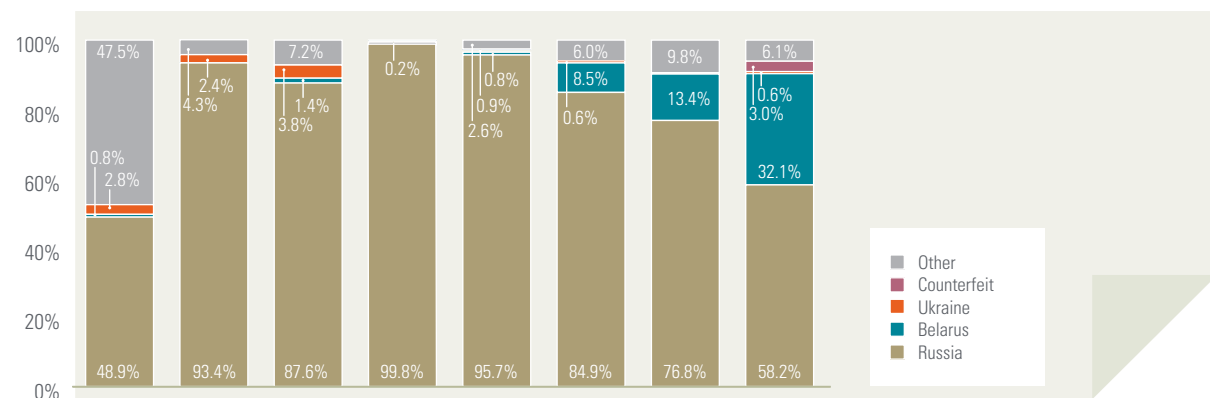
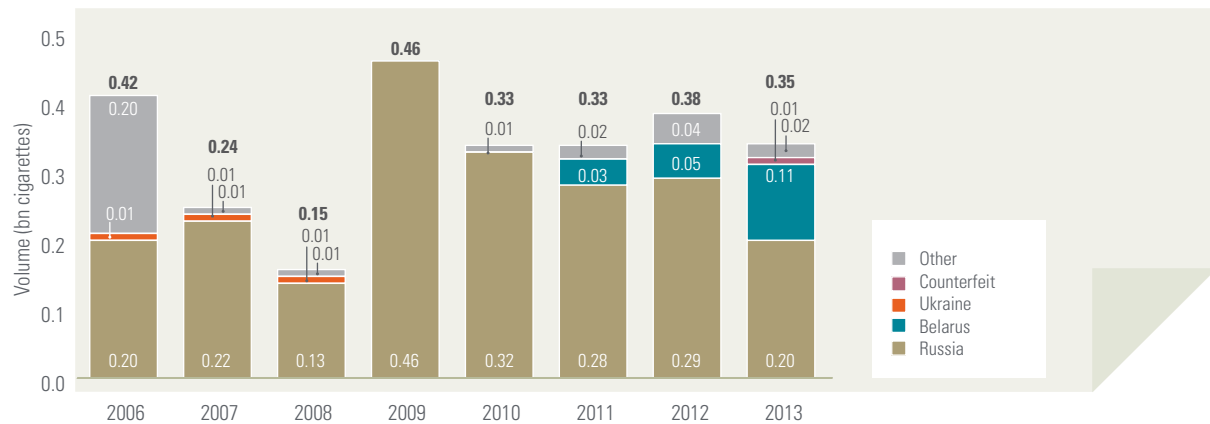
- ND(L) comprises a large number of small individual brand flows, the largest of which is Marlboro, and which declined this year by 16.5% to 0.01bn cigarettes
- “Other” comprises smaller volumes of around 50 brands

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

The decline in C&C was driven by lower volumes from Russia, partly offset by higher volumes from Belarus

C&C by origin - 2006-2013^{(1)(2)(a)(b)}



ESTONIA

C&C has historically been a greater share of total ND in Estonia, which may be due to the close proximity of cheaper non-EU markets, long borders and limited customs resources

- Russian origin cigarettes make up the largest component of C&C as outbound tourism and average packs per trip are not great enough to account for the entire Russian ND incidence per the EPS
- All flows from Belarus are allocated to C&C due to minimal outbound tourism⁽³⁾
- It appears that C&C products are widely consumed in smaller towns (and therefore likely also in rural areas) and this may be due to the relatively low incomes in those areas
- The population has traditionally shown a higher tolerance for illicit products than other EU markets. Estonia also represents one of the key transit routes for illicit products into other Eastern and then Western European markets
- Certain measures have been introduced to tackle the cross border trade, such as the renewal of border technologies. The Estonian government has also introduced an awareness campaign, focusing on educating the consumer about the risks of illicit cigarettes
- Counterfeit cigarettes are a relatively small issue (0.01bn cigarettes out of 0.35bn C&C)
- If these C&C cigarettes had been legally purchased in Estonia, the tax revenue gained would have been approximately €38m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-2012, UN WTO.

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C&C INFLOWS BY BRAND

C&C by brand - 2006-2013 ^{(1)(2)(3)(a)}



Illicit Whites account for 54% of the C&C consumption in Estonia in 2013, with large flows from both Russia and Belarus

- Inflows of More have fallen due to lower flows from Russia, but this has been in part offset by greater incidence of Bayron. The growth in flows from Belarus has resulted in growing incidence of the key Grodno Tobacco brands, such as Fest and Premier

Breakdown of Illicit Whites by type 2006-2013 ^{(1)(2)(a)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO ESTONIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.01	0.00	0.07	0.05	0.08	0.12	0.19	64%
Duty Free	0.00	0.00	0.00	0.00	0.00	0.00	0.00	59%
Unspecified	0.00	0.00	0.00	0.00	0.00	0.00	0.00	(100%)
Total Illicit Whites	0.01	0.00	0.07	0.05	0.08	0.12	0.19	64%

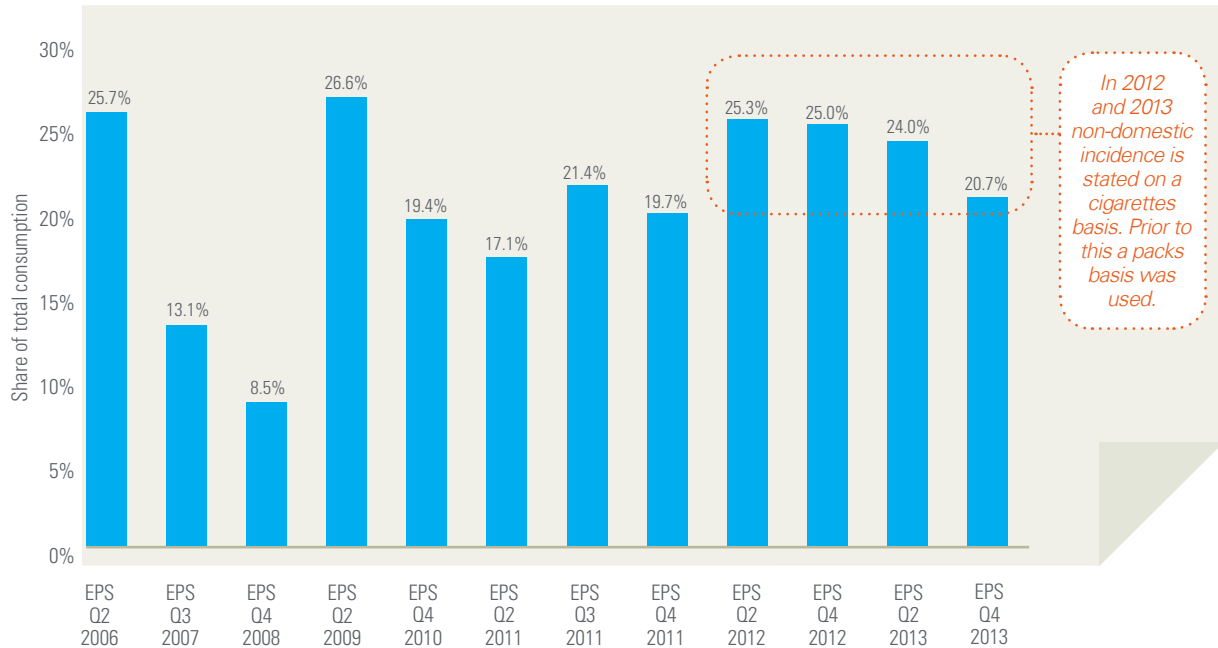
- Country specific Illicit Whites are the main component of the total Illicit Whites volumes, and the largest brands are Bayron (Russia), Fest and Premier (both Belarus)

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

EPS results and EU Flows Model

Empty Pack Survey non-domestic estimates - 2006-2013⁽¹⁾



ESTONIA



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- The EPS in Estonia collected 6,600 packs during the course of the year. This was undertaken in two waves – one conducted in Q2 (April) and one in Q4 (September / October). Each wave collected 3,300 packs across the largest 14 towns and cities. The number of packs collected in each city is weighted by the city population
- Unlike nearby Latvia and Lithuania, Estonia has a largely urban population (70% urban⁽²⁾) and following analysis of the EPS data it was not deemed necessary to re-weight the regions

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013.
 (2) Euromonitor, downloaded January 2014.

ND(L) volume calculations and explanations

KPMG non domestic legal flows Estonia

KPMG NON DOMESTIC LEGAL FLOWS ESTONIA			
Country	ND 2013 (bn sticks) (1)	2013 ND(L) (bn sticks)	% of ND
Latvia	0	0	100

USE OF CONSUMER RESEARCH AND ANY ADJUSTMENTS FOR 2013 DATA							
Country	ND 2013 (bn sticks) (1)	Total trips where cigarettes purchased (m) ⁽²⁾⁽³⁾	Number of packs per trip ⁽²⁾	Total packs (m)	Data sources ⁽²⁾⁽³⁾	2013 ND(L) (bn sticks)	% of ND
Russia	0.25	1.32	2	2.65	Consumer research, WTO	0.05	21%

- To estimate the legal element of inflow from Latvia, consumer research has been used. As this consumer research implies a legal volume greater than the total non-domestic incidence and given the materiality of the flow, this has been capped at 100% of non-domestic inflows
- In the case of Russian inflows:
 - Consumer research appeared to understate the likely number of trips to purchase cigarettes. Instead, trips were modelled as outbound travel multiplied by manufactured cigarette prevalence
 - Consumer research also appeared to understate average packs per trip. It is instead assumed that consumers bring back the legal maximum into Estonia from outside the EU, set at 2 packs

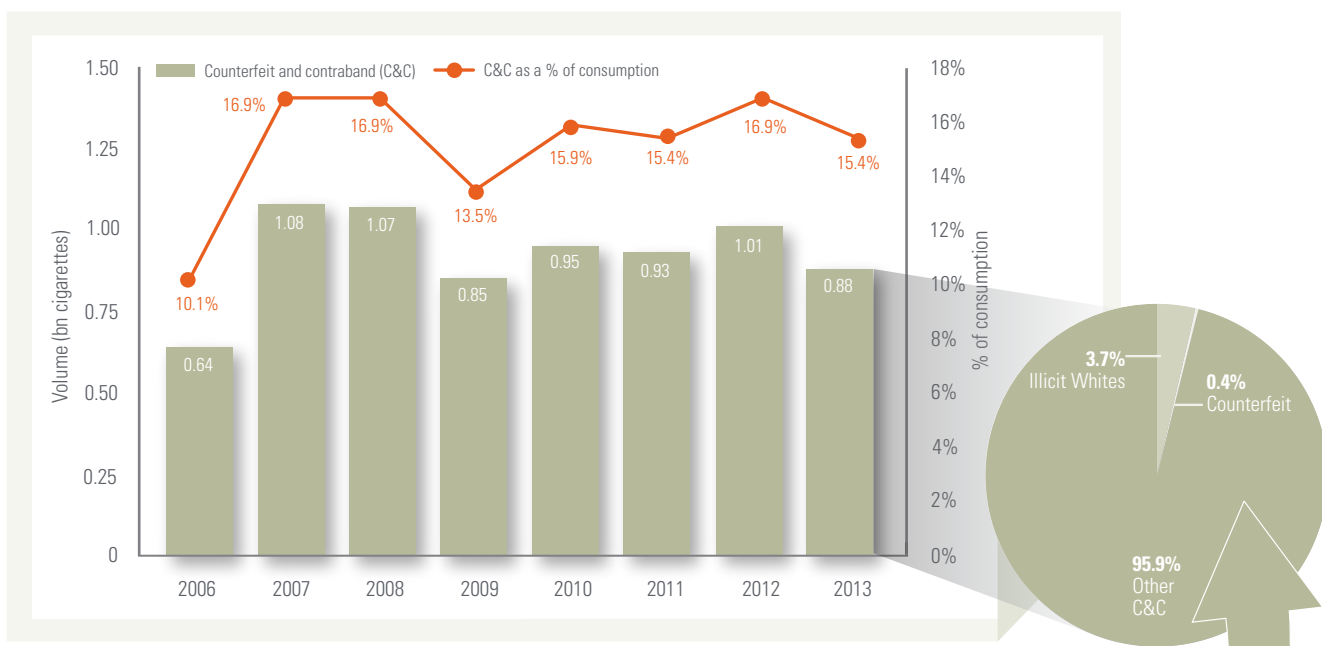
Notes: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) Synovate/Ipsos ND(L) research 2013. (3) UN WTO Tourism Factbook 2008-12, UN WTO.

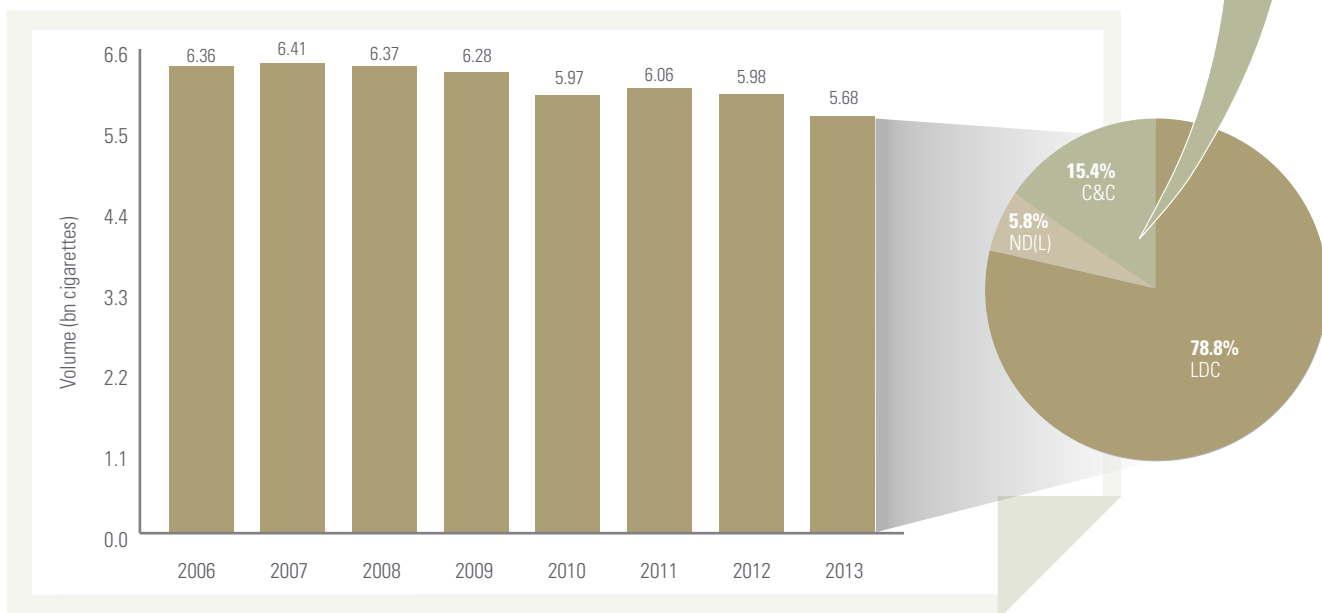


Total consumption declined, along with decline in the Counterfeit & Contraband and Non-Domestic Legal

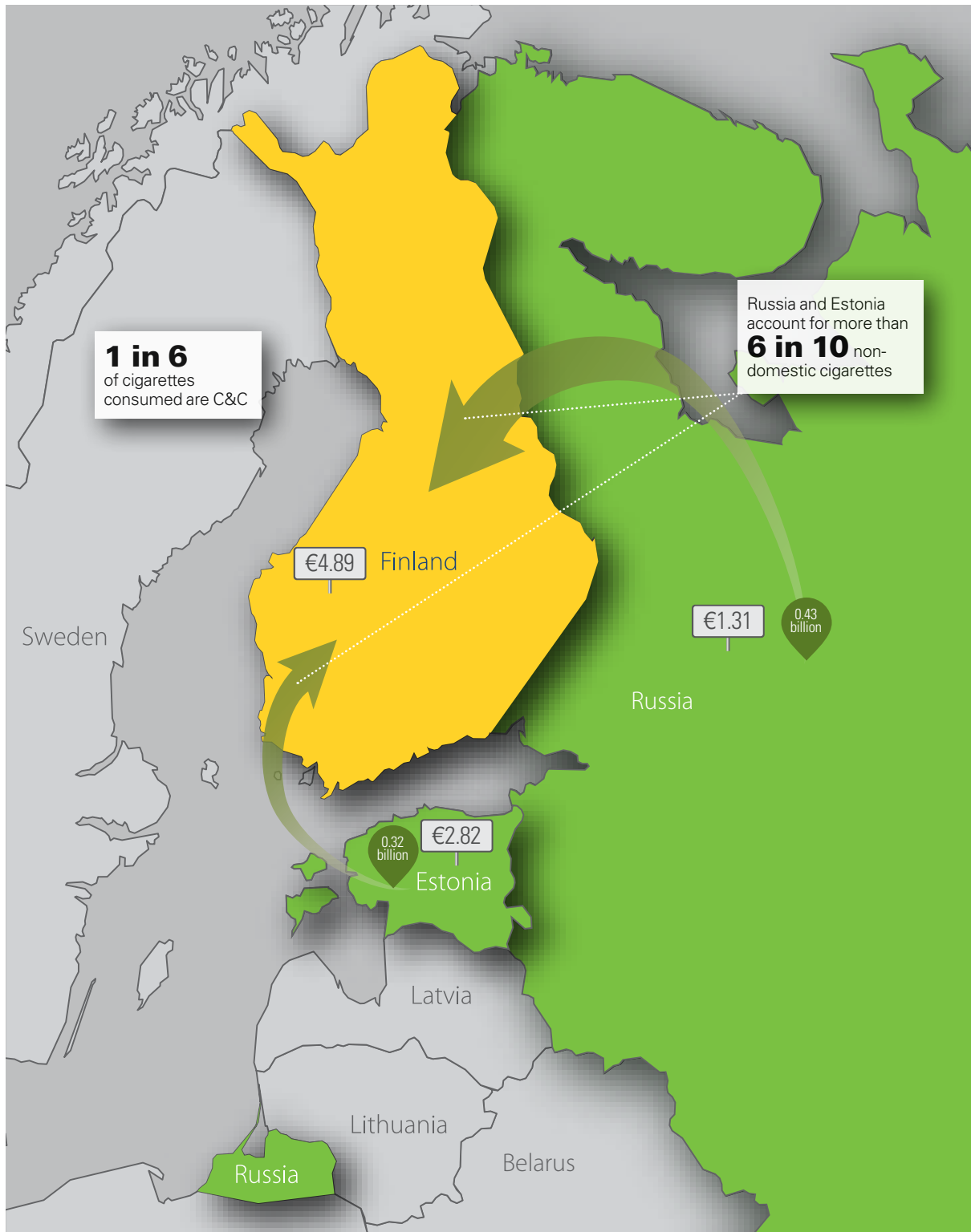
Manufactured cigarette C&C volumes and share of overall consumption 2006-13



Manufactured cigarette consumption 2006-13



KEY INFLOWS AND OUTFLOWS



Main outflow ■
Main inflow ■

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

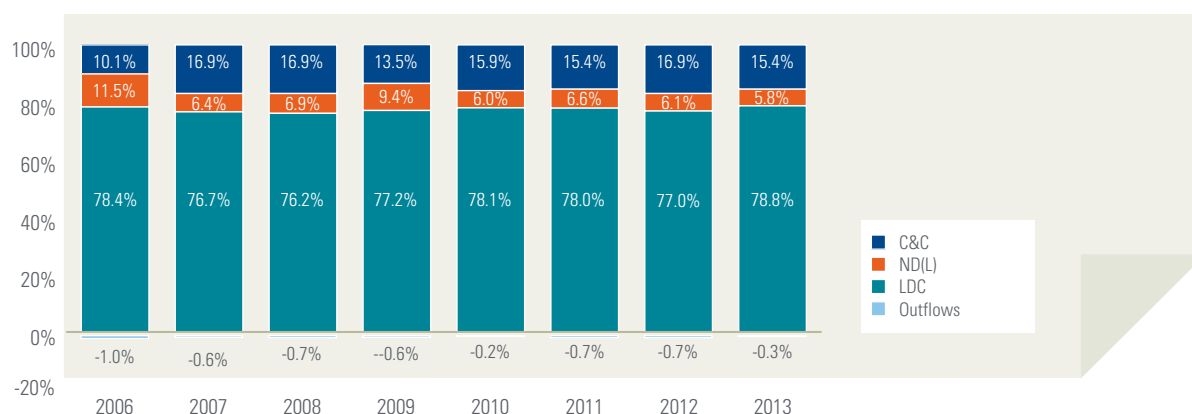
Source: (1) KPMG EU Flows Model.

Total consumption has fallen, reflected in both legal domestic sales and non-domestic volumes

Total manufactured cigarette consumption - Finland ^{(1)(2)(3)(a)}

TOTAL FINLAND CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	5.05	4.95	4.90	4.88	4.68	4.76	4.65	4.49	(3)%
Outflows	-0.07	-0.04	-0.05	-0.04	-0.01	-0.04	-0.04	-0.02	(61)%
Legal domestic consumption (LDC)	4.99	4.91	4.85	4.85	4.67	4.72	4.61	4.47	(3)%
Non-domestic legal (ND(L))	0.73	0.41	0.44	0.59	0.36	0.40	0.36	0.33	(10)%
Counterfeit and contraband (C&C)	0.64	1.08	1.07	0.85	0.95	0.93	1.01	0.88	(13)%
Total non-domestic	1.38	1.49	1.51	1.43	1.31	1.34	1.37	1.20	(12)%
Total consumption	6.36	6.41	6.37	6.28	5.97	6.06	5.98	5.68	(5)%

Share of Finland cigarette consumption by type - 2006-2013 ⁽¹⁾⁽²⁾⁽³⁾



Total manufactured cigarette consumption in Finland fell by 5% in 2013; legal domestic sales (LDS) declined at a slower rate of 3%, while non-domestic volumes experienced a more rapid decline of 12%

- Economic conditions in Finland worsened in 2013 as unemployment rose by 0.4 percentage points to 8.1% and average PDI remained stable ⁽⁴⁾⁽⁵⁾
- LDS volumes may have been impacted by a 2.4% WAP rise in 2013 ⁽⁶⁾
- Consumer research suggests that smoking incidence of manufactured cigarettes has continued its long term decline and reduced by 0.4 percentage points between 2012 and 2013 to 26.7%

Sources: (1) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Independent agency Empty Pack Surveys, 2006 – 2013. (4) Euromonitor Passport. (5) The Economist Intelligence Unit. (6) EU Commission WAP tables.

Russian, Estonian and Duty Free cigarettes are the main inflows to Finland

Prior to 2013, Finnish inflows from Russia were calculated through analysis of seizure data and border crossings. In 2013, only Finnish EPS has been used to create the Russian inflow. As a result of this there has been an estimated reduction in the Russian inflow to Finland. Had the 2012 seizure and tourist flow methodology been used the Russian inflow would have stood at 0.92bn cigarettes

No Illicit Whites brands were present in Duty Free in 2013

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWSTO FINLAND									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Russia	0.62	0.89	0.89	0.83	0.68	0.79	0.82	0.43	(47)%
Estonia	0.43	0.25	0.25	0.27	0.21	0.20	0.21	0.32	51%
Duty Free	0.19	0.29	0.26	0.21	0.30	0.26	0.21	0.28	32%
Ukraine	0.00	0.00	0.02	0.00	0.01	0.00	0.02	0.02	15%
Poland	0.00	0.00	0.00	0.00	0.00	0.00	0.01	0.02	92%
Counterfeit								0.00	n/a
Other	0.13	0.06	0.09	0.12	0.10	0.09	0.11	0.13	23%
Total inflows	1.38	1.49	1.51	1.43	1.31	1.34	1.37	1.20	(12)%

Non-domestic inflows to Finland fell by 12% in 2013. The main component of this decline is a decrease in inflows from Russia

- The largest non-domestic inflows to Finland are from Russia and Estonia
 - The high price differential with Russia, where the WAP of a pack of 20 cigarettes in 2013 was €1.23, may act as an incentive to transport cigarettes into Finland, where the WAP is €4.70⁽²⁾
 - Estonia is a popular holiday destination for Finns, with ferries travelling between the two countries where cigarettes can be easily purchased. The WAP differential between the two countries increased from €1.88 to €2.07 in 2013, which may be driving increased consumer purchases⁽²⁾

Total outflows by destination country – 2006-2013⁽¹⁾

OUTFLOWS FROM FINLAND									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
UK	0.00	0.00	0.01	0.02	0.00	0.00	0.01	0.00	(75)%
Netherlands	0.01	0.00	0.00	0.00	0.00	0.01	0.01	0.00	(65)%
Sweden	0.01	0.02	0.00	0.00	0.01	0.00	0.00	0.00	(2)%
Other	0.05	0.02	0.04	0.01	0.01	0.02	0.02	0.01	(60)%
Total outflows	0.07	0.04	0.05	0.04	0.01	0.04	0.04	0.02	(61)%

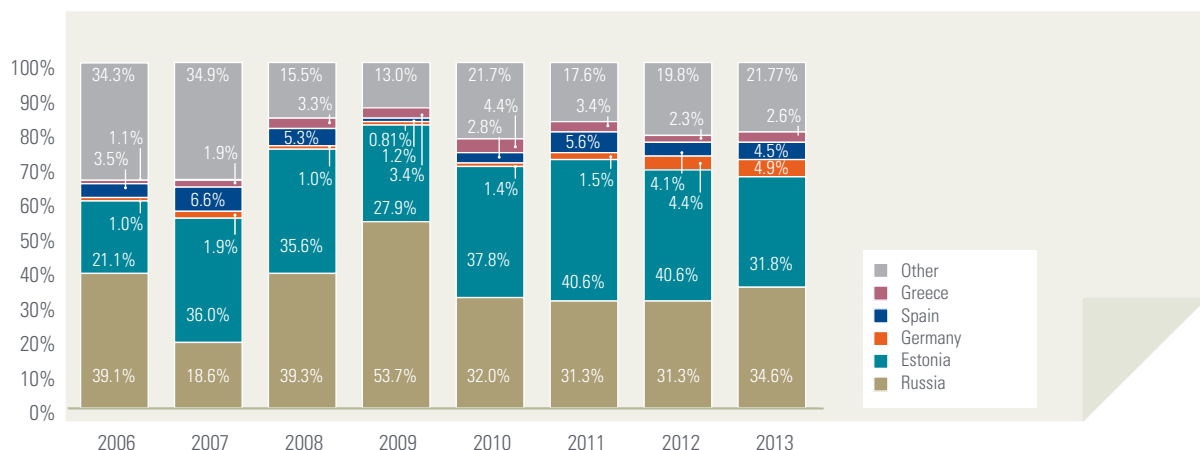
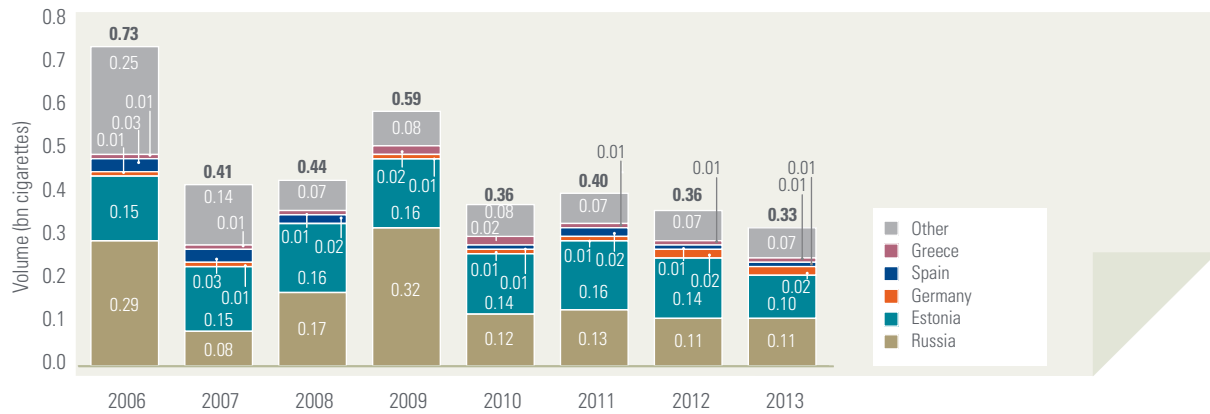
Outflows from Finland have traditionally been low and continue to be so in 2013, decreasing from 0.04bn cigarettes in 2012 to 0.02bn cigarettes in 2013

Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model. (2) EU Commission WAP tables.

Legal inflows declined by 10% in 2013, driven mainly by a decline in volumes from Estonia

ND(L) by origin 2006-2013^{(1)(2)(3)(a)(b)}



Non-domestic legal (ND(L)) flows into Finland are significant, amounting to more than one quarter of total non-domestic consumption. Most legal flows come from Russia and Estonia

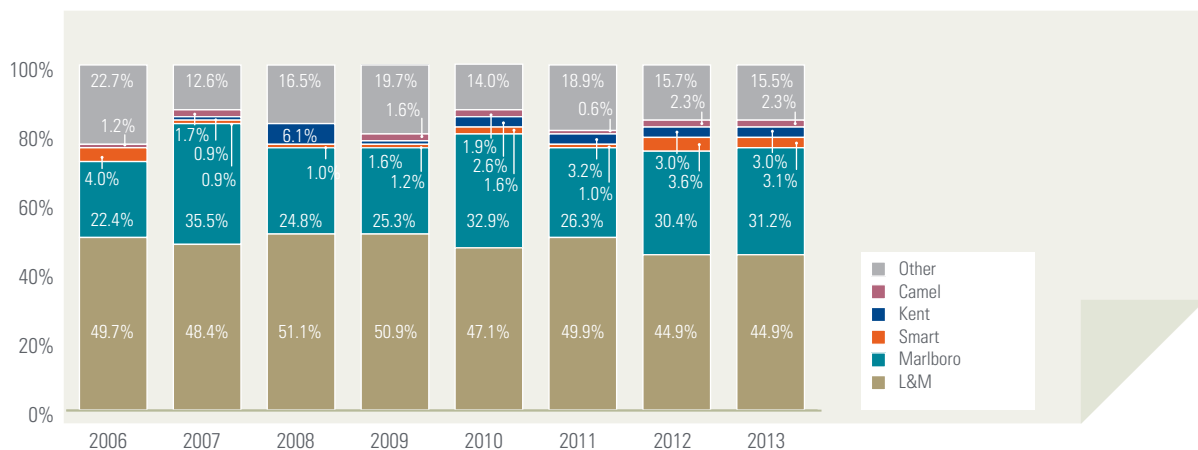
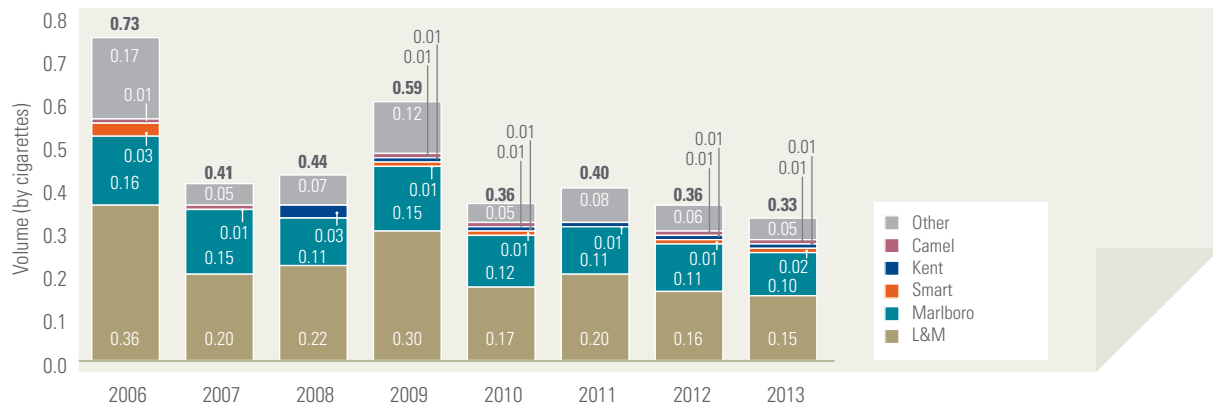
- As a bordering nation with significantly cheaper cigarettes there may be the incentive for cross-border shopping in Russia (see appendix for more details)
- There are significant tourism flows to Estonia, with numerous ferry services running between the two countries (see appendix for more details)

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013^{(1)(2)(3)(a)}



L&M and Marlboro comprise over 75% of non-domestic legal inflows

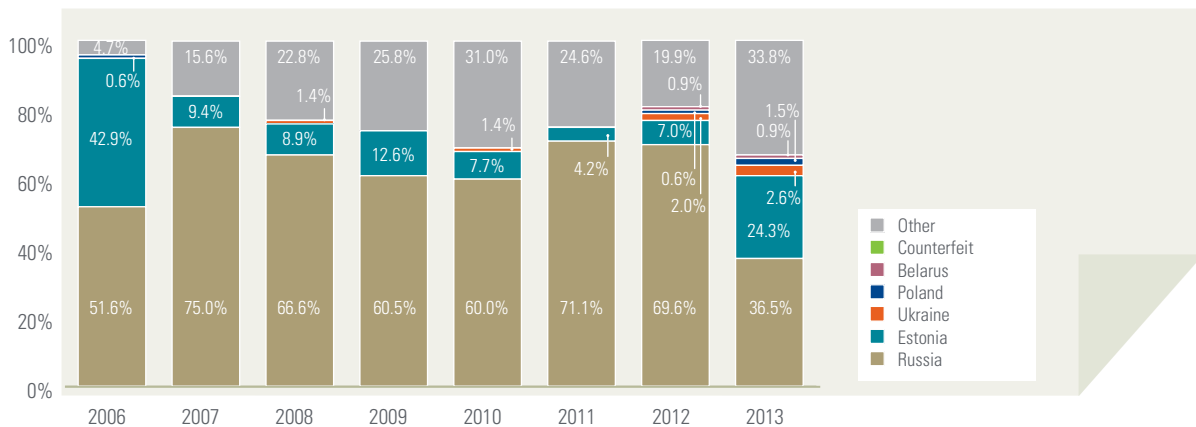
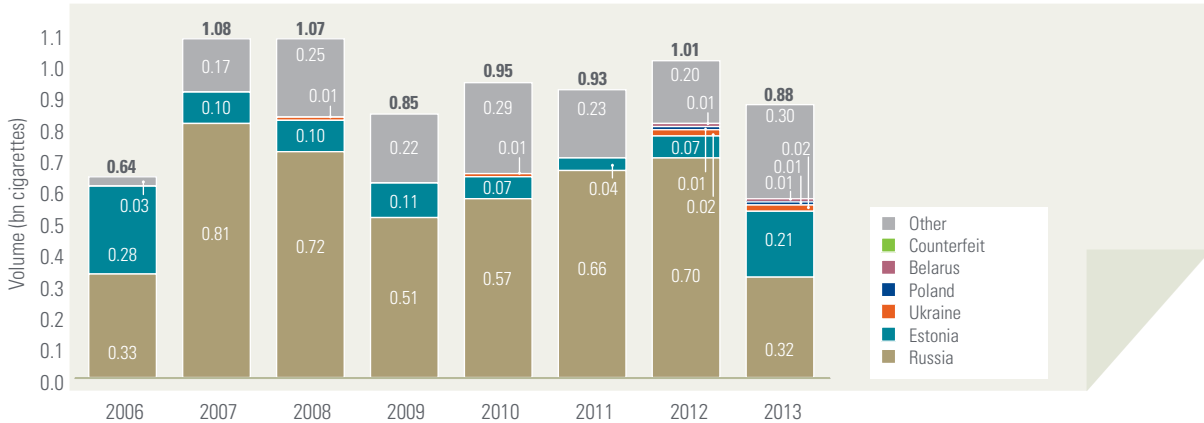
- 80% of L&M and 58% of Marlboro comes from Estonia and Russia, the largest sources of ND(L) into Finland

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model (3) KPMG analysis of data sources provided by manufacturers.

Russia and Estonia are the main sources of contraband product in 2013

C&C by origin - 2006-2013^{(1)(2)(3)(a)}



Total counterfeit and contraband (C&C) in Finland has decreased by 13% between 2012 and 2013

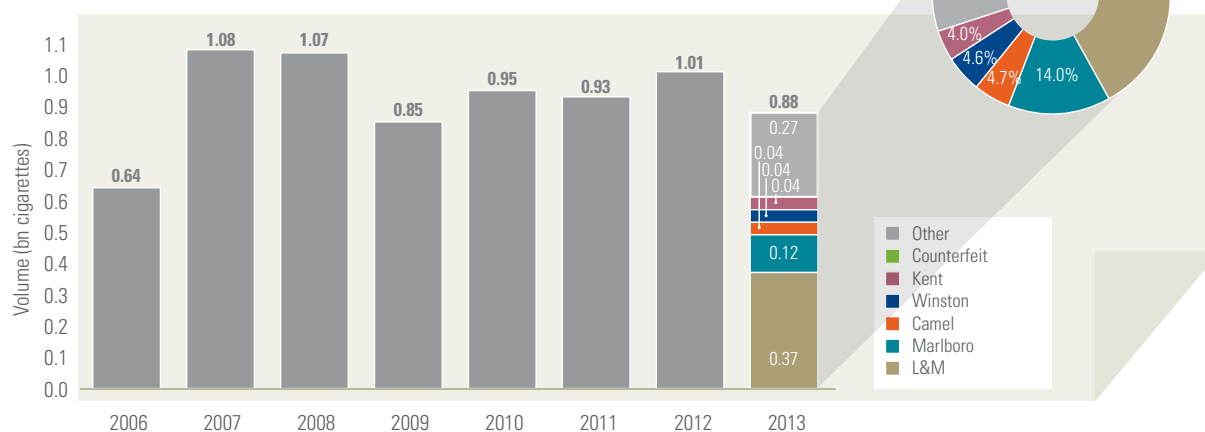
- Inflows from Russia have historically been modelled on a mixture of Finns travelling to Russia, Russians travelling to Finland, and cigarette seizures by Finnish customs. In 2013, this methodology has been revised to be consistent with the overall methodology; the EPS data was used as the sole measure of the Russian inflow in 2013
 - Had the 2012 methodology been used the Russian inflow would have been 0.81 bn cigarettes (0.92 ND inflow less 0.11 ND(L)), giving an increase in overall C&C to 1.34 bn, or 33%
- Inflows from Estonia have increased, which may have been driven by the greater price differential between the two countries, rising from €1.88 to €2.07 in 2013⁽⁴⁾. The most popular brands were L&M and Marlboro, accounting for over 60% of the total Estonian C&C volumes
- If the 0.88bn C&C cigarettes in 2013 had been legally purchased in Finland the revenue gained would have been approximately €159m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers. (4) EU Commission WAP tables.

C&C INFLOWS BY BRAND

C&C by brand - 2006-2013^{(1)(2)(3)(a)}



Russian and Estonian contraband inflows of L&M and Marlboro are the main components of C&C in Finland

Composition of Illicit Whites inflows - 2006-2013^{(1)(3)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO FINLAND								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.00	0.02	0.01	0.02	0.01	0.01	0.03	>100%
Duty Free	0.00	0.00	0.01	0.00	0.00	0.00	0.00	(100)%
Unspecified	0.00	0.00	0.00	0.00	0.00	0.00	0.00	n/a
Total Illicit Whites	0.00	0.02	0.02	0.02	0.01	0.01	0.03	>100%

Illicit Whites represent only a very small proportion of consumption in Finland, accounting for 3% of total C&C volumes in 2013

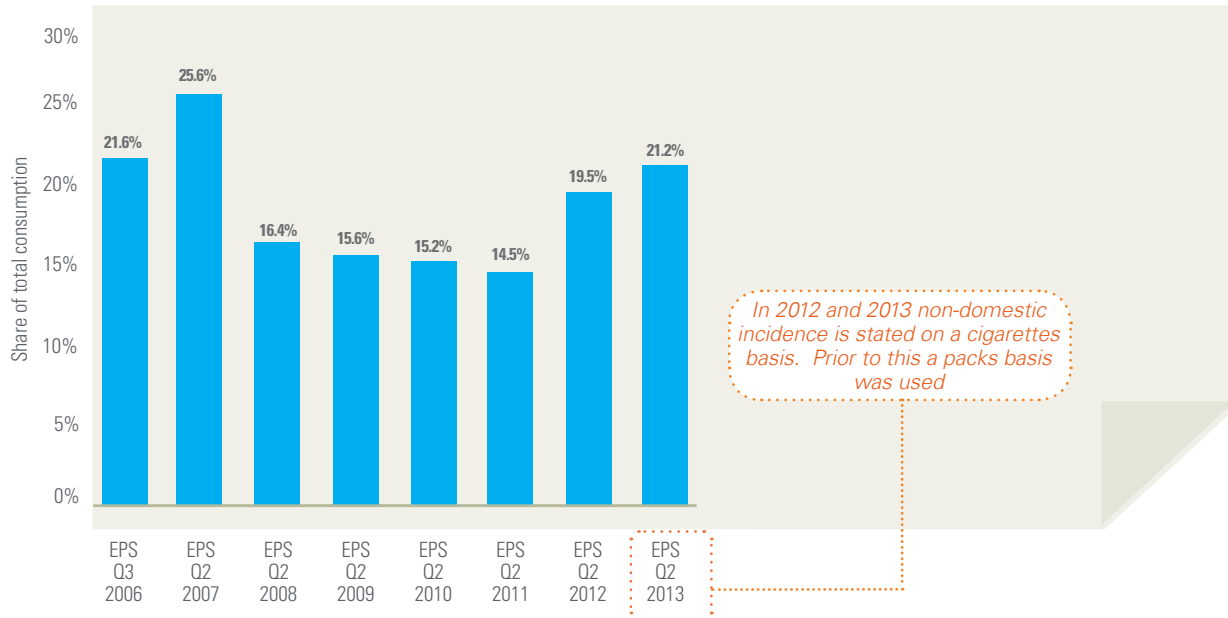
- The most common brands in 2013 were Bayron, Esse and Fest, which contributed approximately one third of the total Illicit Whites volume

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

EPS results & EU Flow model

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



- The EPS Survey in Finland has shown an increase in non-domestic incidence since 2012
- The empty pack survey in Finland collected 5,000 packs during the second quarter of the year. It collects these packs across 11 towns and cities

Source: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

ND(L) volumes calculations and explanations

KPMG non domestic legal flows Finland

KPMG NON DOMESTIC LEGAL FLOWS FINLAND							
Use of consumer research and any adjustments for 2013 data							
Country	ND 2013 ⁽¹⁾	Total trips where cigarettes purchased (m) ⁽²⁾⁽³⁾	Number of packs per trip ⁽²⁾⁽⁵⁾	Total packs ^(m)	Data sources ⁽³⁾⁽⁴⁾⁽⁵⁾	2013 ND(L) (bn sticks)	% of ND
Estonia	0.32	0.5	10	5	UNWTO, Estonian customs	0.10	33%
Russia	0.43	0.6	10	6		0.11	26%

Finnish travel to Estonia decreased by 4% over 2012 levels. It is assumed that the maximum of 10 packs are purchased

Assumes tourists take 10 packs (legal limit) per trip

Consumer research is used to calculate the ND(L) inflow volume to Finland

Estonia is a popular holiday destination for Finns, with regular ferry services between the two countries.

- Tourist flows to Estonia declined by 4% in 2013⁽³⁾
- In 2013 0.54 million trips were made by smokers who purchased cigarettes. The average purchase was 13 packs. As per Estonian customs the maximum permitted export is 10 packs, therefore all packs above this limit are classified as contraband⁽⁴⁾
- This results in 33% of Estonian inflows being classified as legal

ND(L) consumer research identified approximately 600,000 travellers to Russia who purchased cigarettes in 2013

- Russia is a considerably cheaper market than Finland, with a WAP of €1.23 in 2013⁽⁵⁾. In the consumer research, respondents stated that on average they only purchased one pack when travelling to Russia. Due to the large price difference it has been assumed that they would purchase the maximum permitted allowance of 10 packs
- This results in 26% of Russian inflows being classified as legal

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) World Tourism Organization, Yearbook of Tourism Statistics dataset, 2013. (4) Estonian Customs (Tulli), Customs Instructions for Passengers, July 2013. (5) EU Tax tables to see prices and price increases.

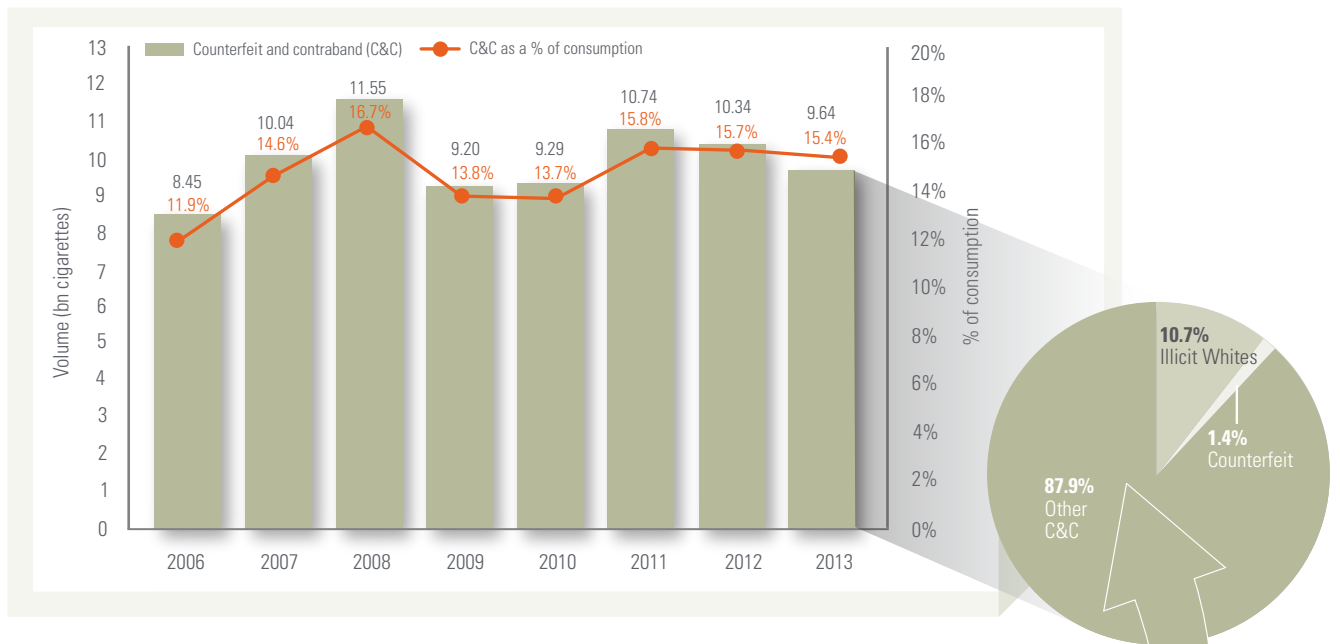


FRANCE

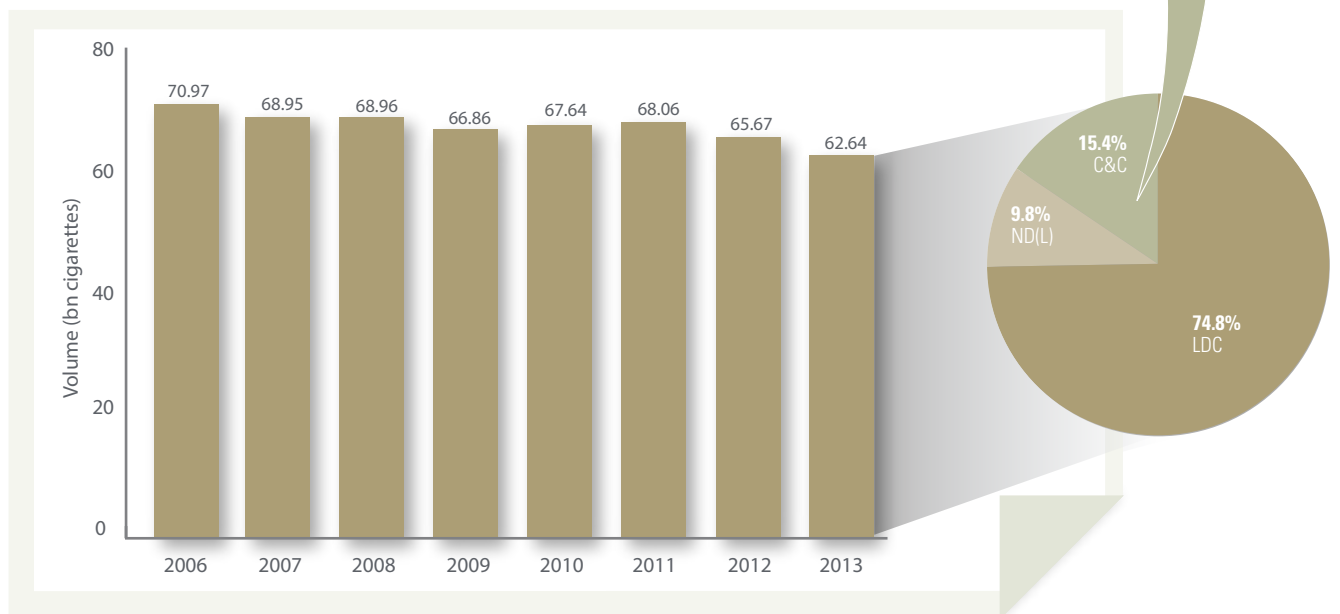


Counterfeit & Contraband volumes declined, compensated by growing Non-Domestic Legal consumption

Manufactured cigarette C&C volumes and share of overall consumption 2006-13



Manufactured cigarette consumption 2006-13

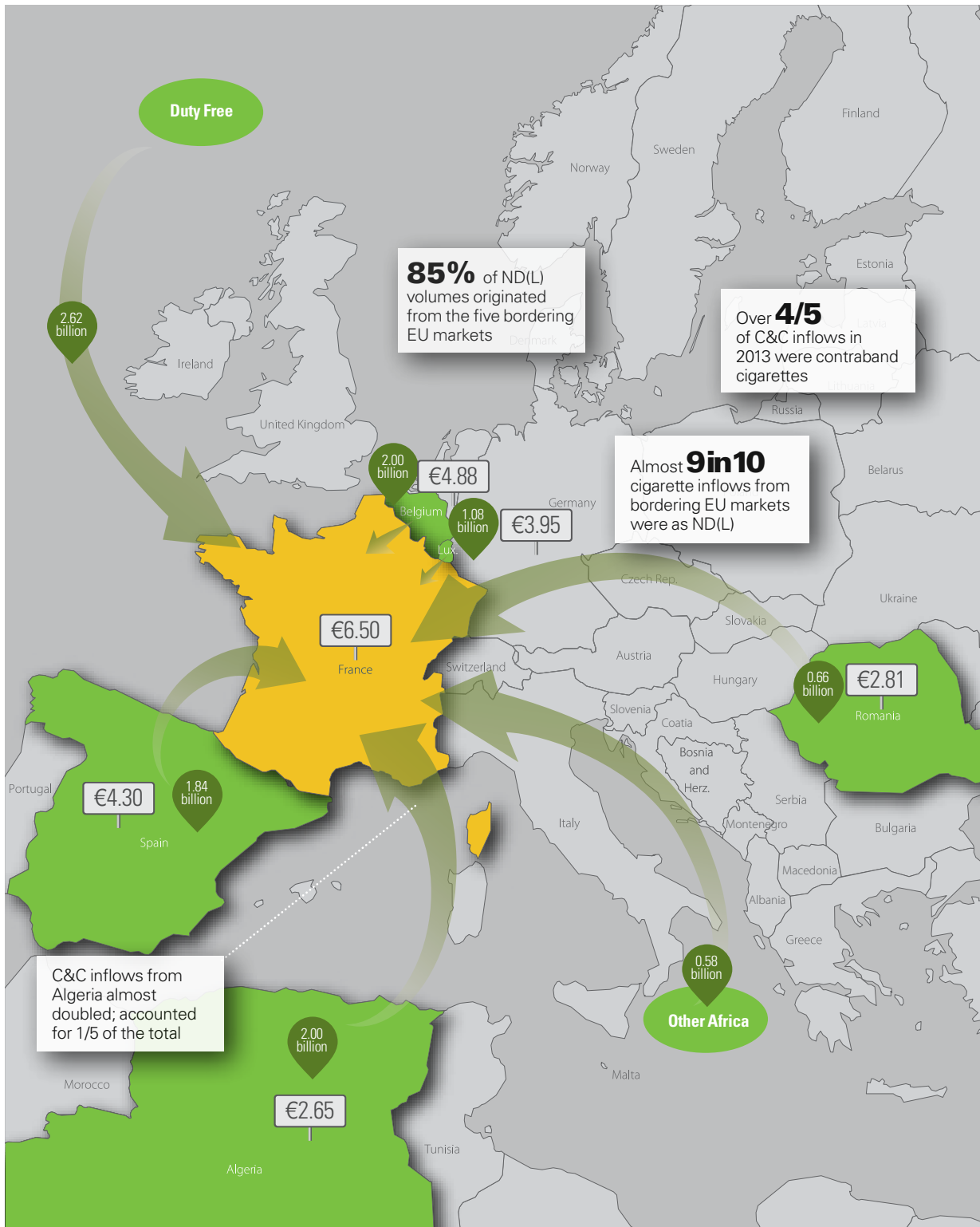


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KEY INFLOWS AND OUTFLOWS



FRANCE

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Main outflow

Main inflow

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

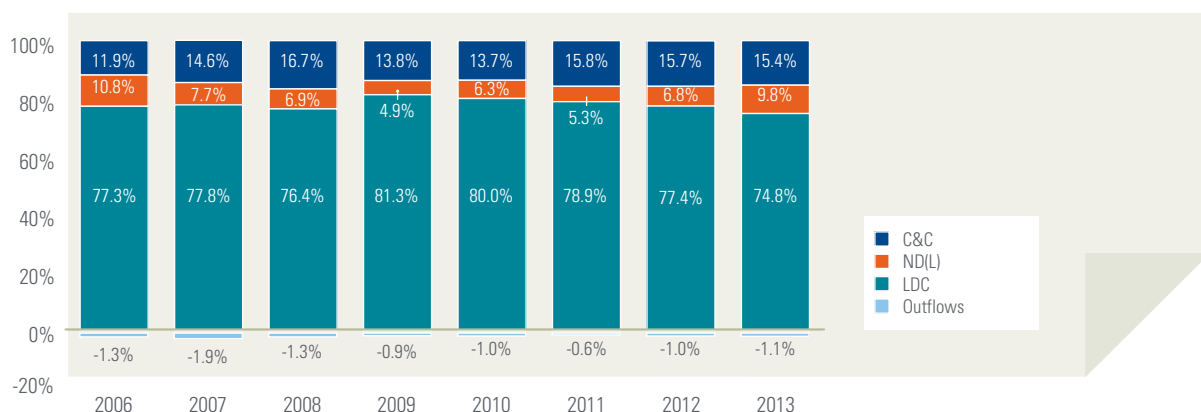
Overall consumption of cigarettes continued to decline although a reduction in legal domestic sales was partially offset by a rise in non-domestic inflows

Legal domestic sales data does not include Corsican volumes, which in 2013 were 0.75bn cigarettes. EPS data classifies packs from Corsica as non-domestic

Total manufactured cigarette consumption – France^{(1)(2)(a)}

TOTAL FRANCE CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	55.77	54.95	53.59	54.99	54.80	54.11	51.46	47.53	(8)%
Outflows	-0.91	-1.32	-0.92	-0.61	-0.68	-0.42	-0.63	-0.66	6%
Legal domestic consumption (LDC)	54.86	53.63	52.67	54.38	54.11	53.69	50.83	46.87	(8)%
Non-domestic legal (ND(L))	7.66	5.29	4.74	3.29	4.24	3.63	4.50	6.13	36%
Counterfeit and contraband (C&C)	8.45	10.04	11.55	9.20	9.29	10.74	10.34	9.64	(7)%
Total non-domestic	16.11	15.33	16.29	12.49	13.53	14.37	14.84	15.77	6%
Total consumption	70.97	68.95	68.96	66.86	67.64	68.06	65.67	62.64	(5)%

Share of France cigarette consumption by type 2006-2013⁽¹⁾⁽²⁾⁽³⁾



The fall in the consumption of manufactured cigarettes continued the downward trend from 2012 at a similar rate of decline, resulting in 7.6% lower legal domestic sales (LDS)

- The €0.40 (6.6%)⁽³⁾ per 20 cigarettes rise in WAP during the year is likely to have been a contributing factor to the decline in legal domestic sales
- Cigarette excise duty was also increased again in July 2013, by €0.20 per 20 cigarettes. A further increase of the same amount came into effect in January 2014⁽³⁾
- Unemployment in France increased by one percentage point to 10.8% in 2013⁽⁴⁾. This continued an almost uninterrupted upwards trend since the global economic crisis in 2008
- There have however been increases in both GDP per capita and PDI per capita in 2013⁽⁴⁾⁽⁵⁾
- Cigarette imports from other EU countries were relaxed in May 2013, from 5 cartons per vehicle to 10 cartons per person⁽⁶⁾. Consumers are therefore more able to satisfy their needs through legitimately imported cigarettes from cheaper foreign markets
- Consumer smoking trends support the decline in consumption of manufactured cigarettes
- Legal fine cut tobacco volumes continue to grow at a steady rate (and account for a growing share of total tobacco sales)⁽⁷⁾, suggesting there may be a degree of switching to alternative tobacco products
- There has also been an element of switching to e-cigarettes by some consumers⁽⁸⁾⁽⁹⁾

Notes: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) EC Excise Duty tables (Part III – Manufactured Tobacco). (4) 2014 Economist Intelligence Unit. (5) Euromonitor, downloaded January 2014. (6) <http://vosdroits.service-public.fr/particuliers/F804.xhtml>. (7) European Commission releases for consumption of fine cut tobacco. (8) www.nytimes.com. (9) www.reuters.com.

Increased inflows were mainly driven by higher volumes from Belgium and Algeria

Total inflows by country of origin 2006-2013^{(1)(a)}

ND INFLOWSTO FRANCE									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	2.84	2.87	4.04	2.20	3.70	3.91	3.13	2.62	(16)%
Belgium	0.53	0.73	0.71	0.48	0.43	0.90	1.01	2.00	99%
Algeria	0.00	0.26	0.41	0.80	1.00	1.12	1.08	2.00	85%
Spain	3.42	3.25	4.38	2.40	2.08	1.57	2.33	1.84	(21)%
Luxembourg	1.00	0.95	0.86	0.58	0.52	0.73	1.11	1.08	(3)%
Counterfeit								0.13	n/a
Other	8.31	7.26	5.89	6.04	5.79	6.14	6.17	6.08	(1)%
Total inflows	16.11	15.33	16.29	12.49	13.53	14.37	14.84	15.77	6%

Non-domestic inflows have increased this year both in terms of volumes and share of total consumption

- The increase was largely the result of inflows from both Belgium and Algeria doubling versus 2012. Although non-domestic as a share of total consumption has been rising slowly since 2009, it has only increased beyond the much higher levels of 2008 this year
- Increased price differentials, combined with higher allowances on imported cigarettes from abroad, are likely to have made non-domestic consumption more attractive
- Despite the overall increase in non-domestic volumes, Duty Free and inflows from Spain both declined during 2013
- Duty Free volumes have typically been one of the largest inflows. Illicit Whites with Duty Free labelling account for only 1.3% of total Duty Free volumes

Total outflows by destination country 2006-2013⁽¹⁾

OUTFLOWS FROM FRANCE									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Belgium	0.07	0.15	0.03	0.16	0.07	0.06	0.09	0.29	>100.%
Netherlands	0.37	0.35	0.12	0.08	0.35	0.13	0.16	0.14	(14)%
Italy	0.02	0.00	0.05	0.04	0.10	0.08	0.14	0.07	(49)%
Spain	0.22	0.31	0.33	0.08	0.01	0.03	0.04	0.07	81%
Other	0.23	0.50	0.40	0.25	0.14	0.11	0.20	0.09	(53)%
Total outflows	0.91	1.32	0.92	0.61	0.68	0.42	0.63	0.66	6%

Outflows from the French market are relatively low, most likely because cigarette prices in France are amongst the highest in Europe

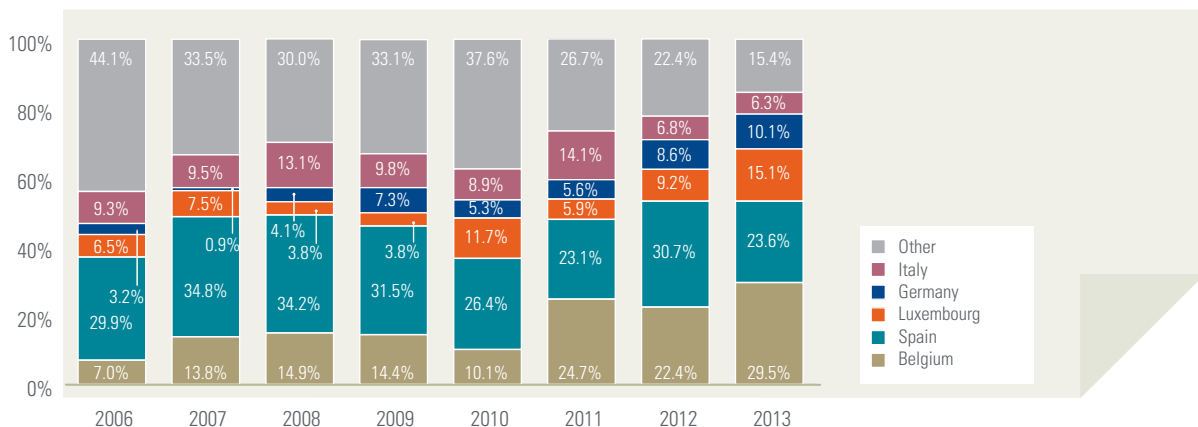
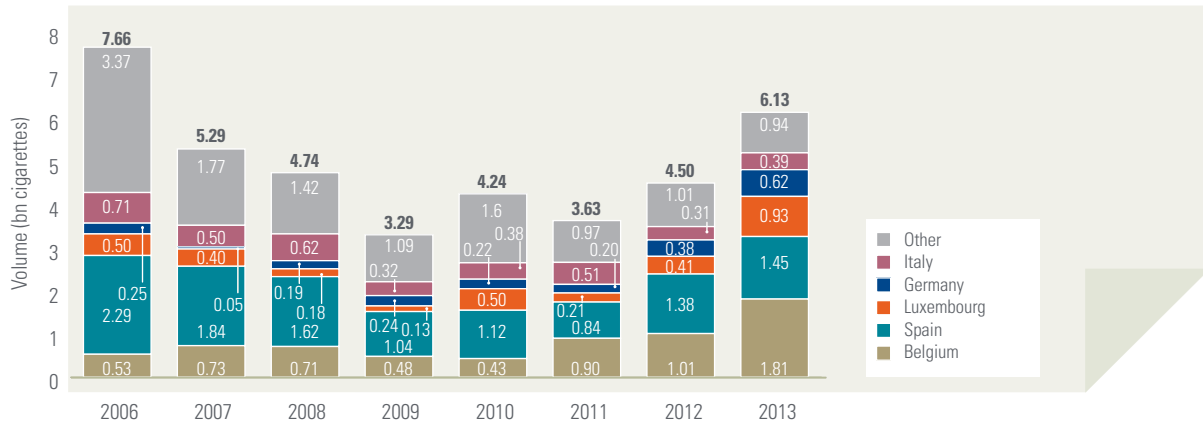
- The WAP of a pack of 20 in France was €6.10 in January 2013⁽²⁾, which exceeded prices charged in all but two of the EU markets considered within this Project SUN Report
- Outflows increased marginally in 2013 as a result of higher flows to Belgium and Spain, though there was a decline in flows to most other markets

Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model. (2) EC Excise Duty tables (Part III – Manufactured Tobacco).

Markets bordering France represent the main sources of ND(L); growth in 2013 was largely due to Belgium and Luxembourg

ND(L) by origin 2006-2013^{(1)(2)(a)(b)}



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Non-domestic legal (ND(L)) volumes have grown in absolute terms and have risen to 9.8% of total consumption from 6.8% in 2012

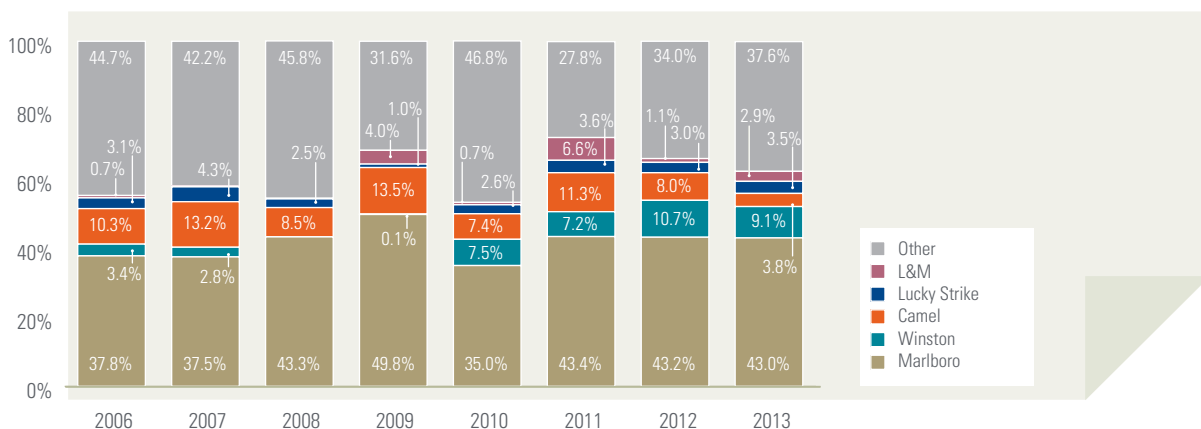
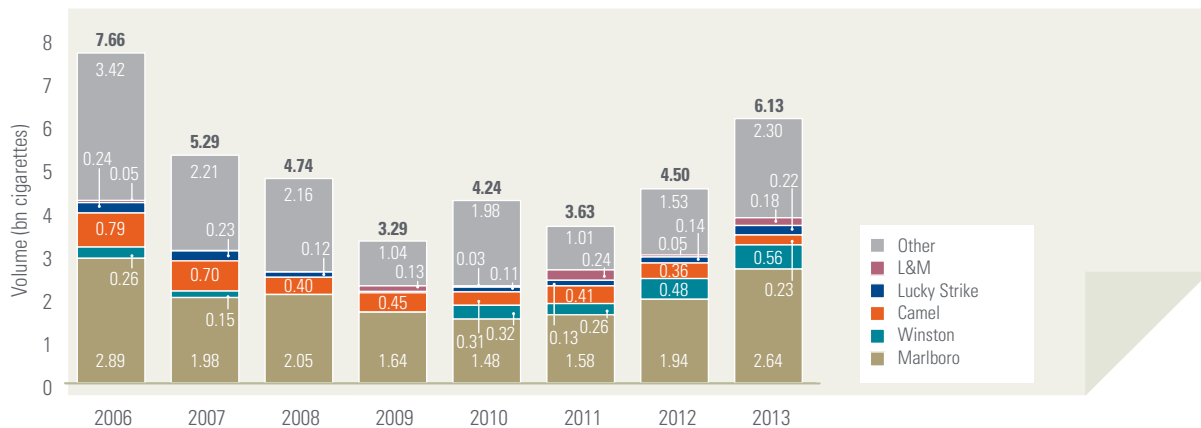
- Greater ND(L) flows from Belgium may have been influenced by a widening price differential for cigarettes and comparatively low levels of GDP per capita in North East France. The WAP differential between France and Belgium for a pack of 20 cigarettes increased from €1.03 in 2012 to €1.33 in 2013
- In addition to price and income factors, another driver of large inflows from Belgium to France is the close proximity of major French population centres to the Belgian border, both in terms of the border shopping effect and the number of cross-border commuters. Legal flows from Belgium are assumed to be 90% of the total incidence, based on tourist, commuter and border belt consumption flows
- Spanish ND(L) also marginally increased in 2013, from 1.38bn cigarettes in 2012 to 1.45bn cigarettes
- Despite an overall decline in inflows from Spain, legal volumes did not follow this trend and this is likely due to a relatively stable level of border purchases and overall outbound travel to Spain
- ND(L) flows from Germany and Italy both increased in the year which may have been in response to a widening price differential. Outbound tourism to both of these markets is significant⁽³⁾, as well as cross-border commuters and border shoppers with Germany. As a result, all of the flows were allocated to ND(L)

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU works model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-12, UN WTO.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013^{(1)(2)(3)(a)}



Growth in legal flows of brands is largely the result of larger volumes of Marlboro and to a lesser extent L&M

- Growth in volumes of ND(L) Marlboro largely originates from Belgium and Germany, with the Empty Pack Survey (EPS) showing greatest increases in incidence in the North East regions of Alsace Lorraine Champagne Ardennes and Nord Picardie
- Belgian inflows also give rise to greater ND(L) incidence of the L&M brand, and this is again most apparent in North East France
- Other legal inflows consist of smaller volumes of almost 40 other brands

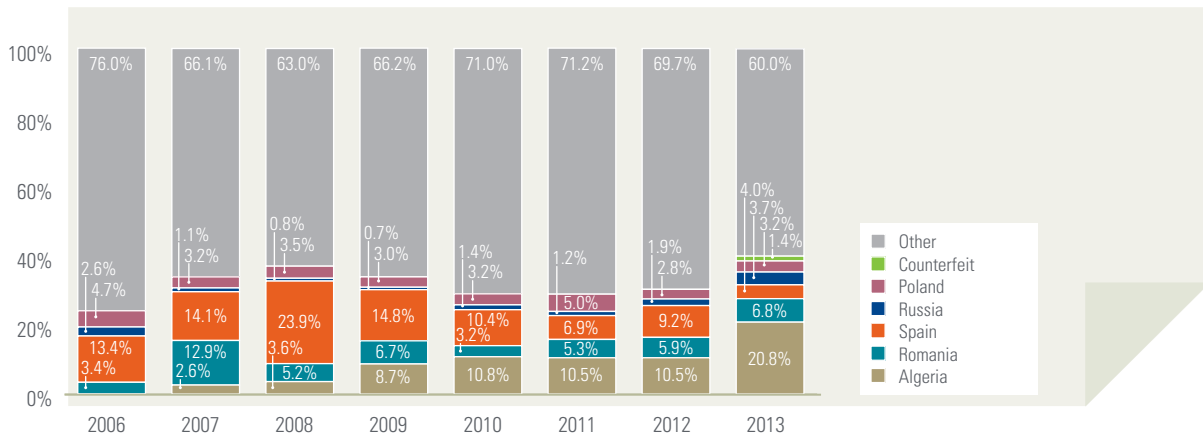
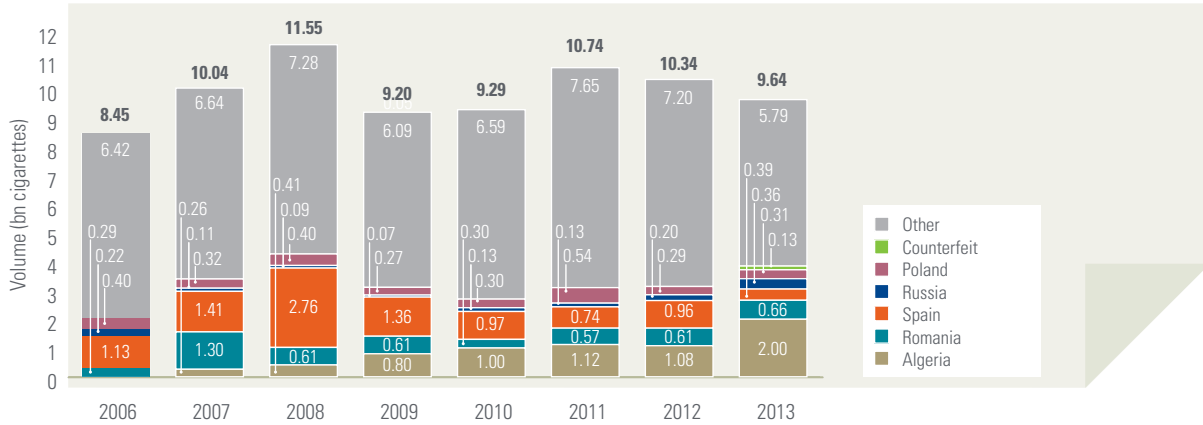
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



Despite a large increase in Algerian flows, total C&C declined in 2013 as illicit flows from markets such as Spain decreased

C&C by origin - 2006-2013^{(1)(2)(3)(a)}



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Although counterfeit and contraband (C&C) volumes were broadly flat in 2013, they increased as a share of total consumption

- Inflows from Algeria increased substantially this year. This was especially evident in major cities such as Marseille, Paris and Lyon as well as the South of France more generally
- Large immigrant populations in major cities are likely to have an effect on Algerian incidence as well as the significant price differential between the markets
- Based on consumer research around the average number of packs per trip and minimal outbound tourism to Algeria⁽³⁾, as well as the implausibility of mass day trip border shopping, this increase has almost entirely been allocated to C&C
- Other C&C inflows such as those from Romania and Russia also increased whilst flows from other Eastern European markets, as well as some from Africa (e.g. Senegal) and Asia made up the remainder of C&C
- Incidence of Romanian and Russian cigarettes was also highest in major cities such as Paris and Lyon

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-12, UN WTO.

C&C INFLOWS BY BRAND

C&C by brand - 2006-2013^{(1)(2)(3)(a)}



Contraband inflows represent the greatest share of C&C volumes with Marlboro the most prevalent contraband brand in France

- Large inflows of Marlboro C&C originated mainly from Algeria, whilst C&C flows of L&M arrived predominantly from Russia

Breakdown of Illicit Whites inflows 2007-2013^{(1)(2)(a)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO FRANCE								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.04	0.17	0.07	0.11	0.18	0.33	0.25	(26)%
Duty Free	0.43	1.02	0.06	0.07	0.01	0.02	0.04	86%
Unspecified	0.00	0.00	1.87	0.85	1.20	0.73	0.75	2%
Total Illicit Whites	0.47	1.19	2.00	1.03	1.39	1.08	1.03	(5)%

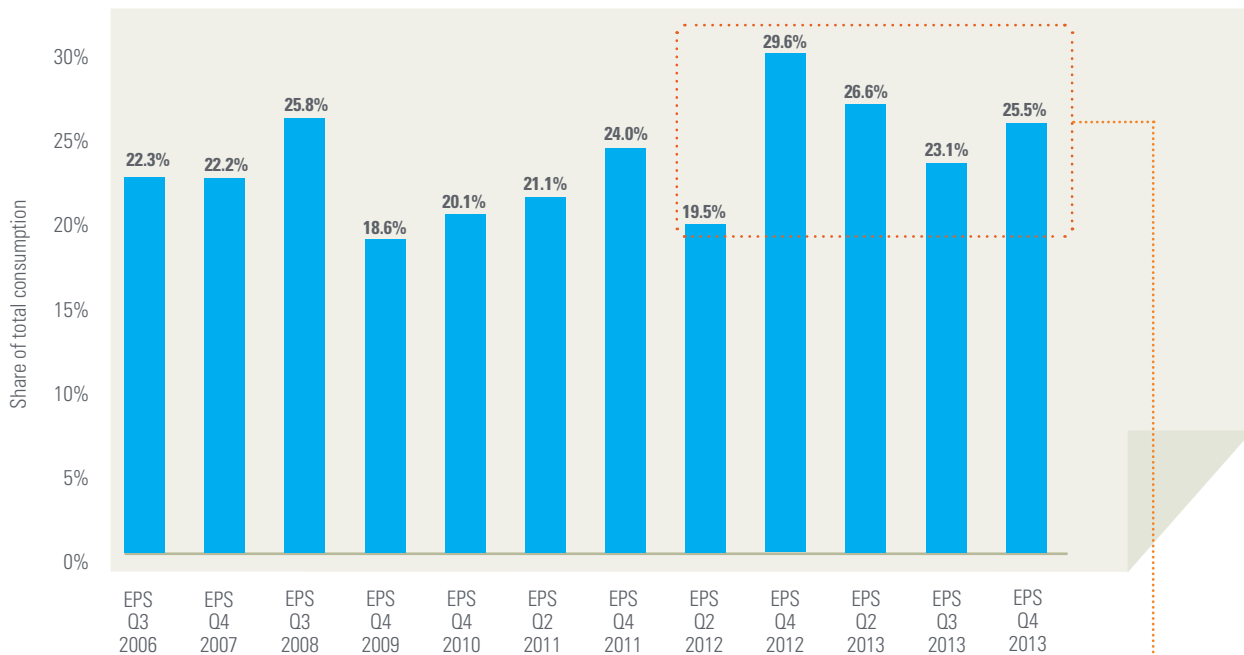
- Illicit Whites brands accounted for 10.7% of total C&C consumption. The most significant Illicit Whites brands in France are American Legend, Austin and Ducal
- Counterfeit appears to only be a small issue in France accounting for only 1.4% of total C&C flows
- If these C&C cigarettes had been legally purchased in France the tax revenue gained would have been approximately €2.4bn

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

EPS results and EU flows model

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used

FRANCE



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- The EPS in France collected 34,500 packs during the course of the year. This was undertaken as three waves – one conducted in Q2 (end of March to start of May), one in Q3 (July and start of August) and one in Q4 (October and start of November). Each wave collected 11,500 packs across a total of 118 cities. A regional sampling plan was used (share of EPS survey based on regional population shares) and the largest cities in each region were selected. The number of packs collected in each city was weighted by the city population
- Each wave of EPS data has been allocated the same weight within the KPMG EU flows model such that each represents a third of the year
- (Non-domestic) Marlboro packs appeared to be overstated in the EPS results when compared to Marlboro's share of legal domestic sales in the country. A second methodology has therefore been used to model ND Marlboro which is more in line with ND(L) results and domestic brand share. The balance has been allocated to other brands. This is further explained in the methodology section of the appendices
- Spanish incidence in the Q2 2013 EPS was very low in South West France when compared to previous years. Border sales data and the ratio of Q2 to Q3 border sales has been used to uplift the Spanish incidence in the Q2 wave. The adjusted incidence is more aligned with prior years' results and the seasonality of Spanish incidence seen across waves

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

ND(L) volumes calculations and explanations

KPMG NON DOMESTIC LEGAL FLOWS FRANCE							
Countries where ND(L) is 100% of total							
Country	ND 2013 (bn sticks) ⁽¹⁾					2013 ND(L) (bn sticks)	% of ND
Germany	0.62					0.62	100%
Use of consumer research and any adjustments for 2013 data							
Country	ND 2013 (bn sticks) ⁽¹⁾	Total trips where cigarettes purchased (m) ⁽²⁾⁽³⁾	Number of packs per trip ⁽²⁾	Total packs ^(m)	Data sources ⁽²⁾⁽³⁾⁽⁴⁾⁽⁵⁾	2013 ND(L) (bn sticks)	% of ND
Belgium	2.00	8.63	10	90.40	Consumer research, WTO	1.81	90%
Spain	1.84	5.04	14	72.32	Consumer research, WTO	1.45	79%
Luxembourg	1.08	6.98	7	46.40	Consumer research, WTO	0.93	86%

- Owing to outbound travel of around 1.85m in the year and a number of large towns and cities in close proximity to the border (meaning significant border shopper and commuter flows), 100% of non-domestic inflows from Germany have been classed as legal flows
- Based on the much larger volumes seen entering France from Belgium, Luxembourg and Spain, additional analysis has been performed to calculate the likely legal share
- For example in the case of Belgium, consumer research, the number of commuters and an estimation of likely border shopper numbers have been used to calculate the legal component of the inflow
 - Per the consumer research, 1.75m trips were made to Belgium in 2013 to purchase cigarettes. On average, 10 packs were purchased per trip and so 18.4m packs (or 0.37bn cigarettes assuming packs of 20 cigarettes) were brought back legally
 - Consumer research is likely to understate inflows from commuters and border belt shoppers however, as the consumer research takes a representative sample of the country whilst on a regional basis there are many large cities located close to the Belgian border
 - For border shoppers an estimate is taken of the likely number of people within 2 hours drive of the Belgian border and the proportion of those people owning a car. Using the cigarette smoking prevalence and average daily consumption data, as well as the legal import limit of 10 cartons per person per trip, the total legal flow is estimated as 1.43bn cigarettes
 - Using inbound commuter numbers, implied smoking prevalence and average daily consumption data, as well as an estimation of the number of working weeks spent in Belgium per year, inflows due to commuters are estimated as 0.01bn
 - In total, estimated legal inflows from Belgium are 1.81bn cigarettes this year
- A similar method to the above is used for Luxembourg and Spain (although flows owing to commuters are not considered for Spain)

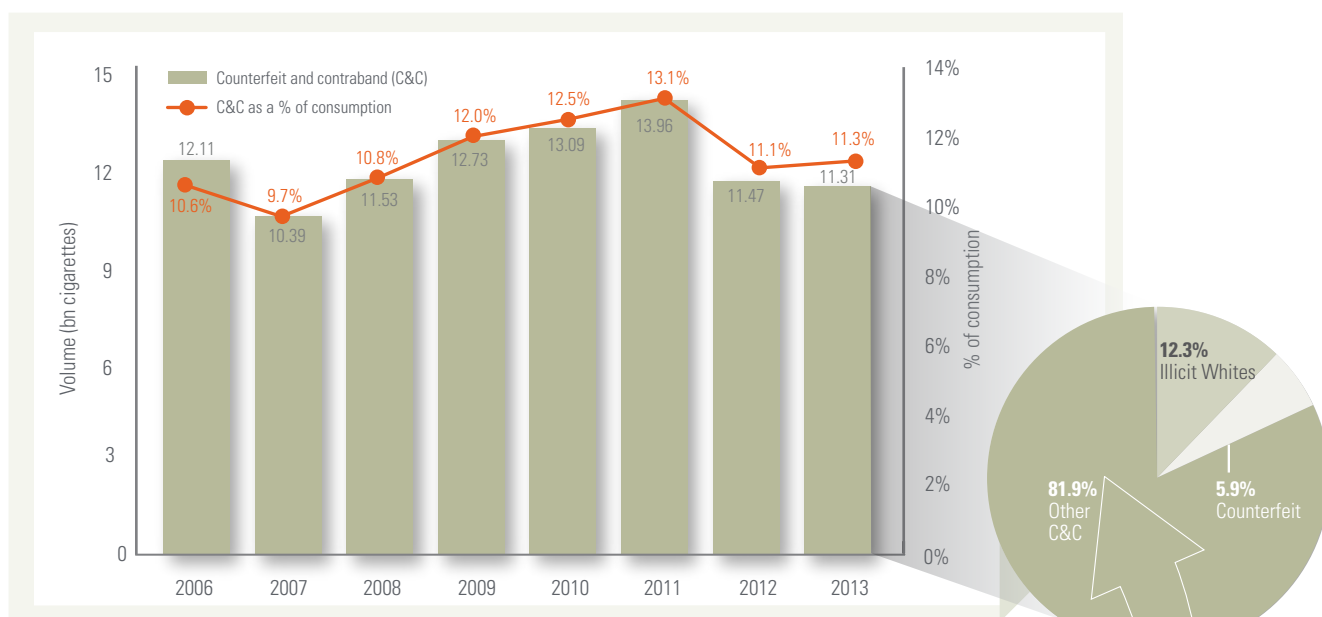
Notes: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.
Sources: (1) KPMG EU Flows Model. (2) Synovate/Ipsos ND(L) research 2013. (3) UN WTO Tourism Factbook 2008-12, UN WTO. (4) Population statistics from Insee.fr. (5) Car ownership data from European Environment Agency.

GERMANY



Higher inflows do not compensate for decline in consumption

Manufactured cigarette C&C volumes and share of overall consumption 2006-13

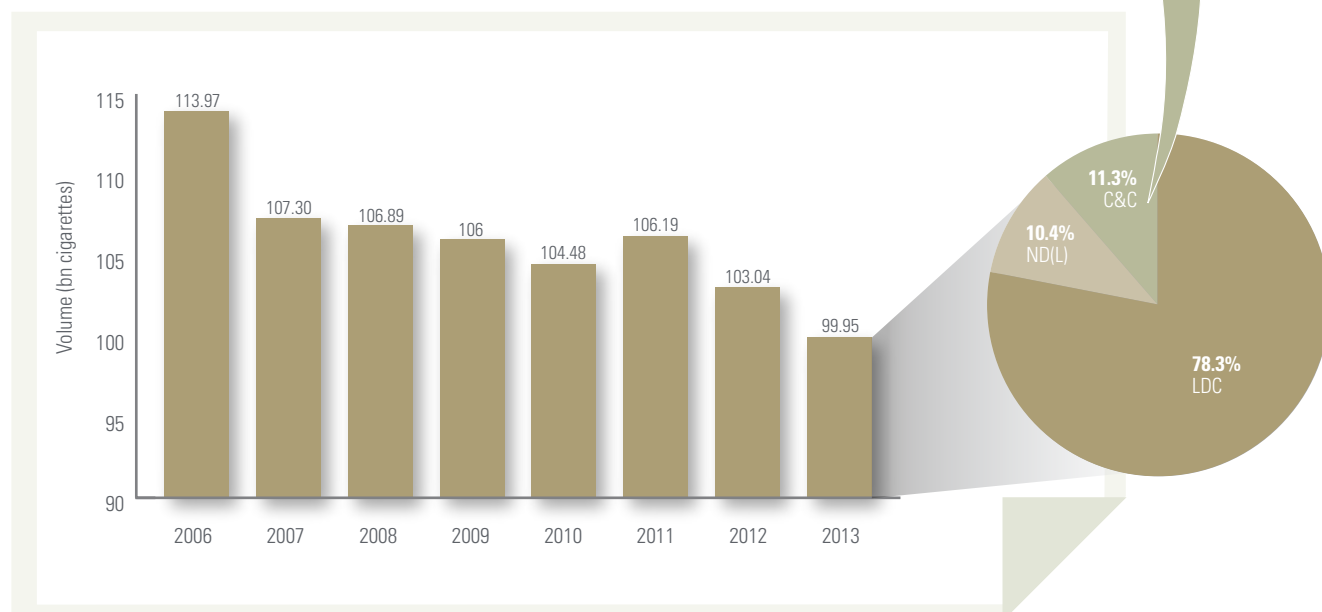


GERMANY

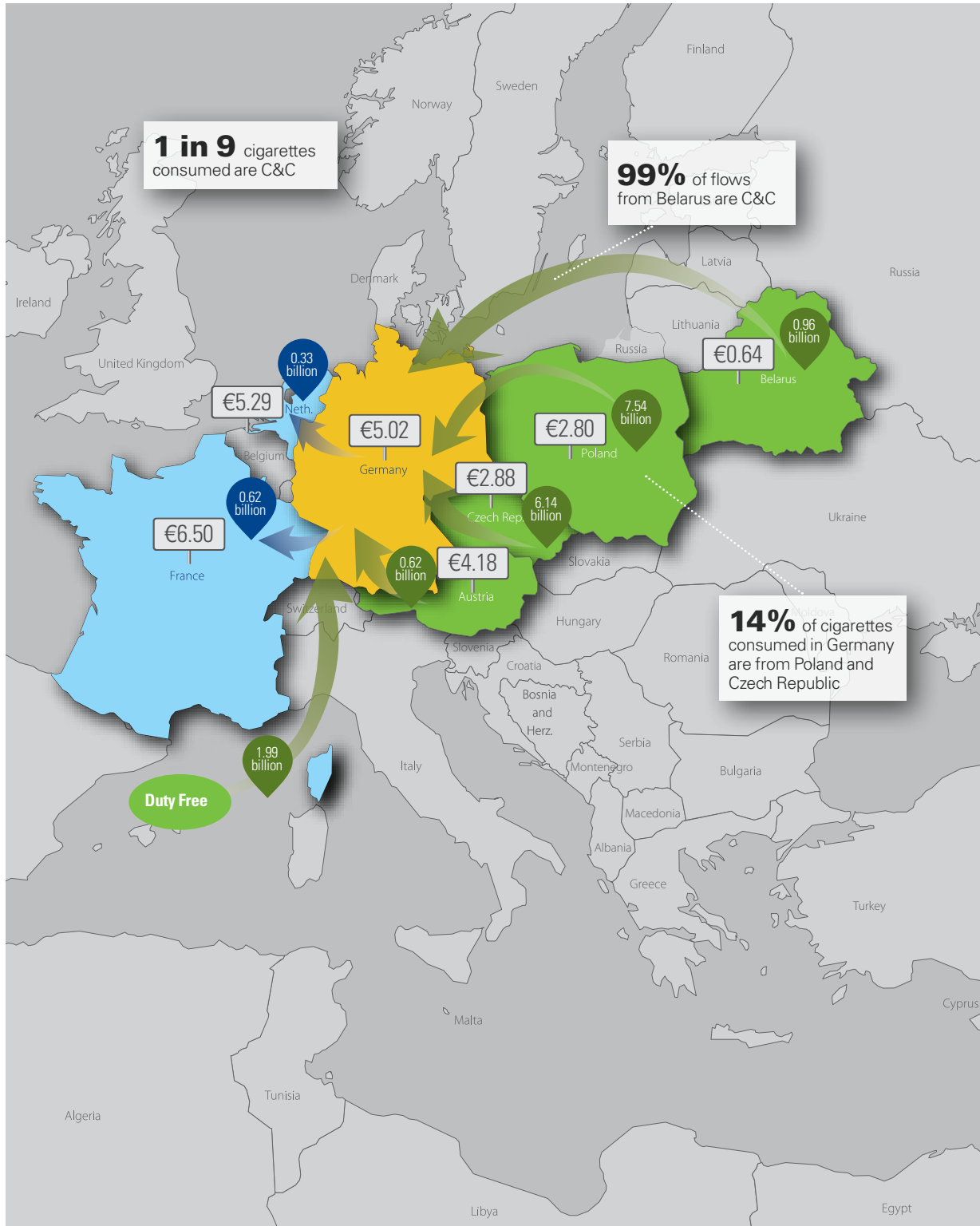


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Manufactured cigarette consumption 2006-13



KEY INFLOWS AND OUTFLOWS



GERMANY



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Main outflow ■
Main inflow ■

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

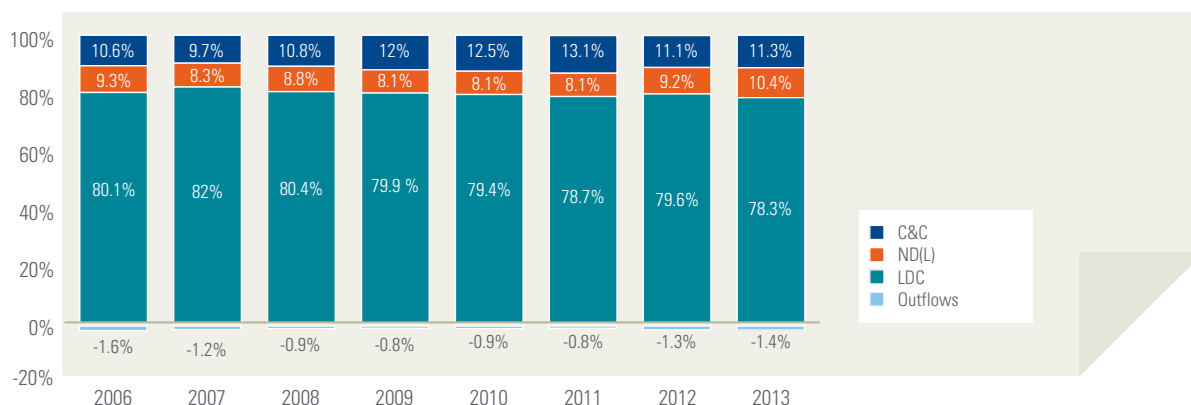
Source: (1) KPMG EU Flows Model.

The decline in legal domestic sales was partially offset by higher inflows

Total manufactured cigarette consumption – Germany⁽¹⁾⁽²⁾

TOTAL GERMANY CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	93.17	89.34	86.95	85.49	83.91	84.47	83.44	79.63	(5)%
Outflows	-1.86	-1.31	-0.97	-0.84	-0.95	-0.86	-1.37	-1.42	3%
Legal domestic consumption (LDC)	91.31	88.03	85.97	84.65	82.96	83.60	82.07	78.21	(5)%
Non-domestic legal (ND(L))	10.55	8.87	9.39	8.62	8.43	8.62	9.50	10.43	10%
Counterfeit and contraband (C&C)	12.11	10.39	11.53	12.73	13.09	13.96	11.47	11.31	(1)%
Total non-domestic	22.66	19.26	20.92	21.35	21.52	22.58	20.98	21.73	4%
Total consumption	113.97	107.30	106.89	106.00	104.48	106.19	103.04	99.95	(3)%

Share of Germany manufactured cigarette consumption by type⁽¹⁾⁽²⁾ -2006-2013



GERMANY



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Whilst legal domestic sales (LDS) declined by 5%, non-domestic volumes increased by 4%

- The decline in overall consumption is consistent with the long-term decline in smoking prevalence seen in Germany, however the decline in LDS appears to be being partially offset by an increase in non-domestic cigarettes
- Manufactured cigarette consumption is unlikely to have been impacted by the economy in Germany which remained stable in 2013. Unemployment fell slightly from 5.5% to 5.3% and PDI increased by 2.5%⁽³⁾

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Euromonitor, downloaded March 2013.

Poland and the Czech Republic were the largest inflow markets, but there was a significant increase from Belarus

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWS TO GERMANY									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Poland	6.53	6.85	6.32	7.54	7.49	8.64	8.54	7.54	(12)%
Czech Republic	3.77	3.28	3.53	3.53	4.66	5.69	5.01	6.14	23%
Duty Free	1.61	0.63	1.99	1.61	1.68	1.53	1.70	1.99	17%
Belarus	0.00	0.00	0.13	0.18	0.43	0.61	0.64	0.96	50%
Austria	0.23	0.17	0.20	0.18	0.33	0.28	0.18	0.62	>100%
Counterfeit								0.66	n/a
Other	10.52	8.33	8.76	8.32	6.93	5.83	4.91	3.82	(22)%
Total inflows	22.66	19.26	20.92	21.35	21.52	22.58	20.98	21.73	4%

Increases in flows from Czech Republic offset by decrease in flows from Poland

4% of Duty Free flow was Illicit Whites

Despite continued price increases in Poland and the Czech Republic, the price difference based on the WAP in each country respectively and in Germany is still €2.22 for Poland and €2.14 for the Czech Republic

- In 2013 there were price increases of 5.5% in Poland and 4.2% in the Czech Republic, where there were also more favourable exchange rates with the Euro in 2013. This may explain the shift between cigarettes coming from Poland to the Czech Republic
- Whilst combined flows from Poland and the Czech Republic accounted for overall growth of 0.13 billion cigarettes, there were changes to inflows from other source countries:
 - It appears that more German consumers are purchasing cigarettes in Austria, where legal domestic sales increased in 2013
 - Increases in flows from Belarus are likely to be almost all C&C
 - Other major flows into Germany come from Russia, Hungary, Serbia and Ukraine

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM GERMANY									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
France	0.68	0.23	0.19	0.24	0.22	0.21	0.52	0.62	18%
Netherlands	0.45	0.29	0.20	0.13	0.35	0.25	0.33	0.33	1%
Poland	0.22	0.23	0.03	0.01	0.00	0.07	0.08	0.10	32%
Other	0.50	0.55	0.55	0.46	0.37	0.33	0.44	0.36	(18)%
Total outflows	1.86	1.31	0.97	0.84	0.95	0.86	1.37	1.42	3%

Outflows from Germany are mainly through border sales to the higher priced markets of France and the Netherlands

- At the end of 2013 the price difference between Germany and the Netherlands was €0.27 and to France was €1.48
- All these flows are assumed to be legal purchases given the large population bases that live close to the German border

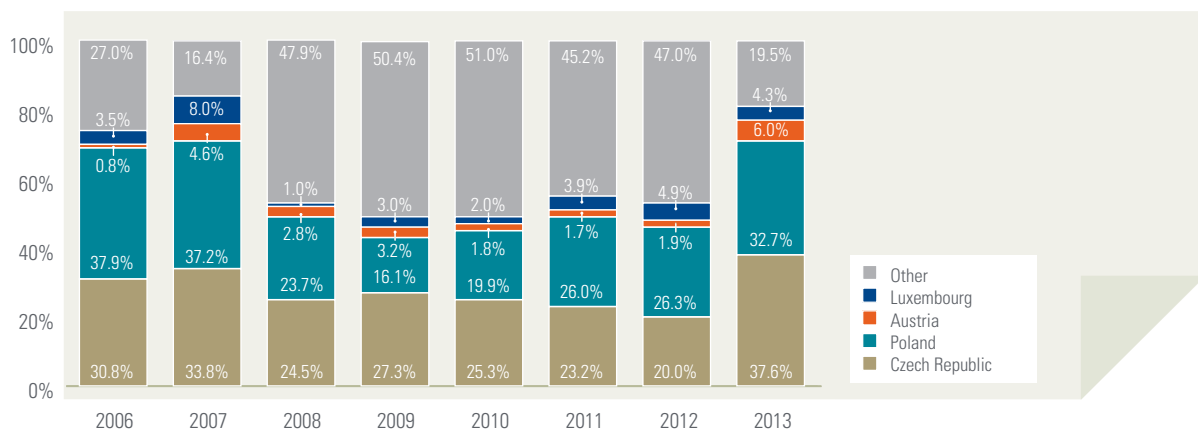
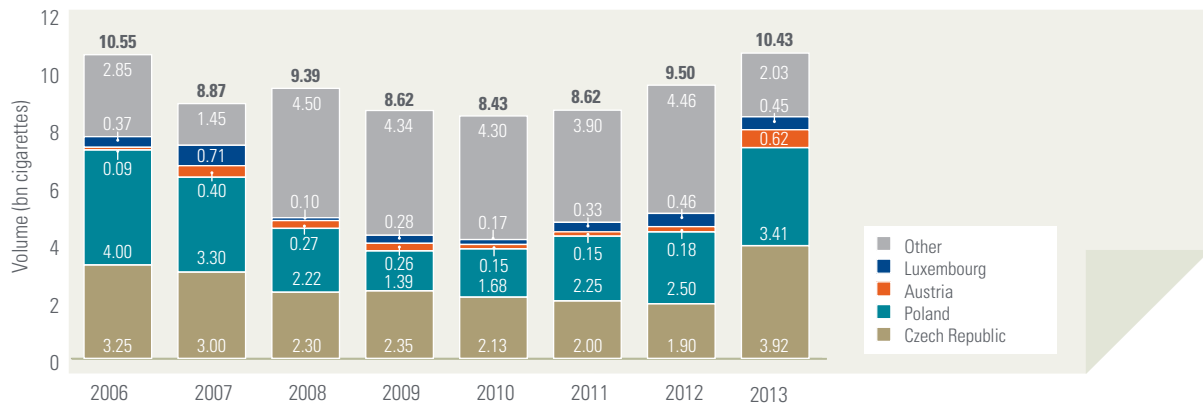
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model.



