



26 February 2009

PRELIMINARY ANNOUNCEMENT - YEAR ENDED 31 DECEMBER 2008

SUMMARY

	2008	2007 restated	Change
Revenue	£12,122m	£10,018m	+21%
Profit from operations	£3,572m	£2,904m	+23%
Basic earnings per share	123.28p	105.19p	+17%
Adjusted diluted earnings per share	128.78p	108.53p	+19%
Dividends per share	83.70p	66.20p	+26%

- The reported Group revenue increased by 21 per cent to £12,122 million as a result of improved pricing, a better product mix, the acquisitions of Tekel and Skandinavisk Tobakskompagni (ST) mid-year and favourable exchange rate movements. Revenue would have increased by 11 per cent at constant rates of exchange.
- The reported Group profit from operations was 23 per cent higher at £3,572 million, or 24 per cent higher if adjusting items are excluded. Profit from operations, at constant rates of exchange and excluding adjusting items, would have been 14 per cent higher, with all regions contributing to this strong result.
- Group volumes from subsidiaries were 715 billion, up 4 per cent, a combination of organic volume growth of 1 per cent and the benefits from the two acquisitions. The four Global Drive Brands continued their strong performance and achieved overall volume growth of 16 per cent with around a quarter of the rise coming from brand migrations.
- Adjusted diluted earnings per share rose by 19 per cent to 128.78p, principally as a result of the strong growth in profit from operations and favourable exchange movements. Basic earnings per share were 17 per cent higher at 123.28p (2007: 105.19p).
- The Board is recommending a final dividend of 61.6p, which will be paid on 6 May 2009. This, together with the interim dividend, will take dividends in respect of 2008 as a whole to 83.70p, an increase of 26 per cent.
- The Chairman, Jan du Plessis, commented "Looking ahead, we remain alert to the possibilities of downtrading. However, our well balanced portfolio of brands covers all major price points, while our geographic diversity further mitigates the risks for shareholders. We are very much aware of the potential challenges but the inherent strength of our businesses, our brands and our people should make us more resilient than most."

ENQUIRIES:

INVESTOR RELATIONS:

Ralph Edmondson/ 020 7845 1180
Rachael Brierley 020 7845 1519

PRESS OFFICE:

David Betteridge/Catherine 020 7845 2888
Armstrong/Elif Boutlu

BRITISH AMERICAN TOBACCO p.l.c.

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CHAIRMAN'S STATEMENT

2008 was an extraordinary year, with financial markets in unprecedented turmoil, economies slowing and confidence badly shaken. Despite these conditions, British American Tobacco continued to deliver excellent results and completed two important acquisitions.

Revenue rose by 11 per cent at constant rates of exchange and by 21 per cent to £12,122 million at current rates. Profit from operations, excluding adjusting items, increased by 14 per cent at constant rates of exchange and by 24 per cent to £3,717 million at current rates. The benefit from the translation of our results into Sterling was £295 million.

Adjusted diluted earnings per share grew by 19 per cent to 128.8p and the Board has recommended a final dividend of 61.6p, an increase of 29 per cent. This brings our total dividend for the year to 83.7p, an increase of 26 per cent. For us, 2008 was an outstanding year.

It rounds off a decade of value creation for shareholders. It is just over 10 years since we demerged our financial services businesses and announced the merger with Rothmans. Over the past 10 years, British American Tobacco has achieved compound growth of 11 per cent in earnings per share and 13 per cent in dividends per share. Our total shareholder return has been 486 per cent, compared to 3 per cent for the FTSE 100 as a whole.

Our continued focus on our four Global Drive Brands (GDBs) has played a major part in these achievements. Last year, our GDBs grew by 16 per cent, with about a quarter of the increase attributable to successful brand migrations. Kent rose by 18 per cent and Pall Mall by 22 per cent and they each achieved sales of over 60 billion cigarettes for the first time. Kent, which is premium priced, is now the Group's biggest brand. Completing a very strong all round performance, Lucky Strike increased by 9 per cent and Dunhill by 7 per cent.