Two thirds of ND(L) volumes came from the Czech Republic and Poland

ND(L) by origin 2006 - 2013^{(1)(2)(a)(b)}



GERMANY



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The majority of ND(L) flows come from Czech Republic and Poland, whilst other ND(L) flows come from other neighbouring countries with lower priced cigarettes

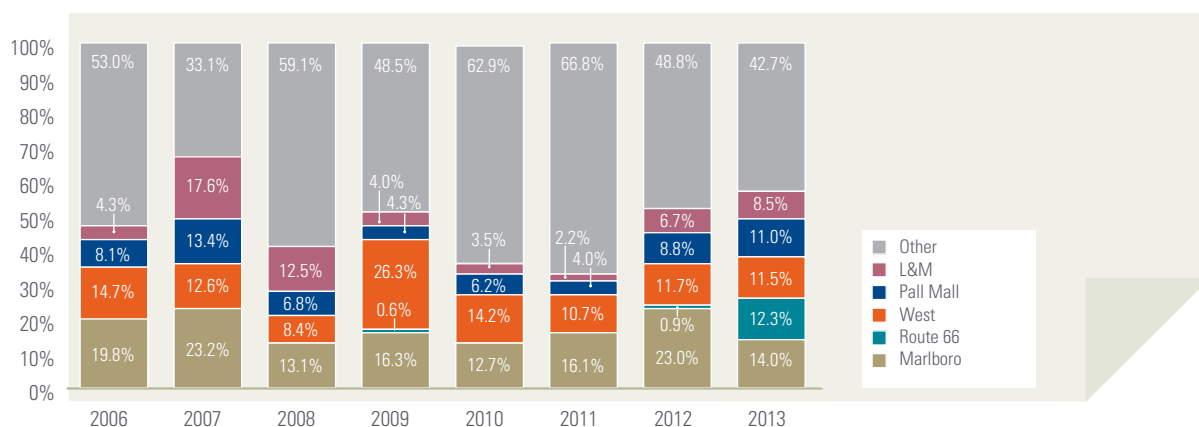
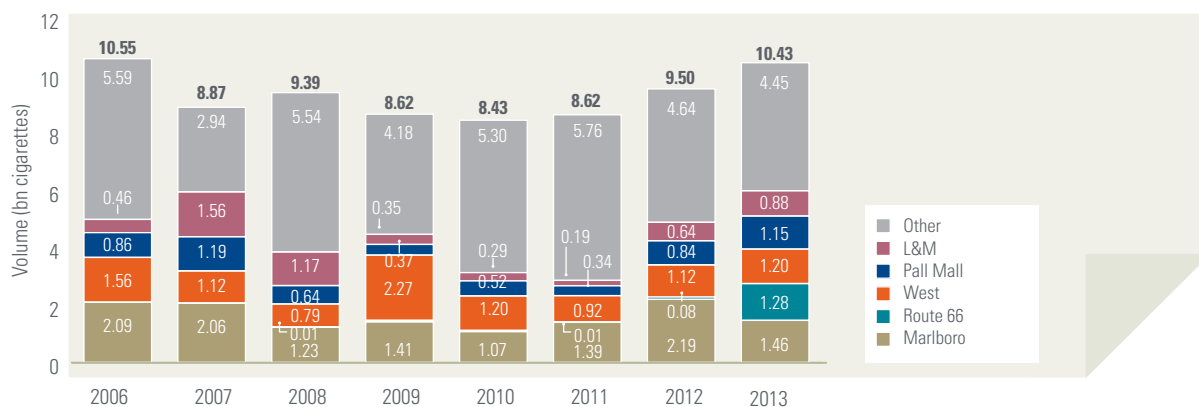
- 70% of ND(L) consumption comes from Czech Republic and Poland
- Both borders are close to large population bases within Germany and the average price difference of €2.18 for Poland and €2.14 for Czech Republic means that consumers could save over €20 per carton, or over €80 if the entire legal limit was purchased
- According to the Yellow Bag Survey, almost 70% of packs collected from Poland were in the East Germany region closest to the Polish border, indicating that those that live closer to the border are more likely to purchase cigarettes across the border
- The Czech Republic has typically been a more popular tourist destination than Poland^(b) which may explain the higher volume of ND(L)
- Flows from other countries such as France and Netherlands (all treated as legal) have fallen significantly, as prices in these countries have risen faster than in Germany, resulting in fewer tourists or commuters likely to bring cigarettes from these countries

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided in appendix.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013^{(1)(2)(3)(a)}



Brands are allocated to ND(L) through border sales data and consumer research

- Sales data from border shops in Poland and the Czech Republic are used in order to allocate the correct percentage of brand sales from each of these countries
- For other countries consumer research is used to estimate the volume
- ND(L) sales tend to incorporate more popular German brands compared to other sales in Poland, however Route 66, with limited distribution within Germany, has become a popular cheaply priced option sold in large boxes
- Large volumes of other popular brands included Gauloises, Benson & Hedges, Lucky Strike and Viceroy

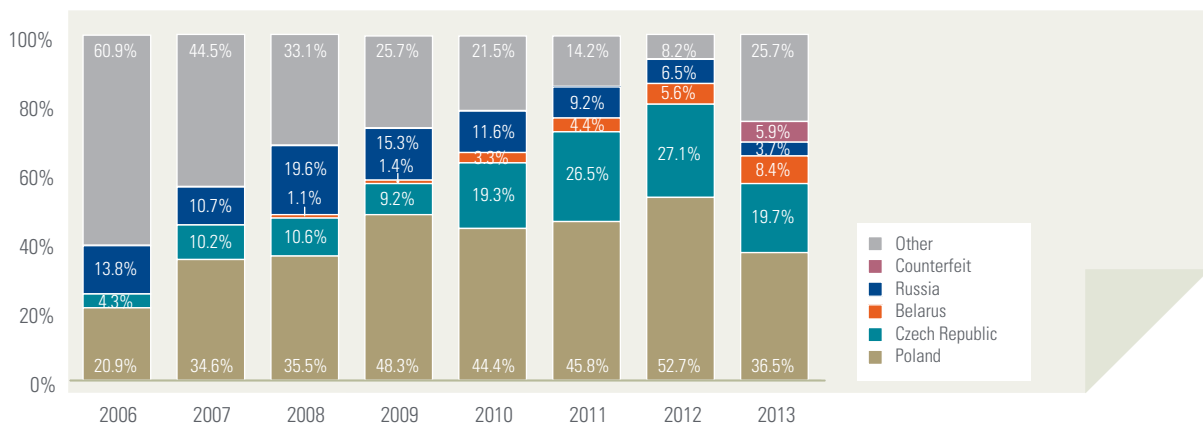
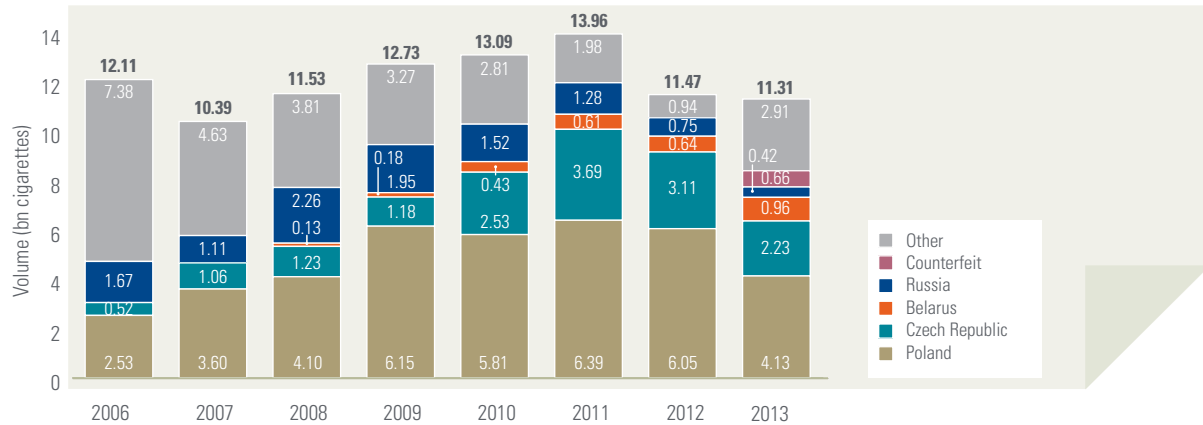
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



Poland and Czech Republic continue to have the largest share of C&C, but in 2013 there were also significant increases from Belarus

Total C&C by origin - 2006-2013^{(1)(2)(a)}



GERMANY



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54% of the flow from Poland and 36% of the flow from Czech Republic was C&C

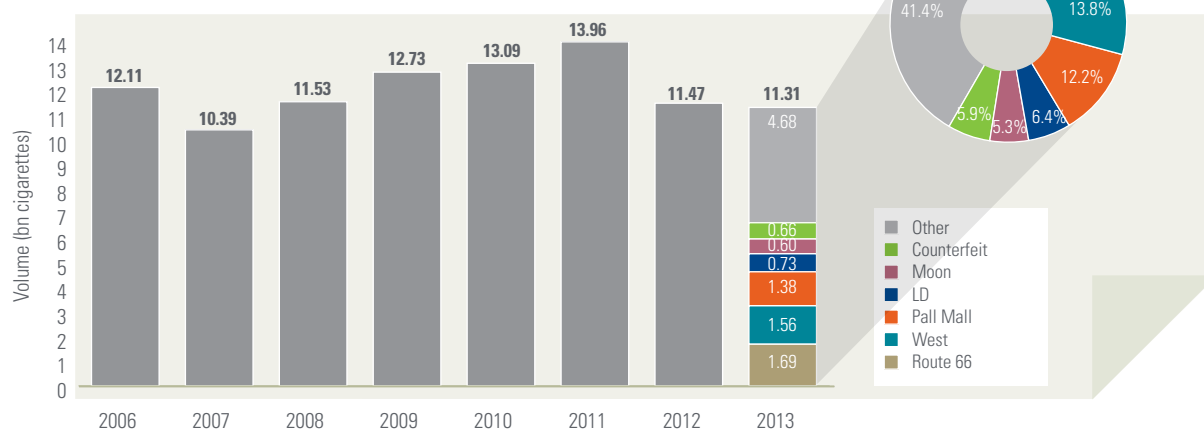
- It is likely that this product was consumed through some individuals exceeding their legal allowance, and by casual street sales in Germany, as many of the packs were collected in East Germany. However, 25% of Polish and Czech packs were collected in West Germany where organised smuggling may be more prevalent
- Over 99% cigarettes from Belarus are C&C. This flow grew by 50% in 2013 and may indicate more sophisticated criminal activity from Belarus, replacing Russia as a large C&C source country
- If all of these cigarettes had been consumed as legally purchased domestic product in Germany, it would have increased taxes raised by the German Government by approximately €2.1 billion

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.

C&C INFLOWS BY BRAND

Total C&C by brand - 2006-2013^{(1)(2)(3)(a)(b)}



Composition of Illicit Whites inflows - 2006-2013^{(1)(3)(b)}

Less than 4% of cigarettes with Duty Free labelling were Illicit Whites

LABELLING OF ILLICIT WHITES INFLOWS TO GERMANY								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country Specific	0.77	2.19	1.89	1.29	1.35	0.90	1.31	45%
Duty Free	0.00	0.10	0.00	0.00	0.01	0.03	0.07	>100%
Unspecified	0.00	0.01	0.12	0.02	0.04	0.00	0.01	>100%
Total Illicit Whites	0.78	2.30	2.01	1.32	1.40	0.93	1.39	49%

The top five C&C brands represent over 50% of the total

- The top five brands consumed as counterfeit and contraband were mainly from Poland and the Czech Republic. These brands are often sold for €2.50 less than similar brands in Germany. Many of these brands often feature in both consumer research surveys and manufacturer sales data and are also widely purchased as ND(L). However, the quantities found in Germany indicate that some of these volumes are allocated to C&C
- Illicit Whites brands grew 49% in 2013 and now make up 12% of total counterfeit and C&C
- 60 brands were Illicit Whites brands. Whilst the source of some of these brands is unknown, many are thought to come from Belarus
 - Fest, manufactured by Grodno Tobacco in Belarus was the largest Illicit Whites brand with 0.4 billion cigarettes consumed in 2013

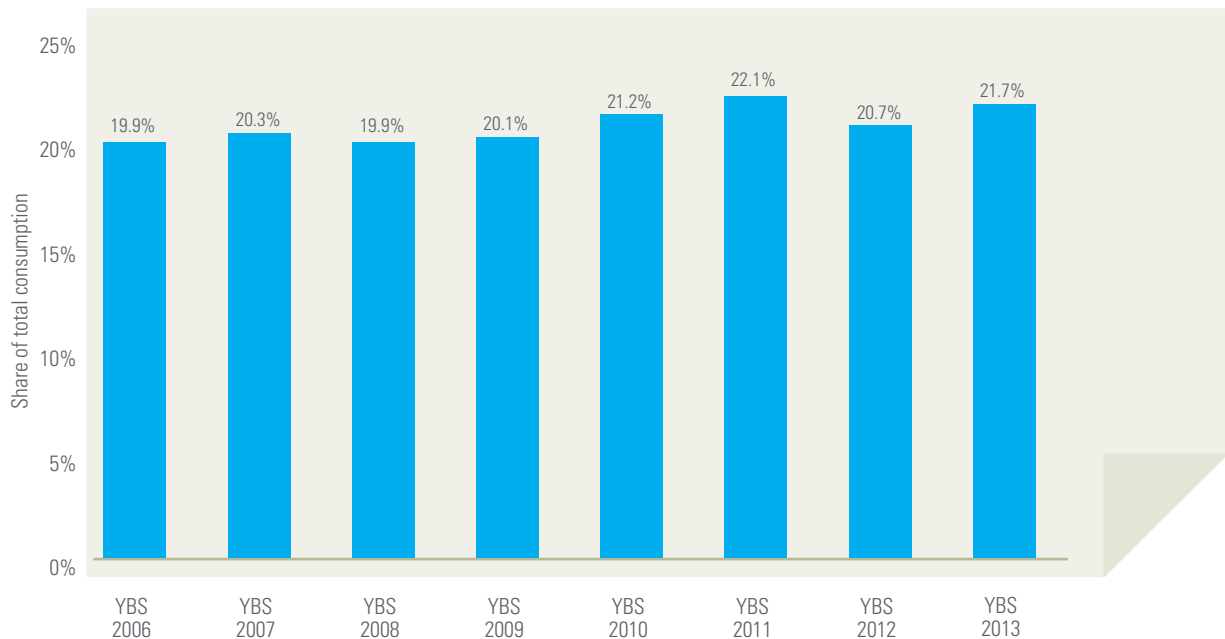
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows
(b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.
(3) KPMG analysis of data sources provided by manufacturers.



EPS results & EU Flow Model

Yellow bag survey non-domestic incidence, 2006-2013⁽¹⁾



GERMANY



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The yellow bag survey in Germany collects 12,000 packs per month from waste recycling centres. This information is collected from 26 recycling centres and is weighted according to the number of packs collected and population base around the recycling centre

- A review of the average pack size is also undertaken by the market research agency which may have had a small impact on the non-domestic incidence (e.g. by 0.1 percentage points in 2012)
- No adjustments were made to the data in our analysis

Sources: (1) Independent agency Empty Pack Surveys, 2006-2013.

ND(L) volume calculations and explanations

KPMG non domestic legal flows Germany

COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 ⁽¹⁾ (bn sticks)	2013 ND(L) (bn sticks)	% of ND
Austria	0.62	0.62	100%
Luxembourg	0.45	0.45	100%

USE OF CONSUMER RESEARCH AND ANY ADJUSTMENTS FOR 2013 DATA							
Country	ND 2013 ⁽¹⁾	Total trips where cigarettes purchased (m) ⁽²⁾⁽³⁾	Number of packs per trip ⁽³⁾	Total packs (m)	Data sources ⁽²⁾⁽³⁾	2013 ND(L) (bn sticks)	% of ND
Czech Republic	6.14	9.2m	21	195.9	Czech Statistical Office, Consumer research	3.92	64%
Poland	7.54	6.6m	25	170.6	Polish Institute of Tourism, Consumer research	3.41	45%

Whilst consumer research has been undertaken in Germany on an annual basis, it has historically under-represented the number of purchases in the Czech Republic and Poland, whilst often over-representing purchases from countries like France and Spain. An alternative method has been developed to consider flows from Poland and the Czech Republic based on the following data-points

- **Border crossings** – Extrapolating historic tourist data from the Czech Statistical Office and the Polish Institute of Tourism gives an estimate of 41.3m trips per year to the Czech Republic and 29m trips per year to Poland
- **Smoking prevalence** – Using the implied smoking prevalence rate of 26.9% it is assumed that all smokers who cross the border buy cigarettes (aged 18 and over)
- **Packs per trip** – The consumer research shows a stable and historic trend that consumers bring back 21 packs from the Czech Republic and 25 packs from Poland – this is within the legal limits

These data points have been used by us in order to calculate the ND(L) volumes for the Czech Republic and Poland

For Luxembourg and Austria, given the high volume of border crossings, along with large samples interviewed within the consumer research, it is assumed that 100% of these flows are considered legal sales

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

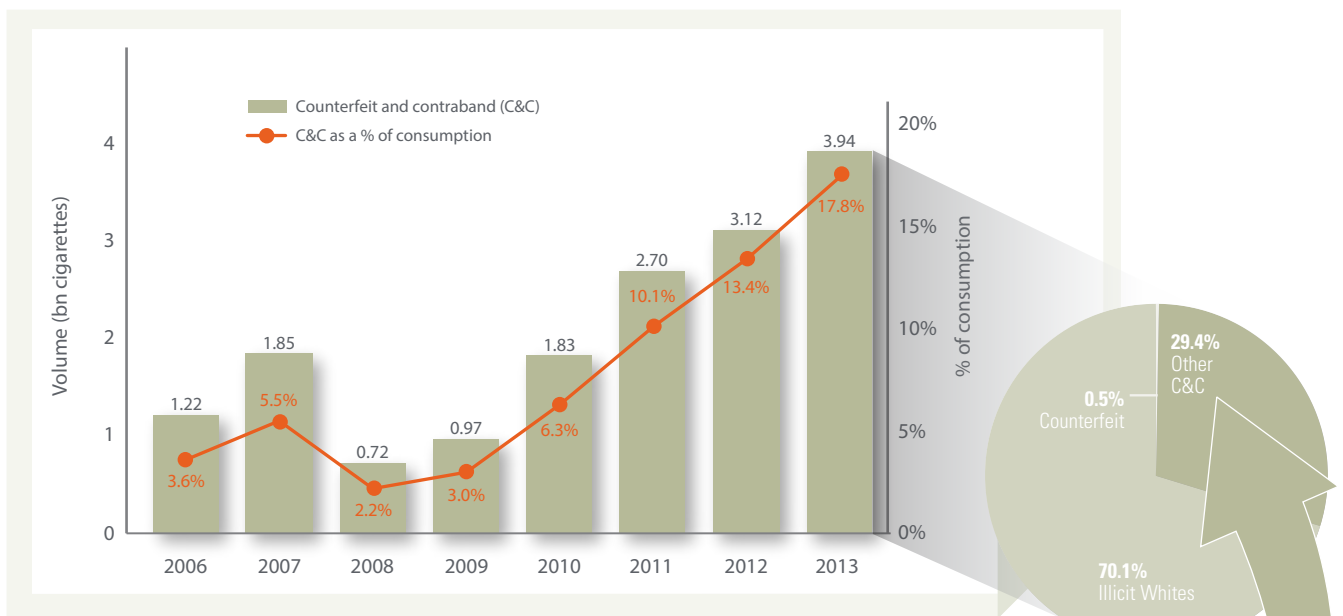


GREECE



Illicit Whites are the largest element of counterfeit and contraband consumption

Manufactured cigarette C&C volumes and share of overall consumption 2006-13

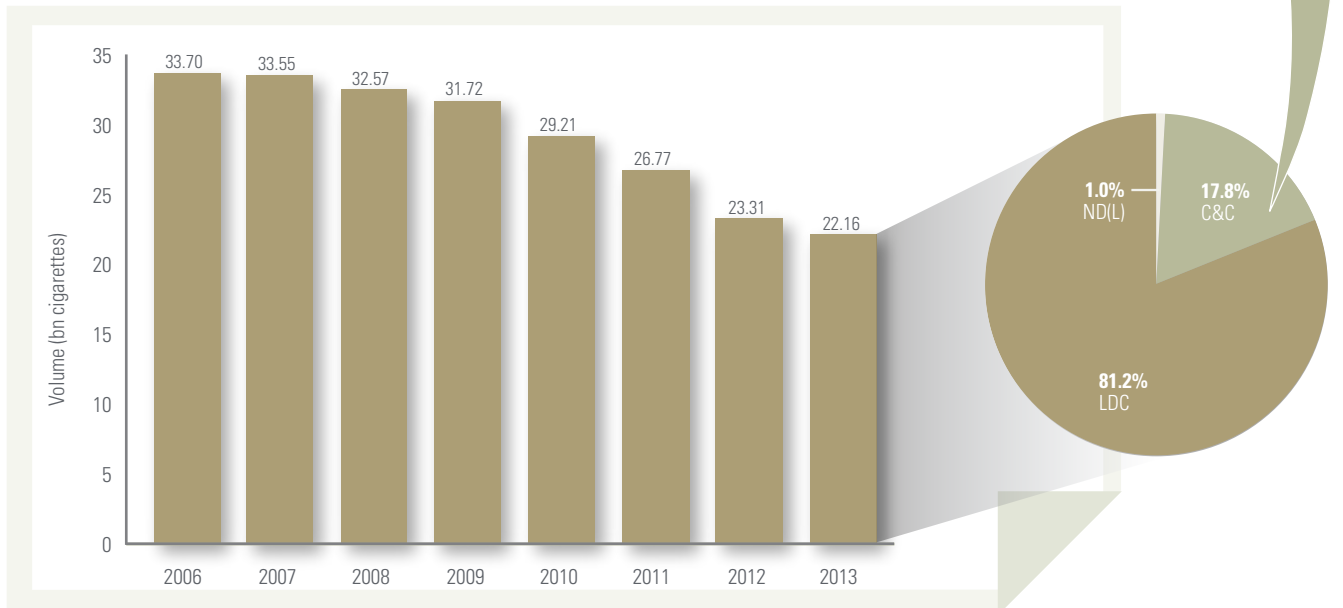


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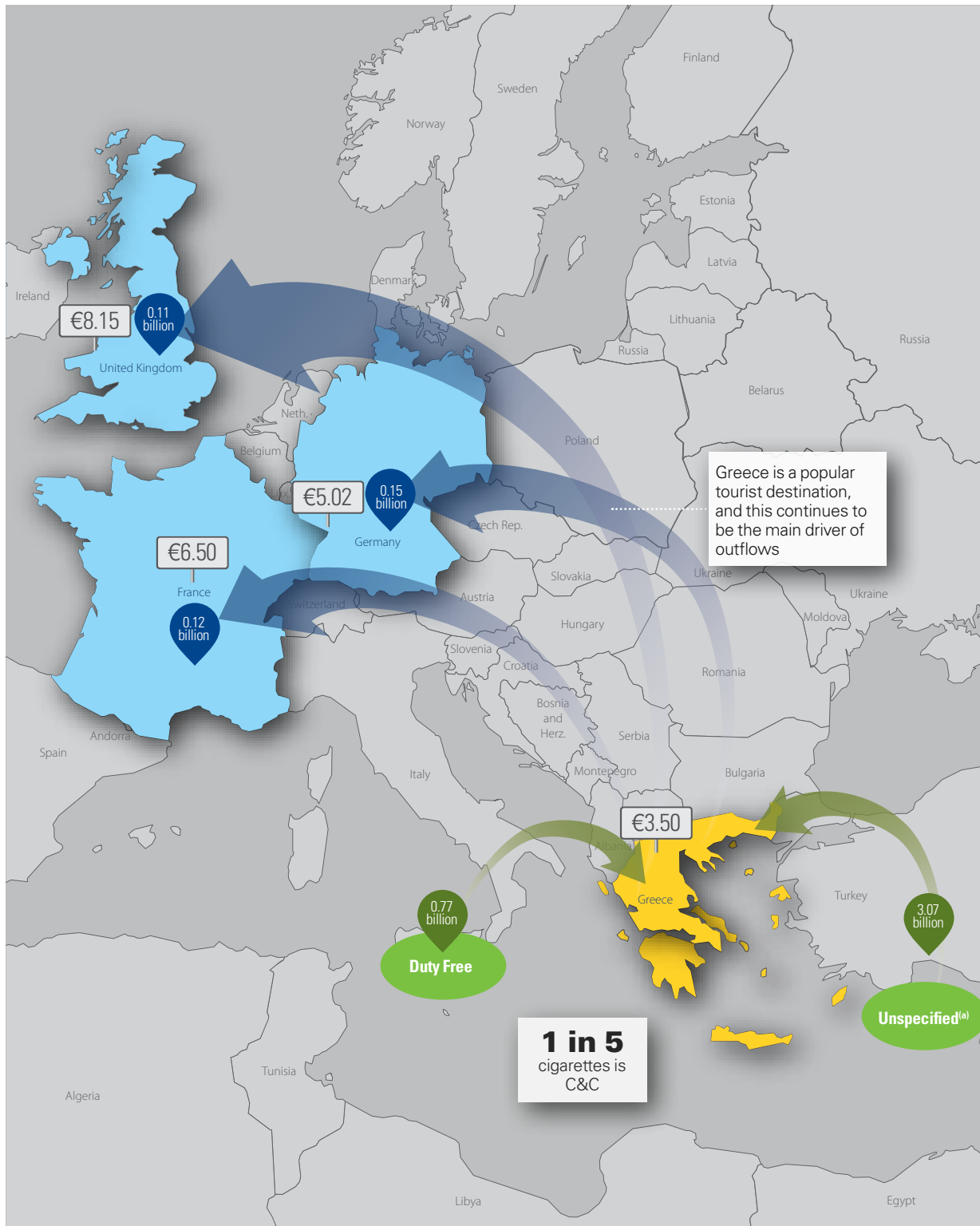


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Manufactured cigarette consumption 2006-13



KEY INFLOWS AND OUTFLOWS



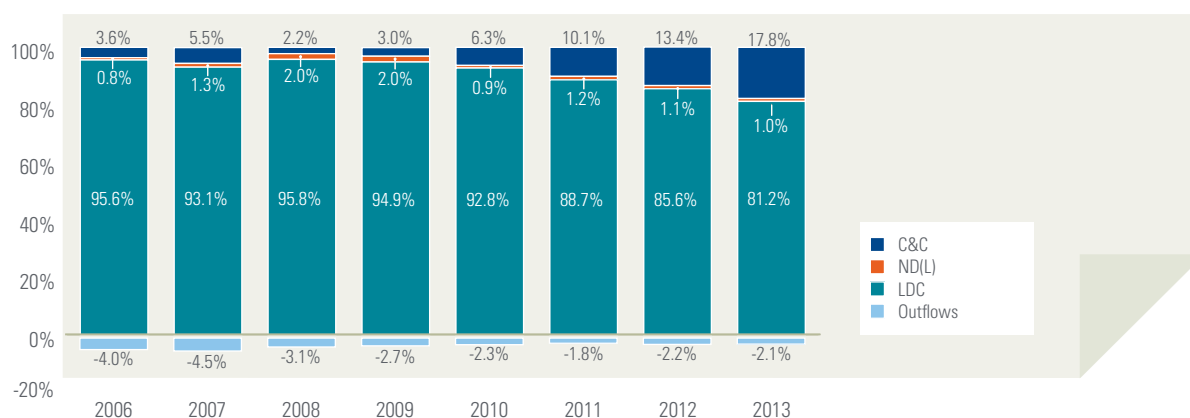
Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.
 Source: (1) KPMG EU Flows Model.

Total consumption declined, despite a sharp increase in C&C volumes

Total manufactured cigarette consumption - Greece ⁽¹⁾⁽²⁾⁽³⁾

TOTAL GREECE CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	33.57	32.74	32.23	30.97	27.78	24.24	20.45	18.46	(10)%
Outflows	-1.34	-1.49	-1.02	-0.85	-0.66	-0.50	-0.50	-0.47	(7)%
Legal domestic consumption (LDC)	32.22	31.25	31.21	30.11	27.12	23.75	19.94	17.99	(10)%
Non-domestic legal (ND(L))	0.26	0.45	0.64	0.64	0.26	0.32	0.25	0.23	(8)%
Counterfeit and contraband (C&C)	1.22	1.85	0.72	0.97	1.83	2.70	3.12	3.94	26%
Total non-domestic	1.48	2.30	1.36	1.61	2.09	3.02	3.37	4.17	24%
Total consumption	33.70	33.55	32.57	31.72	29.21	26.77	23.31	22.16	(5)%

Share of Greece cigarette consumption by type - 2006-2013 ⁽¹⁾⁽²⁾⁽³⁾



- Total manufactured cigarette consumption fell by 5% against a legal domestic sales (LDS) decline of 10%, as smokers appear to have increasingly switched to non-domestic products
- Economic conditions in Greece continued to decline in 2013 as unemployment rose from 24.3% to 27.4% and average PDI declined by 8%. This may have contributed to the decline in LDS volumes, as consumers seek to switch to more affordable alternatives⁽⁴⁾⁽⁵⁾
- There have been significant tax changes in Greece since 2010, as the government reacts to the ongoing recessionary environment. The total tax incidence (excise tax +VAT) as a percent of RSP increased from 73.2% in 2009 to 80.8% in 2013⁽⁶⁾

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Independent agency Empty Pack Surveys, 2006 – 2013. (4) The Economist Intelligence Unit. (5) Euromonitor Passport. (6) EU Tax tables.

INFLOWS AND OUTFLOWS

Three out of four non-domestic packs had unspecified labelling

Main unspecified brands are Gold Mount, RGD and Raquel, accounting for 61% of the total unspecified volume^(b)

Illicit Whites made up 39% of Duty Free inflows

Total inflows by country of origin - 2006-2013^{(1) (a)}

ND INFLOWS TO GREECE									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Unspecified	0.00	0.00	0.00	0.29	0.52	1.21	2.12	3.07	63%
Duty Free	1.04	1.60	1.07	0.86	0.99	1.12	0.76	0.77	8%
Russia	0.01	0.01	0.01	0.08	0.02	0.01	0.04	0.04	18%
Bulgaria	0.01	0.15	0.07	0.04	0.02	0.03	0.03	0.03	(7)%
Serbia	0.03	0.03	0.00	0.00	0.00	0.02	0.01	0.01	>100%
Counterfeit								0.02	n/a
Other	0.38	0.52	0.21	0.33	0.54	0.64	0.42	0.23	(46)%
Total inflows	1.48	2.30	1.36	1.61	2.09	3.02	3.37	4.17	24%

- Illicit Whites of unspecified origin are the main driver of increased non-domestic incidence in 2013
- The main Illicit Whites brands present are Gold Mount, RGD and Raquel, which account for 61% of the total unspecified volume^(b)
- Duty Free volumes continue to be a significant non domestic inflow, though this has declined as a proportion of the total; 39% of Duty Free volumes are Illicit Whites brands with President and Bon the most prevalent
- Greece is also bordered by low price countries such as Albania and Macedonia, but inflows are small from these regions.

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM GREECE									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Germany	0.27	0.28	0.24	0.26	0.19	0.17	0.18	0.15	(19)%
France	0.11	0.13	0.14	0.09	0.12	0.04	0.07	0.12	87%
UK	0.68	0.76	0.32	0.28	0.16	0.12	0.16	0.11	(31)%
Netherlands	0.07	0.06	0.03	0.04	0.02	0.03	0.03	0.03	9%
Italy	0.02	0.07	0.04	0.08	0.08	0.05	0.02	0.02	30%
Austria	0.05	0.03	0.01	0.01	0.01	0.01	0.01	0.01	0%
Other	0.14	0.17	0.23	0.09	0.08	0.06	0.04	0.03	(38)%
Total outflows	1.34	1.49	1.02	0.85	0.66	0.50	0.50	0.47	(7)%

- The largest outflows from Greece are to Germany, France and the UK. Greece is a popular tourist destination for holidaymakers from these countries, and as a result these flows are likely to be driven by travel trends

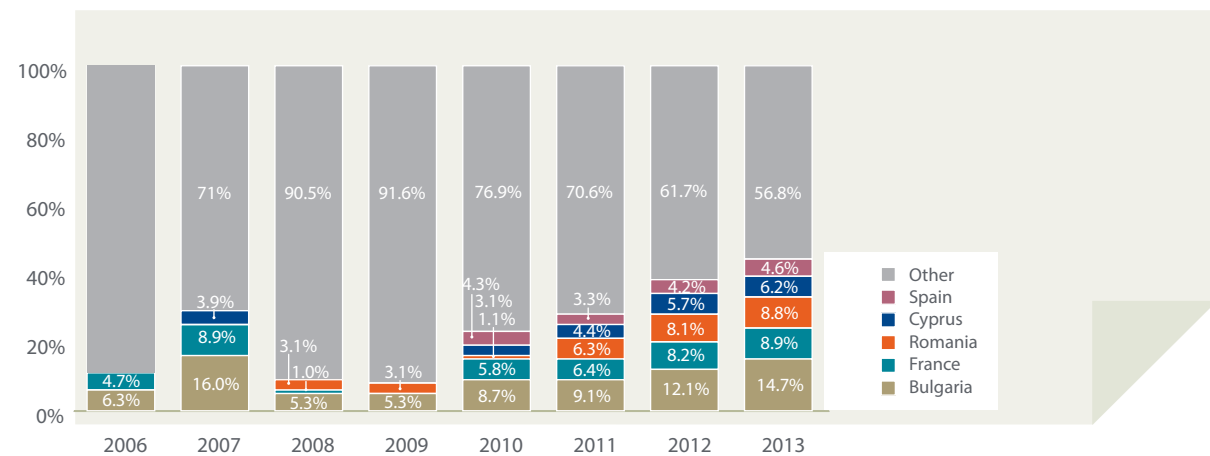
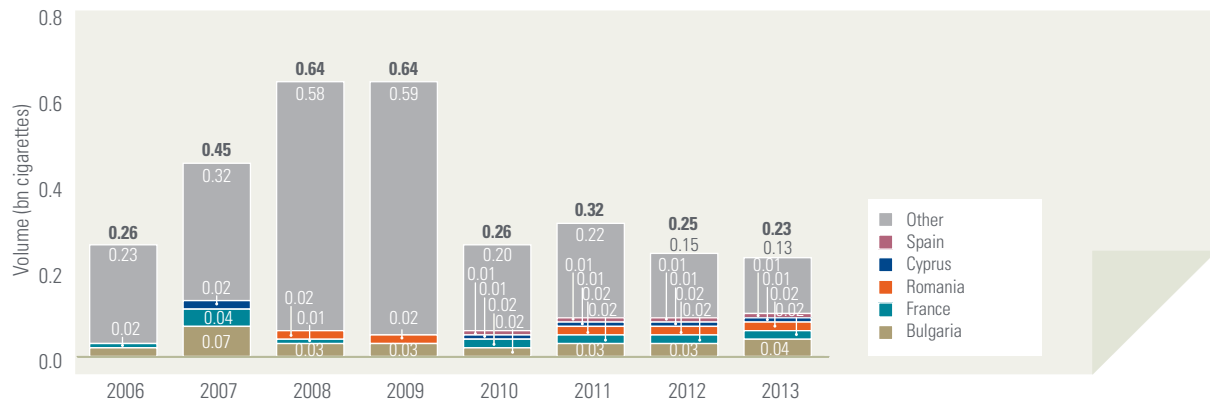
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition. (b) RGD is manufactured by China Tobacco Hubei Industrial LLC.

Source: (1) KPMG EU Flows Model.



ND(L) volumes remained marginal

ND(L) by origin - 2006-2013^{(1)(2)(3)(a)(b)}



- ND(L) inflows to Greece have traditionally been low, and continue to be so in 2013, accounting for only 1% of total consumption
- The main legal sources of non-domestic cigarettes in 2013 were nearby Bulgaria and popular travel destinations such as France, Romania, Cyprus and Spain

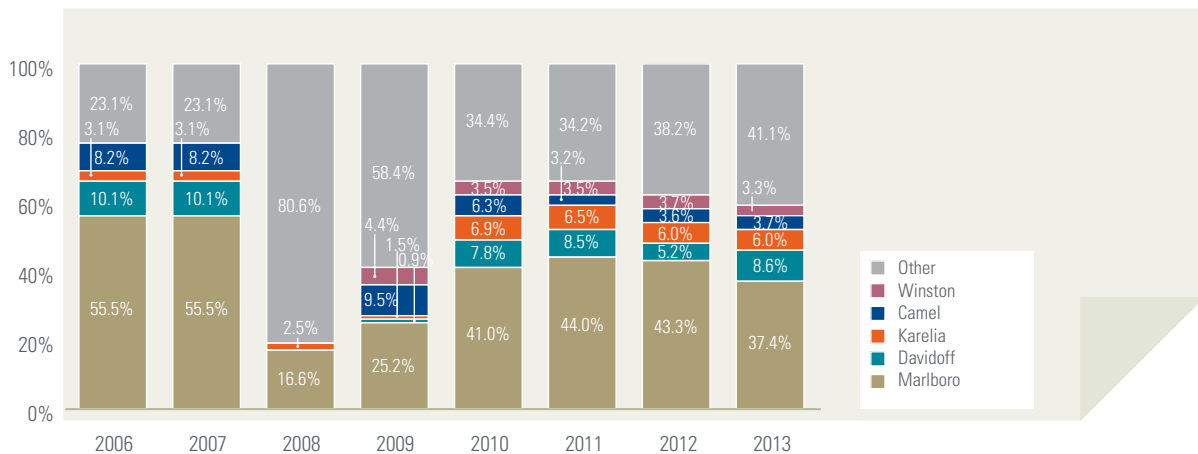
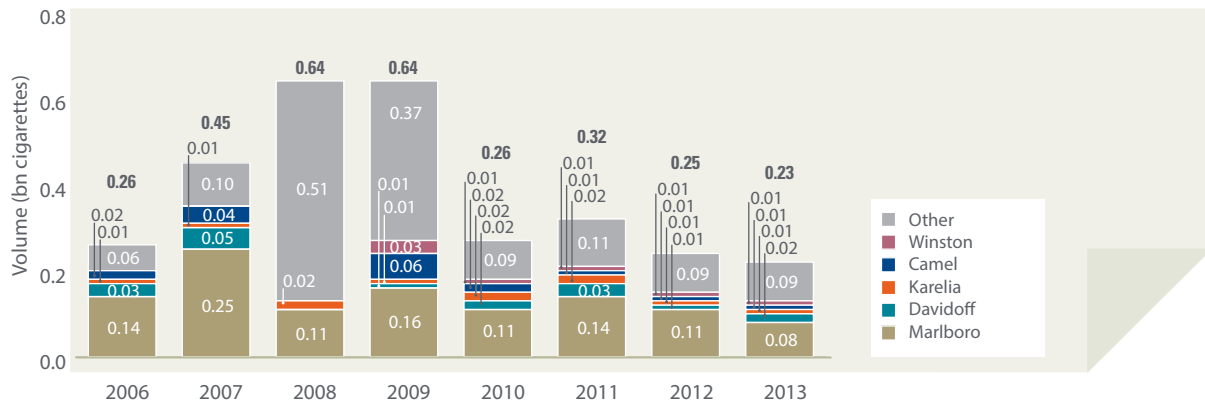
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013^{(1)(2)(3)(a)}



- The most popular ND(L) brands remained consistent with prior year, with only small fluctuations in volume terms

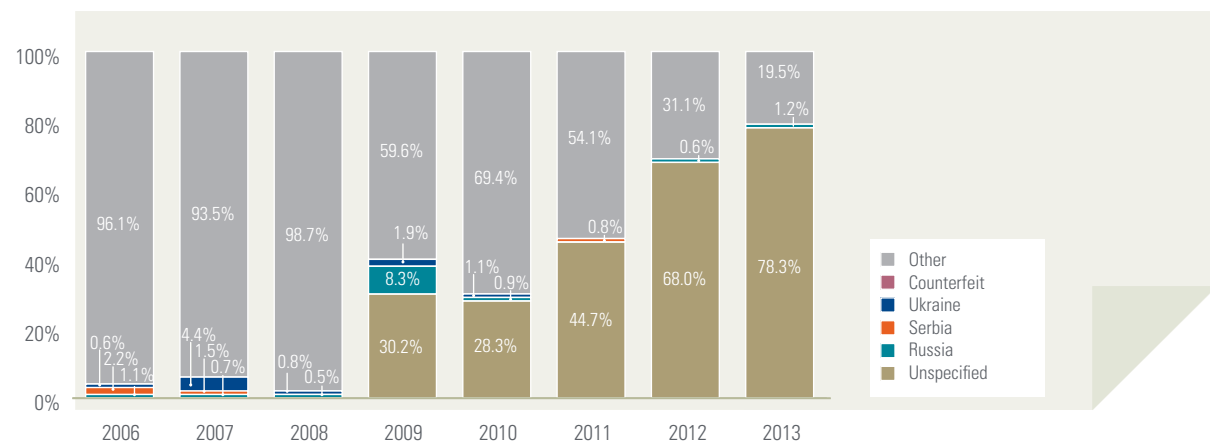
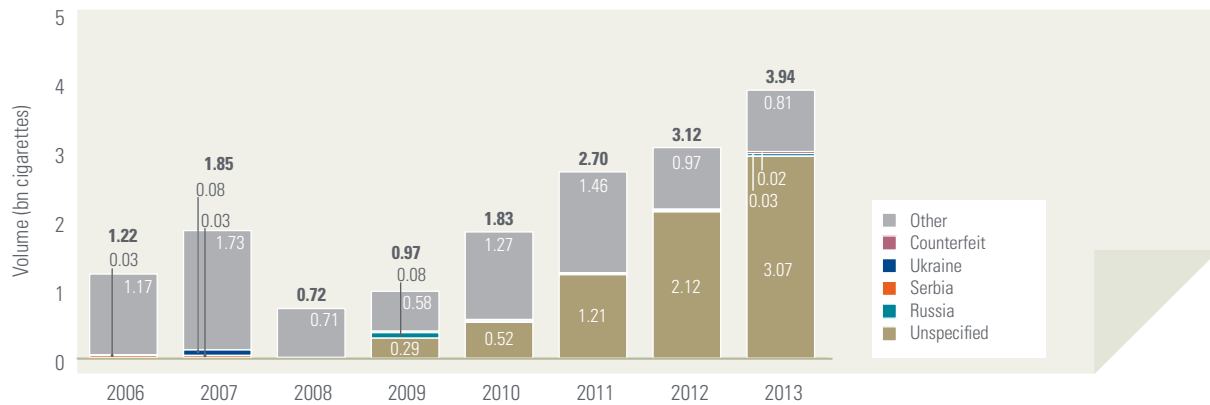
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



Illicit Whites brands with unspecified labelling continued to dominate C&C volumes

C&C by origin - 2006-2013^{(1)(2)(3)(a)}



GREECE



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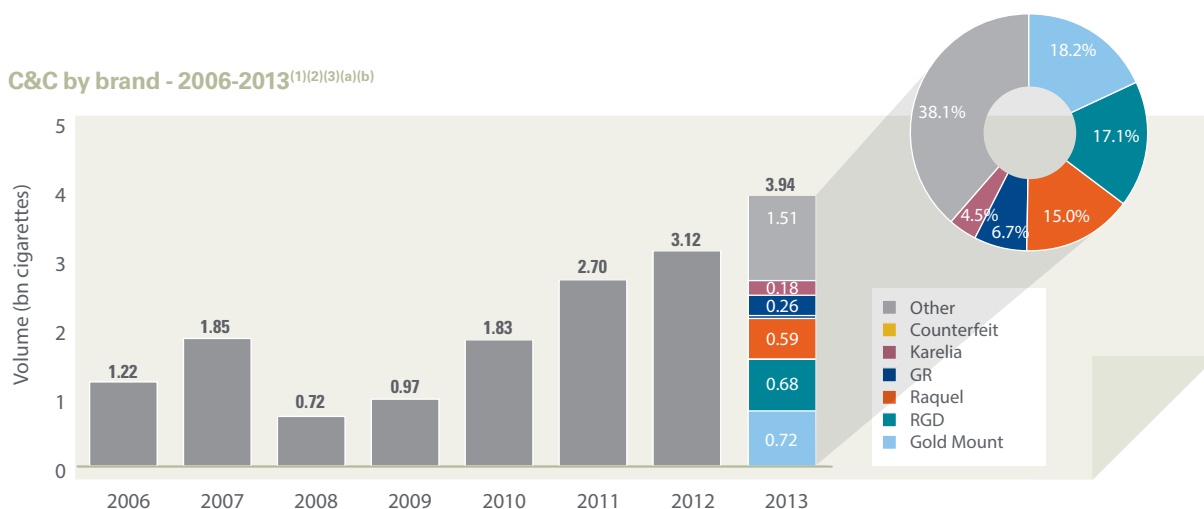
- All unspecified inflows to Greece have been classified as C&C, as they are Illicit Whites brands
- The volume of unspecified C&C in 2013 was dominated by three brands; Gold Mount (23% of the total volume), RGD (21%) and Raquel (17%). All three are Illicit Whites brands.
- If the 3.94bn C&C cigarettes in 2013 had been legally purchased in Greece the tax revenue gained would have been approximately €565m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) UNWTO Tourism Factbook 2008-2012, UNWTO. (3) Synovate/Ipsos ND(L) research 2013. (4) KPMG analysis EU Tax tables to see price increases. (5) Global Consumer Tracking Survey giving smoking incidence.

C&C INFLOWS BY BRAND

C&C by brand - 2006-2013^{(1)(2)(3)(a)(b)}



- Total C&C in Greece has increased by 26% between 2012 and 2013
- Most of this rise can be attributed to an influx of the Illicit Whites brands Gold Mount, RGD and Raquel with unspecified labelling, which account for almost half of the total C&C volume^(c)

Illicit Whites made up 39% of overall Duty Free flows

Composition of Illicit Whites inflows - 2006-2013^{(1)(3)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO GREECE								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.04	0.02	0.02	0.07	0.07	0.13	0.05	(61)%
Duty Free	0.05	0.04	0.20	0.18	0.20	0.43	0.29	(33)%
Unspecified	0.00	0.00	0.02	0.20	0.81	2.07	2.43	17%
Total Illicit Whites	0.09	0.05	0.24	0.46	1.08	2.63	2.76	5%

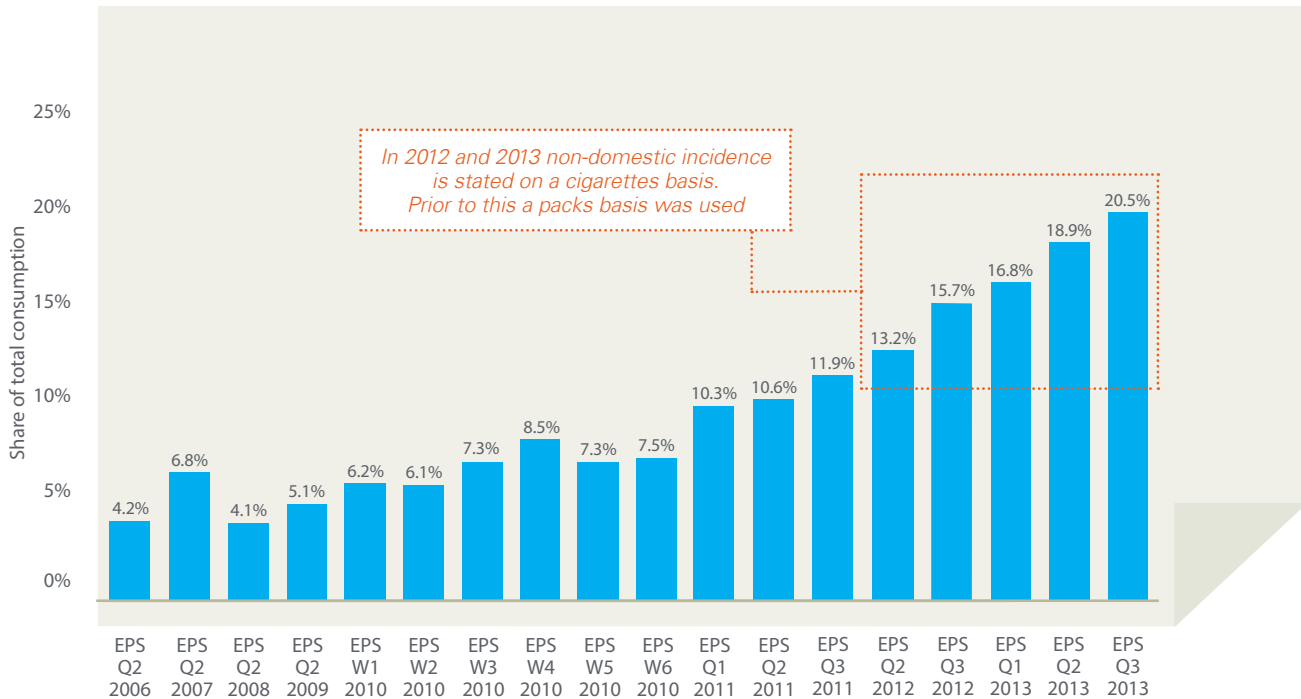
- Volumes of Illicit Whites have shown a steadily increasing trend since 2009
- Gold Mount, Raquel, and RGD are the main Illicit Whites marked as unspecified, accounting for 78% the unspecified Illicit Whites balance^(c)
- President and Bon are the main Illicit Whites marked as Duty Free, accounting for 40% of the Duty Free Illicit Whites balance
- VIP from Georgia contributes 47% of the country specific Illicit Whites

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows (b) A methodology and definition of Illicit Whites is provided in the methodology section. (c) RGD is manufactured by China Tobacco Hubei Industrial LLC

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

EPS results & EU Flow model

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



GREECE



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- The empty pack survey in Greece collected 7,000 packs during the third quarter of the year. It collects these packs across 20 towns and cities. The number of packs collected in the town or city is weighted by its population
- The 2013 EU flows model has been prepared using the Q3 EPS for Greece. This is the only wave that is jointly commissioned by all manufacturers and where all packs have been examined to help determine which are genuine and which are counterfeit. However, the non-domestic incidence of 16.8% and 18.9% that was recorded in Q1 and Q2 respectively has been used to inform the overall non-domestic incidence of 18.8%, despite less data being available to us^(a)

Note: (a) Prior to Q3 2013 EPS results may have been used that were funded by PMI solely, or PMI and a combination of the other manufacturers.

Source: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

ND(L) volumes calculations and explanations

KPMG non domestic legal flows Greece

COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 ⁽¹⁾ (bn sticks)	2013 ND(L) (bn sticks)	% of ND
Bulgaria	0.04	0.04	100

- Consumer research is used to calculate the ND(L) inflow volume to Greece
- There were 0.24 million trips to Bulgaria in 2013 where cigarettes were purchased. On average 7 packs were purchased per trip, giving a total legal volume of 0.04bn cigarettes. The total amount of non-domestic cigarettes from Bulgaria in the EPS study was 0.04bn, and so it is assumed the flow from Bulgaria is 100% legal



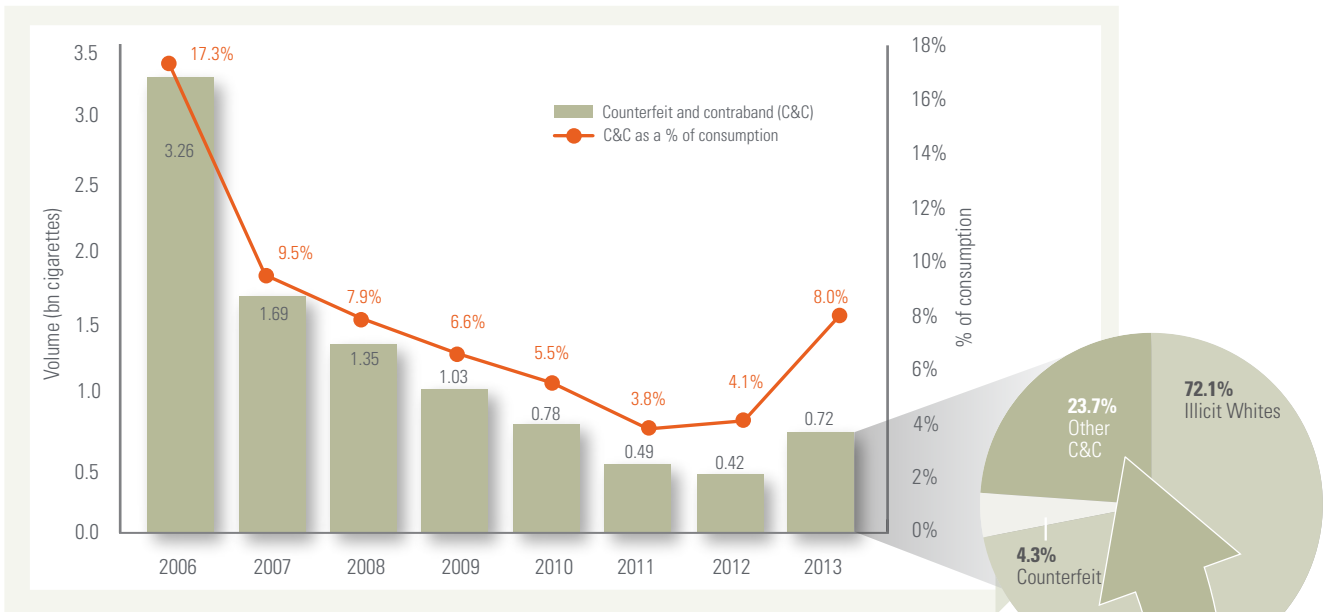
Source: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

HUNGARY



Counterfeit & Contraband increased, and share of consumption doubled

Manufactured cigarette C&C volumes and share of overall consumption 2006-13

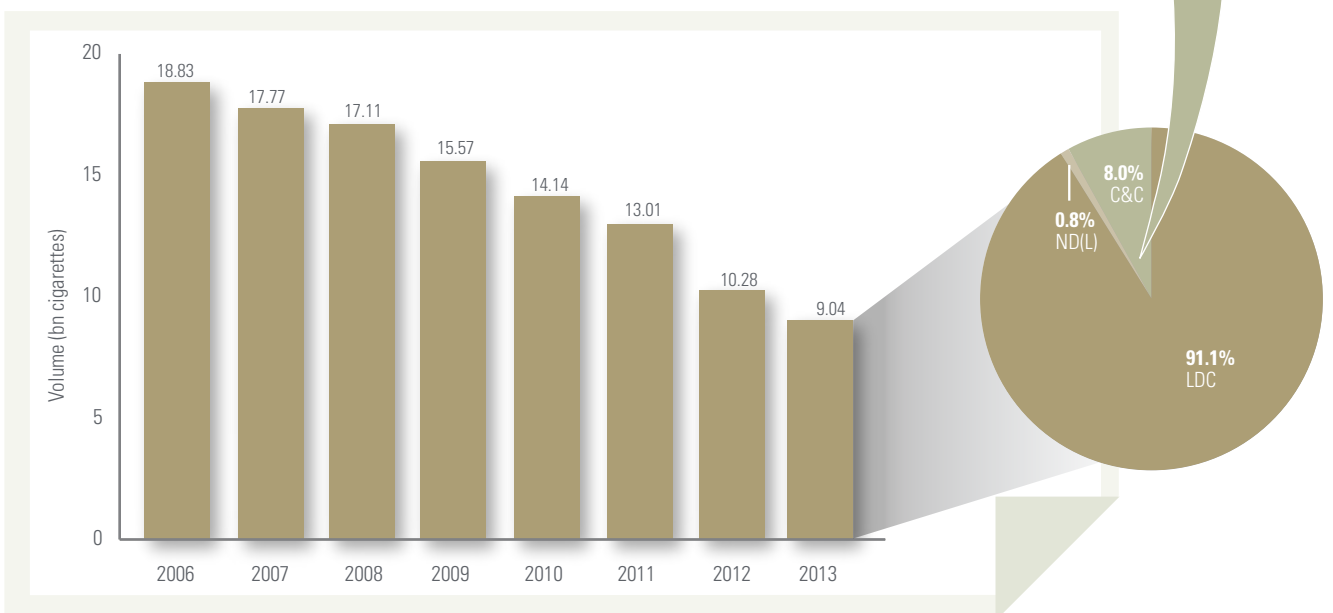


HUNGARY

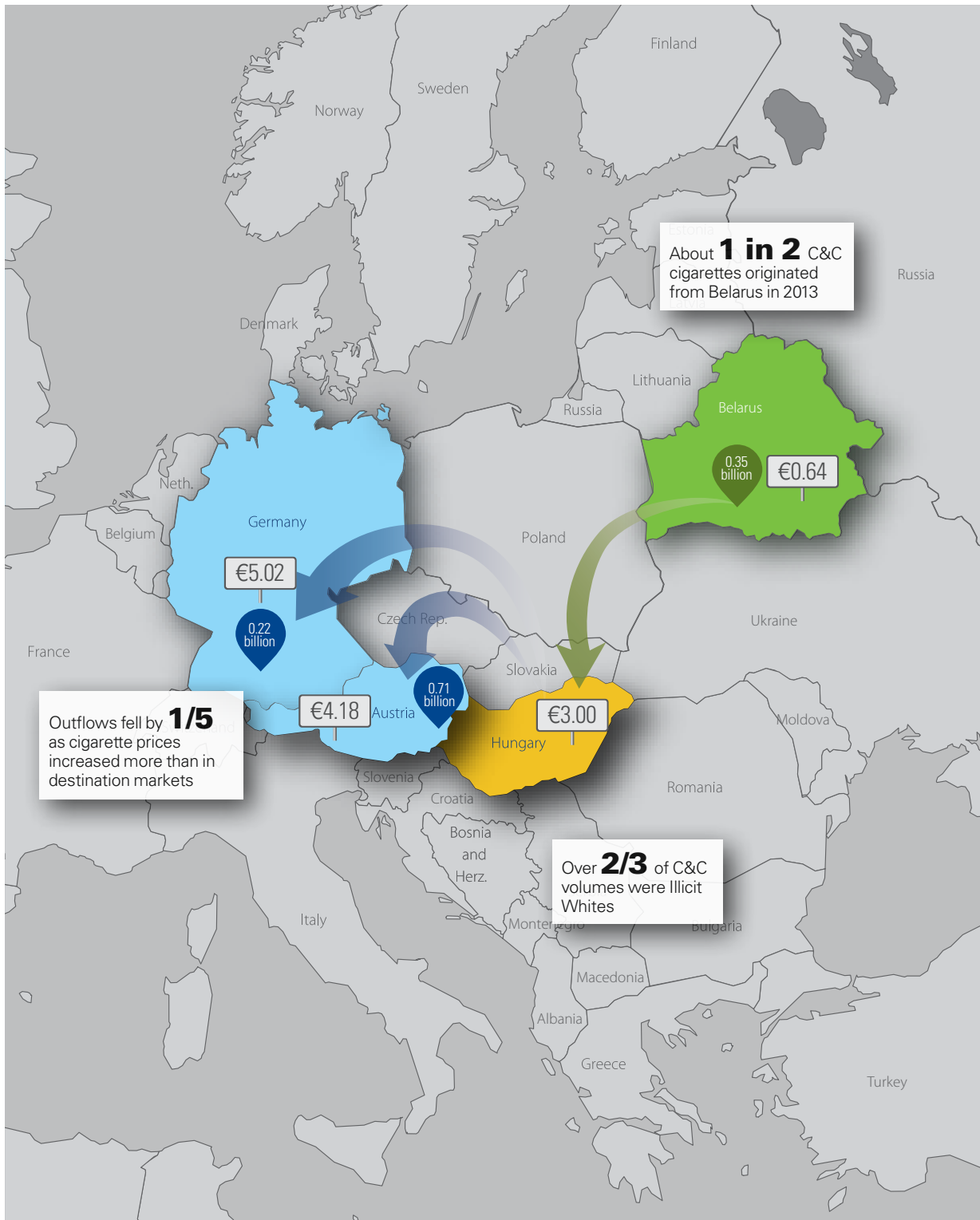


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Manufactured cigarette consumption 2006-13



KEY INFLOWS AND OUTFLOWS



HUNGARY
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Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

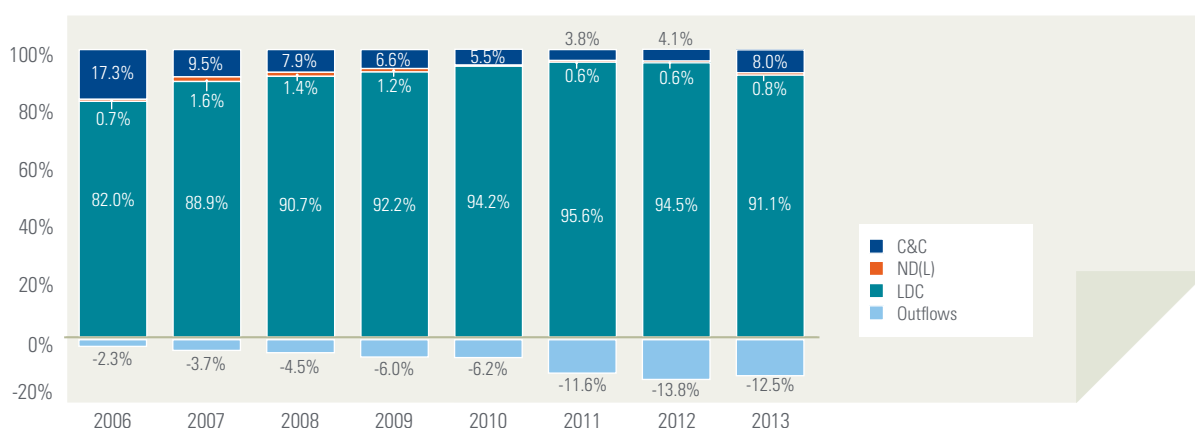
Source: (1) KPMG EU Flows Model.

Consumption of manufactured cigarettes continued to fall in 2013 resulting in a significant decline in legal domestic sales

Total manufactured cigarette consumption – Hungary^{(1)(2)(a)}

TOTAL HUNGARY CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	15.87	16.46	16.30	15.30	14.18	13.94	11.21	9.36	(17)%
Outflows	-0.44	-0.66	-0.78	-0.93	-0.87	-1.50	-1.41	-1.13	(20)%
Legal domestic consumption (LDC)	15.43	15.80	15.53	14.36	13.31	12.44	9.80	8.24	(16)%
Non-domestic legal (ND(L))	0.14	0.28	0.24	0.18	0.05	0.08	0.06	0.08	30%
Counterfeit and contraband (C&C)	3.26	1.69	1.35	1.03	0.78	0.49	0.42	0.72	73%
Total non-domestic	3.40	1.97	1.59	1.21	0.83	0.57	0.48	0.80	68%
Total consumption	18.83	17.77	17.11	15.57	14.14	13.01	10.28	9.04	(12)%

Share of Hungary cigarette consumption by type 2006-2013⁽¹⁾⁽²⁾



In Hungary, consumption of manufactured cigarettes again declined substantially versus 2012 by 12.1%

- The decline was reflected in a 16.5% decrease in legal domestic sales (LDS) of manufactured cigarettes in the year. This took place against an economy showing some signs of recovery
 - There were signs of improvement in some of the key economic indicators; unemployment fell from 10.7% in 2012 to 9.1% in 2013⁽³⁾, while there was also growth in GDP per capita, though PDI remained broadly constant⁽⁴⁾
- The decline in consumption was less than the fall in LDS, as cigarette inflows increased this year
- In December 2012, there was an increase in the specific and ad valorem excise components of cigarette taxation. This contributed to the total 9% increase in WAP⁽⁵⁾
- Legal domestic sales of fine cut tobacco have continued to increase in recent years⁽⁶⁾. This suggests there may have been some switching to OTP by consumers seeking cheaper alternatives
- There have been a number of regulatory changes in the Hungarian tobacco industry in 2013, which are likely to have contributed to the decline in consumption
- The key changes were the introduction of a retail monopoly for tobacco and minimum retail margins on tobacco products. This is explained in further detail on page 149

Note: a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) 2014 Economist Intelligence Unit. (4) Euromonitor, downloaded January 2014. (5) EC Excise Duty tables (Part III – Manufactured Tobacco). (6) European Releases for consumption of fine cut tobacco, 2002-2012.



InfloWS were relatively low but grew significantly as a share of consumption, mainly due to regulatory changes

Total inflows by country of origin 2006-2013^{(1)(a)}

ND INFLOWSTO HUNGARY									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Belarus	0.00	0.00	0.00	0.00	0.00	0.00	0.07	0.35	>100%
Duty Free	0.61	0.17	0.13	0.12	0.01	0.01	0.03	0.16	>100%
Ukraine	2.48	1.42	1.14	0.81	0.46	0.25	0.13	0.07	(46)%
Serbia	0.05	0.06	0.00	0.12	0.19	0.10	0.14	0.06	(53)%
Romania	0.10	0.13	0.11	0.03	0.03	0.03	0.02	0.02	31%
Counterfeit								0.03	n/a
Other	0.17	0.18	0.21	0.13	0.13	0.17	0.09	0.10	13%
Total inflows	3.40	1.97	1.59	1.21	0.83	0.57	0.48	0.80	68%

Inflows increased significantly this year to represent their highest share of total consumption since 2007

- In April 2013, new legislation governing the tobacco market was widely announced throughout the media⁽²⁾⁽³⁾⁽⁴⁾
- The first element was a new tender issued for retail tobacco sales (essentially establishing a state monopoly where only licensed tobacconists can sell cigarettes). As a result, the number of outlets selling cigarettes fell from 42,000 to an initial 4,500 (5,600 by September 2013)
- The second key change was the introduction of a pre-set and fixed retail margin on all tobacco products. These changes were effective July 2013
- During this period, inflows from Belarus increased, whilst Duty Free volumes also increased. ND incidence was especially evident in the Q4 wave of the Empty Pack Surevy (EPS)
- Illicit Whites labelled as Duty Free account for a large proportion of this growth, now representing nine tenths of total Duty Free flows versus 40.0% in 2012. The main Illicit Whites brands in this category appear to be Jin Ling, Lifa and Compliment

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM HUNGARY									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Austria	0.13	0.32	0.45	0.48	0.48	0.99	0.99	0.71	(28)%
Germany	0.12	0.12	0.13	0.16	0.17	0.21	0.20	0.22	12%
Ireland	0.01	0.01	0.03	0.03	0.03	0.04	0.06	0.05	(27)%
Other	0.18	0.20	0.16	0.26	0.19	0.26	0.16	0.14	(9)%
Total outflows	0.44	0.66	0.78	0.93	0.87	1.50	1.41	1.13	(20)%

Outflows from Hungary fell by 20.2% but only declined marginally in terms of share of consumption

- The greatest change was the decline in flows to Austria. With no evident decline in outbound tourism from Austria to Hungary in the year⁽⁵⁾, this may be due to the cigarette price increases relative to other central European markets
- For example, in 2012 a pack of 20 cigarettes could be purchased from the Czech Republic for €2.73 and from Hungary for €2.44 (based on WAP⁽⁶⁾). Hungarian excise increases resulted in prices from these two markets broadly equalising and over the course of 2013
- During this period, flows from Hungary to Austria decreased and appear to have been offset by an increase in flows from Czech Republic to Austria

Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

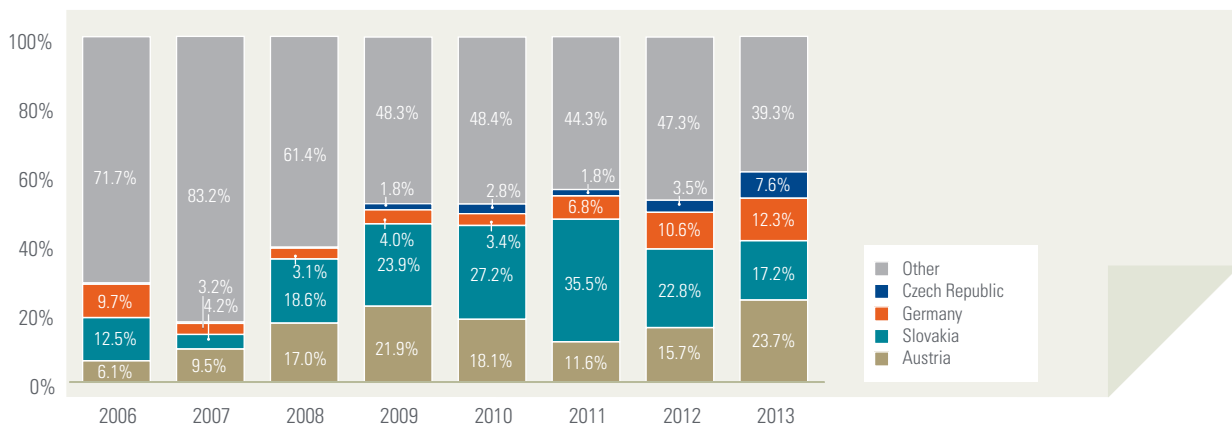
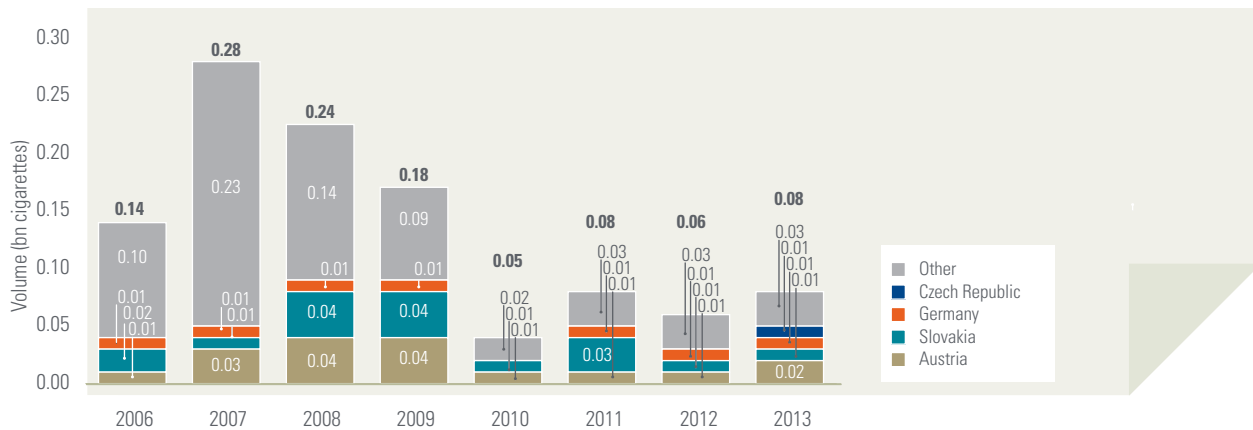
Source: (1) KPMG EU Flows Model. (2) <http://www.bbc.co.uk/news/world-europe-23146659>. (3) Agence France Presse. (4) http://www.bbj.hu/business/state-to-issue-new-tobacco-licenses_65276. (5) UN WTO Tourism Factbook 2008-2012, UN WTO. (6) EC Excise Duty tables (Part III – Manufactured Tobacco).



NON-DOMESTIC LEGAL INFLOW BY COUNTRY

Legal inflows continued to represent a very small share of non-domestic volumes

ND(L) by origin - 2006-2013^{(1)(2)(3)(a)(b)}



HUNGARY



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Non-domestic legal (ND(L)) flows remain low and only marginally increased in 2013

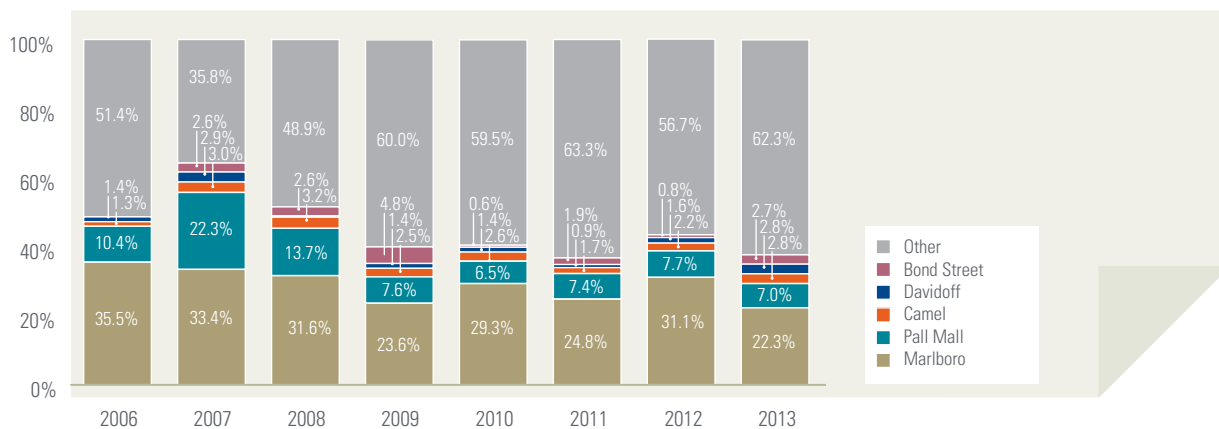
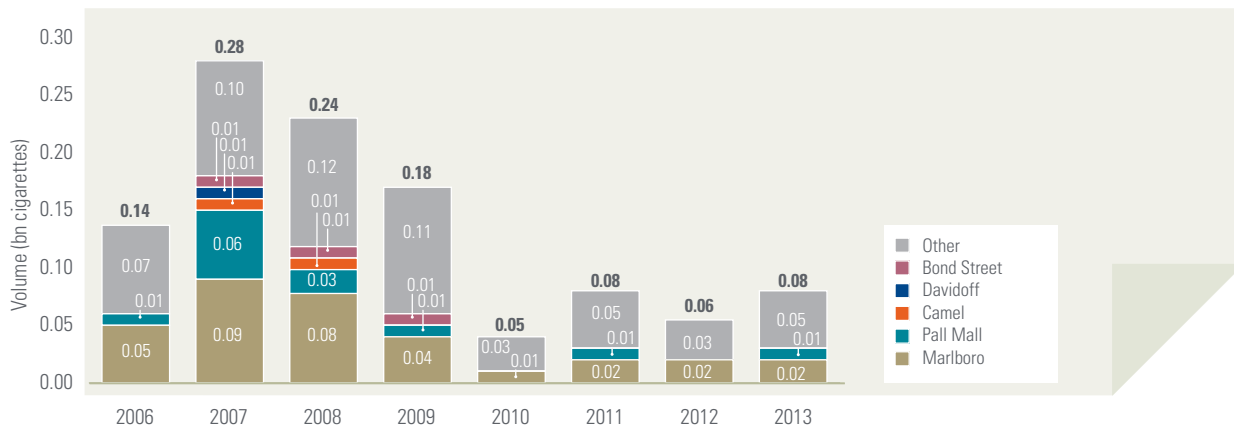
- The largest legal flows into Hungary originate from neighbouring and nearby central European markets such as Austria, Slovakia, Germany and Czech Republic
- Growth in ND(L) was largely driven by greater flows from Austria, which may have been a result of higher outbound tourism during the year⁽³⁾
- There were also greater volumes from Czech Republic and Germany; these flows were entirely classified as legal flows based on these markets being equivalently or higher priced than Hungary

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) UNWTO Tourism Factbook 2008-2012, UNWTO. (3) Synovate/Ipsos ND(L) research 2013. (4) KPMG analysis EU Tax tables to see price increases. (5) Global Consumer Tracking Survey giving smoking incidence.

NON-DOMESTIC LEGAL INFLOW BY BRAND

ND(L) by brand - 2006-2013^{(1)(2)(3)(a)}



Growth in the Pall Mall and Camel brands accounts for most of the increase in ND(L) volumes

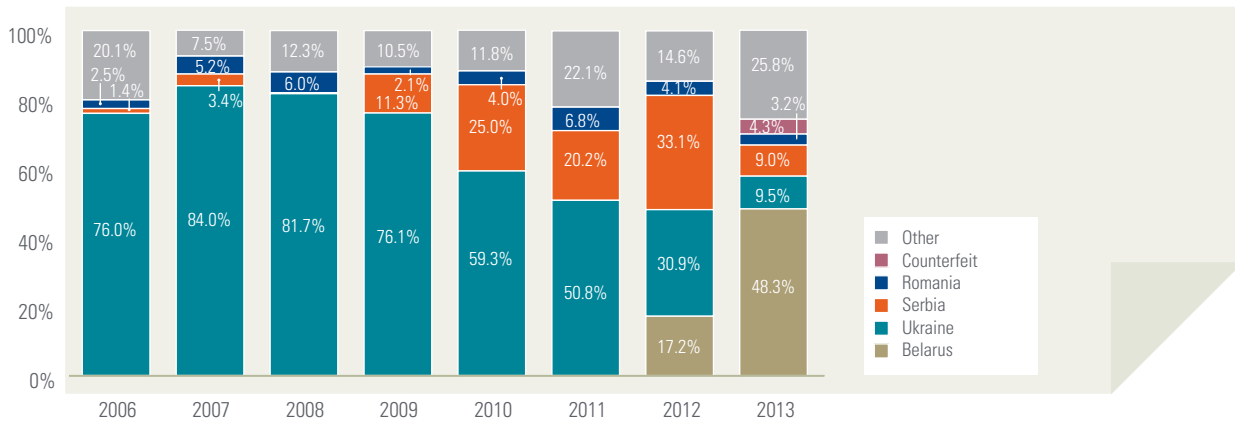
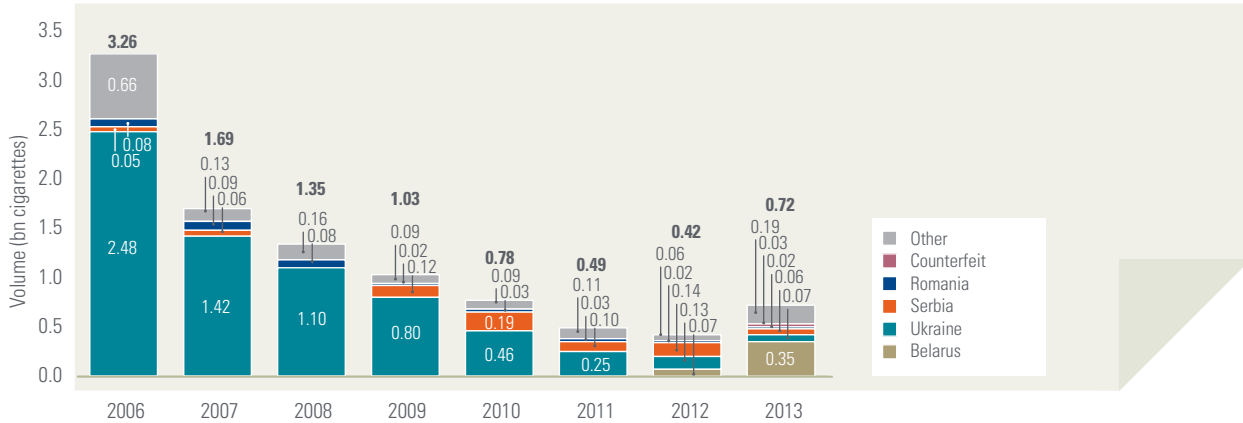
- Legal inflows of cigarettes are comprised of a range of brands, with Marlboro the most popular
- “Other” comprises smaller volumes of around 10-15 individual brands

Note: (a) Additional details of key ND(L) calculations provided overleaf. Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



Overall consumption of counterfeit and contraband products increased substantially, driven by volumes from Belarus

C&C by origin - 2006-2013^{(1)(2)(a)(b)}



HUNGARY



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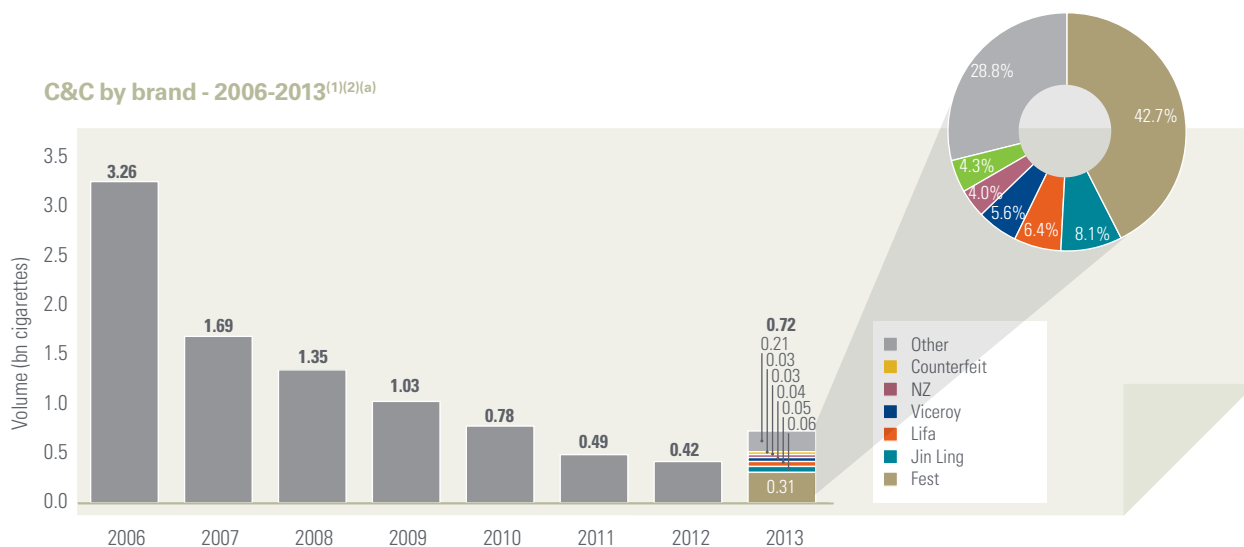
Greater counterfeit and contraband (C&C) volumes account for almost all of the growth in non-domestic incidence in Hungary this year

- The largest increase in flows came from Belarus, which increased from 0.07bn cigarettes to 0.35bn. This was entirely allocated to C&C as a result of minimal and declining outbound tourist flows in the year⁽³⁾
- Despite price increases in Hungary following excise and minimum retail margin changes, flows from some cheaper markets such as Ukraine and Serbia declined
- This may be the result of consumers switching to comparatively cheaper Belarusian origin cigarettes
- "Other" largely comprises Illicit Whites labelled as Duty Free (0.14bn cigarettes)
- Counterfeit cigarettes appear to be a relatively minor issue in Hungary, with flows representing only 4.3% of total C&C consumption this year
- If these C&C cigarettes had been legally purchased in Hungary the tax revenue would have been approximately €87m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-2012, UN WTO.

C&C INFLOWS BY BRAND



Grodno Tobacco brands such as Fest, accounted for most of the growth in C&C by brand, as flows from Belarus increased significantly

- Illicit Whites have become more prevalent in Hungary in 2013
- Illicit Whites with country specific labelling represent the largest share of total Illicit Whites consumption. Brands include Fest and NZ, originating from Belarus. There are also Illicit Whites labelled as Duty Free consumed such as Jin Ling and Lifa, produced by the Baltic Tobacco Factory
- Viceroy continues to enter the Hungarian market as a C&C flow from Ukraine and Serbia

Breakdown of Illicit Whites by type 2007-2013^{(1)(2)(a)(b)}

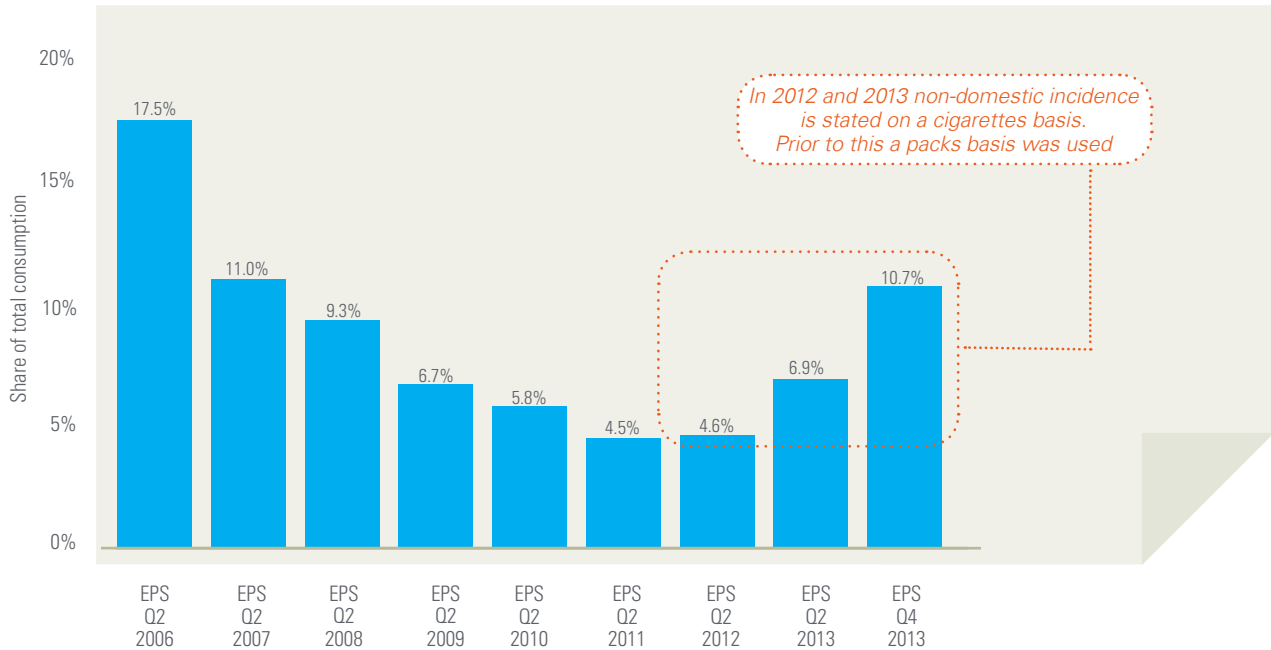
LABELLING OF ILLICIT WHITES INFLOWS TO HUNGARY								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.02	0.00	0.01	0.04	0.01	0.11	0.37	>100%
Duty Free	0.00	0.00	0.01	0.00	0.00	0.01	0.14	>100%
Unspecified	0.00	0.00	0.03	0.02	0.00	0.00	0.01	>100%
Total Illicit Whites	0.03	0.00	0.04	0.06	0.01	0.12	0.52	>100%

Note: (a) Additional details of key ND(L) calculations provided overleaf. Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



EPS results & EU Flow model

Empty Pack Survey non-domestic estimates 2006-2013^{(1)(a)}



HUNGARY



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- The EPS in the Hungary collected 33,996 packs during the course of the year. This was undertaken through two waves, one conducted in Q2 (May and June) and one in Q3/Q4 (September and October). Each wave collected 16,998 packs across the 40 largest cities. The number of packs collected in each city is weighted by the city population
- Until 2010, the empty pack survey in Hungary was used to monitor the illicit cigarette trade and therefore focused on high incidence regions. In 2011, in order to fairly represent the issue across the entire population, 2011, the methodology was changed to that described above. This may account to some extent for the lower non-domestic incidence in the 2011 and 2012 EPS

Note: (a) The independent agency Empty Pack Survey results included 'Focus' results. The results shown above only reflect the 'Base' data.

Source: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

ND(L) volumes calculations and explanations

KPMG non domestic legal flows Hungary^(a)

COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 ⁽¹⁾ (bn sticks)	2013 ND(L) (bn sticks)	% of ND
Austria	0.02	0.02	100%
Slovakia	0.01	0.01	100%
Germany	0.01	0.01	100%

- Consumer research formed the basis of the calculation for the legal component of most of the inflows. In the case of the three inflows however shown above, all non-domestic flows are assumed to be legal as they are all higher or comparably priced markets



Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

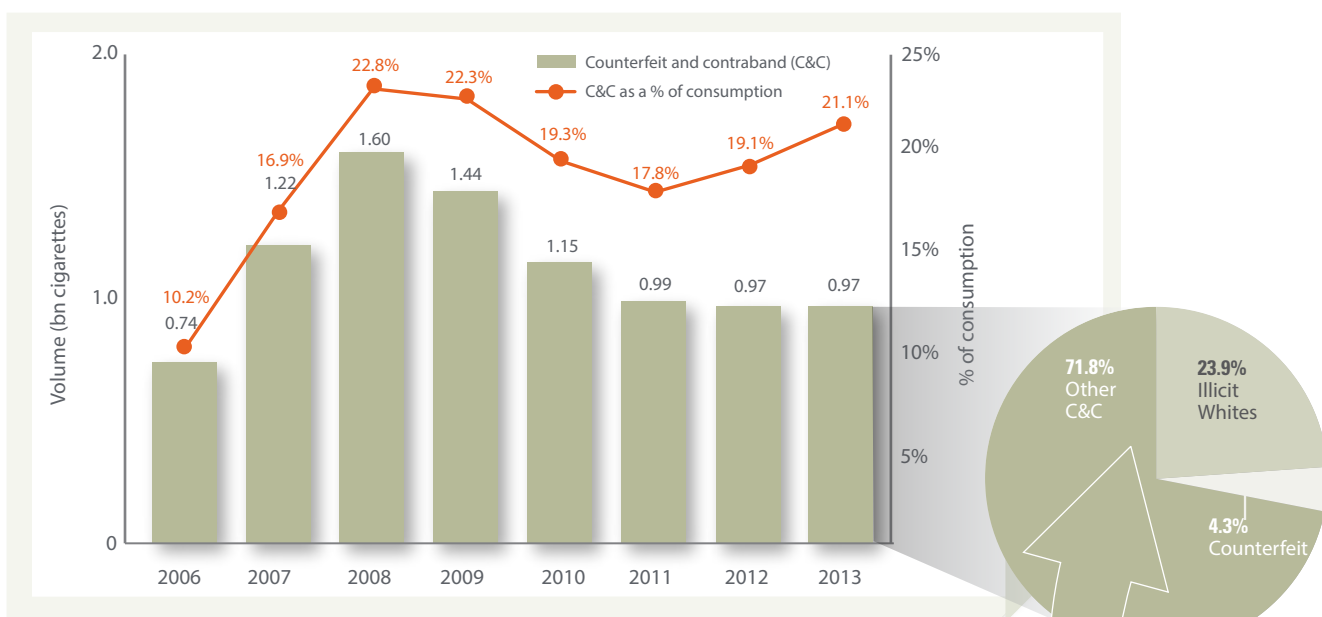
Source: (1) KPMG EU Flows Model.

IRELAND

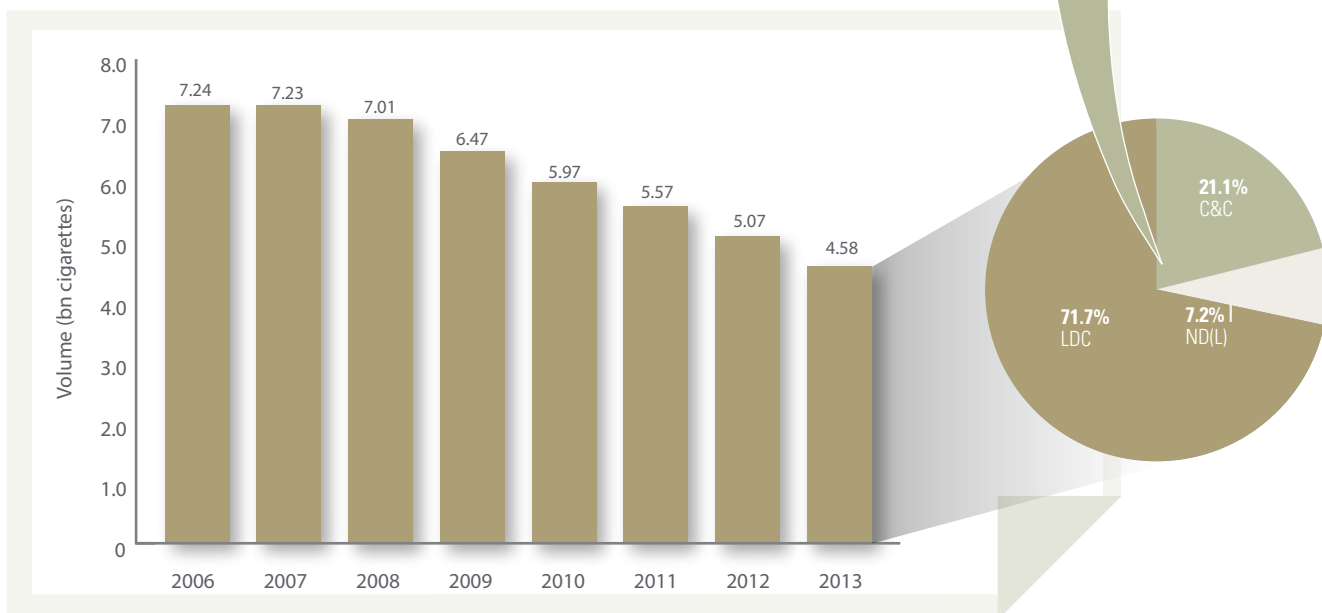


Counterfeit & Contraband volumes remained stable, while increasing as share of consumption

Manufactured cigarette C&C volumes and share of overall consumption 2006-13



Manufactured cigarette consumption 2006-13

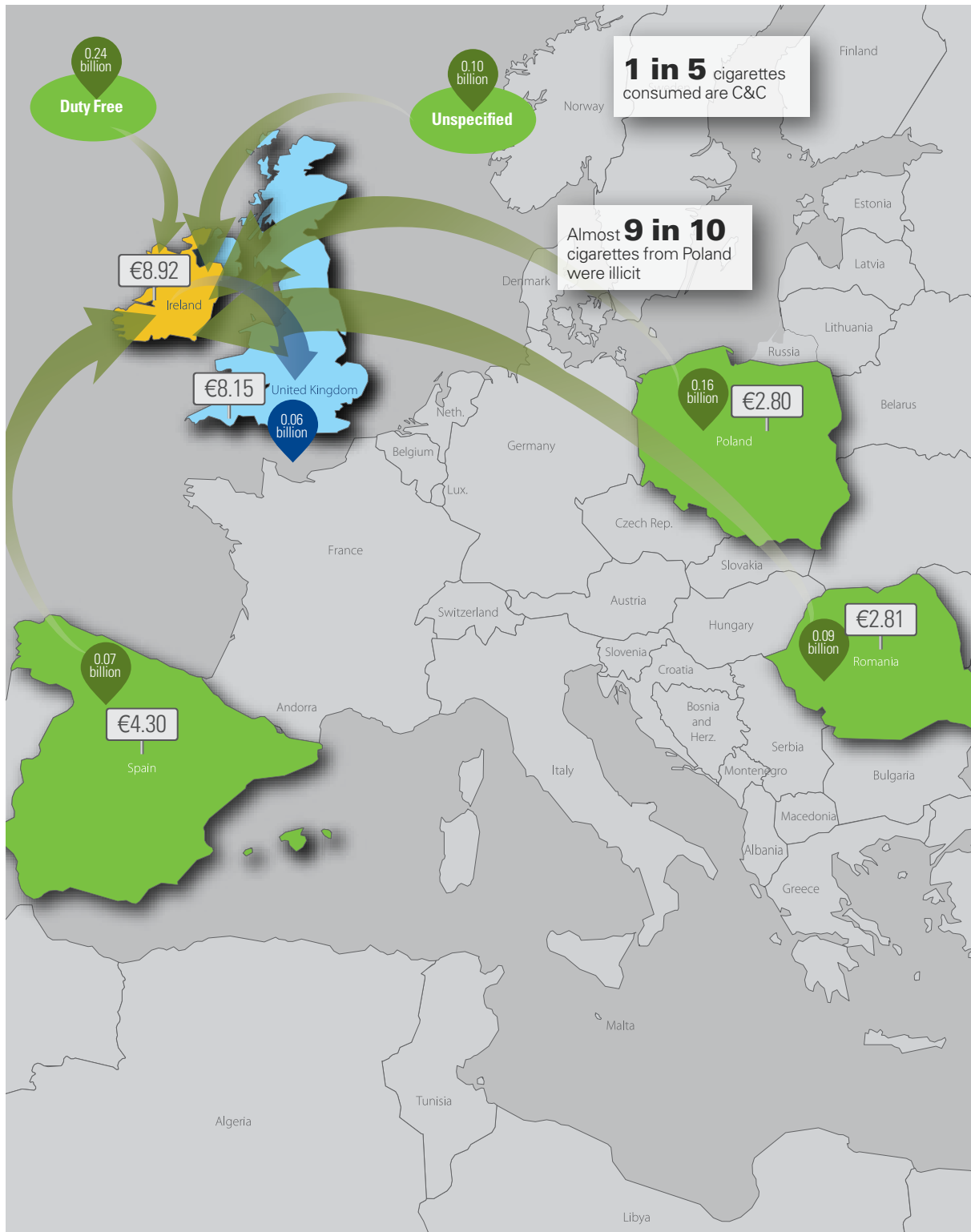


IRELAND



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KEY INFLOWS AND OUTFLOWS



IRELAND
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█ Main outflow
█ Main inflow

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

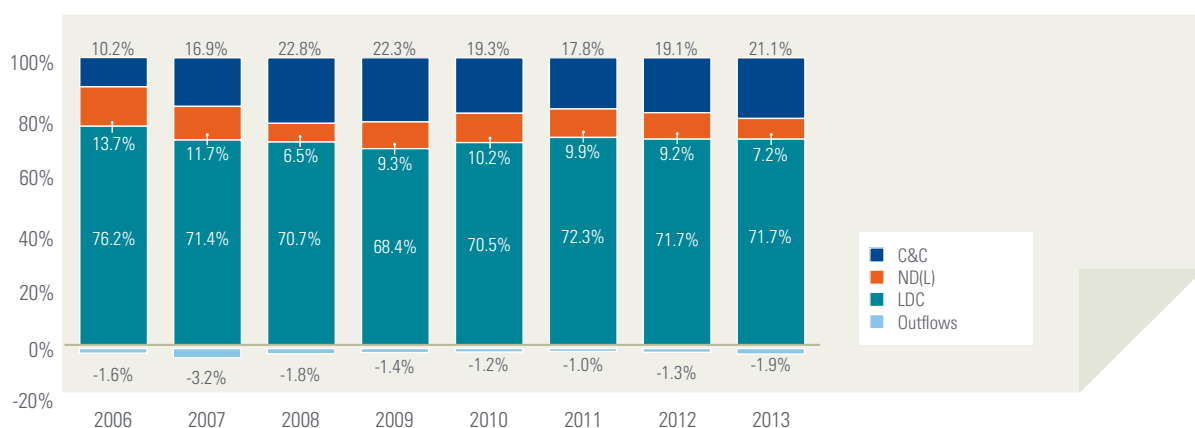
Source: (1) KPMG EU Flows Model.

Consumption of both domestic and non-domestic products declined in volume terms

Total manufactured cigarette consumption – Ireland^{(1)(2)(3)(a)}

TOTAL IRELAND CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	5.63	5.39	5.08	4.52	4.28	4.09	3.70	3.37	(9)%
Outflows	-0.12	-0.23	-0.13	-0.09	-0.07	-0.06	-0.07	-0.09	(31)%
Legal domestic consumption (LDC)	5.52	5.16	4.96	4.43	4.21	4.03	3.63	3.28	(10)%
Non-domestic legal (ND(L))	0.99	0.85	0.45	0.60	0.61	0.55	0.47	0.33	(29)%
Counterfeit and contraband (C&C)	0.74	1.22	1.60	1.44	1.15	0.99	0.97	0.97	0%
Total non-domestic	1.72	2.07	2.05	2.04	1.76	1.54	1.43	1.30	(10)%
Total consumption	7.24	7.23	7.01	6.47	5.97	5.57	5.07	4.58	(10)%

Share of Ireland cigarette consumption by type 2006-2013⁽¹⁾⁽²⁾⁽³⁾



Total manufactured cigarette consumption in Ireland fell by 10% in 2013, with a similar level of decline in both legal domestic sales (LDS) and non-domestic consumption

- Economic conditions in Ireland were mixed in 2013 as unemployment fell from 14.7% to 13.1%, but average PDI declined by 0.3%⁽⁴⁾⁽⁵⁾
- LDS volumes are likely to have been impacted by a 5.3% WAP rise in 2013⁽⁶⁾
- Consumer research suggests that smoking prevalence of manufactured cigarettes has continued its long term decline and has fallen from 28.1% in December 2006 to 21.5% in December 2013⁽⁷⁾

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Source: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Independent agency Empty Pack Surveys, 2006 – 2013. (4) Euromonitor Passport. (5) The Economist Intelligence Unit. (6) EU Commission WAP tables (7) Ipsos MRBI, Cigarette Smoking Prevalence in Ireland, April 2014.

Intra-EU inflows declined, partially offset by significant increases in Duty Free and unspecified products

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWS TO IRELAND									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	0.06	0.03	0.08	0.11	0.11	0.16	0.19	0.24	27%
Poland	0.33	0.37	0.18	0.14	0.22	0.19	0.19	0.16	(13)%
Unspecified	0.00	0.00	0.00	0.12	0.05	0.08	0.06	0.10	54%
Romania	0.05	0.12	0.10	0.08	0.05	0.06	0.10	0.09	(8)%
Spain	0.51	0.49	0.50	0.37	0.25	0.15	0.14	0.07	(48)%
Counterfeit								0.04	n/a
Other	0.77	1.06	1.20	1.21	1.08	0.89	0.76	0.60	(22)%
Total inflows	1.72	2.07	2.05	2.04	1.76	1.54	1.43	1.30	(10)%

Total non-domestic inflows to Ireland reduced by 10% in 2013. Falling inflows from traditional markets such as Spain and Poland were partially offset by increases in Duty Free and unspecified variants

- As the highest priced country in the EU, price differentials to nearby countries are high, which continues to act as an incentive to transport non-domestic cigarettes to Ireland
- 29% of inflows marked as Duty Free were Illicit Whites brands

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM IRELAND									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
UK	0.08	0.14	0.09	0.05	0.02	0.03	0.05	0.06	14%
Netherlands	0.03	0.03	0.00	0.02	0.02	0.01	0.00	0.02	>100%
Italy	0.00	0.00	0.00	0.01	0.00	0.00	0.00	0.00	n/a
Other	0.01	0.07	0.03	0.01	0.03	0.01	0.01	0.00	(44)%
Total outflows	0.12	0.23	0.13	0.09	0.07	0.06	0.07	0.09	31%

Outflows from Ireland continue to be low

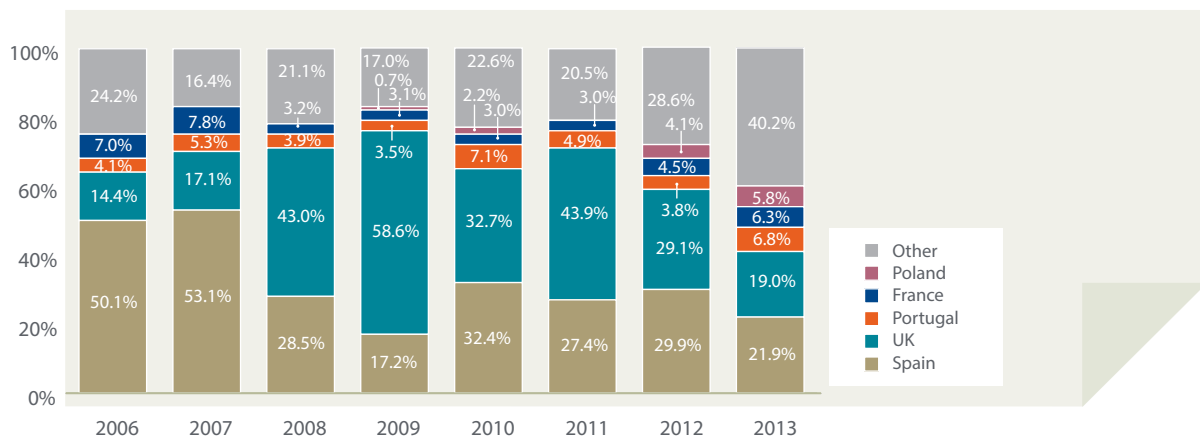
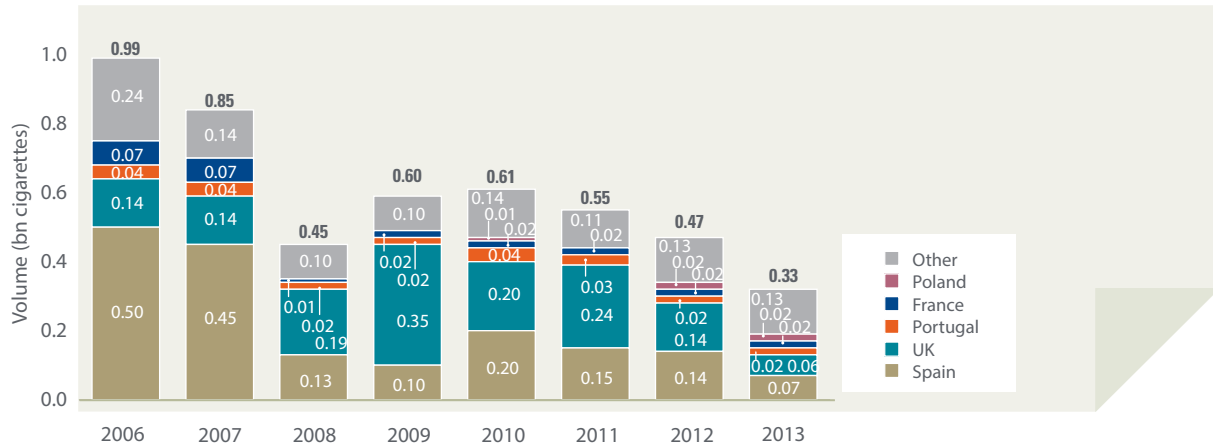
- Outflows in aggregate increased by 32%, however this is from a low base, with the largest outflow being 0.06 billion cigarettes to the UK
- The price gap between the UK and Ireland fell in 2013, decreasing the WAP difference from €0.95 to €0.77. However, with WAP now almost €9.00 per pack in Ireland this may still be driving the incentive to make cross-border purchases, especially for those near the border with the UK⁽²⁾

Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Source: (1) KPMG EU Flows Model. (2) EU Commission WAP tables.

Legal volumes represented one quarter of non-domestic inflows

ND(L) by origin - 2006-2013^{(1)(2)(3)(a)(b)}



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ND(L) inflows have fallen by 29% as a result of reduced incidence of UK and Spanish cigarettes in the EPS, which are assumed to be entirely legal flows

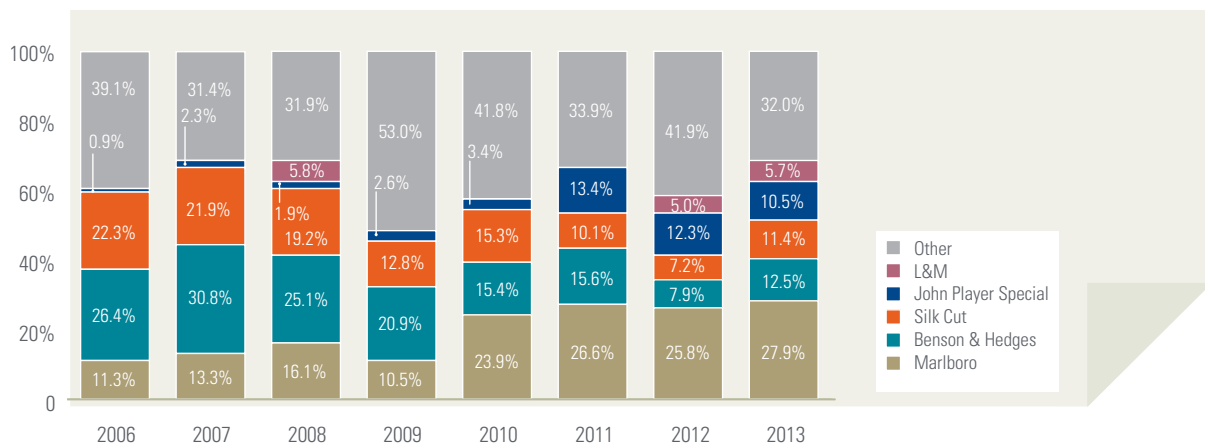
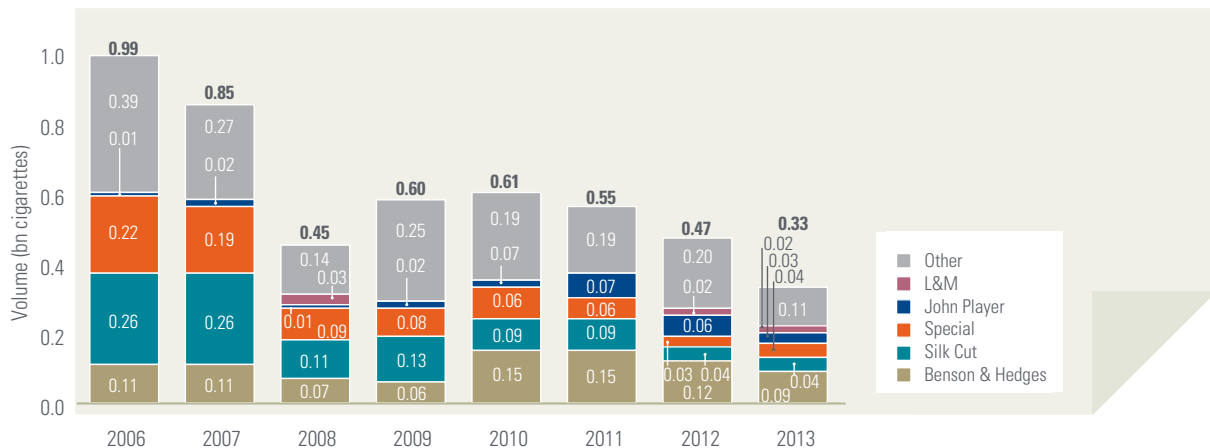
- Spain is the largest source of ND(L) cigarettes in Ireland. It is a popular holiday destination and all flows from Spain are assumed to be legal in 2013
- Cross border shopping and travel to the UK is common, and as a result all inflows from the UK are assumed to be legal
 - This falling ND(L) trend is echoed by Irish Tax and Customs, who state legal non-Irish duty paid as 7% of the total market in 2012, down from 8% in 2011, and 9% in 2010⁽⁴⁾

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Source: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers. (4) Irish Revenue Commissioners, Cigarette Consumption Survey, 2013.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

Total ND(L) by brand - 2006-2013^{(1)(2)(a)}



Marlboro is the most popular ND(L) brand in Ireland

- Most Marlboro originates in Spain and the UK, accounting for over half the legal inflow

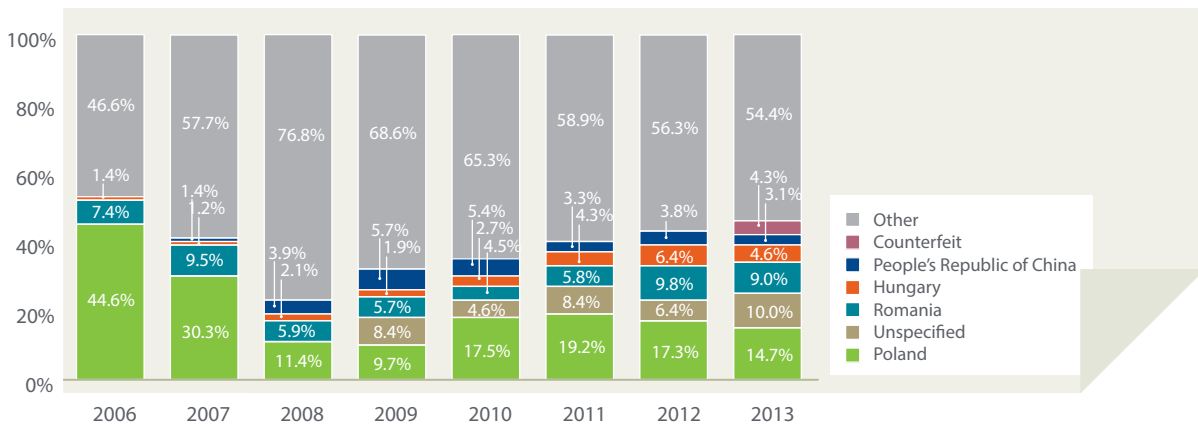
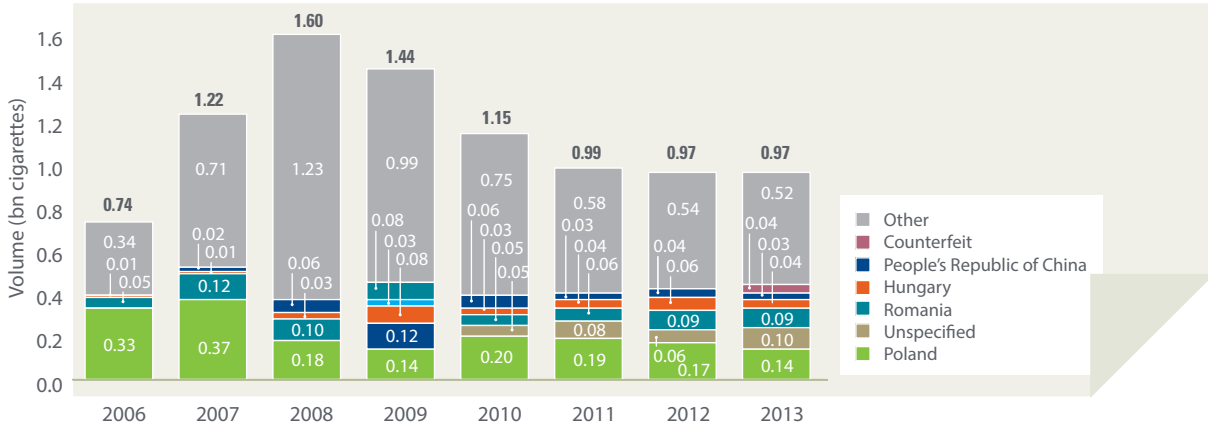
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



C&C was stable with a decrease in Poland inflows offset by a higher volume of Unspecified

Total C&C by origin 2006-2013^{(1)(2)(3)(a)}



IRELAND



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Total C&C in Ireland has remained flat between 2012 and 2013. A decrease from major source countries such as Poland and Romania has been offset by a rise in C&C with unspecified market variant.

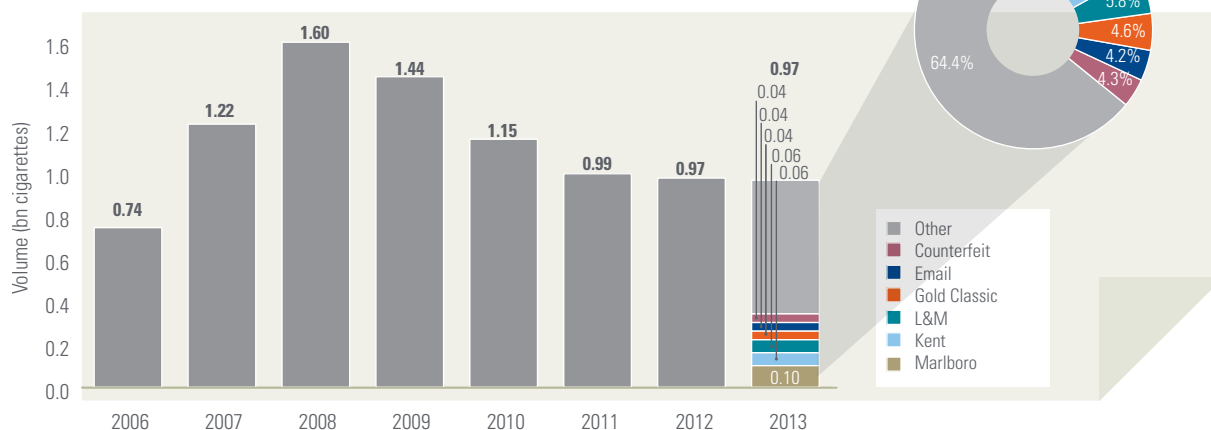
- Poland has traditionally been, and continues to be, the main source of C&C into Ireland, with the most popular brands being Marlboro and L&M
- If the 0.97bn C&C cigarettes in 2013 had been legally purchased in Ireland the tax revenue gained would have been approximately €348m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

C&C INFLOWS BY BRAND

Total C&C by brand 2006-2013^{(1)(2)(3)(a)}



Marlboro, Kent and L&M are the largest C&C brands in Ireland, but the prevalence of Illicit Whites is increasing

- Illicit Whites brands accounted for 24% of total C&C volumes in 2013, up from 15% in 2012
- Irish Revenue Commissioners also made significant seizures of Illicit Whites brands in 2013. The top two brands seized were Gold Classic and Modeng, totalling over 20 million cigarettes in volume⁽³⁾

29% of inflows marked as Duty Free were Illicit Whites brands

Composition of Illicit Whites inflows - 2007-2013^{(1)(3)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO IRELAND								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.03	0.02	0.04	0.10	0.07	0.07	0.07	3%
Duty Free	0.00	0.01	0.00	0.00	0.01	0.03	0.07	>100%
Unspecified	0.00	0.00	0.06	0.02	0.08	0.05	0.09	91%
Total Illicit Whites	0.03	0.04	0.09	0.13	0.16	0.15	0.23	57%

Several Illicit Whites brands have a strong presence in Ireland, mainly with unspecified market variant

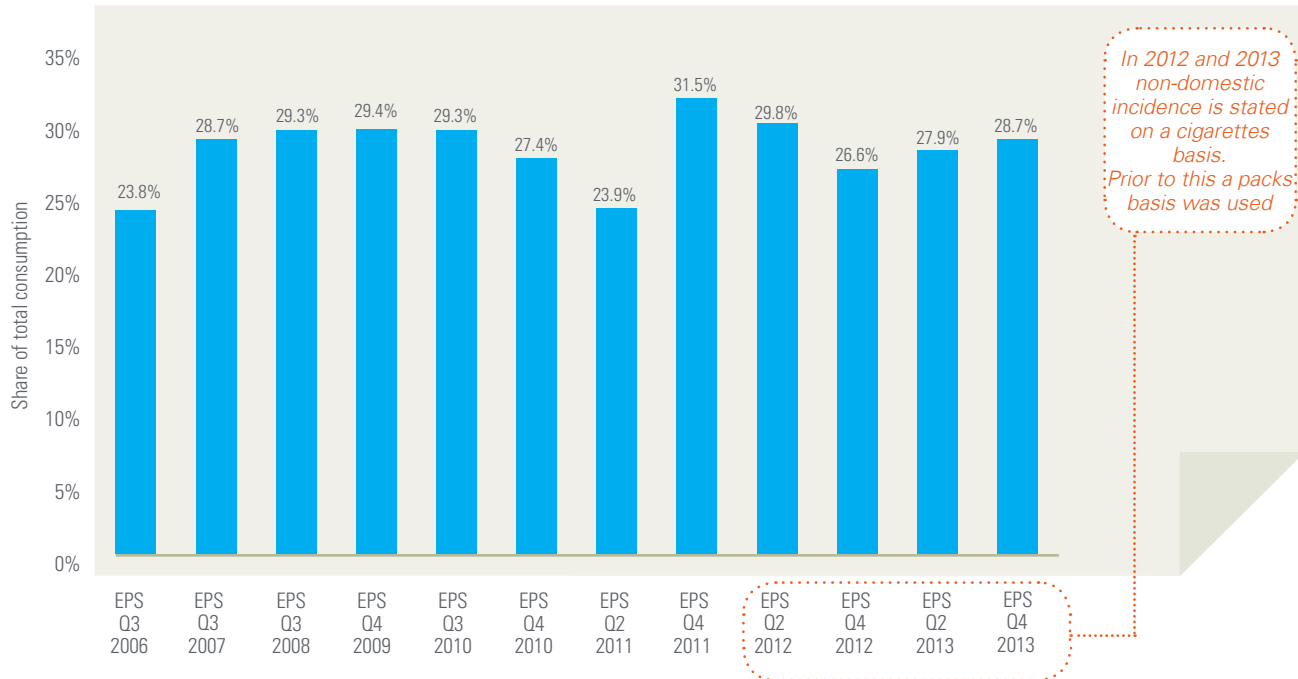
- Gold Classic and Golden Seagies are the main Illicit Whites marked as unspecified, accounting for over 70% the unspecified Illicit Whites balance
- Email, 821 and Toro are the main Illicit Whites marked as Duty Free, accounting for 82% of the Duty Free Illicit Whites balance
- CK and MG from the Canary Islands contribute 48% of the country specific Illicit Whites

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

EPS results & EU flows model

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



IRELAND



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- Irish non-domestic incidence has been consistently high, but has fallen back from a peak in Q4 2011 and Q2 2012
- The empty pack survey in Ireland collected 10,000 packs during the second and fourth quarters of the year. It collects these packs across 22 towns and cities. The number of packs collected in the town or city is weighted by its population

Source: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

ND(L) volumes calculations and explanations

KPMG non domestic legal flows Ireland

COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 ⁽¹⁾ (bn sticks)	2013 ND(L) (bn sticks)	% of ND
Spain	0.07	0.07	100%
UK	0.06	0.06	100%

Consumer research is used to calculate the ND(L) inflow volume to Ireland.

There were 0.34 million trips to Spain in 2013 where cigarettes were purchased. On average 31 packs were purchased per trip, giving a total legal volume of 0.21bn cigarettes. The total amount of non-domestic cigarettes from Bulgaria in the EPS study was 0.07bn, and so it is assumed the flow from Spain is 100% legal.

There are frequent border crossings to the UK from Ireland, both for business purposes and for cross border shopping and tourism. The WAP difference is also low at €0.77, as the UK is also a high priced country. Therefore, such inflows from the UK are assumed to be legal.

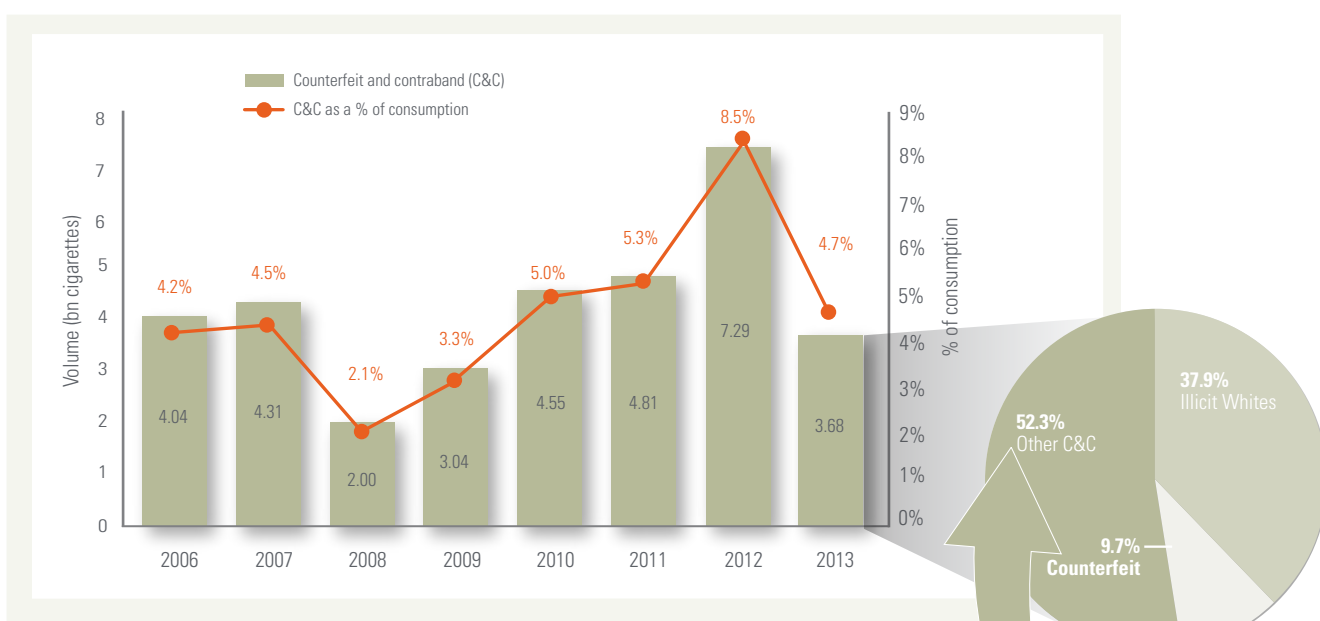


Source: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.

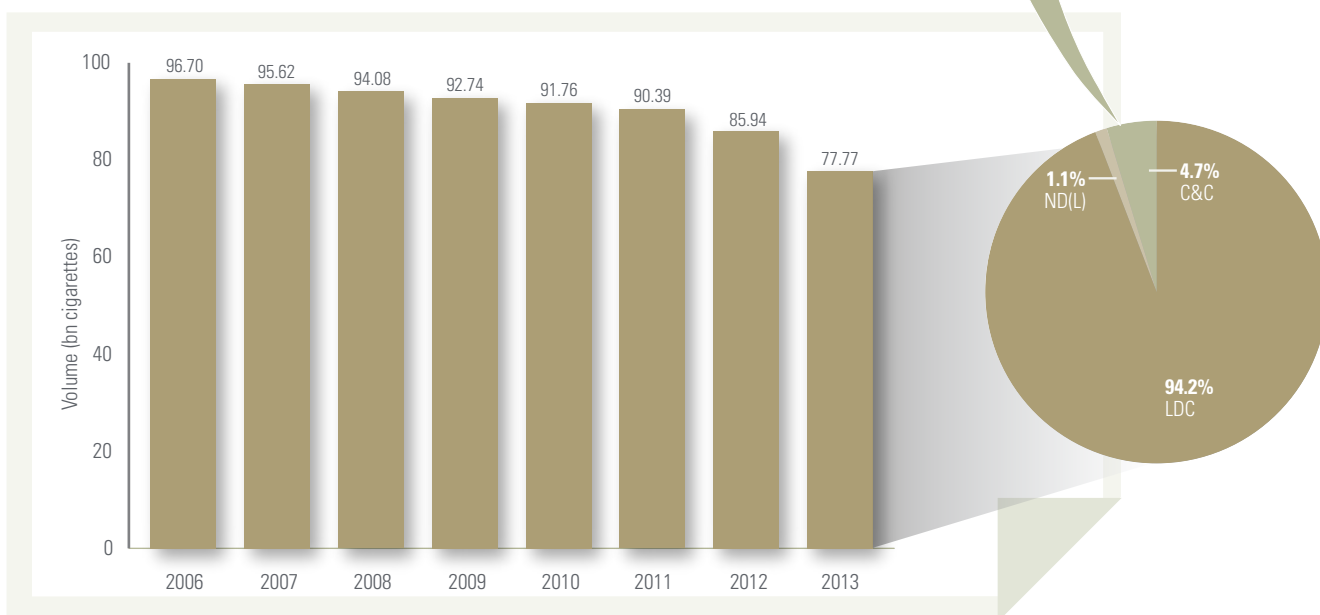


Counterfeit & Contraband fell by 50%, along with total consumption decline

Manufactured cigarette C&C volumes and share of overall consumption 2006-13



Manufactured cigarette consumption 2006-13

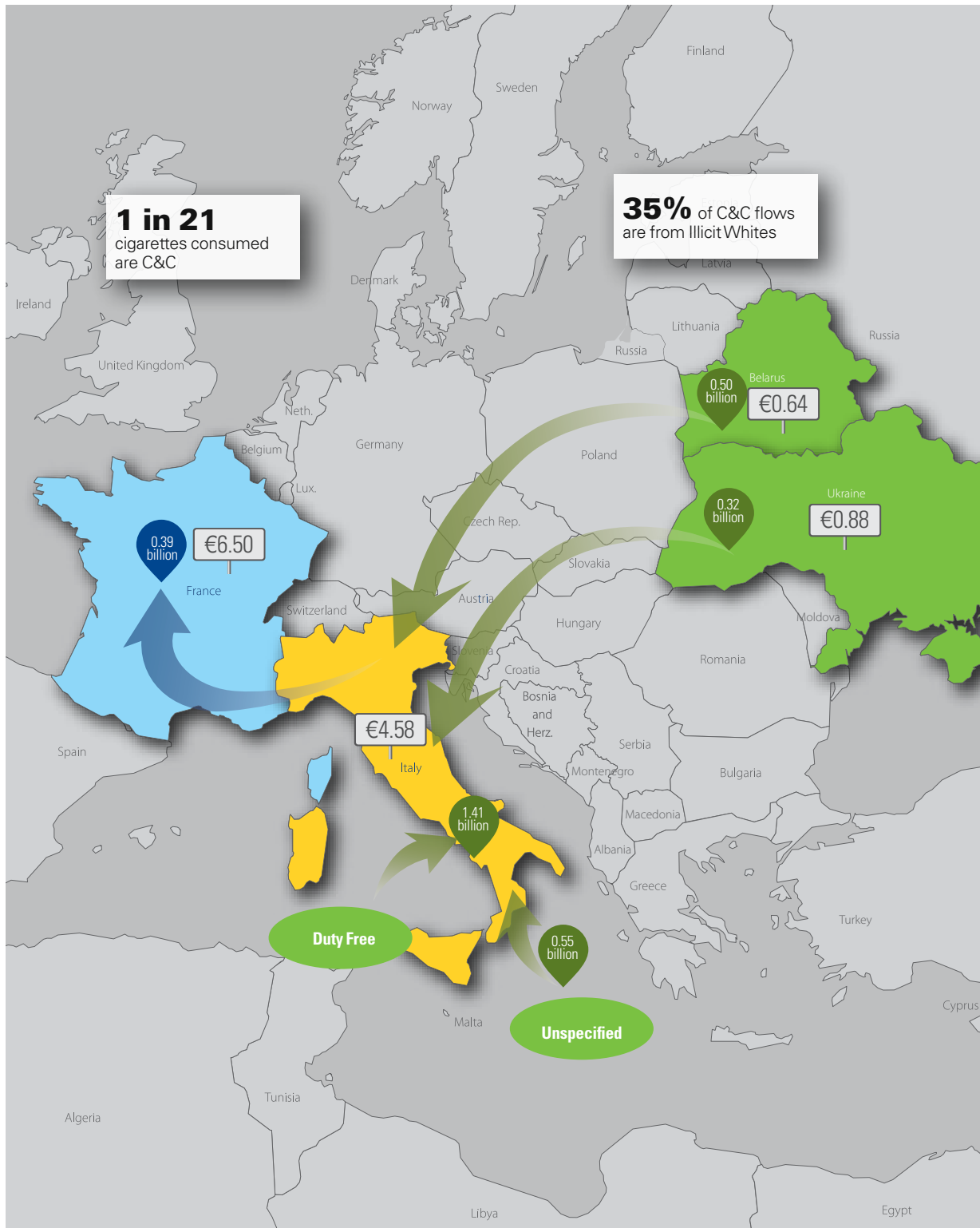


ITALY



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KEY INFLOWS AND OUTFLOWS



ITALY
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Main outflow - █
Main inflow - █

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

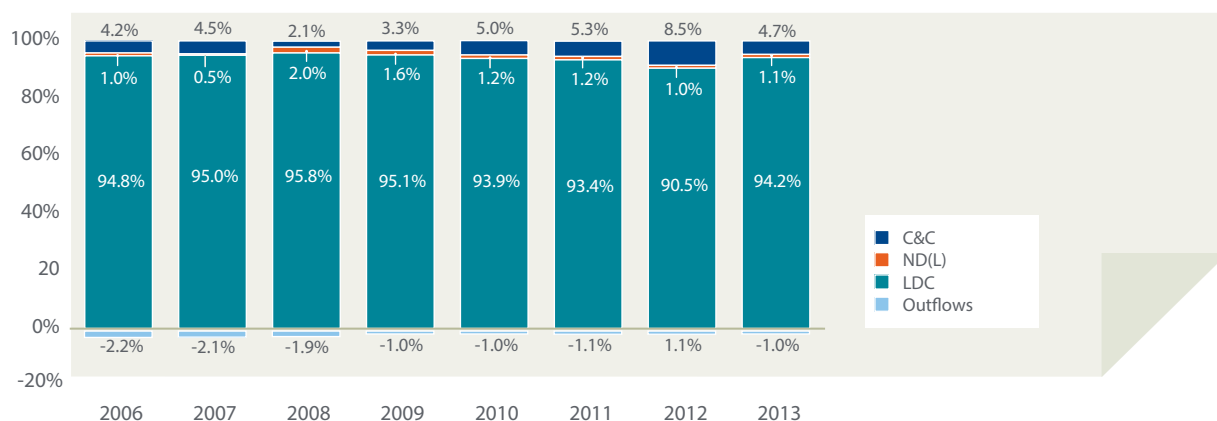
Whilst overall consumption declined by 10%, counterfeit and contraband consumption dropped by 50%

Major decline in consumption reflects both a decline in legal domestic sales and non-domestic incidence

Total manufactured cigarette consumption – Italy⁽¹⁾⁽²⁾⁽³⁾

TOTAL ITALY CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	93.81	92.81	92.00	89.16	87.05	85.47	78.74	74.04	(6)%
Outflows	-2.13	-2.01	-1.83	-0.92	-0.93	-1.01	-0.93	-0.78	(16)%
Legal domestic consumption (LDC)	91.68	90.80	90.17	88.24	86.12	84.46	77.81	73.25	(6)%
Non-domestic legal (ND(L))	0.98	0.51	1.91	1.46	1.09	1.12	0.84	0.84	1%
Counterfeit and contraband (C&C)	4.04	4.31	2.00	3.04	4.55	4.81	7.29	3.68	(50)%
Total non-domestic	5.02	4.82	3.90	4.50	5.64	5.93	8.13	4.52	(44)%
Total consumption	96.70	95.62	94.08	92.74	91.76	90.39	85.94	77.77	(10)%

Share of Italy manufactured cigarette consumption by type⁽¹⁾⁽²⁾ - 2006-2013



Whilst legal domestic sales (LDS) declined by 6% from 2012, it increased to over 94% of overall consumption in Italy as counterfeit and contraband (C&C) declined more significantly

- Consumption of C&C products halved from 2012 levels which may be due to some of the following factors:
 - Additional law enforcement activities and initiatives such as operation “wrong smoke” from the Guardia di Finanza, especially in Naples⁽⁴⁾
 - The withdrawal of Classic which was being heavily counterfeited in Ukraine and had become an increasingly recognised illicit brand
 - The impact of the “super-low” segment which led to a smaller decline in legal domestic sales in the later part of the year
- Overall consumption may have been impacted by the economic situation in Italy, where unemployment grew from 10.7% to 12.2% whilst PDI fell by 2.3%⁽⁵⁾

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Independent agency Empty Pack Surveys, 2006-2013. (4) Guardia di Finanza, “Operazione Wrong smoke - Sequestrati tre quintali di Tabacchi Lavorati Esteri,” October 2013. (5) Eurostat, 2013 data.

InfloWS from Ukraine and Belarus decreased significantly

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWS TO ITALY									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	1.49	1.40	0.92	0.95	1.07	1.14	2.15	1.41	(35)%
Unspecified	0.00	0.00	0.06	0.02	0.14	0.68	0.89	0.55	(38)%
Belarus	0.00	0.00	0.00	0.01	0.01	0.04	0.76	0.50	(35)%
Ukraine	0.89	1.00	0.67	0.92	1.61	1.52	1.83	0.32	(83)%
Other	2.64	2.42	2.26	2.61	2.81	2.56	2.49	1.74	(30)%
Total inflows	5.02	4.82	3.90	4.50	5.64	5.93	8.13	4.52	(44)%

35% of Duty Free labelled products were Illicit Whites

Major declines in large inflows of Illicit Whites and other contraband product.

Italy is mainly bordered by similar or higher priced countries and therefore the majority of flows of cheaper products which enter Italy come from countries which are further away

- Given the low level of travel between Italy and Ukraine and Belarus, a large proportion of these flows are expected to be C&C
- 35% of the brands with Duty Free labelling were Illicit Whites, with large volumes also coming from unspecified and Belarus flows⁽²⁾

Total outflows by destination country – 2006-2013⁽¹⁾

OUTFLOWS FROM ITALY									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
France	0.71	0.50	0.62	0.32	0.38	0.51	0.31	0.39	26%
Netherlands	0.65	0.45	0.25	0.06	0.21	0.18	0.17	0.13	(24)%
Germany	0.16	0.13	0.09	0.08	0.11	0.10	0.10	0.10	(8)%
Other	0.62	0.93	0.87	0.46	0.23	0.23	0.34	0.17	(51)%
Total outflows	2.13	2.01	1.83	0.92	0.93	1.01	0.93	0.78	(16)%

Italy continues to be a low outflow market; outflows from Italy have historically been those purchased by tourists from more expensive markets

- Half of the outflows from Italy went to France in 2013

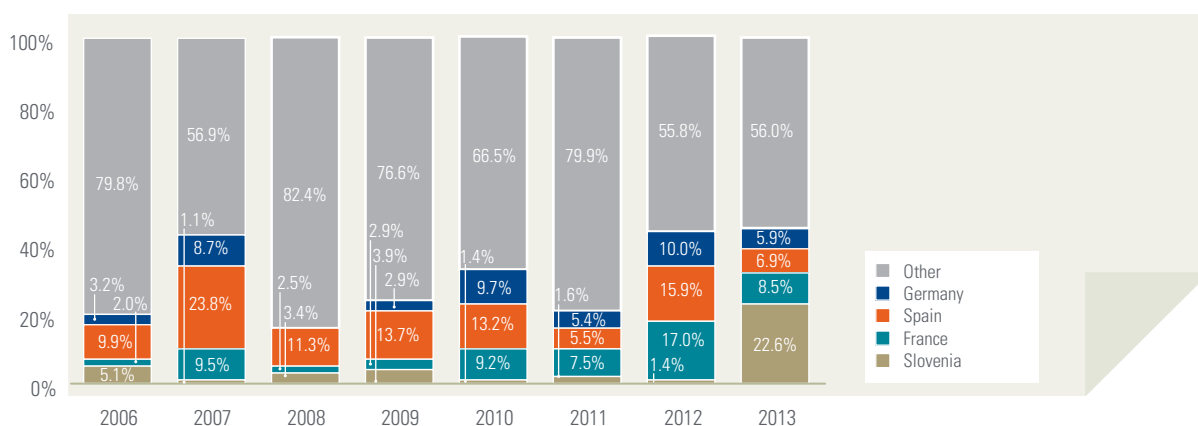
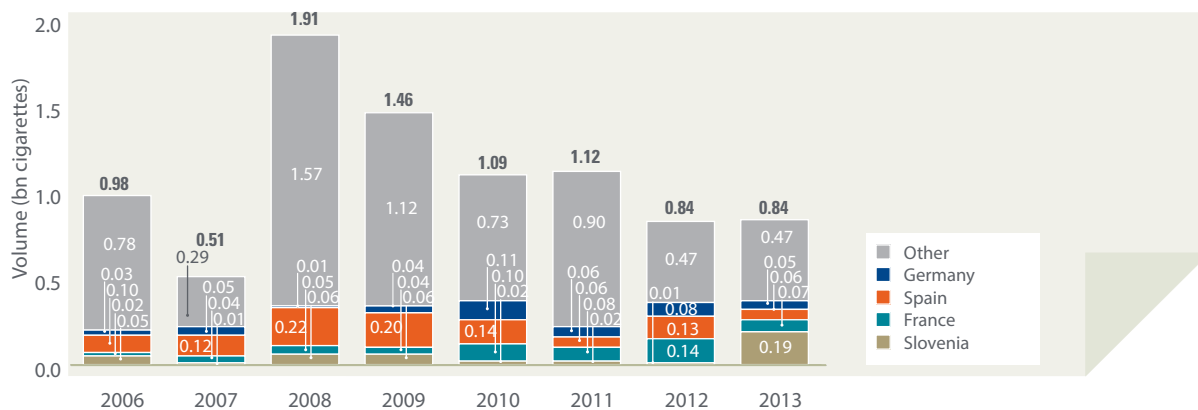
Note: a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of the Italy Empty Pack Survey results.



ND(L) remained stable, accounting for less than one fifth of overall non-domestic consumption

ND(L) by origin 2006 - 2013^{(1)(2)(a)}



ITALY



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The only major ND(L) flow came from Slovenia, a lower-priced bordering market

- Cross-border purchases are only likely in Slovenia, but despite the presence of border shops between Italy and Slovenia, very few Slovenian packs are found in Italy⁽³⁾
- In 2013 cross-border sales data was used to measure flows from Slovenia. Given the low size of this flow, it is assumed that all of it is legal, but that consumption of Slovenian packs is highly concentrated around the border area

Other ND(L) flows came from countries which are either higher priced, or where the number of visits vastly exceeded the size of the overall flow

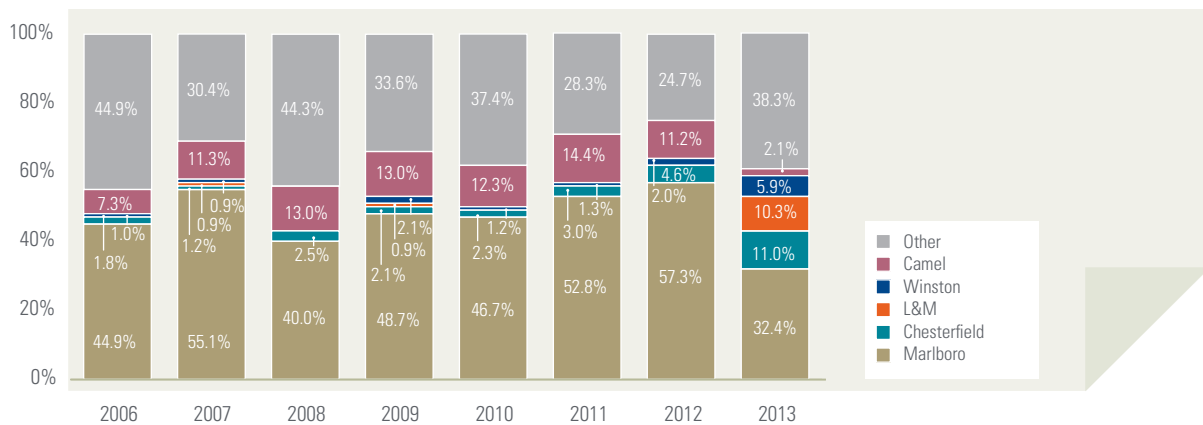
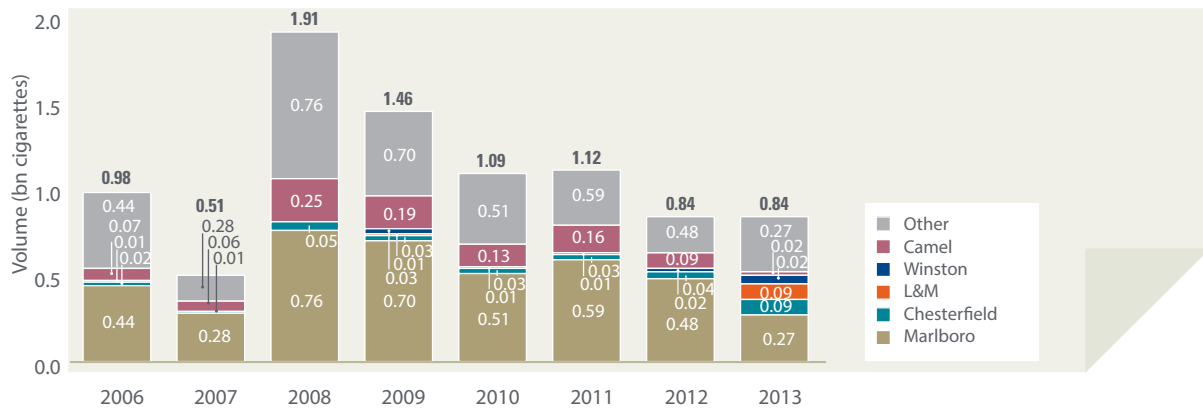
- France and Germany are higher priced markets, and the price in Spain is only €0.22 less than Italy, therefore all of these flows are assumed to be legal
- Historic consumer research has also consistently over-reported purchases from Germany, France and Spain, compared with the number of packs collected. This results in the total number of cigarettes from these countries being capped at 100%

Notes: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

Total ND(L) by brand - 2006-2013^{(1)(2)(a)}



ND(L) sales of Marlboro are replicated by the high market share that it has in Italy

- Marlboro may be over-represented as the next most popular brands in Italy (Diana and MS) do not have significant sales in other countries

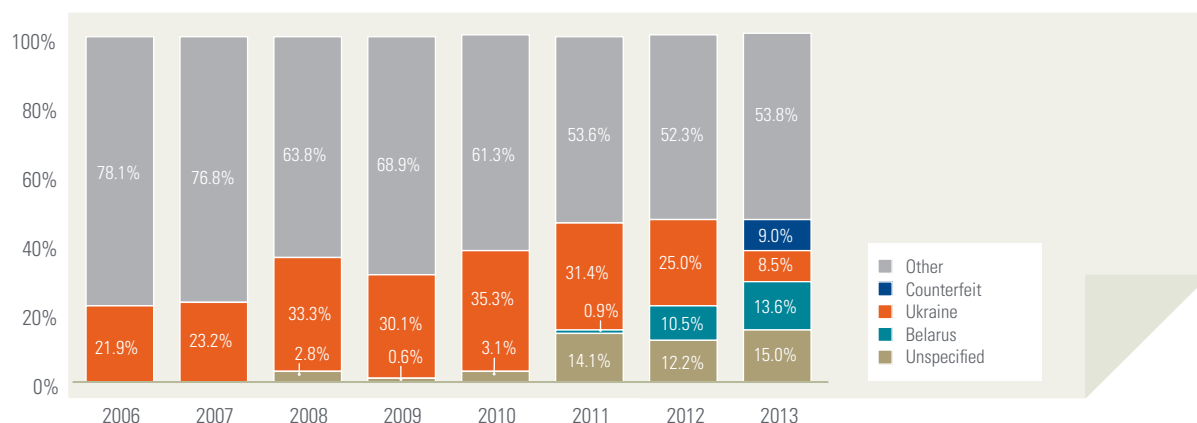
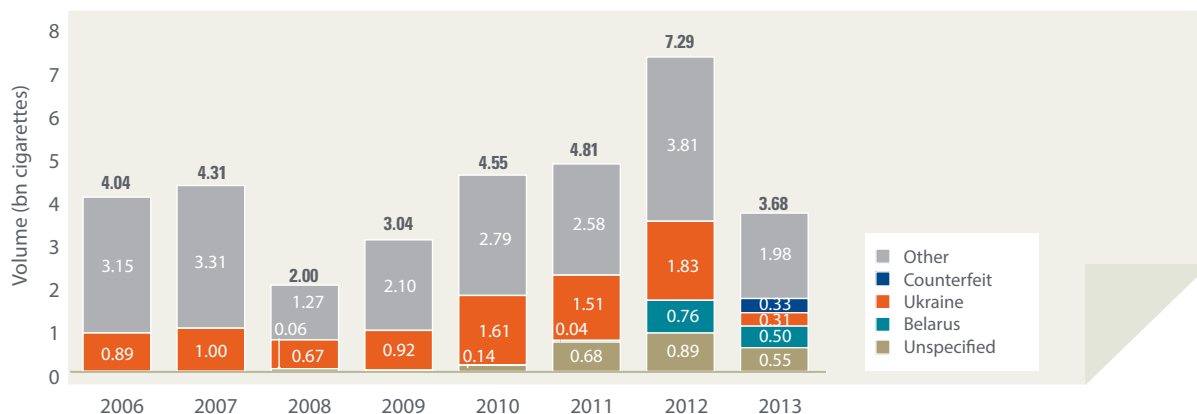
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.



C&C volumes halved in 2013, driven by a decline in major flows, especially Ukraine

Total C&C by origin - 2006 - 2013^{(1)(2)(a)}



ITALY



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Whilst there was a significant decline in the level of C&C from major sources, the largest decline came from Ukraine

- The significant decline in flows from Ukraine can be partially attributed to the withdrawal of Classic, a large proportion of which was counterfeit. This withdrawal is likely to have had a significant impact on the illicit supply chain which was in the main going to Naples⁽³⁾
 - In the Q4 Empty Pack Survey, Classic appeared to have almost disappeared with only 5 out of the 10,000 packs identified following the decision of ITL to stop production
- The development of new illicit supply chains appears to have been hampered by additional law enforcement activities both on the streets and at ports in areas known to have higher levels of illicit trade (see section on Naples)
 - Significant law enforcement initiatives such as Operation “Wrong Smoke,” which resulted in the identification of 157 illicit traders in Naples and uncovered 3 tonnes of illicit cigarettes will have reduced illicit trade in areas known to have significant illicit trade⁽⁴⁾
 - Whilst in 2012 seizures at Ancona (the largest seizures location) declined, it appears that less activity during the economic downturn may have contributed to higher seizures or increased deterrents to smuggling⁽⁵⁾

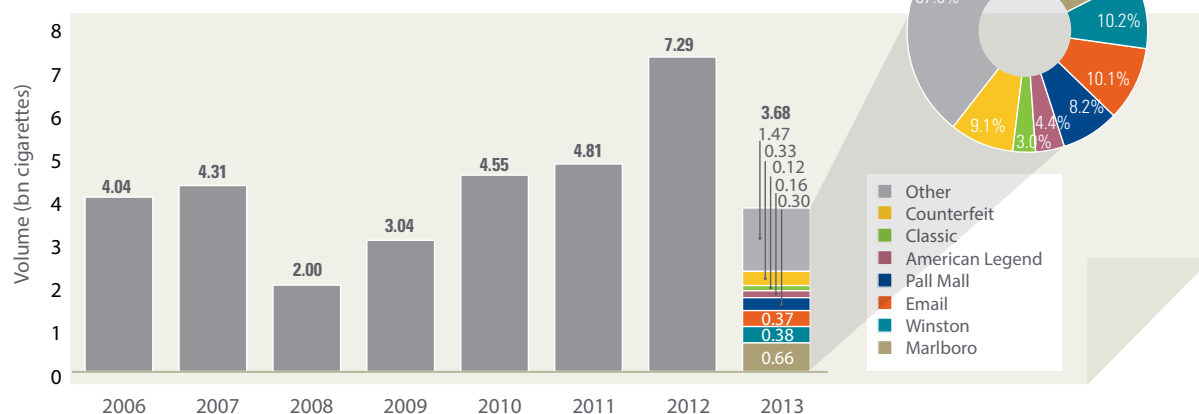
The overall reduction of C&C can be partially attributed to the growth of the super-low segment in Italy

- The super-low segment grew to 4% of overall market share at the end of 2013⁽⁶⁾
- If the total volume of C&C had been consumed legally within the Italian market, an additional tax revenue of approximately €634 million would have been raised by the Italian Treasury
- This volume is calculated using the weighted average price from July 2013 and overall volume of C&C and may differ when compared to other sources

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.
 Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of the Empty Pack Survey results. (4) Guardia di Finanza, “Operazione Wrong smoke - Sequestrati tre quintali di Tabacchi Lavorati Esteri,” October 2013. (5) Transcrime, “Factbook on the illicit trade in tobacco products”, October 2013. (6) KPMG analysis of data sources provided by manufacturers.

C&C INFLOWS BY BRAND

Total C&C by brand - 2006-2013^{(1)(2)(a)}



Illicit Whites made up 35% of overall Duty Free flows

Composition of Illicit Whites inflows – 2007-2013^{(1)(3)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO ITALY								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country Specific	0.04	0.10	0.11	0.24	0.29	0.55	0.44	(20)%
Duty Free	0.00	0.02	0.01	0.09	0.19	0.62	0.50	(19)%
Unspecified	0.00	0.00	0.00	0.05	0.39	0.68	0.36	(47)%
Total Illicit Whites	0.04	0.12	0.12	0.39	0.87	1.84	1.30	(30)%

Whilst well recognised brands, such as Marlboro, Winston and Pall Mall were identified in high volumes, consumption of C&C products in Italy is characterised by the large variety of different brands, many of which are Illicit Whites

- Marlboro, Winston and Classic are some of the most available counterfeit brands, often sold with duty free labelling, and frequently seen in Naples
- Large quantities of “other” smaller brands were collected, including 821 and Yesmoke. These brands, along with Email are produced with Duty Free labelling, despite being manufactured in Italy

Over 50 brands thought to be Illicit Whites were identified, many of which were in small volumes

- The high number of different brands makes identifying specific supply chains more complex
- The Illicit Whites origin is evenly spread between country specific variants, such as Belarus, unspecified variant for brands such as American Legend, and Duty Free labelling, for brands like Email and Napoli
- It is thought that the origin of many of the unspecified brands is the Middle East

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

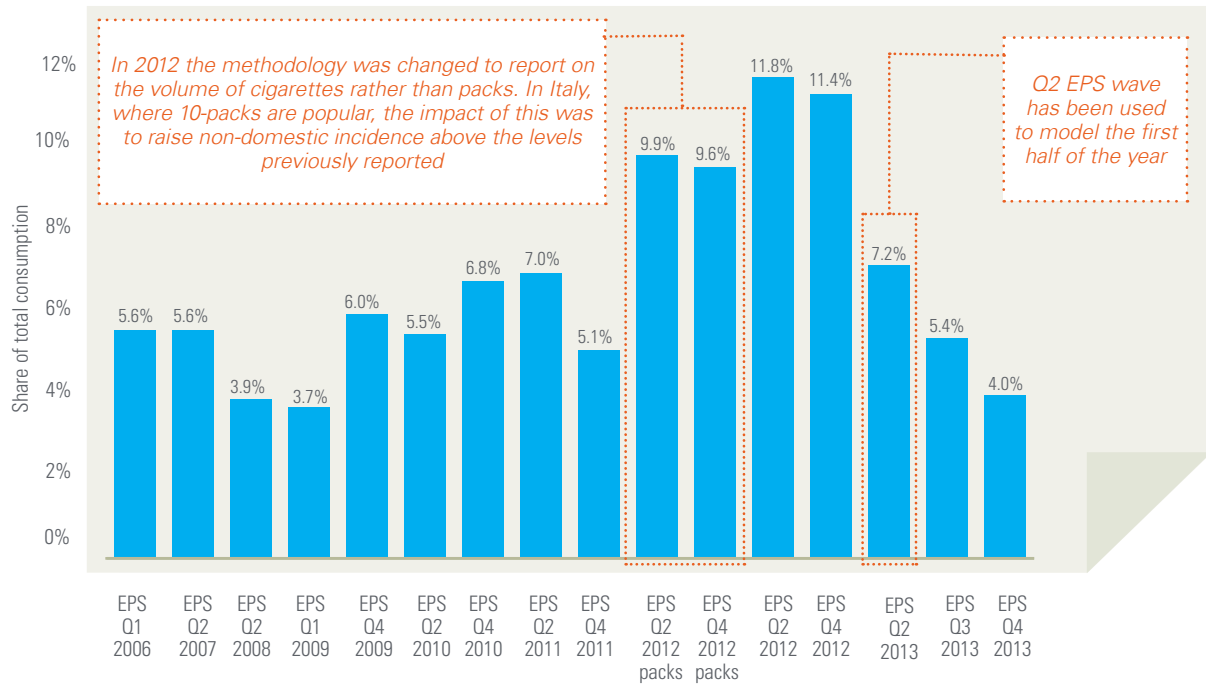
(b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.



EPS non domestic estimates

Empty Pack Survey non-domestic estimates - 2006-2013⁽¹⁾



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- The empty pack survey in Italy collected 30,000 packs during the course of the year. This was undertaken in three separate waves in Q2 (April), Q3 and Q4. The sample focused on 41 cities and the number of packs collected in each city is weighted by the city population
- The Q2 results were weighted in order to reflect the first six months of 2013, with the Q3 and Q4 results weighted equally
- In addition, an adjustment was made to account for the oversampling of 10 packs in the EPS survey
 - 10 packs made up 20% of packs sold in Italy in 2013 but represented 34% of the total sample
 - Therefore, domestic 10 packs were reweighted in line with the IMS data, with the weighting of domestic 20 packs increased proportionally
 - The impact of this adjustment has reduced the non-domestic incidence by 0.2 percentage points

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

ND(L) volume calculations and explanations

KPMG non domestic legal flows Italy

COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 ⁽¹⁾ (bn sticks)	2013 ND(L) (bn sticks)	% of ND
Slovenia	0.19	0.19	100%
France	0.08	0.07	100%
Spain	0.06	0.06	100%
Germany	0.05	0.05	100%

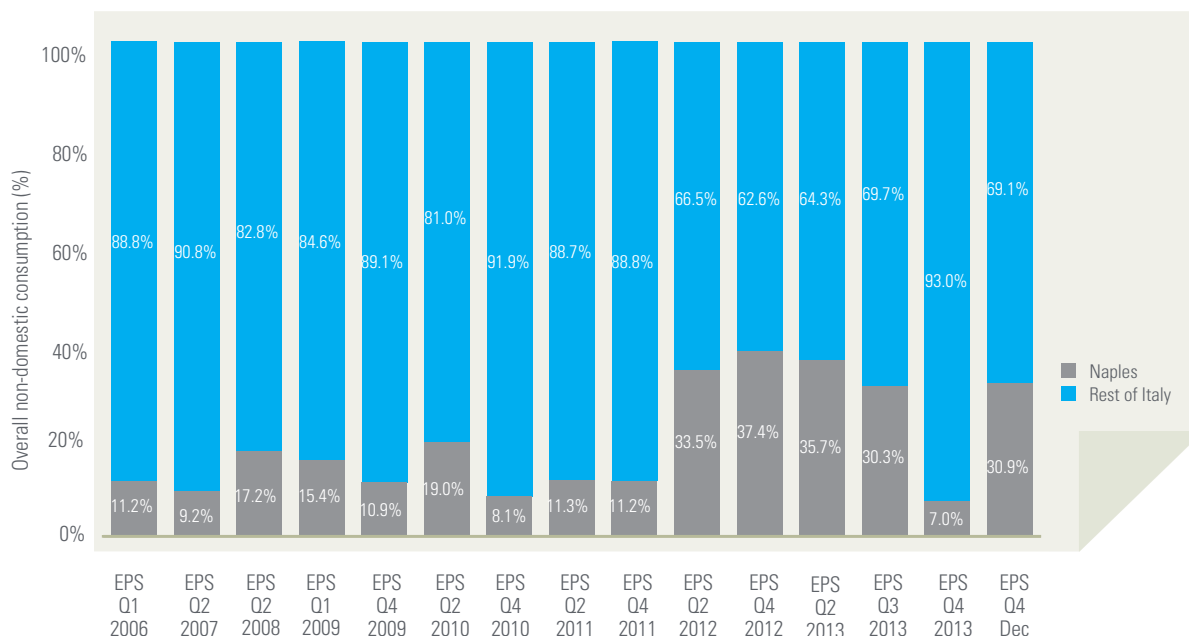
Non-domestic legal flows come from surrounding similar priced markets and countries with large tourist flows

- For Slovenia, as very few packs were identified in Italy despite a high price difference, border sales data for shops on the Italian and Slovenian border was used in order to estimate the overall flow
 - The EPS picked up very small volumes of flows from Slovenia which is adjusted in order to reflect some of the border sales data
 - These shops sold cigarettes in cartons, indicating that the majority of those purchasing cigarettes were buying in bulk
 - Given the relatively low volume of flows compared with the number of border crossings, it is assumed that all of these flows are legal sales
- France, Spain and Germany are all higher or similar priced markets. It is therefore assumed that all the flows are from tourists visiting Italy or from Italians returning from these countries



Naples has historically accounted for large proportion of C&C consumption in Italy but was highly volatile in 2013

Naples and rest of Italy share of non-domestic consumption - 2006-2013⁽¹⁾



ITALY

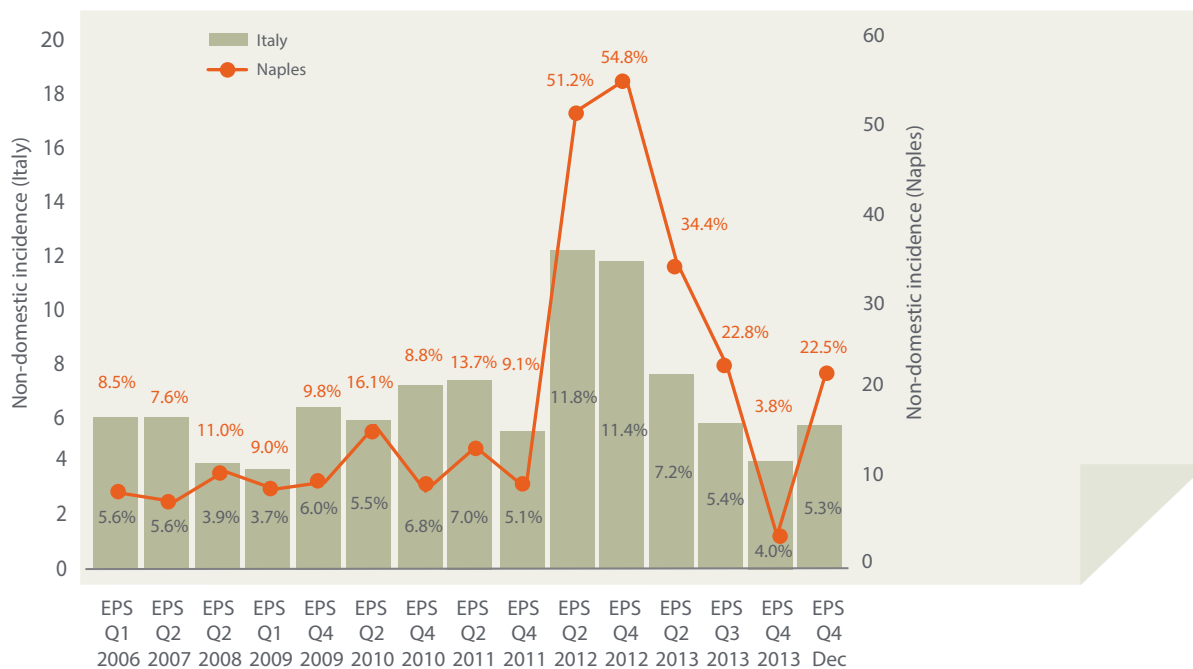


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- Naples has historically had high volumes of illicit consumption, with an average of 30% of the total non-domestic volume coming from approximately 7% of total packs collected
- An additional focus sample was undertaken in December 2013, commissioned by the manufacturers to see if the lower trend recorded in the initial sample had continued
- The December sample demonstrated the volatility in the supply of illicit products which has historically occurred in Naples
 - Within Naples, illicit product has been widely available within market-places and sold door to door
 - Illicit cigarettes are often sold at different prices, with genuine Duty Free product retailing for €3.50 compared to Illicit Whites brands sold for as little as €2⁽²⁾

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013. (2) Transcrime, "Factbook on the illicit trade in tobacco products", October 2013.

Empty pack survey non-domestic incidence - 2006-2013⁽¹⁾



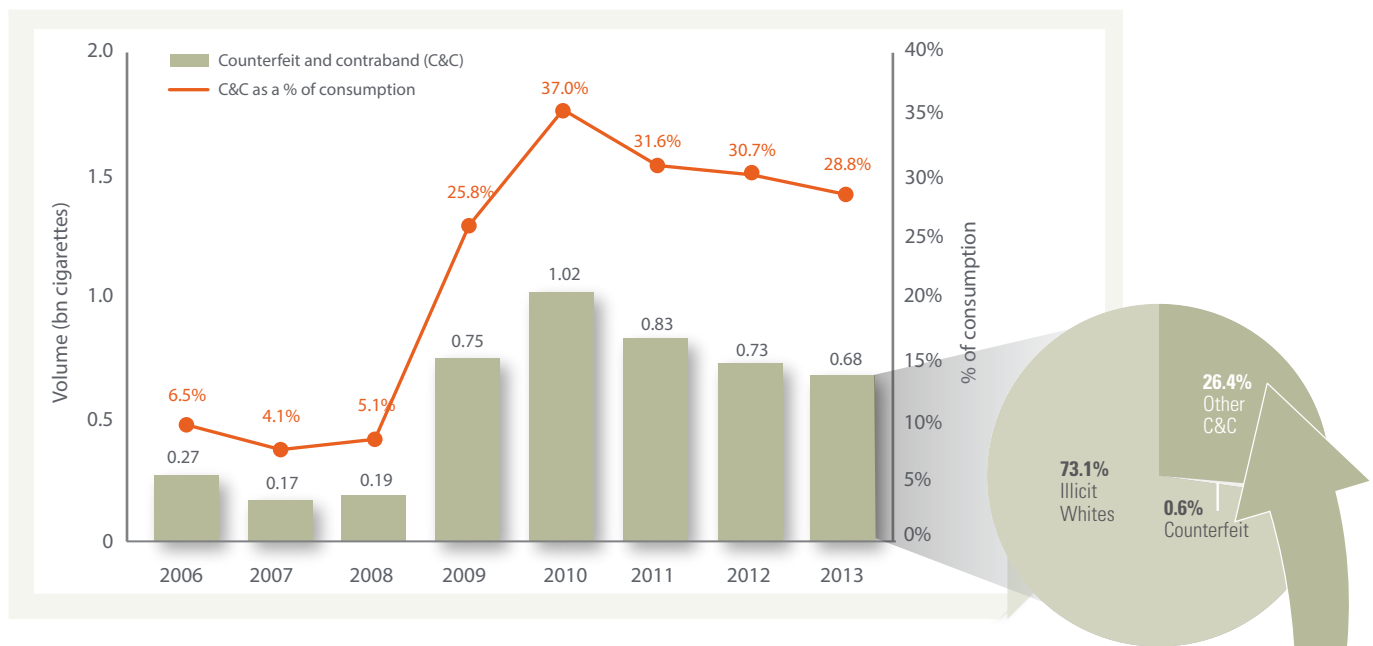
- The illicit cigarette market in Naples is highly developed but the divergent samples recorded in 2013 demonstrate that there has been some success in combating illicit trade
 - The chart above shows the Naples non-domestic incidence. For both quarters in 2012 non-domestic incidence in Naples was over 50%
 - In 2013, non-domestic incidence was far higher than the rest of Italy, with the exception of the Q4 data
- The volatility of the samples in Naples demonstrates the potential volatility in illicit trade levels, however it also shows a downward trend and lowering of overall illicit volumes compared with 2012
- During this time, whilst there were other factors which may have curbed illicit trade, such as the increased law enforcement activities such as “Operation Wrong Smoke”, the withdrawal of Classic and the growth of the super-low segment
- The combination of these factors appears to have been successful in reducing the overall consumption of illicit products in Naples during that time period, therefore considerably lowering illicit consumption in Italy in 2013

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013. (2) Transcrime, “Factbook on the illicit trade in tobacco products”, October 2013.



Counterfeit & Contraband declined as a share of consumption, but remained high relative to other EU countries

Manufactured cigarette C&C volumes and share of overall consumption 2006-13

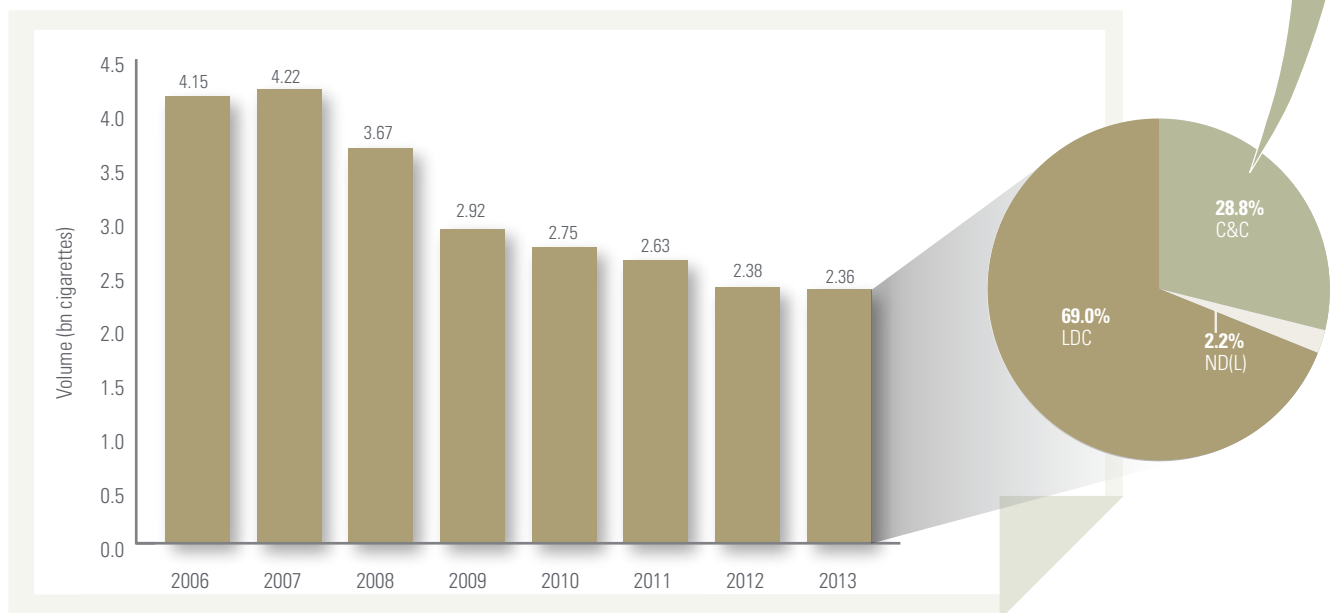


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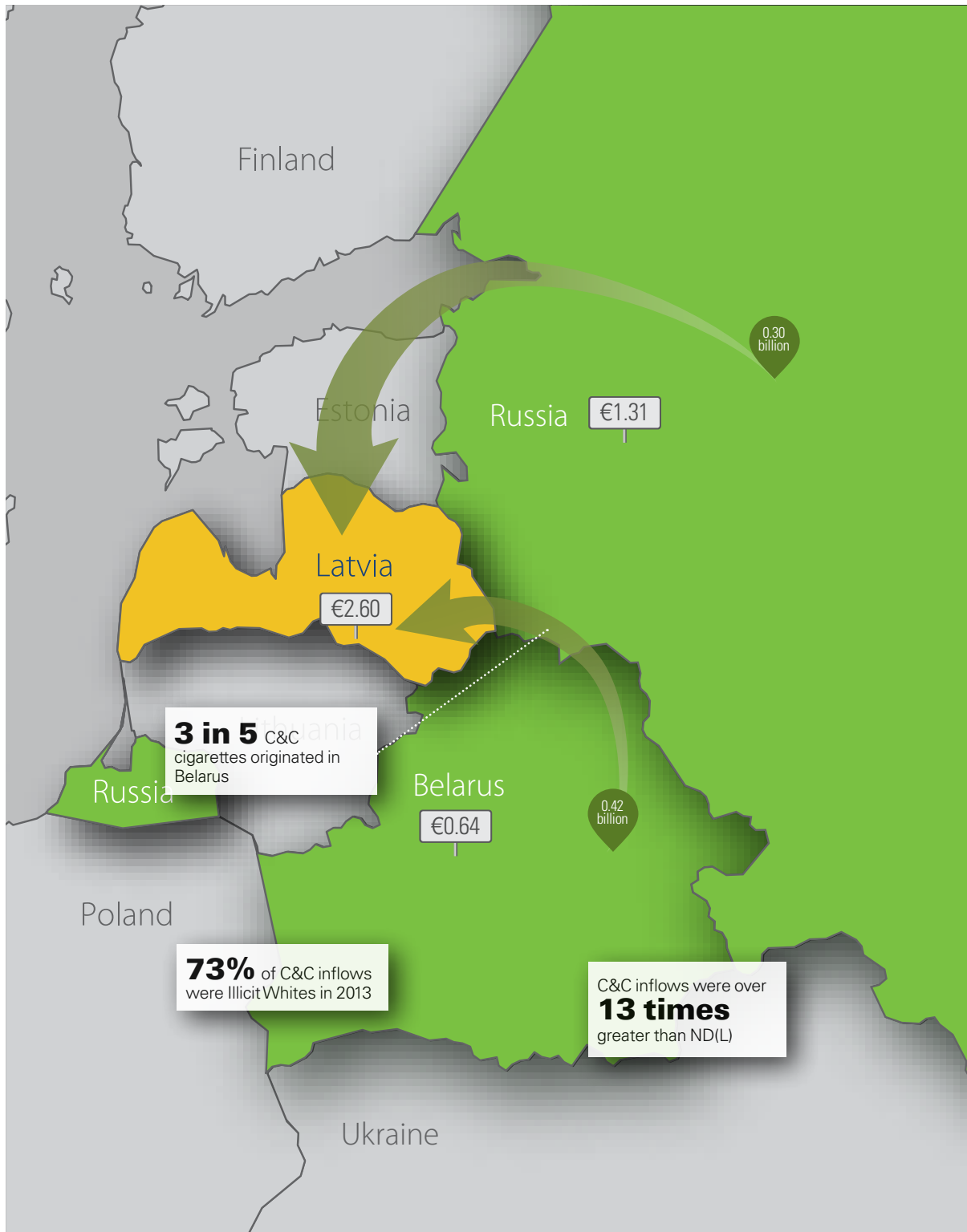


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Manufactured cigarette consumption 2006-13



KEY INFLOWS AND OUTFLOWS



Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

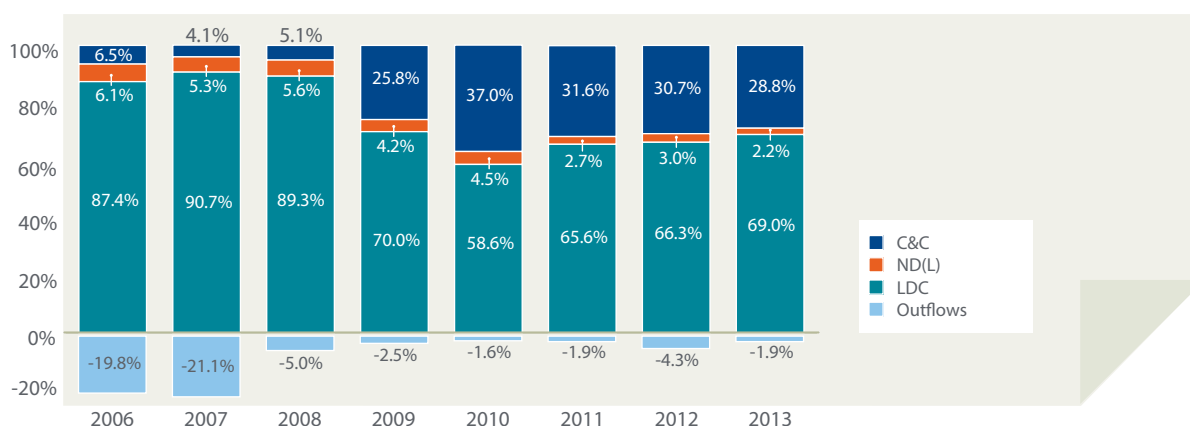
MANUFACTURED CIGARETTE CONSUMPTION

Consumption remained flat, with an increase in legal domestic consumption offset by a decline in non-domestic volumes

Total manufactured cigarette consumption – Latvia^{(1)(2)(a)}

TOTAL LATVIA CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	4.45	4.71	3.46	2.12	1.65	1.77	1.68	1.67	(0)%
Outflows	-0.82	-0.89	-0.18	-0.07	-0.04	-0.05	-0.10	-0.05	(55)%
Legal domestic consumption (LDC)	3.63	3.82	3.28	2.04	1.61	1.72	1.57	1.63	(3)%
Non-domestic legal (ND(L))	0.25	0.22	0.21	0.12	0.12	0.07	0.07	0.05	(28)%
Counterfeit and contraband (C&C)	0.27	0.17	0.19	0.75	1.02	0.83	0.73	0.68	(7)%
Total non-domestic	0.53	0.39	0.39	0.88	1.14	0.90	0.80	0.73	(9)%
Total consumption	4.15	4.22	3.67	2.92	2.75	2.63	2.38	2.36	(1)%

Share of Latvia cigarette consumption by type 2006-2013⁽¹⁾⁽²⁾



Consumption of manufactured cigarettes declined only marginally in 2013, falling 0.6%.

- A number of economic and pricing factors may have contributed to this decline
- Having fallen sharply in 2009 as a result of the global economic crisis, there were increases in both GDP per capita and PDI per capita⁽³⁾⁽⁴⁾
- The rate of unemployment was also down considerably, from 11.4% in 2012 to 9.9%⁽³⁾
- The WAP of cigarettes only increased by 1.9% versus prior year in January 2013, with a 6.9% increase in July 2013. This was largely due to a relatively benign tax environment, where only specific taxation increased marginally in the year⁽⁵⁾

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Source: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) C2014 Economist Intelligence Unit. (4) Euromonitor, downloaded January 2014. (5) EC Excise Duty tables (Part III – Manufactured Tobacco).

Non-domestic inflows continued to represent around a third of total consumption

Total inflows by country of origin 2006-2013^{(1)(a)}

ND INFLOWS TO LATVIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Belarus	0.00	0.00	0.04	0.10	0.24	0.23	0.33	0.42	24%
Russia	0.24	0.17	0.20	0.72	0.86	0.64	0.43	0.30	(30)%
Duty Free	0.04	0.02	0.02	0.01	0.01	0.01	0.01	0.00	(56)%
Lithuania	0.09	0.09	0.12	0.02	0.01	0.00	0.00	0.00	(5)%
Ukraine	0.02	0.00	0.00	0.02	0.01	0.00	0.01	0.00	(82)%
Counterfeit								0.00	n/a
Other	0.14	0.12	0.01	0.01	0.02	0.02	0.02	0.00	(78)%
Total inflows	0.53	0.39	0.39	0.88	1.14	0.90	0.80	0.73	(9)%

Non-domestic (ND) inflows declined by 8.5% in 2013, with a much lower inflow from Russia

- Typically inflows originate from cheaper neighbouring market of Russia and more recently Belarus in the South. Flows from Belarus increased from 0.33bn cigarettes in 2012 to 0.42bn in 2013. Although the price differential declined marginally to €1.74 per 20 cigarettes in January 2013, it then increased to €1.88 in July 2013⁽²⁾, which may have influenced the volume of inflows
- Inflows from Russia fell by 30.1% and Belarus has overtaken Russian as the largest source country. Fewer Russian origin packs were collected during the Empty Pack Survey (EPS) and this was particularly evident in the capital, Riga. This may have been driven by the availability of cheaper manufactured cigarettes from Belarus. In January 2013, the WAP in Russia was €1.16 for 20 cigarettes compared to €0.66 in Belarus⁽²⁾
- Duty Free volumes have typically been low and declined in 2013. Illicit Whites with Duty Free labelling account for 26.0% of total Duty Free volumes and the main brand sold as an Illicit Whites appears to be Jin Ling

Total outflows by destination country 2006-2013⁽¹⁾

OUTFLOWS FROM LATVIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Sweden	0.01	0.06	0.01	0.00	0.00	0.00	0.01	0.01	66%
UK	0.23	0.33	0.04	0.02	0.01	0.02	0.04	0.01	(79)%
Ireland	0.13	0.20	0.02	0.02	0.02	0.01	0.01	0.01	(50)%
Other	0.45	0.31	0.11	0.03	0.02	0.02	0.05	0.02	(55)%
Total outflows	0.82	0.89	0.18	0.07	0.04	0.05	0.10	0.05	(55)%

Outflows remained low as a percentage of consumption, with volumes declining from 0.10bn to 0.05bn in 2013

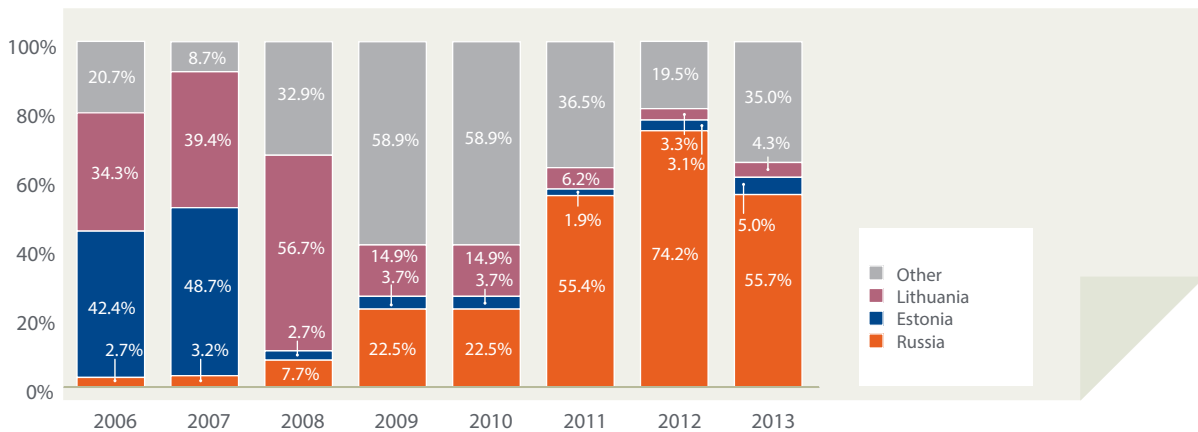
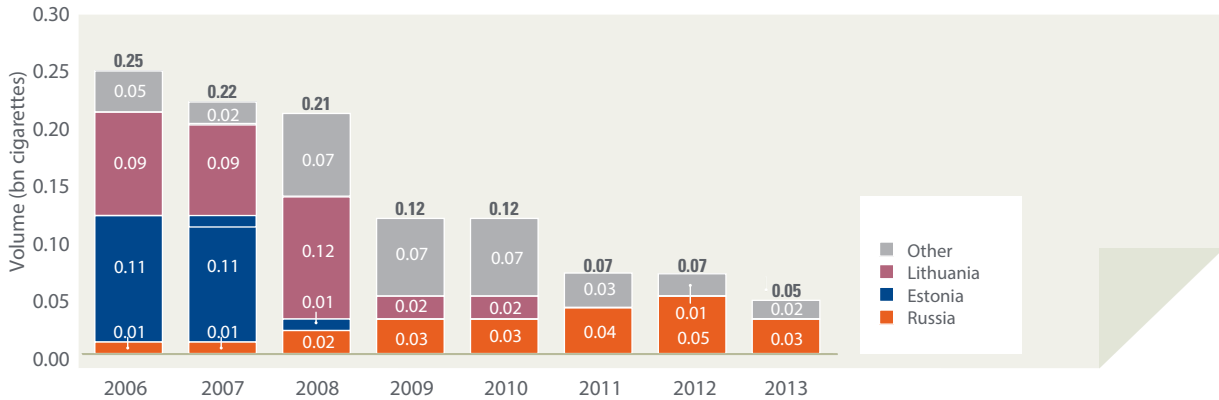
- The largest driver of this is the decrease in flows to the UK. This may have been driven by the international sporting events and Royal Jubilee held in the UK in 2012, as flows peaked in that year

Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Source: (1) KPMG EU Flows Model. (2) EC Excise Duty tables (Part III – Manufactured Tobacco).

ND(L) flows remain a substantially smaller share of consumption than C&C

ND(L) by origin 2006-2013^{(1)(2)(a)(b)}



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Non-domestic legal (ND(L)) volumes in Latvia represent a relatively small share of total ND

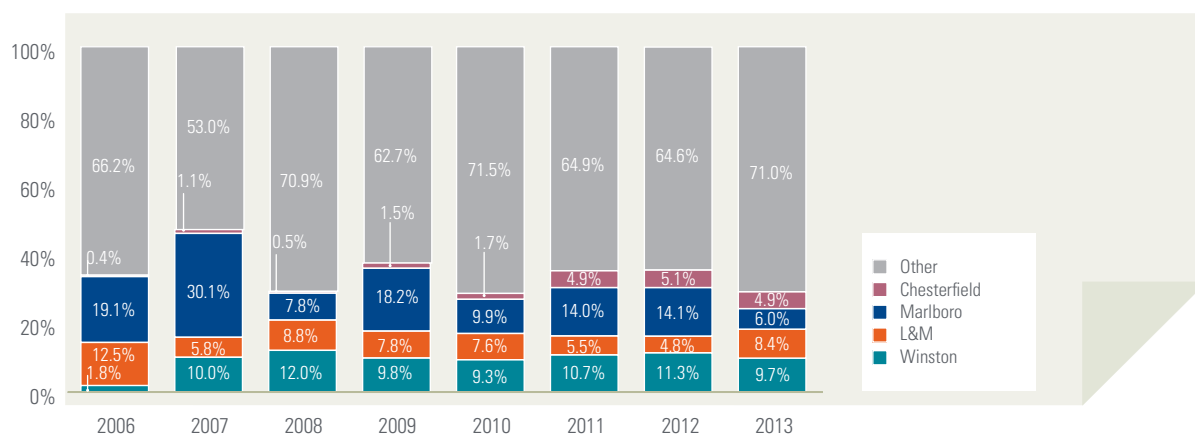
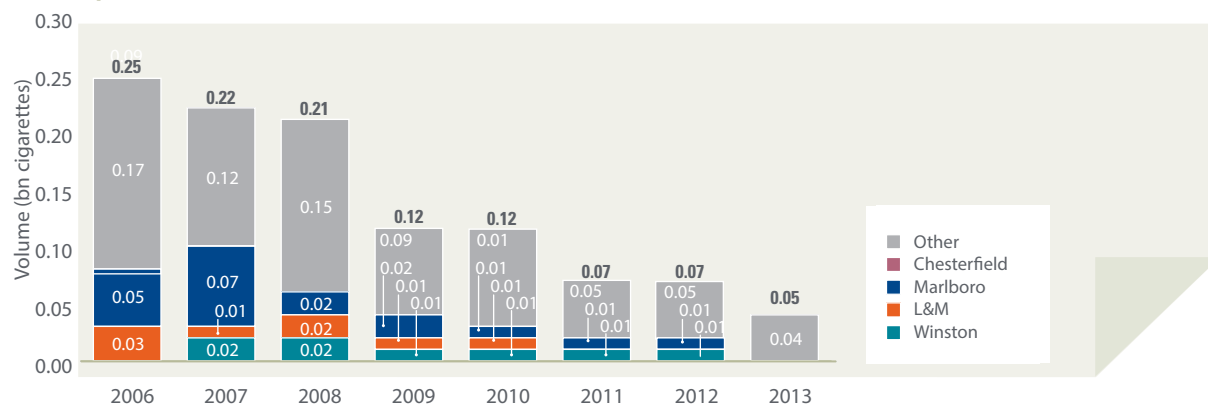
- Cigarette inflows from bordering Estonia and Lithuania are minimal and this is likely due to low price differentials for cigarettes between these three countries
- Most inflows originate from Russia and Belarus. Consumer research indicates that travellers to Russia bring back relatively few packs per trip on average. As such, only about a tenth of inflows from Russia are allocated to ND(L)
- However, there appears to be minimal outbound tourism to Belarus⁽³⁾ and as such less than 0.01bn of the total 0.42bn Belarusian flow is allocated to ND(L)

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-2012, UN WTO.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand 2006-2013^{(1)(2)(a)}



There was a decline in ND(L) volumes of most brands this year

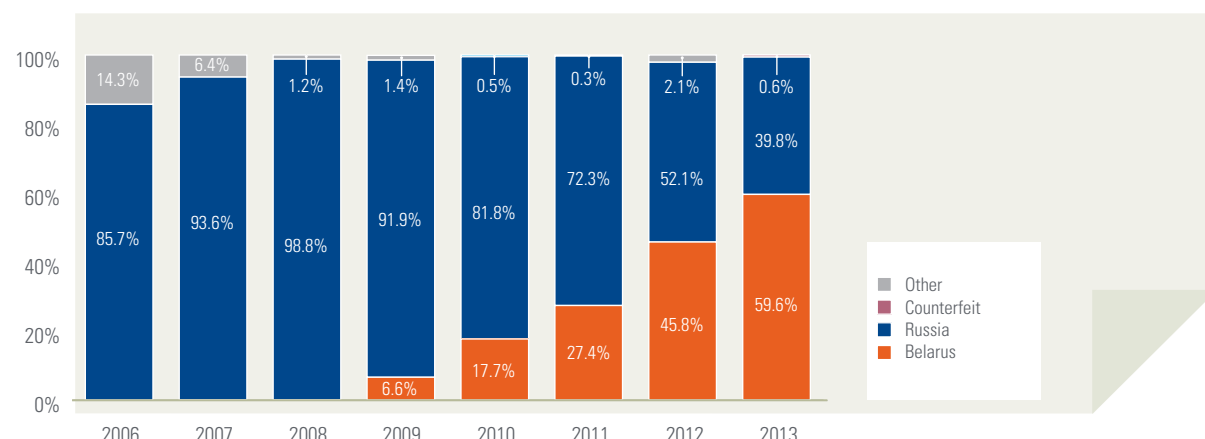
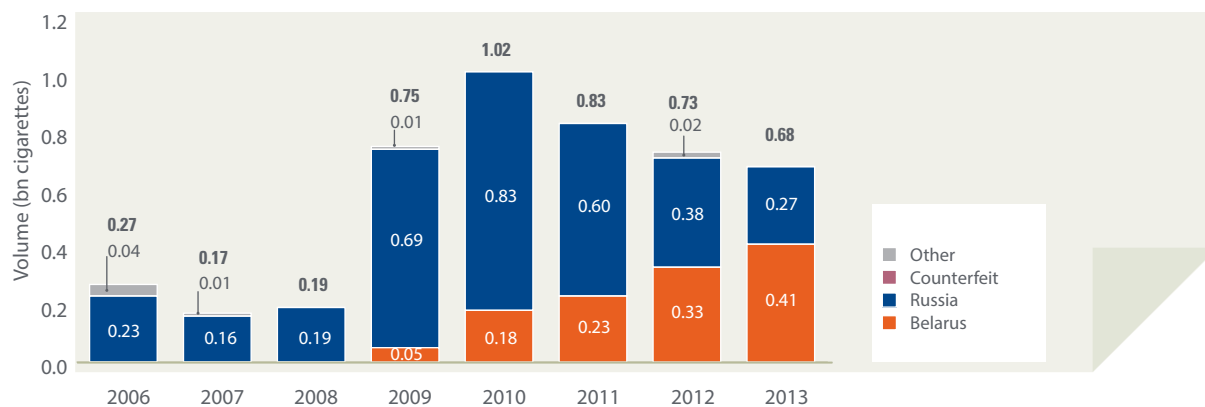
- ND(L) is comprised of a large number of small individual brand flows, the largest of which, Winston, declined this year by 38.7% to less than 0.01bn cigarettes
- Both Winston and Chesterfield ND(L) volumes were impacted by lower legal volumes from Russia
- Greater legal flows of L&M originated from Russia and partly offset the above declines
- "Other" comprises smaller volumes of around 50 brands

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

Belarusian flows now represent the largest source of C&C volumes

C&C by origin 2006-2013^{(1)(2)(a)(b)}



Counterfeit and contraband (C&C) continues to represent the greatest share of total non-domestic volumes which may be due to the close proximity of cheaper non-EU markets, long borders and limited customs resources

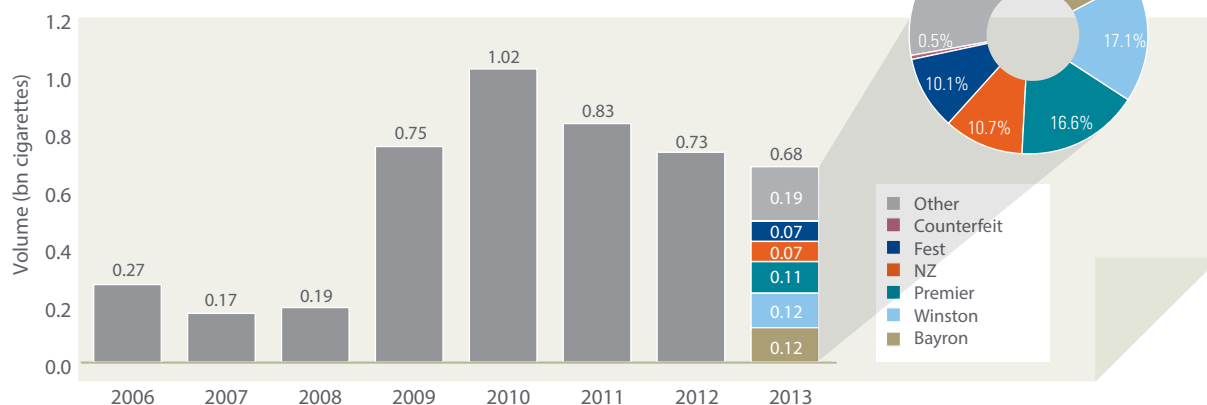
- Belarusian origin packs make up the largest component of C&C, as minimal and declining outbound tourism suggests the increased Belarus incidence has to be almost entirely allocated to illicit flows
- Russian origin packs also represent a large share of total C&C and similarly, outbound tourism and average packs per trip are not great enough to legally account for the entire Russian ND incidence
- It appears that C&C products are widely consumed in smaller towns (and therefore likely also in rural areas) and this may be due to the relatively low incomes in these locations
- The population has traditionally shown a higher tolerance for illicit products than other EU markets. Latvia also represents one of the key transit routes for illicit products into other Eastern and then Western European markets
- In response, an awareness campaign was introduced by the Latvian Government which focused on the risks associated with illicit cigarette consumption and was supported by the Latvian Ministry of Finance. Border technologies have also been renewed (such as registration plate reading systems) though limited overall resources resulted in a modest impact on the issue
- Counterfeit cigarettes are negligible in Latvia, accounting for 0.5% of the total 0.68bn C&C volume. This is likely due to the availability of very cheap cigarettes from neighbouring markets
- If these C&C cigarettes had been legally purchased in Latvia, the tax revenue gained would have been approximately €69m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

C&C INFLOWS BY BRAND

C&C by brand 2006-2013^{(1)(2)(a)}



Contraband cigarettes are less of an issue in Latvia when compared to Illicit Whites, accounting for only 26.4% of C&C volumes

- Flows from Belarus now account for around 60% of total C&C volumes; those manufactured by Grodno Tobacco such as Premier, NZ and Fest all saw substantial percentage increases in C&C flows in 2013

Breakdown of Illicit Whites by type 2007-2013^{(1)(2)(a)(b)}

LABELLING OF ILLICITWHITES INFLOWS TO LATVIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.00	0.05	0.20	0.27	0.36	0.40	0.50	24%
Duty Free	0.00	0.00	0.00	0.00	0.00	0.00	0.00	>100%
Unspecified	0.00	0.00	0.00	0.00	0.00	0.00	0.00	n/a
Total Illicit Whites	0.09	0.05	0.20	0.27	0.36	0.40	0.50	24%

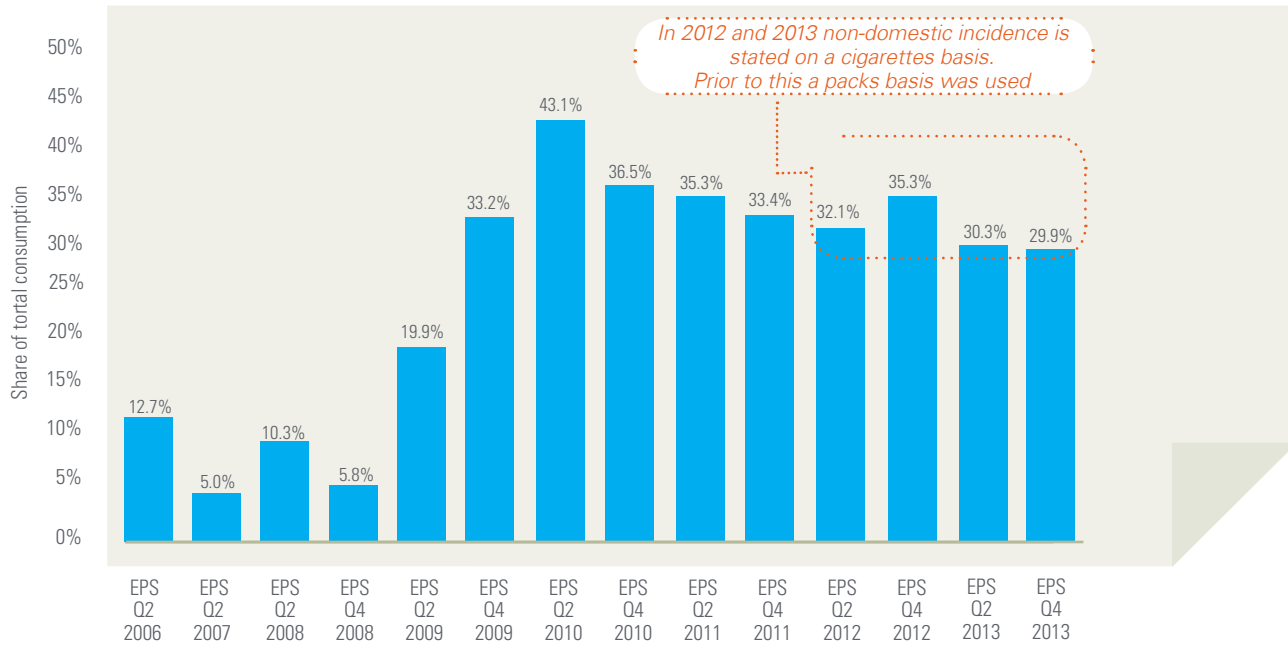
- Illicit Whites appear to be a significant issue in Latvia, accounting for 73.1% of total C&C flows in 2013. Illicit Whites with country specific labelling account for almost the entire balance and the largest brands appear to be Bayron, Premier and NZ

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

EPS results & EU Flows Model

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



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- The EPS in Latvia collected 9,800 packs during the course of the year. This was undertaken as two waves – one conducted in Q2 (April) and one in Q4 (September / October). Each wave collected 4,900 packs across the largest 25 towns and cities. The number of packs collected in each city is weighted by the city population
- To more fairly represent the large rural population in Latvia (58% rural⁽²⁾) and the typically higher incidence in such regions, EPS data was re-weighted in our analysis such that the regional share of the survey aligned with regional population shares. This marginally increased ND incidence from 30.1% to 30.9%

Source: (1) Independent agency Empty Pack Surveys, 2006 – 2013. (2) Euromonitor, downloaded January 2014.

ND(L) volume calculations and explanations

KPMG non domestic legal flows Latvia

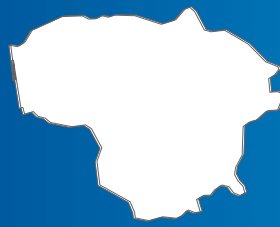
USE OF CONSUMER RESEARCH AND ANY ADJUSTMENTS FOR 2013 DATA							
Country	ND 2013 ⁽¹⁾ (bn sticks)	Total trips where cigarettes purchased (m) ⁽²⁾	Number of packs per trip ⁽³⁾	Total packs (m)	Data sources ⁽²⁾⁽⁴⁾⁽⁵⁾	2013 ND(L) (bn sticks)	% of ND
Russia	0.30	0.14	10	1.43	Consumer research, WTO, WAP pricing tables	0.03	9%

- To estimate the legal element of the inflow from Russia, consumer research has been used.
 - Consumer research appeared to understate the likely number of trips to purchase cigarettes. In our analysis, trips were modelled as outbound travel multiplied by manufactured cigarette prevalence
 - Consumer research also appeared to understate average packs per trip. It is instead assumed that consumers bring back the legal maximum into Estonia from outside the EU, set at 1 carton (by air)

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

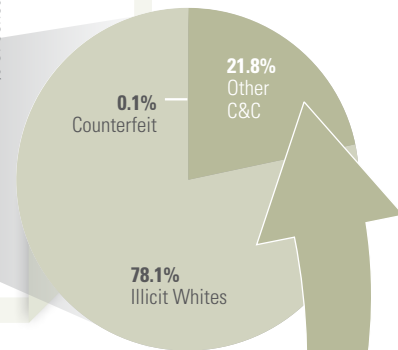
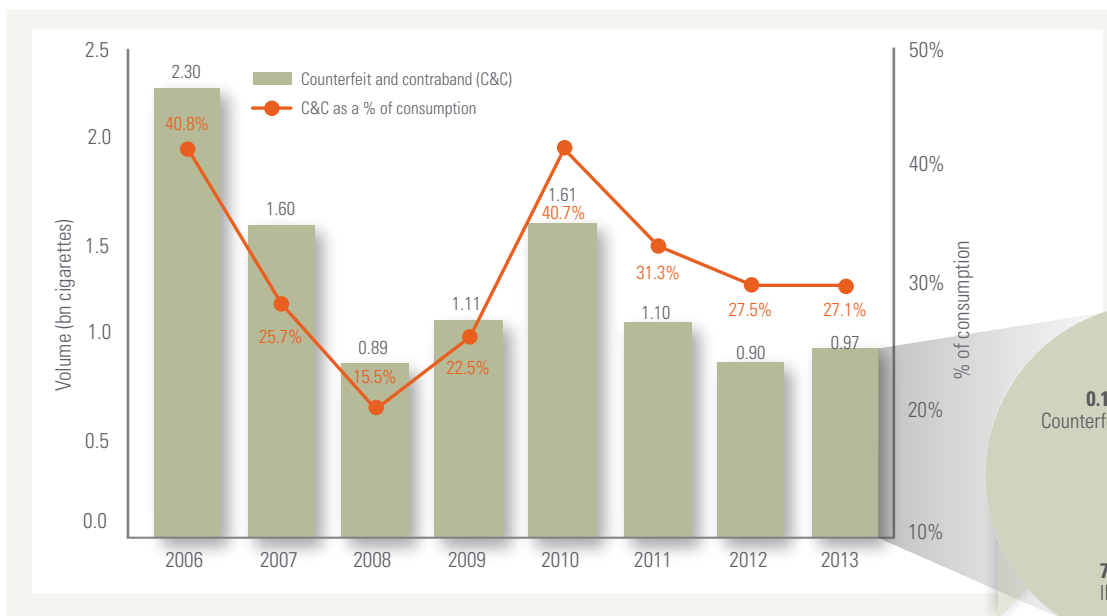
Sources: (1) KPMG EU Flows Model. (2) Synovate/Ipsos ND(L) research 2013. (3) UN WTO Tourism Factbook 2008-12, UN WTO. (4) EC Excise Duty tables (Part III – Manufactured Tobacco).

LITHUANIA



Counterfeit & Contraband increased, along with an overall increase in consumption

Manufactured cigarette C&C volumes and share of overall consumption 2006-13

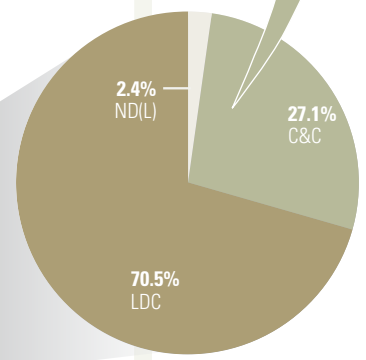
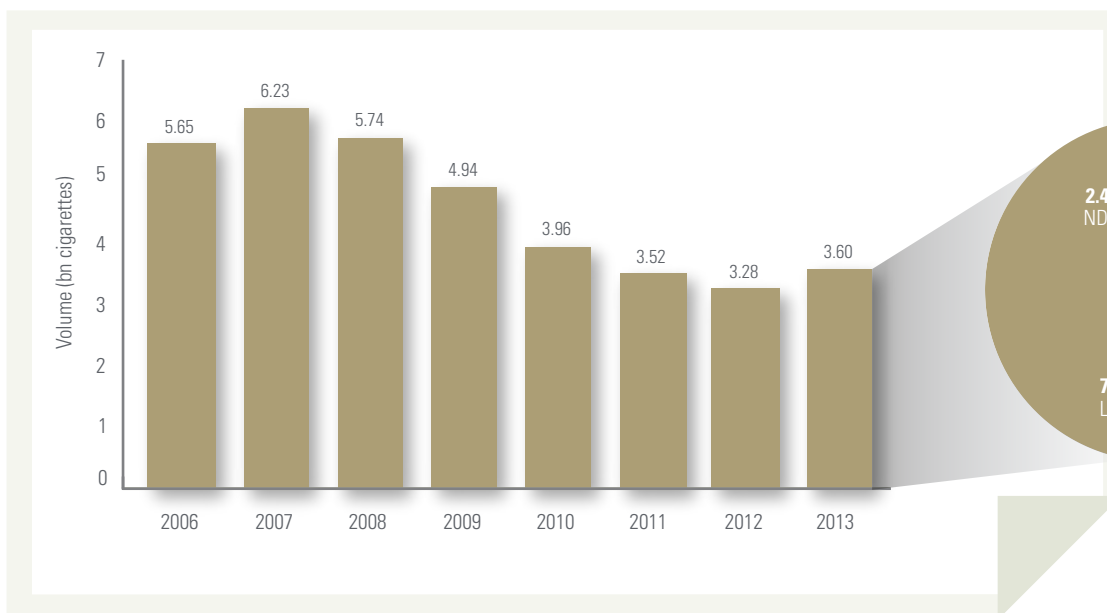


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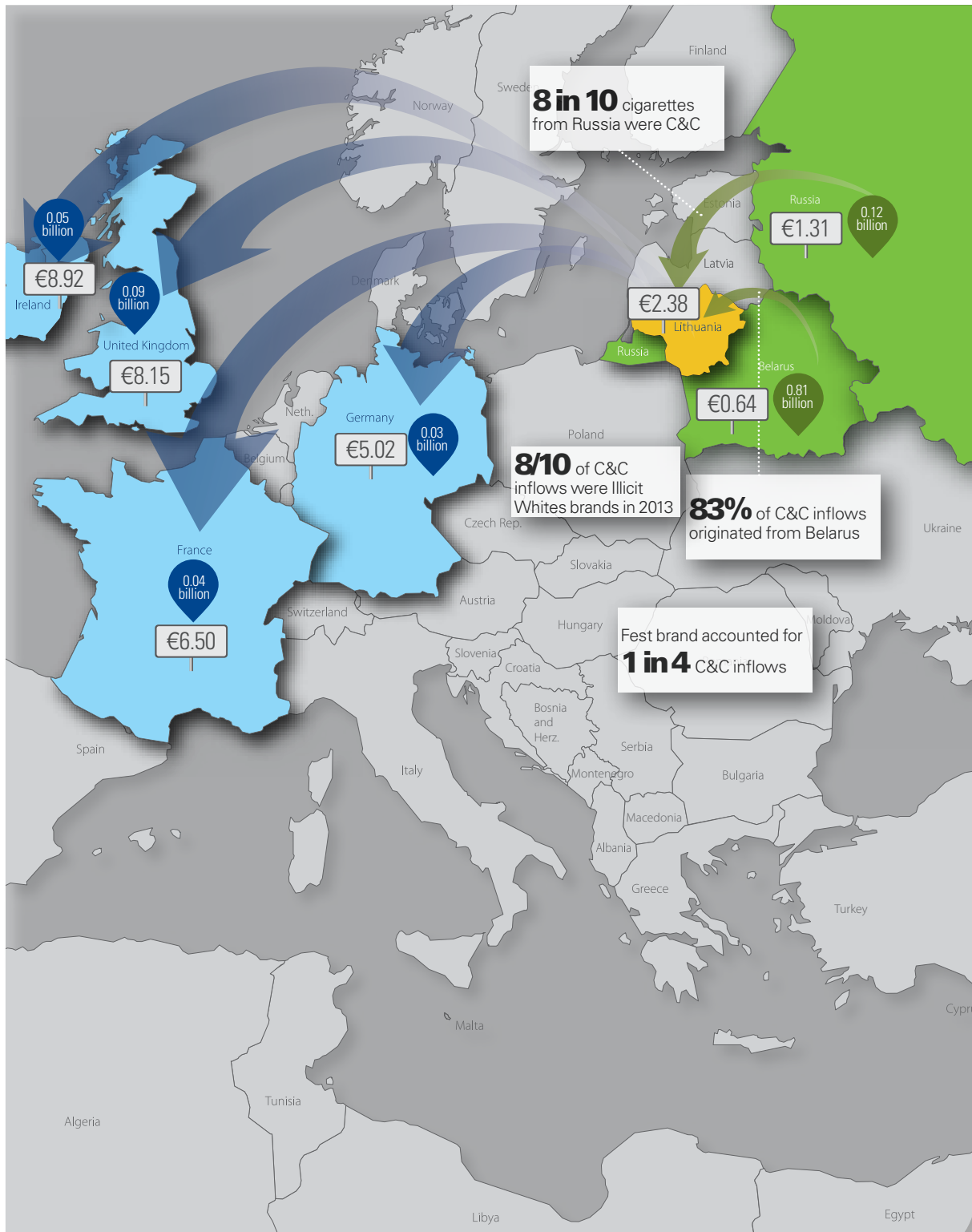


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Manufactured cigarette consumption 2006-13



KEY INFLOWS AND OUTFLOWS



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Main outflow ■
Main inflow ■

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

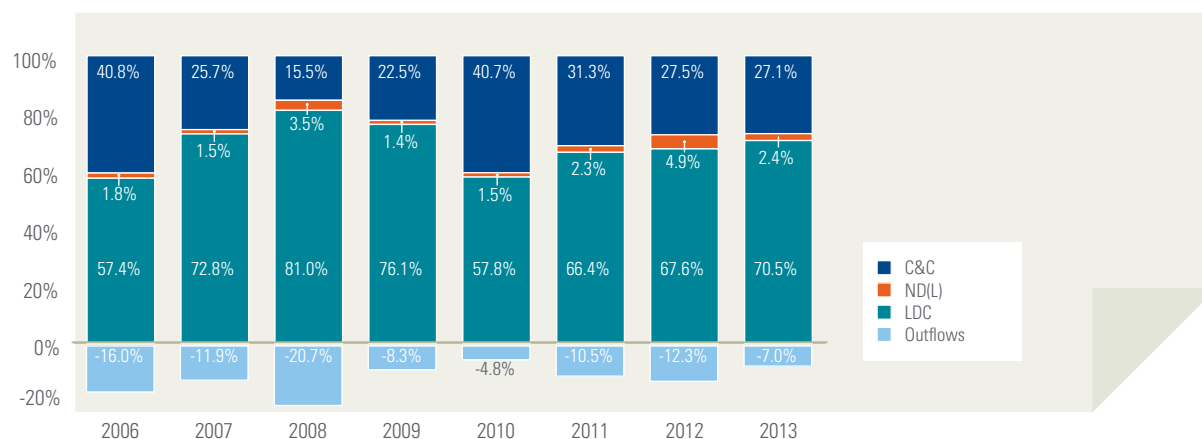
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Consumption grew in 2013, primarily reflected in an increase in legal domestic consumption

Total manufactured cigarette consumption – Lithuania^{(1)(2)(a)}

TOTAL LITHUANIA CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	4.14	5.27	5.84	4.17	2.48	2.70	2.62	2.79	6%
Outflows	-0.90	-0.74	-1.19	-0.41	-0.19	-0.37	-0.40	-0.25	(378)%
Legal domestic consumption (LDC)	3.24	4.53	4.65	3.76	2.29	2.34	2.22	2.54	14%
Non-domestic legal (ND(L))	0.10	0.09	0.20	0.07	0.06	0.08	0.16	0.09	(46)%
Counterfeit and contraband (C&C)	2.30	1.60	0.89	1.11	1.61	1.10	0.90	0.97	8%
Total non-domestic	2.40	1.70	1.09	1.18	1.67	1.18	1.06	1.06	(0)%
Total consumption	5.65	6.23	5.74	4.94	3.96	3.52	3.28	3.60	10%

Share of Lithuanian cigarette consumption by type - 2006-2013⁽¹⁾⁽²⁾⁽³⁾



Consumption of manufactured cigarettes in Lithuania increased in 2013 in contrast to most EU markets

- A number of economic and tax related factors are likely to have contributed to the increase
 - GDP per capita increased by 9.6%⁽³⁾
 - PDI per capita also grew, to €7.6k in 2013 from €7.0k in 2012⁽⁴⁾
 - Unemployment also continued its downward trend (having peaked in 2010 following the economic crisis), falling from 13.4% to 11.8%⁽³⁾
- The above factors indicate some strengthening in the economy which is likely to have supported consumption in general and sales growth in cigarettes
- Based on WAP, the price of a pack of 20 cigarettes increased by 5.8% this year to €2.38⁽⁵⁾. WAP remains lower than the other Baltic states of Estonia and Latvia as well as neighbouring Poland, and the price differential with these markets also grew in the year
- As such, legal domestic sales (LDS) volumes are less likely to be impacted by prices in some neighbouring markets

Notes: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) 2014 Economist Intelligence Unit. (4) Euromonitor, downloaded January 2014. (5) EC Excise Duty tables (Part III – Manufactured Tobacco).