GDB volume now represents over 26 per cent of our total volume, providing us with a significant opportunity to add scale to our key competitive innovations. Moreover, as the GDBs are predominantly premium, our premium volume grew by 5 per cent organically, compared to the 1 per cent level of overall organic growth. Total volumes were up 4 per cent as a result of the combination of this organic growth and the benefit from the acquisitions of Tekel and Skandinavisk Tobakskompagni (ST) in the middle of the year.

As a result of these acquisitions, we now have much stronger market positions in Turkey, Denmark, Sweden, Norway and Poland and both acquisitions are performing in line with expectations, each contributing positively to earnings in 2008.

We have also made further progress with our productivity savings and we are very much on track towards our target of reducing our costs by £800 million by 2012, in addition to the £1 billion saved between 2003 and 2007. The principal areas of focus continue to be the supply chain, through initiatives such as our Global Leaf Pool, overheads and indirect costs. As a result of this focus, our operating margins increased to 31 per cent in 2008.

Moving to associates, ST ceased to be an associate company during the year, following our acquisition of its cigarette and snus businesses. Our share of associates' post-tax profit rose by 5 per cent at constant rates of exchange, if adjusting items are excluded. Their volume amounted to 205 billion cigarettes.

Chairman's statement cont...

At Reynolds American, cigarette volumes were lower and expenses under the Master Settlement Agreement were higher. However, these adverse factors were more than offset by improved pricing for both cigarettes and moist-snuff, as well as double-digit volume growth in moist-snuff and increased productivity in cigarette manufacturing. ITC, in India, continued the strong profit growth seen in recent years.

British American Tobacco's adjusted diluted earnings per share grew by 19 per cent to 128.8p. The substantial improvement in profit from operations, the significant uplift from foreign exchange and the benefit from the share buy-back programme were offset by higher net finance costs, a higher tax rate and an increase in minority interests.

The Board has recommended a final dividend of 61.6 p per share, which will be paid on 6 May 2009 to shareholders on the register at 13 March 2009. This takes the total dividend for the year to 83.7p, an increase of 26 per cent, as we reach our previously stated target of paying out 65 per cent of sustainable earnings in dividends.

In addition, some 22 million shares were bought back at a cost of £400 million and at an average price of 1812p per share. In order to preserve the Group's financial flexibility during a period of economic uncertainty, the Board has decided to suspend the share buy-back programme for the time being. However, we continue to appreciate the merit of having the share buy-back programme in place, together with the financial flexibility it provides, and we will therefore be seeking the necessary authority to resume the buy-back at the Annual General Meeting (AGM) on 30 April.

Arguably the most satisfying feature of our results last year was the high level of cash generation. Free cash flow rose 52 per cent to £2,604 million, exceeding the cost of the share buy-back and the increased level of dividends by more than £800million.

We continue to maintain investment grade credit ratings. The strength of our ratings has underpinned the debt issued during 2007 and 2008 and, despite the impact of the turbulence in financial markets, we are confident of our ability to access the debt capital markets successfully. The Group's central banking facility of £1.75 billion was undrawn as at 31 December 2008.

Thys Visser, who has been a non-executive director since 2001, will be retiring from the Board following the AGM, at the expiry of his current term in office. With his in-depth knowledge of the tobacco industry and his down to earth, no nonsense style, I should like to thank him very much for his contribution to our business over the years.

Looking ahead, we remain alert to the possibilities of downtrading. However, our well balanced portfolio of brands covers all major price points, while our geographic diversity further mitigates the risks for shareholders. We are very much aware of the potential challenges but the inherent strength of our businesses, our brands and our people should make us more resilient than most.

Jan du Plessis
25 February 2009

BUSINESS REVIEW

The reported Group revenue was 21 per cent higher at £12,122 million as a result of improved pricing, a better product mix, the acquisitions of Tekel and Skandinavisk Tobakskompagni (ST) made at the half year and favourable exchange rate movements. At constant rates of exchange, revenue would have increased by 11 per cent.