Most manufactured cigarette inflows originated from non-EU markets, mainly from Belarus and Russia

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWS TO LITHUANIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Belarus	0.02	0.02	0.12	0.23	0.78	0.80	0.76	0.81	7%
Russia	1.57	1.24	0.66	0.87	0.78	0.28	0.18	0.12	(30)%
Duty Free	0.42	0.23	0.08	0.05	0.08	0.08	0.10	0.10	4%
Germany	0.01	0.01	0.01	0.00	0.00	0.00	0.00	0.00	>100%
Counterfeit								0.00	n/a
Other	0.38	0.19	0.23	0.03	0.03	0.02	0.02	0.01	(31)%
Total inflows	2.40	1.70	1.09	1.18	1.67	1.18	1.06	1.06	(0)%

Non-domestic inflows of cigarettes remained constant in 2013 but fell as a percentage of total consumption

- ND inflows continue to remain high as a percentage of total consumption relative to other EU markets. The long border shared with Belarus and Lithuania's proximity to Russia, both of which have substantially lower cigarette prices, are likely to drive this. The Baltic nations may also be used a transit route for cheaper cigarettes through to other Eastern and Western European countries
- Cigarette inflows were flat overall though, with a decline in inflows from Russia potentially as a result of lower outbound tourism in the year (outbound tourism to Russia declined, as did total outbound trips⁽²⁾), offset by increased flows from Belarus
- Duty Free inflows grew marginally in the year with around half of the Duty Free balance made up of Illicit Whites with Duty Free labelling. The main Illicit Whites brands appear to be Compliment and Lifa (both Baltic Tobacco Factory)

Total outflows by destination country – 2006-2013⁽¹⁾

OUTFLOWS FROM LITHUANIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
UK	0.20	0.15	0.32	0.19	0.06	0.21	0.22	0.09	(58)%
Ireland	0.13	0.06	0.12	0.07	0.06	0.06	0.06	0.05	(17)%
France	0.00	0.00	0.05	0.02	0.00	0.02	0.05	0.04	(18)%
Germany	0.04	0.05	0.05	0.02	0.02	0.03	0.03	0.03	(15)%
Other	0.53	0.47	0.64	0.12	0.14	0.05	0.04	0.04	(7)%
Total outflows	0.90	0.74	1.19	0.41	0.19	0.37	0.40	0.25	(38)%

There was a substantial decline in outflows of cigarettes, which fell 37.5% in the year

- Flows to the UK accounted for this decline, falling from 0.22bn cigarettes in 2012 to 0.09bn in 2013, though it still remained the biggest outflow destination

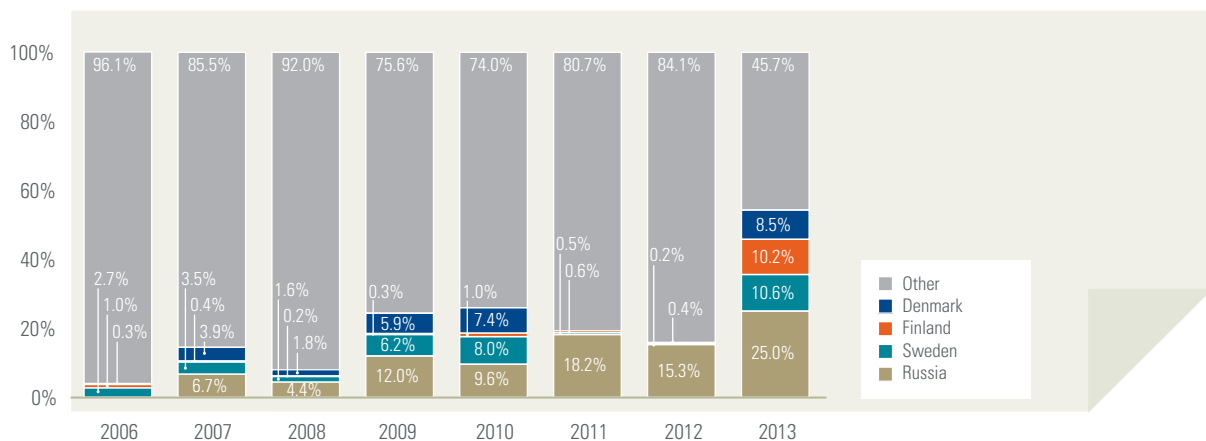
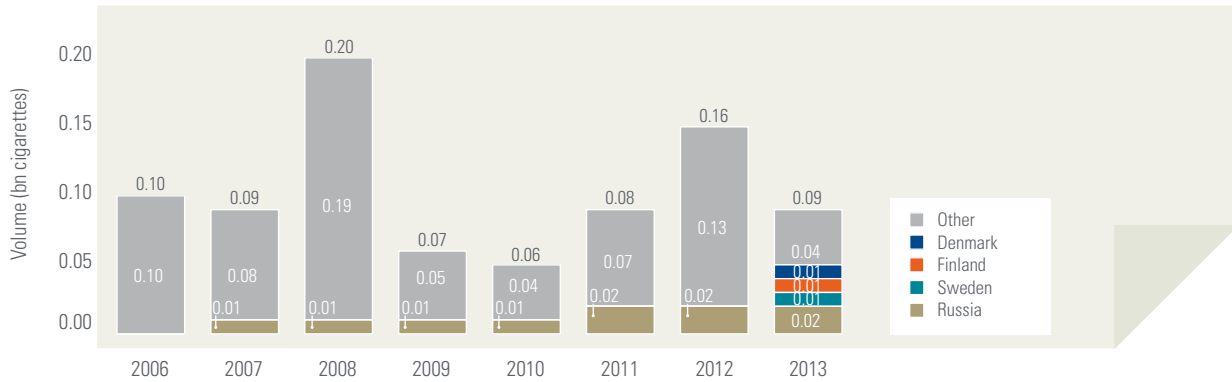
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model. (2) UN WTO Tourism Factbook 2008-2012, UN WTO.



Non-domestic legal volumes remain low and mainly arise from Russia and the Nordic countries

ND(L) by origin - 2006-2013^{(1)(2)(a)(b)}



LITHUANIA



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As a share of total non-domestic inflows, legal volumes remain low and represent only 2.4% of total consumption this year

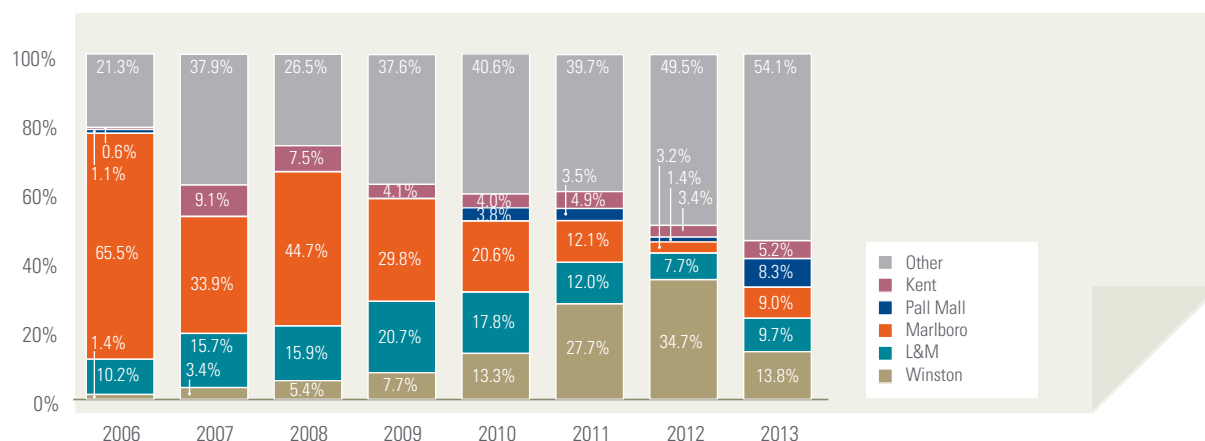
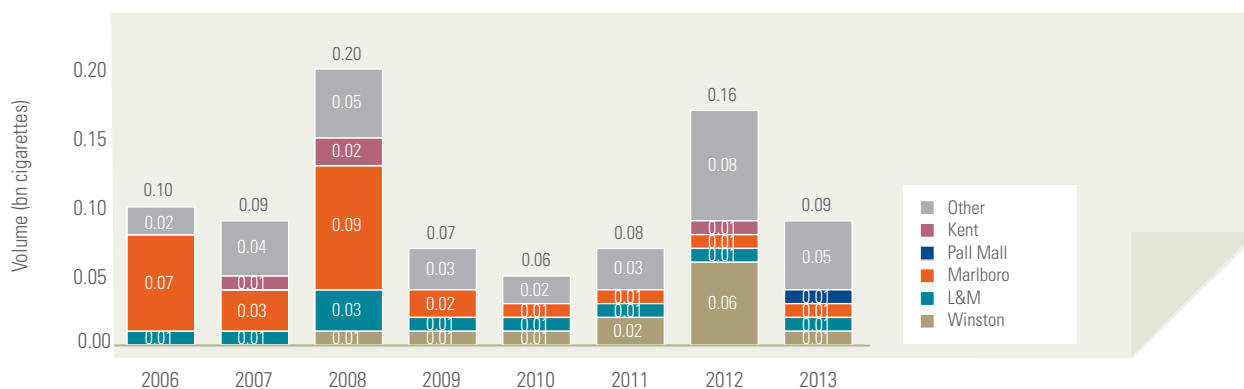
- Non-domestic legal ND(L) flows from Russia declined by 11.1% in 2013, which may have been as a result of lower outbound tourism⁽³⁾. Outbound tourism to Belarus remained low and actually fell during the year. As a result, all of the 0.81 bn inflows were allocated to counterfeit and contraband (C&C)
 - Consumer research, combined with an analysis of relative price levels and changes in tourism show that average packs purchased per trip and tourist flows are not large enough to account for the significant inflows seen from Belarus and Russia
- There are minimal legal inflows from several other markets such as the Nordic countries

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-2012, UN WTO.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013^{(1)(2)(a)}



The decline in ND(L) is evident across a number of brands but has had the greatest impact on Winston volumes

- Although total inflows of Winston have declined, those from Belarus remain high
- Other legal inflows comprises smaller volumes of around 45 brands

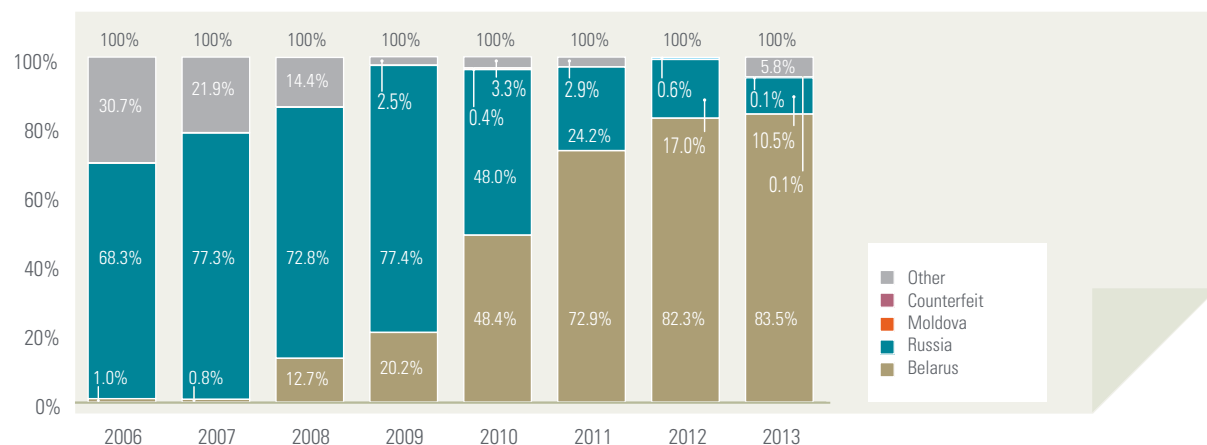
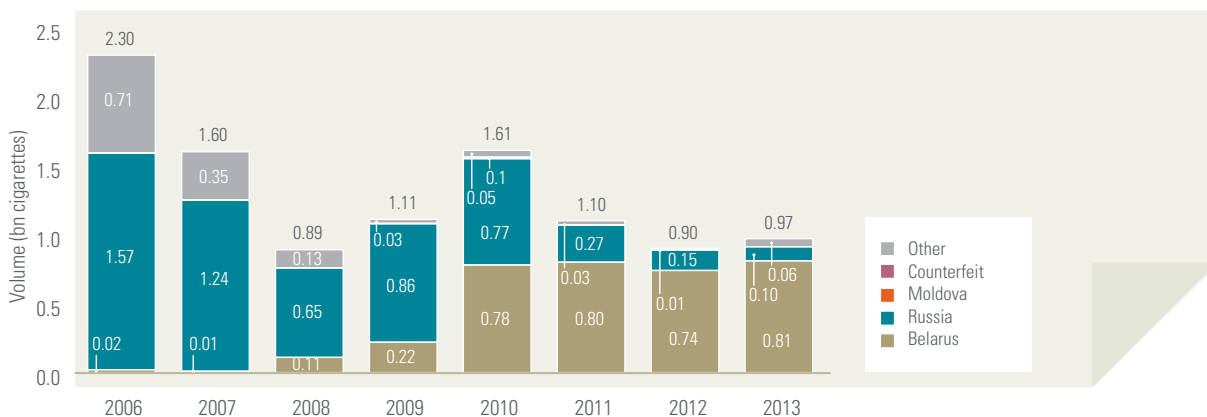
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



C&C inflows from Russia declined again this year; there may have been some substitution for cheaper Belarusian flows

C&C by origin - 2006-2013^{(1)(2)(a)(b)}



LITHUANIA



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C&C volumes increased by 7.8% in 2013. Though C&C has declined marginally as a share of total consumption, it remains high in comparison to other European markets

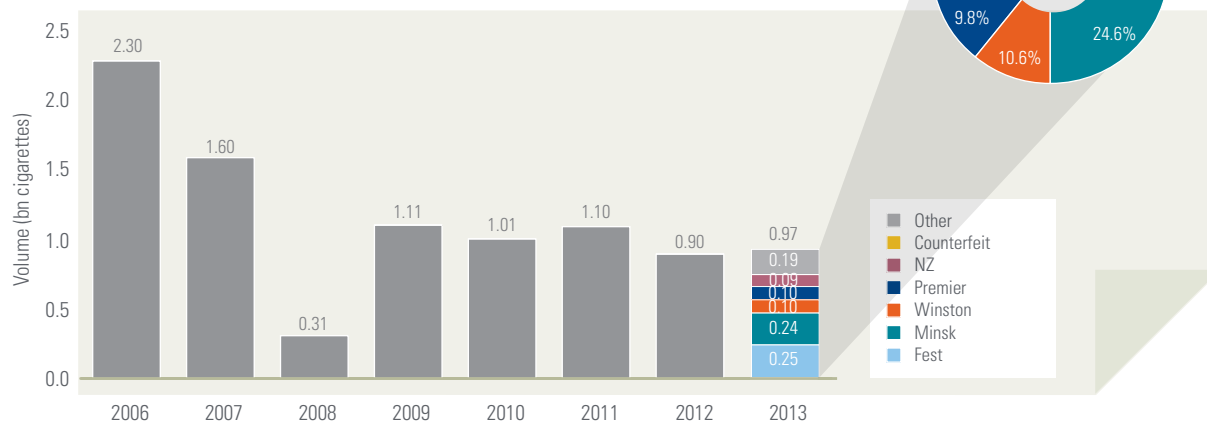
- This is largely driven by the relatively low incomes of the population, especially in smaller urban areas and rural locations, though residents of larger cities also consume illicit cigarettes
- The Lithuanian Government has implemented an awareness campaign which is supported by bodies such as the local police and customs officials in an effort to reduce C&C, though the impact of this is yet to be seen
- Counterfeit cigarettes are only a small share of C&C (0.1%) and this is likely due to the availability of cheap contraband product and Illicit Whites from Russia and Belarus
- If these C&C cigarettes had been legally purchased in Lithuania the tax revenue gained would have been approximately €91m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

C&C INFLOWS BY BRAND

C&C by brand - 2006-2013^{(1)(2)(a)}



Illicit Whites are a significant issue in Lithuania and represent almost 80% of C&C volumes; contraband volumes are much smaller by comparison and form only around a fifth of C&C volumes

- Belarus continues to be the largest source of C&C in Lithuania, with volumes up from 0.74bn in 2012 to 0.81bn this year. The border with Belarus and the cheaper cigarette price differential than that with Russia suggests the availability of large quantities of Belarusian Illicit Whites may be comparatively attractive. The price differential with Belarus based on the WAP for 20 cigarettes increased from €1.59 to €1.70 in 2013, whilst that with Russia grew from €1.09 to €1.12⁽³⁾. In the same time period, C&C on a brand basis shows increased incidence of the Belarus based Grodno Tobacco brands such as Fest, Minsk and Premier
- C&C flows from Russia continued on a downward trend at 33.2% below that in the prior year and again this may in part be due to cheaper cigarettes available from Belarus. Tightening of border controls (such as new registration plate reading systems) may have also had an impact
 - In terms of brands, C&C flows from Russia include Saint George (0.03bn) and Compliment (0.02bn)
- Illicit Whites represent the major share of the total C&C flows into Lithuania. Illicit Whites with country specific labelling are the largest type here and most originate from Belarus. The largest Illicit Whites brands in Lithuania appear to be the Grodno Tobacco brands such as Fest, Minsk and Premier

Breakdown of Illicit Whites by type 2007-2013^{(1)(2)(a)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO LITHUANIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.00	0.03	0.15	0.58	0.65	0.66	0.74	12%
Duty Free	0.00	0.00	0.00	0.00	0.01	0.01	0.02	68%
Unspecified	0.00	0.00	0.00	0.00	0.00	0.00	0.00	n/a
Total Illicit Whites	0.01	0.03	0.15	0.58	0.66	0.67	0.76	13%

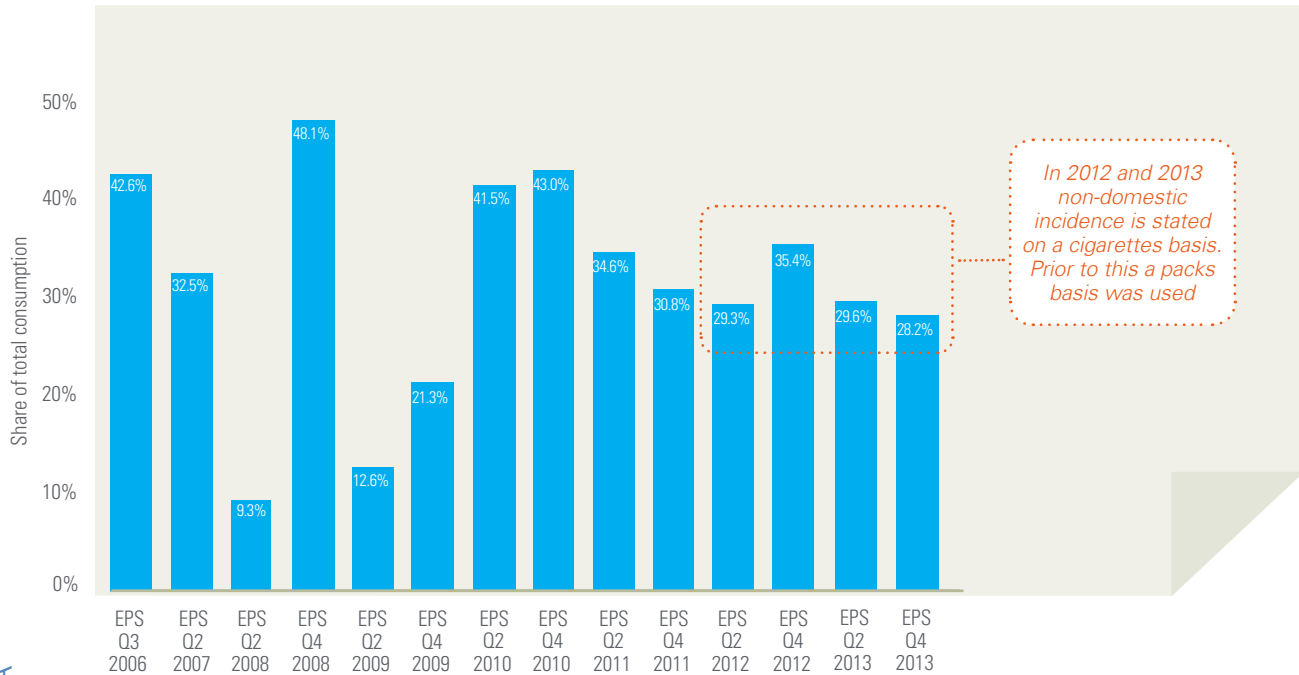
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG analysis of data sources provided by manufacturers. (2) EC Excise Duty tables (Part III – Manufactured Tobacco).



EPS results & EU Flow model

Empty Pack Survey non-domestic estimates - 2006-2013⁽¹⁾



LITHUANIA



- The empty pack survey (EPS) in Lithuania collected 11,600 packs during the course of the year. This was undertaken as two waves – one conducted in Q2 (April) and one in Q3/Q4 (September / October). Each wave collected 5,800 packs across the largest 20 towns and cities. The number of packs collected in each city is weighted by the city population
- To more fairly represent the large rural population in Lithuania (33% rural ⁽²⁾) and the typically higher incidence in such regions in our analysis, EPS data was re-weighted such that the regional share of the survey aligned with regional population shares. This marginally increased ND incidence from 28.9% to 29.6%

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Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013. (2) Euromonitor, downloaded January 2014.

ND(L) volumes calculations and explanations

KPMG non domestic legal flows Lithuania

KPMG NON DOMESTIC LEGAL FLOWS LITHUANIA							
Country	ND 2013 (bn sticks) (1)	Total trips where cigarettes purchased (m) ⁽²⁾⁽³⁾	Number of packs per trip (2)(4)	Total packs (m)	Data sources ⁽²⁾ (3)(4)	2013 ND(L) (bn sticks)	% of ND
Russia	0.12	0.11	10	1.09	Consumer research, WTO	0.02	18%
Sweden	0.00	0.04	11	0.46	Consumer research	0.01	>100%
Finland	0.00	0.02	22	0.44	Consumer research	0.01	>100%

- Consumer research has been used to estimate the legal element of the inflow from Russia:
 - Consumer research appeared to understate the likely number of trips to purchase cigarettes. Instead, trips were modelled in our analysis as outbound travel multiplied by manufactured cigarette prevalence
 - Consumer research also appeared to understate average packs per trip. It is instead assumed in our analysis that consumers bring back the legal maximum into Lithuania from outside the EU, set at 1 carton (by air)
- To estimate the legal element of inflows from Sweden and Finland, consumer research has also been used, though no adjustments have been made in our analysis. Although this consumer research implies a legal volume greater than the total non-domestic incidence, the two flows are considered immaterial and so no capping is applied



Notes: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

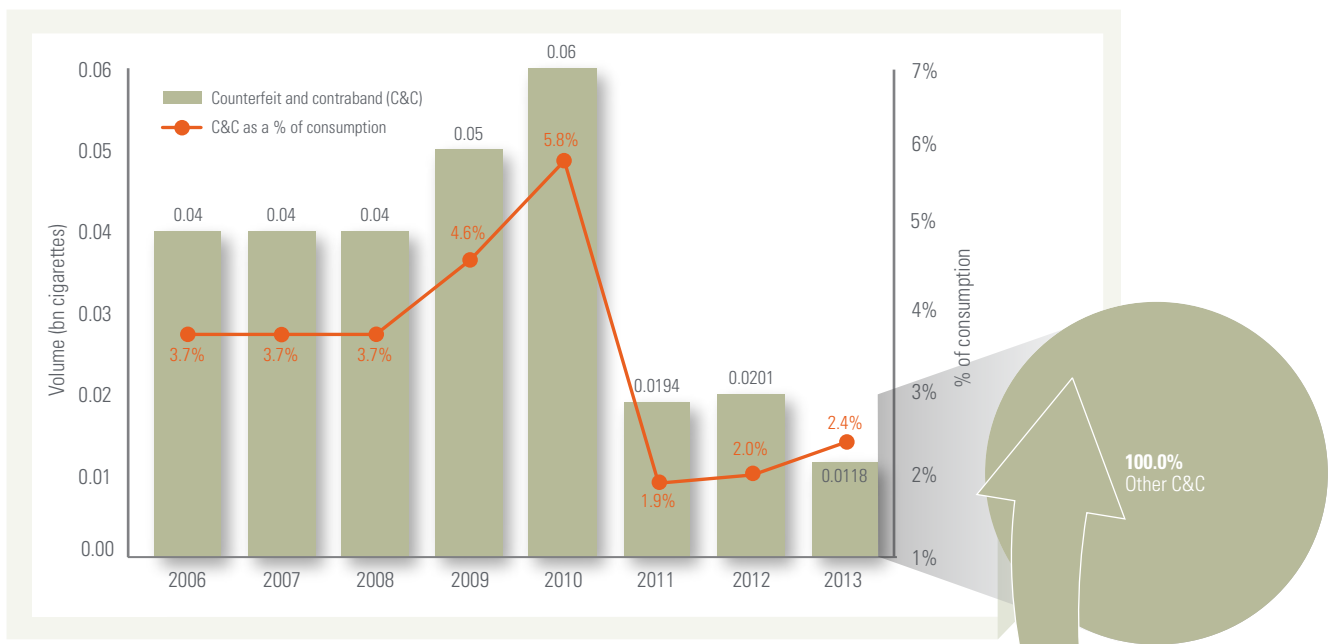
Sources: (1) KPMG EU Flows Model. (2) Synovate/Ipsos ND(L) research 2013. (3) UN WTO Tourism Factbook 2008-12, UN WTO. (4) EC Excise Duty tables (Part III – Manufactured Tobacco).

LUXEMBOURG



Total consumption declined, and Luxembourg remained an outflow country

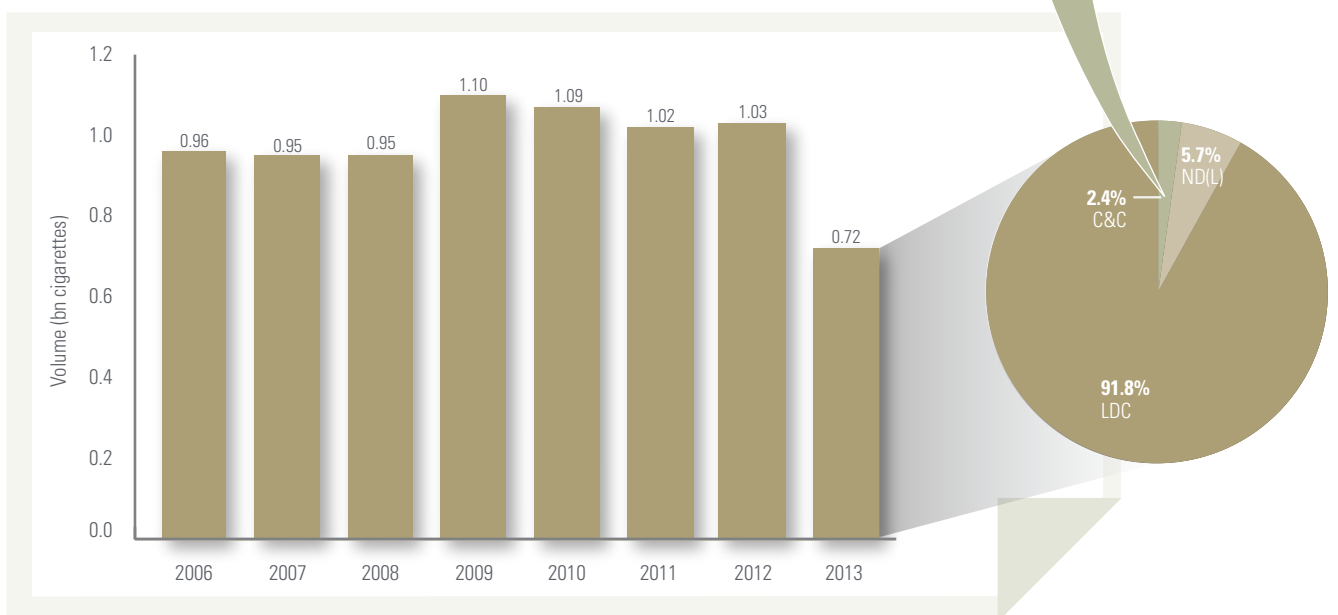
Manufactured cigarette C&C volumes and share of overall consumption 2006-13



LUXEMBOURG

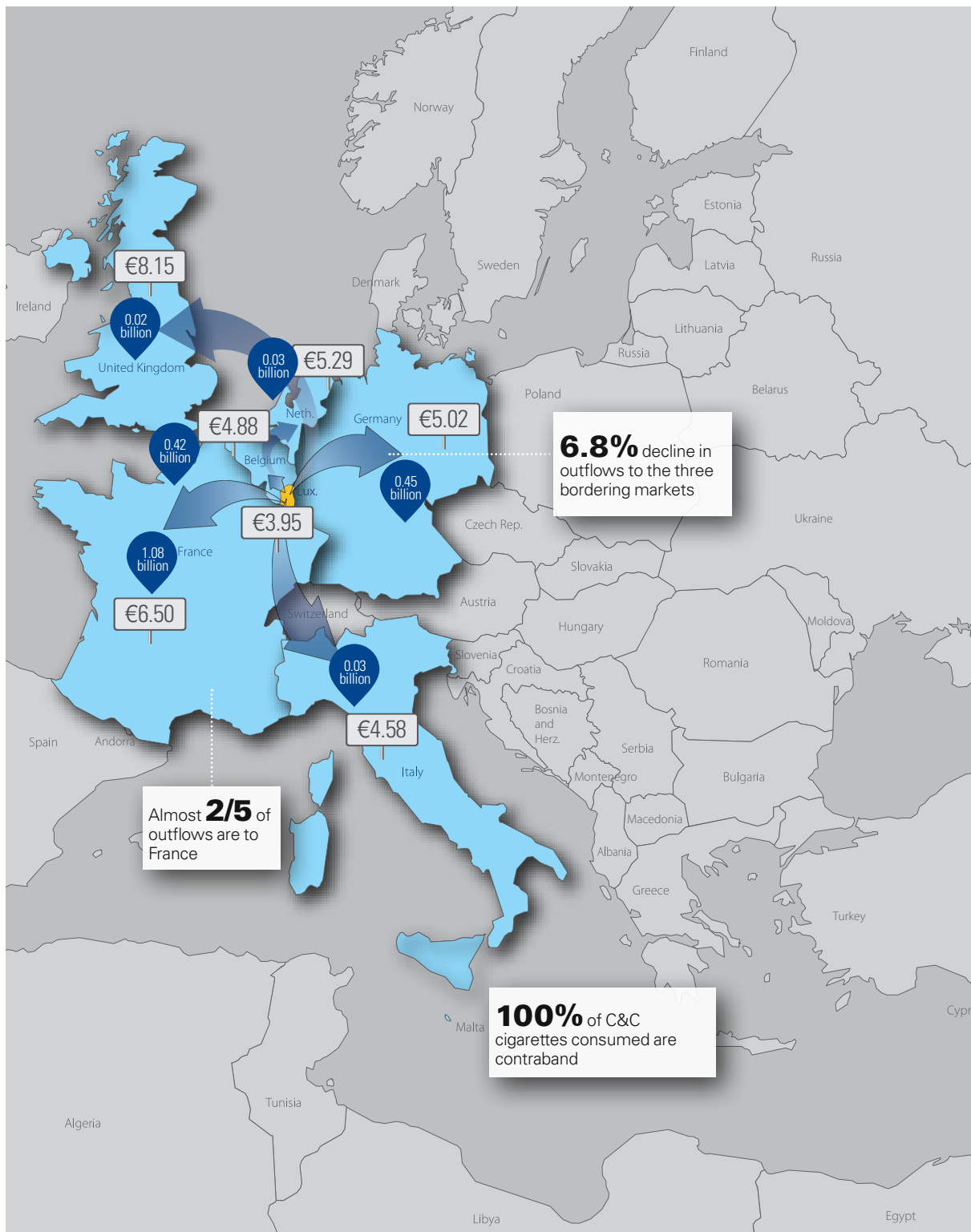


Manufactured cigarette consumption 2006-13



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KEY INFLOWS AND OUTFLOWS



LUXEMBOURG



PROJECT SUN

Main outflow

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.
 Source: (1) KPMG EU Flows Model.

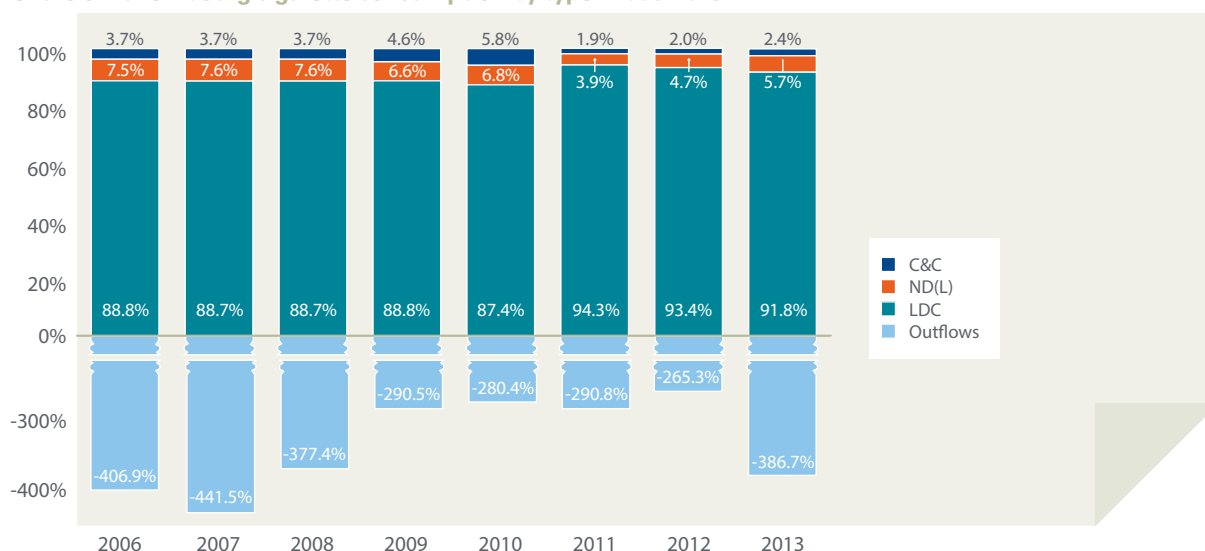
Luxembourg continued to be a predominantly outflow market

Project SUN has been conducted on a pan industry basis for the first time in 2013. This has provided access to previously unavailable data, which has allowed for the calculation of a specific cigarette smoking prevalence rate^{(3)(b)}, which has been used to estimate consumption in 2013. This suggests that prior year consumption may have been overstated.

Total manufactured cigarette consumption – Luxembourg⁽¹⁾⁽²⁾⁽³⁾

TOTAL LUXEMBOURG CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	4.77	5.05	4.43	4.15	3.93	3.94	3.68	3.42	(7)%
Outflows	-3.92	-4.20	-3.59	-3.18	-3.00	-2.98	-2.72	-2.77	%
Legal domestic consumption (LDC)	0.85	0.84	0.84	0.97	0.93	0.96	0.96	0.66	(3)%
Non-domestic legal (ND(L))	0.07	0.07	0.07	0.07	0.07	0.04	0.05	0.04	(14)%
Counterfeit and contraband (C&C)	0.04	0.04	0.04	0.05	0.06	0.02	0.02	0.02	(13)%
Total non-domestic	0.11	0.11	0.11	0.12	0.13	0.06	0.07	0.06	(1)%
Total consumption	0.96	0.95	0.95	1.10	1.07	1.02	1.03	0.72	(30)%

Share of Luxembourg cigarette consumption by type - 2006-2013⁽¹⁾⁽²⁾



Luxembourg is a relatively unique market in comparison to the other EU states with outflows typically a multiple of total domestic consumption

- This is largely a result of the number of inbound cross-border commuters and border shoppers from the surrounding nations and (fiscal) tourists from further afield, the volume of which far outweighs the domestic population
- The scale of outflows is also driven by the relatively large manufactured cigarette price differentials (based on WAP) with neighbouring countries and other Western European markets

Consumption of manufactured cigarettes declined in Luxembourg in 2013

- This is likely in part the result of switching by consumers between tobacco products. OTP volumes have increased at a CAGR of 4.7% between 2006 and 2012 and represent a substantial part of combined LDS⁽⁴⁾
- A decline in LDS is set against a relatively positive economic and cigarette tax environment where:
 - GDP per capita increased by 3% against prior year⁽⁵⁾
 - There was only a marginal increase in the unemployment rate, which remains low comparative to many other European markets (5.9% in 2013)⁽⁵⁾
 - Cross-border commuters make up over half of the workforce in Luxembourg (mainly from France, Germany and Belgium) and have increased in recent years
 - Cigarette prices increased by 2.8% based on WAP in 2013⁽⁶⁾ mainly due to a relatively benign cigarette taxation environment

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section). (b) Prevalence rate calculated using the average manufactured cigarette incidence / OTP incidence ratio for Belgium and Germany.

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) 'Le Tabagisme au Luxembourg en 2013', Fondation Cancer. (4) European Commission releases for consumption of fine cut tobacco. (5) 2014 Economist Intelligence Unit. (6) EC Excise Duty tables (Part III – Manufactured Tobacco).

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Outflow volumes were almost four times greater than domestic consumption; flows to larger neighbouring markets account for this

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWS TO LUXEMBOURG									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
France	0.02	0.02	0.02	0.02	0.01	0.01	0.02	0.01	(41)%
Belgium	0.03	0.03	0.03	0.04	0.06	0.01	0.00	0.01	>100%
Germany	0.02	0.02	0.02	0.02	0.00	0.02	0.01	0.01	(8)%
Duty Free	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.00	(58)%
Counterfeit								0.00	n/a
Other	0.03	0.03	0.03	0.03	0.05	0.02	0.02	0.02	(25)%
Total inflows	0.11	0.11	0.11	0.12	0.13	0.06	0.07	0.06	(14)%

Although ND flows increased marginally as a percentage of total consumption, they remained very small in comparison to other flows

- With domestic prices below those in surrounding markets as well as a small population, inflows tend to be low
- Inflows mainly originate from neighbouring markets and are likely the result of general travel between these countries
- Duty Free flows into Luxembourg declined this year. There were no Illicit Whites packs with Duty Free labelling found in the EPS. This is discussed further on page 205
- 'Other' inflows included volumes from Russia, Italy and Spain.

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM LUXEMBOURG									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
France	1.00	0.95	0.86	0.58	0.52	0.73	1.11	1.08	(3)%
Germany	0.35	0.38	0.44	0.80	0.38	0.41	0.46	0.45	(3)%
Belgium	0.47	0.25	0.31	0.12	0.23	0.47	0.51	0.42	(18)%
Netherlands	0.10	0.07	0.00	0.01	0.02	0.08	0.05	0.03	(38)%
Italy	0.00	0.00	0.00	0.00	0.01	0.00	0.02	0.03	57%
UK	0.00	0.29	0.00	0.01	0.00	0.01	0.02	0.02	10%
Other	2.00	2.28	1.97	1.66	1.83	1.29	0.54	0.74	35%
Total outflows	3.92	4.20	3.59	3.18	3.00	2.98	2.72	2.77	2%

Outflows increased marginally during the year, which may be in part due to the continued low prices for manufactured cigarettes in Luxembourg

- Outflows to some neighbouring markets declined. This may be because the 'package' of goods from Luxembourg is less cheap than in 2012, evidenced by lower diesel and petrol price differentials with Belgium, France, Germany and the Netherlands⁽²⁾
- Luxembourg also experienced higher general inflation than Belgium, France and Germany in 2013⁽³⁾ - This is likely to have impacted the number of border shopping trips and hence cigarette outflows
- OTP incidence in markets such as Belgium and the Netherlands has been on an upwards trend and these products may have been considered as an alternative to cheap cigarettes from Luxembourg

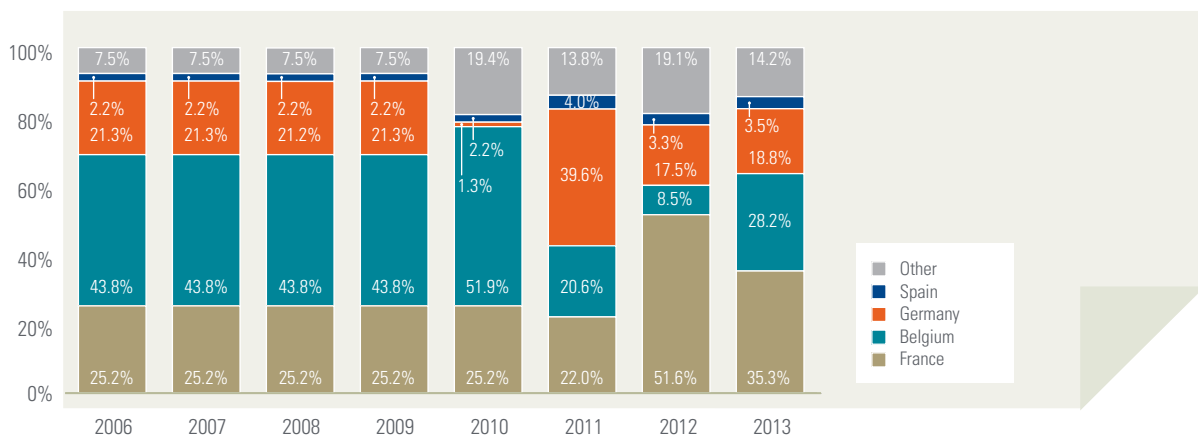
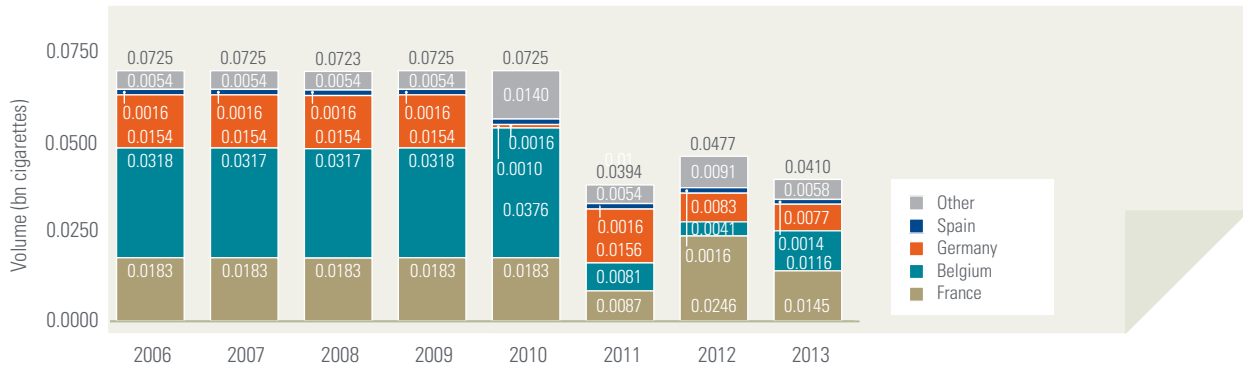
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Source: (1) KPMG EU Flows Model. (2) Euromonitor, downloaded May 2014. (3) Eurostat.



Legal inflows originate mainly from more expensive neighbouring markets and are low as a share of consumption

ND(L) by origin - 2006-2013^{(1)(2)(a)(b)}



LUXEMBOURG



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Non-domestic legal(ND(L)) inflows declined marginally this year mainly due to lower volumes from France

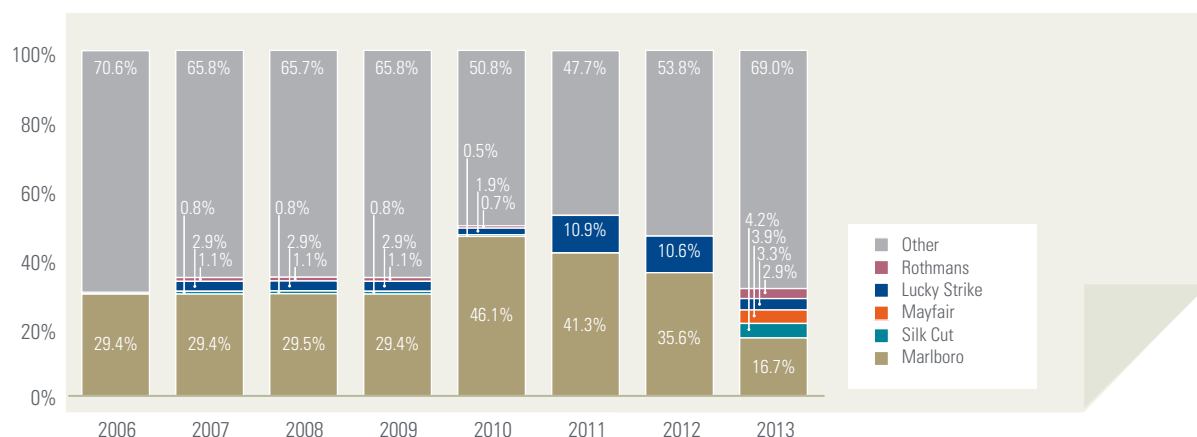
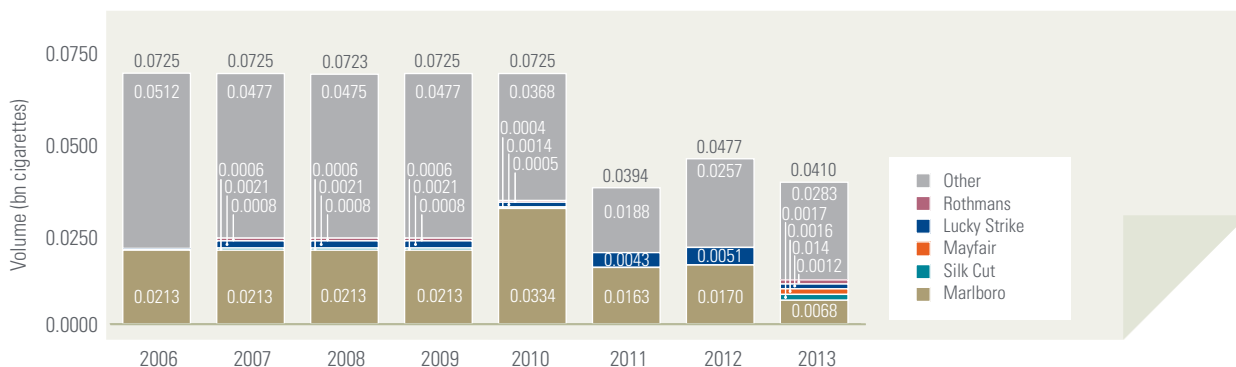
- Flows from more expensive markets such as France, Belgium and Germany were allocated entirely to ND(L) consumption
- There was a decline in French, German and Spanish origin packs whilst those from Belgium had increased incidence
 - These movements are very small in absolute terms and align with fairly consistent outbound tourist flows to these nations
- The decline in legal inflows from France may be explained by the price of a 'package' of goods in Luxembourg increasing this year, impacting border shopper numbers

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013^{(1)(2)(a)}



The brand split of legal inflows to Luxembourg continued to be spread across a wide range of brands

- Marlboro continues to be the most popular brand despite inflow volumes more than halving during 2013
- Lucky Strike volumes have fallen due to fewer French inflows

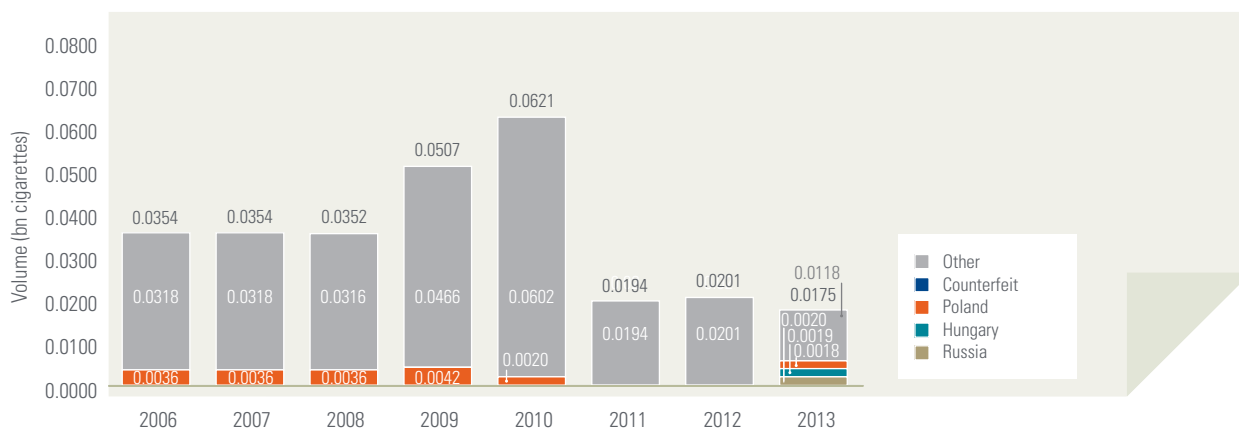
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



Counterfeit and contraband inflows to Luxembourg were stable and represented only a small share of total consumption

Total C&C by origin - 2006-2013^{(1)(2)(3)(a)}



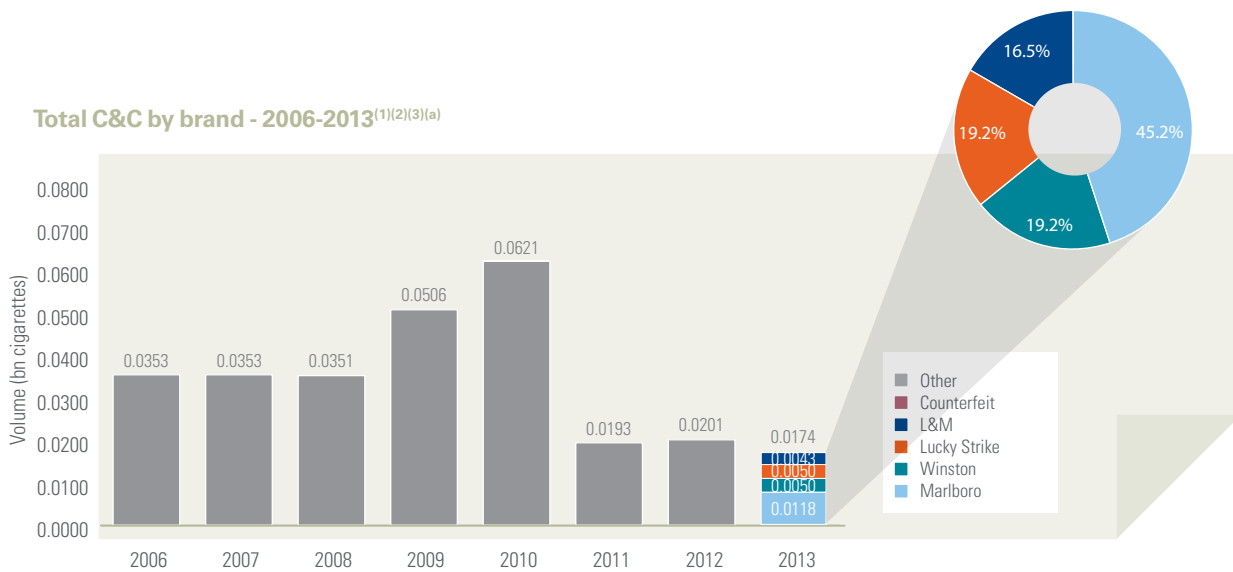
Counterfeit and contraband(C&C) volumes remained stable in 2013 and remain low as a share of total consumption

- There were no counterfeit cigarettes collected during the empty pack survey suggesting that counterfeit cigarettes are not an issue in Luxembourg
- If these C&C cigarettes had been legally purchased in Luxembourg the tax revenue gained would have been approximately €2.4m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-2012, UN WTO.

C&C INFLOWS BY BRAND



Small C&C inflows of legitimate brands arise from markets such as Ukraine, Kosovo and some Duty Free flows

- The majority of C&C brands in Luxembourg are contraband inflows

Composition of Illicit Whites inflows – 2007-2013^{(1)(3)(b)}

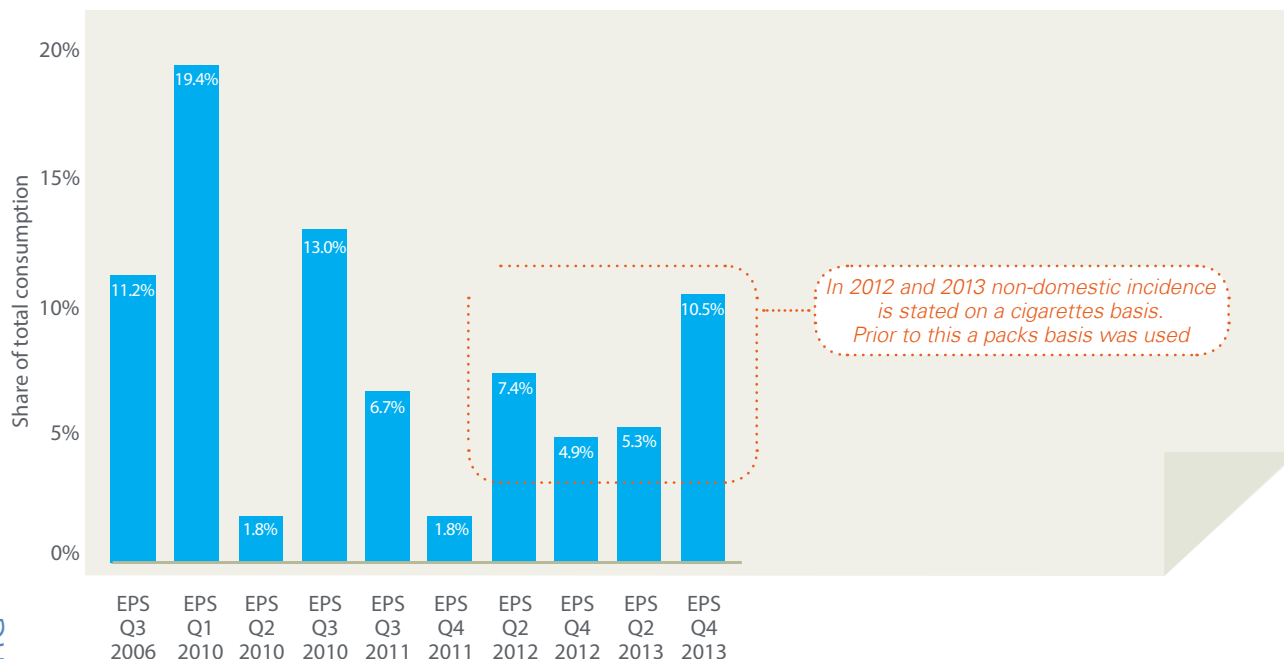
LABELLING OF ILLICIT WHITES INFLOWS TO LUXEMBOURG								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.00	0.00	0.00	0.00	0.00	0.00	0.00	(100)%
Duty Free	0.00	0.00	0.00	0.00	0.00	0.00	0.00	n/a
Unspecified	0.00	0.00	0.00	0.00	0.00	0.00	0.00	(100)%
Total Illicit Whites	0.01	0.01	0.01	0.00	0.00	0.01	0.00	(100)%

- There were no Illicit Whites flows identified in 2013

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

EPS results & EU Flow model

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾

LUXEMBOURG



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- The empty pack survey (EPS) in Luxembourg collected 400 packs during the course of the year. This was undertaken as two waves, one in Q2 (May) and one in Q4 (November). Each wave collected 200 packs across 2 cities and the number of packs collected in each city is weighted by the city population
- Analysis of the EPS results highlighted that each city's share of the sample did not tie with its share of the total population of Luxembourg. The results were re-weighted in our analysis to help ensure the non-domestic incidence across the population of both cities was more accurately reflected. This marginally increased non-domestic incidence from 7.9% to 8.1%

Estimation of consumption

- The nature of the manufactured cigarette market in Luxembourg, characterised by large outflows and a relatively small domestic market, makes the exact measurement of domestic consumption a challenge
- The estimation of outflows from Luxembourg requires the measurement of flows from Luxembourg into all other markets. These inflows are very difficult to accurately measure as they are likely to be quite concentrated geographically within markets and are also small relative to the overall domestic market of the destination country. Consequently, this approach is likely to underestimate the volume of flows out of Luxembourg and hence overstate domestic consumption
- Smoking consumer survey data is used in our analysis to adjust the estimation of consumption by calculating a balancing figure for outflows
 - Domestic consumption by residents, cross border commuters and international tourists is estimated using data points such as incidence rates, daily smoker percentages and average cigarettes consumed per day in order to estimate total consumption for Luxembourg
 - The equivalent calculation is then performed for Belgium and the resulting consumption figure compared to that derived from the EU flows model
 - An uplift for under-reporting is then applied to give an adjusted estimate for total consumption. A balancing outflow figure is used to achieve this, which reflects the difficulty in estimating outflows from Luxembourg
 - This implies total consumption of 0.72bn cigarettes in 2013, 30.3% lower than prior year

Source: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

ND(L) volumes calculations and explanations

KPMG non domestic legal flows Luxembourg

COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 ⁽¹⁾ (bn sticks)	2013 ND(L) (bn sticks)	% of ND
France	0.01	0.01	100%
Belgium	0.01	0.01	100%
Germany	0.01	0.01	100%

- Consumer research formed the basis of the calculation for the legal component of most of the inflows. In the case of the three inflows however shown above, all non-domestic flows are assumed to be legal as they are all higher priced markets



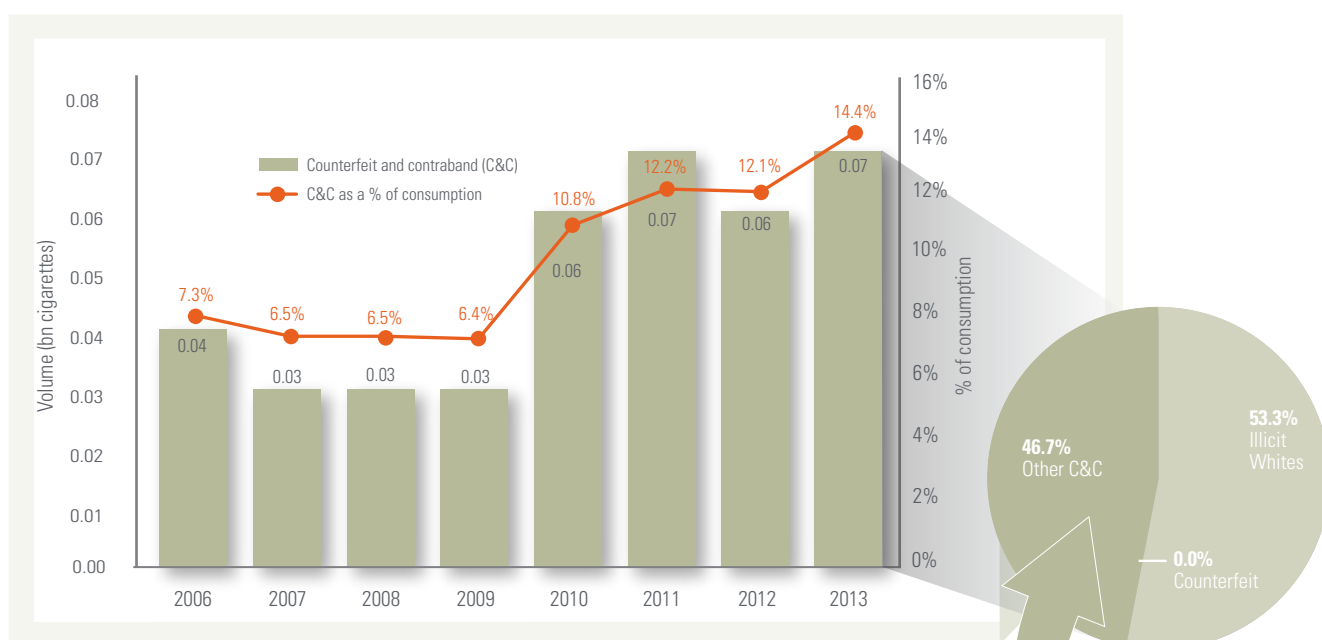
Notes: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Source: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

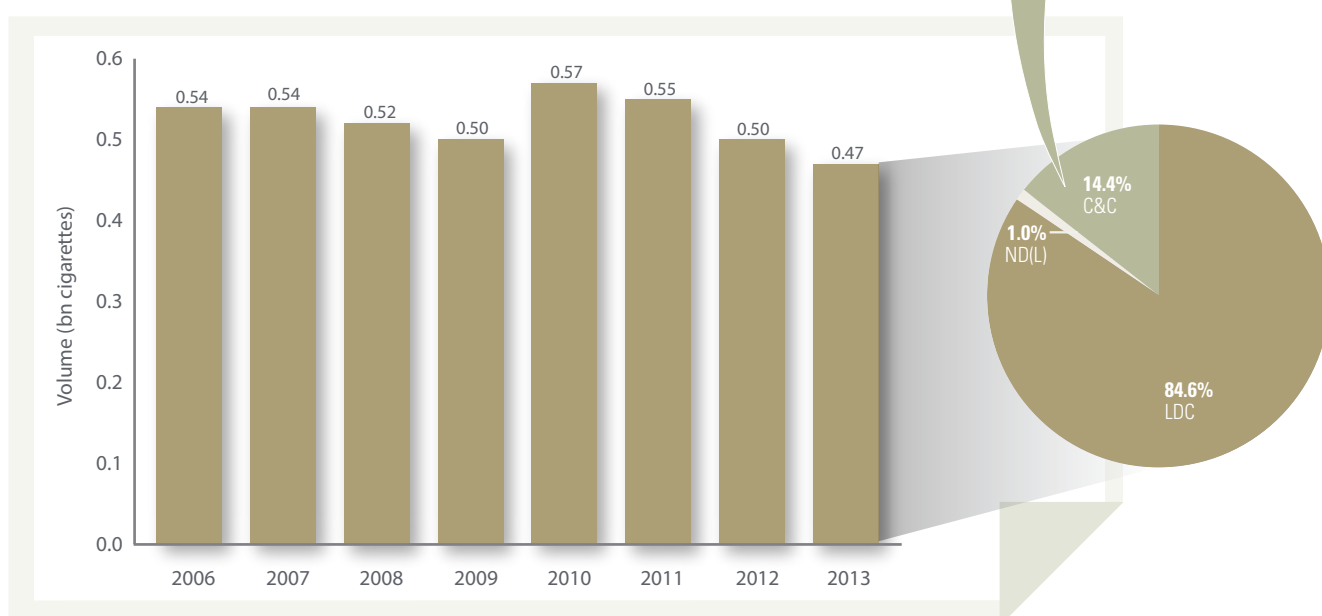


Counterfeit & Contraband grew, whilst overall consumption declined

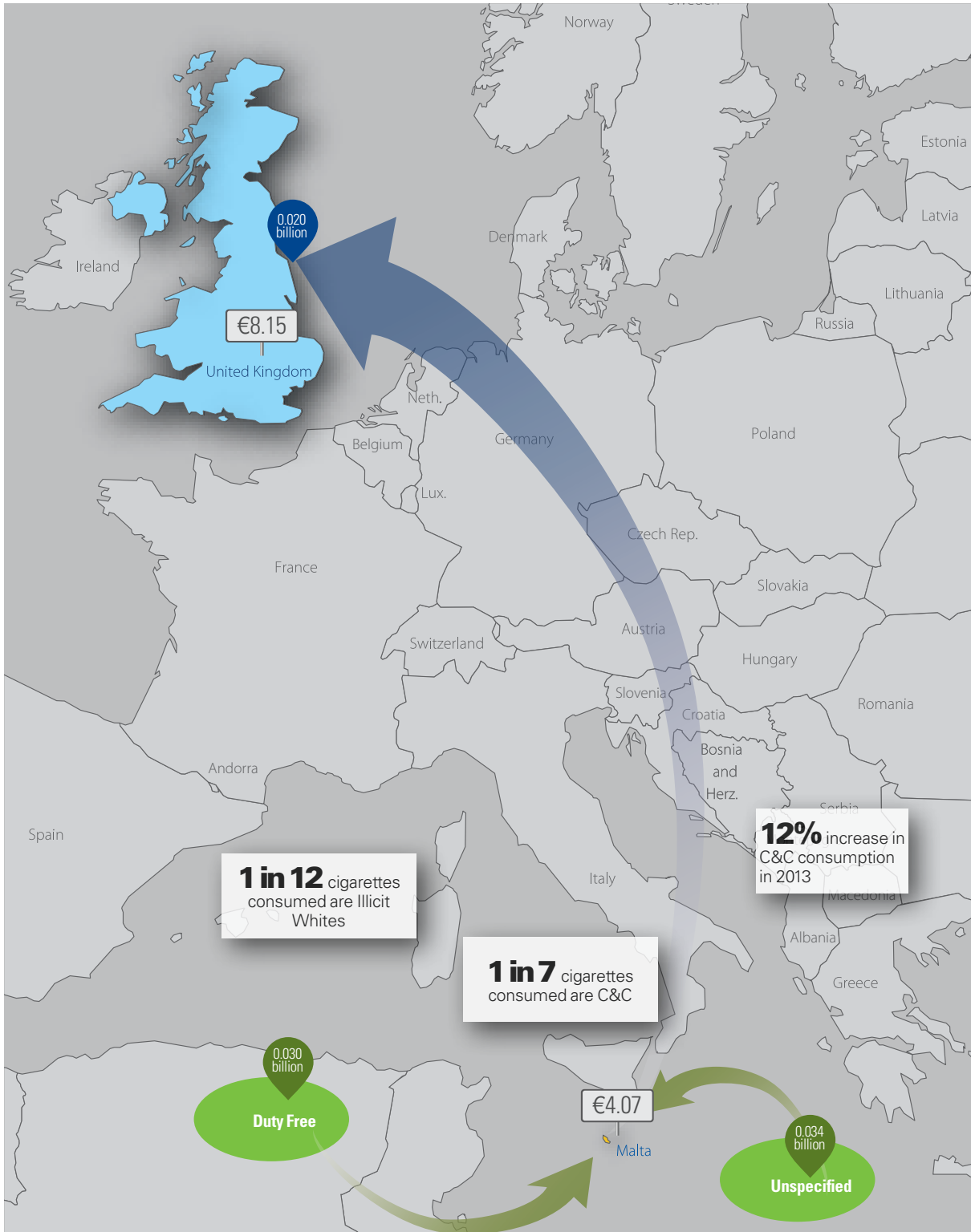
Manufactured cigarette C&C volumes and share of overall consumption 2006-13



Manufactured cigarette consumption 2006-13



KEY INFLOWS AND OUTFLOWS



Main outflow █
 Main inflow █

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

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MALTA

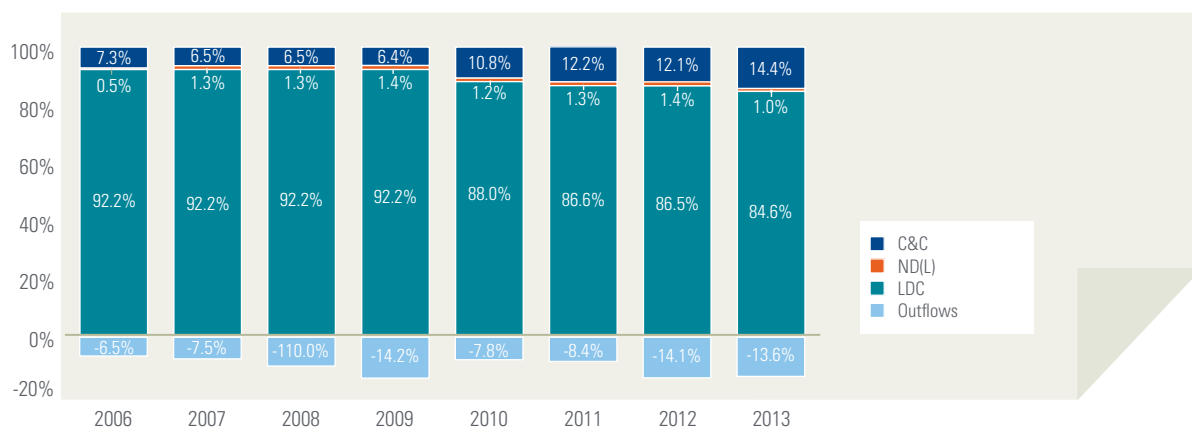
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Overall consumption declined but C&C slightly increased

Total manufactured cigarette consumption – Malta^{(1)(2)(a)}

TOTAL MALTA CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	0.535	0.535	0.535	0.529	0.550	0.520	0.505	0.463	(8)%
Outflows	-0.035	-0.040	-0.052	-0.070	-0.044	-0.046	-0.071	-0.064	(9)%
Legal domestic consumption (LDC)	0.500	0.495	0.482	0.458	0.505	0.474	0.434	0.399	(8)%
Non-domestic legal (ND(L))	0.003	0.007	0.007	0.007	0.007	0.007	0.007	0.005	(33)%
Counterfeit and contraband (C&C)	0.040	0.035	0.034	0.032	0.062	0.067	0.061	0.068	12%
Total consumption	0.542	0.536	0.523	0.497	0.574	0.547	0.502	0.472	(6)%

Share of Malta cigarette consumption by type 2006-2013⁽¹⁾⁽²⁾



Overall consumption decreased by 6% in 2013 as the decline in legal domestic consumption was only partly offset by an increase in non-domestic consumption

- The decline in legal domestic sales (LDS) may have been impacted by a 7% increase in specific excise from € 77 to €82.50 per 1,000 cigarettes. The WAP of a pack of cigarettes however decreased by 1.6%⁽³⁾
- The vulnerability of the Maltese economy to external shocks in Europe may also have had an adverse impact on legal sales as unemployment rose to 6.5%⁽⁵⁾

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Source: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) EC Excise Duty tables (Part III – Manufactured Tobacco) as at January 2013/January 2014. (4) Euromonitor Passport. (5) The Economist Intelligence Unit.

The two main inflow sources remained unspecified and Duty Free

Total inflows by country of origin 2006-2013^{(1)(a)}

Illicit Whites made up 23% of Duty Free inflows

ND INFLOWSTO MALTA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Unspecified	0.000	0.000	0.000	0.000	0.022	0.028	0.041	0.034	(16)%
Duty Free	0.030	0.030	0.029	0.027	0.034	0.032	0.021	0.030	48%
Italy	0.005	0.005	0.005	0.004	0.001	0.001	0.001	0.002	75%
Bulgaria	0.000	0.000	0.000	0.000	0.001	0.000	0.000	0.001	>100%
Russia	0.002	0.002	0.002	0.002	0.000	0.002	0.000	0.001	88%
Counterfeit								0.000	n/a
Other	0.005	0.005	0.005	0.005	0.010	0.010	0.004	0.004	2%
Total inflows	0.042	0.042	0.041	0.039	0.069	0.074	0.068	0.073	7%

Total non-domestic inflows increased this year both in volume terms and as a share of consumption

- The majority of non-domestic cigarettes were Duty Free or Unspecified cigarettes, accounting for approximately 90% of total non-domestic flows. The main Duty Free brands included Marlboro, L&M and Portman

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM MALTA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
UK	0.027	0.027	0.044	0.039	0.035	0.037	0.051	0.020	(61)%
Netherlands	0.004	0.004	0.000	0.004	0.000	0.006	0.002	0.011	>100%
France	0.000	0.000	0.007	0.020	0.007	0.000	0.000	0.010	n/a
Belgium	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.008	n/a
Germany	0.000	0.000	0.000	0.000	0.000	0.000	0.005	0.005	9%
Italy	0.000	0.010	0.000	0.005	0.000	0.000	0.009	0.004	(56)%
Other	0.004	0.000	0.001	0.003	0.003	0.002	0.003	0.006	81%
Total outflows	0.035	0.040	0.053	0.071	0.045	0.046	0.071	0.064	(9)%

Total outflows decreased by 9% in 2013 as flows to the UK reduced

- Outflows to the UK, a higher priced market which was mainly accounted for by tourist flows, reduced by 61%
- This was partially offset by increased outflows to the Netherlands and France

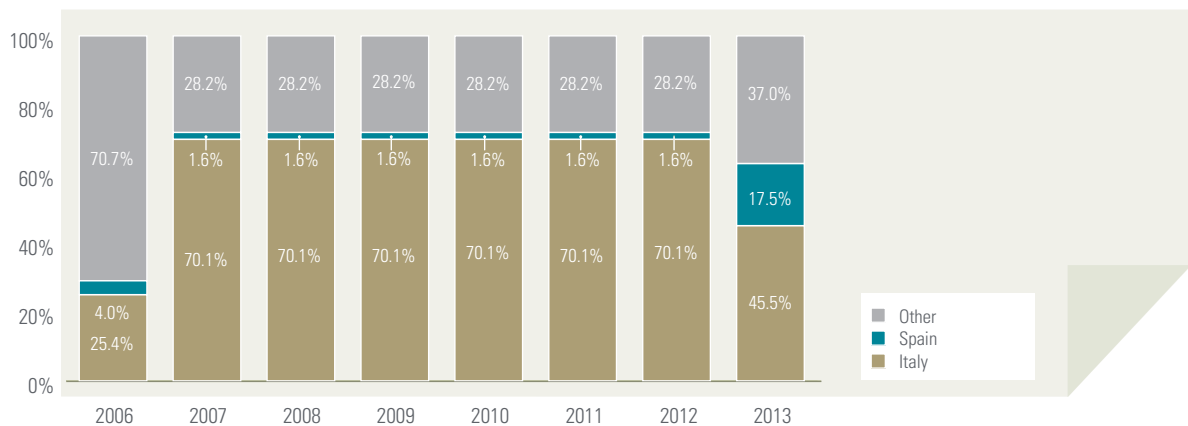
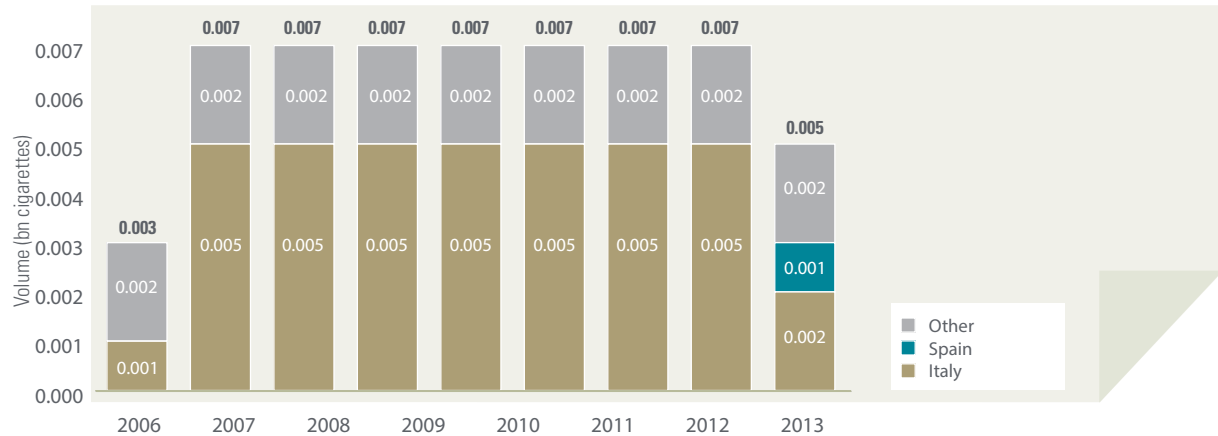
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Source: (1) KPMG EU Flows Model.



ND(L) volumes remained low, showing a declining trend

ND(L) by origin - 2006-2013^{(1)(2)(a)(b)}



ND(L) volumes reduced due predominantly to a decline of inflows from Italy, partially offset by a small increase in inflows from Spain

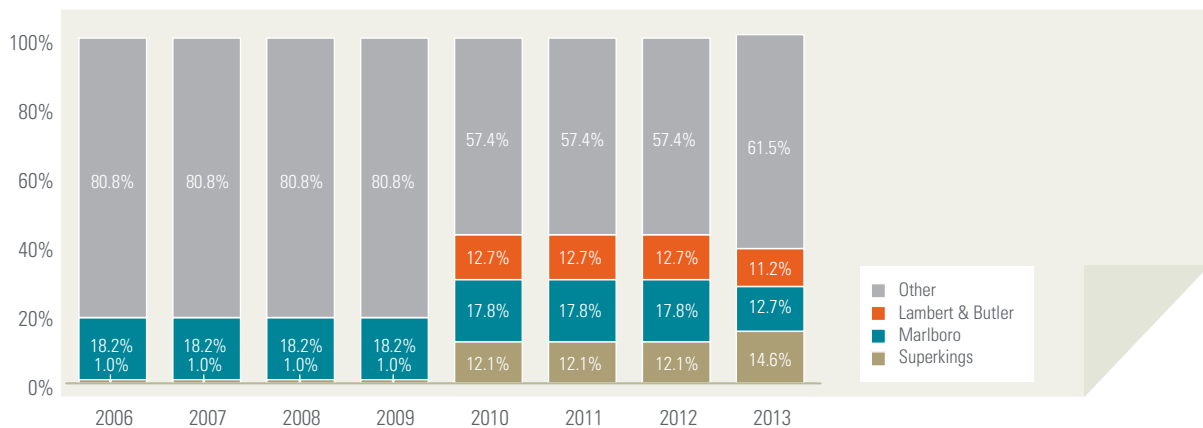
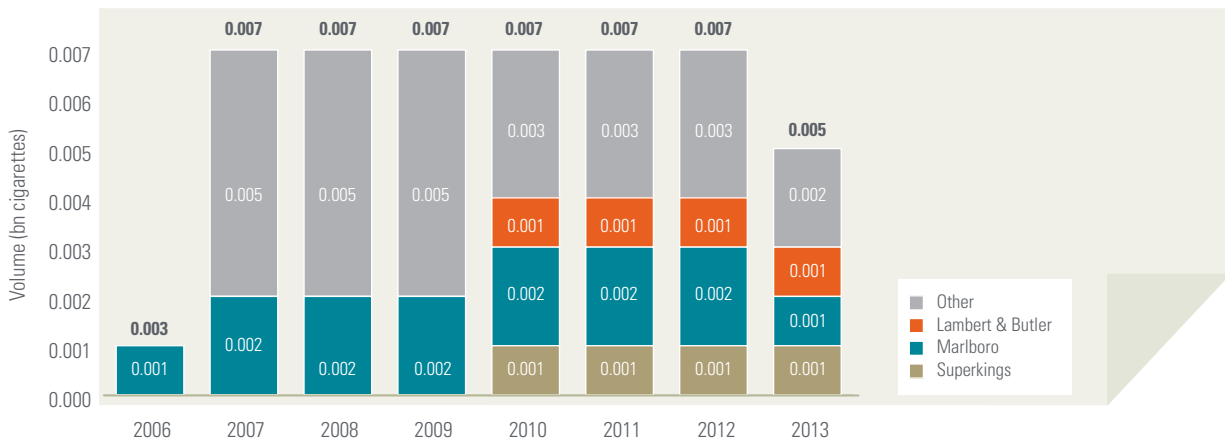
- The WAP price difference between Italy and Malta was generally low at €0.49 in 2013⁽³⁾. All inflows were therefore categorised as ND(L) consumption
- The decline in Italian inflows was likely to have been impacted by fewer trips to Italy reported in the consumer and travel research in 2013, as well as fewer packs originating from Italy picked up in the EPS survey
- ND(L) flows continued to form only a small part of total non-domestic flows, accounting for approximately 7%

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) EC Excise Duty tables (Part III – Manufactured Tobacco) as at January 2013/ January 2014.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

Total ND(L) by brand 2006-2013^{(1)(2)(a)}



The increase in ND(L) inflows was relatively consistent amongst the brands with highest non-domestic incidence

- Superkings, Marlboro and Lambert & Butler together account for 60% of total ND(L) inflows
- “Other” legal inflows consist of smaller volumes of approximately 40 other brands

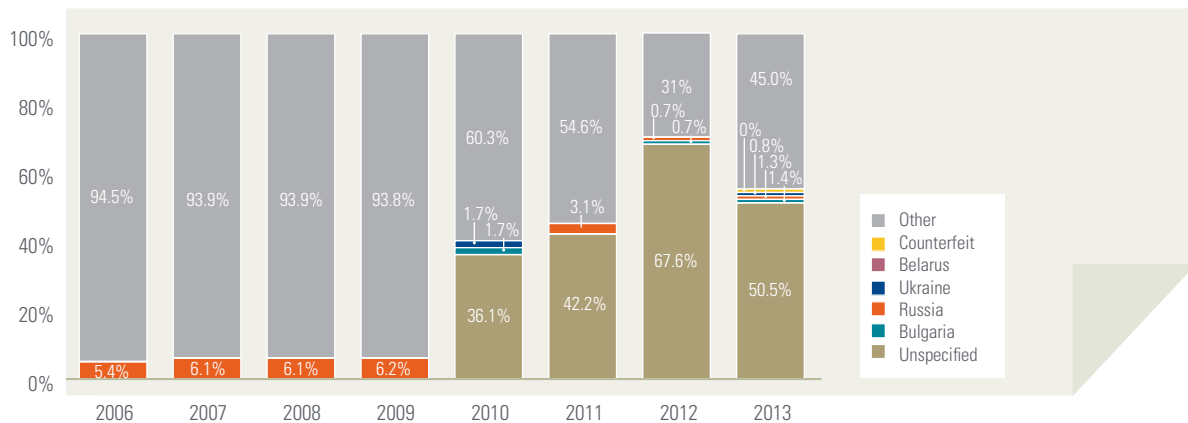
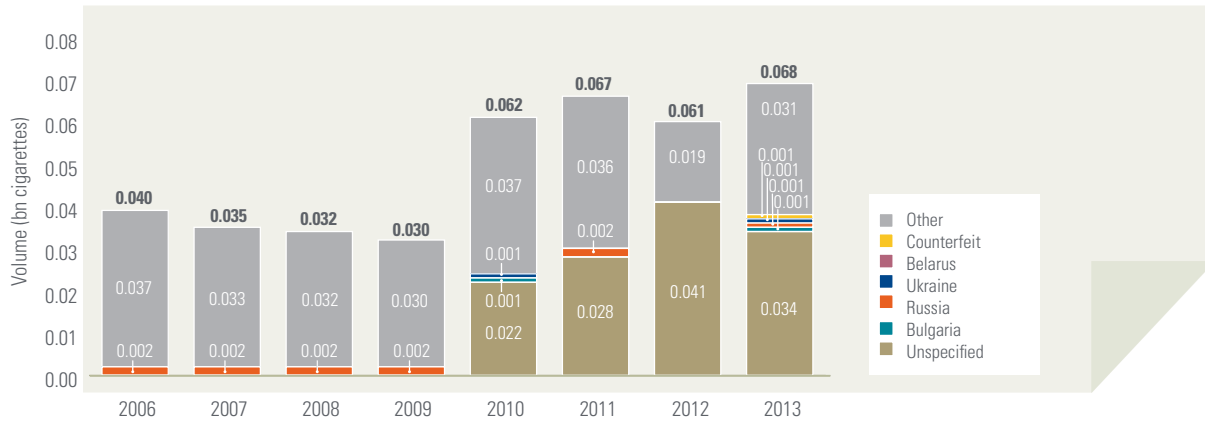
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



C&C volumes increased slightly, driven by an increase in volumes from Eastern Europe

Total C&C by origin 2006-2013^{(1)(2)(a)}



Unspecified cigarettes accounted for 50% of C&C flows, while Bulgaria and Russia were the main source countries for contraband cigarettes

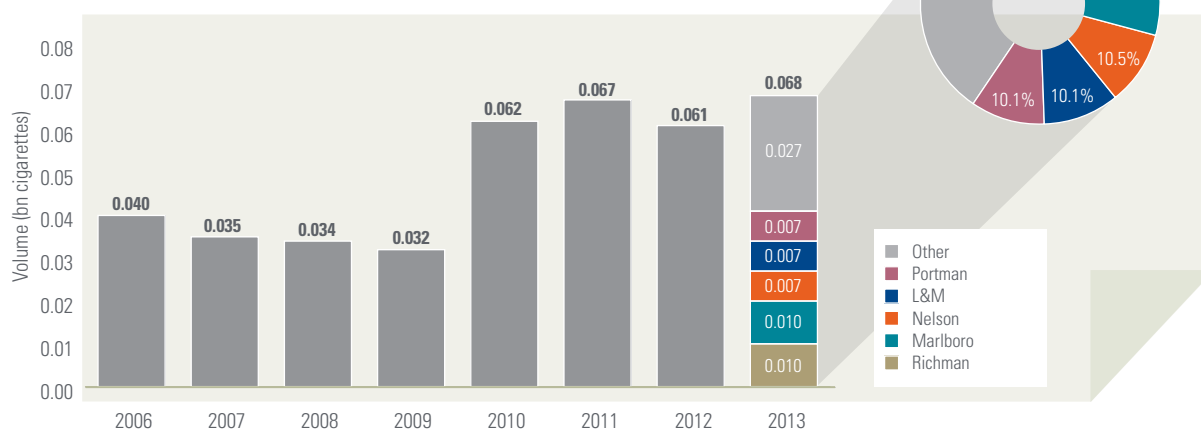
- No trips to Eastern European countries such as Bulgaria, Russia, Ukraine and Belarus were reported in the consumer research, thus all inflows were categorised as C&C
- The sharp growth in inflows from these countries was likely due to relatively large WAP differences that existed with Malta, ranging from €1.69 with Bulgaria to €3.43 with Belarus (per pack of 20 cigarettes)⁽³⁾

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) C Excise Duty tables (Part III – Manufactured Tobacco) as at January 2013/ January 2014.

C&C INFLOWS BY BRAND

Total C&C by brand - 2006-2013^{(1)(2)(a)}



Breakdown of Illicit Whites by type 2007-2013^{(1)(2)(a)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO MALTA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country Specific	0.000	0.000	0.000	0.002	0.002	0.001	0.001	(28)%
Duty Free	0.000	0.000	0.000	0.000	0.000	0.003	0.007	>100%
Unspecified	0.000	0.000	0.000	0.017	0.017	0.034	0.028	(16)%
Total Illicit Whites	0.005	0.005	0.004	0.019	0.019	0.038	0.036	(5)%

Contraband and Illicit Whites flows accounted for all of the C&C consumption in Malta; no counterfeit cigarettes were identified within the EPS

- The largest contraband brand was Richman, followed by Marlboro
- If the total volume of C&C had been consumed legally within Malta, an additional tax revenue of approximately €11 million would have been raised by the Maltese Treasury

Consumption of Illicit Whites brands was broadly constant in 2013

- The marginal decline in overall Illicit Whites consumption was likely to have been driven by a decrease in Illicit Whites with unspecified labelling
- American Legend inflows declined by over 50%, although this was offset by growth in emerging brands such as Nelson and Portman
- Within Illicit Whites with Duty Free labelling, the majority of inflows were Portman

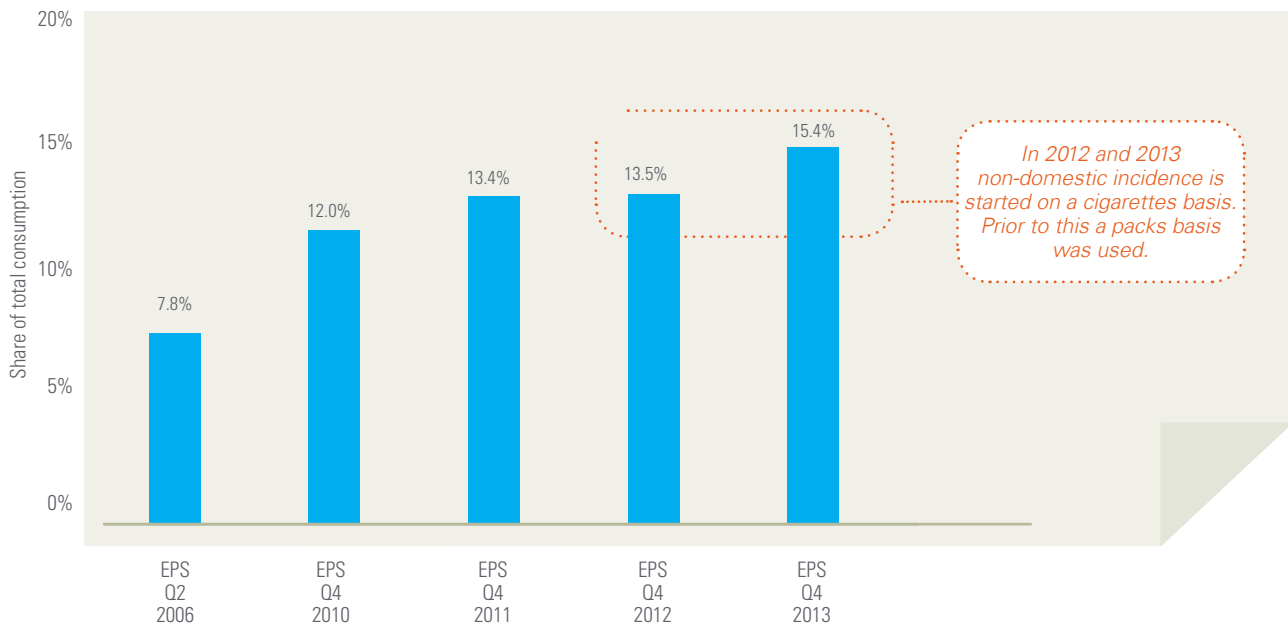
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows; (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



EPS non domestic estimates

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



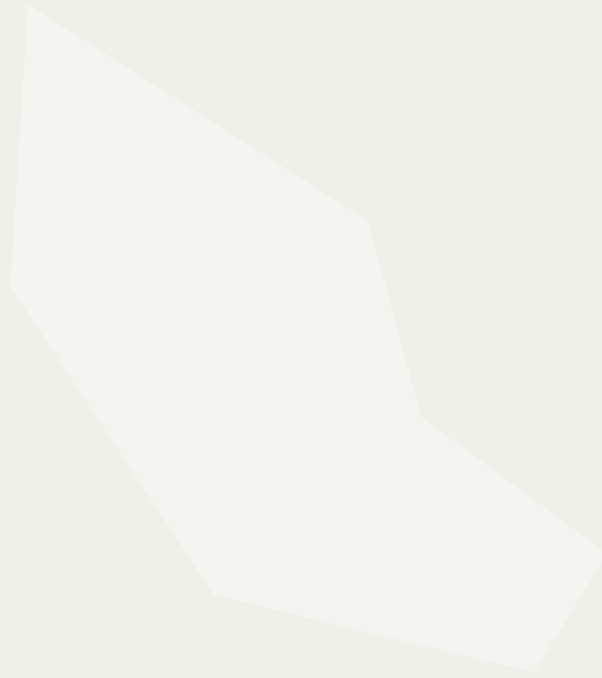
- The empty pack survey in Malta collected 1,000 packs during the course of the year. This was undertaken in 1 wave conducted in Q4 (October- November)
- The sample focused on the largest 8 cities in Malta. The number of packs collected in each city is weighted by the city population
- No adjustments were made to the data in our analysis

MALTA



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Sources: (1) MSIIntelligence, 2006 – 2013.



MALTA



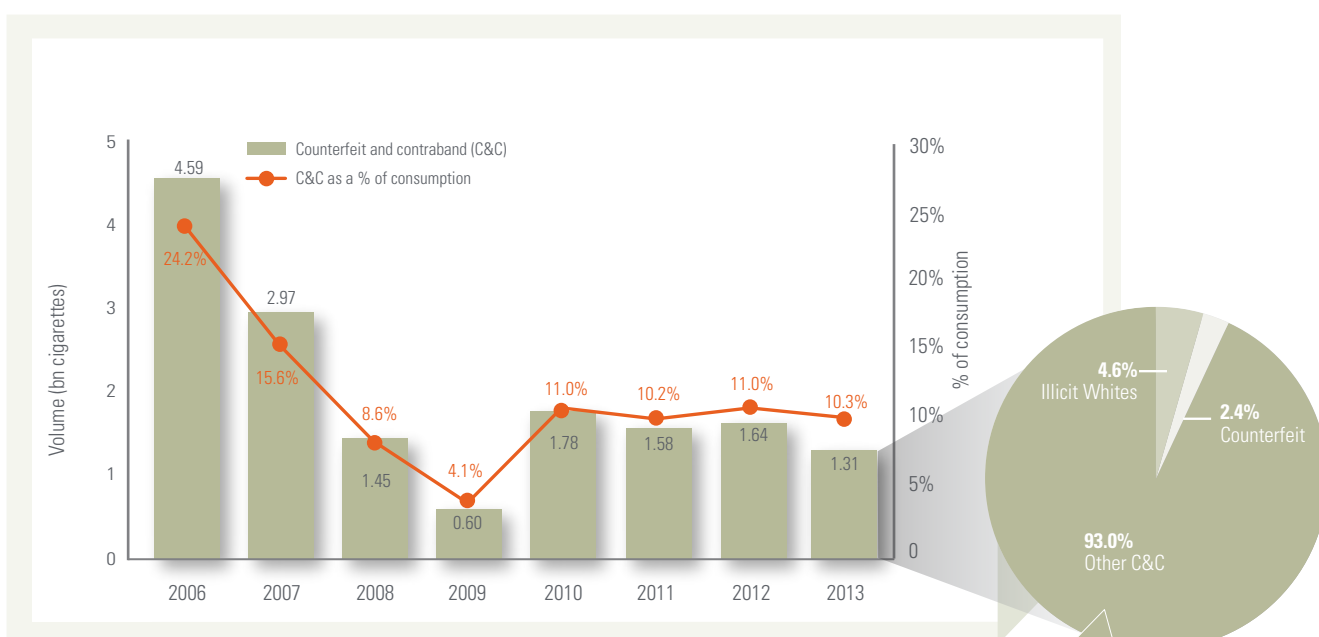
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Counterfeit and Contraband volumes declined to less than half of Non-Domestic inflows

Manufactured cigarette C&C volumes and share of overall consumption 2006-13

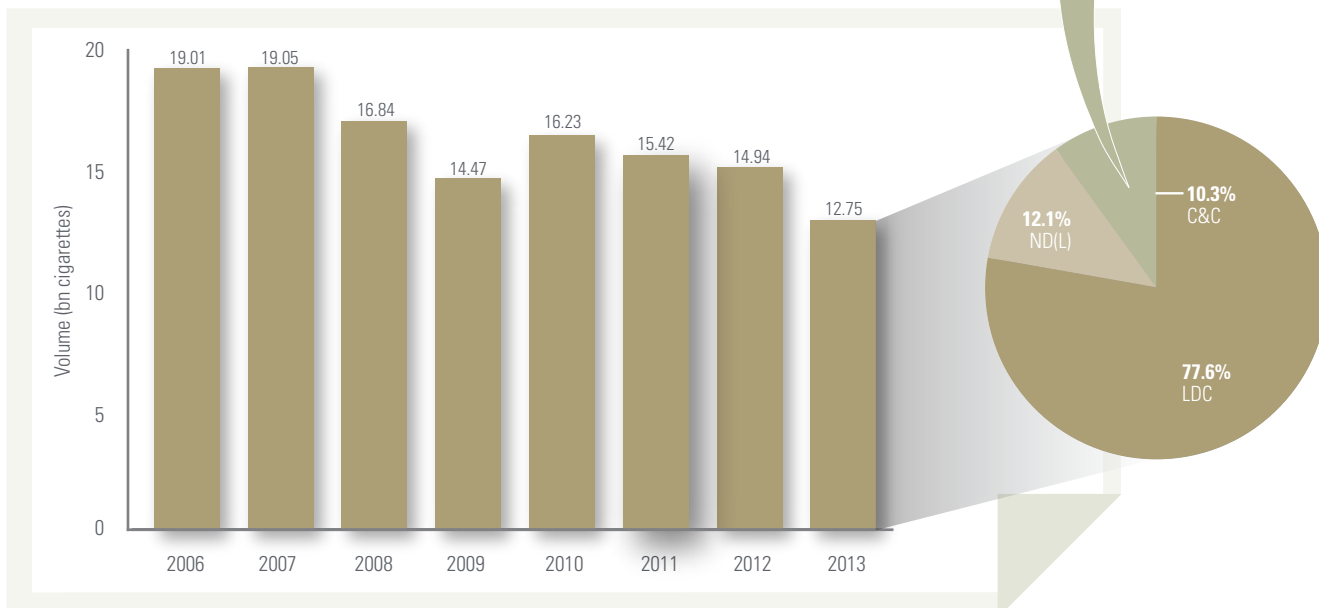


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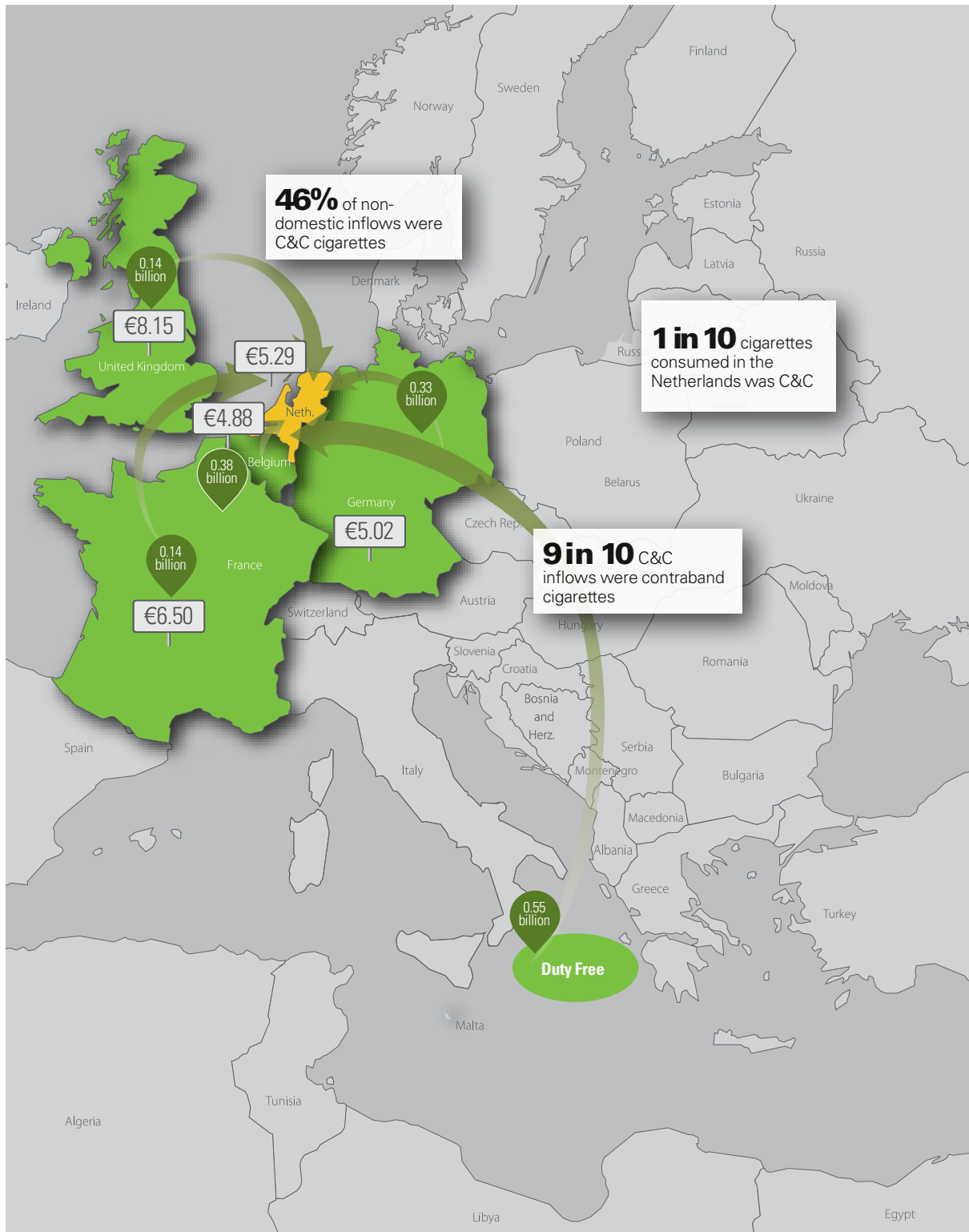



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Manufactured cigarette consumption 2006-13



KEY INFLOWS AND OUTFLOWS



Main outflow 

 Main inflow 

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

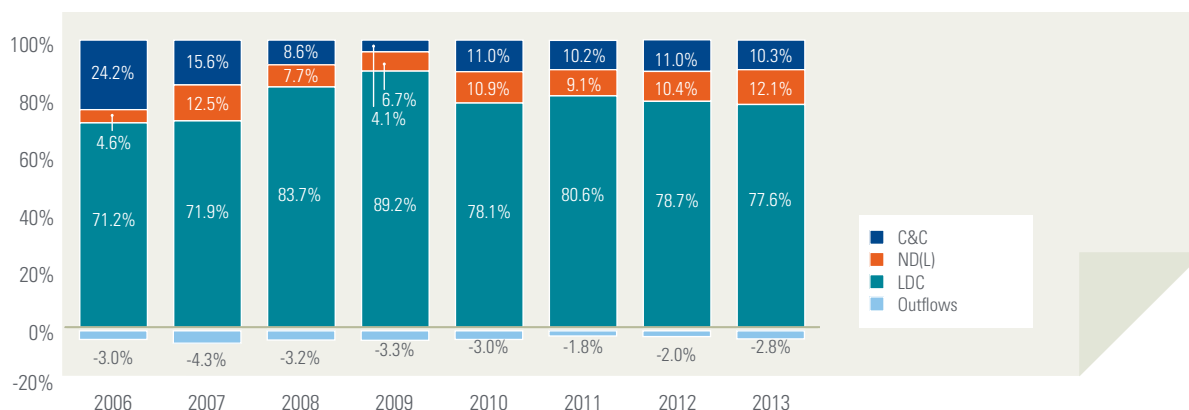
MANUFACTURED CIGARETTE CONSUMPTION

Cigarette consumption has continued to decline, reflected in a fall in both legal domestic and non-domestic consumption

Total manufactured cigarette consumption – Netherlands^{(1)(2)(a)}

TOTAL NETHERLANDS CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	14.11	14.51	14.62	13.39	13.16	12.71	12.05	10.25	(15)%
Outflows	-0.57	-0.82	-0.53	-0.48	-0.49	-0.27	-0.29	-0.36	21%
Legal domestic consumption (LDC)	13.54	13.69	14.09	12.91	12.67	12.44	11.75	9.89	(16)%
Non-domestic legal (ND(L))	0.87	2.38	1.30	0.97	1.77	1.41	1.55	1.54	(0)%
Counterfeit and contraband (C&C)	4.59	2.97	1.45	0.60	1.78	1.58	1.64	1.31	(20)%
Total non-domestic	5.46	5.36	2.75	1.56	3.55	2.98	3.19	2.85	(11)%
Total consumption	19.01	19.05	16.84	14.47	16.23	15.42	14.94	12.75	(15)%

Share of Netherlands cigarette consumption by type - 2006-2013⁽¹⁾⁽²⁾



Total consumption of manufactured cigarettes declined by 14.7% in 2013, with legal domestic sales (LDS) declining at a similar rate

- Although there are some signs of economic stabilisation, other indicators highlight the ongoing difficult economic backdrop in the Netherlands which may have impacted sales
- GDP per capita improved marginally this year whilst PDI per capita remained steady⁽³⁾. Unemployment continued to increase, rising from 5.3% to 6.7%⁽⁴⁾. This is still relatively low however, in comparison to many other EU markets
- Changes to the taxation and regulatory environment for cigarettes will have also impacted sales and consumption
- In January 2013, specific excise taxation was increased from €135.66 per 1,000 cigarettes to €167.84⁽⁵⁾. This contributed to a WAP increase of 5.1% in the year from €5.03 per 20 cigarettes to €5.29⁽⁴⁾ and a widening price differential with bordering nations
 - LDS declines have been more pronounced along the borders as compared to the country average
- OTP continue to represent a significant share of total legal tobacco sales though volumes and share have declined over this period⁽⁶⁾

Notes: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Euromonitor, downloaded January 2014. (4) 2014 Economist Intelligence Unit. (5) EC Excise Duty tables (Part III – Manufactured Tobacco). (6) European Commission releases for consumption of fine cut tobacco.

Non-domestic inflows have grown as a percentage of consumption whilst outflows from the Netherlands remained low

Total inflows by country of origin - 2006-2013 ^{(1)(a)}

ND INFLOWS TO NETHERLANDS									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	0.83	0.80	0.45	0.38	0.59	0.59	0.66	0.55	(16)%
Belgium	0.54	0.73	0.13	0.15	0.24	0.29	0.32	0.38	18%
Germany	0.45	0.29	0.20	0.13	0.35	0.25	0.33	0.33	1%
UK	0.20	0.25	0.15	0.11	0.20	0.14	0.15	0.14	(2)%
France	0.37	0.35	0.12	0.08	0.35	0.13	0.16	0.14	(14)%
Counterfeit								0.03	n/a
Other	3.07	2.93	1.70	0.71	1.83	1.58	1.58	1.28	(19)%
Total inflows	5.46	5.36	2.75	1.56	3.55	2.98	3.19	2.85	(11)%

Inflows grew as a share of consumption, which may have been influenced by price increases ahead of bordering markets

- Inflows of manufactured cigarettes declined by 10.5% to 2.85bn cigarettes in 2013, but grew as a percentage of total consumption. The decline in absolute terms is likely to be the result of lower cigarette incidence, whilst those still smoking manufactured cigarettes seem increasingly likely to choose non-domestic products
- Duty free inflows declined in 2013. Historically, Illicit Whites labelled as Duty Free have represented a very small share of total Duty Free volumes and this year only Monus, Ronhill and Yun Yan brands were picked up during the Empty Pack Survey (EPS)
- The decline in Duty Free was almost entirely due to Other Duty Free volumes
- 'Other' inflows included Italy (0.13bn), Russia (0.13bn), Poland (0.09bn) and Spain (0.07bn)

Total outflows by destination country - 2006-2013 ⁽¹⁾

OUTFLOWS FROM NETHERLANDS									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Belgium	0.09	0.05	0.02	0.11	0.13	0.06	0.04	0.17	>100%
France	0.14	0.26	0.08	0.14	0.09	0.08	0.07	0.07	8%
Germany	0.18	0.16	0.20	0.13	0.14	0.07	0.06	0.03	(53)%
Other	0.16	0.35	0.23	0.10	0.13	0.06	0.12	0.08	(33)%
Total outflows	0.57	0.82	0.53	0.48	0.49	0.27	0.29	0.36	21%

Outflows from the Netherlands remained relatively low as a percentage of consumption, with total flows increasing 21.1% this year

- This was largely driven by greater flows to Belgium. Based on higher cigarette prices in the Netherlands, this is likely the result of general travel (either by Belgians or Dutch consumers disposing of packs in Belgium whilst there buying cheaper cigarettes)

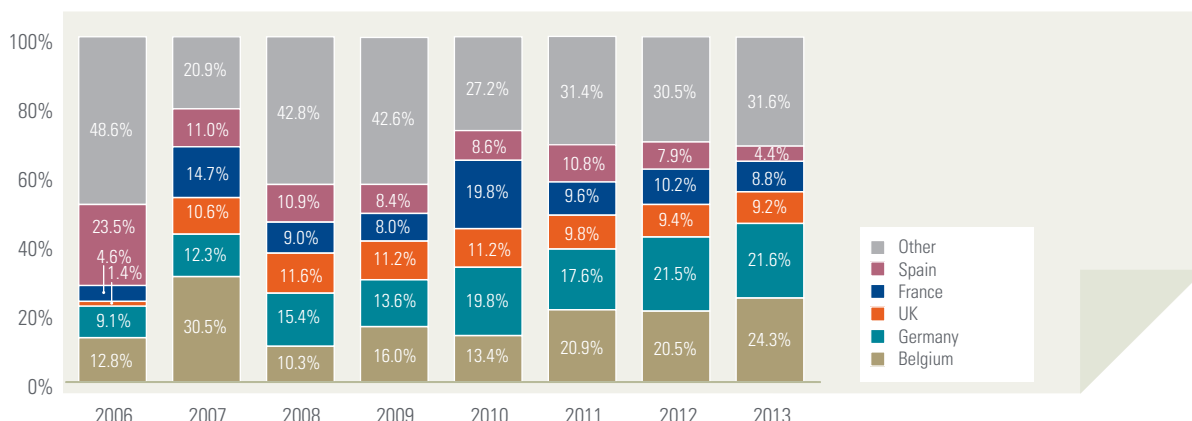
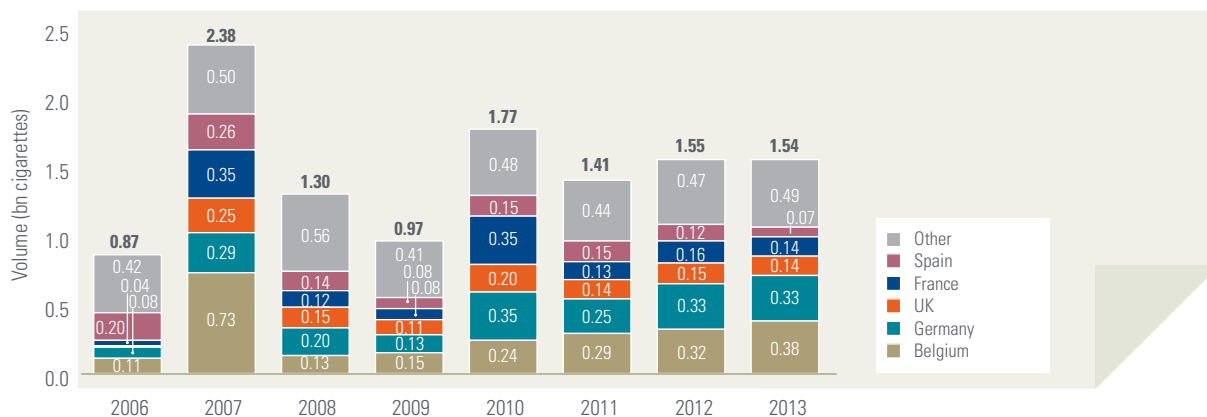
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model.



Non-domestic legal volumes remained stable, originating mainly from Western European markets

ND(L) by origin - 2006-2013 (1)(2)(3)(a)(b)



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Non-domestic legal (ND(L) flows remained stable in 2013, and this resulted in an increase in share of total consumption

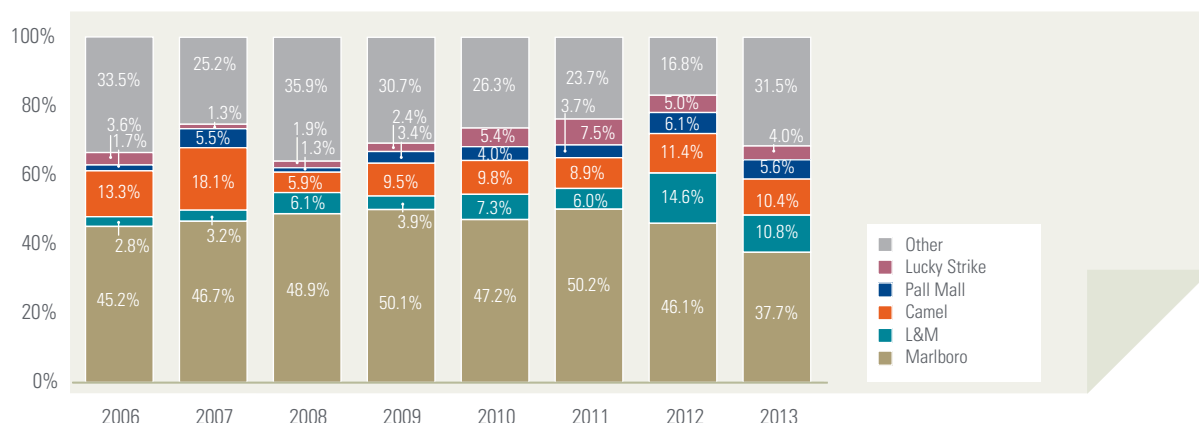
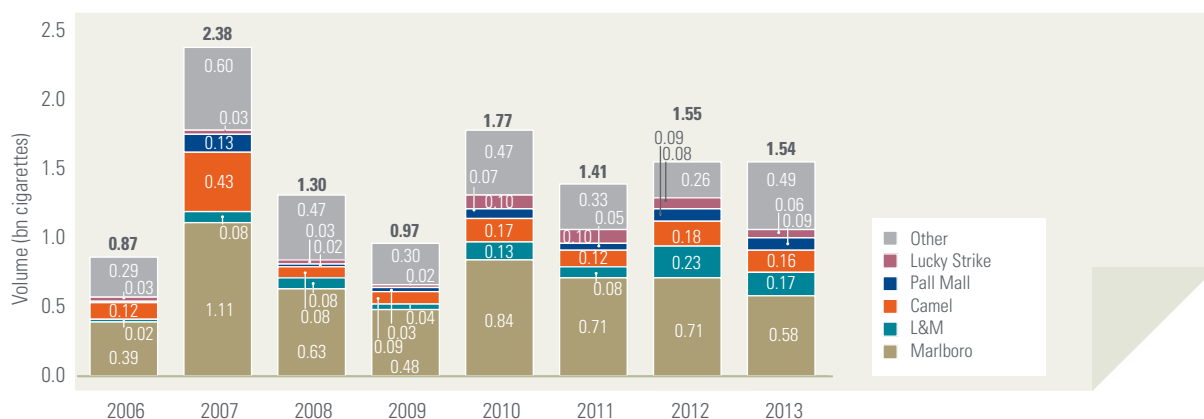
- Inflows from Belgium increased in 2013 and this is likely as a result of the greater price differential for cigarettes between the two countries. Based on WAP, prices in Belgium increased from €4.67 per 20 cigarettes last year to €4.77 in 2013 (or by 2.3%). In contrast, Dutch prices increased from €5.03 per 20 cigarettes to €5.29 (or by 5.1%)⁽³⁾. The empty pack surveys conducted in the Netherlands this year show greater incidence is especially seen in Western and Belgian bordering towns and cities
- Inflows from Germany remain a large part of the total, as a 2.8% increase in German WAP (per 20 cigarettes)⁽³⁾ this year meant the price differential with Netherlands grew
- There was however a 14.1% decrease in inflows from France this year and this is likely to be due to both the proportionately greater price increase in France (7.0% versus prior year) and lower outbound tourism⁽⁴⁾. Other inflows also declined marginally, due to non-EU and Duty Free flows
- 'Other' legal inflows included volumes from Italy, Luxembourg, Greece and Denmark

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) EC Excise Duty tables (Part III – Manufactured Tobacco). (4) UN WTO Tourism Factbook 2008-12, UN WTO.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013 ^{(1)(2)(a)}



Despite a decline in ND(L) inflows of Marlboro and L&M amongst others, inflows of other smaller volume brands increased to almost offset this

- Due to oversampling of the Marlboro brand in the EPS, a second methodology was used in our analysis to calculate inflow volumes, as explained on page [10]
- "Other" non-domestic legal inflows comprise smaller volumes of almost 30 brands, including Chesterfield, Gauloises and Kent

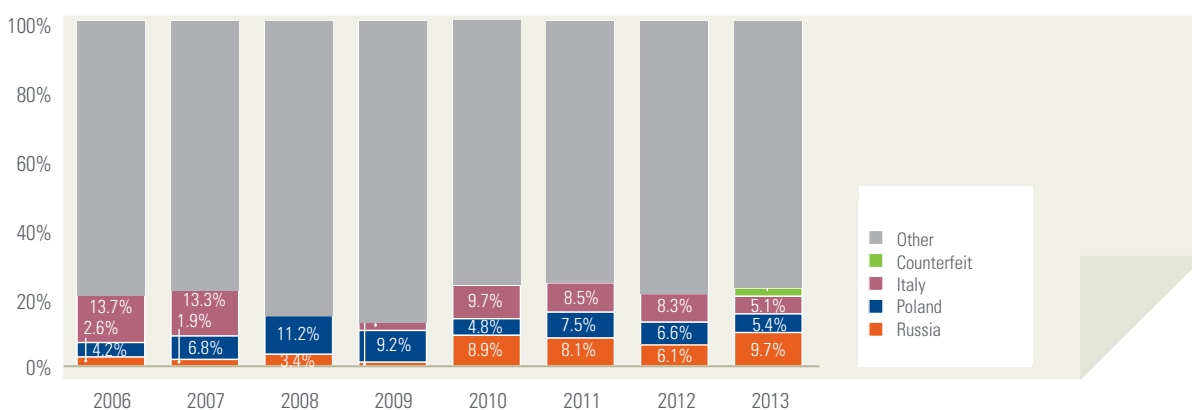
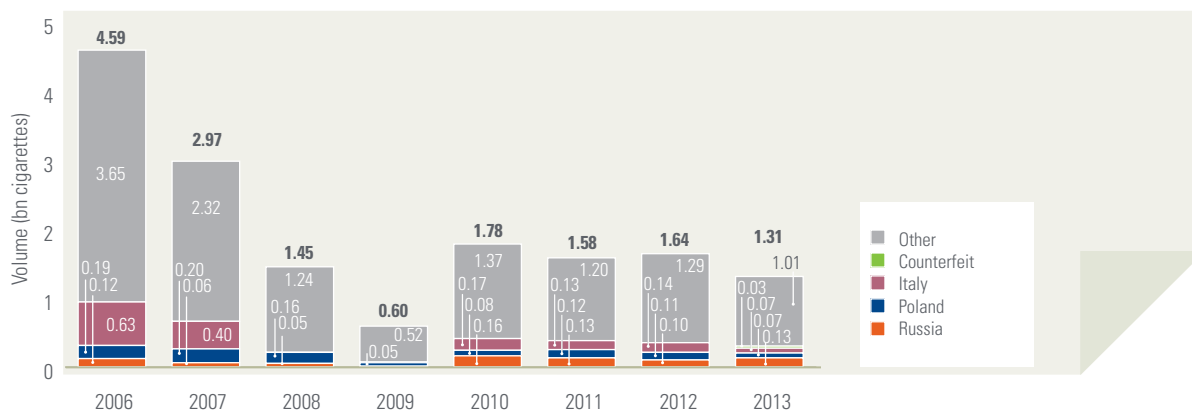
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



Counterfeit and contraband volumes fell this year and represented a smaller share of consumption than non-domestic legal

C&C by origin - 2006-2013 ^{(1)(2)(3)(a)}



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Counterfeit and contraband (C&C) volumes declined by 20% in 2013

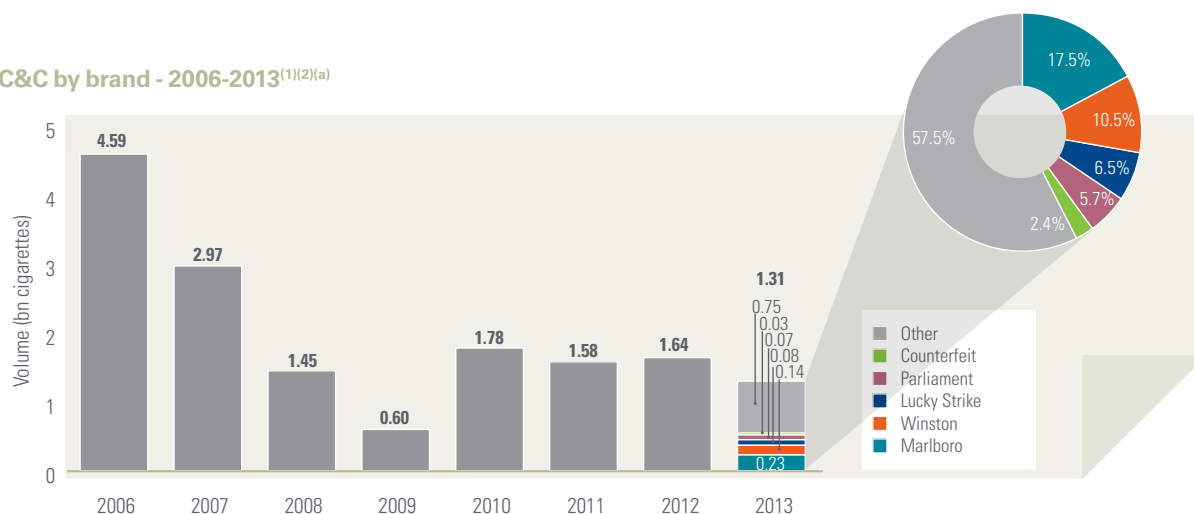
- Russia is now the largest source of C&C inflows and as outbound travel from the Netherlands has fallen⁽³⁾, the increased volumes are all classed as illicit
- Inflows from Poland fell 34.3% to 0.07bn cigarettes as fewer Polish origin packs were picked up during the EPS waves. This may be due to the reduced price differential in the year (based on WAP, Polish cigarettes was €2.75 per 20 cigarettes cheaper than Dutch cigarettes last year but this fell to €2.38 in January 2013⁽⁴⁾). The availability of cheaper Russian cigarettes, as well as smaller increases in cheaper Ukrainian flows may also have had a substitutive impact
- C&C inflows from Italy fell significantly as large outbound tourist flows⁽³⁾ suggested a greater proportion of inflows were legal.
- "Other" C&C is largely made up of Other non-EU flows and some Duty Free, both of which contribute to the decline in volumes in 2013
- Counterfeit cigarettes do not appear to be a significant issue in the Netherlands as volumes of 0.03bn cigarettes only account for 2.4% of total C&C consumption
- If these C&C cigarettes had been legally purchased in the Netherlands, the tax revenue gained would have been approximately €290m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-12, UN WTO. (4) EC Excise Duty tables (Part III – Manufactured Tobacco).

C&C INFLOWS BY BRAND

C&C by brand - 2006-2013^{(1)(2)(a)}



Contraband appears to be the main source of C&C in the Netherlands, with volumes accounting for over 90% of total C&C inflows this year

- From a brands perspective, Marlboro, Winston and Lucky Strike are the most frequently occurring C&C brands, originating mainly from Eastern European markets as well as some Italian, Middle Eastern and Duty Free flows. "Other" comprises a large number of small balances

Breakdown of Illicit Whites by type - 2007-2013^{(1)(2)(a)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO NETHERLANDS								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.27	0.01	0.00	0.13	0.10	0.10	0.05	(46)%
Duty Free	0.07	0.00	0.00	0.05	0.02	0.01	0.00	(37)%
Unspecified	0.00	0.00	0.00	0.00	0.01	0.01	0.00	(72)%
Total Illicit Whites	0.35	0.02	0.00	0.17	0.13	0.12	0.06	(48)%

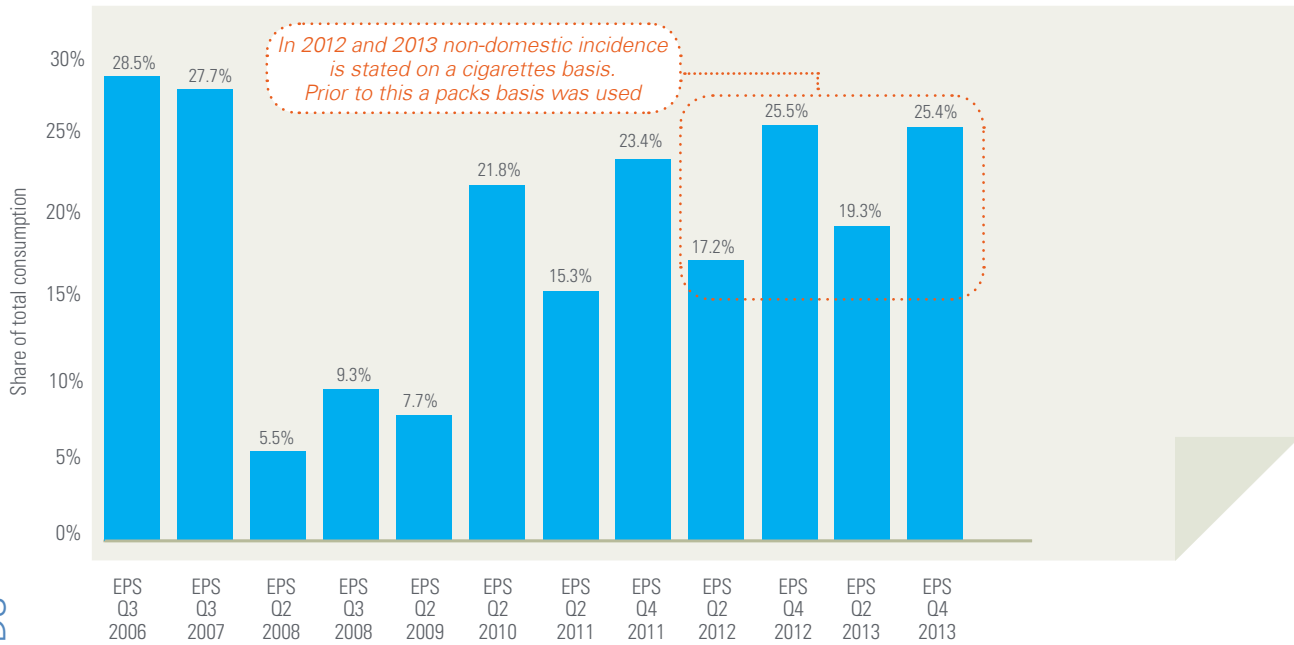
- Illicit Whites form only a small share of the C&C inflows, representing 4.6% of C&C volumes in 2013. Most Illicit Whites consumed in the Netherlands are have country specific labelling. The main brands sold as Illicit Whites appear to be Esse, Natural American Spirit and Wills

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

EPS results & EU Flow model

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



NETHERLANDS



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- The empty pack survey (EPS) in the Netherlands collected 14,000 packs during the course of the year. This was undertaken as two waves – one conducted in Q2 (April/May) and one in Q3/Q4 (September/October). Each wave collected 7,000 packs across the largest 50 towns and cities. The number of packs collected in each city is weighted by the city population
- There are minor differences in non-domestic incidence by region in the Netherlands, however these are not as pronounced as many other EU markets. Incidence peaks in border regions such as Groningen and Nord-Brabant, and is lowest in Zuid-Holland, Flevoland and Friesland
- (Non-domestic) Marlboro packs appeared to be overstated in the EPS results when compared to Marlboro’s share of legal domestic sales in the country. A second methodology has therefore been used in our analysis to model ND Marlboro which is more in line with ND(L) results and domestic brand share. The balance has been allocated to other brands. This is further explained in the methodology section of the appendices

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

NDL volumes calculations and explanations

KPMG non domestic legal flows Netherlands

COUNTRIES WHERE ND(L) IS 100% OF TOTAL				
Country	ND 2013 (bn sticks) (1)		2013 ND(L) (bn sticks)	% of ND
Belgium	0.38		0.38	100%
Germany	0.33		0.33	100%

USE OF CONSUMER RESEARCH AND ANY ADJUSTMENTS FOR 2013 DATA							
Country	ND 2013 (bn sticks) (1)	Total trips where cigarettes purchased (m) ⁽²⁾⁽³⁾	Number of packs per trip ⁽²⁾	Total packs (m)	Data sources ⁽²⁾⁽³⁾	2013 ND(L) (bn sticks)	% of ND
Italy	0.13	0.22	15	3.32	WTO, consumer research	0.07	50%

- Owing to outbound travel of around 4.2m and 1.9m respectively in the year and a number of large towns and cities in close proximity to the border (meaning significant border shopper flows), 100% of non-domestic inflows from Belgium and Germany have been classed as legal flows
- Legal domestic sales have also declined faster in border regions of the Netherlands than the country average as a result of these inflows from neighbouring markets
- For Italy, consumer research seemed to understate the likely legal component of inflows and so the following adjustments were applied in our analysis
 - Consumer research appeared to understate trips to buy cigarettes (0.09m) when compared to total outbound travel (1.7m trips) multiplied by cigarette smoking incidence and trips data for 2011 was used instead (0.22m). This was then adjusted for the change in overall tourism between 2011 and 2013
 - Consumer research also appeared to understate average packs purchased per trip (1 carton) when compared to other major Southern European holiday destinations for Dutch consumers. It was assumed a similar number of packs is brought back from Italy as from Greece and Spain (15 packs)
 - In total, estimated legal inflows from Italy are 0.07bn cigarettes this year (or 50.1% of legal volumes)

Notes: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) Synovate/Ipsos ND(L) research 2013. (3) UN WTO Tourism Factbook 2008-12, UN WTO.



POLAND



Counterfeit & Contraband remained relatively stable both in terms of volumes and share

Manufactured cigarette C&C volumes and share of overall consumption 2006-13

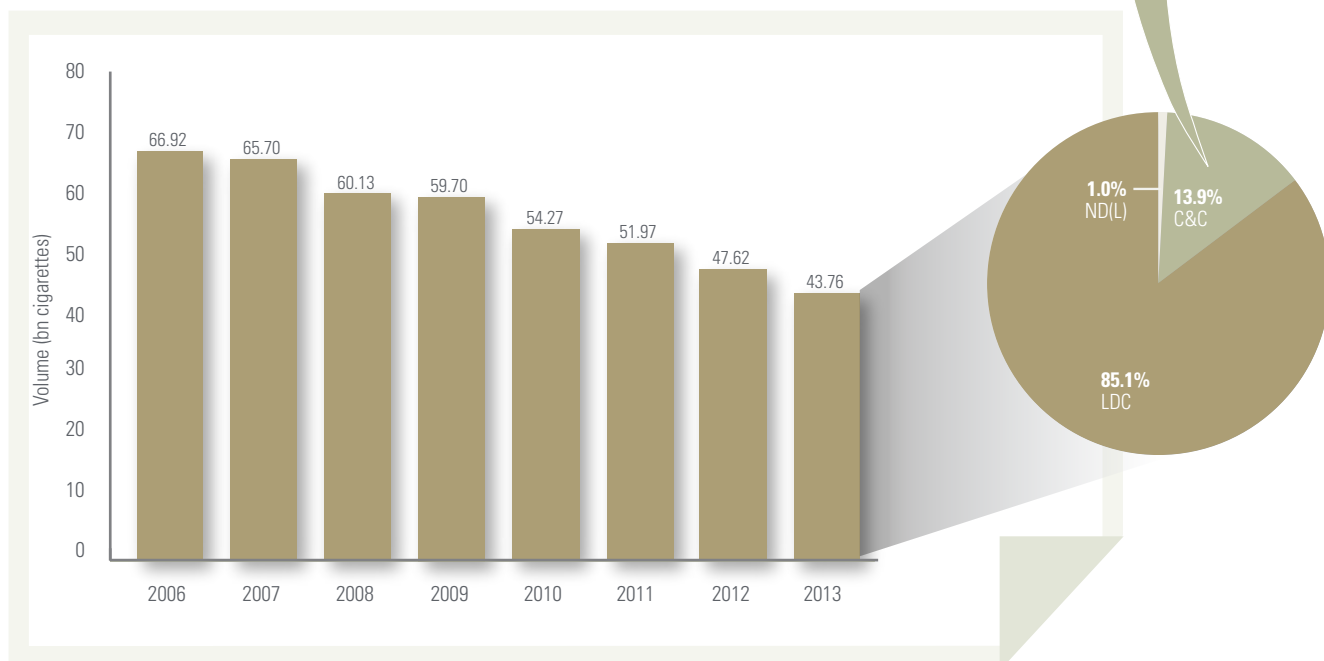


POLAND

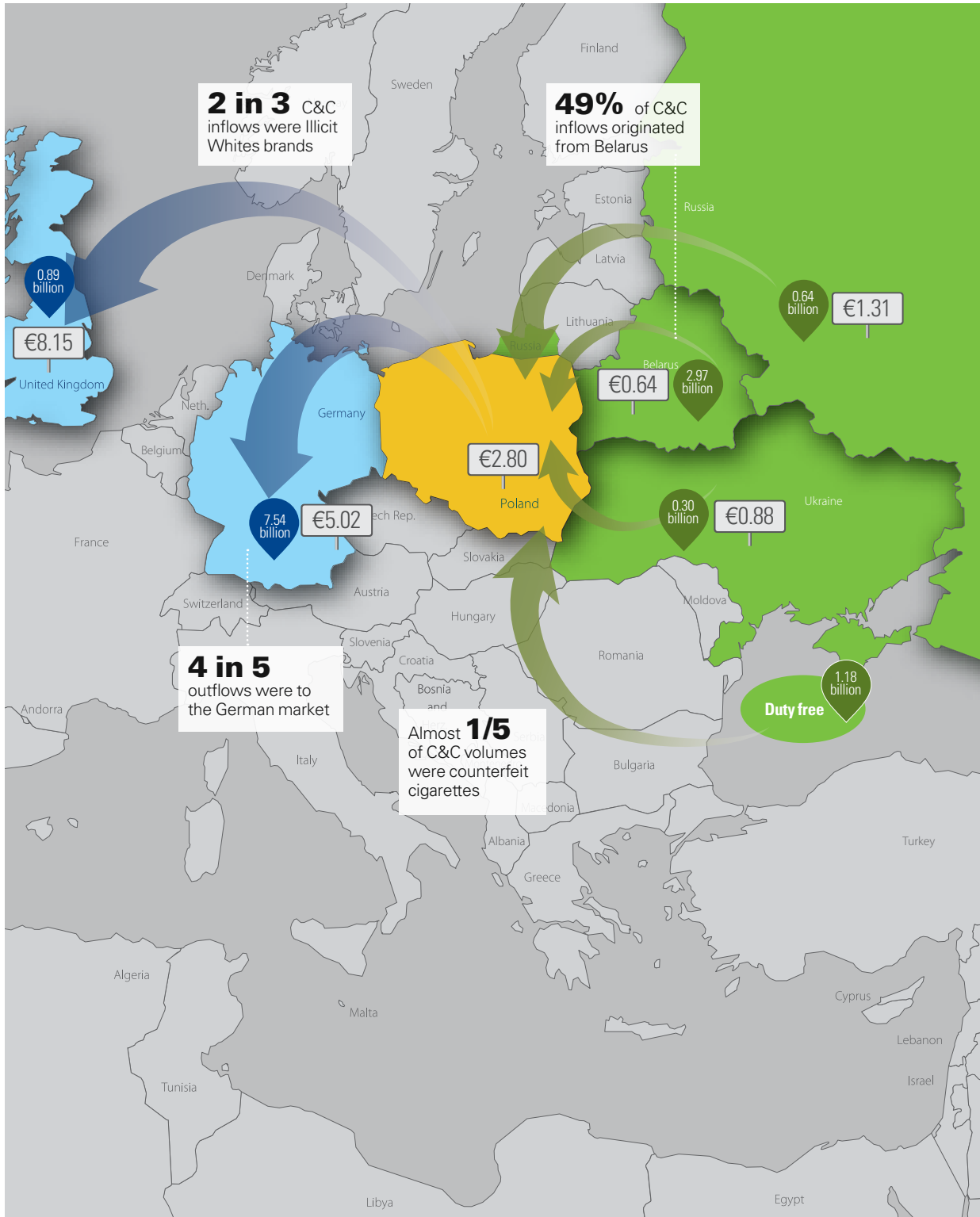


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Manufactured cigarette consumption 2006-13



KEY INFLOWS AND OUTFLOWS



POLAND
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Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

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Total consumption fell, with a decline in both domestic and non-domestic volumes

Total manufactured cigarette consumption - Poland ^{(1)(2)(a)}

TOTAL POLAND CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	72.44	69.91	63.14	61.12	57.32	55.55	52.15	46.63	(11)%
Outflows	-9.94	-9.47	-8.81	-9.43	-9.35	-10.80	-11.36	-9.39	(17)%
Legal domestic consumption (LDC)	62.50	60.44	54.32	51.68	47.97	44.75	40.79	37.24	(9)%
Non-domestic legal (ND(L))	0.61	0.57	0.89	0.94	0.53	0.55	0.63	0.43	(32)%
Counterfeit and contraband (C&C)	3.80	4.69	4.92	7.07	5.77	6.68	6.20	6.10	(2)%
Total non-domestic	4.41	5.26	5.80	8.02	6.30	7.23	6.83	6.52	(5)%
Total consumption	66.92	65.70	60.13	59.70	54.27	51.97	47.62	43.76	(8)%

Share of Poland cigarette consumption by type - 2006-2013 ⁽¹⁾⁽²⁾



Total manufactured cigarette consumption declined by 8.1% in 2013, while counterfeit and contraband (C&C) declined by only 1.7%, increasing as a proportion of total consumption by 0.9 percentage points

- Legal domestic sales (LDS) volumes are likely to have been impacted by a 16.2% increase in the WAP (Euros) during the year (or an 8.9% increase based on Polish Zloty), resulting in average pack prices moving above the PLN10 price point⁽³⁾
 - This price rise was in part driven by a 10%⁽³⁾ increase in specific cigarette excise duty
 - As of 1 January 2014 Poland achieved the minimum EU requirement for taxation of €90 per 1,000 cigarettes⁽³⁾. With the obligation to meet this condition by 2018, additional excise increases to 2018 are expected to be lower than the period 2010-2014
- In the wider economic environment, despite marginal growth in PDI⁽⁴⁾, unemployment increased to 13.5% in 2013⁽⁵⁾
- The wider availability of other cheaper alternatives to manufactured cigarettes, such as OTP, bulk leaf and e-cigarettes, is also likely to have impacted sales
 - E-cigarette sales have increased in recent years, with prices much lower as they are not subject to excise duty
 - Bulk tobacco sales have also grown and despite duty being imposed on dry leaf, it continues to be a lower priced option. In addition, some of this product was sold as wet leaf, to exploit a loop hole evading the duty, which was closed on 1st January 2014

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Source: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) EC Excise Duty tables (Part III – Manufactured Tobacco). (4) Euromonitor, downloaded January 2014 (5) 2014 Economist Intelligence Unit.

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Significant levels of inflow and outflow volumes reflect wide price differentials for cigarettes with neighbouring East and West markets

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWS TO POLAND									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Belarus	0.0202	0.0711	0.0338	0.0304	0.0239	0.0366	0.0352	0.0397	12% (16)%
Duty Free	0.0052	0.0429	0.0117	0.0036	0.0223	0.0250	0.0262	0.0218	0% 90%
Russia	0.0082	0.0023	0.0207	0.0235	0.0108	0.0201	0.0283	0.0264	0% (24)%
Ukraine	0.0167	0.0258	0.0042	0.0071	0.0196	0.0170	0.0107	0.0130	0% (72)%
Spain	0.0022	0.0023	0.0003	0.0001	0.0100	0.0107	0.0108	0.0110	0% 32%
Other	0.23	0.32	0.58	0.59	0.20	0.22	0.15	0.13	14% (15)% n/a
Total ND(L)	0.2616	0.4582	0.6474	0.6454	0.2664	0.3228	0.2571	0.2319	(8)% (74)%
Total inflows	4.41	5.26	5.80	8.02	6.30	7.23	6.83	6.52	(5)%

A large increase of Duty Free labelled inflow volumes was more than offset by a reduction in inflows from historically key source countries, such as Belarus, Russia and Ukraine

- Non-domestic inflows from other Eastern European markets such as Ukraine and Russia declined during the year, in some part due to major manufacturers limiting production of certain brands in those markets in order to manage these cross border flows
 - In addition, some inflows previously classified as originating from Ukraine are now correctly identified as counterfeit, as a result of the study being undertaken on a pan-industry basis resulting in additional data and analysis undertaken by manufacturers in 2013
- Over four fifths of the Duty Free inflows were Illicit Whites brands, which drives almost all the growth seen this year. The main brands sold as Illicit Whites appear to be Jin Ling, Brendal, EB and Compliment

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM POLAND									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Germany	6.53	6.85	6.32	7.54	7.49	8.64	8.54	7.54	(12)%
UK	1.40	1.02	0.93	1.01	0.86	0.96	1.72	0.89	(48)%
France	0.41	0.32	0.41	0.28	0.30	0.55	0.31	0.32	3%
Ireland	0.33	0.37	0.18	0.14	0.22	0.19	0.19	0.16	(13)%
Sweden	0.27	0.23	0.19	0.04	0.05	0.06	0.13	0.12	(8)%
Other	1.00	0.67	0.79	0.42	0.43	0.40	0.46	0.34	(25)%
Total outflows	9.94	9.47	8.81	9.43	9.35	10.80	11.36	9.39	(17)%

A decline in outflows was mainly the result of lower flows to Germany and the UK, though they remained the biggest outflow destinations

- Excise driven price increases in Poland and foreign exchange movements made the Czech origin product comparatively cheaper for the German market
 - The WAP differential per 20 cigarettes between Germany and Poland reduced slightly from €2.23 to €2.22 in 2013⁽²⁾

Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

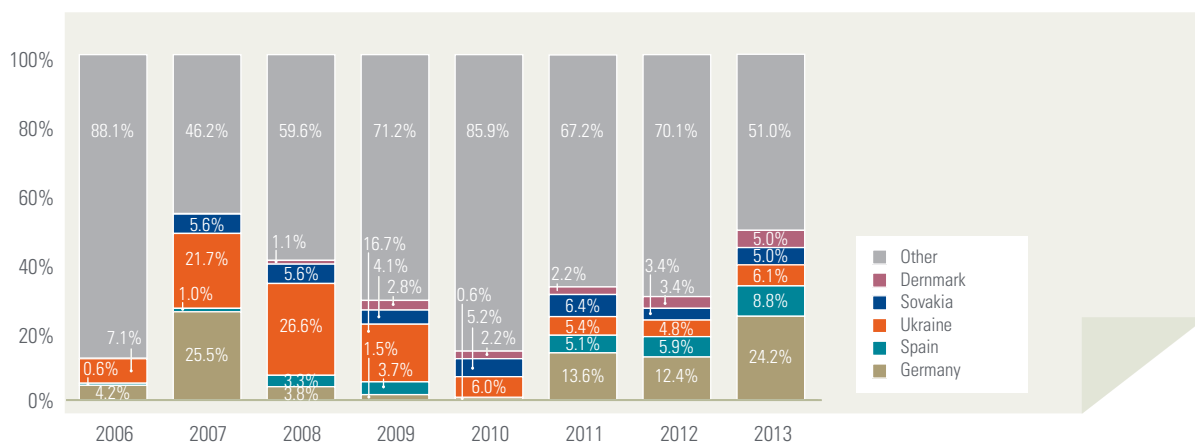
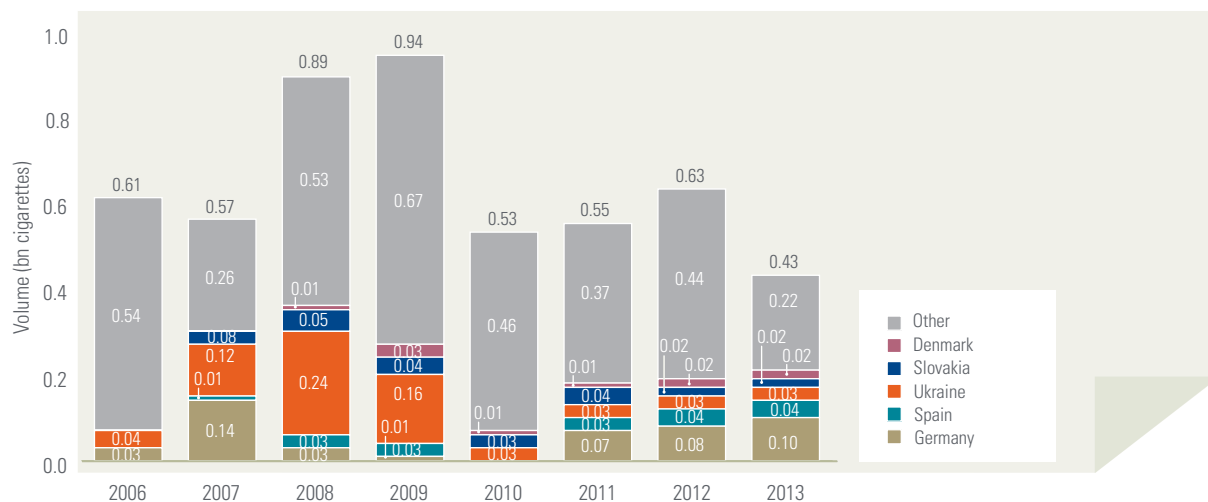
Source: 1) KPMG EU Flows Model (2) EC Excise Duty tables (Part III – Manufactured Tobacco).

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Non-domestic legal inflows represent only 7% of total non-domestic volumes

ND(L) by origin - 2006-2013^{(1)(2)(a)(b)}



POLAND



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Non-domestic legal (ND(L)) flows into Poland have historically been low in comparison to C&C volumes, with Germany and Spain the main source countries

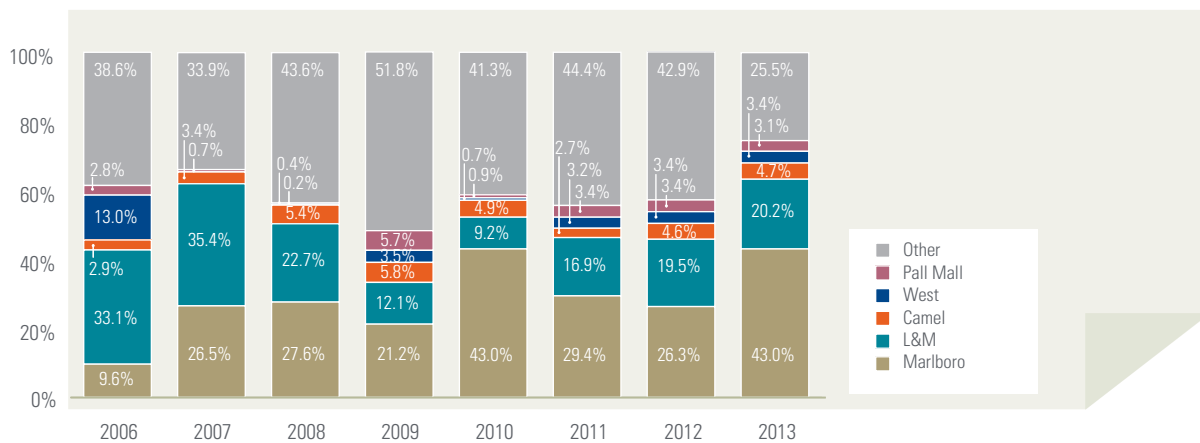
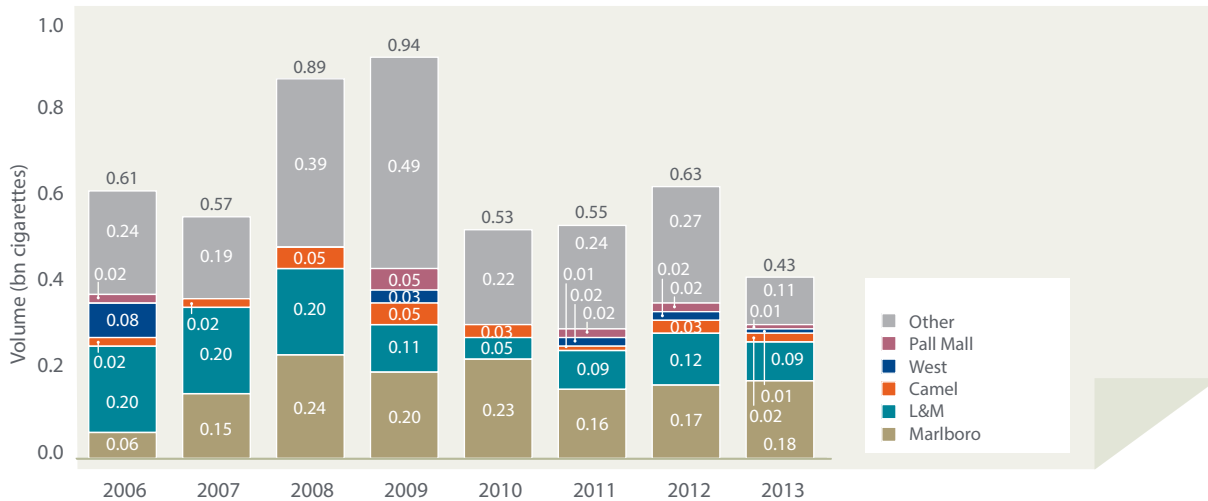
- Growth in outbound tourism to Germany⁽³⁾ has resulted in a 32% increase in ND(L) volumes, however this was more than offset by a decline in small ND(L) inflows from a large number of other countries
- Prices in Germany, Spain and Denmark exceeded those in Poland and were therefore also classed entirely as ND(L) flows. Similarly, price differentials with the bordering countries such as Slovakia were minimal and therefore all flows were assumed to be ND(L)

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) UN WTO Tourism Factbook 2008-2012, UN WTO.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013^{(1)(2)(a)}



The most popular ND(L) brands remained consistent in 2013

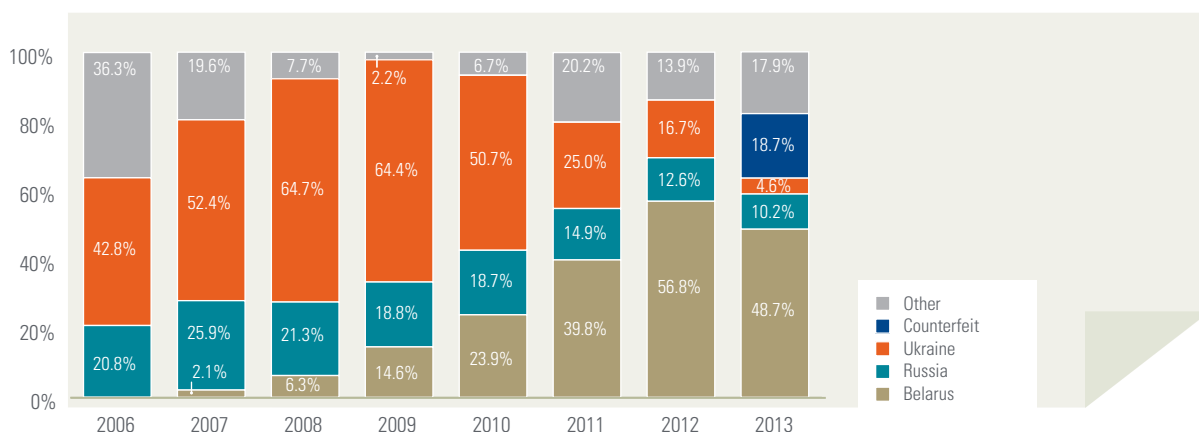
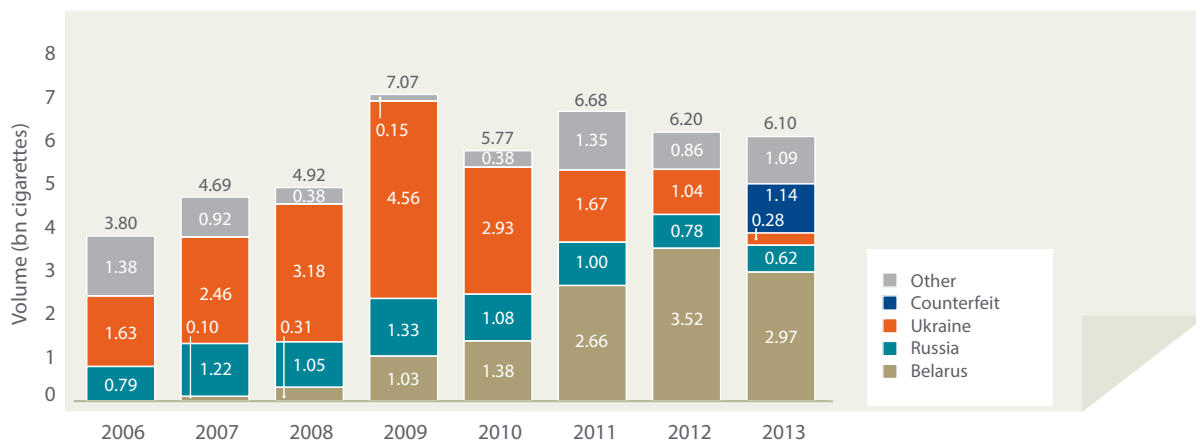
- Marlboro continued to be the most popular brand and is typically the most purchased brand abroad as it is often the most available

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

Overall counterfeit and contraband volumes declined slightly whilst counterfeit is around one fifth of the total

C&C by origin - 2006-2013^{(1)(2)(a)(b)}



POLAND



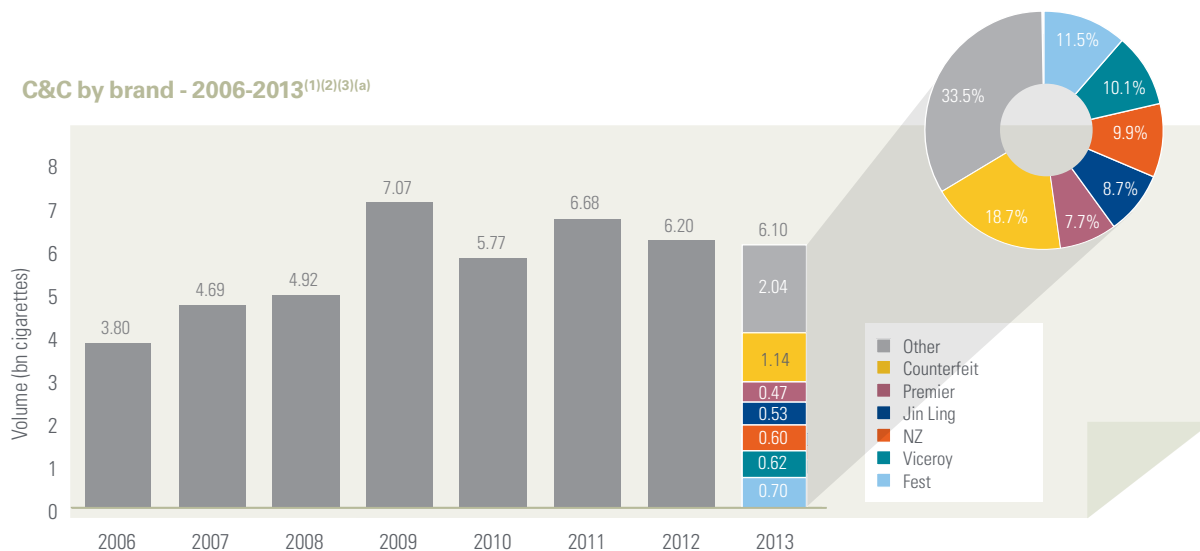
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The slight decline in C&C was primarily the result of lower inflows from Belarus and Russia, with some volumes previously attributed to Ukraine now reclassified as counterfeit as new information was made available

- Total outbound travel to Belarus is low and declining⁽³⁾
 - Import restrictions on cigarettes being brought back from Belarus into Poland have recently tightened to two packs per person
 - This, combined with the consumer research, resulted in almost 100% of the flows from Belarus classified as C&C
- Tourist travel to Russia is high and increasing, however consumer research indicates that on average only 1 pack was brought back from Russia per trip, resulting in low levels of ND(L) and therefore most of this flow is C&C
- Seizures remained relatively high in Poland however volumes seized in 2013 (around 1% of consumption) were below the recent peak in 2009 and have declined year-on-year since then⁽⁴⁾
- If these cigarettes had been legally purchased in Poland the tax revenue gained would have been approximately €685m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. Sources: (1) KPMG EU Flows Model. (2) UNWTO Tourism Factbook 2008-2012, UNWTO. (3) Synovate/Ipsos ND(L) research 2013. (4) KPMG analysis EU Tax tables to see price increases.

C&C INFLOWS BY BRAND



IllicitWhites brands are prevalent in Poland and represented around two thirds of total C&C volumes consumed

- This includes the Grodno Tobacco brands from Belarus which account for the majority of the 2.95bn cigarettes classified as country specific IllicitWhites
- The Brendal brand, labelled as Duty Free, has emerged in 2013 and accounted for 0.21bn of the IllicitWhites flows, having previously had no discernible presence. Combined with Jin Ling, these two brands largely accounted for the 0.97bn IllicitWhites labelled as Duty Free
- Viceroy accounted for approximately 10% of total C&C inflows in 2013
- As a result of the study being undertaken on a pan-industry basis in 2013 and new information made available, the total level of counterfeit volumes has been estimated for the first time, which accounted for 19% of C&C volumes

Composition of IllicitWhites inflows - 2007-2013^{(1)(3)(b)}

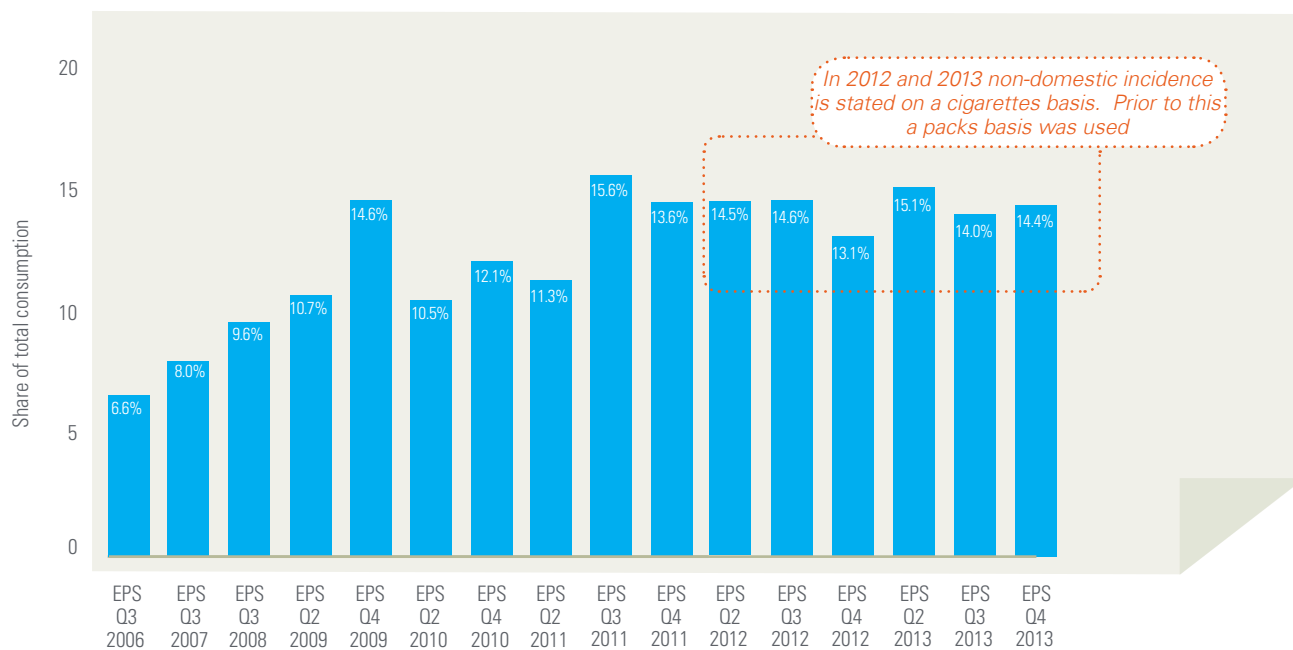
LABELLING OF ILLICITWHITES INFLOWS TO POLAND								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.12	0.49	1.16	1.46	2.89	3.39	2.95	(13)%
Duty Free	0.00	0.00	0.07	0.05	0.15	0.35	0.97	>100%
Unspecified	0.00	0.00	0.00	0.00	0.31	0.13	0.08	(42)%
Total IllicitWhites	0.12	0.49	1.23	1.51	3.35	3.87	3.99	3%

Note: (a) Additional details of key ND(L) calculations provided overleaf. Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



EPS results and EU Flows Model

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



POLAND



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- The empty pack survey (EPS) in Poland collected 51,000 packs during the course of the year. This was undertaken as three waves – one conducted in Q2 (April), one in Q3 (August) and one in Q4 (October / November). Each wave collected 17,000 packs across a total of 70 cities, comprising the largest 40 cities and 30 smaller towns. The number of packs collected in each city was weighted by the city population
- Non-domestic incidence in Poland varies significantly by region and also between urban and rural areas. Per the EPS, ND incidence was greatest in the regions of Podkarpackie (28.2%, borders Ukraine), Podlaskie (40.0%, borders Belarus) and Warminsko-Mazurskie (41.4%, borders Russia). Moreover, non-domestic incidence appeared to be a greater issue in smaller towns and rural areas. Weighted EPS results for 2013 gave an ND incidence of 12.5% for the largest 20 cities surveyed, compared to 17.0% for the other 50 towns and cities
- As a result, to more fairly represent the large rural population in Poland and the typically higher incidence in such regions, EPS data was re-weighted in our analysis such that the regional share of the survey aligned with regional population shares. This marginally increased ND incidence from 14.2% to 14.9%

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

ND(L) volumes calculations and explanations

KPMG non domestic legal flows Poland

COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 (bn sticks) ⁽¹⁾	2013 ND(L) (bn sticks)	% of ND
Germany	0.10	0.10	100%

COUNTRIES WHERE ND(L) IS 100% OF TOTAL							
Country	ND 2013 (bn sticks) ⁽¹⁾	Total trips where cigarettes purchased (m) ⁽²⁾⁽³⁾	Number of packs per trip (m)	Total packs (m)	Data sources ⁽²⁾⁽³⁾⁽⁴⁾	2013 ND(L) (bn sticks)	% of ND
Ukraine	0.30	0.62	2	1.30	Consumer research	0.03	9%

- To estimate the legal element of inflows from Germany, consumer research has been used. As this consumer research implies a legal volume greater than the total non-domestic incidence and given the materiality of the flow, this has been capped at 100% of non-domestic inflows
- In the case of Ukraine, consumer research again formed the basis of the calculation for the legal component of flows. This was then updated for a decline in outbound tourism⁽³⁾ and relative price changes (the price differential increased in the year implying more packs would be brought back per trip). On this basis, the legal element was estimated as 0.03bn cigarettes, or 9% of the total inflow

Notes: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) Synovate/Ipsos ND(L) research 2013. (3) UN WTO Tourism Factbook 2008-2012, UN WTO. (4) EC Excise Duty tables (Part III – Manufactured Tobacco).

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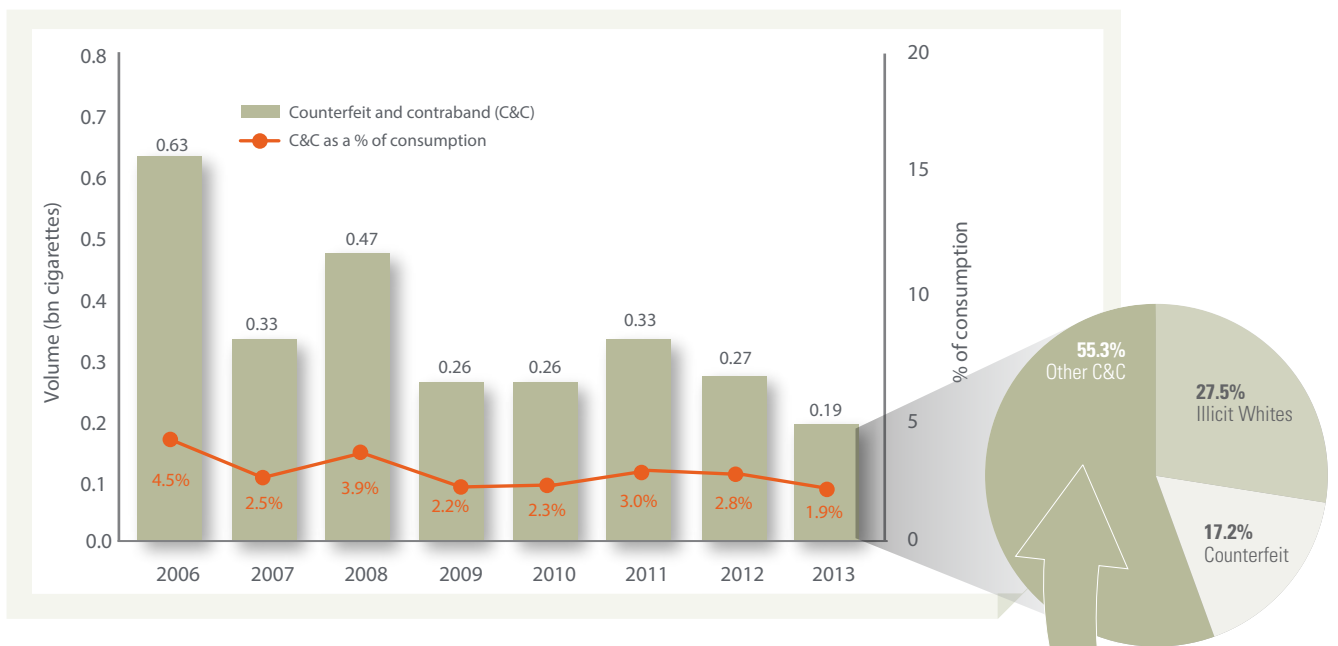


PORTUGAL



Consumption remained stable, while Counterfeit and Contraband declined, compensated by lower outflows

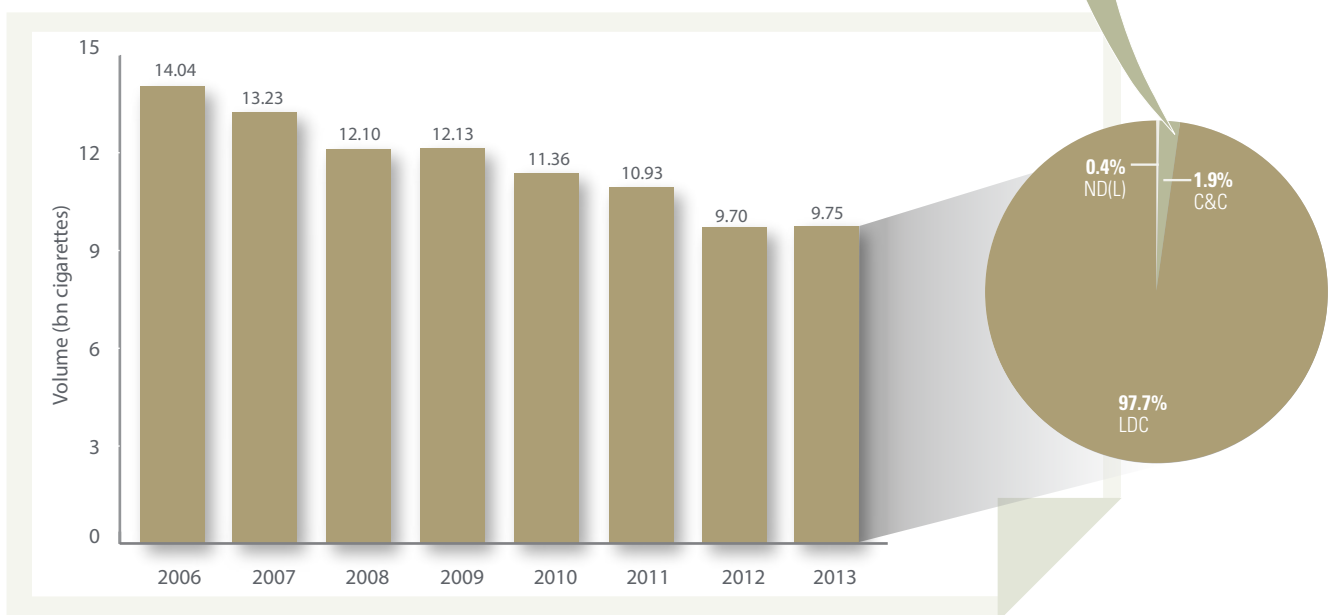
Manufactured cigarette C&C volumes and share of overall consumption 2006-13



PORTUGAL

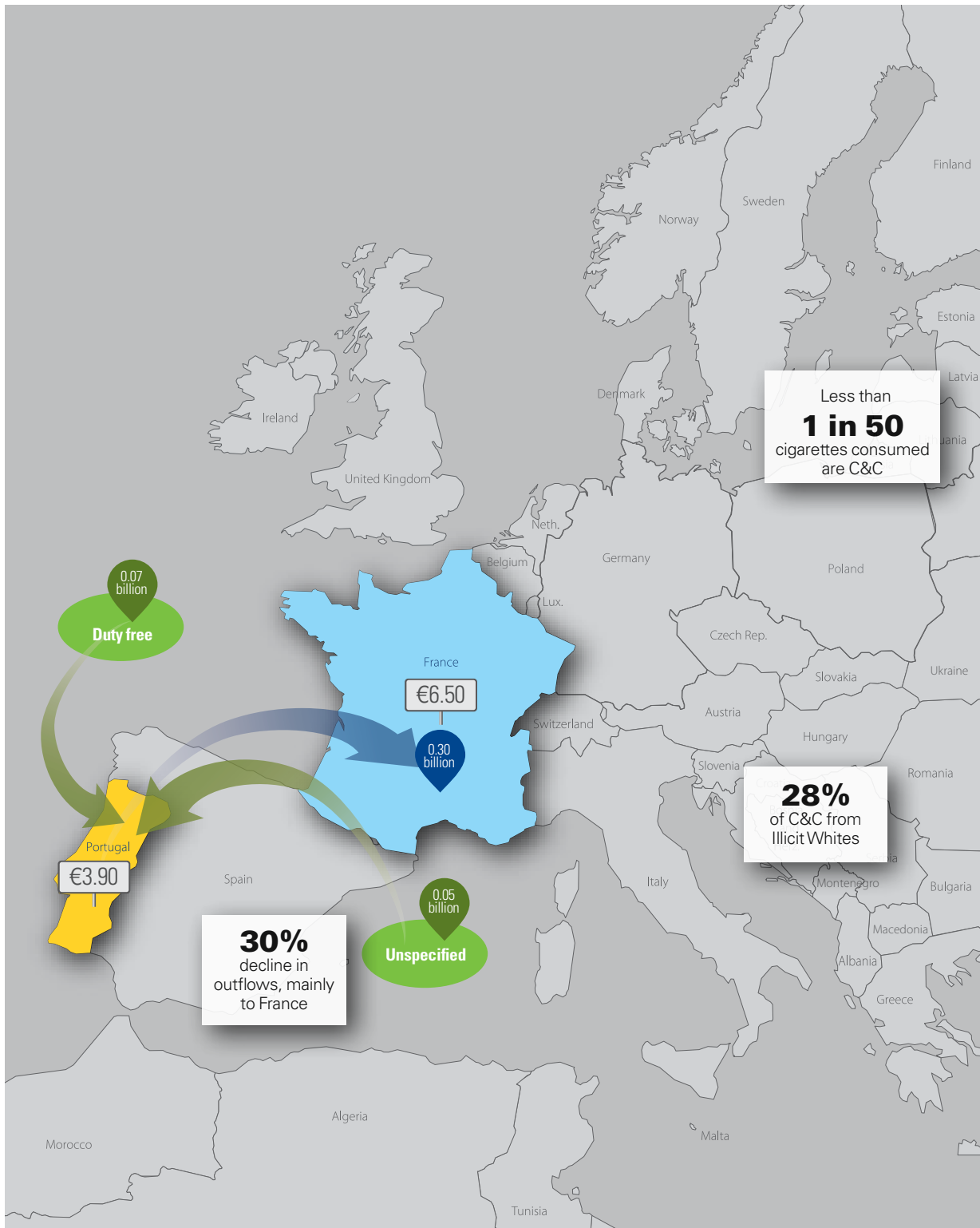


Manufactured cigarette consumption 2006-13



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KEY INFLOWS AND OUTFLOWS



PORTUGAL
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Main outflow █
Main inflow █

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

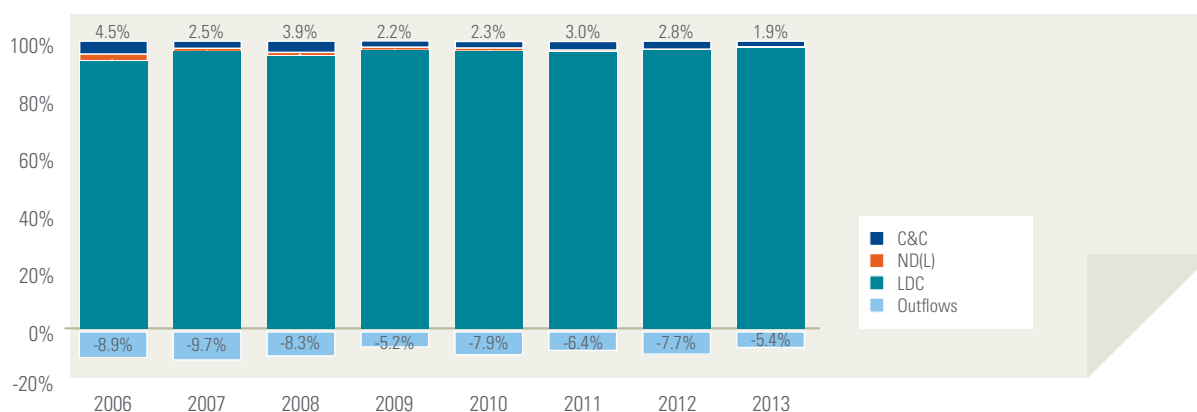
MANUFACTURED CIGARETTE CONSUMPTION

Overall consumption has remained stable, with a decrease in legal domestic sales and non-domestic inflows offset by a fall in outflows

Total manufactured cigarette consumption - Portugal^{(1)(2)(3)(a)}

TOTAL PORTUGAL CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	14.33	14.03	12.48	12.37	11.86	11.23	10.13	10.04	(1)%
Outflows	-1.24	-1.28	-1.00	-0.63	-0.89	-0.70	-0.75	-0.52	(30)%
Legal domestic consumption (LDC)	13.08	12.75	11.48	11.73	10.97	10.53	9.38	9.52	2%
Non-domestic legal (ND(L))	0.32	0.14	0.15	0.13	0.13	0.07	0.05	0.03	(23)%
Counterfeit and contraband (C&C)	0.63	0.33	0.47	0.26	0.26	0.33	0.27	0.19	(31)%
Total non-domestic	0.95	0.48	0.62	0.39	0.39	0.40	0.32	0.22	(30)%
Total consumption	14.04	13.23	12.10	12.13	11.36	10.93	9.70	9.75	0%

Share of Portugal cigarette consumption by type 2006-2013⁽¹⁾⁽²⁾⁽³⁾



Total manufactured cigarette consumption in Portugal remained stable in 2013, with a 2% increase in legal domestic consumption offset by a 30% fall in non-domestic consumption

- Economic conditions in Portugal may have had an impact on overall consumption as unemployment rose from 15.7% to 16.3% and average personal disposable income declined by 2% in 2013⁽⁴⁾⁽⁵⁾
- Legal domestic sales (LDS) volumes may also have been impacted by a 1.3% weighted average price rise in 2013⁽⁶⁾

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a sticks basis. Prior to this a packs basis was used.

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011) (3) Ipsos Empty Pack Surveys, 2006 – 2013 (4) Euromonitor Passport. (5) The Economist Intelligence Unit (6) EU Commission WAP tables.

Duty Free and Unspecified products continued to be the largest inflows

Illicit Whites with Duty Free labelling on accounted for 5% of Duty Free flows

Total inflows by country of origin - 2006-2013 ^{(1)(a)}

ND INFLOWS TO PORTUGAL									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	0.101	0.061	0.060	0.061	0.055	0.084	0.065	0.071	10%
Unspecified	0.000	0.000	0.000	0.000	0.002	0.069	0.061	0.049	(21)%
Russia	0.003	0.000	0.000	0.000	0.005	0.007	0.003	0.006	>100%
Spain	0.697	0.201	0.453	0.129	0.107	0.040	0.023	0.003	(86)%
Sweden	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.003	n/a
Counterfeit								0.032	n/a
Other	0.152	0.214	0.109	0.204	0.225	0.200	0.167	0.058	(65)%
Total inflows	0.952	0.476	0.621	0.394	0.393	0.401	0.319	0.224	(30)%

Non-domestic inflows to Portugal fell by 30% in 2013, largely due to falling Illicit White volumes from unspecified markets

- Duty Free cigarettes remain the largest non-domestic inflow.
- 25% of packs of unspecified market variant were Illicit White brands
- Flows into Spain may have been impacted by falling tourist numbers, which have been decreasing since 2008⁽²⁾

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM PORTUGAL									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
France	0.562	0.482	0.471	0.274	0.514	0.411	0.435	0.301	(31)%
UK	0.305	0.511	0.335	0.124	0.102	0.105	0.150	0.069	(54)%
Netherlands	0.034	0.049	0.033	0.011	0.025	0.026	0.028	0.034	21%
Germany	0.068	0.056	0.026	0.022	0.031	0.031	0.032	0.033	3%
Spain	0.176	0.117	0.058	0.143	0.082	0.028	0.036	0.027	(26)%
Ireland	0.021	0.010	0.032	0.028	0.042	0.047	0.017	0.022	29%
Other	0.074	0.052	0.044	0.029	0.093	0.046	0.045	0.031	(31)%
Total outflows	1.243	1.281	1.002	0.634	0.892	0.697	0.747	0.521	(30)%

Outflows from Portugal have declined by 30% in 2013, with the largest declines to France and the UK, despite widening price gaps

- In 2013 the WAP difference between Portugal and France increased from of €2.25 to €2.60 and from €3.67 to €4.26 for the UK⁽³⁾

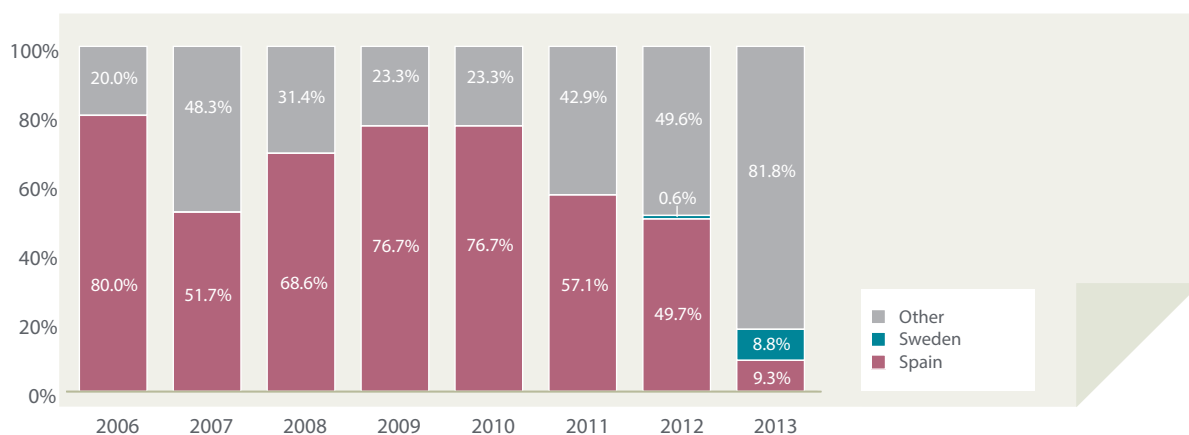
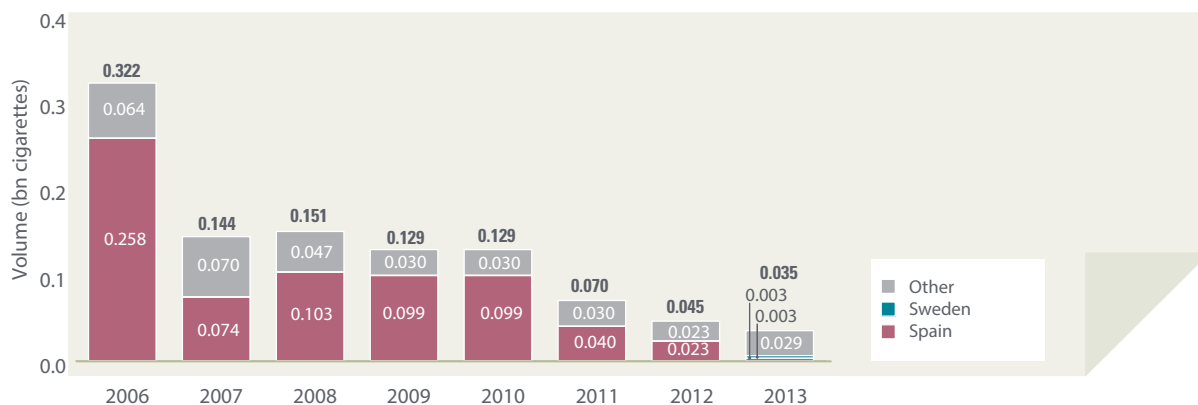
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Source: (1) KPMG EU Flows Model (2) World Tourism Organisation, Data on Outbound Tourism dataset, 2014. (3) EU Commission WAP tables.



Non-domestic legal volumes remained low and continued to decline

ND(L) by origin - 2006-2013 ^{(1)(2)(3)(a)(b)}



PORTUGAL



The largest non-domestic legal (ND(L)) inflows to Portugal are from Spain

- Spain is a popular tourist destination for Portuguese travelling abroad and is a higher priced market than Portugal, therefore all flows are considered legal

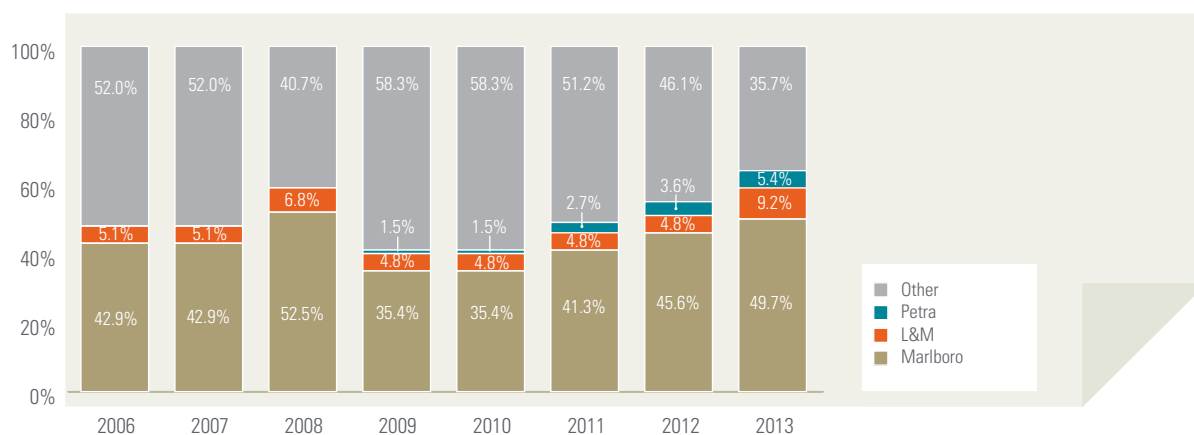
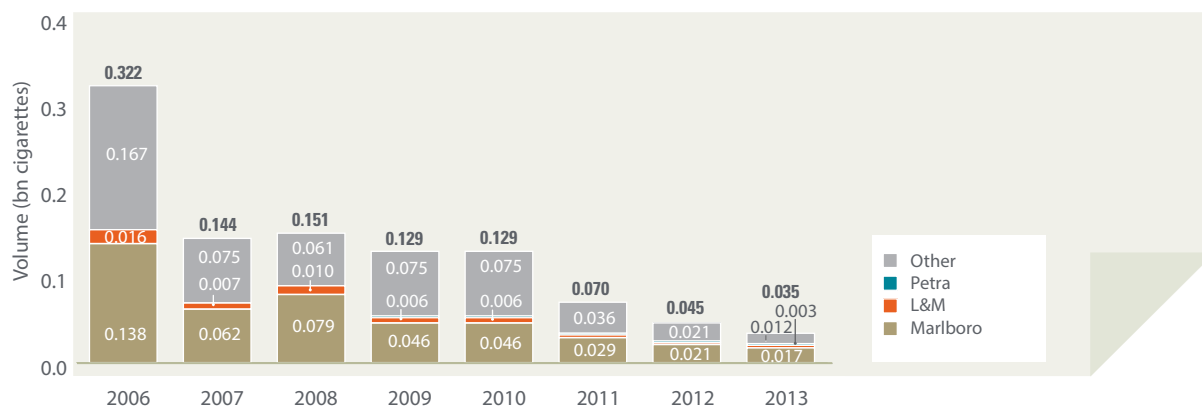
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Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013 ^{(1)(2)(3)(a)}



ND(L) inflows declined by 23% in 2013, with Marlboro and "other" brands accounting for the greatest share of the fall

- The most popular ND(L) brand is Marlboro. Packs from Brazil, Cape Verde, France, Germany and Spain comprise 47% of the Marlboro ND(L) balance

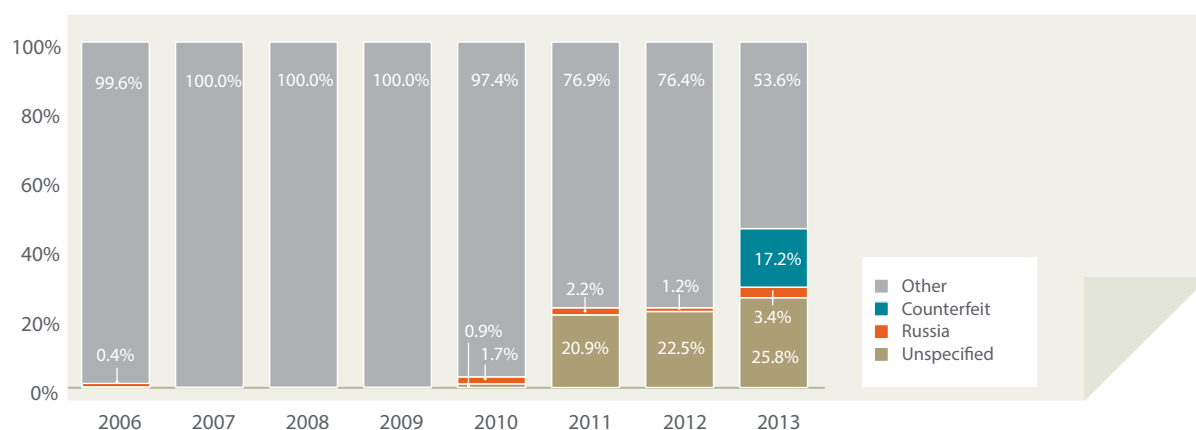
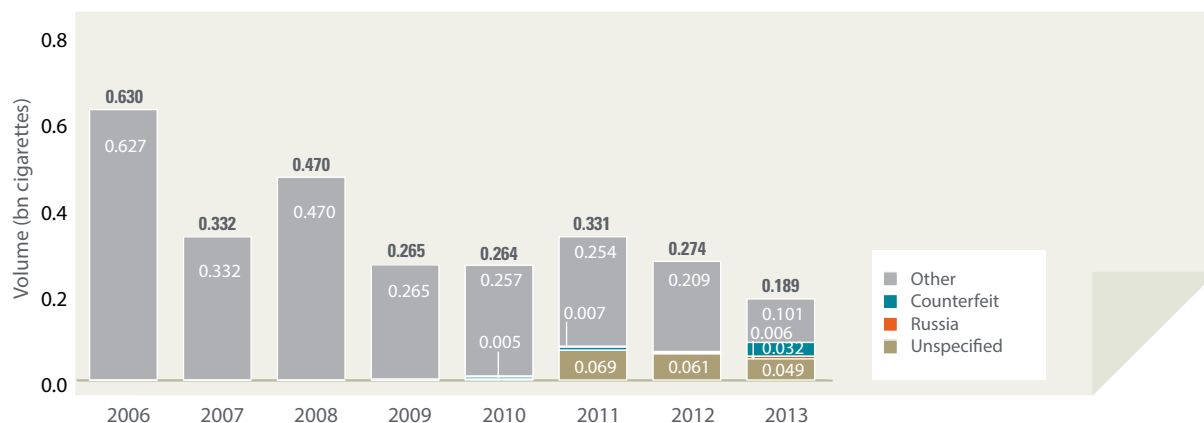
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



Counterfeit and contraband continued to decline in 2013

C&C by origin - 2006-2013 ^{(1)(2)(3)(a)}



PORTUGAL



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Total counterfeit and contraband (C&C) in Portugal decreased by 31% between 2012 and 2013, reflected mainly in a decrease in brands of unspecified origin

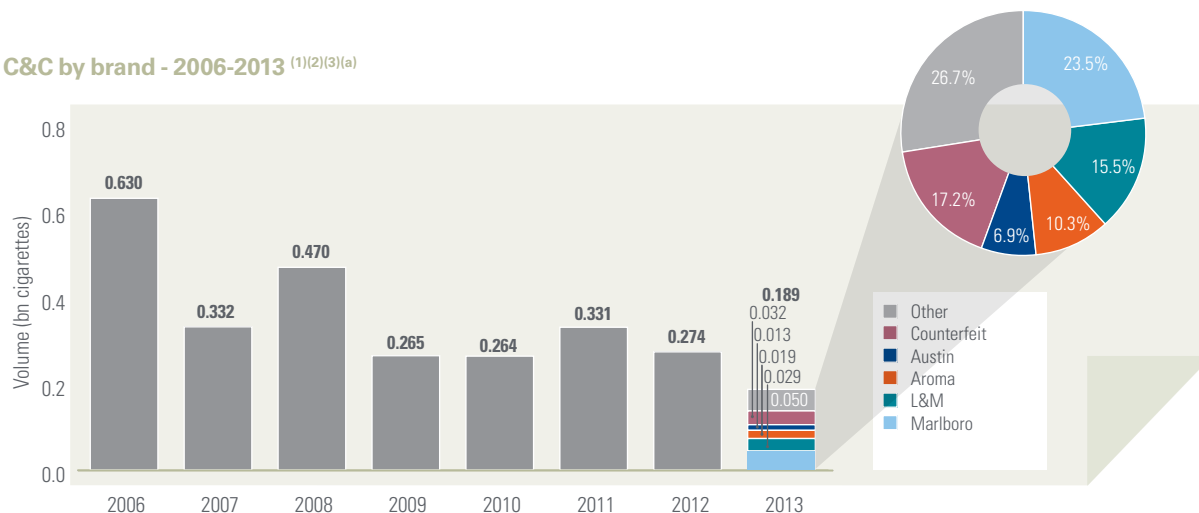
- If the total volume of C&C had been consumed legally within Portugal, it is estimated that an additional tax revenue of approximately €29 million would have been raised by the Portuguese Treasury

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

C&C INFLOWS BY BRAND

C&C by brand - 2006-2013 ^{(1)(2)(3)(a)}



A fall in the prevalence of Illicit White brands such as Austin and Elixir accounts for the overall decline in C&C, though counterfeit volumes as a proportion of total C&C consumption were relatively high

- Counterfeit volumes in Portugal were 17% of C&C in 2013, compared to an EU average of 6%

Breakdown of Illicit Whites by type - 2007-2013 ^{(1)(3)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO PORTUGAL								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country Specific	0.008	0.034	0.012	0.012	0.047	0.109	0.041	(62)%
Duty Free	0.000	0.000	0.000	0.000	0.000	0.004	0.001	(80)%
Unspecified	0.000	0.000	0.000	0.000	0.011	0.016	0.010	(40)%
Total Illicit Whites	0.008	0.034	0.012	0.012	0.058	0.129	0.052	(60)%

Illicit Whites with Duty Free labelling on accounted for 5% of Duty Free flows

Illicit Whites are a decreasing part of illicit cigarette consumption in Portugal, accounting for 27% of C&C volumes in 2013 compared to 47% in 2012

- The majority of Illicit Whites in 2013 displayed country specific labelling
- The main Illicit Whites brands were Aroma and Austin, comprising 63% of Illicit Whites volumes

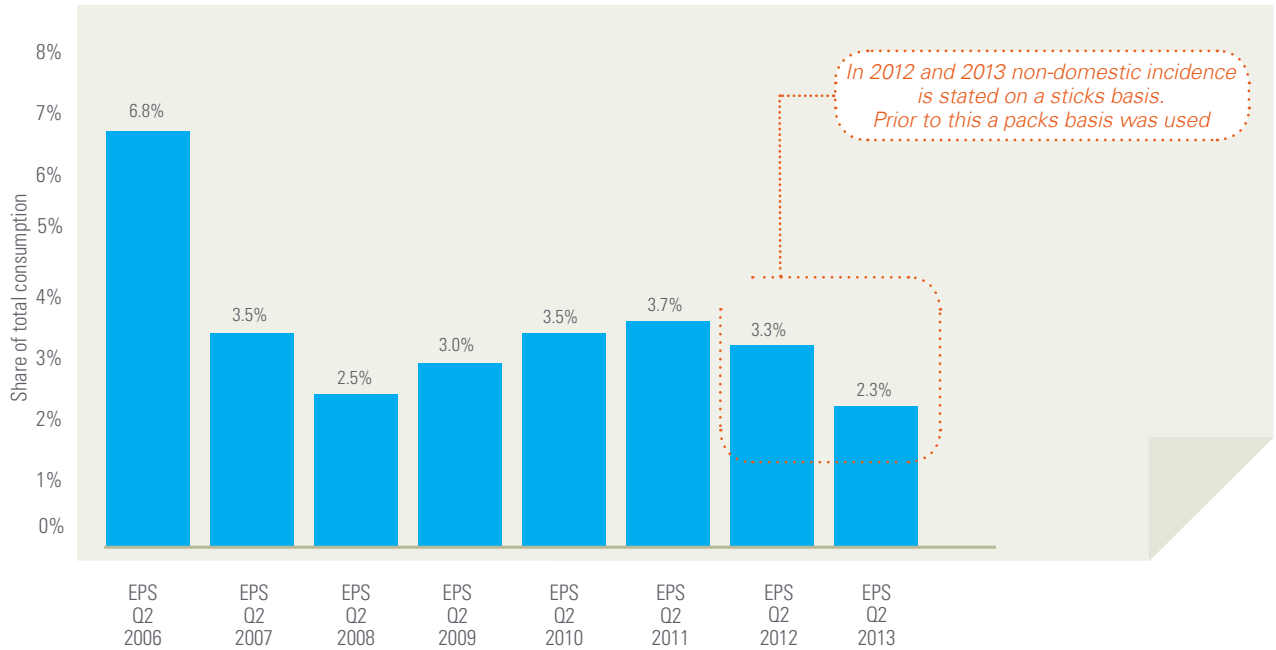
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



EPS results & EU Flow model

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



EPS has shown a decrease in non-domestic incidence since 2012

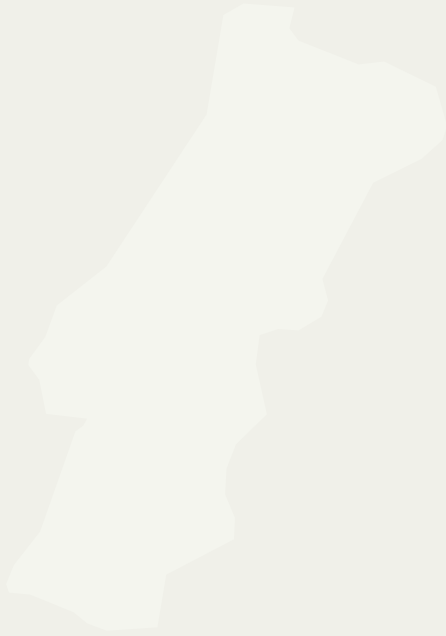
- The empty pack survey in Portugal collected 3,000 packs during the second and fourth quarters of the year. It collects these packs across 10 towns and cities. The number of packs collected in the town or city is weighted by its population
- No further weighted adjustments were made to the data

PORTUGAL



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Source: (1) Ipsos Empty Pack Surveys, 2006 – 2013.