The reported Group profit from operations was 23 per cent higher at £3,572 million, up 24 per cent if adjusting items, as explained on pages 22 and 23, are excluded. All regions contributed to this strong result at current rates of exchange. Profit from operations, excluding adjusting items, would have been 14 per cent higher at constant rates of exchange, with all regions up.

Group volumes from subsidiaries were 715 billion, up 4 per cent, a combination of organic volume growth of 1 per cent and the benefit of additional volumes from the two acquisitions, made earlier this year.

The four Global Drive Brands continued their strong performance and achieved overall volume growth of 16 per cent. Around a quarter of the growth was contributed by brand migrations.

Kent volume grew by 18 per cent with excellent growth in Russia, Romania, Kazakhstan, Ukraine and Chile and from new markets like Kyrgyzstan, Mongolia and Serbia, while it also benefited from a brand migration in South Africa. Volumes were lower in Japan, although market share increased.

Dunhill rose by 7 per cent, with growth in South Korea, Taiwan, Australia, South Africa, Russia, Romania, France, Italy and Saudi Arabia, while volumes were maintained in Malaysia, leading to an increase in market share.

Lucky Strike volumes were up 9 per cent with good growth in Spain, Italy, France, Chile, Brazil and Argentina, partly offset by declines in Japan and Germany as a result of lower industry volumes.

Pall Mall increased volumes by 22 per cent with the geographic roll-out to more markets, such as Pakistan, Malawi, Mexico and Belarus, and the continued growth in Turkey, Romania, Uzbekistan, Hungary, the Netherlands and Malaysia. This was partly offset by lower volumes in Poland, Russia, Spain, Greece and Italy.

In the fourth quarter, revenue grew by 26 per cent to £3,418 million and profit from operations, excluding adjusting items, was up 36 per cent to £962 million, mainly as a result of the inclusion of ST and Tekel in 2008, as well as the benefits from exchange rate movements. This information is shown on the quarterly analysis of profits.

In **Europe**, profit at £1,213 million was up £371 million, as a result of the ST acquisition and excellent performances in Russia, Uzbekistan, Romania and Spain, with growth in Germany, France, Switzerland and Italy, partially offset by decreases in Hungary, the Czech Republic and Belgium. These results benefited from the more favourable pricing environment, an improved product mix and exchange rates. At constant rates of exchange, profit would have increased by £235 million or 28 per cent.

Excluding the benefit from the acquisition of ST, profit increased by £279 million, up 33 per cent, or £144 million, up 17 per cent at constant rates of exchange.

Regional volumes were up 4 per cent at 254 billion, benefiting from the acquisition of ST. Volume increases in Poland, Romania, Uzbekistan, Switzerland and Spain were more than offset by decreases in Russia, Italy, Germany, Ukraine and the Czech Republic.

Business review cont...

The acquisition of ST in the middle of the year resulted in significant additional profit for the region.

In Italy, Lucky Strike performed very well although overall volumes were adversely impacted by the decline of local brands and the disposal of some brands in 2007. Profit increased as a result of lower product costs due to continuing productivity programmes and reduced overheads, partly offset by reduced volumes.

Volumes in Germany declined as industry volumes shrank while market share was slightly lower. However, Pall Mall, performed well by growing volume and market share. Profit increased as a result of higher margins from a combination of price increases, reduced product costs and overhead savings.

While industry volumes in France were lower, volume and market share grew, led by Dunhill, Lucky Strike and Pall Mall. Profit increased as a result of higher prices and overhead savings.

In Switzerland, Parisienne, Lucky Strike and Pall Mall continued to grow market share and profit increased due to higher volumes and improved margins.

In the Netherlands, profits were down as a result of slightly lower volumes, despite an increase in market share. Industry volumes in Belgium were severely impacted by last year's excise-driven price increase and, together with the sale of the pipe and cigar business in 2007, resulted in lower profit. Market share improved, assisted by the successful migration of Winfield to Pall Mall.

In Spain, strong profit growth and higher volumes were achieved due to the excellent volume and share growth of Lucky Strike, coupled with a more favourable pricing environment.