PORTUGAL



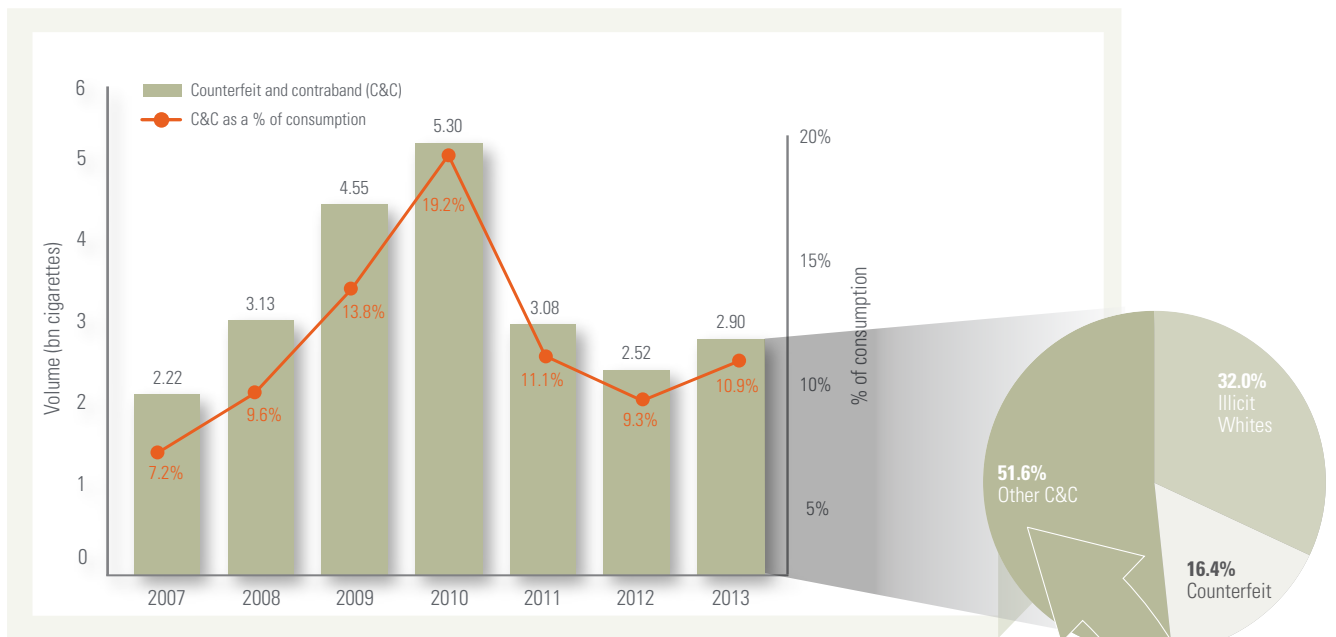
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ROMANIA



Consumption remained relatively stable, with increased Counterfeit & Contraband volumes partially compensating a decline in Legal Domestic Sales

Manufactured cigarette C&C volumes and share of overall consumption 2007-2013

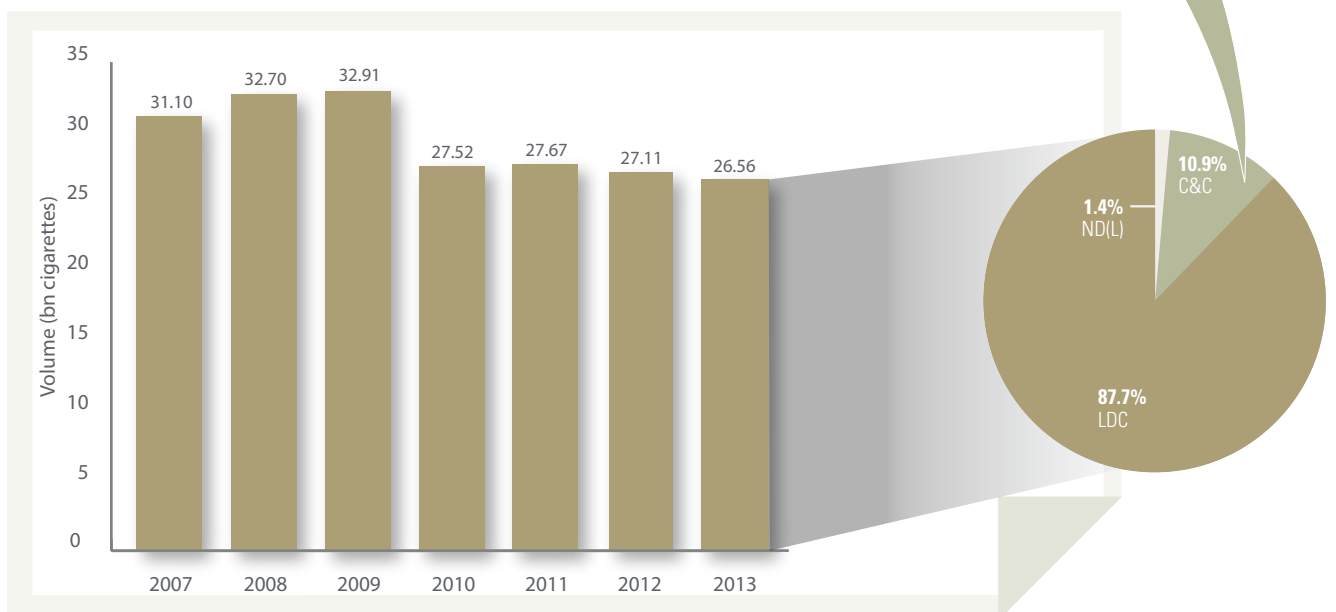


ROMANIA

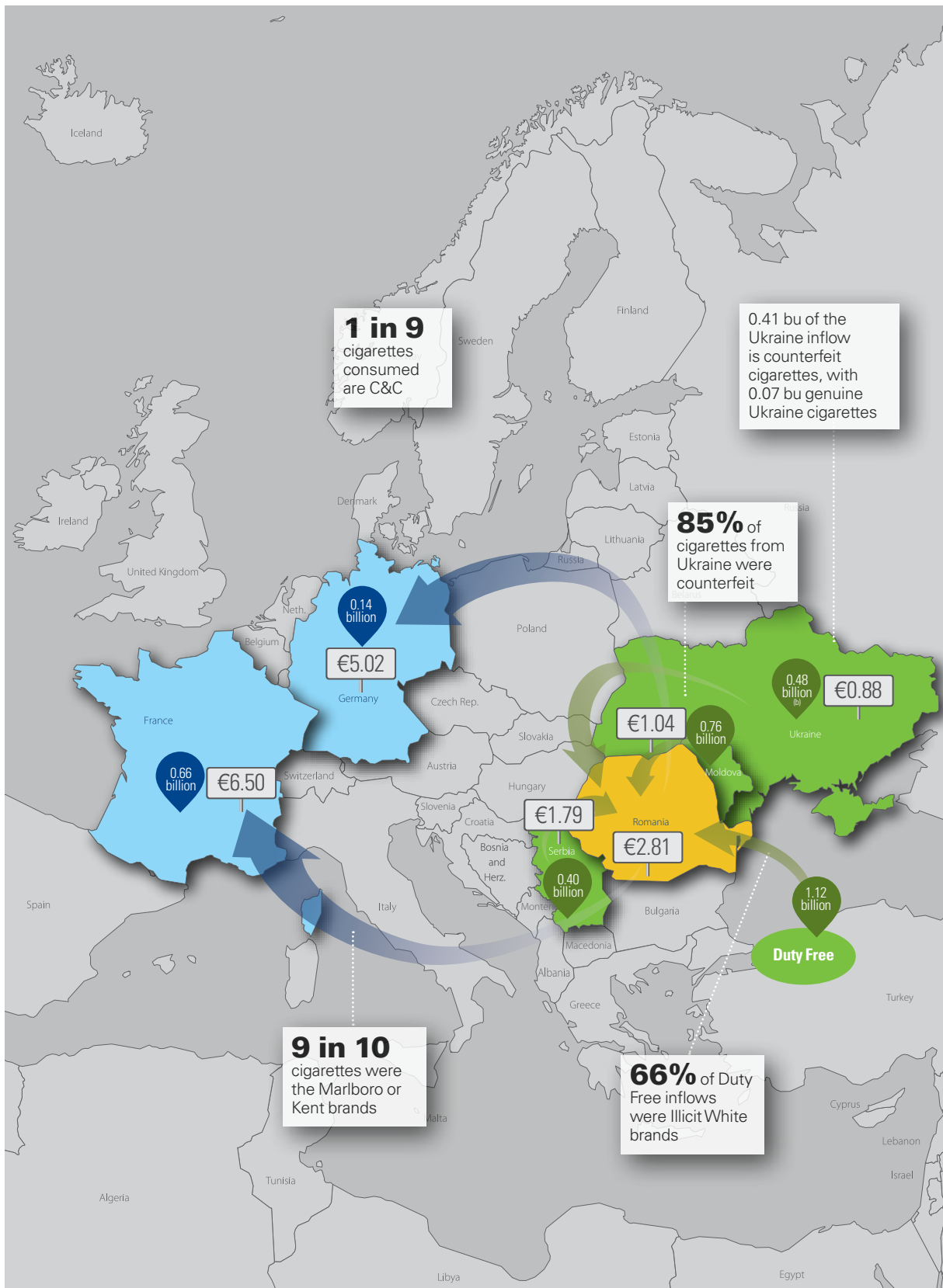


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Manufactured cigarette consumption 2007-2013



MANUFACTURED CIGARETTE CONSUMPTION



ROMANIA



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Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow. (b) 0.41bn of the Ukrainian inflow is counterfeit cigarettes, with 0.07bn genuine Ukrainian cigarette.

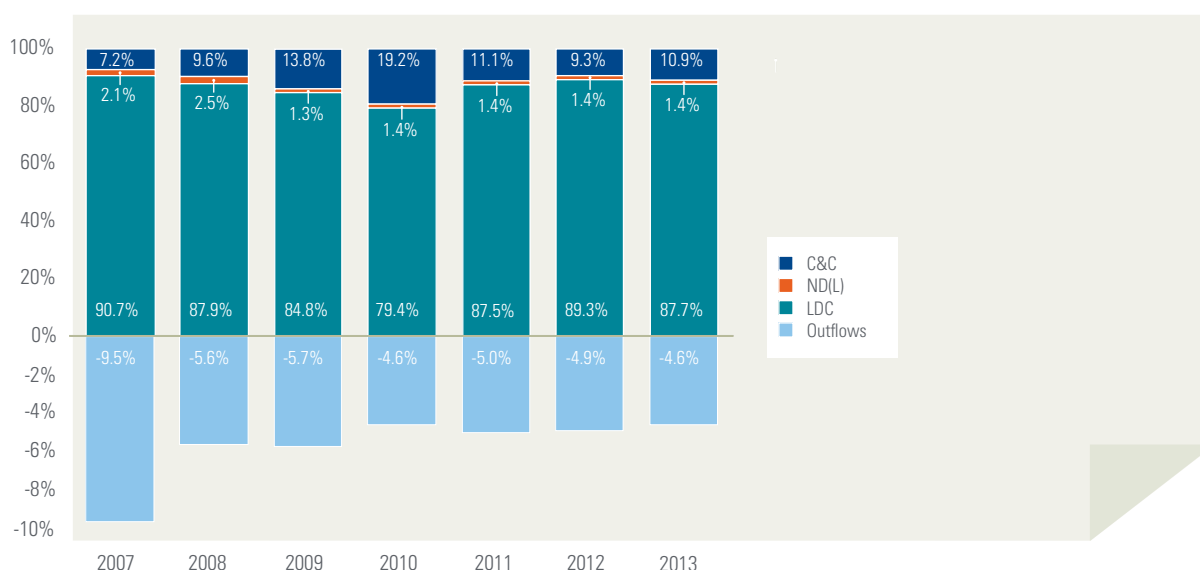
Source: (1) KPMG EU Flows Model.

Overall consumption declined but C&C slightly increased

Total manufactured cigarette consumption – Romania^{(1)(2)(3)(a)}

TOTAL ROMANIA CONSUMPTION								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	31.15	30.57	29.81	23.10	25.58	25.54	24.49	(4)%
Outflows	-2.94	-1.83	-1.89	-1.26	-1.37	-1.33	-1.21	(9)%
Legal domestic consumption (LDC)	28.21	28.75	27.92	21.84	24.21	24.21	23.28	(4)%
Non-domestic legal (ND(L))	0.66	0.82	0.44	0.38	0.38	0.38	0.38	0%
Counterfeit and contraband (C&C)	2.22	3.13	4.55	5.30	3.08	2.52	2.90	15%
Total non-domestic	2.89	3.95	4.99	5.67	3.46	2.90	3.27	13%
Total consumption	31.10	32.70	32.91	27.52	27.67	27.11	26.56	(2)%

Share of Romania cigarette consumption by type 2007-2013⁽¹⁾⁽²⁾⁽³⁾



Manufactured cigarette consumption fell by 2% in 2013, with a 4% fall in legal domestic sales (LDS) partially offset by a 13% increase in non-domestic consumption

- Economic conditions in Romania are relatively positive; unemployment has remained largely flat, moving from 5.6% to 5.7% between 2012 and 2013, while average PDI has risen by 9%⁽⁴⁾⁽⁵⁾
- However, legal domestic sales (LDS) volumes are likely to have been impacted by a 17.2% WAP rise in 2013.⁽⁶⁾ This may also have encouraged some consumers to seek out cheaper alternatives to their usual brands

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Independent agency Empty Pack Surveys, 2006 – 2013. (4) Euromonitor Passport. The Economist Intelligence Unit. (6) EU Commission WAP tables.



InfloWS increased in 2013 mainly driven by higher volumes of Illicit Whites with Duty Free and Unspecified labelling

Total inflows by country of origin 2007-2013^{(1)(2)(3)(a)}

ND INFLOWS TO ROMANIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	1.29	0.76	1.23	0.93	0.65	0.46	1.12	>100%
Moldova	0.60	1.64	2.01	1.90	1.10	0.95	0.76	(20)%
Serbia	0.02	0.01	0.07	0.95	0.75	0.69	0.40	(41)%
Unspecified	0.00	0.00	0.35	0.34	0.12	0.16	0.29	80%
Ukraine	0.90	1.36	0.98	1.07	0.59	0.55	0.07	(88)%
Counterfeit							0.47	n/a
Other	0.09	0.18	0.34	0.47	0.25	0.10	0.16	55%
Total inflows	2.89	3.95	4.99	5.67	3.46	2.90	3.27	13%

Jin Ling is the major Illicit White brand marked as Duty Free. This brand accounts for 53% of the Duty Free total

Others total includes volumes from Belarus and Italy

0.41bn cigarettes marked as counterfeit are from Ukraine

Non-domestic inflows to Romania rose by 13% in 2013. This increase is largely driven by Illicit Whites with Duty Free labelling

- Price differentials between Romania and its non-EU bordering countries are high, with the cheaper markets of Moldova, Ukraine and Serbia the main sources of non-domestic product
- Ukraine is a major source of counterfeit packs, accounting for almost 90% of all counterfeit packs found in the EPS survey

Total outflows by destination country 2007-2013⁽¹⁾⁽²⁾⁽³⁾

OUTFLOWS FROM ROMANIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
France	1.30	0.61	0.62	0.32	0.57	0.62	0.66	6%
Germany	0.09	0.11	0.10	0.10	0.10	0.14	0.14	(2)%
Ireland	0.12	0.10	0.08	0.05	0.06	0.10	0.09	(8)%
Italy	0.68	0.29	0.51	0.18	0.12	0.09	0.09	(5)%
UK	0.14	0.25	0.30	0.37	0.32	0.19	0.05	(73)%
Belgium	0.03	0.01	0.10	0.03	0.03	0.06	0.03	(44)%
Other	0.59	0.46	0.19	0.21	0.18	0.13	0.15	23%
Total outflows	2.94	1.83	1.89	1.26	1.38	1.33	1.21	(9)%

On a country-by-country basis, outflows from Romania have remained relatively consistent, with an overall fall of 9% largely attributable to falling volumes to the UK

- Flows to the UK have fallen despite a widening of the WAP gap in 2013 to €5.34, up from €4.88 in 2012⁽⁴⁾. This continues a long-term decline since 2010

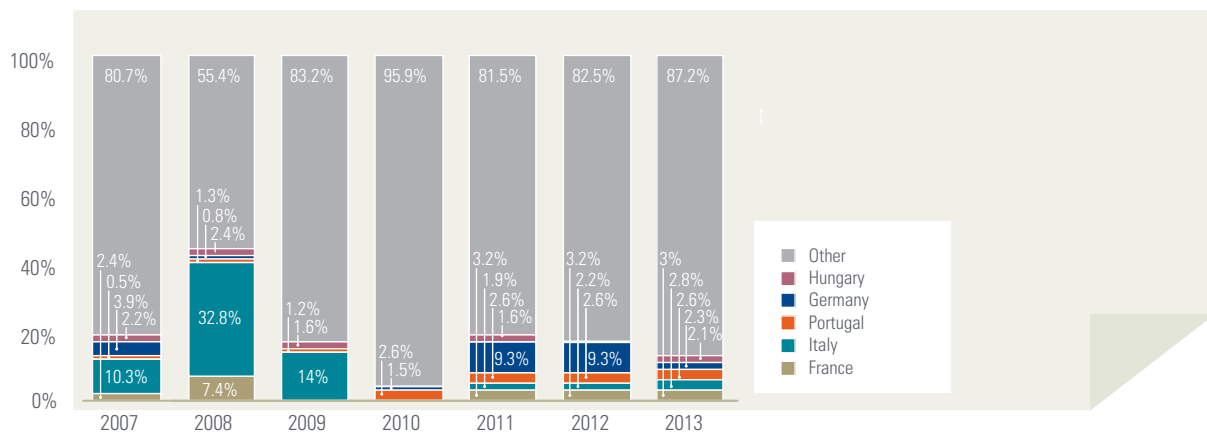
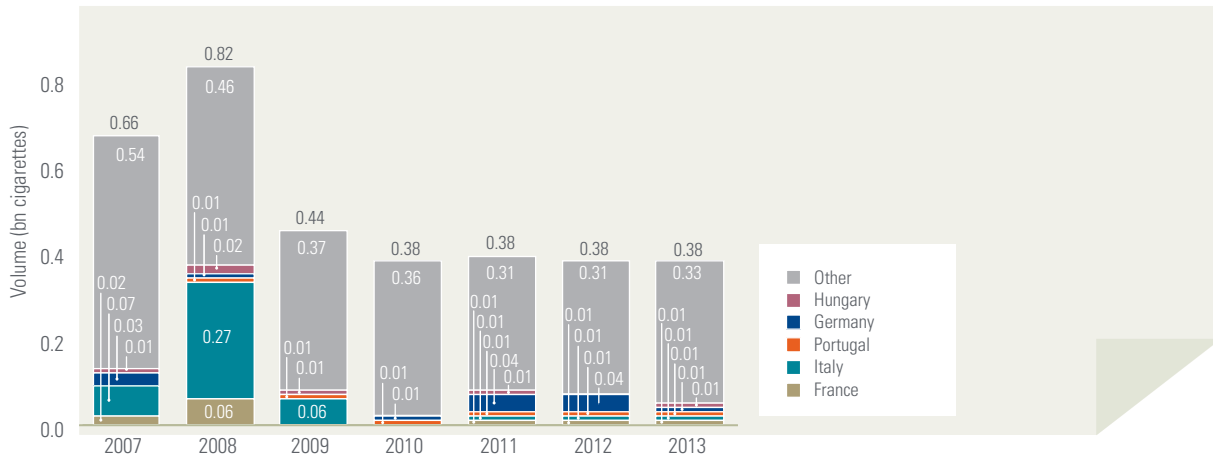
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers. (4) EU Commission WAP tables.



Non-domestic legal volumes remained low

ND(L) by origin - 2007-2013^{(1)(2)(3)(a)(b)}



ROMANIA



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Major non-domestic legal flows originate in popular travel destinations

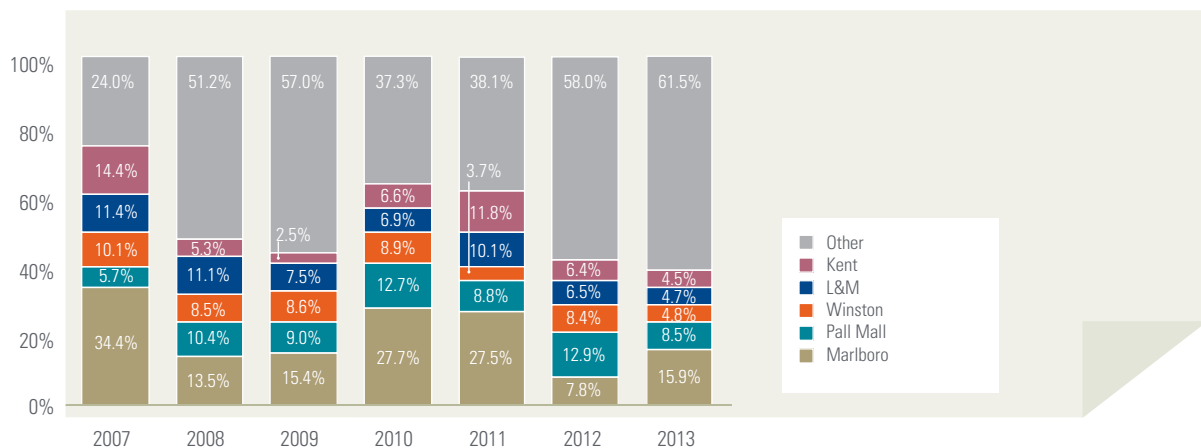
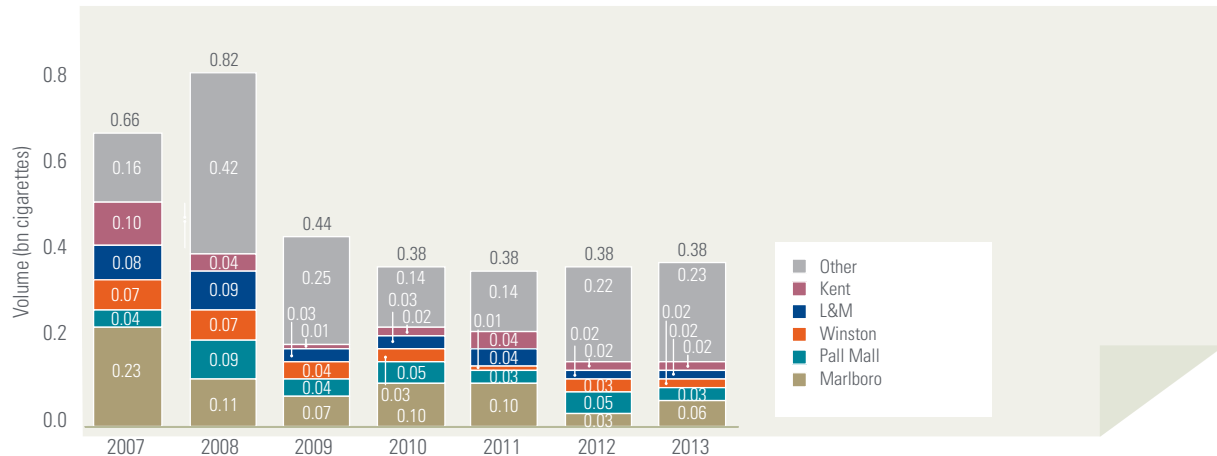
- The main ND(L) source countries are popular travel destinations such as France, Italy, Portugal, Germany and Hungary. As these are higher or similarly priced markets 100% of the inflows are considered to be legal
- Although the majority of non-domestic cigarettes originate from Moldova and Serbia, ND(L) consumer research shows that travel to these areas is relatively low. Both the number of trips and number of packs brought back legally were low compared with the total non-domestic inflows identified, therefore these are to be considered as illicit inflows

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

Total ND(L) by brand 2007-2013^{(1)(2)(3)(a)}



Marlboro continues to be the most prevalent legally purchased non-domestic brand

- Popular travel destinations in Western Europe, such as France, Germany, Italy, Portugal and the UK are the sources of 58% of this inflow

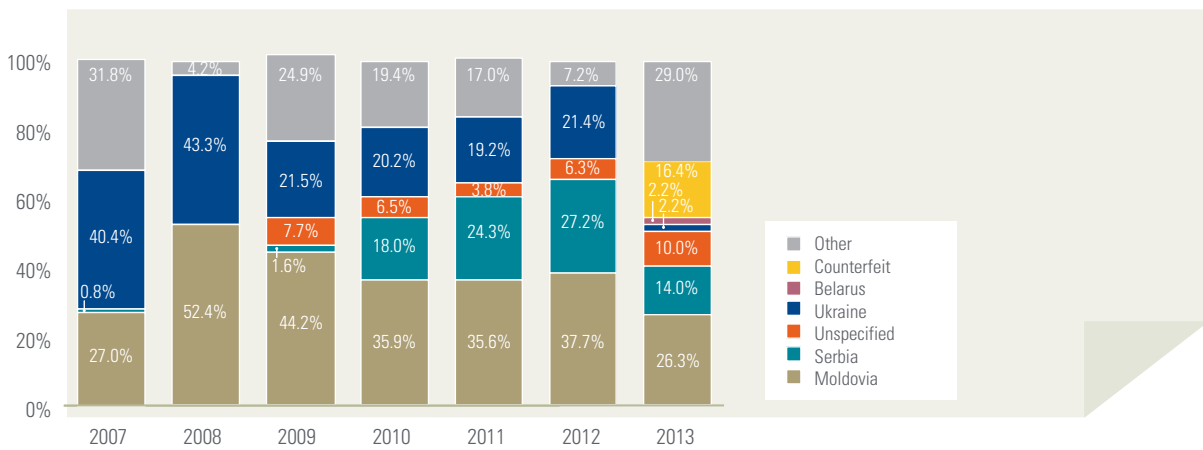
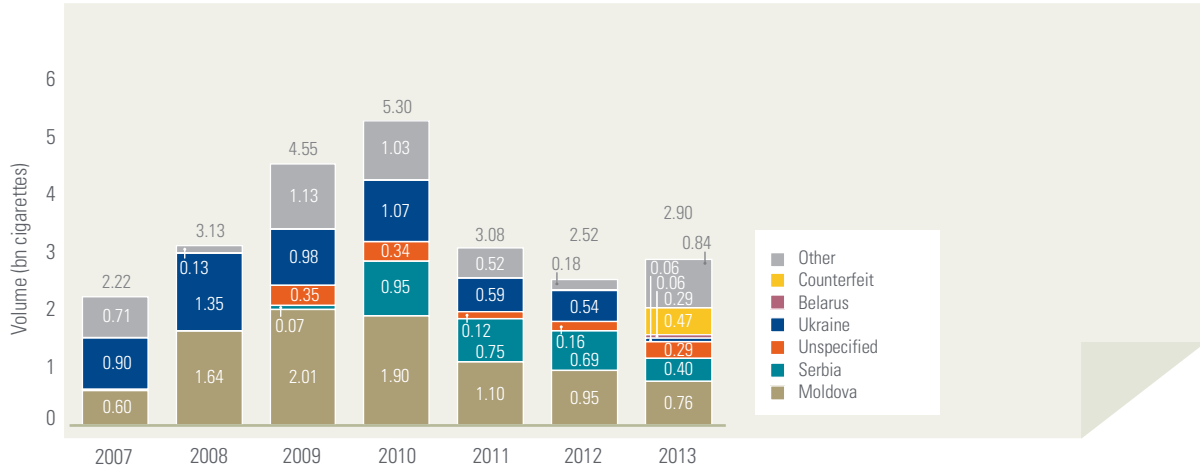
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



Moldovan and Serbian C&C volumes are declining, and being replaced with Illicit Whites bearing Duty Free or unspecified markings

Total C&C by origin 2007-2013^{(1)(2)(3)(a)}



ROMANIA



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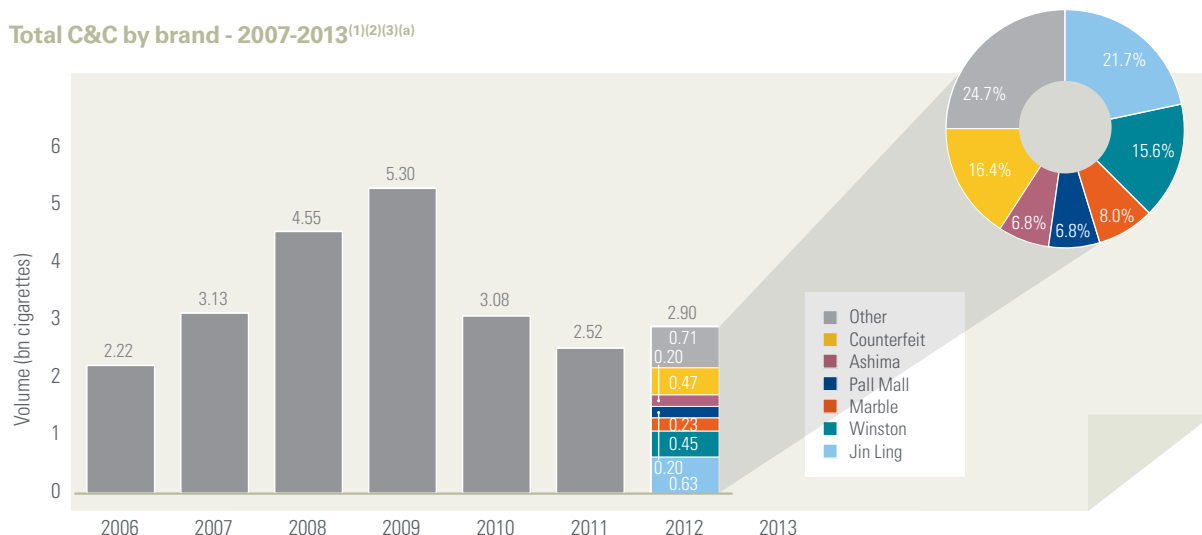
Total C&C in Romania increased by 15% between 2012 and 2013, driven by an increase in Illicit White brands marked as Duty Free and unspecified labelling. Ukraine is driving counterfeit volumes

- Analysis of the ND(L) consumer research and travel and purchasing patterns show that less than 1% of the flows from Moldova and Serbia are legal. The remaining flows are therefore classified as contraband, representing 40% of total C&C consumption in Romania
- Counterfeit volumes are significant in Romania, at 16% of total C&C volumes. 87% of the counterfeit packs collected bore Ukrainian labelling, with the most counterfeited brand being Viceroy
- Ashima and Trokadero account for 82% of the packs of unspecified origin
- If the 2.89bn C&C cigarettes in 2013 had been legally purchased in Romania the tax revenue gained would have been approximately €311m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.
 Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.
 (3) KPMG analysis of data sources provided by manufacturers.

C&C INFLOWS BY BRAND

Total C&C by brand - 2007-2013 ^{(1)(2)(3)(a)}



Breakdown of Illicit Whites inflows 2007-2013 ^{(1)(3)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO ROMANIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.14	0.05	0.04	0.58	0.54	0.40	0.13	(68)%
Duty Free	0.17	0.10	0.08	0.09	0.23	0.18	0.74	>100%
Unspecified	0.00	0.00	0.13	0.21	0.08	0.02	0.05	>100%
Total Illicit Whites	0.31	0.15	0.25	0.87	0.85	0.60	0.93	54%

66% of Duty Free inflows were Illicit White brands

Illicit White volumes continue to grow, especially in brands with Duty Free and unspecified labelling

- Jin Ling is the main Illicit White marked as Duty Free, accounting for over 90% of the Duty Free Illicit White balance
- Trokadero is the dominant Illicit White marked as unspecified, accounting for 90% of the unspecified Illicit White balance
- Fast from Serbia and Fest from Belarus contribute 75% of the country specific Illicit Whites
- Counterfeit packs bore Ukrainian labelling

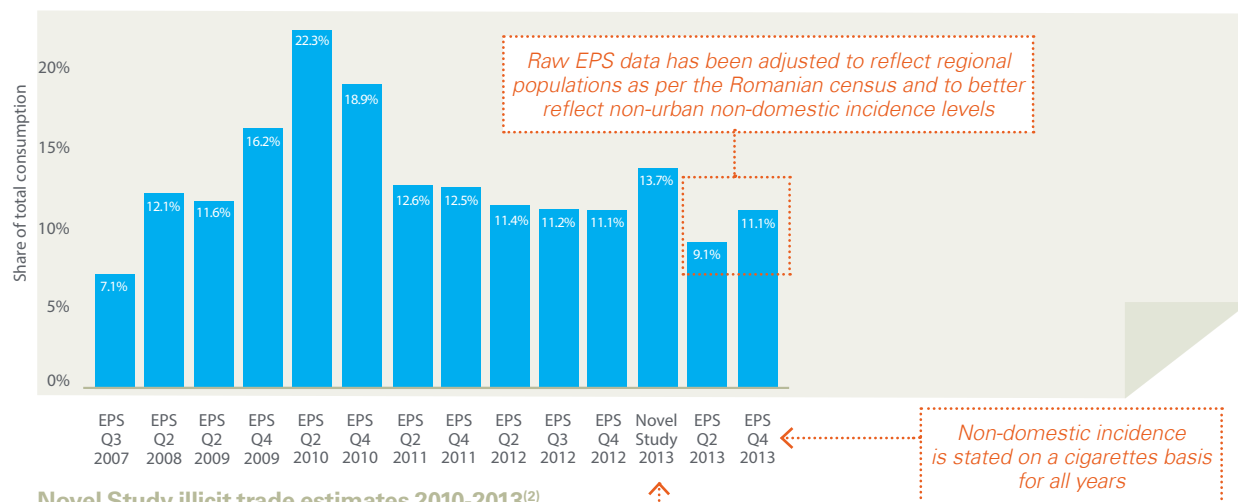
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

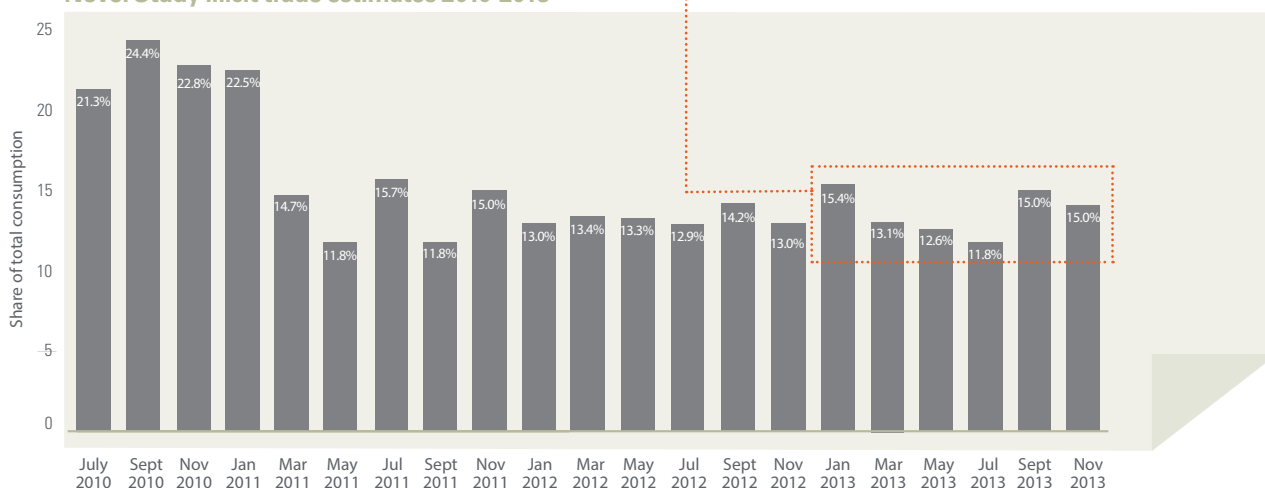


EPS results, Novel survey results and EU flows model

Empty Pack Survey non-domestic estimates - 2007-2013⁽¹⁾



Novel Study illicit trade estimates 2010-2013⁽²⁾



EPS has shown a marked decline in non-domestic incidence since 2010. In 2013 additional data sources have been used to support and refine the EPS data collected

- The empty pack survey in Romania collected 18,600 packs during the second and fourth quarters of the year. It collects these packs across 47 towns and cities. The number of packs collected in the town or city is weighted by its population
- An adjustment was made to align the regional populations sampled in the EPS with that of the latest Romanian census results (2011). This resulted in an increase in weighting of the Central, South West, North East and South regions, and a decrease in the Bucharest, South East North West and West regions⁽³⁾
 - This population re-weighting is consistent with the approach taken in 2012
- The Novel Illicit Trade Tracking Study is an additional source of non-domestic incidence data in Romania. It is a household interview programme that sampled over 15,000 respondents in 150 statistically representative rural and urban areas in 2013
 - EPS data has been compared with the Novel study, noting that most of the discrepancy between the two is due to large variances between the results in the Western and North West regions, possibly as a result of the EPS study's reliance on sampling within urban areas only. The Western and North West regions of the EPS were therefore adjusted upwards to reflect the lack of rural coverage in the EPS. This increased non-domestic incidence in Romania from 9.9% to 12.3%

Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013. (2) Novel Illicit Trade Tracking Study, November 2013. (3) Romanian Census Results, 2011.



Non-domestic legal volumes calculations and explanations

KPMG non domestic legal flows Romania

KPMG NON DOMESTIC LEGAL FLOWS ROMANIA ^(a)			
Countries where ND(L) is 100% of total			
Country	ND 2013 ⁽¹⁾	2013 ND(L) (bn sticks) ⁽²⁾	% of ND
France	0.01	0.01	100%
Italy	0.01	0.01	100%
Germany	0.01	0.01	100%
Hungary	0.01	0.01	100%

Consumer research is used to calculate the ND(L) element of the inflow to Romania.

- For France, Italy, Germany and Hungary there were significant outbound tourist flows from Romania. This is consistent with their status as popular holiday destinations. Total travel volumes and packs purchased were such that 100% of the inflow from these countries are considered legal

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. 2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.

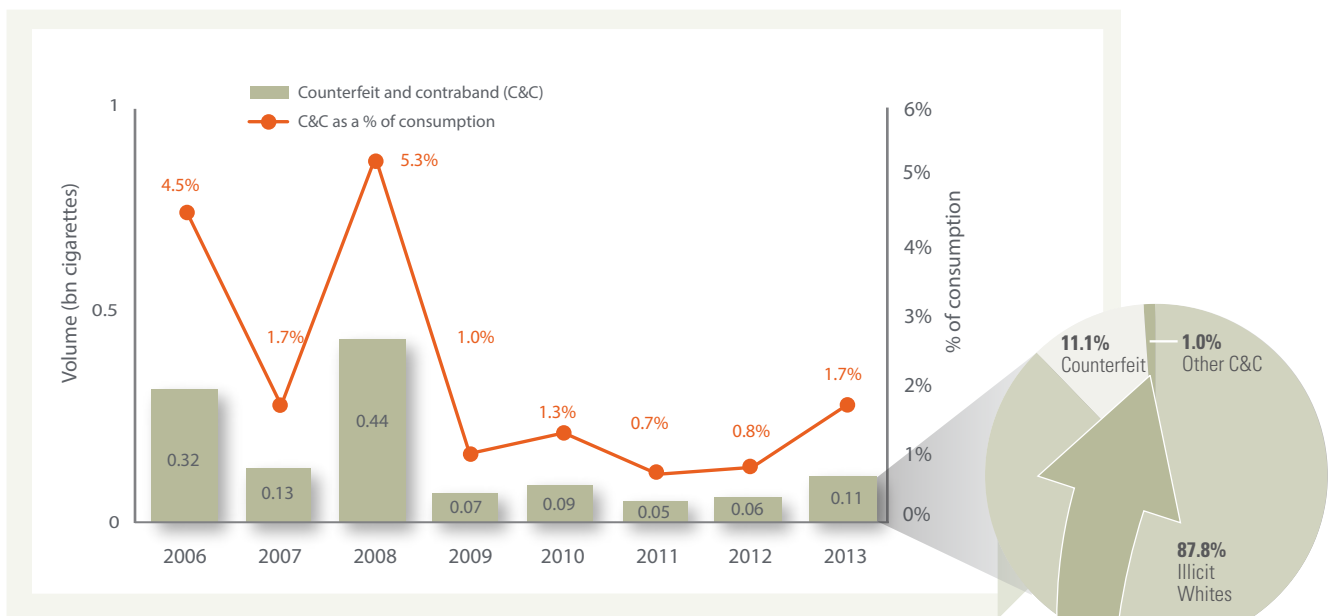


SLOVAKIA



Counterfeit and contraband volumes are low as a share of overall consumption and broadly equal to non-domestic legal inflows

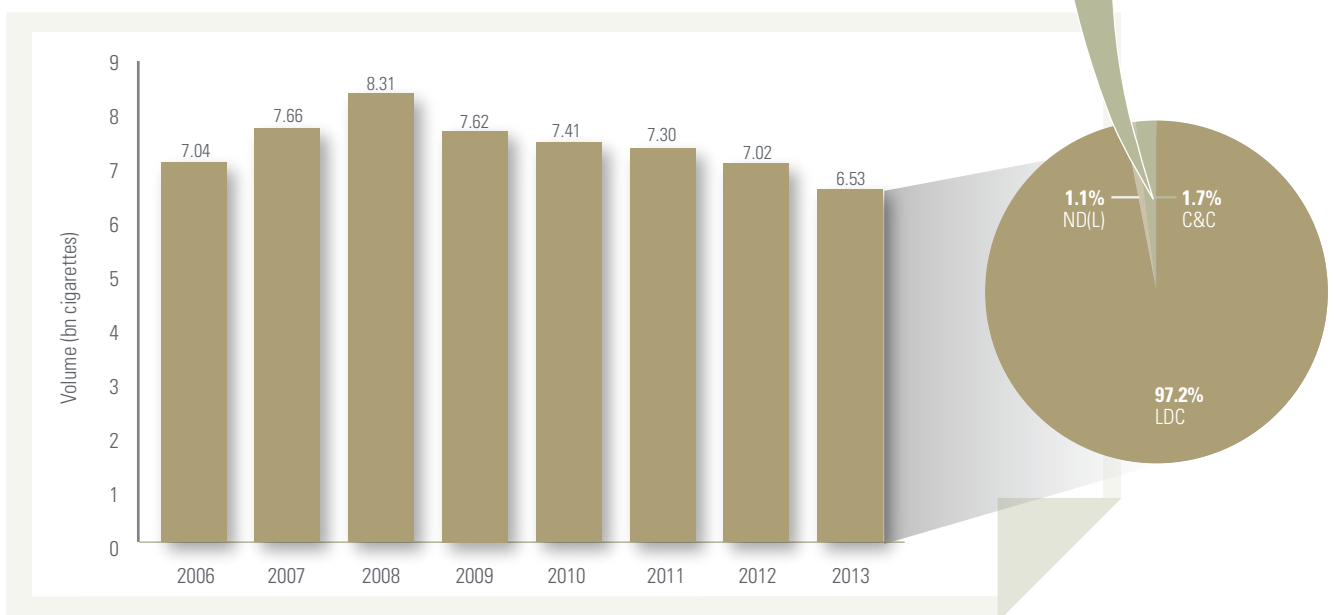
Manufactured cigarette C&C volumes and share of overall consumption 2006-13



SLOVAKIA

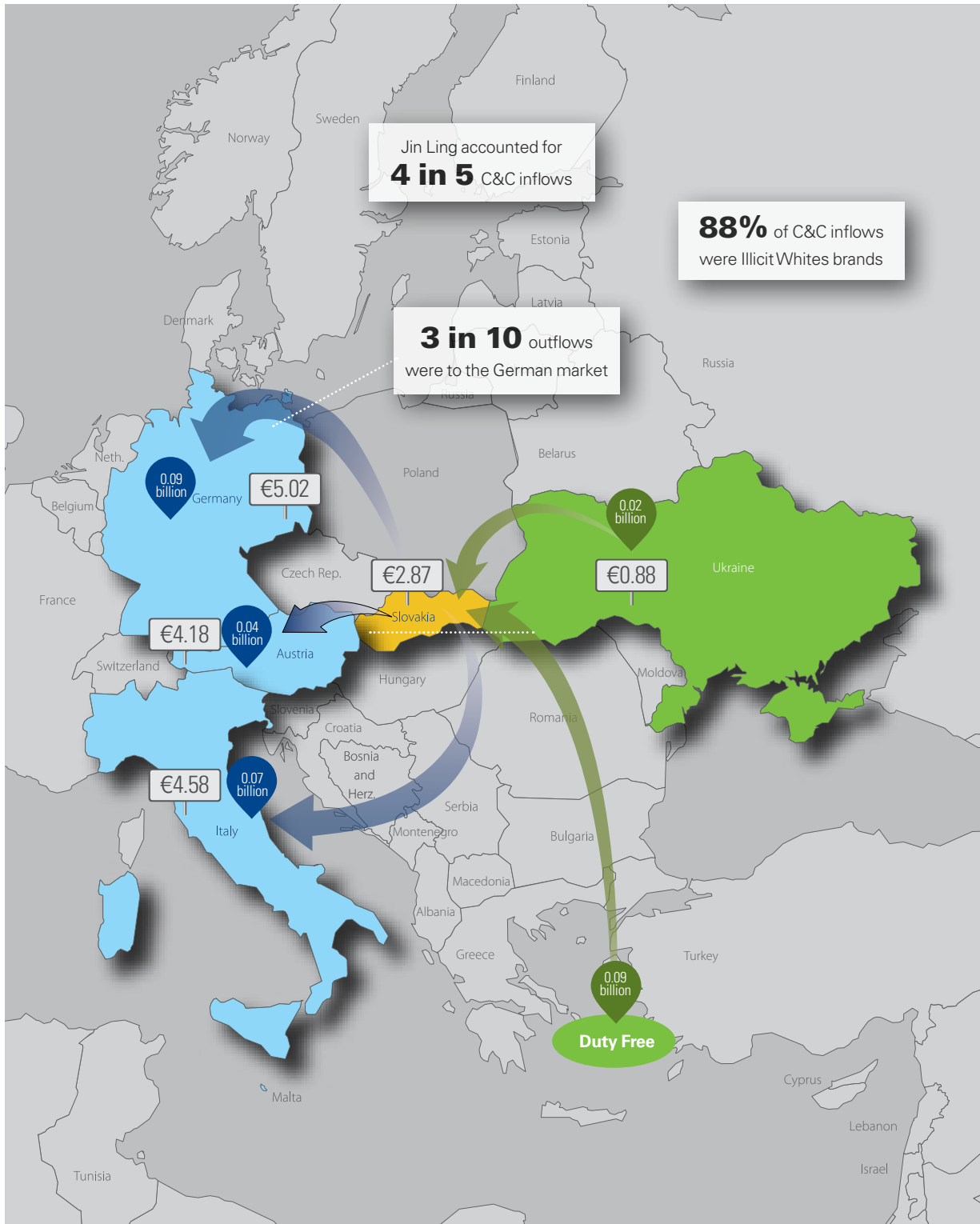


Manufactured cigarette consumption 2006-13



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KEY INFLOWS AND OUTFLOWS



SLOVAKIA



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Main outflow 
 Main inflow 

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

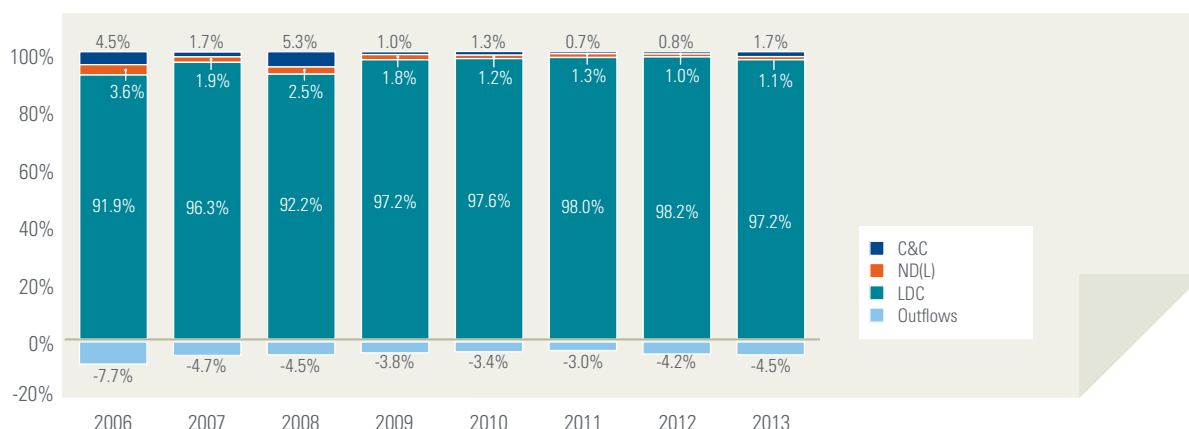
Source: (1) KPMG EU Flows Model.

Overall consumption declined but counterfeit and contraband increased

Total manufactured cigarette consumption – Slovakia^{(1)(2)(3)(a)}

TOTAL SLOVAKIA CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	7.01	7.74	8.03	7.69	7.48	7.36	7.19	6.64	(78)%
Outflows	-0.54	-0.36	-0.37	-0.29	-0.25	-0.22	-0.29	-0.29	(0)%
Legal domestic consumption (LDC)	6.47	7.38	7.66	7.40	7.23	7.15	6.89	6.35	(8)%
Non-domestic legal (ND(L))	0.25	0.15	0.21	0.14	0.09	0.10	0.07	0.07	2%
Counterfeit and contraband (C&C)	0.32	0.13	0.44	0.07	0.09	0.05	0.06	0.11	96%
Total non-domestic	0.57	0.28	0.65	0.21	0.18	0.15	0.13	0.18	44%
Total consumption	7.04	7.66	8.31	7.62	7.41	7.30	7.02	6.53	(7)%

Share of Slovakia manufactured cigarette consumption by type⁽¹⁾⁽²⁾ - 2006-2013



SLOVAKIA



PROJECT SUN

Legal domestic sales (LDS) in Slovakia declined by 7.6% in 2013, driven by an accelerated reduction in the consumption of manufactured cigarettes

- The Slovakian cigarette market experienced a 5.7%⁽³⁾ increase in WAP during the year, up from €2.72 per 20 cigarettes in January to €2.87 in July 2013
- The economic environment remained uncertain:
 - Unemployment increased from 13.6% to 14.1%⁽⁴⁾ and may have encouraged some consumers to purchase cheaper cigarettes from neighbouring Eastern European markets, as the market experienced an increase in overall NDI
 - However, GDP per capita increased in 2013 from €12.9k to €13.6k, whilst there was also a marginal increase in PDI per capita of 1.8% versus 2012⁽⁵⁾

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) EC Excise Duty tables (Part III – Manufactured Tobacco). (4) 2014 Economist Intelligence Unit. (5) Euromonitor, downloaded January 2014.

InfloWS increased in 2013 mainly driven by higher volumes of Illicit Whites with Duty Free and unspecified labelling

Total inflows by country of origin 2006-2013^{(1)(a)}

ND INFLOWS TO SLOVAKIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	0.04	0.02	0.03	0.00	0.02	0.01	0.07	0.09	31%
Ukraine	0.29	0.15	0.39	0.08	0.05	0.05	0.01	0.02	>100%
Czech Republic	0.04	0.05	0.08	0.04	0.02	0.02	0.01	0.02	>100%
Belarus	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.01	>100%
Hungary	0.00	0.00	0.01	0.06	0.03	0.04	0.03	0.01	(74)%
Counterfeit								0.01	n/a
Other	0.05	0.03	0.09	0.02	0.04	0.01	0.06	0.07	17%
Total inflows	0.57	0.28	0.65	0.21	0.18	0.15	0.13	0.18	44%

Non-domestic inflows to Slovakia increased in absolute terms and as a share of total consumption, however inflows continue to be low as a share of consumption in comparison to other EU markets

- The main inflows are sourced from the significantly cheaper bordering nation of Ukraine, as well as Belarus and Czech Republic, the latter of which is likely due to large tourism flows
- Duty Free flows into Slovakia increased this year, however the majority of the Duty Free inflow was comprised of Illicit Whites brands. This is discussed further on page 265

Total outflows by destination country 2006-2013⁽¹⁾

OUTFLOWS FROM SLOVAKIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Germany	0.07	0.06	0.04	0.04	0.04	0.04	0.07	0.09	33%
Italy	0.00	0.02	0.02	0.00	0.02	0.02	0.05	0.07	34%
Austria	0.08	0.06	0.06	0.04	0.03	0.04	0.04	0.04	0%
France	0.09	0.01	0.03	0.00	0.02	0.01	0.02	0.03	1%
UK	0.04	0.04	0.07	0.08	0.05	0.02	0.03	0.02	(31)%
Other	0.27	0.16	0.16	0.12	0.09	0.09	0.08	0.05	(40)%
Total outflows	0.54	0.36	0.37	0.29	0.25	0.22	0.29	0.29	(0)%

Outflows from Slovakia remained broadly constant versus prior year, although flows to both Germany and Italy increased as manufactured price differentials between the markets remained substantial

- Inflows to Germany were larger from neighbouring Poland, Czech Republic and Austria, whilst inflows to Italy from the cheaper markets of Ukraine and Belarus outweighed those from Slovakia
- Outflows to the UK, Ireland and the Czech Republic decreased during the year, offsetting much of the increase in flows to Germany and Italy

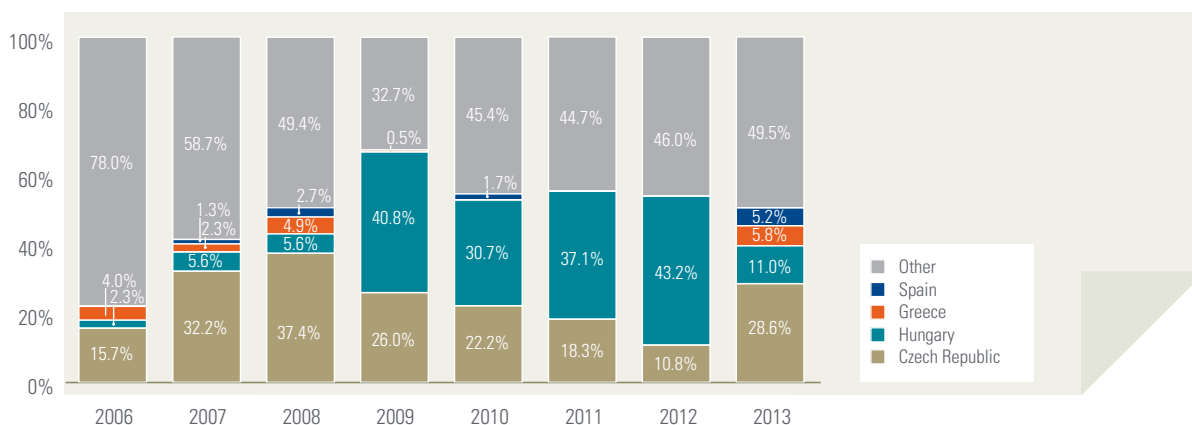
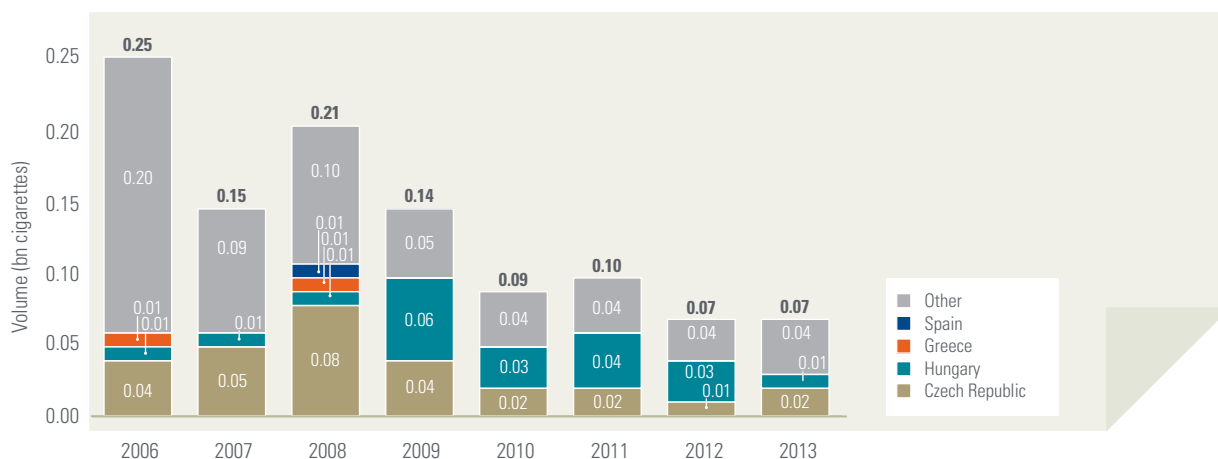
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model.



Non-domestic legal volumes remained low

ND(L) by origin - 2006-2013^{(2)(3)(a)(b)}



Overall non-domestic legal (ND(L)) inflows remained flat during the year, though there was an increase in flows from the Czech Republic during the year

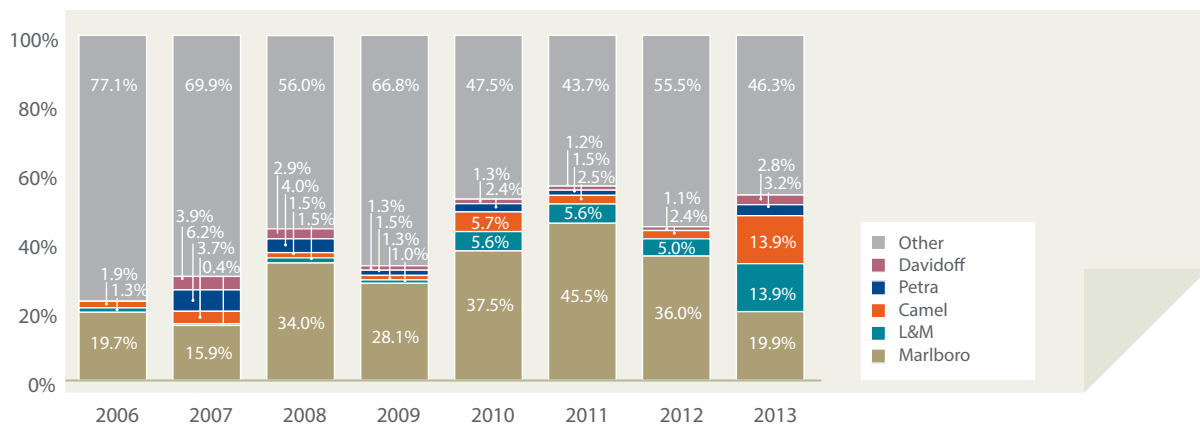
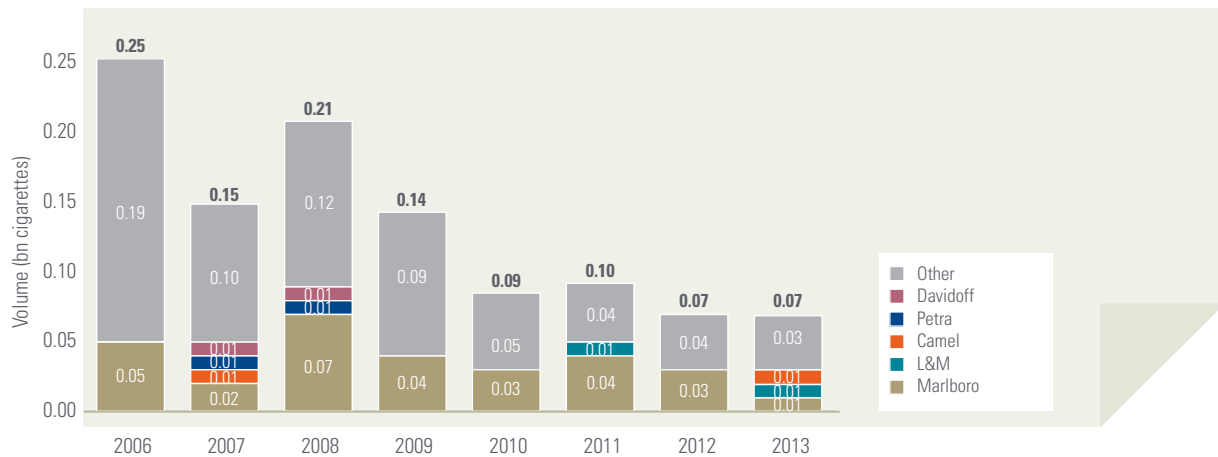
- The widening of the price differential between the two countries is likely to have been a key driver of this
- The WAP for a pack of 20 cigarettes was €2.73 in Czech Republic in 2012 versus €2.72 in Slovakia⁽³⁾. By July 2013, prices were €2.76 and €2.87 respectively, but equalised later in the year
- There was also greater outbound tourism to Czech Republic which may have increased the volume of cigarette purchases brought back into Slovakia⁽⁴⁾
- Inflows from Hungary declined in 2013, offsetting the increase from the Czech Republic. This is most likely due to substantial price increases in Hungary in the year (WAP was €2.44 per 20 cigarettes in 2012 versus to €2.93 in 2013⁽³⁾), which resulted in Hungarian cigarettes became more expensive than Slovakian product
- This is a consequence of the major regulatory changes undertaken in Hungary this year, such as the imposition of a minimum retail margin on tobacco products and the reduced number of licensed retailers

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers. (3) EC Excise Duty tables (Part III – Manufactured Tobacco). (4) UN WTO Tourism Factbook 2008-2012, UN WTO.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand - 2006-2013^{(2)(3)(a)}



There were marginal increases in legal inflows of a number of legitimate brands this year

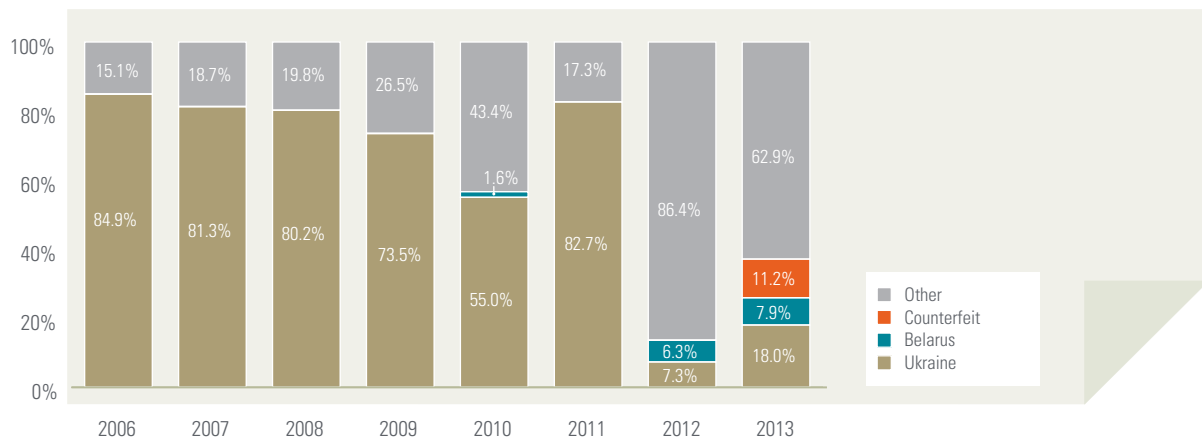
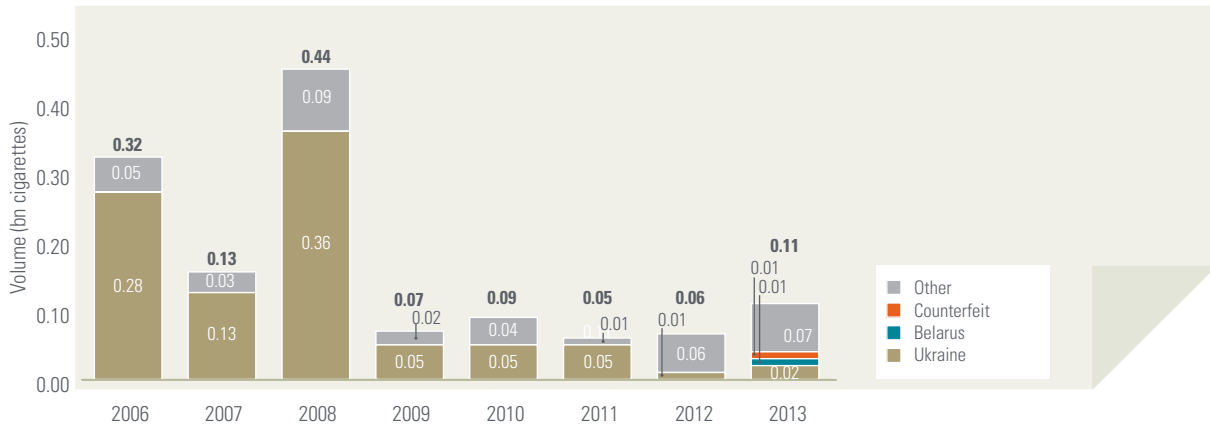
- The most significant change in ND(L) by brand was also due to the impact of the regulatory changes in Hungary, resulting in a decline in Marlboro inflows
- Other legal inflows comprise smaller volumes of over 60 brands

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

Counterfeit and contraband volumes increased in 2013

C&C by origin - 2006-2013^{(2)(3)(a)(b)}



SLOVAKIA



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Increased inflows from Ukraine and Belarus have been allocated to counterfeit and contraband (C&C) flows

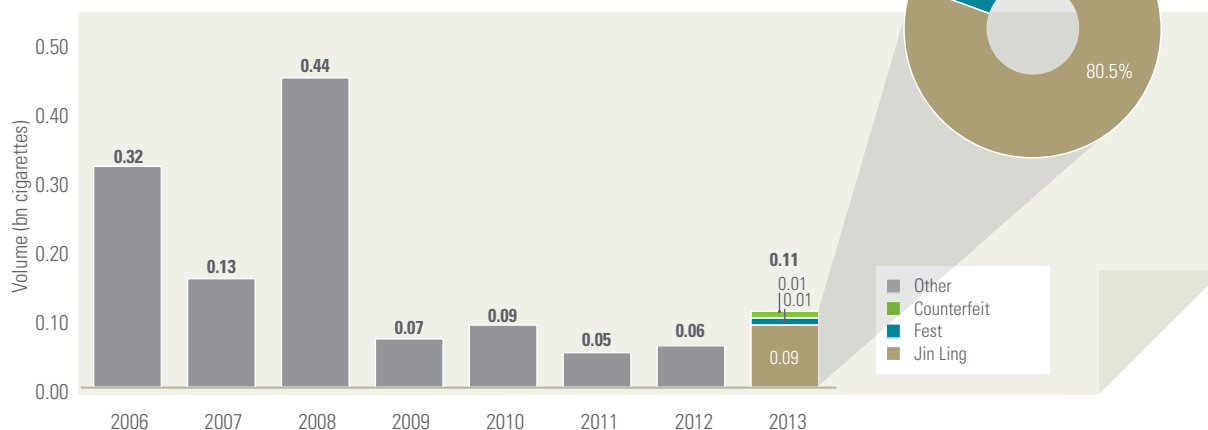
- There was a substantial decline in outbound tourism from Slovakia to Ukraine in recent years⁽³⁾ and consumer research indicates people bring back very few packs per trip on average, which suggests the majority of the inflow from Ukraine is considered as C&C
- Similarly, low outbound tourist flows also suggests that cigarette inflows from Belarus are also C&C
- If these cigarettes had been legally purchased in Slovakia the tax revenue gained would have been approximately €13m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) UNWTO Tourism Factbook 2008-2012, UNWTO. (3) Synovate/Ipsos ND(L) research 2013. (4) KPMG analysis EU Tax tables to see price increases.

C&C INFLOWS BY BRAND

C&C by brand - 2006-2013^{(2)(3)(a)(b)}



Combined Illicit Whites brands represent the majority of the total C&C inflow to Slovakia, a large proportion of which are labelled Duty Free

- Jin Ling, a major Illicit Whites brand, was the biggest overall C&C brand in Slovakia in 2013 and represents the majority Illicit Whites with Duty Free labelling as shown in the table below
- There was also a high incidence of Grodno Tobacco brands such as Fest as a result of high inflows from Belarus, representing most of the “Country specific Illicit Whites” category below

Breakdown of Illicit Whites inflows 2007-2013^{(1)(2)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO SLOVAKIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.00	0.01	0.00	0.02	0.01	0.00	0.01	>100%
Duty Free	0.00	0.00	0.00	0.00	0.00	0.04	0.09	>100%
Unspecified	0.00	0.00	0.00	0.00	0.00	0.00	0.00	n/a
Total Illicit Whites	0.00	0.01	0.00	0.03	0.01	0.04	0.10	>100%

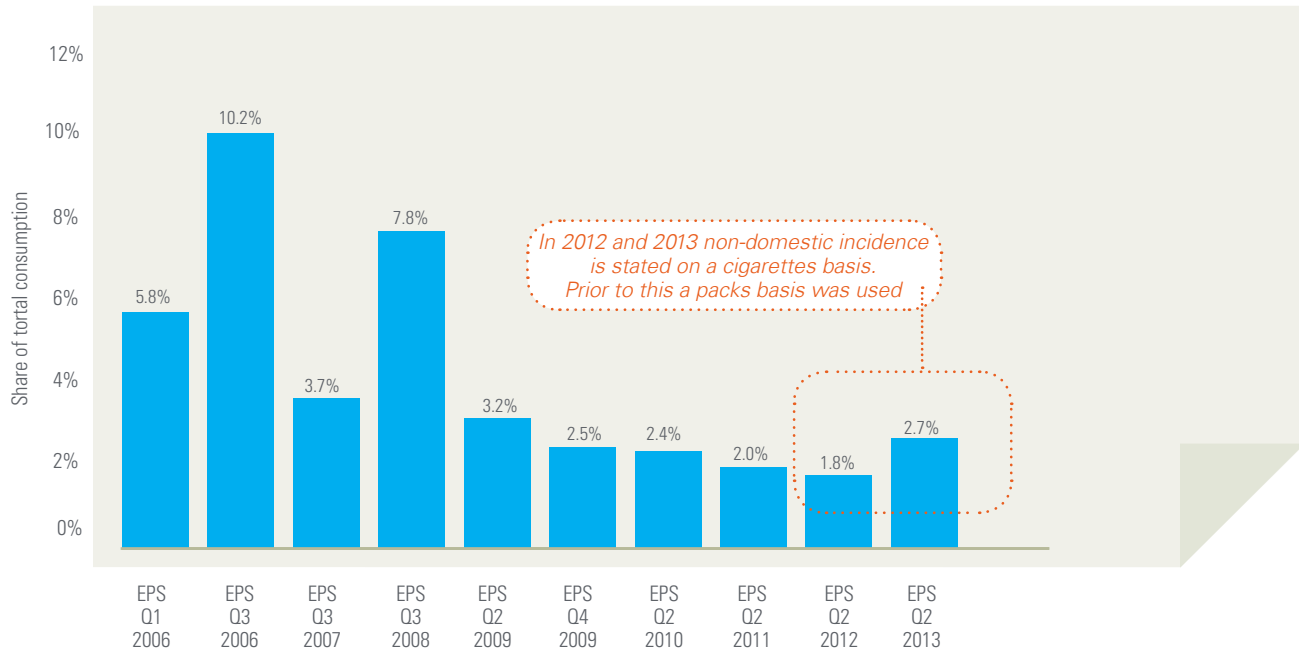
Note: (a) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



EPS results and EU flows model

Empty Pack Survey non-domestic market estimates - 2006-2013^{(1)(a)}



SLOVAKIA



- The empty pack survey (EPS) in Slovakia collected 5,000 packs during the course of the year. This was undertaken as a single wave conducted in Q2 (April). The sample focused on 25 cities and the number of packs collected in each city was weighted by the city population
- As a result of a large rural population in Slovakia (55% of the total population⁽²⁾), the EPS data was re-weighted such that the regional share of the EPS sample is more representative. This adjustment marginally increased non-domestic incidence from 2.7% to 2.8%

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Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013. (2) Euromointor, downloaded January 2014.

ND(L) legal volumes calculations and explanations

KPMG non domestic legal flows Slovakia ^{(1)(3)(b)}

KPMG NON DOMESTIC LEGAL FLOWS SLOVAKIA ^(a)			
Countries where ND(L) is 100% of total			
Country	ND 2013 ⁽¹⁾	2013 ND(L) (bn sticks)	% of ND
Czech Republic	0.02	0.02	100%
Hungary	0.01	0.01	100%

- To estimate the legal element of inflows from Czech Republic and Hungary, consumer research has been used. As this consumer research implies a legal volume greater than the total non-domestic incidence and given the materiality of each flow, these have been capped at 100% of non-domestic inflows in our analysis



Notes: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) Synovate/Ipsos ND(L) research 2013.

SLOVENIA



Counterfeit & Contraband decreased in line with total consumption

Manufactured cigarette C&C volumes and share of overall consumption 2006-13

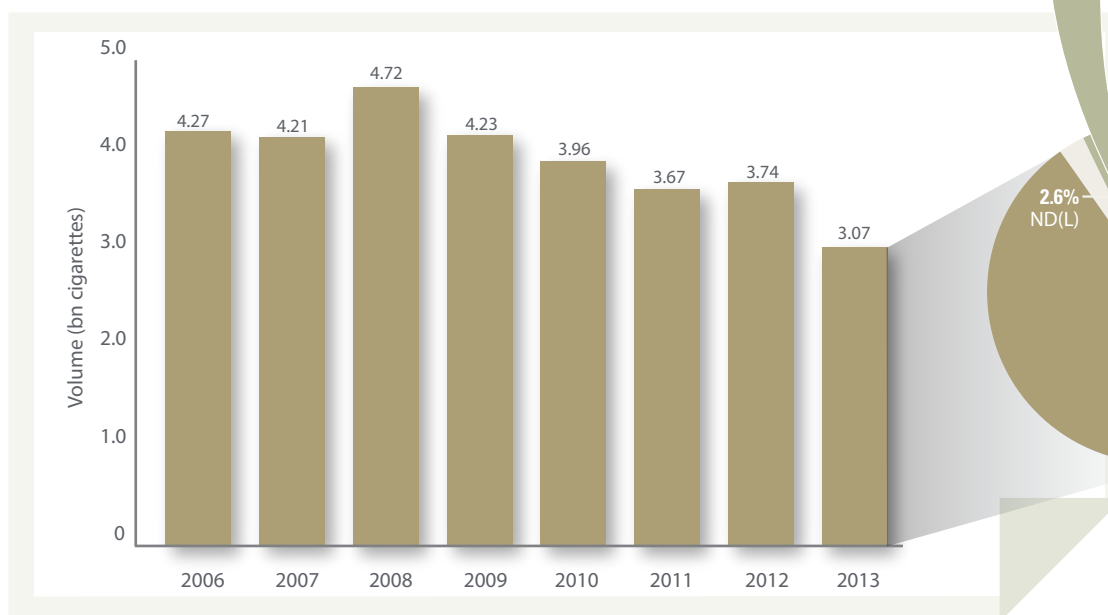


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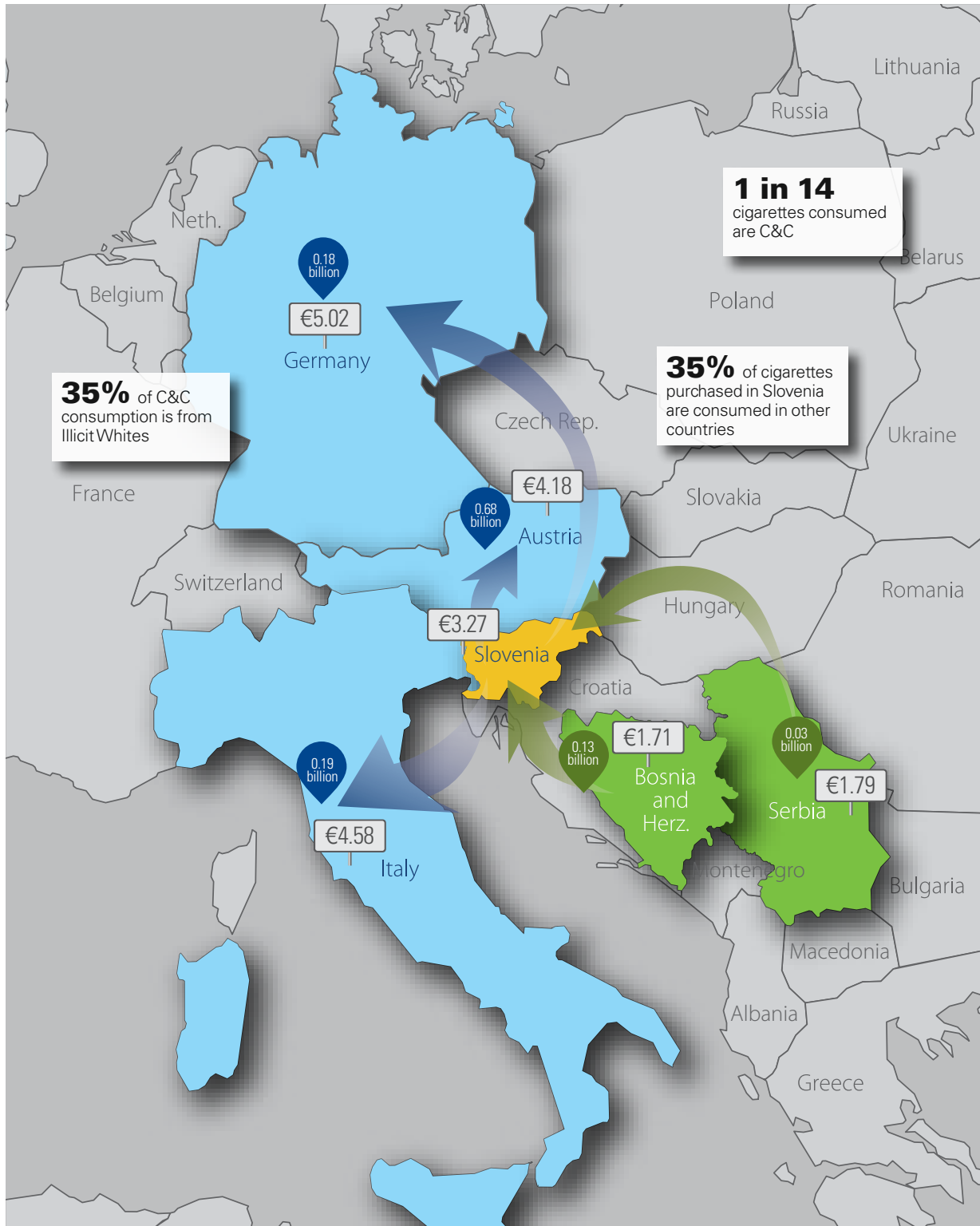


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Manufactured cigarette consumption 2006-13





KEY INFLOWS AND OUTFLOWS



SLOVENIA



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Main outflow 
Main inflow 

Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

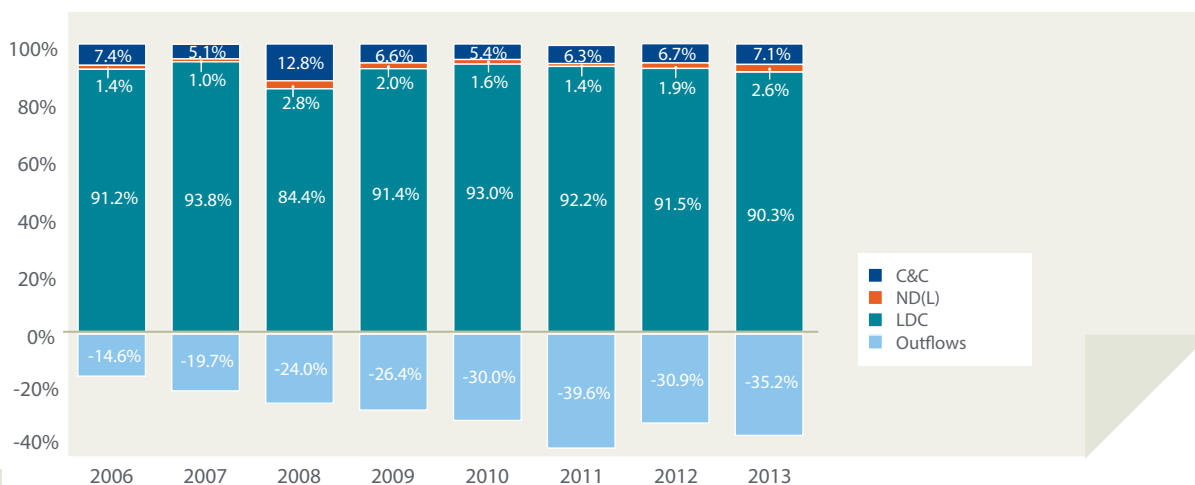
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Total consumption declined as both LDS and non-domestic volumes decreased

Total manufactured cigarette consumption – Slovenia⁽¹⁾⁽²⁾⁽³⁾

TOTAL SLOVENIA CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	4.52	4.78	5.11	4.98	4.87	4.84	4.57	3.86	(16)%
Outflows	-0.62	-0.83	-1.13	-1.11	-1.19	-1.45	-1.15	-1.08	(6)%
Legal domestic consumption (LDC)	3.90	3.95	3.98	3.86	3.68	3.39	3.42	2.77	(19)%
Non-domestic legal (ND(L))	0.06	0.04	0.13	0.08	0.06	0.05	0.07	0.08	14%
Counterfeit and contraband (C&C)	0.32	0.22	0.60	0.28	0.21	0.23	0.25	0.22	(12)%
Total non-domestic	0.38	0.26	0.74	0.36	0.28	0.29	0.32	0.30	(7)%
Total consumption	4.27	4.21	4.72	4.23	3.96	3.67	3.74	3.07	(18)%

Share of Slovenia cigarette consumption by type 2006-2013⁽¹⁾⁽²⁾⁽³⁾



Manufactured cigarette consumption fell by 18% in 2013 whilst LDS fell by 16%

- Legal domestic sales volumes are likely to have been impacted by a 10.8% WAP rise in 2013
- Economic conditions in Slovenia may also have had an adverse impact on legal sales as unemployment rose from 12% to 13% and average PDI declined by 2%⁽⁴⁾

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Independent agency Empty Pack Surveys, 2006 – 2013. (4) Euromonitor, Downloaded March 2013.

Both inflows and outflows fell in 2013

Total inflows by country of origin - 2006-2013 ^{(1)(a)}

INFLOWS TO SLOVENIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Bosnia and Herzegovina	0.15	0.12	0.44	0.26	0.16	0.19	0.19	0.13	(32)%
Serbia	0.04	0.02	0.01	0.02	0.05	0.02	0.04	0.03	(27)%
Austria	0.03	0.00	0.03	0.00	0.00	0.00	0.00	0.01	>100%
Other	0.16	0.12	0.25	0.08	0.07	0.08	0.08	0.12	56%
Total inflows	0.38	0.26	0.74	0.36	0.28	0.29	0.32	0.30	(7)%

Total inflow volumes declined by 7% in 2013, with a reduction in flows from Bosnia & Herzegovina offset by an increase in small flows from a number of other countries

- The main inflow market is Bosnia & Herzegovina which accounts for just under half of total non-domestic consumption
- More than half of the Duty Free flows which came into Slovenia in 2013 were Illicit Whites brands. The main brand sold as Illicit Whites appears to be the brand Napoli

Total outflows by destination country – 2006-2013 ⁽¹⁾

OUTFLOWS FROM SLOVENIA									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Austria	0.23	0.53	0.73	0.79	0.85	1.04	0.83	0.68	(18)%
Italy	0.06	0.14	0.19	0.13	0.09	0.21	0.10	0.19	87%
Germany	0.25	0.07	0.10	0.14	0.16	0.13	0.16	0.18	12%
Other	0.08	0.08	0.11	0.05	0.09	0.07	0.07	0.04	>100%
Total outflows	0.62	0.83	1.13	1.11	1.19	1.45	1.15	1.08	(6)%

Outflows in aggregate fell by 6%, largely driven by a large decline in outflows to Austria

- The price gap between Slovenia and Austria narrowed in 2013, reducing the WAP difference from €1.00 to €0.91. This may have led to a reduction in the incentive to smuggle cigarettes or make cross-border purchases between Austria and Slovenia, contributing to the reasons for the decline in legal domestic sales in Slovenia
- Whilst very few Slovenian packs are collected in Italy, border sales data suggests a flow of 0.19 billion cigarettes. In addition the price difference of €1.27 would indicate an incentive to purchase cigarettes across the border

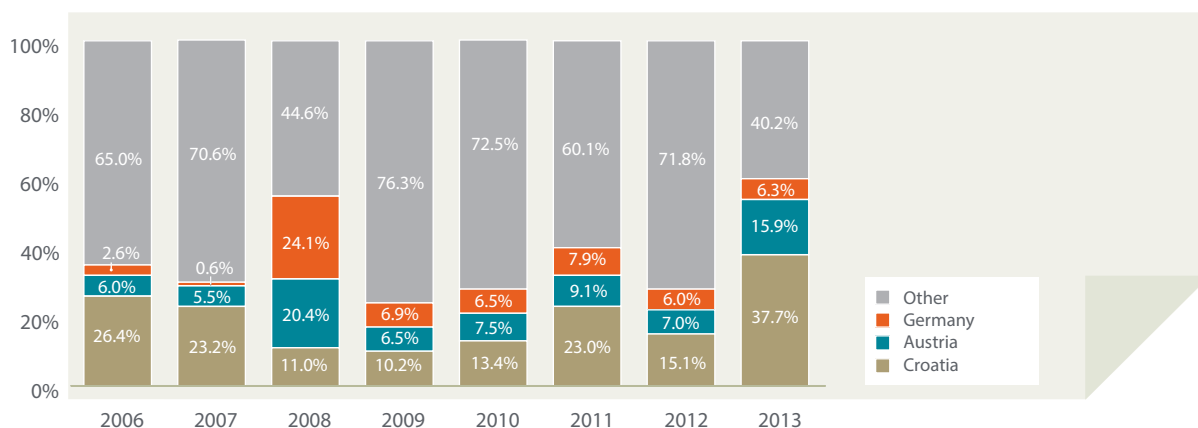
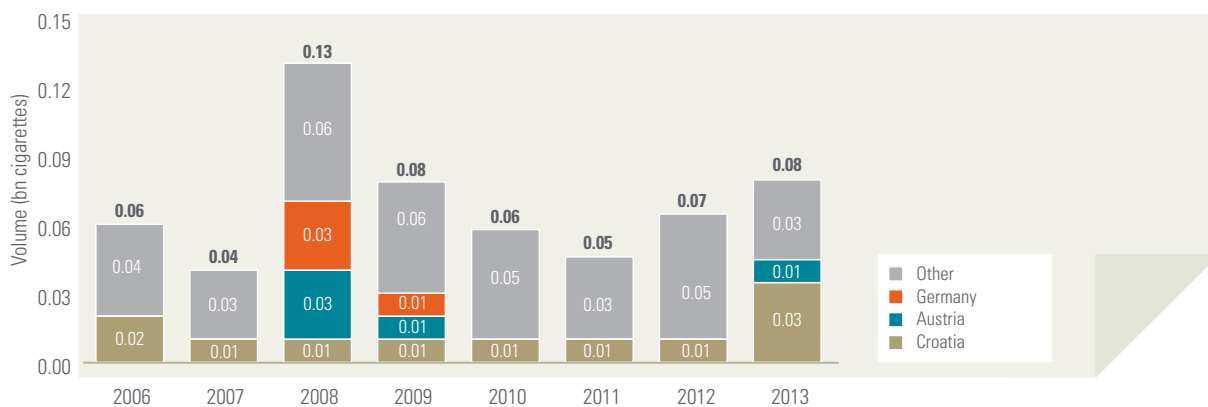
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model.



Non-domestic legal consumption grew, supported by increased tourist flows

ND(L) by origin 2006-2013^{(1)(2)(3)(a)}



SLOVENIA



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Price differentials between Slovenia and its bordering countries are generally low, resulting in low levels of flows between each country

- Croatia has the lowest WAP difference to Slovenia of €0.57 and as a result there are relatively small flows between neighbouring countries
- All product coming into Slovenia from these bordering countries has therefore been categorised as ND(L) consumption
- The largest inflows, from Bosnia & Herzegovina and Serbia are mainly C&C

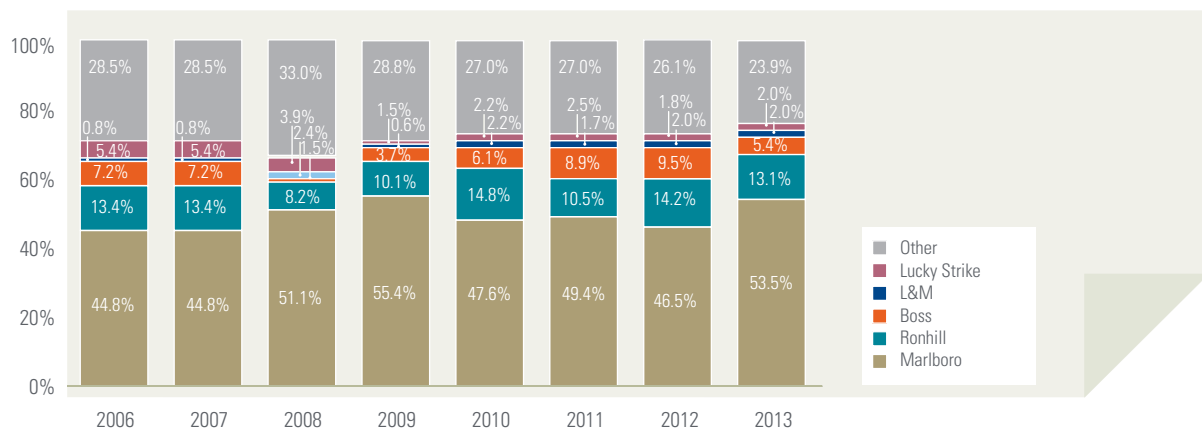
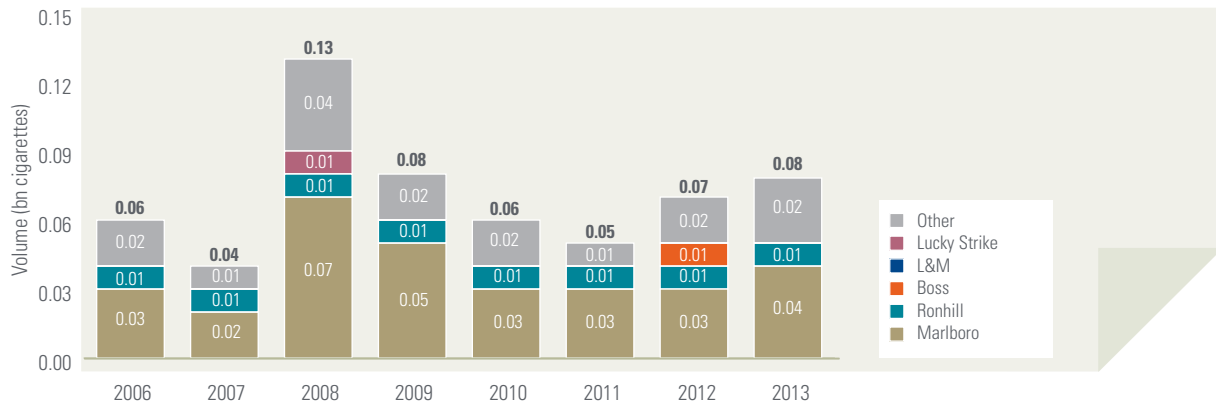
Note: (a) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.

(3) KPMG analysis of data sources provided by manufacturers.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

ND(L) by brand 2006-2013^{(1)(2)(3)(a)}



The most popular ND(L) brands remained consistent in 2013

- Marlboro continues to be the most popular brand and is typically the most purchased brand abroad as it is often the most available
- Other ND(L) brands purchased are similar to brands which are popular in Slovenia

Note: (a) Additional details of key ND(L) calculations provided overleaf.

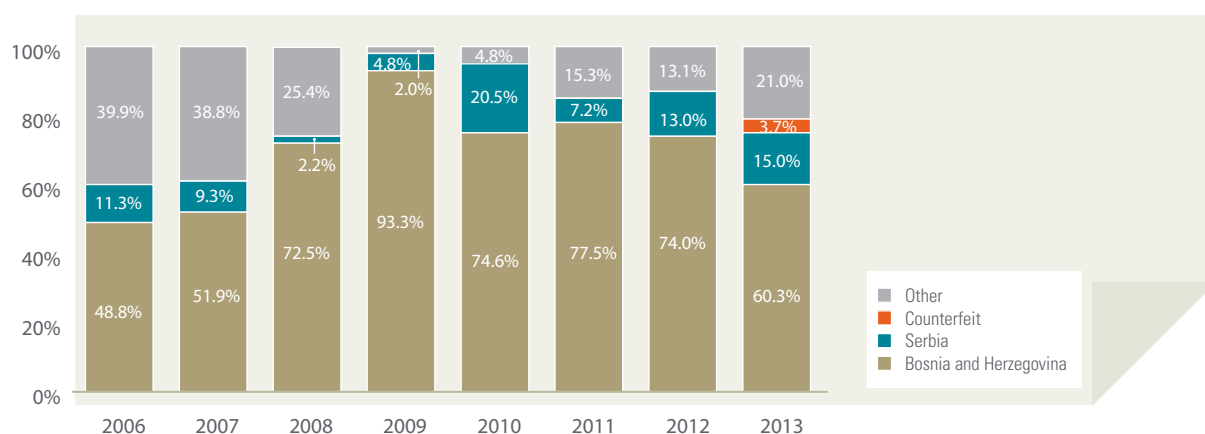
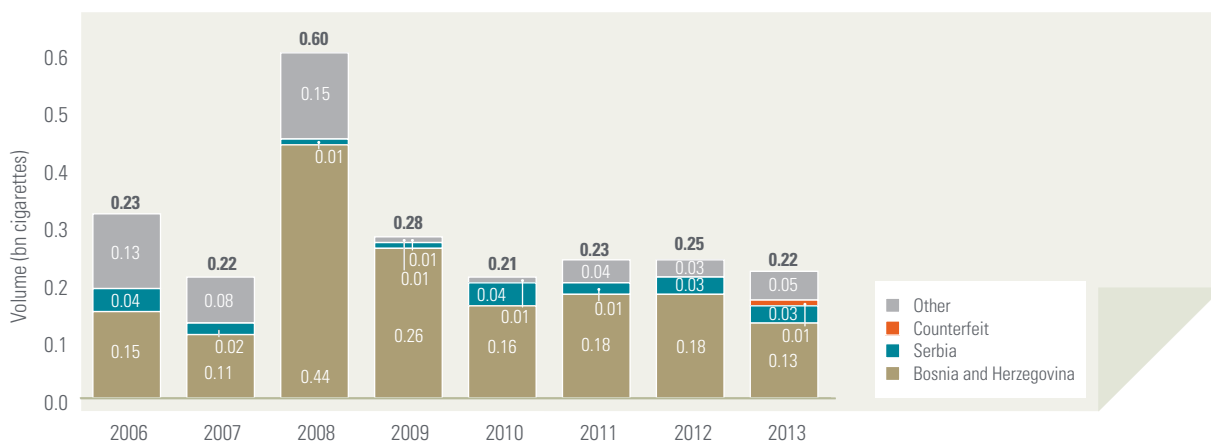
Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.

(3) KPMG analysis of data sources provided by manufacturers.



C&C decreased by 12%, driven by a decrease in flows from Bosnia & Herzegovina

Total C&C by origin 2006-2013 ^{(1)(2)(3)(a)}



SLOVENIA



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The majority of total non-domestic cigarettes originate from Bosnia & Herzegovina and Serbia with the majority assumed to be C&C

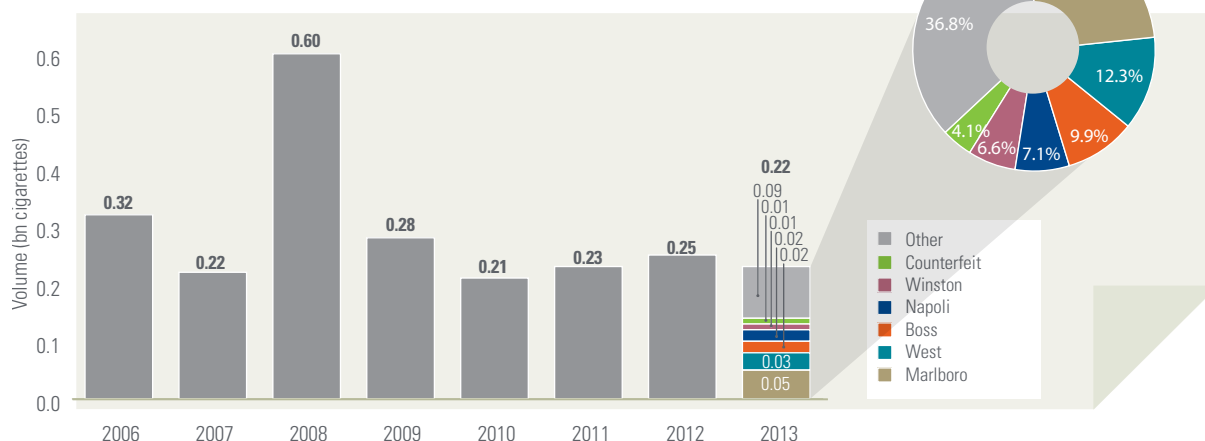
- Analysis of the consumer research and travel and purchasing patterns shows that 3% of the flows from Bosnia & Herzegovina and 12% of the flows from Serbia are legal as the number of trips and legal limits allowed do not allow further consumption
- According to tourist data, a total of 67,000 trips were made to Serbia in 2012, whilst 40,000 trips were made to Bosnia & Herzegovina. This is broadly in line with 70,000 trips to Serbia and 50,000 trips to Bosnia & Herzegovina to purchase cigarettes identified by the consumer research data
- The majority of those that travel to these countries bring back cigarettes, with the average number of packs brought back at 3 from Serbia and 4 from Bosnia & Herzegovina. This falls between the 2-pack limit for those travelling by land and the 10-pack limit for those travelling by air
- The remaining contraband identified by our analysis in Slovenia comes from other countries in the Balkans or with unspecified labelling
- If the total volume of counterfeit and contraband had been consumed legally within the Slovenian market, an additional tax revenue of approximately €27 million would have been raised by the Slovenian Treasury

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

C&C INFLOWS BY BRAND

Total C&C by brand 2006-2013 ^{(1)(2)(3)(a)}



60% of Duty Free flows to Slovenia are Illicit Whites

Breakdown of Illicit Whites by type - 2007-2013 ^{(1)(2)(a)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO SLOVENIA								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country Specific	0.033	0.049	0.031	0.030	0.020	0.011	0.023	>100%
Duty Free	0.015	0.001	0.000	0.000	0.000	0.007	0.022	>100%
Unspecified	0.000	0.000	0.000	0.000	0.000	0.004	0.001	>(100)%
Total Illicit Whites	0.048	0.051	0.031	0.030	0.020	0.022	0.046	>100%

Marlboro was the biggest contraband brand, accounting for 24% of C&C volumes, while Illicit Whites accounted for a further 21%

- The largest contraband brand was Marlboro, which mainly came from Bosnia & Herzegovina and Serbia, whilst West came predominantly from Serbia
- Illicit Whites brands made up almost one third of counterfeit and contraband consumption in Slovenia in 2013. The majority of Illicit Whites with Duty Free labelling came from the brand Napoli, manufactured by BBJ Italy, which has no legal distribution within the EU and is therefore categorised as an Illicit Whites
- A small component of Duty Free also came from Jin Ling, manufactured by the Baltic Tobacco Factory
- Illicit Whites with country specific labelling were mainly from Bosnia & Herzegovina and Kosovo, where there are many brands which are not legally sold within the European Union, including Ronhill and York

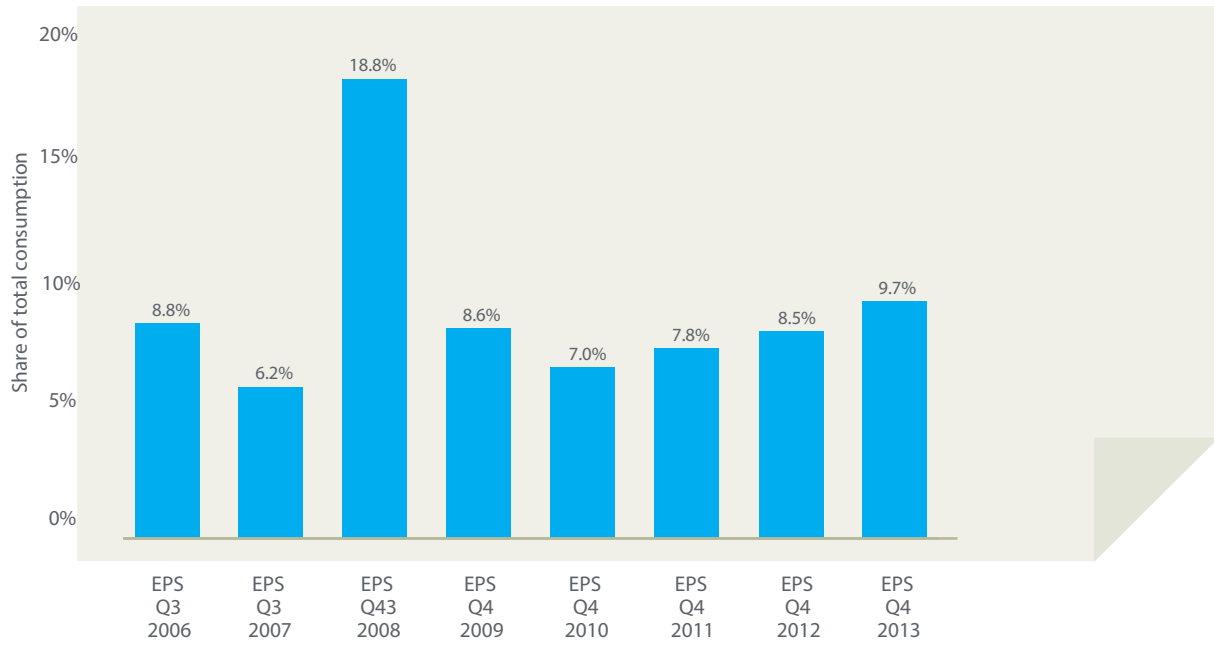
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



EPS results

Empty Pack Survey non-domestic estimates 2006-2013⁽¹⁾



SLOVENIA

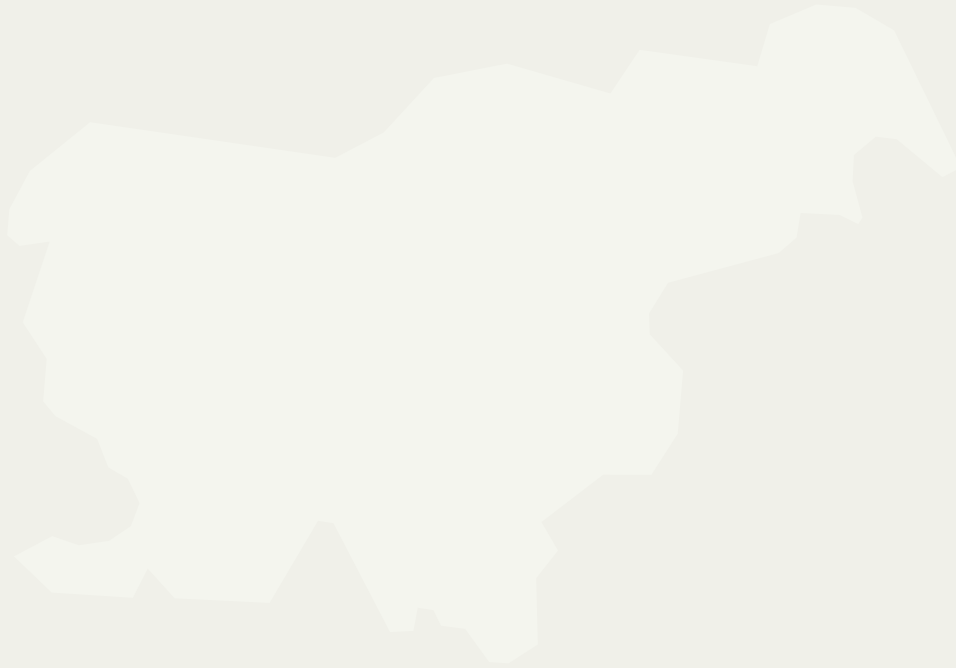


- The empty pack survey in Slovenia collected 3,000 packs during the fourth quarter of the year. It collects these packs once a year across 8 of the largest cities in Slovenia. The number of packs collected in the city is weighted by the city population
- No additional adjustments were made to the data in our analysis

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Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) MSIIntelligence Empty Pack Surveys, 2007 – 2013.



SLOVENIA



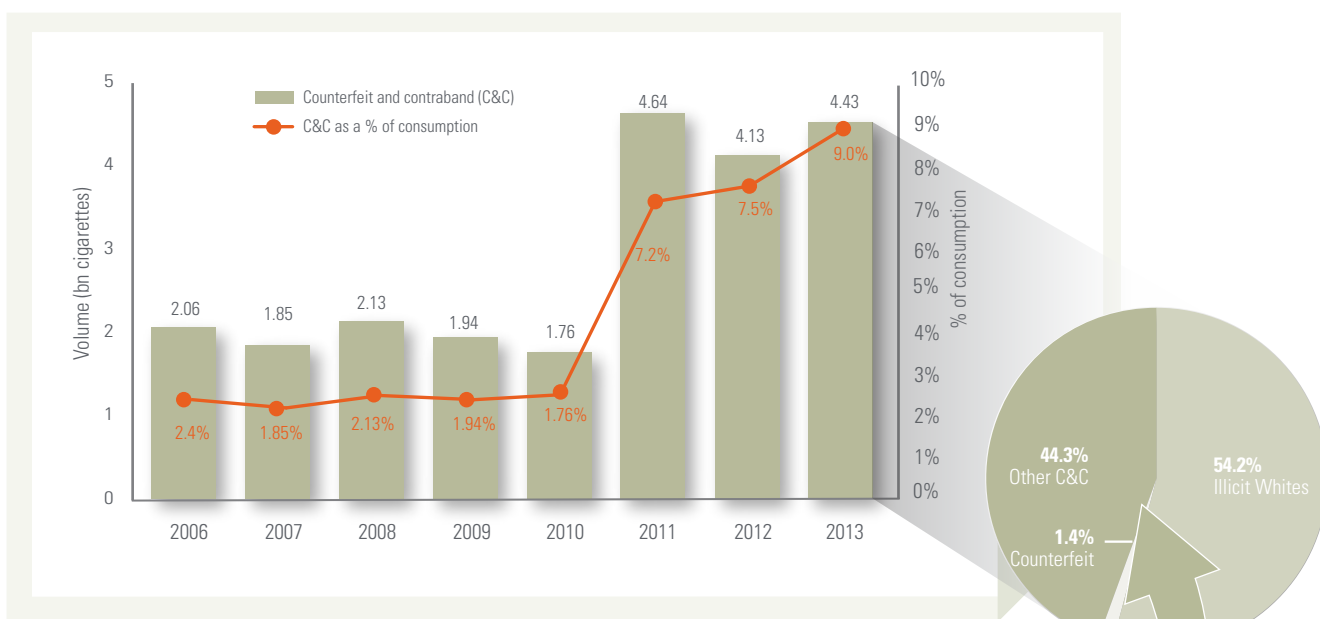
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SPAIN



Counterfeit and contraband consumption comes from surrounding markets, with high volumes of Illicit Whites

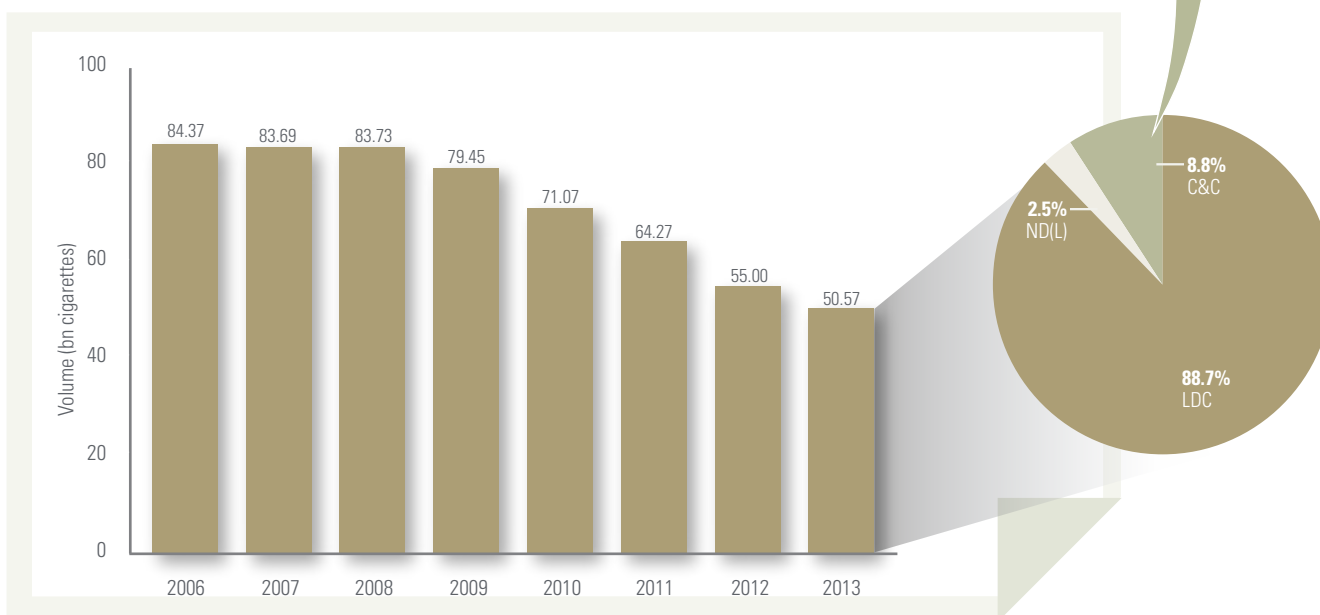
Manufactured cigarette C&C volumes and share of overall consumption 2006-13



SPAIN

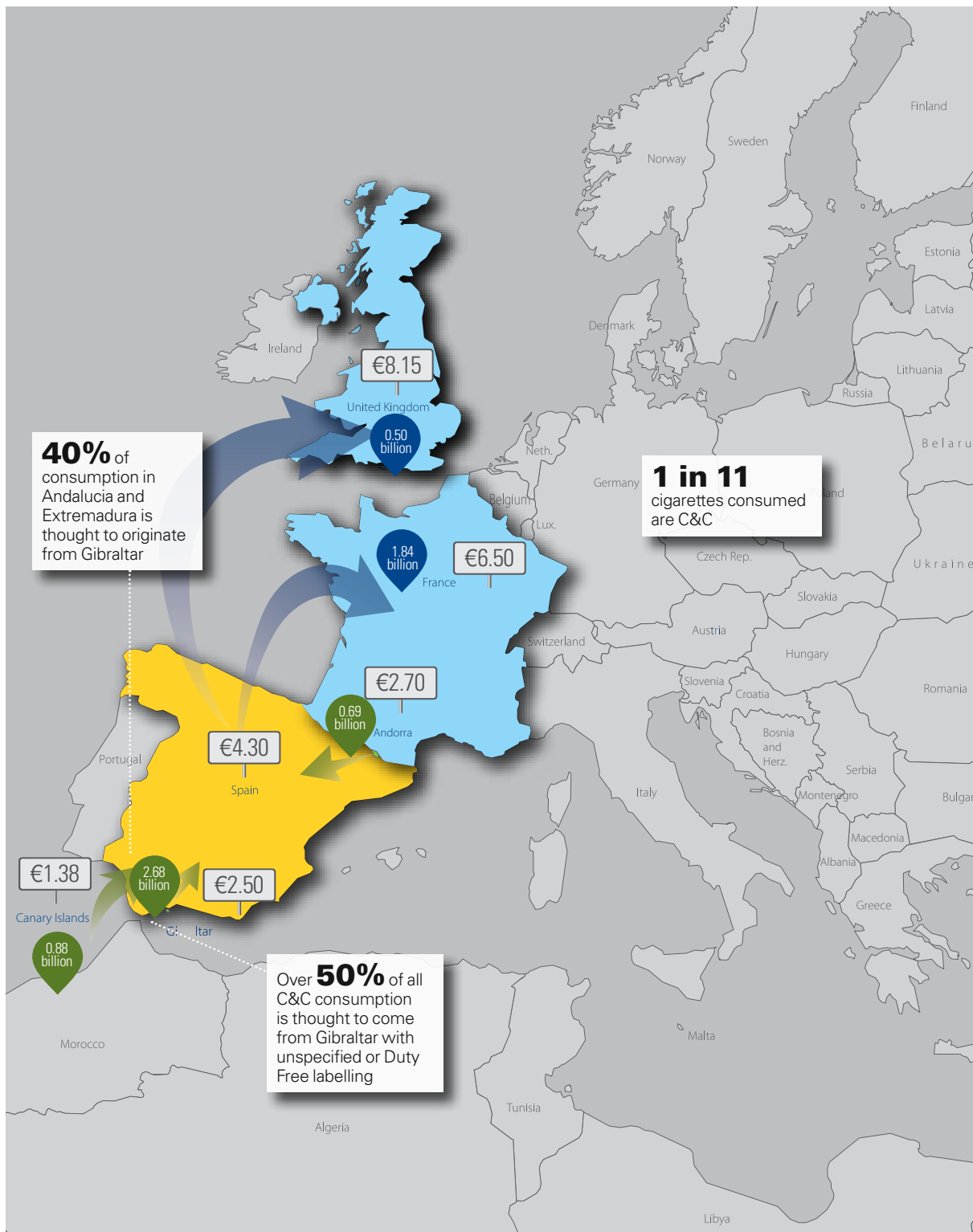


Manufactured cigarette consumption 2006-13



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MANUFACTURED CIGARETTE CONSUMPTION



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Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

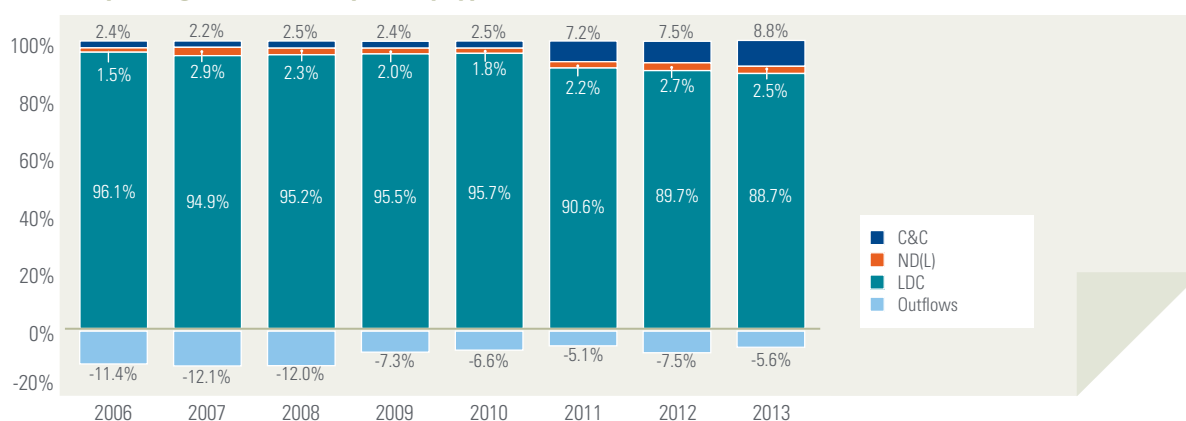
MANUFACTURED CIGARETTE CONSUMPTION

Overall consumption has declined with significant falls in legal domestic sales partially offset by decreasing outflows

Total manufactured cigarette consumption – Spain⁽¹⁾⁽²⁾

TOTAL SPAIN CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	90.69	89.51	89.74	81.67	72.70	61.52	53.50	47.71	(11)%
Outflows	-9.61	-10.10	-10.04	-5.76	-4.68	-3.30	-4.14	-2.85	(31)%
Legal domestic consumption (LDC)	81.08	79.41	79.70	75.91	68.01	58.21	49.35	44.86	(9)%
Non-domestic legal (ND(L))	1.23	2.43	1.91	1.60	1.30	1.41	1.51	1.29	(15)%
Counterfeit and contraband (C&C)	2.06	1.85	2.13	1.94	1.76	4.64	4.13	4.43	10%
Total non-domestic	3.29	4.28	4.03	3.54	3.06	6.05	5.64	5.71	1%
Total consumption	84.37	83.69	83.73	79.45	71.07	64.27	55.00	50.57	(8)%

Share of Spain cigarette consumption by type - 2006-2013⁽¹⁾⁽²⁾



Whilst overall consumption of manufactured cigarettes in Spain fell by 8% in 2013, the volume of counterfeit (C&C) and contraband increased by 7%, rising to 8.8% of total consumption

- Both legal domestic sales (LDS) and non-domestic legal (ND(L)) purchases fell significantly by 11% and 15% respectively, however, some of this consumption appears to have been replaced by C&C
- In 2013 there were also 6.7% price increases which may have had an impact on overall consumption
- The economic environment in Spain may also have had an impact on cigarette consumption, with PDI falling for the fifth year in a row and unemployment rising to 26%, the second highest in Europe⁽³⁾
- Outflows also appear to have declined significantly, with the volume of Spanish packs identified in France and the UK significantly lower than in previous years

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Euromonitor, Downloaded March 2014.

SPAIN



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Spain's main inflows were from Gibraltar, the Canary Islands and Andorra

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWS TO SPAIN									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Unspecified	0.00	0.00	0.00	0.00	0.02	1.31	0.97	1.53	58%
Duty Free	1.07	1.65	1.29	1.55	1.30	1.86	1.51	1.36	(10)%
Canary Islands	0.00	0.44	0.64	0.79	1.11	1.39	1.61	0.88	(46)%
Andorra	0.00	0.00	0.00	0.35	0.15	0.79	0.81	0.69	(15)%
Counterfeit								0.07	n/a
Other	2.22	2.18	2.10	0.85	0.48	0.70	0.74	1.18	60%
Total inflows	3.29	4.28	4.03	3.54	3.06	6.05	5.64	5.71	1%

ESTIMATED FLOWS FROM GIBRALTAR ^(a)									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Gibraltar estimate		0.21	0.24	0.24	0.70	1.88	1.96	2.68	37%

4% of Duty Free flows are Illicit Whites

This is the first year that an estimation has been given for Gibraltar flows as new information has been provided

The majority of inflows into Spain come from the surrounding low-priced markets of Gibraltar, Andorra and the Canary Islands

- These markets are either low-tax or tax free and the price difference between Spain and each market is approximately between €2.50 and €3.00 per pack, equating to a €25 to €30 saving on a carton
- Whilst most packs from Andorra and the Canary Islands have clear markings to determine where they have come from, packs sold in Gibraltar are not required to have national tax stamps. As a result a large proportion of packs that come from Gibraltar may have Duty Free labelling or "unspecified"
- By assuming that Duty Free and "unspecified" packs from the empty pack survey collected in Andalucia and Extremadura were sold in Gibraltar, it is possible to estimate the size of the Gibraltar inflow⁽²⁾
- By applying the same estimation for previous years, it appears that flows from Gibraltar have increased significantly since 2009

OUTFLOWS FROM SPAIN									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
France	3.42	3.25	4.38	2.40	2.08	1.57	2.33	1.84	(21)%
UK	4.07	4.22	3.17	1.91	1.15	0.81	1.04	0.50	(52)%
Germany	1.10	0.92	0.73	0.52	0.44	0.35	0.26	0.19	(26)%
Other	1.03	1.71	1.76	0.94	1.00	0.57	0.51	0.32	(36)%
Total outflows	9.61	10.10	10.04	5.76	4.68	3.30	4.14	2.85	(31)%

The significant decline in outflows was predominantly accounted for by a fall in flows to France and the UK

- Although France and the UK continue to represent the greatest share of outflows (80% in 2013), volumes flowing out to both markets declined significantly in 2013; volumes to other smaller outflow markets also reduced
- The lower outflows may be partially explained by price increases in Spain, resulting in its prices becoming more comparable to the rest of Europe
- There was also less contraband leaving Spain, as cheaper alternatives for France and the UK have emerged, such as from Algeria to France and from Pakistan and Belarus for the UK
- An analysis of sales data in the regions around France and Spain indicates that sales in the areas of France bordering Spain fell less than the rest of France. In Spain, sales within the region bordering France appear to have fallen more significantly than the rest of the market, supporting the decline in outflow

Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model. (2) Independent agency Empty pack Surveys, 2006-13.

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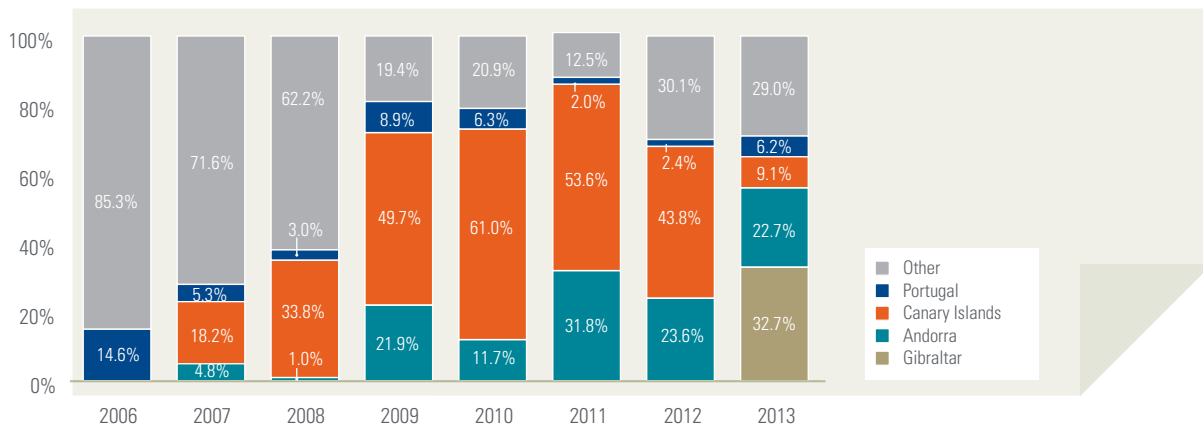
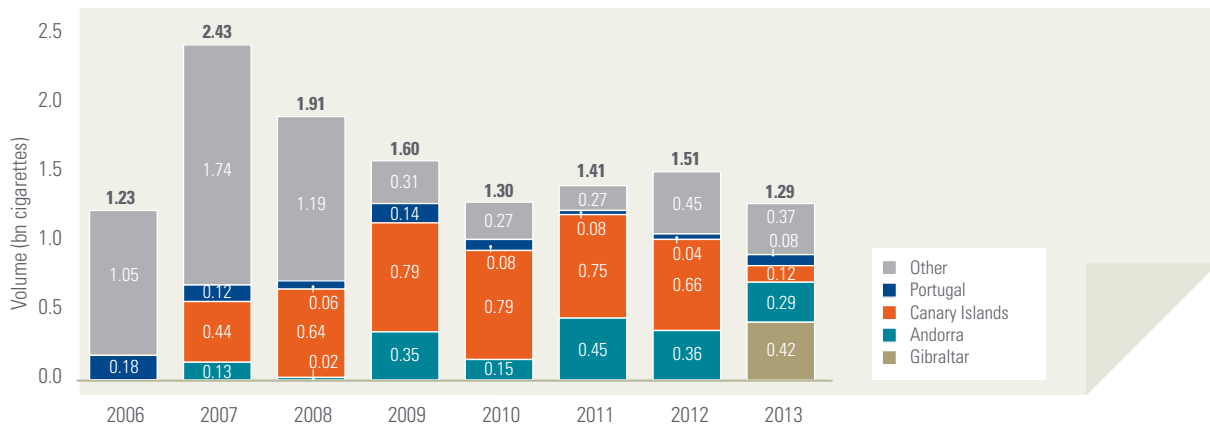
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The largest non-domestic legal volumes came from the lower priced markets of Gibraltar and Andorra

ND(L) by origin - 2006-2013^{(1)(2)(3) (a)(b)}



SPAIN



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An estimation of flows from Gibraltar has been provided in 2013, made possible by conducting the study on a pan industry basis for the first time and thereby gaining access to previously unavailable data sources; this analysis suggests a decline in ND(L) inflows

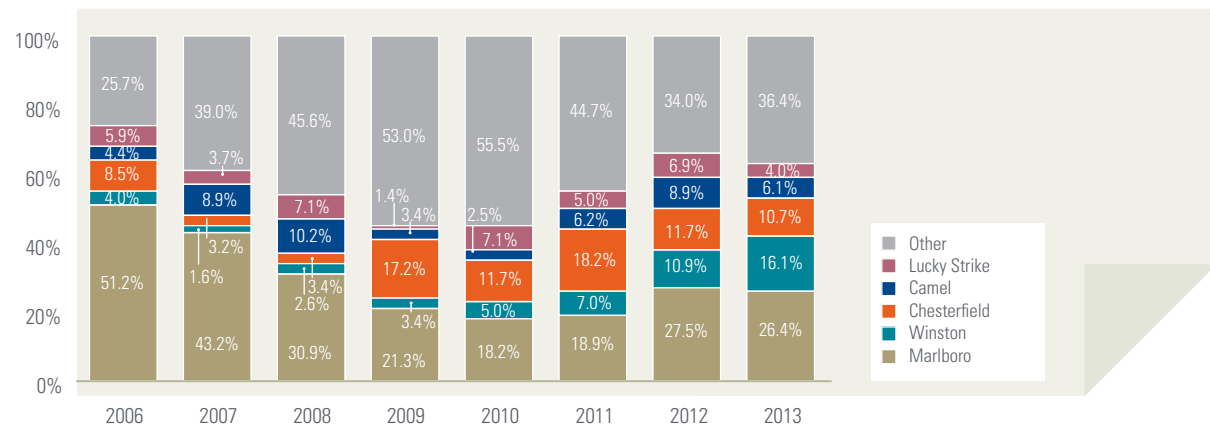
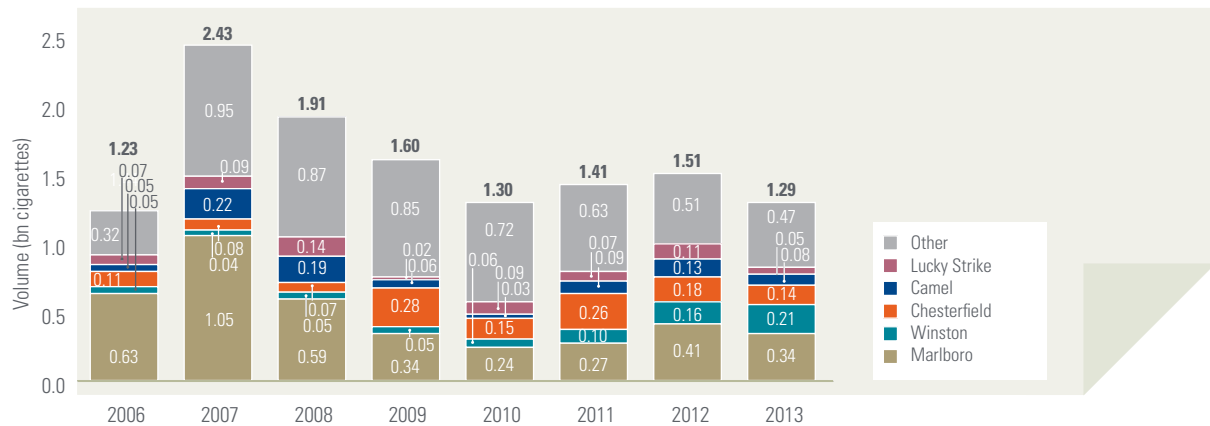
- In order to estimate the ND(L) volume from Gibraltar, visitors from Spain and smoking prevalence data was used (please see methodology and appendices)
- Despite a high overall inflow from Gibraltar, legal border sales are low as commuters and local people living within 20 miles of the border are only allowed to purchase 80 cigarettes per month
- The reduction in the estimation of flows from the Canary Islands came as a result of reducing the number of packs to the legal limit of 2 cartons and analysing the tourist flows
- The ND(L) flow from Andorra reduced owing to a decline in visitors to Andorra in 2013

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) Local government sources. (3) Synovate/Ipsos ND(L) research 2013.

NON-DOMESTIC LEGAL INFLOWS BY BRAND

Total ND(L) by brand - 2006-2013^{(1)(2)(a)}



Although there was an overall decline in ND(L) inflows, the most popular brands historically continued to represent a relatively high share of the volumes

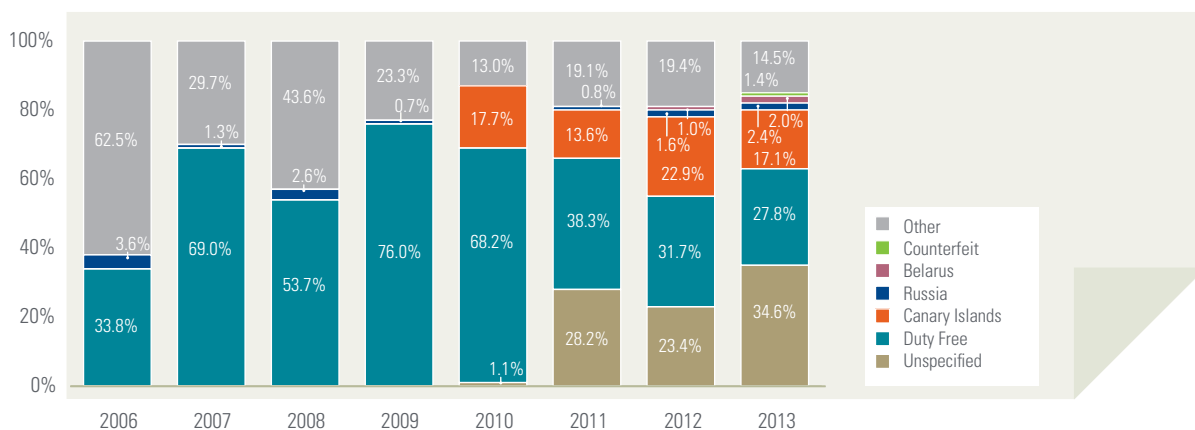
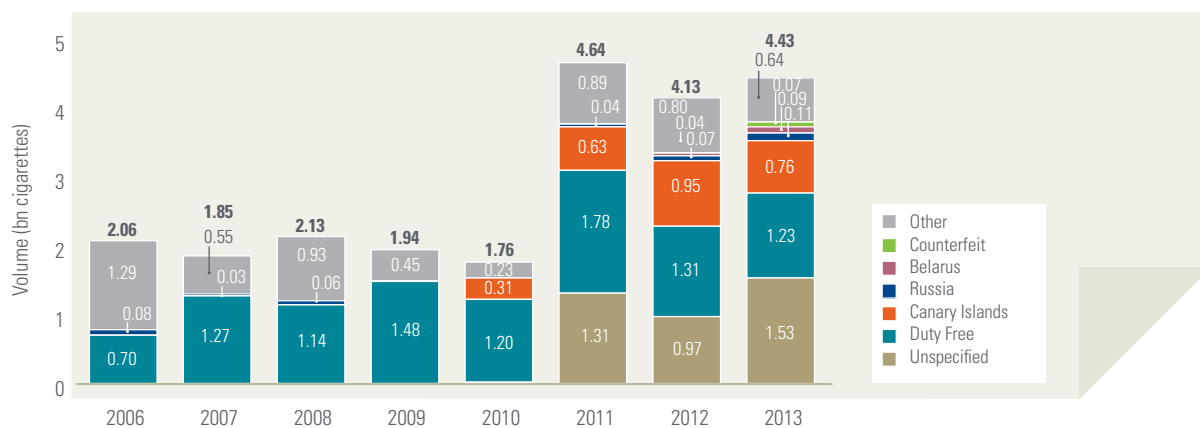
- Consumers tend to purchase premium brands when travelling abroad which they may not purchase as their usual brand
- This results in well known brands such as Marlboro representing a consistently high share of ND(L) inflows
- Other non-domestic legal brands tend to be those which are also popular in Spain

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.
Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



Counterfeit and contraband volumes increased mainly driven by an increase from unspecified sources, likely to be from Gibraltar

Total C&C by origin - 2006-2013^{(1)(2)(a)}



SPAIN



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Despite increased border protection, half of all C&C that enters Spain is estimated to come from Gibraltar

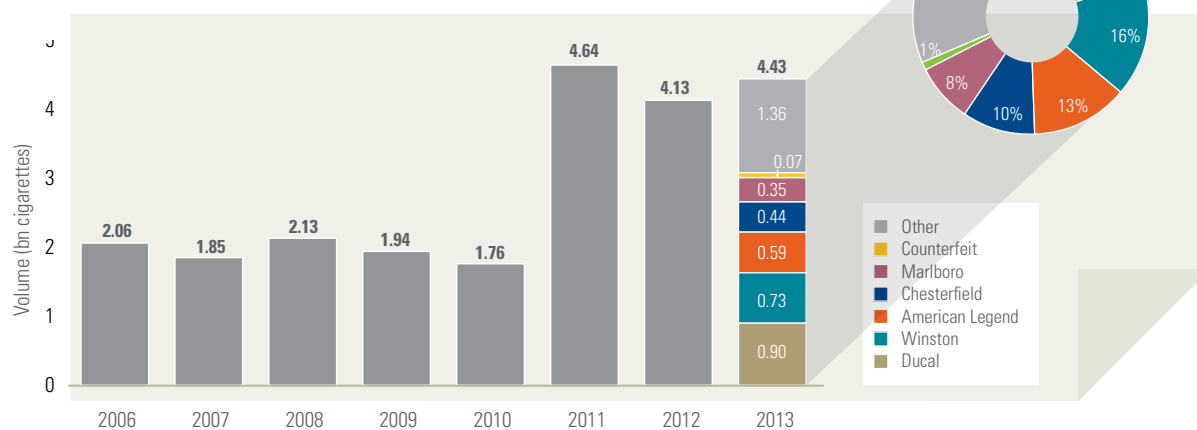
- A large proportion of this volume are Illicit Whites brands such as American Legend, Ducal, Elixir and Gold Classic. These brands have limited distribution
- In addition, large volumes of Winston and Chesterfield are also sold in Gibraltar with Duty Free labelling
- Unspecified and “other Duty Free” packs are predominantly picked up in the adjacent region of Andalucia, (see methodology and appendices) and are therefore likely to come from Gibraltar. Given the total estimated flow of 2.68 billion, the level of C&C from Gibraltar is likely to be approximately 2.3 billion cigarettes
- The significant volumes of Ducal, Elixir and Gold Classic which originate in the Canary Islands but are not available for purchase in Spain may have been manufactured for cheap export
- If the total volume of counterfeit and contraband had been consumed legally within the Spanish market, an additional tax revenue of approximately €718 million would have been raised by the Spanish Treasury

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.

C&C INFLOWS BY BRAND

Total C&C by brand - 2006-2013^{(1)(2)(a)(b)}



Breakdown of Illicit Whites by type - 2007-2013^{(1)(2)(a)(b)}

LABELLING OF ILLICIT WHITES INFLOWS TO SPAIN								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country Specific	0.01	0.08	0.06	0.20	1.37	1.18	1.39	18%
Duty Free	0.00	0.00	0.00	0.00	0.00	0.04	0.05	20%
Unspecified	0.00	0.00	0.00	0.00	0.20	0.61	1.01	65%
Total Illicit Whites	0.01	0.08	0.06	0.21	1.57	1.83	2.45	34%

Duty Free Illicit Whites made up just 4% of overall Duty Free volumes

C&C brands consist mainly of Illicit Whites brands sold without tax stamps, and legitimate brands sold with Duty Free labelling from Gibraltar

- The largest Illicit Whites brands were Ducal and American Legend, making up over 50% of the total
- Other large C&C brands not mentioned included Austin, Gold Classic and Elixir, however there was a high proliferation of smaller brands, with over 50 Illicit Whites brands identified in Spain in 2013
- Consumption of Illicit Whites brands appear to be increasing, with some illicit brands being sold with Spanish health warnings
- Illicit Whites brands make up the majority of the "unspecified" volume which comes into Spain through Gibraltar
- Compared with other countries, very few Illicit Whites brands are labelled as Duty Free as sales in Gibraltar do not require any form of tax stamp
- Illicit Whites brands with foreign tax stamps come from countries such as Belarus and Ukraine

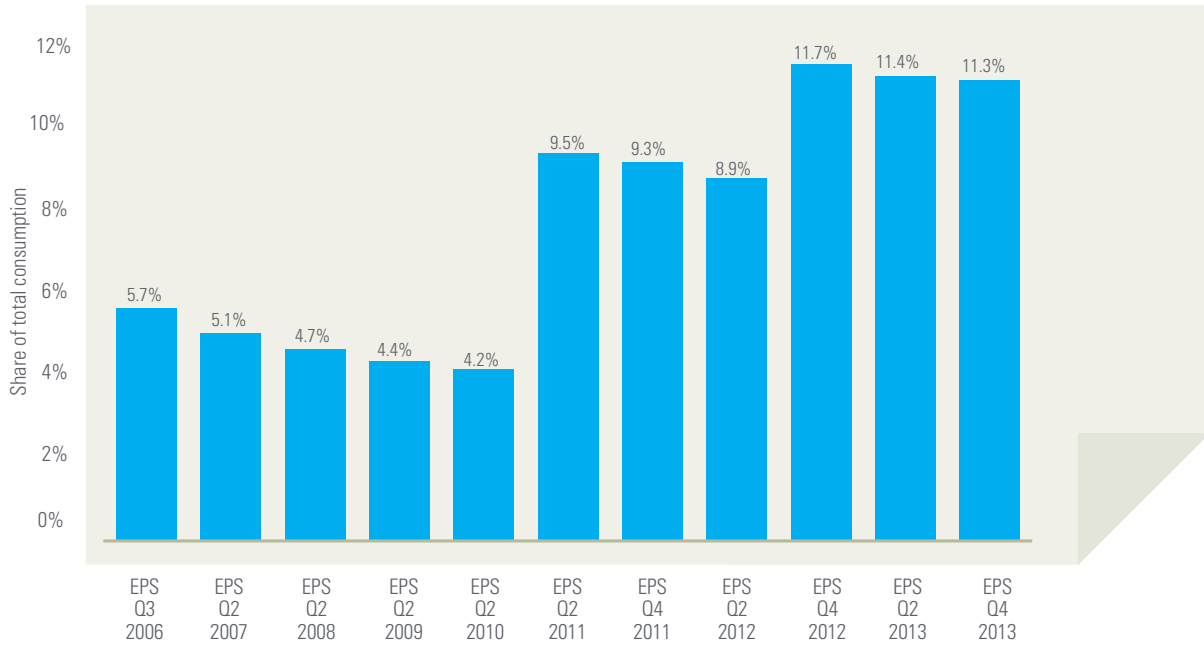
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (2) KPMG analysis of data sources provided by manufacturers.



EPS non domestic estimates

Empty Pack Survey non-domestic estimates - 2006-2013 ⁽¹⁾



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- The empty pack survey in Spain collected 30,000 packs during the course of the year. This was undertaken in 2 waves conducted in Q2 (April and May) and Q4 (October). The sample focused on 59 cities and the number of packs collected in each city is weighted by the city population
- No adjustments were made to the data in our analysis

Sources: (1) Independent agency Empty Pack Surveys, 2006-2013.

Non-domestic legal volume calculations and explanations

KPMG non domestic legal flows Spain

2. USE OF CONSUMER RESEARCH AND ANY ADJUSTMENTS FOR 2013 DATA							
Country	ND 2013 ⁽¹⁾	Total trips where cigarettes purchased (m) ⁽²⁾⁽³⁾	Number of packs per trip ⁽³⁾⁽⁴⁾	Total packs (m)	Data sources ⁽²⁾⁽³⁾⁽⁴⁾	2013 ND(L) (bn sticks)	% of ND
Canary Islands	0.88	0.29m	20	5.8	Tourist flows, Consumer research	0.12	14%
Andorra	0.69	0.72m	20	14.4	Tourist flows, Consumer research	0.29	41%
Gibraltar	2.68	2.10m	10	16.4	Tourist flows, Consumer research	0.42	16%

Travel data is used to calculate the non-domestic legal component of the Spain inflow. For Gibraltar, 10.64 million visits were made from Spain in 2013. It is assumed that 81.3% of these visitors are over 18 and that 24.1% buy cigarettes – the implied smoking prevalence rate in Spain. It is also assumed that each purchase consists of 1 carton, the legal limit to take into Spain from Gibraltar. Whilst those that live close to the border are allowed to purchase 80 cigarettes per month from Gibraltar, the consumer research indicated that the majority of those that purchased cigarettes brought back a carton, so no further adjustments are made. The result is we estimate that 12% of cigarettes thought to come from Gibraltar are legal.

A similar method has been applied to calculating the non-domestic legal volumes from Andorra and the Canary Islands, using both the number of trips made to each region from Spain and the implied smoking prevalence. For each region, consumer research indicates that the legal limit of 2 cartons per purchase is applied. The result is that legal flows from Andorra are estimated to represent 41% of the overall flow and 14% from the Canary Islands. The volume of non-domestic legal cigarettes from Andorra has decreased owing to a decrease in the number of visitors to the region in 2013.

Consumer research has historically indicated a higher level of non-domestic legal flows from the Canary Islands. However, the capping of the overall number of packs to two cartons per trip and a detailed analysis of tourist flows from the Canary Islands to Spain suggests that a larger proportion of the packs collected in Spain are contraband.

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) Local government sources. (3) Synovate/Ipsos ND(L) research 2013.

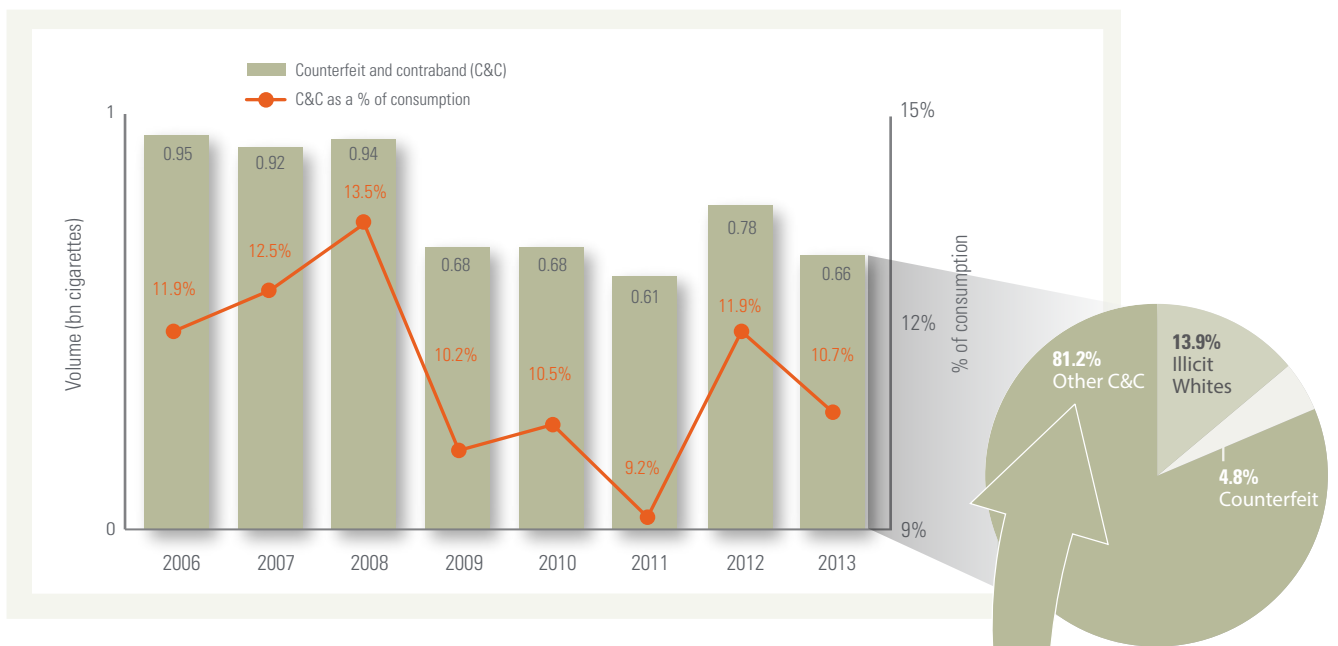


SWEDEN



Counterfeit & Contraband volumes decreased faster than total consumption

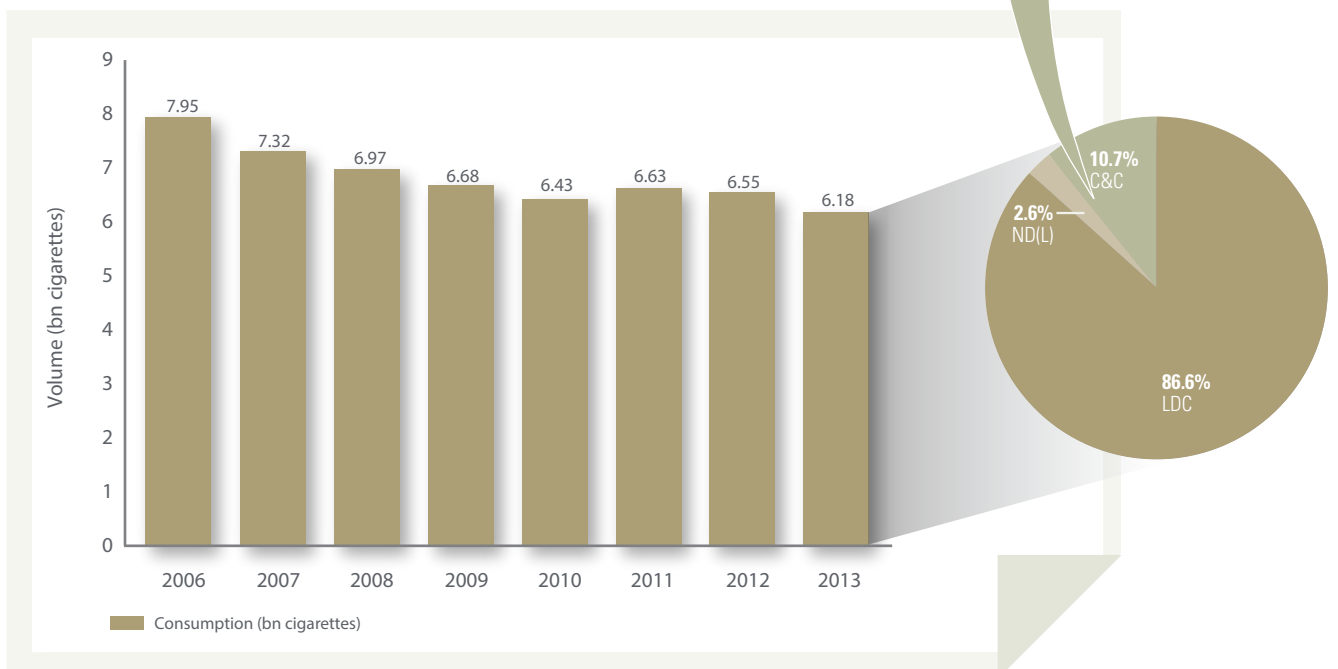
Manufactured cigarette C&C volumes and share of overall consumption 2006-13



SWEDEN

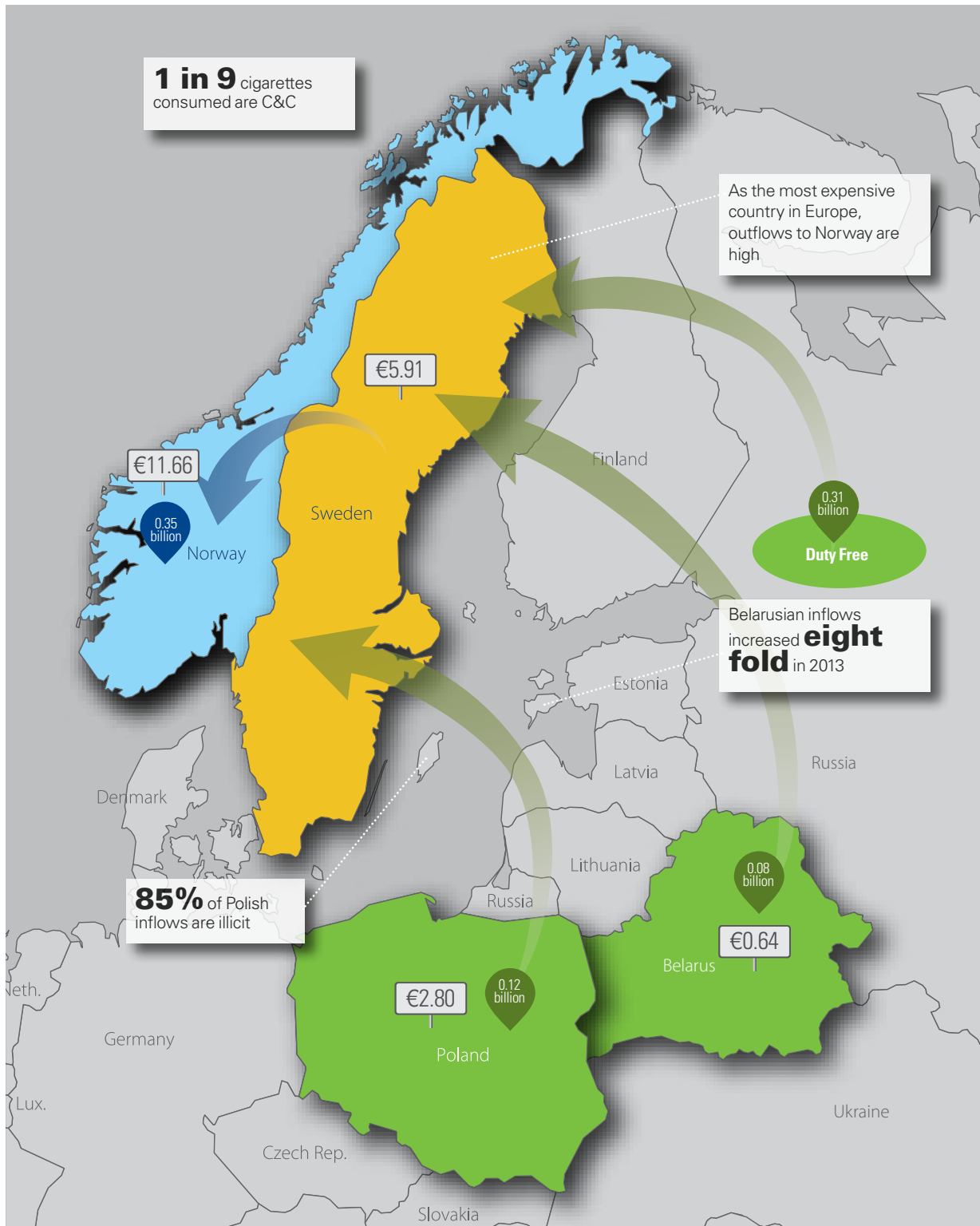


Implied cigarette smoking prevalence 2006-13



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MANUFACTURED CIGARETTE CONSUMPTION



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Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

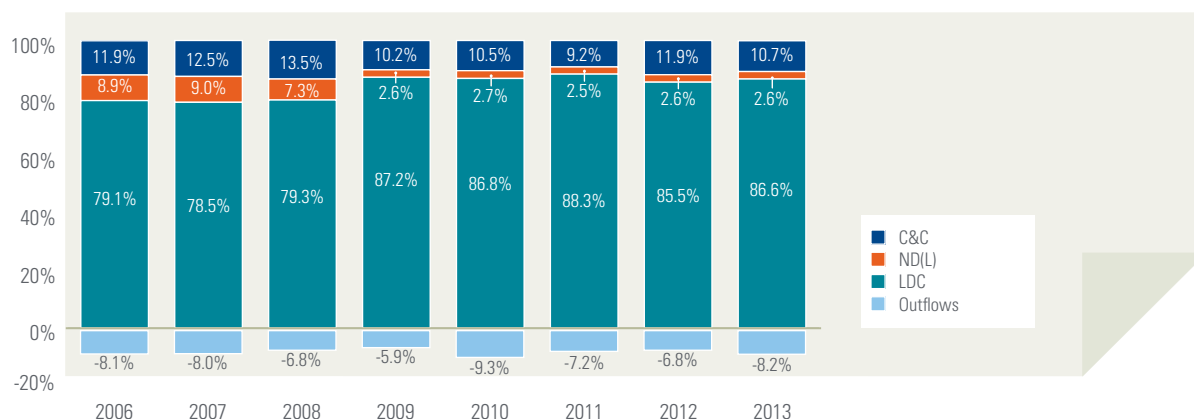
Total consumption has fallen, reflected in the decline of both legal domestic sales and non-domestic volumes

Total manufactured cigarette consumption – Sweden^{(1)(2)(3)(a)}

TOTAL SWEDEN CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	6.93	6.33	6.00	6.22	6.18	6.33	6.04	5.87	(3)%
Outflows	-0.64	-0.58	-0.47	-0.39	-0.60	-0.48	-0.44	-0.51	15%
Legal domestic consumption (LDC)	6.29	5.74	5.52	5.83	5.58	5.85	5.59	5.36	(4)%
Non-domestic legal (ND(L))	0.71	0.66	0.51	0.17	0.17	0.17	0.17	0.16	(5)%
Counterfeit and contraband (C&C)	0.95	0.92	0.94	0.68	0.68	0.61	0.78	0.66	(15)%
Total non-domestic	1.66	1.58	1.44	0.85	0.85	0.78	0.95	0.83	(13)%
Total consumption	7.95	7.32	6.97	6.68	6.43	6.63	6.55	6.18	(6)%

Domestic Illicit Whites were 0.8% of total consumption in 2013

Share of Sweden cigarette consumption by type - 2006-2013⁽¹⁾⁽²⁾⁽³⁾



Total manufactured cigarette consumption in Sweden fell by 6% in 2013, legal domestic sales (LDS) declined at a slower rate of 3%, while non-domestic volumes experienced a more rapid decline of 13%

- Economic conditions in Sweden improved in 2013 as unemployment remained stable at 8.0% and average PDI improved by 3.0%⁽⁴⁾⁽⁵⁾
- LDS volumes may have been impacted by a 3.1% WAP increase in 2013⁽⁶⁾
- Consumer research suggests that smoking incidence of manufactured cigarettes has increased slightly by 0.4 percentage points between 2012 and 2013 to 20.0%

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section).

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Independent agency Empty Pack Surveys, 2006 – 2013. (4) Euromonitor Passport. (5) The Economist Intelligence Unit. (6) EU Commission WAP tables.

Duty Free cigarettes were the largest non-domestic inflows to Sweden. There was a sizable outflow to Norway

Total inflows by country of origin - 2006-2013^{(1)(a)}

ND INFLOWS TO SWEDEN									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	0.50	0.53	0.52	0.26	0.33	0.23	0.24	0.31	29%
Poland	0.27	0.23	0.19	0.04	0.05	0.06	0.13	0.12	(8)%
Belarus	0.00	0.00	0.00	0.00	0.00	0.00	0.01	0.08	>100%
Russia	0.16	0.15	0.15	0.18	0.07	0.06	0.08	0.04	(50)%
Denmark	0.17	0.07	0.08	0.03	0.05	0.01	0.03	0.01	(53)%
Counterfeit								0.03	n/a
Other	0.56	0.59	0.50	0.33	0.36	0.41	0.45	0.23	(50)%
Total inflows	1.66	1.58	1.44	0.85	0.85	0.78	0.95	0.83	(13)%

Poland continues to be the main country specific inflow to Sweden. However, Belarusian inflows have shown a marked increase in 2013

- Duty Free inflows are the largest non-domestic inflow into Sweden, with Marlboro and L&M comprising over half of the inflow
- Winston and Fest cigarettes are the main component of the increase in flows from Belarus, making up over 90% of the Belarusian flow

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM SWEDEN									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Norway	0.50	0.37	0.31	0.23	0.30	0.32	0.28	0.35	23%
Germany	0.00	0.00	0.00	0.01	0.00	0.00	0.01	0.05	>100%
Denmark	0.10	0.10	0.10	0.05	0.17	0.11	0.04	0.04	(5)%
Netherlands	0.00	0.02	0.00	0.01	0.05	0.03	0.02	0.02	(20)%
Italy	0.00	0.00	0.00	0.00	0.02	0.00	0.00	0.01	n/a
UK	0.02	0.02	0.02	0.06	0.00	0.00	0.05	0.01	(74)%
Other	0.02	0.07	0.05	0.03	0.06	0.02	0.04	0.03	(31)%
Total outflows	0.64	0.58	0.47	0.39	0.60	0.48	0.44	0.51	15%

- Increased outflows to Norway and Germany are the main movements behind a 17% overall increase
- The price gap between Norway and Sweden fell in 2013, reducing the WAP difference from €6.12 to €5.75. The price gap is, however, still significant, with cigarettes in Sweden almost half the price of Norway, and as such a small reduction in price gap is unlikely to reduce demand⁽²⁾
- Of the outflows to Germany, 0.04bn of the 2013 balance is the Goal and Yesmoke Illicit Whites brands, both of which have Swedish health warnings, however Yesmoke is an Italian manufacturer, while the manufacturer of Goal is Juriga SIA in Latvia. As such it appears that these cigarettes are not actually made in or destined for Sweden, but have been given misleading markings or tax stamps in order to evade customs

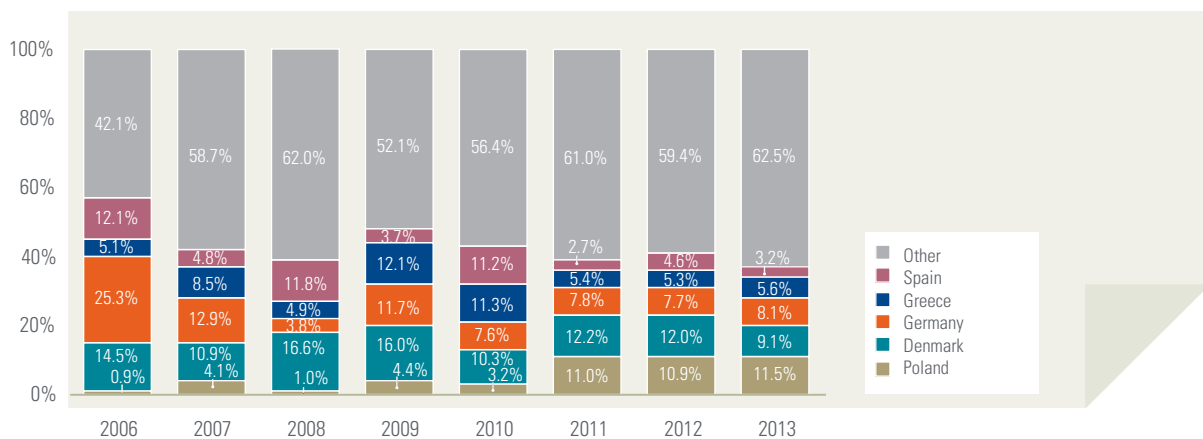
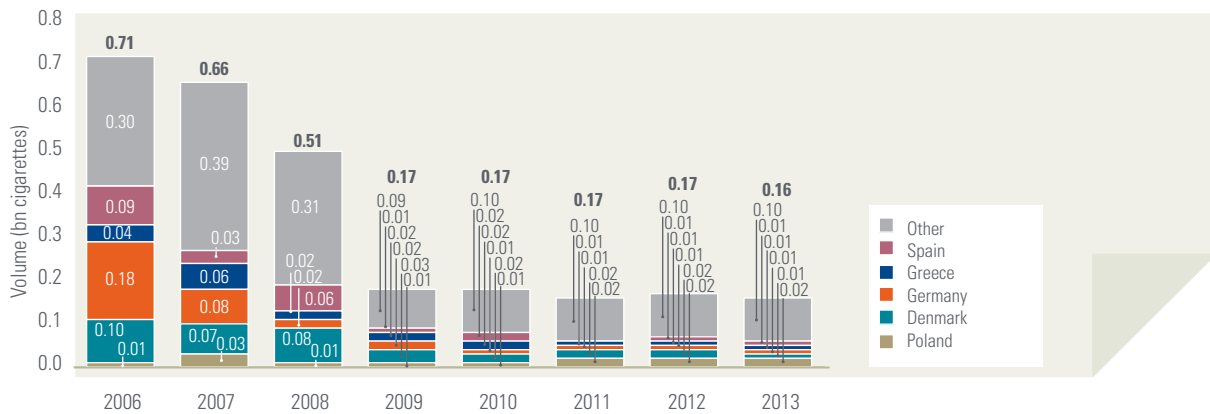
Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free labelling. Given this complexity, precise reporting to separate Duty Free into ND(L) and C&C is not provided. The Illicit Whites component is broken out in the "C&C inflows by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model (2) EU Commission WAP tables.



Non-domestic legal volumes declined slightly, accounting for one fifth of inflows

ND(L) by origin - 2006-2013^{(1)(2)(3)(a)(b)}



Falling volumes from Denmark and Spain led to an overall 5% decline in non-domestic legal (ND(L)) inflows in 2013

- Poland continues to be the main source of ND(L) inflows
 - Consumer research identified approximately 20,000 travellers to Poland who purchased cigarettes. Respondents stated that the average number of packs brought back when cigarettes were purchased was 48, which is in line with EU guidelines
 - This results in 15% of Polish inflows being classified as legal
- Denmark and Spain are popular travel destinations for Swedes travelling abroad. Consumer research identified sufficient trips and purchases per trip to designate these flows as 100% legal in our analysis
- Consumer research shows that there were very few trips made to Belarus where cigarettes were purchased. As a result all inflows from Belarus were classified as C&C

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

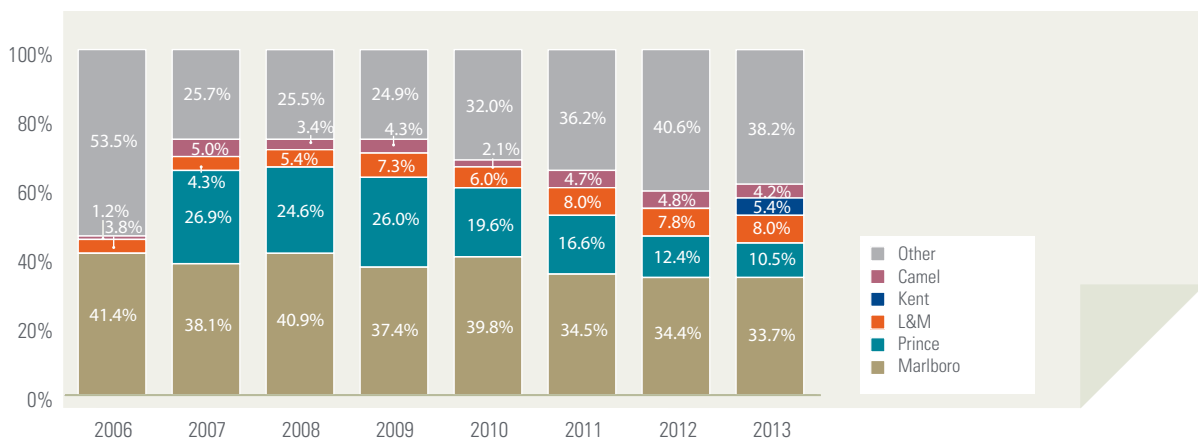
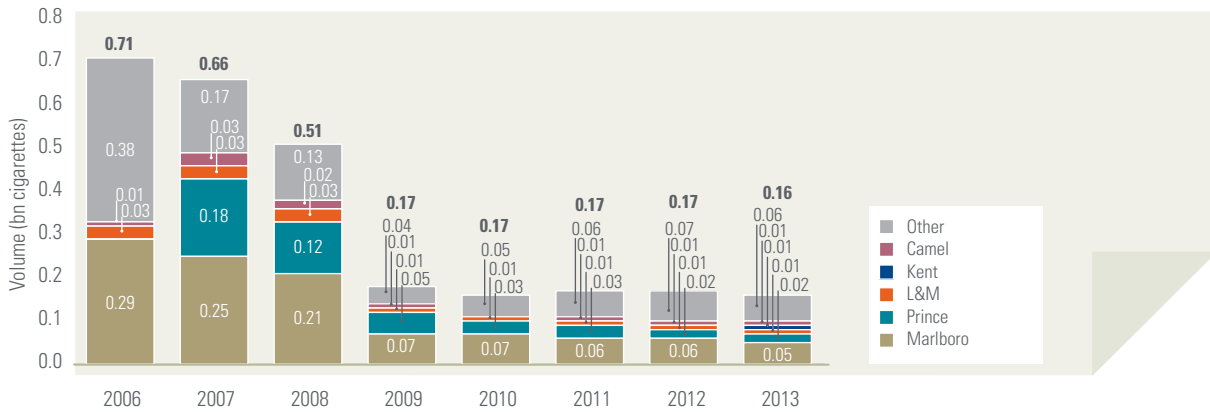
SWEDEN



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NON-DOMESTIC LEGAL INFLOWS BY BRAND

Total ND(L) by brand - 2006-2013^{(1)(2)(3)(a)}



Marlboro was the dominant ND(L) brand in 2013

- The major source countries for this inflow are Denmark, Finland, Greece, Thailand and Turkey. These markets account for 44% of the total Marlboro inflow

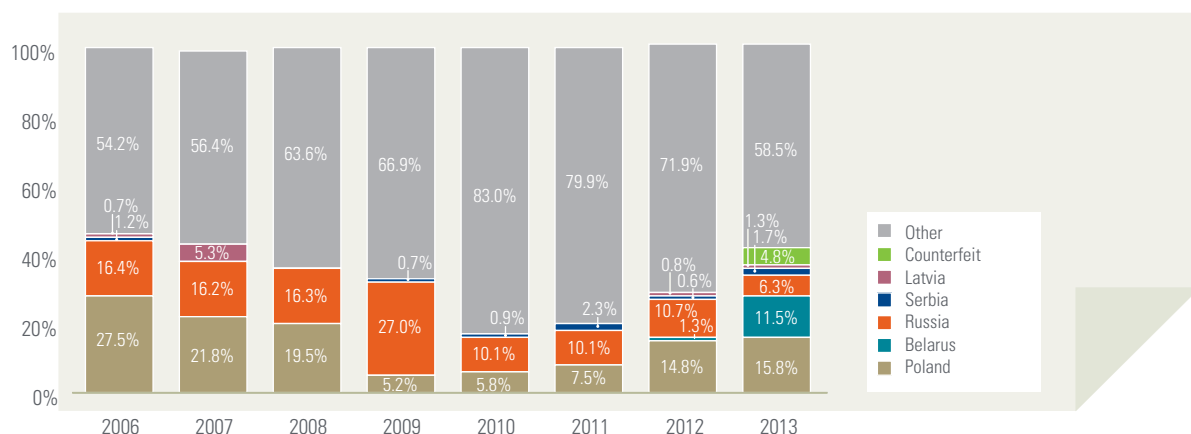
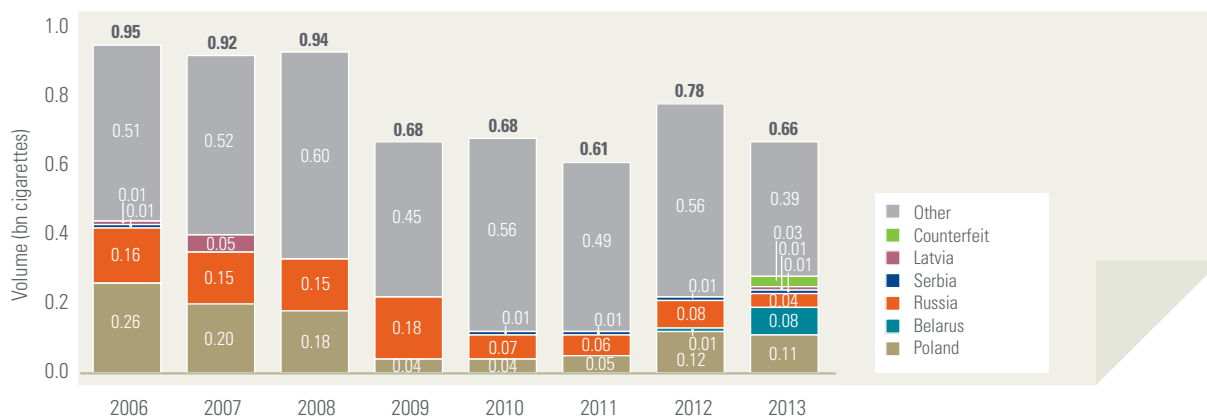
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



Poland remained the main source of C&C, although Belarusian inflows have increased

C&C by origin - 2006-2013^{(1)(2)(3)(a)}



SWEDEN



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Domestic Illicit Whites have traditionally been a large component of Swedish C&C volumes; in 2013, their volumes have reduced

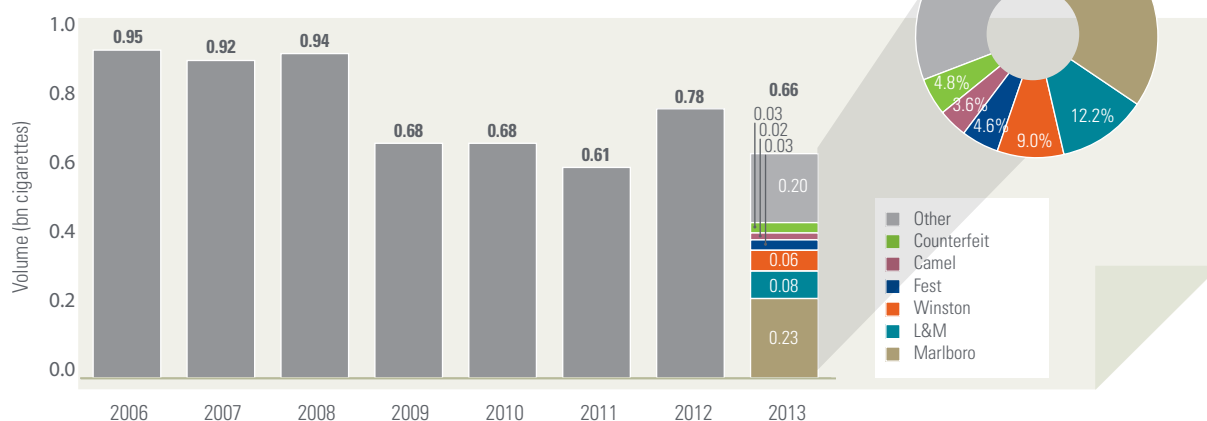
- In 2012, domestic Illicit Whites accounted for 3.3% of total consumption, or 0.22bn cigarettes. In 2013 this reduced to 0.8%, or 0.05bn cigarettes
 - The 2013 Tobaksrapport by HUI Research attributes this 2.5 percentage point reduction to increased efforts by police and municipality inspectors in several Swedish towns. The town of Gävle, on the East Coast North of Stockholm, experienced the largest decline in domestic Illicit Whites (from 24.5% of total consumption in 2012 to 1 percent in 2013) due to intense and consistent investigations by the local police authority⁽⁴⁾
- Increased incidence of Winston and the Illicit Whites brand Fest are driving the increased Belarus inflow
- If the 0.66bn C&C cigarettes in 2013 had been legally purchased in Sweden the tax revenue gained would have been approximately €151m

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers. (4) Tobaksrapport 2013, HUI Research, 2013.

C&C INFLOWS BY BRAND

C&C by brand - 2006-2013^{(1)(2)(3)(a)}



Marlboro is the most prevalent C&C brand in Sweden, with Polish and Duty Free packs the main component

Composition of Illicit Whites inflows - 2007-2013^{(1)(3)(b)}

Illicit Whites made up 13% of overall Duty Free flows

LABELLING OF ILLICITWHITES INFLOWS TO SWEDEN								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.00	0.03	0.14	0.08	0.15	0.03	0.05	72%
Duty Free	0.00	0.00	0.00	0.00	0.01	0.03	0.04	49%
Unspecified	0.00	0.00	0.00	0.00	0.00	0.01	0.01	(57)%
Total Illicit Whites	0.01	0.03	0.14	0.08	0.16	0.07	0.09	40%

Illicit Whites were 14% of C&C flows in 2013

- The main brands were Jin Ling and Fest, which comprised 48% of the 0.09bn total

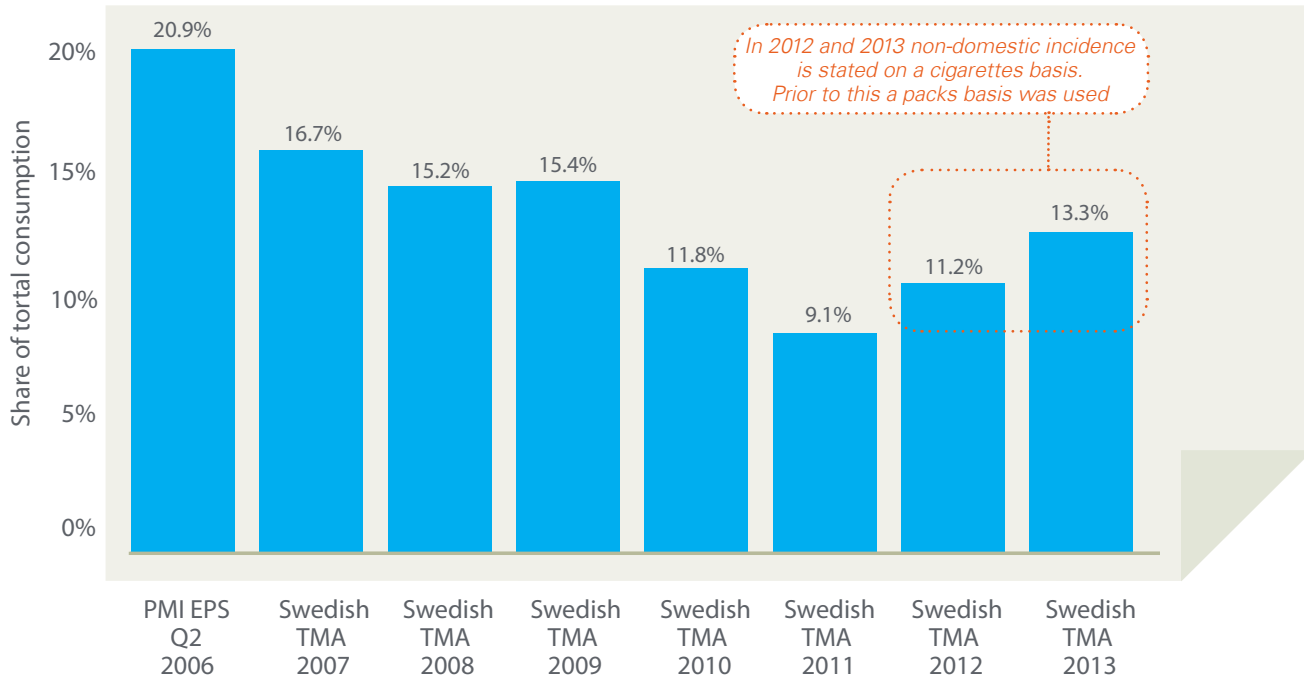
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) A methodology and definition of Illicit Whites is provided in the methodology section.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



EPS results & EU Flow model

Empty Pack Survey non-domestic estimates - 2006-2013⁽¹⁾⁽²⁾



- The empty pack survey in Sweden collected 10,000 packs during the second quarter of the year. It collects these packs across 29 towns and cities

SWEDEN



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Sources: (1) Swedish TMA Empty Pack Surveys, 2007 – 2013.
 (2) Tobaksrapport 2013, HUI Research, 2013.

Non-domestic legal volumes calculations and explanations

KPMG non domestic legal flows Sweden

COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 ⁽¹⁾	2013 ND(L) (bn sticks)	% of ND
Denmark	0.01	0.01	100%
Spain	0.01	0.01	100%

Consumer research is used to calculate the ND(L) inflow volume to Sweden

Denmark and Spain are both popular tourist destination for Swedes travelling abroad, with only neighbouring Norway a more popular destination

There were 0.35 million trips to Denmark in 2013 where cigarettes were purchased. On average 3 packs were purchased per trip, giving a total legal volume of 0.02bn cigarettes. The total amount of non-domestic cigarettes from Denmark in the EPS study was 0.01bn, and so it is assumed the flow from Denmark is 100% legal

There were 0.12 million trips to Spain in 2013 where cigarettes were purchased. On average 14 packs were purchased per trip, giving a total legal volume of 0.04bn cigarettes. The total amount of non-domestic cigarettes from Spain in the EPS study was 0.01bn, and so it is assumed the flow from Spain is 100% legal

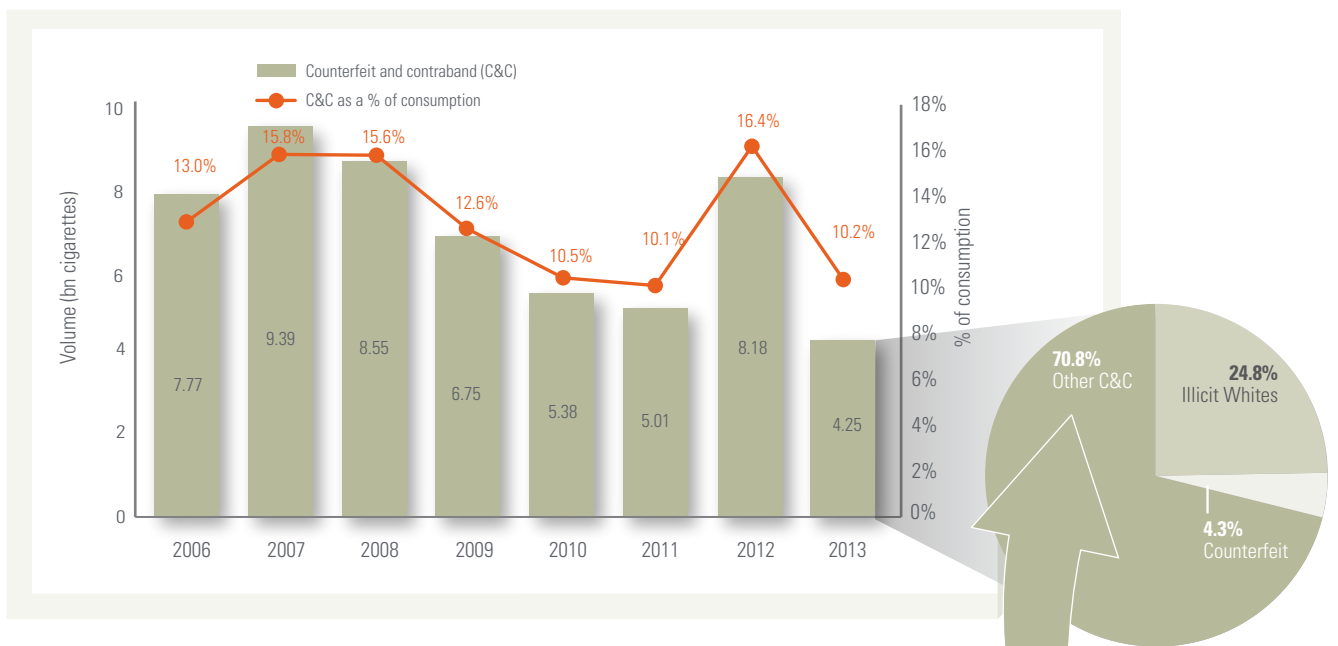


Sources: (1) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model.



After an isolated high in 2012, Counterfeit & Contraband has returned to the levels consistent with 2010 and 2011

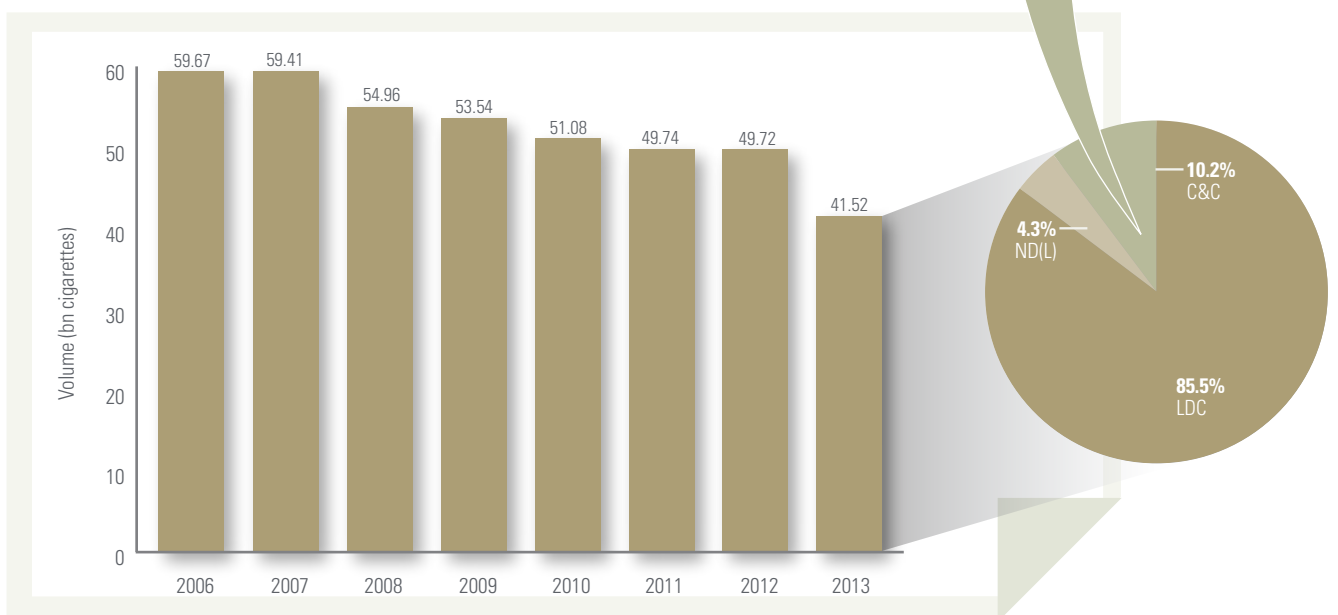
Manufactured cigarette C&C volumes and share of overall consumption 2006-13



UK

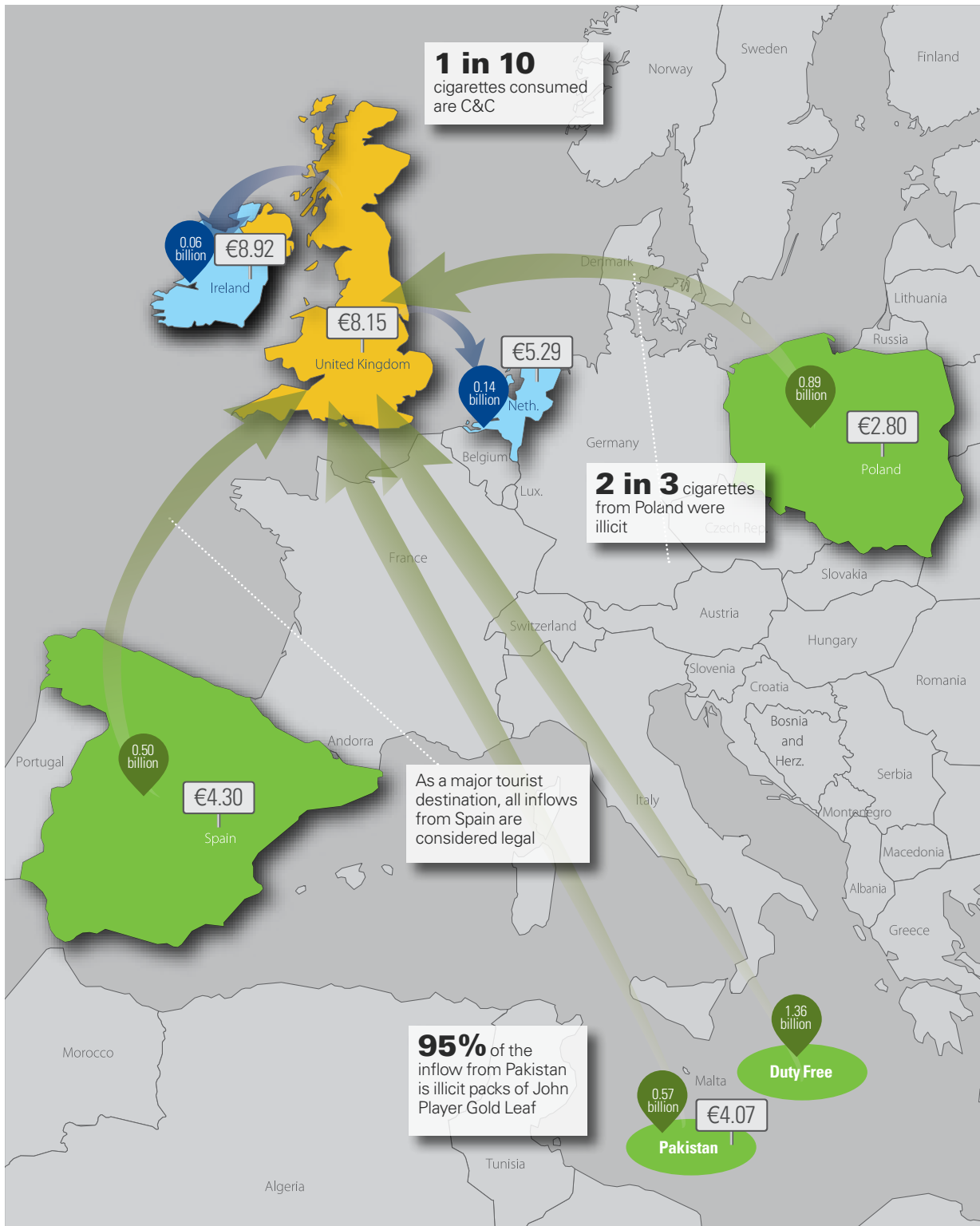


Manufactured cigarette consumption 2006-13



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KEY INFLOWS AND OUTFLOWS



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Note: (a) Map shows major flows. Countries which are both source and destination countries are coded according to the larger flow.

Source: (1) KPMG EU Flows Model.

MANUFACTURED CIGARETTE CONSUMPTION

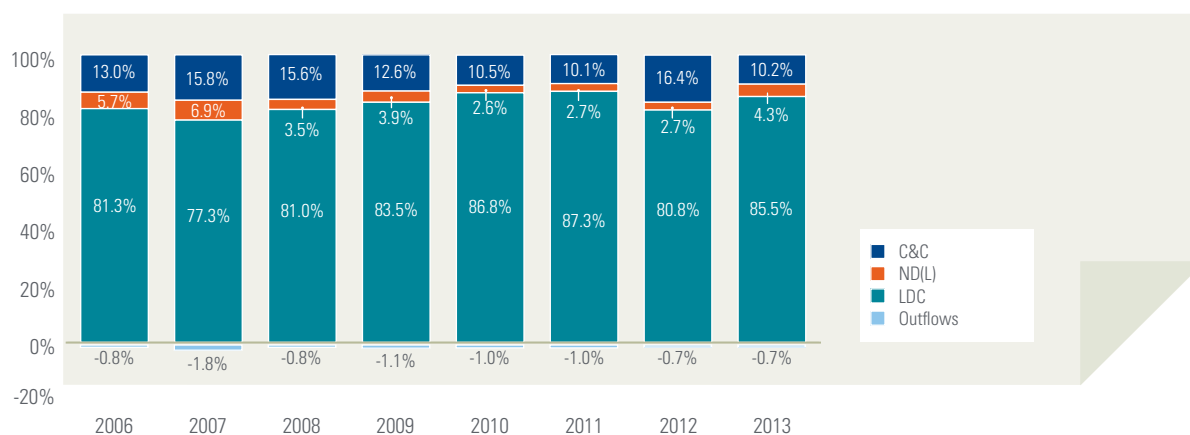
Total consumption fell in 2013, however the decline in non-domestic consumption was likely to have been the result of one-off events in 2012, distorting the long term trend

2012 non-domestic results were exceptionally high due to the large non-domestic incidence as per the Q4 EPS survey. One-off events taking place around that time period may have resulted in an overstatement of non-domestic volumes for the full year, which has exaggerated the non-domestic decline in 2013

Total manufactured cigarette consumption – UK^{(1)(2)(3)(a)}

TOTAL UK CONSUMPTION									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS)	49.01	46.99	44.97	45.27	44.85	43.89	40.55	35.77	(12)%
Outflows	-0.48	-1.05	-0.47	-0.57	-0.50	-0.49	-0.37	-0.28	(24)%
Legal domestic consumption (LDC)	48.53	45.94	44.50	44.70	44.35	43.40	40.19	35.49	(12)%
Non-domestic legal (ND(L))	3.37	4.08	1.91	2.10	1.35	1.32	1.36	1.78	31%
Counterfeit and contraband (C&C)	7.77	9.39	8.55	6.75	5.38	5.01	8.18	4.25	(48)%
Total non-domestic	11.14	13.47	10.46	8.85	6.73	6.33	9.54	6.03	(37)%
Total consumption	59.67	59.41	54.96	53.54	51.08	49.74	49.72	41.52	(16)%

Share of UK cigarette consumption by type - 2006-2013⁽¹⁾⁽²⁾⁽³⁾



Falling legal domestic sales (LDS) and non-domestic incidence drove a 16% decline in manufactured cigarette consumption in the UK in 2013

- Economic conditions in the UK improved slightly in 2013 as unemployment fell from 8.0% to 7.6% and average PDI increased by 0.6%⁽⁴⁾⁽⁵⁾
- However, an 8.5% WAP rise in 2013 is likely to have impacted LDS volumes⁽⁶⁾

A number of one-off factors are likely to have influenced the 2012 Q4 EPS result and alternative data sources suggest this may have overstated non-domestic incidence for the full year; other evidence suggests the volume decline from 2011 to 2013 is likely to have been more steady and consistent than the significant drop implied above

- The 2012 UK results suggested a significant increase in non-domestic consumption as a result of the Q4 EPS, which recorded 21% NDI compared with 13% in Q2 2012 and an average of 13% in 2010 and 2011 combined
- The timing of the Q4 2012 EPS in October may have reflected the impact of the Olympic Games and a favourable Sterling to Euro exchange rate, with larger levels of tourist inflows and relaxed border controls (discussed further in the counterfeit and contraband pages) likely to have created one-off peak in non-domestic inflows
- Project SUN has been conducted on a pan industry basis for the first time in 2013, allowing access to previously unavailable data sources. The next page discusses alternative estimates that suggest there has been a more gradual decline from 2011 to 2013 and may have allowed for further refinement of the 2012 results, had it been available at the time

Note: (a) In 2012 and 2013 non-domestic incidence is stated on a cigarettes basis. Prior to this a packs basis was used (see methodology section)

Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers. (2) Synovate/Ipsos ND(L) research 2013 (Ipsos acquired Synovate in 2011). (3) Independent agency Empty Pack Surveys, 2006 – 2013. (4) Euromonitor Passport. (5) The Economist Intelligence Unit. (6) EU Commission WAP tables.

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The JTI Pack Swap Survey consistently reports a similar trend to the EPS, with the exception of the 2012 results

Total manufactured cigarette consumption as per JTI pack swap survey non-domestic estimates – UK⁽¹⁾⁽²⁾

TOTAL UK CONSUMPTION AS PER JTI PACK SWAP SURVEY NON-DOMESTIC ESTIMATES									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Legal domestic sales (LDS) as per Project Sun	49.01	46.99	44.97	45.27	44.85	43.89	40.55	35.77	(12)%
Outflows as per Project Sun	-0.48	-1.05	-0.47	-0.57	-0.50	-0.49	-0.37	-0.28	(24)%
Legal domestic consumption (LDC)	48.53	45.94	44.50	44.70	44.35	43.40	40.19	35.49	(12)%
Non-domestic incidence as per JTI pack swap survey			17.8%	16.1%	12.9%	12.4%	13.0%	13.5%	4%
Total non-domestic			9.64	8.58	6.57	6.14	6.00	5.54	(8)%
Total consumption			54.14	53.27	50.92	49.55	46.19	41.03	(11)%

Alternative estimates are available for the UK non-domestic cigarette market, including the Pack Swap Survey, undertaken by JTI. Compared to Project Sun non-domestic incidences are largely similar in 2013, but year on year changes differ due to differing estimates of the 2012 incidence

- The JTI pack swap is a household sampling programme that commenced in 1998 undertaken by independent research agencies and commissioned for JTI
- It is designed to be a statistically representative sample that can calculate a measurement of non-domestic cigarettes in the UK
 - 56 waves are undertaken each year with a random location sampling plan that is designed to be representative of the UK as a whole as regards to gender, age group, social class and region
 - Each wave contacts approximately 2,000 respondents aged over 18 who are interviewed at their home by an interviewer from an independent research agency
 - If respondents smoke they are guided through a survey regarding their purchasing habits, and are then asked if they are willing to provide their current pack. Around 63% of smokers agree to exchange their packs when asked
 - This yields approximately 8,000 manufactured cigarette packs that are subsequently analysed by JTI
- JTI believes the results should be considered the minimum volume of non-domestic incidence in the UK, as respondents may well under-report their smoking habits or refuse to exchange their pack if they know it is counterfeit or contraband

UK



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Sources: (1) KPMG EU Flows Model and analysis of data sources provided by manufacturers for LDS and outflows calculation.
(2) JTI Pack Swap Survey Results 2008-2013.

The main inflows were from Duty Free and Poland

Total inflows by country of origin - 2006-2013^{(1)(a)}

Main Duty Free brands are Marlboro, Lambert and Butler, Regal and Benson & Hedges (95% BAT variant), accounting for 58% of 2013 Duty Free volume

Main Unspecified brands are Gold Classic, Palace and Richman, accounting for 62% of the total

ND INFLOWS TO UK									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Duty Free	0.56	1.61	0.88	0.83	0.85	1.20	1.63	1.36	(17)%
Poland	1.40	1.02	0.93	1.01	0.86	0.96	1.72	0.89	(48)%
Pakistan	0.00	0.01	0.03	0.09	0.20	0.20	0.35	0.57	63%
Spain	4.07	4.22	3.17	1.91	1.15	0.81	1.04	0.50	(52)%
Unspecified	0.00	0.00	0.00	0.32	0.44	0.25	0.26	0.33	27%
Counterfeit								0.18	n/a
Other	5.11	6.61	5.44	4.68	3.22	2.91	4.53	2.20	(51)%
Total inflows	11.14	13.47	10.46	8.85	6.73	6.33	9.54	6.03	(37)%

As one of the highest priced countries in the EU, price differentials to nearby countries are high, which can act as an incentive to transport non-domestic cigarettes to the UK

- The largest non-domestic inflows to the UK are from Poland, Pakistan and Spain
- Unspecified inflows are once again increasing after falling back in volume in 2011 and 2012. The majority of unspecified packs are the Illicit Whites brands Gold Classic, Palace and Richman

Total outflows by destination country - 2006-2013⁽¹⁾

OUTFLOWS FROM UK									
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Netherlands	0.20	0.25	0.15	0.11	0.20	0.14	0.15	0.14	(2)%
Ireland	0.03	0.14	0.19	0.35	0.20	0.24	0.14	0.06	(54)%
France	0.20	0.49	0.00	0.03	0.04	0.04	0.02	0.04	80%
Greece	0.00	0.00	0.00	0.01	0.00	0.00	0.01	0.01	51%
Germany	0.01	0.00	0.01	0.00	0.00	0.00	0.01	0.01	16%
Spain	0.00	0.13	0.08	0.02	0.01	0.00	0.01	0.01	(21)%
Other	0.05	0.04	0.04	0.05	0.05	0.06	0.05	0.02	(62)%
Total outflows	0.48	1.05	0.47	0.57	0.50	0.49	0.37	0.28	(24)%

The UK's high price position also results in low outflows of cigarettes to other EU countries

- Outflows in aggregate fell by 24%, with the main driver a sharp decline in outflows to Ireland. The price gap between the UK and Ireland fell in 2013, decreasing the WAP difference from €0.95 to €0.77. This may have reduced the incentive for cross-border shopping⁽²⁾

Note: (a) The Duty Free inflow contains both "other" Duty Free product and Illicit Whites which have Duty Free stamps on them. The Illicit Whites component is broken out in the "C&C by brand" section. See Methodology section which outlines Illicit Whites brands and definition.

Sources: (1) KPMG EU Flows Model. (2) EU Commission WAP tables.

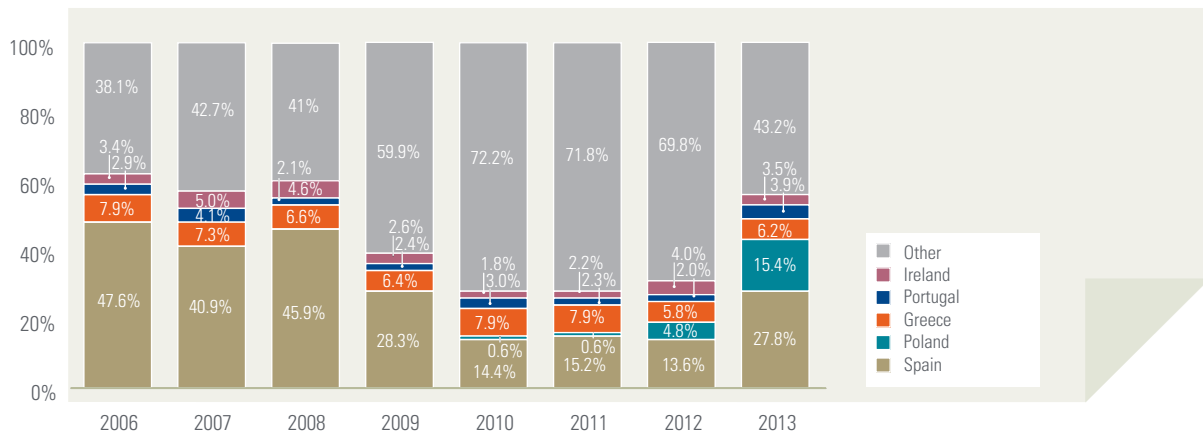
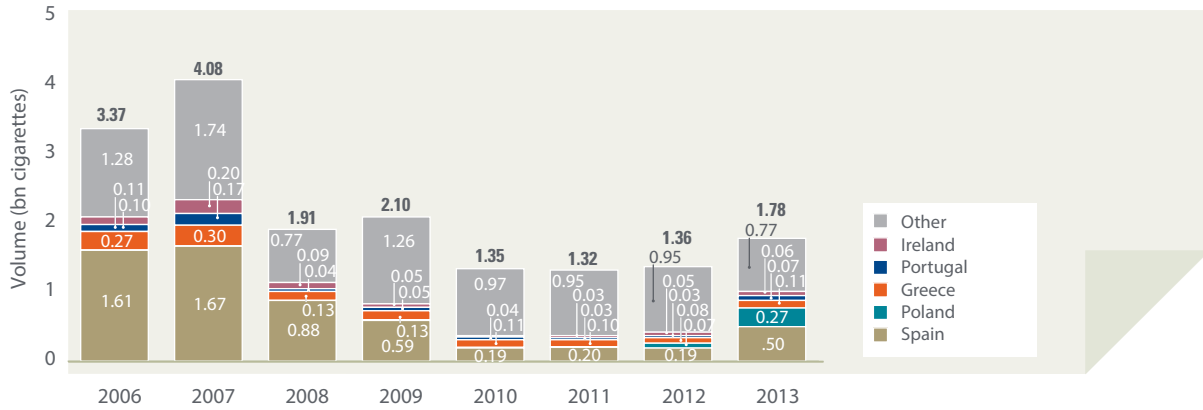
UK



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ND(L) volumes went up, as a result of an increase in all major flows

ND(L) by origin - 2006-2013^{(1)(2)(3)(a)(b)}



- ND(L) inflows into the UK have increased in 2013, driven by increased travel by UK residents and greater purchase quantities when travelling
- Spain and Greece are popular tourist destinations, and this is reflected in the ND(L) consumer research. Travel volumes and average purchases are sufficiently high for all inflows from these countries to be assumed to be legal
- Traveller numbers to Poland appeared under-represented in the 2013 consumer survey, and as a result were adjusted upwards using additional tourism data sources (refer to appendix for further details)
- Although Pakistan is a major source of non-domestic product, travellers who purchase cigarettes and average purchase volumes are low. As such most Pakistani origin inflows are categorised as C&C

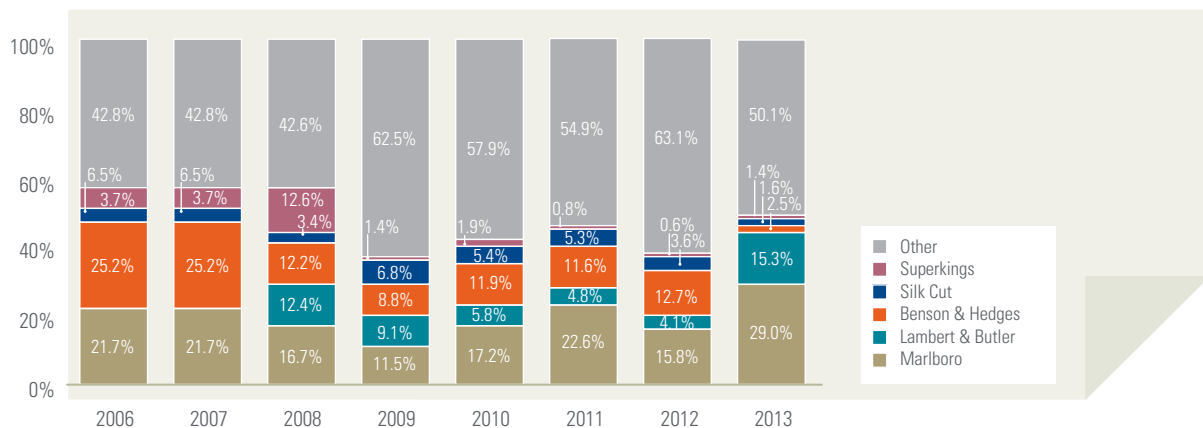
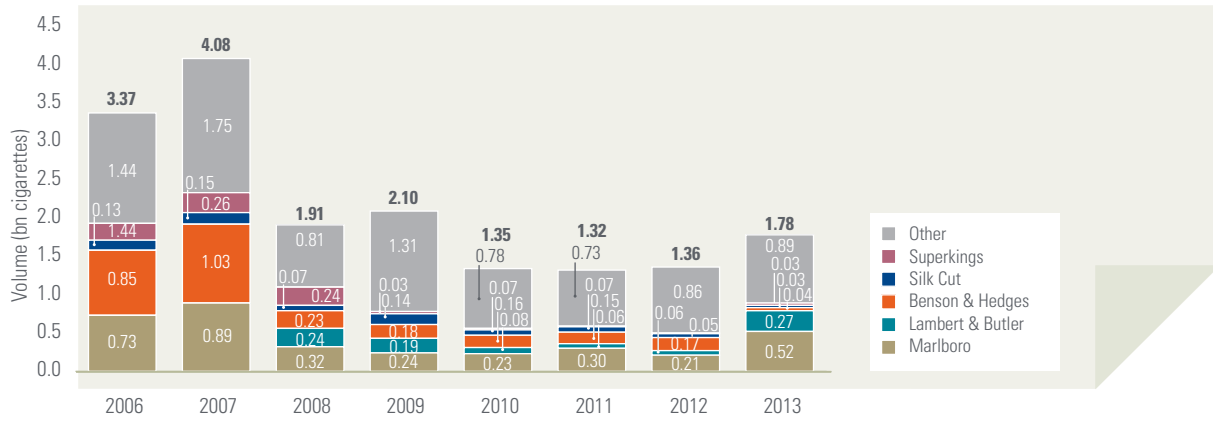
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows. (b) Additional details of key ND(L) calculations provided overleaf.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



NON-DOMESTIC LEGAL INFLOWS BY BRAND

Total ND(L) by brand - 2006-2013^{(1)(2)(3)(a)}



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Marlboro remains the most popular ND(L) brand in the UK

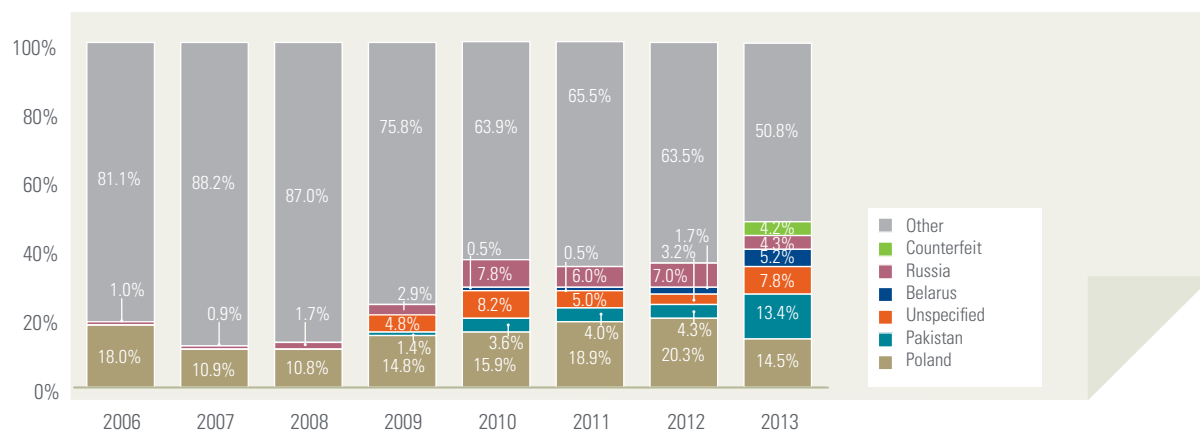
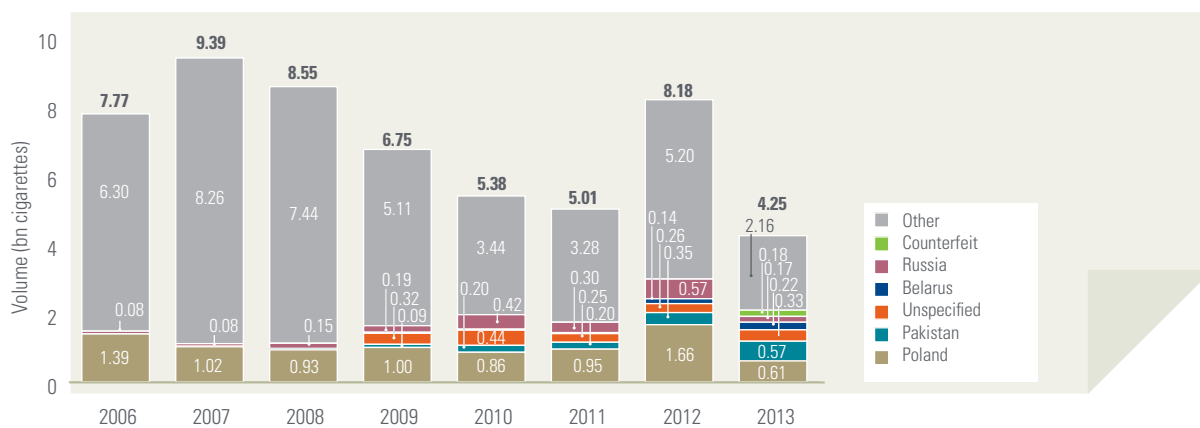
- 31% of the total legal Marlboro inflow comes from Poland
- 34% of the legal Lambert and Butler inflow came from Greece and Spain, both of which are popular holiday destinations from the UK

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.

A large decline in C&C inflows in 2013 was partially due to the impact of one-off events in 2012

Total C&C by brand - 2006-2013^{(1)(2)(3)(a)}



Total C&C in the UK appears to have decreased by 48% between 2012 and 2013, however much of this fall can be attributed to non-domestic levels falling back in line with long-term trends after a spike in non-domestic incidence in Q4 of 2012

- The National Audit Office highlighted that during the Olympic games Border Force staff shortages and the requirement to prioritise full passenger checks while managing queuing times reduced the time they spent undertaking other duties, such as customs controls⁽⁴⁾
- Poland has traditionally been, and continues to be, the main source of C&C into the UK, with the most popular brands being Marlboro and L&M
- Pakistan continues to grow as a source of C&C, 95% of which is the John Player Gold Leaf brand
- Inflows from Belarus and unspecified locations have continued to increase in 2013, and are mainly composed of Illicit Whites brands such as Fest (from Belarus) and Gold Classic, Palace and Richman (unspecified)
- If the 4.25bn C&C cigarettes in 2013 had been legally purchased in the UK the tax revenue gained would have been approximately €1.5bn

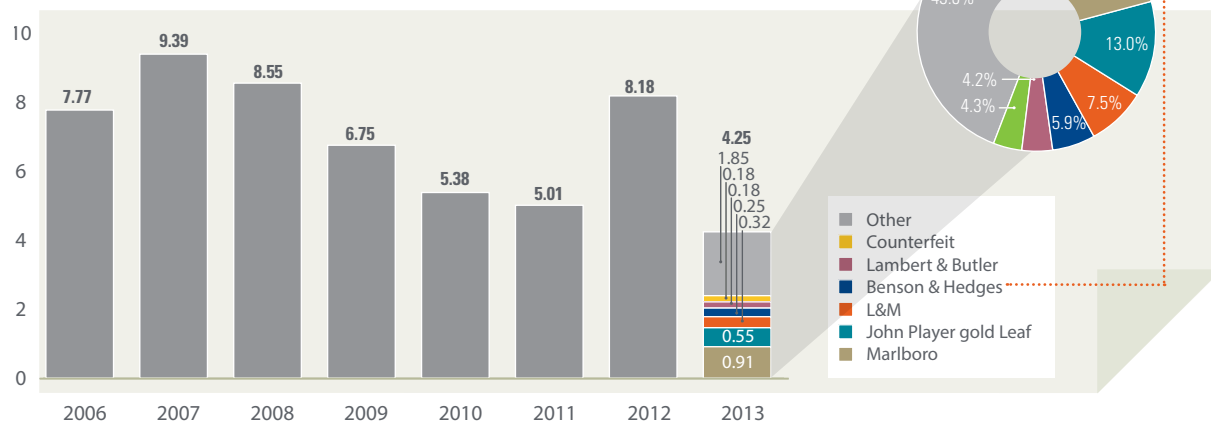
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers. (4) NAO – The Border Force: Securing the border, 4 September 2013.