In Russia, a strong performance by the premium brands, Kent, Dunhill and Vogue, continued to improve the product mix and, with higher prices, profit increased significantly. Volumes were lower as a result of the decline in low price and local brands following price increases that were not immediately followed by competitors.

Profit in Romania increased significantly, benefiting from higher volumes, price increases and the improved product mix, partially offset by higher marketing investment. The strong growth of volumes, driven by the continued success of the Global Drive Brands led to increased market share.

The tobacco market in the Czech Republic was heavily impacted during 2008 by the effect of the trade buying at the end of 2007 in anticipation of an excise increase, resulting in lower profit and volumes.

The accelerated decline of industry shipments in Poland was the result of significant excise-driven price increases during the last two years. Competitive market conditions continued and with the increase in illicit trade, profitability was adversely impacted. Volumes increased as a result of the inclusion of the ST businesses.

In Hungary, volumes were slightly down although Dunhill and Pall Mall performed well despite price competition. This, coupled with higher marketing investment, led to lower profit.

In Ukraine, volume and market share decreased slightly due to the decline of low priced local brands, largely offset by the excellent performance of Kent. Results improved significantly with the improved mix, price increases and cost control, despite the volume decline and higher marketing spend.

The impressive performance of Kent in Kazakhstan and Pall Mall in Uzbekistan led to increased volumes and, with higher prices and better cost control, resulted in higher profit.

Business review cont...

In **Asia-Pacific**, profit rose by £132 million to £804 million, mainly attributable to strong performances in Pakistan, Vietnam, Bangladesh, Australia and Malaysia and also benefiting from favourable exchange rates. At constant rates of exchange, profit would have increased by £79 million or 12 per cent. Volumes at 153 billion were 5 per cent higher as good increases in Pakistan, Bangladesh and South Korea were partially offset by lower volumes in Vietnam, Malaysia and Sri Lanka.

Profit in Australia was up as a result of higher margins and exchange rate movements, partially offset by the impact of increased competitor discounting activities. In New Zealand, profit improved, benefiting from price rises, cost efficiencies and exchange movements. Volumes in Australia and New Zealand were similar to last year, but both Dunhill and Pall Mall increased market share.

In Malaysia, strong profit growth was achieved as a result of price increases, a better product mix and continued productivity savings. Dunhill and Pall Mall grew market share, with good results from Kent after its relaunch in August 2008. Volumes were lower due to the overall industry decline, the high levels of illicit trade and another significant excise increase during the third quarter of 2008.

In Vietnam, strong profit growth was achieved through higher prices, a solid performance in the premium segment and cost saving initiatives. Volumes were down due to lower industry volumes, although market share increased strongly with outstanding performances from Craven 'A', Dunhill and State Express 555.

Volumes in South Korea were higher than last year and market share was up as a result of the good performance from Dunhill. Good profit growth was achieved through higher margins, increased volumes and an improved product mix, partly offset by the weakening of the currency.

In Taiwan, volumes were slightly down despite the significant growth of Dunhill. Profit was lower, adversely impacted by the marketing investment behind Dunhill.

In Pakistan, volume and market share continued to grow strongly. The volume growth, coupled with higher prices, resulted in a profit increase, however, this was more than offset by the weakening of the currency.

In Bangladesh, strong growth in volumes, price increases and a better product mix resulted in an impressive increase in profit.

Profit in Sri Lanka was well ahead, benefiting from price rises, a better product mix and continued productivity improvements. Volumes were lower, although overall market share grew with the good performances of Dunhill and Pall Mall.

Profit in **Latin America** increased by £78 million to £759 million, mainly as a result of an excellent performance in Brazil and exchange rate movements. At constant rates of exchange, profit would have increased by £25 million or 4 per cent. Volumes were down 2 per cent at 147 billion after declines in Mexico and Venezuela.

In Brazil, profit grew strongly, benefiting from higher margins, an improved product mix and a stronger local currency. Market share increased on volumes in line with last year. Leaf export results improved substantially benefiting from higher volumes, higher pricing and the appreciation of the US dollar.

Business review cont...

Volumes in Mexico were lower, resulting in a reduced market share. A price increase in January was not sufficient to fully recover the earlier excise increase and, combined with higher marketing investment behind the GDBs, resulted in a reduced profit.

In Argentina, profit rose mainly as a result of a stronger local currency. Higher margins and an improved product mix, due to the good performance of Lucky Strike, were offset by higher variable costs and higher salaries due to inflationary pressures.

In Chile, volumes were slightly up with the strong growth of Kent and Lucky Strike, while profit was higher due to price increases and product mix benefits, partially offset by higher marketing investment.

In Venezuela, volumes were lower following high excise-driven price increases in the last quarter of 2007 and price rises in 2008. Increased illicit trade resulted in a lower market share, adversely affecting profit.

Volumes in the Central America and Caribbean area were down as a result of lower industry volumes and the resurgence in illicit trade. However, profit increased as margins improved and the local currencies strengthened.

Profit in the **Africa and Middle East** region grew by £69 million to £536 million mainly as a result of the acquisition of Tekel and the good performance of Nigeria. At constant rates of exchange, profit would have increased by £76 million or 16 per cent. Volumes were 19 per cent higher at 120 billion, following increases in Nigeria, Egypt and Saudi Arabia, coupled with the additional volumes from the acquisition of Tekel during the year. These increases were partially offset by the disposal of the Chesterfield trademark in South Africa.

In South Africa, profit was only slightly higher than last year, adversely impacted by the weaker exchange rate. In local currency, profit growth was achieved as a result of higher prices and an improved product mix, partially offset by the decline in volumes. Volumes and market share were lower following the termination of the Chesterfield trademark license agreement at the end of 2007. Dunhill and Peter Stuyvesant continued to deliver strong share performances, while Kent performed well after its migration from Benson & Hedges.

Profit in Nigeria increased as a result of good volume growth, a favourable exchange rate, an improved product mix, productivity benefits and higher margins.

In the Middle East, profit and volumes were higher due to the impressive growth of Dunhill in Saudi Arabia. Strong sales across the Caucasus led to volume, market share and profit increases as Kent performed well.

In Turkey, the acquisition of the cigarette assets of Tekel was completed in June 2008 (see page 26) and was successfully integrated with the existing business, which reached break even in 2008 following good organic volume growth. GDBs grew strongly with good performances by Kent and Pall Mall.

Business review cont...

Profit from the **America-Pacific** region increased by £69 million to £515 million. This was principally due to the improved contribution from both Canada and Japan and stronger currencies. At constant rates of exchange, profit would have increased by £13 million or 3 per cent. Volumes at 41 billion were 4 per cent lower than last year.

Profit in Canada increased with the contribution to the Group at £297 million. This was the result of higher pricing, lower distribution costs and a stronger exchange rate, partly offset by lower volumes and a weaker product mix. At constant rates of exchange, profit was £272 million, down 2 per cent. Overall market share at 52 per cent was slightly lower than last year as the decline in the premium segment was not offset by the growth in the value-for-money and low-price segments.

In Japan, market share was up due to the strong performance of Kool and stable market shares of Kent and Lucky Strike, although volumes were lower as a result of the continued decline in total industry volumes. Profit was up as a result of a favourable exchange rate, higher pricing and an improved mix.

Unallocated costs, which are net corporate costs not directly attributable to individual regions, were £110 million (2007 restated: £106 million).

The above regional profits were achieved before accounting for restructuring and integration costs, the Canadian settlement, amortisation of trademarks and gains on disposal of businesses and trademarks, as explained on pages 22 and 23.

Results of associates

Associates principally comprise Reynolds American and ITC. ST was an associate until 2 July 2008 when the cigarette and snus businesses of ST were acquired and from that date it was consolidated into the Group results.

The Group's share of the post-tax results of associates increased by £61 million, or 14 per cent, to £503 million. Excluding adjusting items, explained on page 28, the Group's share of the post-tax results of associates increased by £28 million to £477 million, reflecting the impact of the increase in profit from Reynolds American and ITC, partly offset by the impact of the ST transaction (see page 24).