C&C INFLOWS BY BRAND

Total C&C by origin - 2006-2013^{(1)(2)(3)(a)}



Established brands from the four major manufacturers are the largest component of C&C in the UK

- Marlboro is the most prevalent C&C brand in the UK. The main source country is Poland, which contributes 0.4bn cigarettes to the Marlboro C&C total
- Almost all the John Player Gold Leaf contraband is of Pakistani origin

11% of Duty Free inflows were Illicit Whites brands

Composition of Illicit Whites inflows - 2007-2013 (1)(3)(b)

LABELLING OF ILLICIT WHITES INFLOWS TO UK								
Billion cigarettes	2007	2008	2009	2010	2011	2012	2013	2012-13 %
Country specific	0.03	0.01	0.03	0.05	0.09	0.12	0.15	19%
Duty Free	0.06	0.04	0.18	0.52	0.39	0.72	0.59	(17)%
Unspecified	0.00	0.00	0.08	0.16	0.19	0.22	0.31	42%
Total Illicit Whites	0.09	0.05	0.29	0.72	0.67	1.06	1.06	(1)%

Illicit Whites are becoming an increasingly significant part of illicit trade in the UK, accounting for one quarter of C&C volumes in 2013

- Jim, Jin Ling and Bon are the main Illicit Whites marked as Duty Free, accounting for over half the Duty Free Illicit Whites balance
- Gold Classic, Richman and Palace are the main Illicit Whites marked as unspecified, accounting for more than half the unspecified Illicit Whites balance
- Fest from Belarus and Jing Ling from Russia contribute over 40% of the country specific Illicit Whites

Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows (b) A methodology and definition of Illicit Whites is provided in the methodology section.

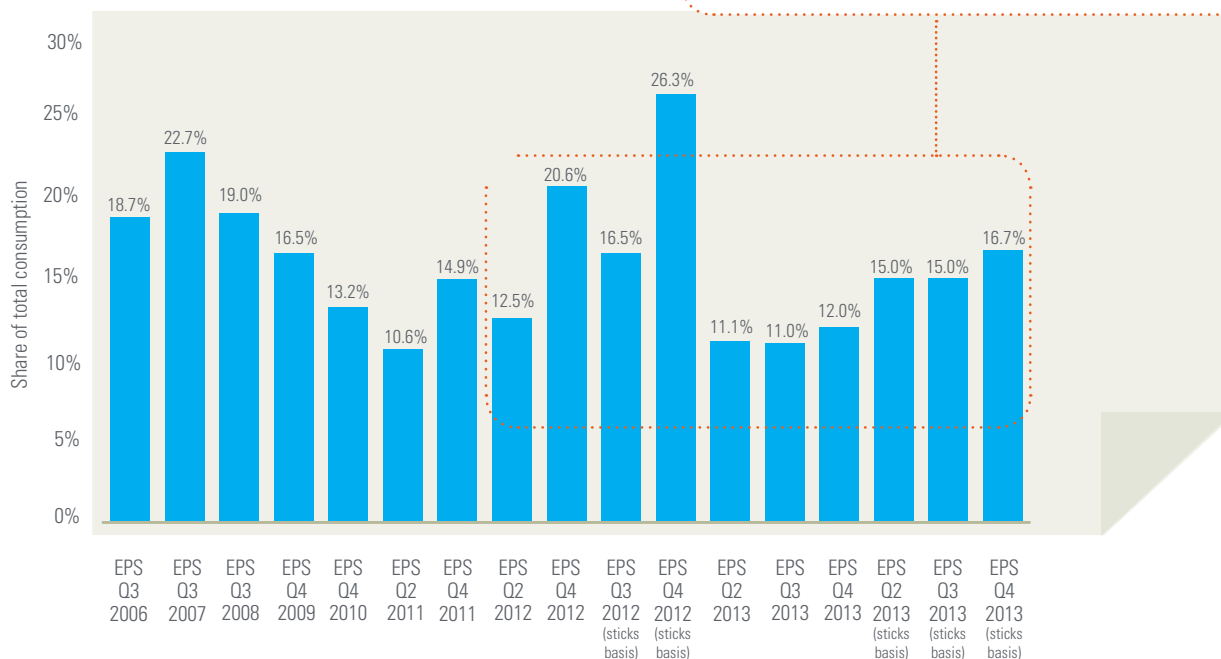
Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) KPMG analysis of data sources provided by manufacturers.



EPS results and EU flows model

Model results for 2012 and 2013 are calculated on a cigarettes basis. 2011 and prior results are on a packs basis.
 Results have been calculated on a stick basis to give a more accurate picture of the true volume of non-domestic product in the UK and to make the survey more comparable to other government and industry studies.

Empty Pack Survey non-domestic estimates - 2006-2013⁽¹⁾



- There is an element of seasonality in the UK EPS survey, with higher non-domestic incidence in the last quarter of the year. There is also a tendency to oversample domestic 10 packs, which has been corrected for in the Project Sun analysis
- The empty pack survey in the UK collected 38,100 packs during the second, third and fourth quarters of the year. It collects these packs across 105 towns and cities. The number of packs collected in the town or city is weighted by its population
- Since 2011 a seasonality effect has been noticeable in the UK EPS data, with Q4 being consistently higher than the other quarters. This may be attributable to UK travellers traditionally taking overseas holidays in July, August and September, with cigarettes purchased abroad then being consumed later
 - This seasonality may be another factor in the unusually high EPS incidence of 26.3% that was measured in Q4 2012
- In 2012 and 2013 an adjustment was made in our analysis to account for oversampling of domestic 10 packs. Comparing the number of UK 10 packs collected in the EPS with the legal domestic sales of 10 packs highlighted that they were oversampled by around 30% in the EPS survey. This adjustment leads to a decrease in non-domestic incidence as it increases the number of domestic packs with more than 10 cigarettes, thereby reducing the non-domestic proportion

UK



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Sources: (1) Independent agency Empty Pack Surveys, 2006 – 2013.

KPMG non domestic legal flows UK^(a)

2013 ND(L) research shows both an increase in travel and an increase in packs per trip to these countries

COUNTRIES WHERE ND(L) IS 100% OF TOTAL				
Country	ND 2013 ⁽¹⁾ (bn sticks)	2013 ND(L) (bn sticks)		% of ND
Spain	0.50	0.50		100%
Greece	0.11	0.11		100%
Portugal	0.07	0.07		100%
Ireland	0.06	0.06		100%

USE OF CONSUMER RESEARCH AND ADJUSTMENTS FOR 2013 DATA							
Country	ND 2013 ⁽¹⁾	Total trips where cigarettes purchased (m) <small>(2),(3),(4)</small>	Number of packs per trip ⁽²⁾	Total packs (m)	Data sources ⁽⁴⁾	2013 ND(L) (bn sticks)	% of ND
Poland	0.89	0.4m	37	2.4	Euromonitor	0.27	31%

Consumer research is used to calculate the ND(L) element of the inflow to the UK.

Spain, Greece and Portugal are popular holiday destinations, and traveller numbers and average packs purchased were large enough to classify these flows as 100% legal

Ireland has traditionally been a major source of cross-border shopping from the UK, especially from Northern Ireland. Given the frequency of border crossing and that Ireland is a higher priced market than the UK, this flow has also been considered 100% legal

ND(L) consumer research identified 65,000 travellers to Poland who purchased cigarettes. The average number of packs brought back when cigarettes were purchased was 37, which is in line with EU recommended limits

- However, Polish smoking incidence of 26.5% as per implied consumption data, and 1.6m trips to Poland per year suggests approximately 370,000 trips by smokers who are likely to purchase cigarettes. This was deemed a more realistic number of trips than that in the consumer research, and combining this with an average purchase of 37 packs leads to a ND(L) share from Poland of 0.27bn cigarettes, or 31% (5)

Although it is a major non-domestic source country, consumer research shows that only around 85,000 trips were made to Pakistan where cigarettes were purchased. The average number of packs brought back when cigarettes were purchased was 10, which is consistent with the 10 pack limit from Pakistan. This results in 3% of Pakistan inflows being assumed to be legal

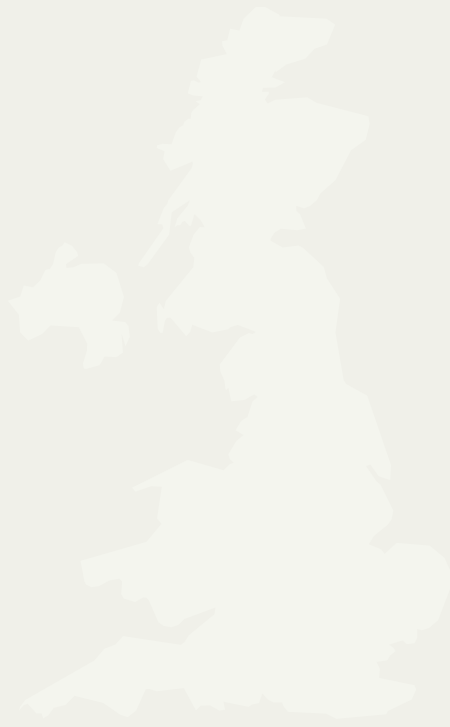
Note: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total inflows.

Sources: (1) KPMG EU Flows Model. (2) KPMG analysis of Synovate/Ipsos ND(L) research 2013 and EU flows model. (3) World Tourism Organization, Yearbook of Tourism Statistics dataset, 2013. (4) Euromonitor Passport travel data.

UK



PROJECT SUN



UK



PROJECT SUN



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METHODOLOGY

OVERVIEW



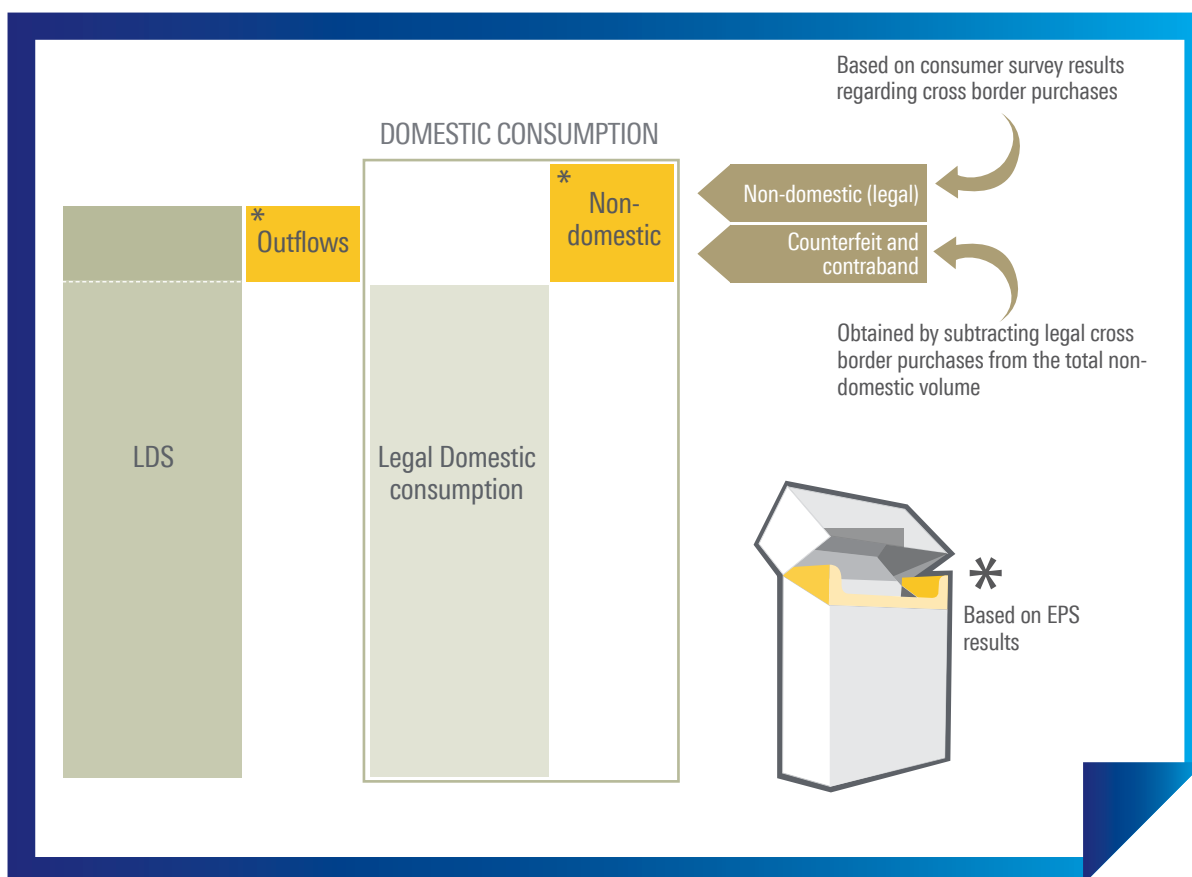
<p>KPMG has developed and refined its methodology for estimating counterfeit and contraband incidence across the 28 EU markets since 2006</p>	<p>The methodology has been tested extensively and refined to help deliver robust and defensible results</p> <ul style="list-style-type: none"> • Our approach integrates multiple sources and custom-built analytical tools • In 2013, Project SUN was commissioned jointly by the four major tobacco manufacturers (British American Tobacco plc, Imperial Tobacco Limited, JT International SA and Philip Morris International Management SA) for data covering 2013. KPMG LLP were previously commissioned by Philip Morris International Management SA to produce reports covering 2006 to 2012 ('Project STAR'). This has provided access to previously unavailable data sources in 2013
<p>The methodology is based primarily on objective evidence from LDS and EPS results, which are input to the bespoke KPMG EU Flows Model</p>	<p>The KPMG EU Flows Model is a dynamic, iterative model that is based on LDS and EPS results and is used to estimate overall manufactured cigarette volumes</p> <ul style="list-style-type: none"> • The KPMG EU Flows model has been developed by KPMG to specifically measure inflows and outflows of cigarettes between EU countries for the purpose of this Report. It is an iterative data driven model that uses LDS and EPS results to estimate the volume of non-domestic outflows and inflows to and from each EU Member State • LDS are the starting point of the methodology, from which outflows of legal sales to other countries are then subtracted to estimate legal domestic consumption • Non-domestic inflows from other countries are then added in to give an estimate for the total consumption within a market • This methodology has been developed by KPMG for the manufactured cigarettes market specifically. For that reason, an assessment of the OTP market (both legal and illicit) is excluded from the scope of this report
<p>EPS results provide a robust indication of the incidence of non-domestic and counterfeit packs by country of origin</p>	<p>EPS is the only market research method that relies purely on physical evidence, avoiding the variability of consumer bias found in interview-based methods</p> <ul style="list-style-type: none"> • The EPSs are conducted by independent market research agencies on a consistent basis across all the EU markets, allowing for direct comparison of data and the identification of inflows and outflows between all of the countries analysed • Over 500,000 packs were collected in 2013 as part of this research • Further detail regarding the reliability and validity of EPS, the sampling approach and results by country at a regional level are provided later in this document
<p>Primary market research, combined with tourism & travel trends and pricing changes, is used to estimate legal non-domestic cigarette purchases</p>	<p>The key objective of the market research programme undertaken by independent market research agencies is to estimate genuine, legal non-domestic tobacco purchases (including cross border shopping) in each market</p> <ul style="list-style-type: none"> • ND(L) data used in the analysis in the 2013 Project SUN Report is based upon approximately 160,000 full interviews and over 14,000 net respondents. This research was updated in 5 Member States during 2013 where over 27,000 interviews were conducted • Primary research is critical to deliver robust results as no other sources of sufficient detail and accuracy are available for legal cross border shopping <p>In addition to the research programme, ND(L) data has been adjusted by KPMG to reflect inbound visitor inflows and relative price changes</p> <ul style="list-style-type: none"> • This is especially relevant in countries where primary research was not carried out in 2013 <ul style="list-style-type: none"> - World Tourism Organisation⁽¹⁾ data is the primary source used to help corroborate travel trends, supplemented with other publicly available data - European commission releases⁽²⁾ are used to calculate changes in the weighted average price of a pack of cigarettes between regions

Sources: (1) UN WTO Tourism Factbook 2008-12.
 (2) European Commission Excise Duty tables (Part III – Manufactured Tobacco).

METHODOLOGY – OVERVIEW

Project SUN uses LDS, EPS results and other consumer research to estimate the volume of C&C cigarettes consumed in the EU

<p>There are some specific limitations in the Project SUN methodology</p>	<p>Given the innate complexity of measuring C&C, we recognise there are some limitations within the methodology</p> <ul style="list-style-type: none"> • There are broadly two types of limitations: scope exclusions and source limitations - scope exclusions include areas which cannot or have not been accounted for in our scope of work and approach, such as geographic, brand (non-participating manufacturer counterfeit), category exclusions (OTP) and legal domestic product flows out of the EU - source limitations include the availability of information and the potential errors inherent with any data sources such as sampling criteria, coverage issues and seasonality factors
<p>To help improve the accuracy of results, some minor refinements were necessary at a country level</p>	<p>Triangulation of results from alternative sources identified a few markets where country-to-country flows required minor adjustment</p> <ul style="list-style-type: none"> • In nearly all instances, overall country results and flows from the KPMG EU Flows Model appeared reasonable, however, in a limited number of instances, specific adjustments were made to country-to-country flows where additional data provided by manufacturers allowed for further refinement of the analysis



The Project SUN methodology was developed by KPMG. It has been deployed on a consistent basis since 2006, enabling comparisons to be made between counterfeit and contraband volumes from year to year. The OECD considers Project SUN “the most authoritative assessment of the level of counterfeit and contraband cigarettes across EU member states”

Calculation of non-domestic incidence on a stick basis in 2012 and 2013

Overview	<p>Prior to 2012, the KPMG EU Flows Model assumed that all packs collected were the same size (20 cigarettes). In 2012 the model was updated to take into account different pack sizes, and this approach has continued in 2013</p> <ul style="list-style-type: none"> • This update to the approach was made to help give a more accurate result for the volume flows between EU countries, as pack sizes vary on a country to country basis
Process	<p>EPS results provide the number of cigarettes in each packet</p> <ul style="list-style-type: none"> • It is therefore possible to calculate the total number of sticks accounted for by the pack collection despite the different sized packs, hence improving the overall accuracy of volume estimations
Impact	<p>The effect of this change on non-domestic incidence was dependant upon whether the typical domestic pack size was greater or less than the average pack size of 20 on a country by country basis</p> <ul style="list-style-type: none"> • The average pack contains 20 cigarettes • In countries where the average domestic pack size was less than 20 cigarettes (for example, most LDS in the UK and Italy are of 10 or 20 cigarette packs, giving an average domestic pack size of less than 20 cigarettes, and in Denmark domestic cigarettes are sold in packs of 19), then the conversion to a sticks basis is likely to decrease the proportion of domestic cigarettes in the EPS sample, giving a higher non-domestic incidence than estimating on a pack basis • In countries where the average domestic pack size is greater than 20 cigarettes (for example in Luxembourg domestic packs typically contain 20, 25 or 30 cigarettes), then the conversion to a sticks basis is likely to increase the proportion of domestic cigarettes in the EPS sample, giving a lower non-domestic incidence than estimating on a pack basis



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METHODOLOGY – LDS

LDS are the combination of sales data from all four manufacturers (BAT, ITL, JTI and PMI) and are built up on an individual brands basis

- Where available, LDS estimates for total market volumes and for manufacturers' own brands were provided for each country, by each manufacturer
- Each manufacturer's estimate of its own brands in that market, together with Nielsen data for all other brands, were then used to model total LDS in that country. An implied brand share is also calculated
- The total market figure was then compared to the market estimates provided by each manufacturer to cross check the modelled volume
- In previous years, Nielsen estimates were used for all non-PMI brands. The availability of sales by country and brand from all four manufacturers in 2013 has facilitated a more detailed analysis of LDS which has been input to the KPMG EU Flows model

Example LDS methodology ^{(1)(a)}

Manufacturer's estimate of their own brands used to model total sales

Country 1	BAT		ITL		JTI		PMI		Nielsen	Differences b/n manufacturers (bn sticks)			Section	Combined	
	LDS (bn sticks)	Market share (%)	LDS (bn sticks)	Market share (%)	LDS (bn sticks)	Market share (%)	LDS (bn sticks)	Market share (%)		BAT vs PMI	Imp vs PMI	JTI vs PMI		LDS (bn sticks)	Market share (%)
Brand A							5.25	20.8%				5.25	PMI	5.25	21.0%
Brand B	4.50	18.4%											BAT	4.50	18.0%
Brand C					3.80	15.0%					3.80		JTI	3.80	15.2%
Brand D			3.10	12.5%						3.10			ITL	3.10	12.4%
Brand E			2.40	9.7%						2.40			ITL	2.40	9.6%
Brand F					2.20	8.7%					2.20		JTI	2.20	8.8%
Brand G	1.50	6.1%											BAT	1.50	6.0%
Brand H									1.00				Nielsen	1.00	4.0%
Brand I							0.75	3.0%				0.75	PMI	0.75	3.0%
Brand J			0.50	2.0%						0.50			ITL	0.50	2.0%
Total market (bn sticks)	24.50		24.75		25.25		25.30							25.00	100.0%

Nielsen data used for brands not owned by BAT, ITL, JTI or PMI

Modelled LDS figure compared to manufacturer estimates



Where appropriate, nationally agreed external estimates of LDS have been used instead of the above approach

- In certain markets, publicly available estimates of legal manufactured cigarette sales are widely used by manufacturers, industry participants, government bodies and non-governmental organisations
- In these instances, it has been deemed more appropriate to incorporate these recognised estimates of LDS in the KPMG EU Flows model
- This is the case with:
 - Bulgaria: figure reported by the Bulgarian Customs Agency
 - France: figure reported by Altadis
 - Spain: figure reported by the Tobacco Commissioner
- The difference is then allocated to 'Undefined' brands in the above calculation

Note: (a) Example volumes included do not reflect actual sales data and are for illustrative purposes.

(b) LDS for Denmark was adjusted for forestalling seen in December 2013.

Sources: (1) LDS data provided by all four manufacturers.

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EPSs provide a highly objective and robust view of the incidence of non-domestic and counterfeit packs in each of the EU 28 countries sampled



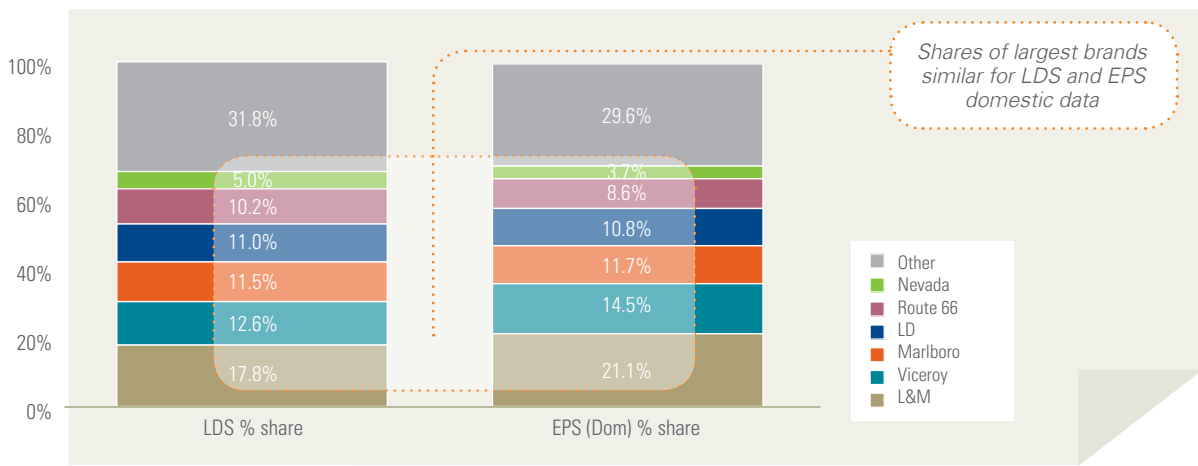
<p>Overview</p>	<p>EPSs are a research system of collecting discarded empty cigarette packs, the results of which are used to estimate the share of domestic (duty paid), non-domestic (non-duty paid) and counterfeit packs in each of the markets</p> <ul style="list-style-type: none"> • EPSs are conducted by independent market research agencies in each of the countries sampled. The surveys are commissioned by the manufacturers and the sampling plan is designed by the agencies in conjunction with the manufacturers to help make the sampling plan statistically representative within each given country • Results are based on a large sample of packs collected in various towns and cities throughout the countries, although the exact collection plan differs by country. Accuracy and credibility of results is driven by sound design of the sampling plan <ul style="list-style-type: none"> - Most country surveys sample the largest cities, the exceptions being: <ul style="list-style-type: none"> - Austria: 601 communes (administrative districts) are covered in the sample - France and UK: A regional sampling plan is used and the largest cities within those regions sampled. Regional shares of the EPS sample are proportionate to regional populations - Germany: The Yellow Bag Survey (YBS) collection occurs at waste recycling depots; 500 packs are randomly collected at 26 depots each month - Poland: The largest 40 cities and 30 smaller towns are sampled. This reflects the large rural population in Poland and the typically higher non-domestic incidence outside Polish cities - Romania: Sampling across three tiers: 1) largest 24 cities, 2) 12 cities (population > 40,000) and 3) 14 cities (population > 18,000) • Results are not subject to respondent behaviour and are therefore less prone to sampling errors than many other alternative methodologies • Evidence is based purely on physically collected packs, leaving no scope for respondent confusion • Results reflect actual overall non-domestic share and provide a good snapshot of brands consumed
<p>Process</p>	<p>EPSs rely purely on physical evidence, avoiding the variability of consumer bias in interview-based methods</p> <ul style="list-style-type: none"> • The independent market research agencies randomly collect empty packs of any brand and market variant from streets and easy access bins • Homes and workplaces are not visited and the collection route specifically excludes sports stadia, shopping malls and stations, or any other locations where non-domestic incidence is likely to be higher as a result of a skewed population visiting these areas • Once packs are collected, they are sorted by manufacturer and the number of packs with domestic versus non-domestic tax stamps are counted to determine the proportion of packs that did not originate from that jurisdiction (including Duty Free variants) <ul style="list-style-type: none"> - In cases where tax stamps are not shown on a packet, health warning and packaging characteristics are used to determine the source market • In markets where collection is handled centrally, packs are sent to the manufacturers for analysis to determine which are genuine and which are counterfeit. Only the manufacturers can determine this, based on inks, paper and other characteristics • KPMG uses the results of the EPSs to extrapolate overall consumption in the market by projecting LDS net of outflows, using the percentage of non-domestic cigarettes in the market as found through EPSs as inflows
<p>Coverage</p>	<p>EPSs are designed to be fit for purpose and the coverage per market is tailored to the size of the market, the likelihood of high non-domestic incidence and the manufacturers' share of the legal market</p> <ul style="list-style-type: none"> • Large surveys (10,000 packs or more collected): Austria, Bulgaria, Czech Republic, France, Germany, Hungary, Ireland, Italy, Lithuania, Netherlands, Poland, Romania, Spain, Sweden, UK • Medium surveys (5,000-9,999 packs): Belgium, Denmark, Estonia, Finland, Greece, Latvia, Slovakia • Small surveys (300-4,999 packs): Croatia, Cyprus, Luxembourg, Malta, Portugal, Slovenia

METHODOLOGY – EPS

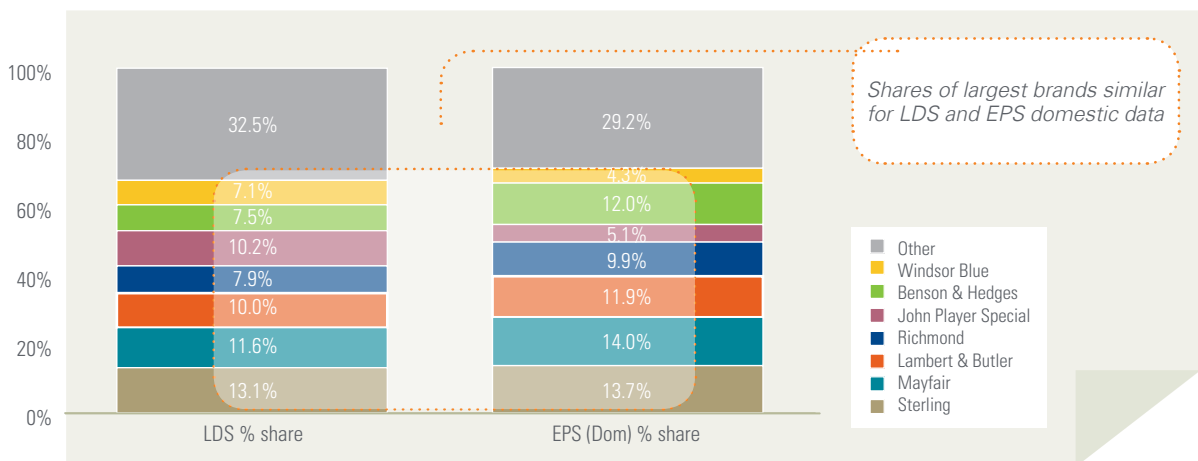
For many markets, the brand shares of domestic origin packs collected during the EPSs closely reflect the brand shares seen in the LDS data

- As brand shares of domestic origin packs closely reflect the brand shares seen in LDS, EPSs are therefore considered more reflective of actual consumption in a market, compared with results derived from focusing solely on illicit trade hotspots within cities
- This provides further confidence that the packs identified as non-domestic also fairly reflect the volume and brands actually consumed in that market (see exceptions on next page)
- As the EPSs collect any brand and market variant, there is no bias towards any specific brand being collected
- Two examples are shown below, for Poland and the United Kingdom

Comparison of LDS and domestic EPS brand Shares – Poland^(a)



Comparison of LDS and domestic EPS brand Shares – United Kingdom^(a)



Note: (a) Number of 'top' brands shown chosen to reflect approximately two thirds of the total market on an LDS and EPS basis.

Sources: (1) Analysis of LDS data provided by participating manufacturers.

(2) Independent agency EPSs, 2006-2013.



Where EPS results by brand deviate significantly from LDS brand shares, the methodology used by KPMG has been refined to adjust for this

- Some premium brands may be oversampled, largely due to their wide availability. For example, in 2013 oversampling of Marlboro in the EPS was seen in Belgium, France, Ireland, the Netherlands and Spain whereby a large proportion of Marlboro packs were collected than would be expected given domestic brand shares
- A second methodology has been used by KPMG to model non-domestic Marlboro which is more in line with the domestic brand share and the ND(L) results. This is discussed in detail on page 324. The balance is then allocated across 'Other' brands

In some other cases, additional analysis of the EPS data results in some further adjustments being made by KPMG in our analysis

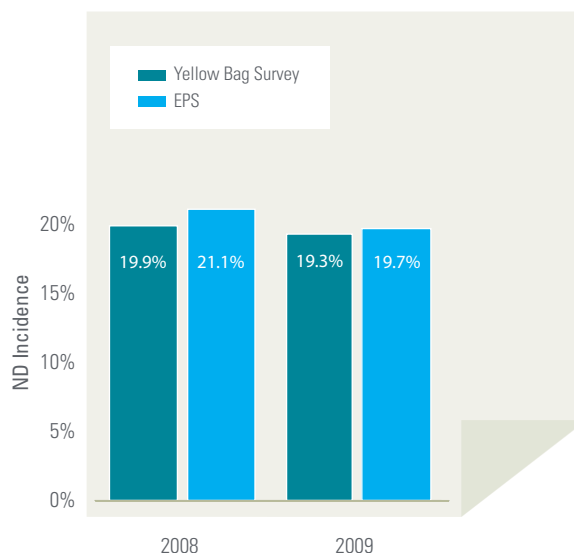
- Analysis is undertaken to compare the regional share of the EPS to the regional population share in each country. In markets where there is a large rural population or where specific inflows are seen to be under/overstated due to sampling, a regional adjustment may be made to re-weight the EPS results
- In markets where a large price change took place at a specific point in the year which has distorted non-domestic flows, EPS waves may be re-weighted to reflect differing periods of the year (i.e. if a price change took place in September, Q2 EPS results may reflect eight months and Q4 EPS results four months of the year)
- More specific adjustments may be made where, for example, actual sales data or travel statistics give a more accurate picture of incidence from a particular country



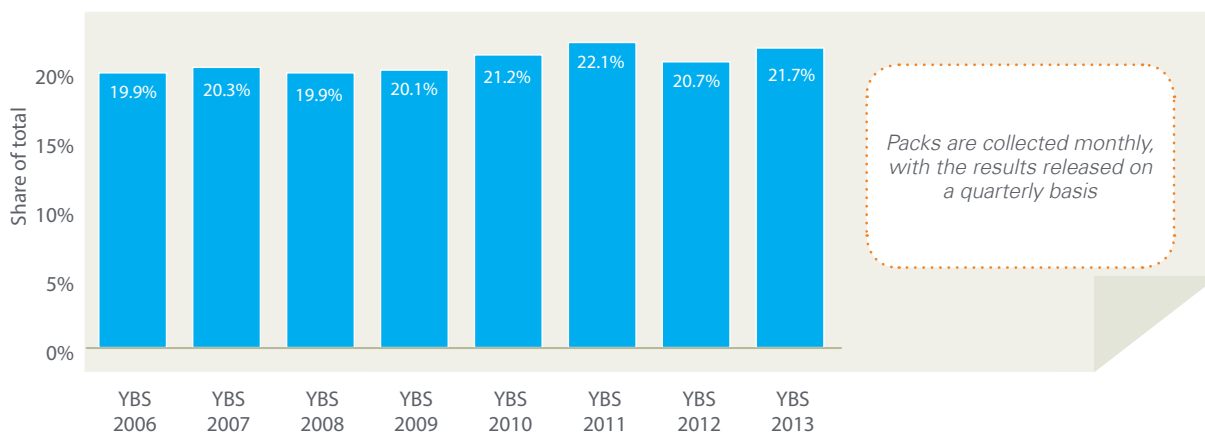
For Germany a comparison was undertaken by KPMG between the YBS and EPS methodologies in 2008 and 2009 which showed similar results

- The Yellow Bag Survey collects 500 packs per month from 24 waste disposal centres throughout Germany. As such, packs collected within Germany come from domestic and commercial waste disposal, rather than street collections and easy access public bins -
- Compared to the EPS street collection, the YBS results in a greater number of packs collected from a greater number of sources
- The monthly collection is also more regular than the quarterly waves conducted in the EPS
- In 2008 and 2009 quarterly EPSs were also undertaken within Germany
- The non-domestic incidence measured by the EPS was 1.2 percentage points higher in 2008 and 0.4 percentage points higher in 2009
- The results of this comparison demonstrates that the EPS collection methodology produces results which are broadly in line with the YBS and helps to validate the EPS methodology used in other countries

YBS and EPS results 2008-2009 ⁽¹⁾⁽²⁾



Germany historical Yellow Bag Surveys ⁽¹⁾



The low level of variance in German results supports the validity of using EPSs to monitor trends in cigarette consumption

- A low level of variance in the trend for non-domestic consumption has been apparent in each survey at both national and regional levels

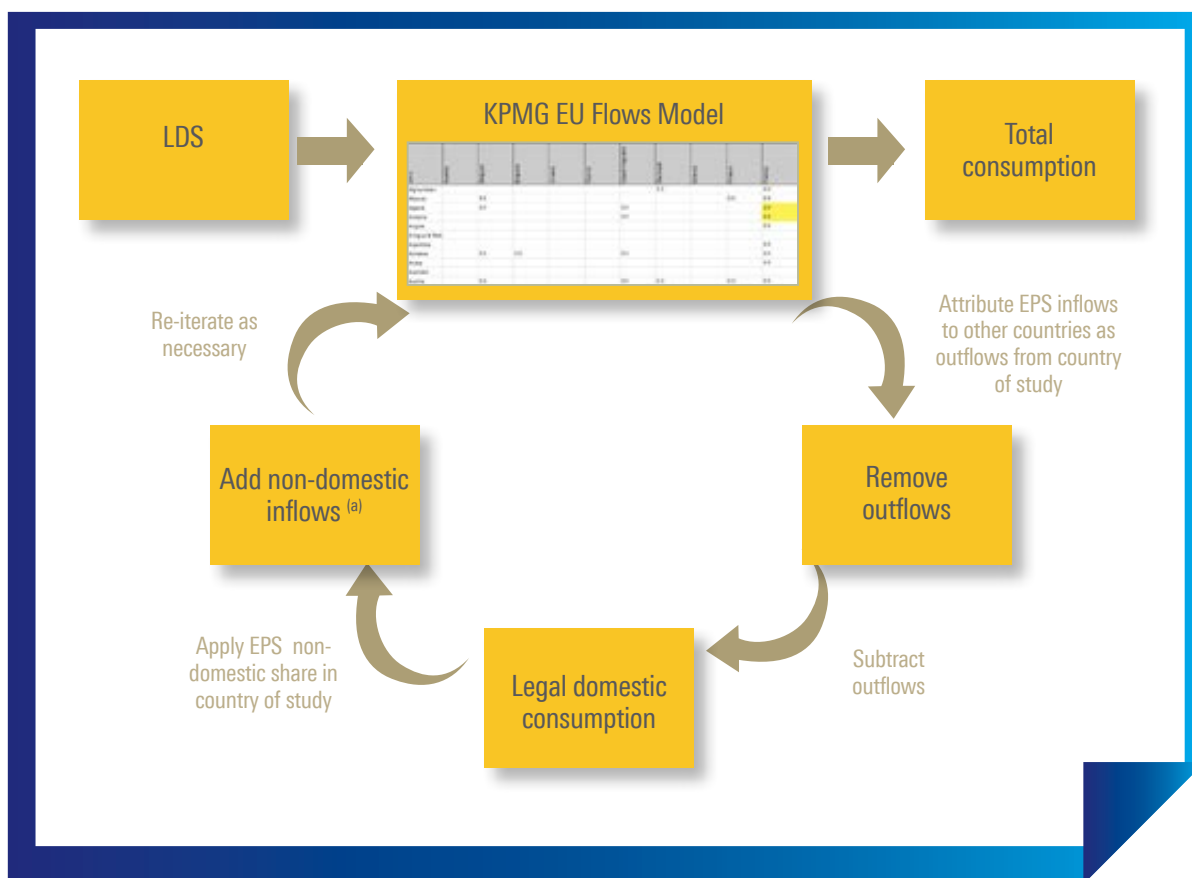
There is a strong correlation between changes in the German results and other sources including LDS, manufacturer shipment data and the observations of government bodies on cross border flows

- Underlying trends in country of origin and brand align with expectations and are corroborated by external sources

Sources: (1) Ipsos Yellow Bag Surveys, 2008-2009.
 (2) Ipsos Empty Pack Surveys, 2008-2009.

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The KPMG EU Flows Model is a dynamic, iterative model that is principally based on LDS and EPS results

- LDS are the starting point of the model from which outflows of legal sales to other countries are then subtracted to estimate legal domestic consumption in a market
- Non-domestic inflows from other countries are then added back in to give an estimate for the total consumption within a market
- The model is then re-iterated as necessary reflecting the relationship of inflows and outflows between all 28 EU countries
- EPS results provide a measurement of the share of non-domestic packs by country of origin in all markets
 - EPS results provide a consistent source across all 28 markets of non-domestic packs by country of origin from which we can calculate total product outflow from each market to the other 27 markets

Note: (a) The methodology to identify the ND(L) and C&C components of non-domestic flows is explained overleaf .



Brand share validation



Methodology comparison		
	Methodology one	Methodology two
Description	Non-domestic share of brand x Total consumption gap	Non-domestic share of brand x LDS by brand
Process	<ul style="list-style-type: none"> Any under/overstatement of domestic share of brands in EPS is not reflected in their non-domestic shares 	<ul style="list-style-type: none"> Any under/overstatement of domestic and non-domestic share of brands in EPS is proportional - i.e. If domestic packs of a brand are under/oversampled in the EPS, non-domestic packs are as well
Strengths	<ul style="list-style-type: none"> Brand totals tally to overall total of non-domestic Can track flows by brand and country Can calculate non-domestic volumes where no legal sales are present 	<ul style="list-style-type: none"> More robust for brands which are under/overweight in the EPS samples at a domestic brand share level
Limitations	<ul style="list-style-type: none"> Some potential to overstate premium brands due to concentration on cities in EPS - May lead to small IMS share / large EPS share discrepancies 	<ul style="list-style-type: none"> Totals by brand will not necessarily match total overall - most effective as an estimate of share of non-domestic for major brands

Two parallel methodologies for calculating non-domestic brand share were used to help ensure that reliable and realistic results were achieved

- While results at an overall market level were in line with domestic brand shares, smaller sample sizes at a brand level have the potential to introduce distortions
- In order to improve the accuracy of brand results, a dual methodology was used to estimate non-domestic brand-level results in each market
- The results from both approaches were then compared to both LDS and ND(L) brand results for corroboration
- In almost all markets and for the vast majority of brands the results for the two approaches were highly consistent
- In a few markets there were some brand-level discrepancies. In these markets, adjustments were made based on the weight of evidence from both approaches and the LDS and ND(L) findings to estimate the non-domestic brand share

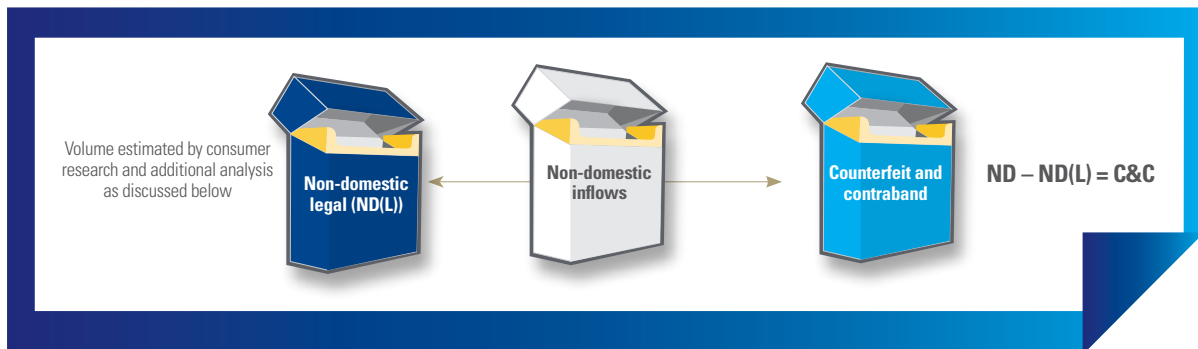
Brand share methodology two was used in a limited number of instances to help ensure that the results were both reliable and realistic

- Methodology one is the most universally applicable and was therefore used where both approaches were consistent. Where an adjustment from methodology one was deemed by KPMG to be required, a combination of both approaches or methodology two was applied as appropriate
- For Marlboro inflows in a few countries, a combination of both approaches or methodology two was used as it appears to give more reliable and robust results
 - Methodology two was used for Marlboro in France, Ireland and Belgium
 - A combination of both approaches was used for Marlboro in Spain and the Netherlands

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Non-domestic Legal analysis and assumptions



The non-domestic legal component of total non-domestic volumes is calculated using consumer research and refined on the basis of additional corroborating sources such as travel trends, border crossing and cigarette pricing data

Counterfeit and contraband volumes are the remaining ND balance after subtracting ND(L)

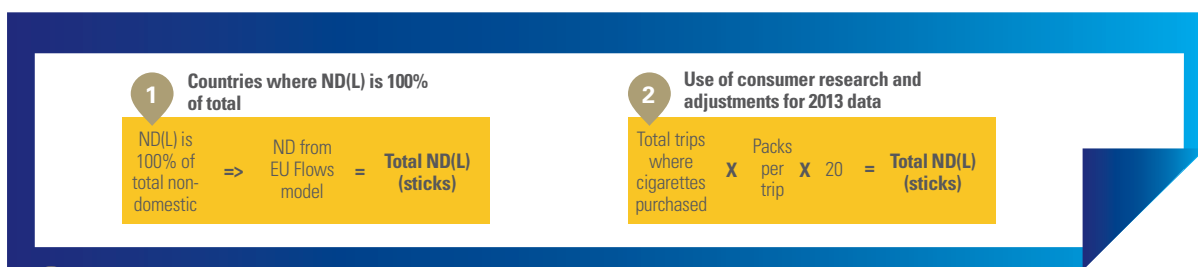
- Consumer research forms the basis of the ND(L) calculation. This is discussed overleaf
- Additional data sources are then analysed and may be used to adjust legal flows, where relevant, as below:

1) Flows where ND(L) is 100% of total ND

- Non-domestic product found in EPSs from higher priced inbound tourist/visitor countries is likely to represent an incidental inflow and is therefore categorised entirely as legal
- Where legal volumes per the consumer research exceed total non-domestic volumes (from the EPS), material flows are capped at 100% ND. Immaterial flows are not capped

2) Use of consumer research and adjustments for 2013

- For some material non-domestic legal flows, trips and packs were adjusted respectively for changes in travel trends and changes in relative prices (between markets) for manufactured cigarettes in 2013
- In exceptional cases where consumer research understated the flow of consumers, travel data and (implied) manufactured cigarette smoking prevalence were used instead
- In other cases where average packs purchased per trip seemed unreasonable, this was adjusted, for example by considering the legal purchase quantity or average packs from comparable markets



1 COUNTRIES WHERE ND(L) IS 100% OF TOTAL			
Country	ND 2013 (bn sticks) ⁽¹⁾	2013 ND(L) (bn sticks)	% of ND
Germany	0.62	0.62	100%

2 USE OF CONSUMER RESEARCH AND ANY ADJUSTMENTS FOR 2013 DATA								
Country	ND 2013 (bn sticks) ⁽¹⁾	Total trips where cigarettes purchased (m) ⁽²⁾⁽³⁾	Number of packs per trip ⁽²⁾	Total packs (m)	Data sources ⁽²⁾ ₍₃₎₍₄₎₍₅₎	2013 ND(L) (bn sticks)	2013 ND(L) (bn sticks)	% of ND
Belgium	0.62	8.63 ^(b)	10	90.40	Consumer research, WTO	1.81	0.62	90%

Notes: (a) KPMG calculates the split between C&C and ND(L) by calculating the ND(L) volume and subtracting from the total non domestic inflows.

Sources: (1) KPMG EU Flows Model. (2) Synovate/Ipsos ND(L) research 2013. (3) UN WTO Tourism Factbook 2008-12, UN WTO. (4) Population statistics from Insee.fr. (5) Car ownership data from European Environment Agency.

Consumer research approach to ND(L) analysis -

Approach	<ul style="list-style-type: none"> • Consumer research is conducted by independent market research agencies in selected countries. These take the form of consumer surveys which are commissioned by KPMG. The research questionnaire and sampling plan is designed by the agencies in conjunction with KPMG to help make the sampling plan statistically representative within each given country • The key objective of the market research programme (undertaken for the 2013 study by Ipsos) was to estimate genuine, legal non-domestic purchases of cigarettes in each market • The approach was to measure the number and volume of tobacco purchase instances from a complete, nationally representative sample of males and females, aged 19 years and over who have travelled abroad in the past 12 months <ul style="list-style-type: none"> - These results were then weighted and projected by age and gender to a national level to estimate the volume of legal non-domestic cigarettes brought back into each market by travellers returning from overseas and used in our analysis -The 2013 market research incorporated an extensive interview programme across 5 markets, totalling 2,300 full interviews from over 27,000 gross respondents
Sample	<ul style="list-style-type: none"> • The sample was drawn from a nationally representative database and was representative of both urban and rural areas, age and gender <ul style="list-style-type: none"> - A random sampling approach was used to help ensure results were reliable and could be projected to the total target population • A target of 7,000 gross contacts (i.e. agreed to be interviewed and aged 19 years and over) or 500 net (i.e. travelled abroad and purchased tobacco products in the past year) was set <ul style="list-style-type: none"> - These targets were considered sufficient by KPMG to derive accurate volume estimates once projected to the national population and set based on past experience from the research agencies and findings from previous reports
Data collection	<ul style="list-style-type: none"> • In each market, the method used was Computer Aided Telephone Interviewing (CATI) • The interview script was consistent across all markets, translated into local language and translated back into English for quality control purposes
Validation tools	<ul style="list-style-type: none"> • Validation tools were built into the script to enhance accuracy of responses, for example: <ul style="list-style-type: none"> - Respondents were asked to recall all trips abroad in the past year and purchase volumes and brands for each trip - For each trip, the purpose of visit was also recorded to ensure final results appear logical and within a reasonable range
Results capping	<ul style="list-style-type: none"> • In order to record legal personal purchases only, results were capped at an individual respondent level <ul style="list-style-type: none"> - Total annual purchases were limited to 1,000 packs per person, considered the absolute upper level for a heavy smoker who makes all of their purchases abroad - Purchases from non-EU destinations were limited to a maximum of 10 packs per trip in line with Duty Free purchase restrictions

Non-domestic legal research: gross and net respondents ^{(1)(a)}



Note: (a) * denotes country where ND(L) research was not updated in 2013.

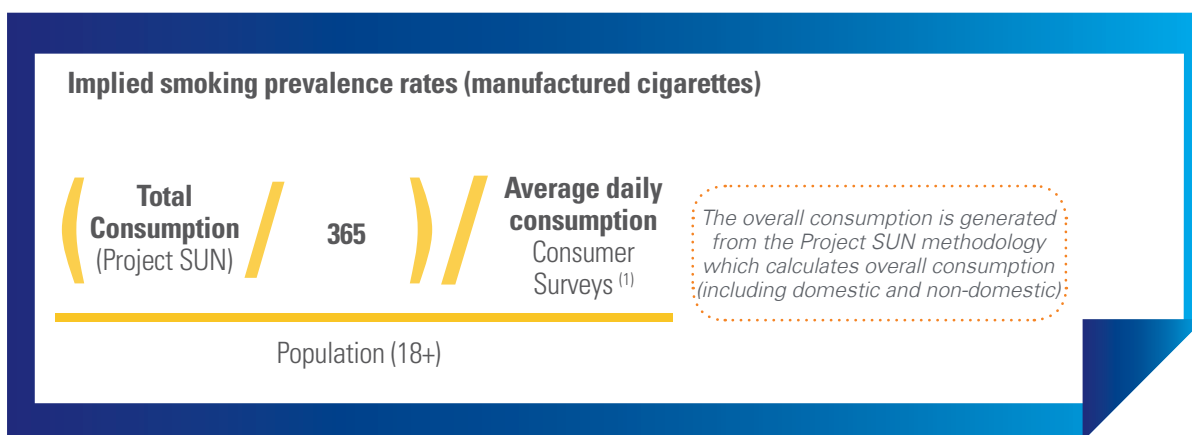
Source: (1) AC Nielsen, Ipsos/Synovate.



Non-domestic Legal analysis and assumptions

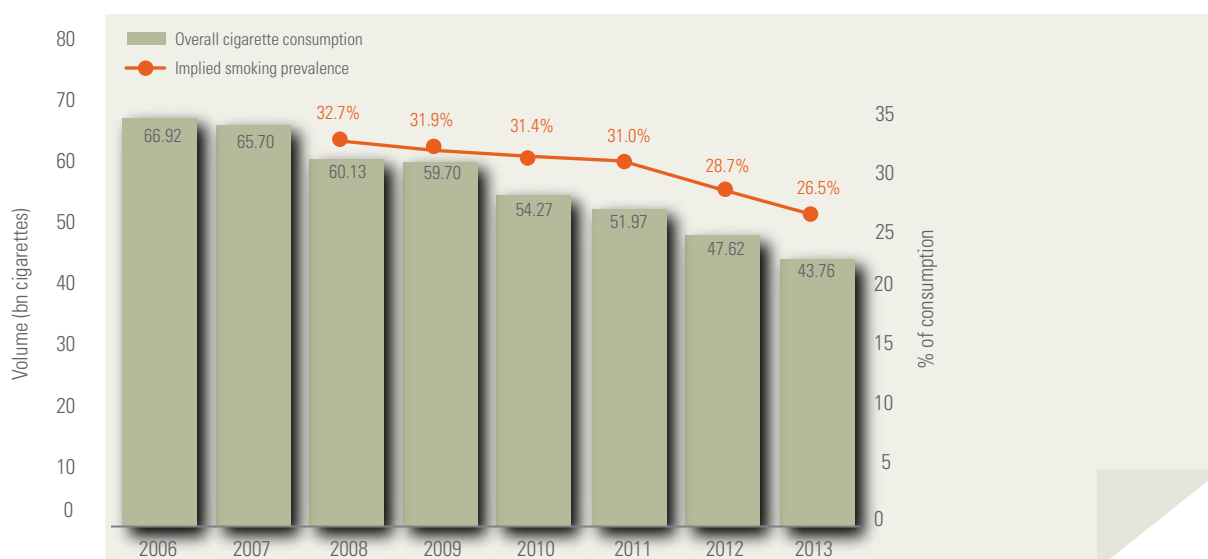
Calculation of implied smoking prevalence rate

- In order to calculate some of the non-domestic legal volumes, an approach is used by KPMG which reviews border crossings and the likely number of crossings which lead to the purchase of cigarettes. In order to undertake this calculation a national smoking prevalence figure is used.
- As a result, for the first time in 2013, a calculation has been developed in Project SUN to give the implied smoking prevalence by country, based on the overall consumption volumes calculated using the equation below. This measure is used in any ND(L) calculations.



- The implied smoking prevalence rate can be used to show how overall consumption of manufactured cigarettes impacts the prevalence rate as shown with the example of Poland below. In most cases the trend follows the same pattern as consumer survey based approaches.
- The approach enables a consistency for any ND(L) calculations

Manufactured cigarette consumption and implied smoking prevalence, Poland 2006-2013⁽²⁾



Sources: (1) Consumer surveys provided by manufacturers
 (2) KPMG EU flows model



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METHODOLOGY – ILLICIT WHITES ANALYSIS

Illicit Whites have grown at a CAGR of 40% between 2007 and 2013 and now account for 33% of total C&C volumes in the EU. As such, they represent a significant part of our overall analysis

- Illicit Whites are defined as
 - Cigarettes that are usually produced legally in one country/market, primarily for smuggling. While they may also be exported legally from some countries, they are smuggled across borders during their transit to their final destination market where they have limited or no legal distribution and are sold without payment of tax⁽¹⁾
- Each participating manufacturer provided Illicit Whites brand lists. A compiled list was developed for the purpose of Project SUN analysis
- Once the brand has been identified, its overall volume was determined across the EU

*Five of the top 20 Illicit Whites brands by volume in 2013 are manufactured by Grodno Tobacco
The 13 Grodno Tobacco brands identified as Illicit Whites account for 5.01bn cigarettes, or 25.5% of the total*

LARGEST ILLICIT WHITES BRANDS BY VOLUME (2013) ⁽²⁾			
Brand	Manufacturer	Source country	Volume (bn cigarettes)
Fest	Grodno Tobacco	Belarus	2.10
Jin Ling	Baltic Tobacco Factory	Russia	1.66
American Legend	Karelia Tobacco	Greece	1.49
Ducal	H. Van Landewyck GMBH	Multiple source countries	0.98
NZ	Grodno Tobacco	Belarus	0.92
Gold Mount	Kaane American International Tobacco	United Arab Emirates	0.86
Minsk	Grodno Tobacco	Belarus	0.77
Raquel	Explosal Ltd.	Cyprus	0.75
Premier	Grodno Tobacco	Belarus	0.72
RGD	China National	China	0.70
Gold Classic	Explosal Ltd.	Cyprus	0.51
Email	Manifattura Italiana Tabacco	Italy	0.43
Brendal	Unspecified TMOs	Unspecified	0.31
Elixir	H. Van Landewyck GMBH	Multiple source countries	0.27
Yesmoke	Yesmoke Tobacco	Italy	0.27
Queen	Grodno Tobacco	Belarus	0.23
Ronhill	TDR	Bosnia and Herzegovina	0.23
Lifa	Baltic Tobacco Factory	Russia	0.23
Corsair	King's Tobacco	Multiple source countries	0.22
President	European Tobacco	Lebanon	0.21
			13.87
Share of total volume	<i>Despite identifying over 350 Illicit Whites brands, the top 20 account for over two thirds of total volume this year</i>		70.7%
Total Illicit Whites			19.61

Sources: (1) ITIC.

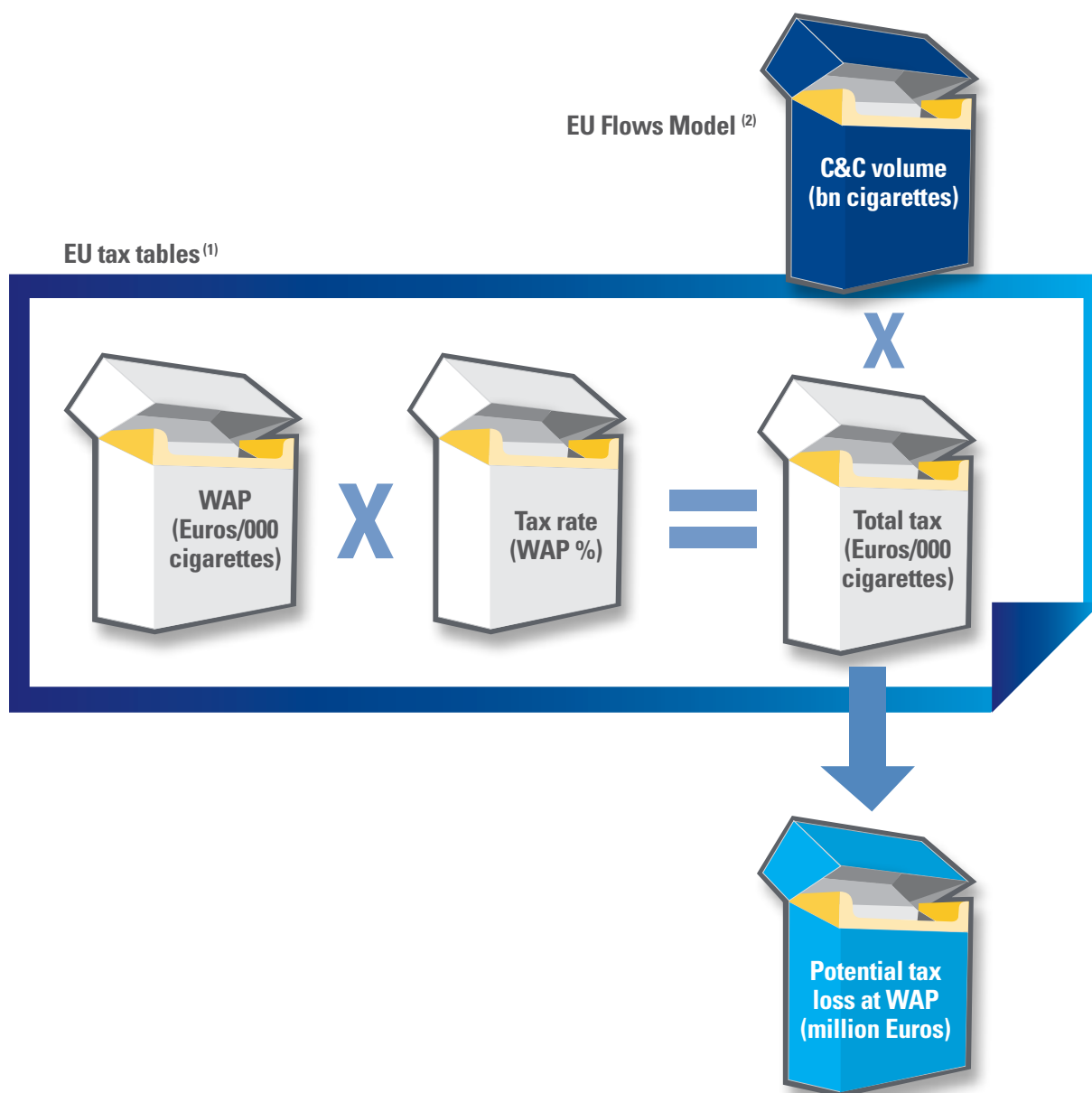
(2) KPMG EU Flows Model and analysis of data sources provided by manufacturers.

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Tax losses are calculated to estimate the tax revenue that would have been gained had the volume of C&C cigarettes consumed been legally purchased in that country

- The calculation shown below was performed for each country:
 - EU tax tables were used to determine the WAP for cigarettes in July 2013
 - This is then multiplied by the tax rate (as a % of WAP)
 - The resultant tax (per 1,000 cigarettes) is multiplied by the C&C consumption volumes for that country per the EU Flows Model to give the total potential tax loss based on WAP
- Total tax losses for the EU 28 countries based on WAP were estimated to be €10.9bn in 2013
- This was a decrease versus prior year (2012: €12.5bn)



Sources: (1) EC Excise Duty tables (Part III – Manufactured Tobacco) as at 1 July 2013.

(2) KPMG EU Flows Model and analysis of data sources provided by manufacturers.

APPENDICES – LIMITATION OF RESULTS

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Scope limitations

- There are specific scope exclusions which cannot be or have not been accounted for in our approach:
 - geographic exclusions
 - brand exclusions: non-major manufacturer counterfeit
 - category exclusions: OTP
 - LDS product flows out of the EU

Source limitations

- Limitations are, of necessity, present with any primary information source
- This primarily affects EPS, LDS and ND(L) sources
- For example, limitations can arise from:
 - sampling criteria
 - coverage issues
 - timing/seasonality factors
 - specific regional or demographic exclusions

We have designed a methodology that we consider is robust and inclusive. However, given the innate complexity of C&C, our methodology has some limitations, which we have sought to minimise.



APPENDICES – LIMITATION OF RESULTS

Limitation	Detail	Impact	Adjustment
Geographic coverage	<ul style="list-style-type: none"> We have limited our geographic coverage in some markets where extension would significantly impair confidence levels in the ND(L) research for the further territories included In some instances (e.g. Greek islands), LDS data is also insufficient for the purposes of this study 	<ul style="list-style-type: none"> Spanish results only cover mainland Spain and do not include the Canary Islands, Balearic Islands or Ceuta & Melilla French results cover only mainland France and do not include Corsica. As a result, LDS from Corsica are not included in France consumption figures Portuguese results only cover mainland Portugal and do not include Madeira or the Azores Greek results only cover mainland Greece and do not include the Greek islands UK results only cover Great Britain and Northern Ireland and do not include the Channel Islands 	Not adjusted for
Non-major manufacturer counterfeit	<ul style="list-style-type: none"> EPS results do not identify counterfeit packs that have been made by manufacturers other than British American Tobacco plc, Imperial Tobacco Limited, JT International SA and Philip Morris International Management SA - only the manufacturer / trademark owner can confirm whether their brand pack is genuine 	<ul style="list-style-type: none"> In some instances, the volume of legal domestic consumption may be overstated where domestic counterfeit variants are identified – this may lead to minimal understatements of C&C volumes for some brands Moreover, we cannot distinguish between non-major manufacturer brand counterfeit (non-domestic variants) and contraband product, although this will not impact the overall volume of C&C 	Not adjusted for
OTP	<ul style="list-style-type: none"> EPSs collect cigarette packs only Non-domestic consumption for OTP cannot be measured via EPS results 	<ul style="list-style-type: none"> Reports in a number of countries suggest that non-domestic consumption of OTP may have been growing in recent years. These observations are supported by Customs organisations in some countries 	Not adjusted for
Non-EU outflows	<ul style="list-style-type: none"> In order to calculate consumption, we have assumed no outflows of LDS outside the EU, with the exception of outflows from Sweden to Norway 	<ul style="list-style-type: none"> Net outflows besides those from Sweden to Norway are believed to be minimal, supported by both anecdotal evidence and from non-EU EPS surveys (for example, Switzerland) Non-EU LDS outflows are not considered to be material due to the high prices relative to other parts of the world and Duty Free import restrictions 	Partially adjusted for





Source	Limitation
EPSs	<ul style="list-style-type: none"> • Whilst the EPS for every country is designed to be representative of the overall population, in some countries, owing to the geographical circumstances or demographics it is not possible to ensure that the sample is fully representative. This may be because: <ul style="list-style-type: none"> - the sample is more heavily weighted towards populous, urban areas and therefore may not be fully representative of consumption habits in rural regions (for example, in Romania) - homes and workplaces or public spaces are not covered • Results from Germany are based on a monthly analysis of approximately 10,000 packs collected at recycling centres and so are not directly comparable with the EPS results from other countries due to the difference in methodology, however, both methods produce similar results (see methodology section for details) • Although EPS dates are selected to minimise seasonal factors, there may be specific events that impact the results such as significant price changes between countries and major sporting events <ul style="list-style-type: none"> - in some instances the timing of EPSs has changed between years. In order to ensure comparability of results, monthly LDS figures, consumption trends and visitor data are all analysed and adjustments made where appropriate • Brand and market variant share can only be extrapolated with a degree of statistical accuracy for brands where a sufficiently large number of packs have been collected • EPS results are analysed to identify any outliers that may impact results, such as geographic concentrations of a specific brand or market variant. Brand specific data is also compared to known sales in the source market to identify whether results are credible <ul style="list-style-type: none"> - where data suggests a sampling or data capture error may have occurred at a specific location, results are adjusted and the remainder of the survey is re-weighted accordingly • In some specific instances it is not possible to differentiate between Duty Free and Duty Paid variants from the empty packs collected as the tear tape on the packet is required in order to make the necessary distinction

- **However, EPS represents a consistent and independent source of non-domestic share across markets based purely on physical evidence collected. Brand trends and analysis of country flows from EPS results further supports this conclusion**

APPENDICES – LIMITATION OF RESULTS

Source	Limitation
LDS	<ul style="list-style-type: none"> • In some cases tax stamp data may not correspond to the calendar year and may also be distorted by inventory holdings in advance of increases in taxation. In these instances we have used the LDS source considered by local country management to be representative of smoker consumption during the calendar year, or official government data sources (for example, in Bulgaria) • AC Nielsen Retail Audit data is derived from retail sales information but may exclude particular sales channels or retailers <ul style="list-style-type: none"> - In markets where we have used Retail Audit data, AC Nielsen have calculated an appropriate uplift to derive total market sales, including volumes not accounted for in Retail Audit data • Slight timing variances may arise between the date the product was shipped and actual consumption but, following discussions with local management, this is not considered significant and the full year LDS information we have is considered to be a fair and accurate representation in each market
ND(L)	<ul style="list-style-type: none"> • As with any CATI-based market research approach, our samples may potentially exclude certain demographic segments, in particular, those without a permanent home, registered address or telephone line • The nature of the market research programme requires that people can recall, with a high degree of accuracy, trip and purchase volumes undertaken over the past year. However, pilot and roll-out results give us confidence that this is not a significant issue for respondents • Respondents are asked to recall purchase volumes in packs and we assume 20 cigarettes per pack for our pack to cigarette conversion • To help ensure that we record legal imports only, we have capped total individual purchases and applied a cap to imports from certain source countries where import restrictions apply • Due to the nature of the survey, market research does not capture ND(L) product arising from inbound tourism. However, these flows are likely to be limited in nature and, in many cases, can be adjusted within the ND(L) methodology through the use of corroborating sources • It is not possible to reliably distinguish between Duty Free and Duty Paid variants in the ND(L) research due to the consumer confusion when buying cigarettes abroad, particularly in airports when travelling intra-EU. We have however attempted to estimate legal Duty Free purchases by using ND(L) inflows from non-EU markets as an approximation. This approach assumes that EU nationals purchase Duty Free variants when they travel to non-EU markets and buy cigarettes as measured by the ND(L) research <ul style="list-style-type: none"> - this assumption is predicated on the fact that Duty Free variants are typically available at a lower prices than legal tax-paid cigarettes in non-EU destination countries




























APPENDICES – EPS RESULTS BY COUNTRY

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APPENDICES – EPS RESULTS FOR EU 28 COUNTRIES

EU 28 countries		Number of packs		ND incidence	
Region		2012	2013	2012	2013
Austria		27,494	25,485	22%	20%
Belgium		5,800	5,600	15%	17%
Bulgaria		13,000	13,000	19%	21%
Croatia		3,000	3,000	9%	5%
Cyprus		1,000	1,000	4%	6%
Czech Republic		21,003	21,004	3%	5%
Denmark		10,000	5,300	6%	6%
Estonia		6,600	6,600	25%	22%
Finland		5,000	5,000	20%	21%
France		23,000	34,500	25%	25%
Germany		23,166	32,089	21%	22%
Greece		14,000	7,000	14%	20%
Hungary		12,350	24,709	4%	9%
Ireland		10,000	10,000	28%	28%
Italy		20,000	40,000	12%	5%
Latvia		9,800	9,800	34%	30%
Lithuania		12,800	12,800	32%	29%
Luxembourg		326	400	6%	8%
Malta		1,050	1,000	13%	15%
Netherlands		14,000	14,000	21%	22%
Poland		51,000	51,000	14%	15%
Portugal		3,000	3,000	3%	2%
Romania		27,900	18,600	11%	10%
Slovakia		5,000	5,000	2%	3%
Slovenia		3,000	3,000	9%	11%
Spain		29,484	29,404	10%	11%
Sweden		10,000	10,000	12%	13%
UK		25,400	38,099	21%	15%
Total		485,006	518,302	15%	15%



APPENDICES – EPS RESULTS BY COUNTRY

Austria EPS results by region, 2012-13⁽¹⁾

Austria Region	Number of packs		ND incidence	
	2012	2013	2012	2013
Burgenland	3,907	2,987	17%	15%
Kärnten	5,531	5,546	41%	35%
Niederösterreich	4,144	3,871	21%	19%
Oberösterreich	3,586	3,180	16%	22%
Salzburg	1,066	1,663	4%	9%
Steiermark	3,263	2,398	12%	13%
Tirol	1,309	1,581	5%	6%
Vorarlberg	381	308	1%	2%
Wien	4,307	3,951	23%	20%
Total	27,494	25,485	22%	20%



Source: (1) Austria Chamber of Commerce Empty Pack Surveys, 2012-2013.

APPENDICES – EPS RESULTS BY COUNTRY

Belgium EPS results by region, 2012-13⁽¹⁾


Belgium Region		Number of packs		ND incidence	
		2012	2013	2012	2013
Aalst		0	100	0%	6%
Anderlecht		0	120	0%	9%
Antwerp		1,086	550	14%	12%
Antwerpen		0	550	0%	14%
Arlon		0	160	0%	44%
Brugge		0	240	0%	19%
Brussels		951	500	15%	18%
Charleroi		0	460	0%	13%
East Flanders		662	100	9%	18%
Flemish Brabant		325	0	8%	0%
Genk		0	200	0%	20%
Gent		0	500	0%	12%
Hainaut		670	0	17%	0%
Hasselt		0	200	0%	25%
Kortrijk		0	200	0%	20%
Leuven		0	200	0%	13%
Liege		481	440	10%	31%
Limburg		337	0	9%	0%
Luxembourg		271	0	64%	0%
Mechelen		0	200	0%	20%
Mons		0	200	0%	10%
Namur		466	240	10%	25%
Sambreville		0	160	0%	21%
Schaerbeek		0	280	0%	16%
West Flanders		551	0	9%	0%
Total		5,800	5,600	15%	17%


Source: (1) MS Intelligence Empty Pack Surveys, 2012-2013.



APPENDICES – EPS RESULTS BY COUNTRY

Bulgaria and Croatia EPS results by region, 2012-13⁽¹⁾

Bulgaria Region		Number of packs		ND incidence	
		2012	2013	2012	2013
Blagoevgrad				0%	0%
Burgas		660	660	12%	17%
Dobric		300	300	11%	11%
Gabrovo				0%	0%
Grad Sofia		3,960	3,960	15%	20%
Haskovo		708	708	31%	25%
Jambol		244	244	25%	20%
Kjustendil				0%	0%
Lovec		352	352	18%	16%
Montana				0%	0%
Pazardzik		236	236	29%	32%
Pernik		264	264	16%	11%
Plovdiv		1,114	1,114	17%	18%
Razgrad				0%	0%
Ruse		492	492	9%	17%
Silistra				0%	0%
Sliven		302	302	37%	31%
Sumen		266	266	6%	3%
Varna		1,102	1,102	12%	22%
Veliko Tarnovo				0%	0%
Vidin				0%	0%
Other		3,000	3,000	28%	26%
Total		13,000	13,000	19%	21%

Croatia Region		Number of packs		ND incidence	
		2012	2013	2012	2013
Osijek		193	193	18%	20%
Pula		132	132	12%	12%
Rijeka		294	294	9%	1%
Sesvete		126	126	10%	3%
Slavonski Brod		124	124	43%	18%
Split		383	383	7%	4%
Zadar		163	163	3%	1%
Zagreb		1,585	1,585	7%	4%
Total		3,000	3,000	9%	5%


Source: (1) Nielsen Empty Pack Surveys, 2012-2013.



APPENDICES – EPS RESULTS BY COUNTRY

Cyprus, Czech Republic and Denmark EPS results by region, 2012-13⁽¹⁾⁽²⁾⁽³⁾

Cyprus 	Number of packs		ND incidence	
	2012	2013	2012	2013
Larnaca	150	150	2%	4%
Limassol	318	300	3%	5%
Nicosia	422	400	5%	8%
Paphos	110	150	2%	5%
Total	1,000	1,000	4%	6%

Czech Republic 	Number of packs		ND incidence	
	2012	2013	2012	2013
Jihocesky Kraj	724	724	4%	3%
Jihomoravsky Kraj	2,148	2,148	3%	5%
Karlovarsky Kraj	300	300	3%	4%
Kralovehradecky Kraj	526	526	3%	4%
Liberecky Kraj	1,034	1,034	3%	4%
Moravoslezsky Kraj	3,332	3,332	3%	6%
Olomoucky Kraj	1,062	1,062	4%	5%
Pardubicky Kraj	510	510	2%	5%
Plzensky Kraj	948	948	3%	6%
Praha	7,113	7,114	3%	5%
Stredocesky Kraj	636	636	3%	5%
Ustecky Kraj	1,750	1,750	3%	6%
Vysocina	496	496	2%	4%
Zlinsky Kraj	424	424	2%	5%
Total	21,003	21,004	3%	5%

Denmark 	Number of packs		ND incidence	
	2012	2013	2012	2013
Capital Region	5,186	2,593	6%	6%
Mid Jutland	2,028	1,014	6%	7%
North Jutland	842	421	6%	6%
South Denmark	1,944	1,122	6%	5%
Zealand		150	0%	9%
Total	10,000	5,300	6%	6%

Sources: (1) Nielsen Empty Pack Surveys, 2012-2013.


(2) Ultex Empty Pack Surveys, 2012-2013.


(3) MS Intelligence Empty Pack Surveys, 2012-2013.



APPENDICES – EPS RESULTS BY COUNTRY

Estonia and Finland EPS results by region, 2012-13⁽¹⁾⁽²⁾

Estonia		Number of packs		ND incidence	
		2012	2013	2012	2013
Region					
Harju		3,200	3,200	21%	18%
Ida-Viru		1,100	1,100	48%	46%
Lääne		200	200	22%	27%
Lääne-Viru		200	200	30%	24%
Pärnu		300	300	18%	16%
Saare		200	200	24%	24%
Tartu		800	800	14%	13%
Valga		200	200	40%	41%
Viljandi		200	200	18%	22%
Võru		200	200	22%	22%
Total		6,600	6,600	25%	22%

Finland		Number of packs		ND incidence	
		2012	2013	2012	2013
Region					
Keski-Suomi		329	329	27%	22%
Kymenlaakso		222	222	19%	23%
Paijat-Hame		255	255	23%	23%
Pirkanmaa		537	537	20%	23%
Pohjois-Savo		244	244	22%	22%
Prohiois-Pohianmaa		357	357	18%	20%
Uusimaa		2,610	2,610	19%	21%
Varsinais-Suomi		446	446	16%	20%
Total		5,000	5,000	20%	21%



Sources: (1) Nielsen Empty Pack Surveys, 2012-2013.

(2) MS Intelligence Empty Pack Surveys, 2012-2013.

APPENDICES – EPS RESULTS BY COUNTRY

France EPS results by region, 2012-13⁽¹⁾


France Region	Number of packs		ND incidence	
	2012	2013	2012	2013
Alsace Lorraine Champagne Ardennes	2,200	3,300	34%	36%
Aquitaine	1,400	2,100	31%	26%
Auvergne Limousin	1,000	1,500	25%	19%
Basse Haute Normandie	1,600	2,400	23%	18%
Bourgogne Franche Comte	2,000	3,000	23%	21%
Bretagne	2,000	3,000	17%	17%
Centre	1,000	1,500	20%	22%
Ile De France	3,000	4,500	21%	24%
Languedoc Roussillon Midi Pyrenees	1,600	2,400	30%	24%
Nord Picardie	2,000	3,000	32%	33%
Pays De Loire Poitou Charentes	1,600	2,400	17%	18%
Provence Alpes Cote D Azur	1,600	2,400	29%	30%
Rhone Alpes	2,000	3,000	18%	26%
Total	23,000	34,500	25%	25%




Source: (1) MS Intelligence Empty Pack Surveys, 2012-2013.

APPENDICES – EPS RESULTS BY COUNTRY

Germany and Greece EPS results by region, 2012-13⁽¹⁾⁽²⁾

Germany		Weighted number of packs		ND incidence	
Region		2012	2013	2012	2013
Baden-Württemberg		2121	1946	12%	10%
Bavaria		2977	3437	24%	30%
Berlin		1591	1416	45%	40%
Brandenburg		832	1824	75%	75%
Bremen		0	391	0%	10%
Hamburg		870	852	10%	10%
Hesse		3232	7299	11%	11%
Lower Saxony		1141	1071	12%	13%
Mecklenburg-Vorpommern		900	1920	39%	41%
North Rhine-Westphalia		4675	5199	12%	14%
Rhineland-Palatinate		0	887	0%	11%
Saxony		3049	3062	46%	49%
Saxony-Anhalt		0	1049	0%	36%
Schleswig-Holstein		902	806	15%	13%
Thüringen		876	930	31%	42%
Total		23,166	32,089	21%	22%


Greece		Number of packs		ND incidence	
Region		2012	2013	2012	2013
Attica		4600	2300	20%	25%
Central Greece		400	200	15%	19%
Central Macedonia		3000	1500	15%	22%
Crete		1000	500	5%	22%
East Macedonia/Thrace		800	400	15%	25%
Epirus		600	300	12%	16%
Ionian Islands		400	200	12%	16%
South Aegean		400	200	17%	9%
Thessaly		1200	600	7%	15%
West Greece		1200	600	6%	8%
West Macedonia		400	200	16%	17%
Total		14,000	7,000	14%	20%

Sources: (1) Ipsos Yellow Bag Surveys, 2012-2013 (Germany).

(2) Nielsen Empty Pack Surveys, 2012-2013.

APPENDICES – EPS RESULTS BY COUNTRY

Hungary and Ireland EPS results by region, 2012-13⁽¹⁾⁽²⁾

Hungary		Number of packs		ND incidence	
Region		2012	2013	2012	2013
Bács-Kiskun		980	1960	6%	11%
Baranya		0	0	0%	0%
Békés		420	840	6%	13%
Borsod-Abaúj-Zemplén		205	410	0%	0%
Budapest		6249	12500	4%	9%
Csongrád		205	410	22%	21%
Fejér		211	430	2%	3%
Győr-Moson-Sopron		535	1070	1%	7%
Hajdú-Bihar		1195	2390	6%	11%
Heves		390	780	2%	7%
Jász-Nagykun-Szolnok		205	409	0%	0%
Komárom-Esztergom		145	290	4%	9%
Nógrád		0	0	0%	0%
Pest		915	1830	3%	5%
Somogy		490	980	0%	4%
Szabolcs-Szatmár-Bereg		205	410	0%	0%
Tolna		0	0	0%	0%
Vas		0	0	0%	0%
Veszprém		0	0	0%	0%
Zala		0	0	0%	0%
Total		12,350	24,709	4%	9%


Ireland		Number of packs		ND incidence	
Region		2012	2013	2012	2013
Connacht		800	800	24%	30%
Leinster		6450	6450	29%	29%
Munster		2550	2550	28%	27%
Ulster		200	200	29%	29%
Total		10,000	10,000	28%	28%


Sources: (1) GfK Hungary Empty Pack Surveys, 2012-2013.
 (2) MS Intelligence Empty Pack Surveys, 2012-2013.



APPENDICES – EPS RESULTS BY COUNTRY

Italy and Latvia EPS results by region, 2012-13⁽¹⁾⁽²⁾

Italy		Number of packs		ND incidence	
Region		2012	2013	2012	2013
Abruzzo		182	400	10%	2%
Calabria		276	552	4%	5%
Campania		1808	3648	45%	17%
Emilia Romagna		2172	4416	7%	3%
Friuli Venezia Giulia		304	608	28%	2%
Lazio		4246	7892	6%	4%
Liguria		904	1796	5%	3%
Lombardia		2580	5284	10%	9%
Marche		152	400	7%	2%
Piemonte		1504	3080	8%	4%
Puglia		986	1968	6%	3%
Sicilia		1956	3920	8%	4%
Toscana		1062	2128	7%	3%
Trentino Alto Adige		172	400	9%	2%
Umbria		416	896	7%	2%
Veneto		1280	2612	13%	3%
Total		20,000	40,000	12%	5%

Latvia		Number of packs		ND incidence	
Region		2012	2013	2012	2013
Kurzeme		1200	1200	35%	32%
Latgale		1400	1400	40%	46%
Pieriga		1400	1400	26%	29%
Riga		4000	4000	33%	27%
Vidzeme		800	800	27%	32%
Zemgale		1000	1000	40%	25%
Total		9,800	9,800	34%	30%


Sources: (1) MS Intelligence Empty Pack Surveys, 2012-2013.

(2) Nielsen Empty Pack Surveys, 2012-2013.



APPENDICES – EPS RESULTS BY COUNTRY

Lithuania, Luxembourg and Malta EPS results by region, 2012-13⁽¹⁾⁽²⁾

Lithuania		Number of packs		ND incidence	
		2012	2013	2012	2013
Region					
Alytus		800	800	36%	40%
Kaunas		3000	3000	32%	28%
Klaipeda		1600	1600	24%	18%
Marijampole		600	600	55%	35%
Panevezys		800	800	38%	36%
Siauliai		800	800	29%	28%
Taurage		200	200	46%	44%
Telsiai		800	800	36%	31%
Utena		600	600	19%	16%
Vilnius		3600	3600	34%	31%
Total		12,800	12,800	32%	29%

Luxembourg		Number of packs		ND incidence	
		2012	2013	2012	2013
Region					
Esch-Sur-Alzette		160	160	0%	7%
Luxembourg		166	240	12%	8%
Total		326	400	6%	8%

Malta		Number of packs		ND incidence	
		2012	2013	2012	2013
Region					
Northern		383	350	12%	14%
Northern Harbour		544	550	14%	16%
Southern Harbour		123	100	16%	16%
Total		1,050	1,000	13%	15%

Sources: (1) Nielsen Empty Pack Surveys, 2012-2013.

(2) MS Intelligence Empty Pack Surveys, 2012-2013.



APPENDICES – EPS RESULTS BY COUNTRY

Netherlands and Poland EPS results by region, 2012-13⁽¹⁾⁽²⁾

Netherlands		Number of packs		ND incidence	
Region		2012	2013	2012	2013
Drenthe		206	206	21%	22%
Flevoland		502	502	20%	20%
Friesland		334	334	22%	18%
Gelderland		1088	1088	19%	24%
Groningen		358	358	18%	27%
Limburg		760	760	25%	24%
North Brabant		1862	1862	23%	25%
North Holland		3078	3078	19%	24%
Overijssel		996	996	22%	22%
South Holland		3954	3954	23%	19%
Utrecht		862	862	18%	24%
Total		14,000	14,000	21%	22%

Poland		Number of packs		ND incidence	
Region		2012	2013	2012	2013
Dolnoslaskie		3,900	3,900	4%	7%
Kujawsko-Pomorskie		2,775	2,775	8%	11%
Lodzkie		3,375	3,375	25%	22%
Lubelskie		2,550	2,550	25%	28%
Lubuskie		1,350	1,350	4%	4%
Malopolskie		2,925	2,925	8%	12%
Mazowieckie		8,100	8,100	22%	22%
Opolskie		1,800	1,800	3%	4%
Podkarpackie		2,850	2,850	33%	28%
Podlaskie		1,425	1,425	42%	40%
Pomorskie		2,325	2,325	3%	2%
Slaskie		7,350	7,350	11%	11%
Swietokrzyskie		1,575	1,575	5%	5%
Warminsko-Mazurskie		2,400	2,400		
Wielkopolskie		4,050	4,050	1%	2%
Zachodniopomorskie		2,250	2,250	3%	5%
Total		51,000	51,000	14%	15%

Sources: (1) MS Intelligence Empty Pack Surveys, 2012-2013.


(2) Almares Research Empty Pack Surveys, 2012-2013.




APPENDICES – EPS RESULTS BY COUNTRY

Portugal, Romania and Slovakia EPS results by region, 2012-13⁽¹⁾

Portugal		Number of packs		ND incidence	
		2012	2013	2012	2013
Center		162	162	1%	0%
Lisboa		1910	1910	2%	2%
North		928	928	6%	3%
Total		3,000	3,000	3%	2%

Romania		Number of packs		ND incidence	
		2012	2013	2012	2013
Bucharest		7,423	5,027	11%	8%
Center		3,749	2,512	5%	2%
North-East		3,627	2,276	15%	18%
North-West		3,228	2,278	9%	10%
South		2,639	1,687	15%	13%
South-East		4,057	2,573	12%	11%
West		3,176	2,247	13%	13%
Total		27,900	18,600	11%	10%


Slovakia		Number of packs		ND incidence	
		2012	2013	2012	2013
Banskobystricky Kraj		450	450	0%	1%
Bratislavsky Kraj		1,200	1,200	1%	1%
Kosicky Kraj		800	800	4%	7%
Nitriansky Kraj		650	650	1%	1%
Presovsky Kraj		600	600	5%	7%
Trenciansky Kraj		400	400	2%	0%
Trnavsky Kraj		300	300	0%	3%
Zilinsky Kraj		600	600	0%	1%
Total		5,000	5,000	2%	3%


Source: (1) Ipsos Empty Pack Surveys, 2012-2013.



APPENDICES – EPS RESULTS BY COUNTRY

Slovenia and Spain EPS results by region, 2012-13⁽¹⁾⁽²⁾

Slovenia		Number of packs		ND incidence	
Region		2012	2013	2012	2013
Celje		211	211	8%	10%
Koper		141	141	17%	11%
Kranj		207	207	27%	4%
Ljubljana		1,530	1,530	8%	10%
Maribor		535	535	7%	13%
Nova Gorica				0%	0%
Novo Mesto		131	131	0%	7%
Ptuj		102	102	0%	6%
Velenje		143	143	17%	27%
Total		3,000	3,000	9%	11%

Spain		Number of packs		ND incidence	
Region		2012	2013	2012	2013
Andalucia		5,098	5,070	33%	39%
Aragon		1,095	1,100	3%	1%
Asturias		839	823	4%	6%
Basque Country		1,469	1,490	6%	7%
Cantabria		304	293	8%	5%
Castilla Y Leon		1,309	1,311	7%	3%
Castilla-La Mancha		289	288	1%	3%
Catalonia		5,299	5,298	7%	8%
Comunidad Valenciana		2,782	2,778	3%	4%
Extremadura		258	257	42%	39%
Galicia		1,074	1,077	10%	8%
La Rioja		252	256	2%	5%
Madrid		7,974	7,928	4%	4%
Murcia		1,105	1,102	5%	5%
Navarra		337	332	6%	3%
Total		29,484	29,404	10%	11%


Sources: (1) Nielsen Empty Pack Surveys, 2012-2013.

(2) Ipsos Empty Pack Surveys, 2012-2013.



APPENDICES – EPS RESULTS BY COUNTRY

Sweden EPS results by region, 2012-13⁽¹⁾


Sweden		Number of packs		ND incidence	
Region		2012	2013	2012	2013
Blekinge		90	90	16%	4%
Dalarna		101	101	7%	4%
Gävleborg		190	190	15%	6%
Götaland		84	84	17%	5%
Halland		226	226	14%	4%
Jönköping		233	233	6%	8%
Kalmar		97	97	3%	10%
Kronoberg		154	154	4%	8%
Norrbottn		126	126	3%	3%
Örebro		272	272	13%	11%
Östergötland		500	500	9%	13%
Skåne		1,177	1,177	22%	26%
Skellefteå		90	90	0%	4%
Södermanland		225	225	12%	13%
Södertälje		167	167	9%	17%
Stockholm		3,461	3,461	11%	12%
Uppsala		355	355	10%	11%
Värmland		162	162	8%	6%
Västerbotten		209	209	4%	2%
Västernorrland		136	136	7%	12%
Västmanland		296	296	9%	7%
Västra Götaland		1,649	1,649	13%	12%
Total		10,000	10,000	12%	13%

Source: (1) HUI Research Empty Pack Surveys, 2012-2013.



APPENDICES – EPS RESULTS BY COUNTRY

UK EPS results by region, 2012-13⁽¹⁾

UK Region		Number of packs		ND incidence	
		2012	2013	2012	2013
East Midlands		1,803	2,704	25%	15%
East Of England		2,328	3,492	21%	17%
London		3,099	4,648	29%	19%
North East England		1,087	1,630	19%	17%
North West England		2,908	4,362	19%	16%
Northern Ireland		728	1,092	18%	12%
Scotland		2,187	3,281	11%	10%
South East England		3,457	5,185	23%	17%
South West England		2,129	3,194	23%	16%
Wales		1,254	1,881	14%	13%
West Midlands		2,278	3,416	22%	15%
Yorkshire And The Humber		2,143	3,214	23%	14%
Total		25,400	38,099	21%	15%



Source: (1) MS Intelligence Empty Pack Surveys, 2012-2013.

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APPENDICES – SOURCES

External data sources

The sources listed below are those used only in the 2013 analysis in this 2013 Project SUN Report. Sources for analysis and findings for previous years can be found in previous year reports

Other Sources

'Achat de tabac à l'étranger : Bruxelles ouvre les frontières', RMC (France), March 2013

Almares Research Empty Pack Surveys, 2006-2013

Arrivals of tourists by country of usual residence, 1980-2012, Republic of Cyprus, Statistical Service, downloaded April 2014

Bulgarian Customs Agency data for legal domestic sales volumes in 2012 and 2013

Croatian Statistical Office, Tourism statistics, 2013

Czech Statistical Office, "Overnight visitors, 2013"; Downloaded March 2014

'Dutch Government unveils 2014 tax plan', Tax News, September 2013

Economist Intelligence Unit, 2014

Estonian Customs (Tulli), Customs Instructions for Passengers, July 2013

European Commission Excise Duty tables (Part III – Manufactured Tobacco) as at July 2012, January 2013 and July 2013

European Commission Releases for consumption of fine cut tobacco 2002-2012

Eurostat, 'Euro area annual inflation down to 0.7%', November 2013

Foreign exchange rates, Euromonitor, downloaded March 2014

Fuel prices, Euromonitor, downloaded April 2014

Gallus et al. "Temporal changes of under-reporting of cigarette consumption in population-based studies"; Tobacco Control Journal, 2011

GfK Empty Pack Surveys, 2006-2013

Government of Andorra, "Arrivals from Spain, 2013"; Reviewed March 2014

Government of Gibraltar, "Land, Air and Sea entrances to Gibraltar, 2013"; Reviewed March 2014

Gross Domestic Product (GDP), Euromonitor, downloaded March 2014

HMRC, Tobacco Tax Gap Estimates, 2012/13, 11th October 2013

HUI Research Empty Pack Surveys, 2006-2013

'Hungary's tobacco law: Leaked tape causes outrage', BBC News, July 2013

'In France, an E-Cigarette Bubble?', New York Times, October 2013

Ipsos Empty Pack Surveys, 2006-2013

Ipsos Yellow Bag Surveys, 2006-2013 (Germany)

Irish Health and Safety Executive, Cigarette Smoking Prevalence in Ireland, April 2014

Irish Revenue Commissioners, Cigarette Consumption Survey, 2013

Irish Examiner, Fears Gangs to Produce Counterfeit Cigarettes in Ireland, February 2014

JTI Pack Swap Survey Results 2008-2013



External data sources

Other Sources
MS Intelligence Empty Pack Surveys, 2006-2013
NAO –The Border Force: Securing the border, 4 September 2013
Nielsen Empty Pack Surveys, 2006-2013
Novel Illicit Trade Tracking Study, November 2013
Personal Disposable Income (PDI), Euromonitor, downloaded March 2014
Polish institute of Tourism, “Border crossings from Germany, 2012,” Downloaded March 2014
Polish Institute of Tourism, “Overnight visitors, 2013” Downloaded March 2014
Romanian Census Results, 2011
Rural and urban population estimates, Euromonitor, downloaded January 2014
Seizure data, Polish Ministry of Finance
‘Smoking Ban for All Cafes from 1 July 2014’, NIS News, 2014
Smoking incidence, Fondation Cancer (Luxembourg)
‘State to issue new tobacco licenses’, Budapest Business Journal, April 2013
Statistik Austria, unemployment data
Synovate / Ipsos ND(L) research 2013
Tobaksrapport 2013, HUI Research, 2013
Tourism statistics, January- December 2013, Republic of Cyprus, Statistical Service, downloaded April 2014
‘Travailleurs frontaliers occupés au Luxembourg selon la résidence et la nationalité (en 1 000 personnes) 1974 – 2012’, Inspection Générale de la Sécurité Sociale
Ultex Empty Pack Surveys, 2006-2013
UNWTO Tourism Factbook 2008-12, UNWTO
Unemployment, Euromonitor, downloaded March 2014



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The scope of work below forms the basis of our contract with the Beneficiaries

1. This study will report on the estimated size and composition of the total cigarette market (including counterfeit and contraband products), as detailed below, for each of the 28 EU Member States.
2. The findings from the work on the 28 EU Member States will be used to produce a report which includes a consolidated section covering an overall view of the total EU market. We will also provide a section in the report on counterfeit and contraband flows for each of the EU Member States.
3. Our analysis of the cigarette market will be based on a methodology that incorporates primary research, market analysis, expert interview programmes and existing industry surveys.
 - For each of the EU Member States, we will use in market sales data to estimate LDS and estimate Legal Domestic Consumption by subtracting outflows to other countries based on the results of EPSs.
 - Non domestic inflows for each EU Member State will be based on the results of EPSs and added to Legal Domestic Consumption to estimate Total Consumption.
 - Third party consumer research and analysis of tourism flows will be used to estimate the proportion of non-domestic inflows that are counterfeit and contraband for each Member State
 - The bespoke Project STAR methodology will be used to analyse the inflows and outflows between all of the EU Member States, based on the data sources above.
 - Additional data sources (as per section 11 of the scope) will be used to refine our analysis
4. KPMG will also conduct analysis on Illicit Whites on the same basis as per section 3 of the scope. This will be reported in the consolidated section of the report.
5. Upon finalisation of our work, KPMG will provide to BAT, ITL, JTI and PMI data tables containing the following information;
 - Summary of EU total counterfeit and contraband inflows by source and destination market;
 - Detailed analysis of total non-domestic outflows to the EU split by destination market and brand for the following source countries: Ukraine; Russia; Moldova; Belarus; Serbia; Poland; and the Czech Republic.
6. KPMG will be prepared to present our findings to OLAF at interim stages in the project as required and at the final EU Member States presentation. The KPMG Project SUN team will also be made available to support up to two other external stakeholder presentations following the publication of the report under the terms of this agreement. Additional presentations or interviews, translation costs and the costs of KPMG personnel from other KPMG network firms are outside the scope of this letter and we would agree the costs of such services with you separately and in addition to the Project SUN fee as per section 5 of the Engagement Letter.
7. BAT, ITL, JTI and PMI will form a Steering Group as the primary point of contact for KPMG, which will oversee the project from the client side, and will be responsible for data provision, arranging country meetings or calls where appropriate, collating central feedback where appropriate and overseeing the timetable. Data will be provided directly to KPMG separately by each of BAT, ITL, JTI and PMI.
8. KPMG will facilitate three country clustered workshops with each of BAT, ITL, JTI and PMI country leaders for 10 priority EU Member States to help build a shared understanding of: data sources and their limitations; indicative results and their possible implications for the country's anti-illicit trade activity; BAT, ITL, JTI and PMI's respective anti-illicit trade strategies; communications plans, including fact gaps and hypotheses; and additional research requirements.
 - The 10 priority EU Member States are: France; Germany; Greece; Ireland; Italy; Netherlands; Poland; Romania; Spain and the UK;
 - The three cluster meetings will consist of:
 - a. Germany; the Netherlands; Poland
 - b. France; Ireland; the UK
 - c. Greece; Italy; Romania; Spain

Note: *BAT: British American Tobacco plc*
ITL: Imperial Tobacco Limited
JTI: JT International SA
PMI: Philip Morris International Management SA

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9. KPMG will share country specific preliminary results separately with the management teams of BAT, ITL, JTI and PMI for each of the priority EU Member States as outlined in section 8 of the scope and provide opportunity for feedback and comment from each of those management teams within the agreed timetable. We will communicate the updated results to each of those management teams and provide opportunity for one further set of comments before finalising our results.
 - For the remaining 18 non-priority EU Member States, KPMG will share preliminary findings of our analysis with the management teams of BAT, ITL, JTI and PMI for each non-priority Member State via a central point of contact for each of BAT, ITL, JTI and PMI. Feedback from non-priority EU Member States will be collected centrally by a point of contact for each of BAT, ITL, JTI and PMI and communicated to us within the agreed timetable. KPMG will communicate directly with the management teams of non-priority Member States only on an exceptions basis.
10. In addition to the detailed EU report and management meetings, KPMG will also undertake to manage and lead key intervention sessions between the BAT, ITL, JTI, PMI Steering Group and KPMG team, these being:
 - Project Kick Off (to take place week commencing 2nd December 2013) to agree detailed project process and approach, reporting format and highlight potential communication considerations at a EU Member State level;
 - A review of preliminary EU and Member State level findings for each of the 28 EU Member States and address key challenges and actions, to take place in early March 2014.
 - A review of updated EU and Member State level findings for each of the 28 EU Member States and address key challenges and actions, to take place in late March 2014.
11. Information from several independent sources will be used. These sources will include:
 - Tobacco industry research and statistics;
 - Sales data provided by BAT, ITL, JTI and PMI and/or Tobacco Manufacturers' Associations. Sales data will be provided separately for BAT, ITL, JTI and PMI and will remain confidential. The Project SUN report will only provide aggregated sales data that cannot be attributed to any of BAT, ITL, JTI or PMI;
 - Where available, regional sales data will be provided to help corroborate cross border trends between neighbouring countries. This will be provided separately by BAT/ITL/JTI and PMI and will remain confidential (not to be published in the report);
 - BAT, ITL, JTI and PMI consumer survey data will be provided to help corroborate consumption trends arising from Project SUN results and identify further areas of analysis (e.g. extent of smokers switching to roll-your-own (RYO) products).
 - Estimates of non-domestic consumption used by BAT, ITL, JTI and PMI management teams in each market (where available). These estimates will be provided to us separately by BAT, ITL, JTI and PMI to provide evidence-based support for observed trends in each of the EU Member States and will remain confidential.
 - Detailed survey results will be made available by BAT, ITL, JTI and PMI to KPMG in a timely manner for analysis purposes;
 - Information regarding the methodology and sampling plan will be provided by BAT, ITL, JTI and PMI to KPMG for our work.
 - EPSs commissioned jointly and/or individually by BAT, ITL, JTI and PMI will be conducted by third party research providers in a majority of Member States and the results thereof will be provided to KPMG as soon as they are available to allow us to consider these alongside market-specific information provided separately by BAT, ITL, JTI and PMI.

Note: BAT: British American Tobacco plc
 ITL: Imperial Tobacco Limited
 JTI: JT International SA
 PMI: Philip Morris International Management SA

- Independent third party non-domestic research;
 - Surveys to analyse the flows of non-domestic (legal) sales will be undertaken by third party consumer research agencies in a limited number of Member States (5) with coverage to be agreed upon between BAT, ITL, JTI and PMI and KPMG;
 - Such third party research will be contracted directly by KPMG and recharged equally to BAT, ITL, JTI and PMI;
 - In those markets where research is not conducted, KPMG will provide estimates of the trend in non-domestic (legal)consumption using both historical consumer research results and third party statistics regarding travel and tourism trends.
 - Expert opinions and expert panel data;
 - In areas where information provided may be inconclusive we will undertake structured interview programmes designed to capture and quantify the opinions of relevant expert groups including, among others, customs and law enforcement officials.
 - Existing public studies and statistics;
 - Research and data published by government agencies (including Ministries of Finance), health bodies, customs authorities, market researchers and academics will be provided by BAT, ITL, JTI and PMI management teams to help corroborate findings.
12. Interviews and data from external sources will be obtained on a best efforts basis. We will work with BAT, ITL, JTI and PMI to identify and contact key customs and Manufacturer's Associations members. We will require access to identified BAT, ITL, JTI and PMI personnel throughout this project and our ability to deliver this scope depends on this access being made available.



Note: *BAT: British American Tobacco plc*
 ITL: Imperial Tobacco Limited
 JTI: JT International SA
 PMI: Philip Morris International Management SA

If you would like further information, please talk to your usual KPMG contact or contact:

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