The contribution from Reynolds American to the post-tax results was up 20 per cent at £339 million, or 12 per cent at constant rates of exchange. Excluding the impairment of trademarks, the benefit from the termination of the joint venture agreement and costs of the organisational restructuring in 2008, it was 13 per cent higher at £326 million (2007: post tax results of £289 million excluding trademark impairments of £7 million). At constant rates of exchange, the contribution would have been £302 million, or 5 per cent higher than last year. Earnings were up as lower cigarette volumes and higher settlement obligations were more than offset by higher cigarette and moist-snuff pricing, increased productivity at R J Reynolds and double-digit moist-snuff volume growth at Conwood.

The Group's main associate in India, ITC, continued its strong profit growth and its contribution to the Group rose by £9 million, or 8 per cent, to £117 million. At constant rates of exchange, the contribution would have been £113 million, or 5 per cent higher than last year.

Associates' volumes decreased by 11 per cent to 205 billion largely as a result of the ST transaction. With the inclusion of associates' volumes, total Group volumes were 919 billion (2007: 914 billion).

DIVIDENDS

The Board recommends to shareholders a final dividend of 61.6 pence per ordinary share of 25p for the year ended 31 December 2008. If approved by shareholders at the Annual General Meeting to be held on 30 April 2009, the dividend will be payable on 6 May 2009 to shareholders registered on either the UK main register or the new South African branch register on 13 March 2009 (the record date).

In compliance with the requirements of STRATE, the electronic settlement and custody system used by the JSE Limited (JSE), the following salient dates for the payment of the dividend are applicable:

Last day to trade cum dividend (JSE):	Friday 6 March 2009
Shares commence trading ex dividend (JSE):	Monday 9 March 2009
Shares commence trading ex dividend (LSE):	Wednesday 11 March 2009
Record date (JSE and LSE):	Friday 13 March 2009
Payment date:	Wednesday 6 May 2009

As the Group reports in sterling, dividends are declared and payable in sterling except for shareholders on the branch register in South Africa whose dividends are payable in rand. A rate of exchange of £:R = 14.32310 as at 24 February 2009 (the closing rate on that date as quoted by Bloomberg), results in an equivalent final dividend of 882.30296 SA cents per ordinary share. From the close of business on 6 March 2009 until the close of business on 13 March 2009, no transfers between the UK main register and the South African branch register will be permitted and no shares may be dematerialised or rematerialised between 9 March 2009 and 13 March 2009, both days inclusive.

The following is a summary of the dividends declared for the years ended 31 December 2008 and 2007:

	Pence per share	2008 £m	Pence per share	2007 £m
Ordinary shares				
Interim				
- 2008 paid 17 September 2008	22.1	440		
- 2007 paid 12 September 2007			18.6	377
Final				
- 2008 payable 6 May 2009	61.6	1,221		
- 2007 paid 7 May 2008			47.6	953
	<u>83.7</u>	<u>1,661</u>	<u>66.2</u>	<u>1,330</u>

In accordance with IFRS, the proposed final dividend amounting to £1,221 million (2007: £953 million), payable on 6 May 2009, will be recognised in the Group accounts for the year ending 31 December 2009. For the year ended 31 December 2008, the accounts include the final dividend paid in respect of the year ended 31 December 2007, amounting to £953 million and the interim dividend amounting to £440 million, paid on 17 September 2008. For the year ended 31 December 2007, the accounts include the final dividend paid in respect of the year ended 31 December 2006, amounting to £821 million and the 2007 interim dividend, amounting to £377 million.

RISKS AND UNCERTAINTIES

The principal risks and uncertainties affecting the business activities of the Group were identified under the 'Key Group risk factors' section of the Annual Report and Accounts for the year ended 31 December 2007, a copy of which is available on the Group's website www.bat.com. The key Group risks have been reviewed and updated and are summarised in a table that will be included in the Annual Report for the year ended 31 December 2008 that will be available on the Group's website at the end of March 2009. The table provides a brief description of the key risks to which the Group's operations are exposed and it identifies, in each case, their potential impact on the Group and the principal processes in place to manage the risk.

The key Group risks are summarised under the headings of:

- Illicit trade
- Excise and tax
- Financial
- Marketplace
- Regulation
- Litigation
- Information technology

GOING CONCERN

The Annual Report has been prepared on the going concern basis. After reviewing the Group's annual budgets, plans and financing arrangements, the Directors consider that the Group has adequate resources to continue operating for the foreseeable future. A full description of the business activities, its financial position, cash flows, liquidity position, facilities and borrowing position, together with the factors likely to affect its future development, performance and position, are set out in the Business Review and Financial Review and in the notes to the accounts, all of which will be included in the Annual Report that will be available on the Group's website, www.bat.com at the end of March 2009.

The Group has, at the date of this report, sufficient financing available for its estimated existing requirements for the next twelve months. This, together with the proven ability to generate cash from trading activities, the performance of the Group's Global Drive Brands, its leading market positions in a number of markets and its geographical spread, as well as numerous contracts with established customers and suppliers across different geographical areas and industries, provides the Directors with the confidence that the Group is well placed to manage its business risks successfully despite the current financial conditions and uncertain outlook in the general global economy and financial climate.

GROUP INCOME STATEMENT

For the year ended 31 December

	2008 £m	2007 £m restated
Gross turnover (including duty, excise and other taxes of £21,799 million (2007: £17,086 million))	<u>33,921</u>	<u>27,104</u>
Revenue	12,122	10,018
Raw materials and consumables used	(3,335)	(2,802)
Changes in inventories of finished goods and work in progress	19	30
Employee benefit costs	(1,907)	(1,587)
Depreciation and amortisation costs	(430)	(336)
Other operating income	281	205
Other operating expenses	<u>(3,178)</u>	<u>(2,624)</u>
Profit from operations	3,572	2,904
after (charging)/crediting		
- restructuring and integration costs	(160)	(173)
- Canadian settlement	(102)	
- amortisation of trademarks	(24)	
- gains on disposal of businesses and trademarks	141	75
Finance income	267	136
Finance costs	(658)	(405)
Net finance costs	(391)	(269)
Share of post-tax results of associates and joint ventures	503	442
after (charging)/crediting:		
- trademark impairments	(20)	(7)
- additional ST income	13	
- termination of joint venture	45	
- restructuring costs	(12)	
Profit before taxation	<u>3,684</u>	3,077
Taxation on ordinary activities	(1,025)	(790)
Profit for the year	<u>2,659</u>	<u>2,287</u>
Attributable to		
Shareholders' equity	<u>2,457</u>	<u>2,130</u>
Minority interests	<u>202</u>	<u>157</u>
Earnings per share		
Basic	<u>123.28p</u>	<u>105.19p</u>
Diluted	<u>122.54p</u>	<u>104.46p</u>

The restatement of the 2007 results reflects the change in the Group's accounting policy for recognition of actuarial gains and losses, together with the early adoption of IFRIC14, as explained on page 16.

See notes on pages 16 to 48.

GROUP STATEMENT OF RECOGNISED INCOME AND EXPENSE

For the year ended 31 December

	2008 £m	2007 £m restated
Differences on exchange	937	320
Difference on exchange reclassified and reported in profit for the year	(22)	
Cash flow hedges		
- net fair value gains	180	15
- reclassified and reported in profit for the year	(173)	(42)
- reclassified and reported in net assets	1	
Available-for-sale investments		
- net fair value gains	1	1
- reclassified and reported in profit for the year	(6)	1
Net investment hedges		
- net fair value losses	(672)	(35)
- differences on exchange on borrowings	(178)	
Revaluation of existing business <i>page 25</i>	179	
Retirement benefit schemes		
- actuarial (losses)/gains in respect of subsidiaries	(547)	95
- surplus recognition in respect of subsidiaries		9
- actuarial (losses)/gains in respect of associate companies	(396)	17
Tax on items recognised directly in SORIE	184	(53)
Net (losses)/gains	(512)	328
Profit for the year <i>page 11</i>	<u>2,659</u>	<u>2,287</u>
Total recognised income for the year	<u>2,147</u>	<u>2,615</u>
- shareholders' equity	<u>1,913</u>	<u>2,443</u>
- minority interests	<u>234</u>	<u>172</u>
Effect of changes in accounting policy at 1 January 2007:		
- shareholders' equity		(104)
- minority interest		-

The Group has prepared a Statement of Recognised Income and Expense (SORIE), rather than a Statement of Changes in Total Equity as previously presented, following the accounting policy change for recognition of actuarial gains and losses, together with the early adoption of IFRIC14, as explained further on page 16.

See notes on pages 16 to 48.

GROUP BALANCE SHEET

At 31 December

	2008 £m	2007 £m restated
Assets		
Non-current assets		
Intangible assets	12,318	8,105
Property, plant and equipment	3,076	2,378
Investments in associates and joint ventures	2,552	2,316
Retirement benefit assets	75	37
Deferred tax assets	392	264
Trade and other receivables	193	123
Available-for-sale investments	27	22
Derivative financial instruments	176	153
Total non-current assets	18,809	13,398
Current assets		
Inventories	3,177	1,985
Income tax receivable	137	85
Trade and other receivables	2,395	1,845
Available-for-sale investments	79	75
Derivative financial instruments	420	82
Cash and cash equivalents	2,309	1,258
	8,517	5,330
Assets classified as held for sale	225	36
Total current assets	8,742	5,366
Total assets	27,551	18,764

The restatement of the 2007 balance sheet reflects the change in Group accounting policy for recognition of actuarial gains and losses, together with the early adoption of IFRIC14, as explained on page 16.

See notes on pages 16 to 48.

GROUP BALANCE SHEET

At 31 December

	2008 £m	2007 £m restated
Equity		
Capital and reserves		
Share capital	506	506
Share premium, capital redemption and merger reserves	3,905	3,902
Other reserves	955	658
Retained earnings	1,578	1,805
Shareholders' funds	<u>6,944</u>	<u>6,871</u>
after deducting		
- cost of treasury shares	<u>(745)</u>	<u>(296)</u>
Minority interests	<u>271</u>	<u>218</u>
Total equity	<u><u>7,215</u></u>	<u><u>7,089</u></u>
Liabilities		
Non-current liabilities		
Borrowings	9,437	6,062
Retirement benefit liabilities	848	360
Deferred tax liabilities	599	336
Other provisions for liabilities and charges	186	165
Trade and other payables	166	149
Derivative financial instruments	199	49
Total non-current liabilities	<u><u>11,435</u></u>	<u><u>7,121</u></u>
Current liabilities		
Borrowings	2,724	861
Income tax payable	300	227
Other provisions for liabilities and charges	295	263
Trade and other payables	4,718	2,976
Derivative financial instruments	864	225
	<u>8,901</u>	<u>4,552</u>
Liabilities directly associated with assets classified as held for sale		2
Total current liabilities	<u><u>8,901</u></u>	<u><u>4,554</u></u>
Total equity and liabilities	<u><u>27,551</u></u>	<u><u>18,764</u></u>

The restatement of the 2007 balance sheet reflects the change in Group accounting policy for recognition of actuarial gains and losses, together with the early adoption of IFRIC14, as explained on page 16.

See notes on pages 16 to 48.

GROUP CASH FLOW STATEMENT

For the year ended 31 December

	2008 £m	2007 £m
Cash flows from operating activities		
Cash generated from operations <i>page 33</i>	4,156	3,181
Dividends received from associates	326	285
Tax paid	(943)	(866)
Net cash from operating activities	<u>3,539</u>	<u>2,600</u>
Cash flows from investing activities		
Interest received	125	114
Dividends received from investments	2	2
Purchases of property, plant and equipment	(448)	(416)
Proceeds on disposal of property, plant and equipment	62	46
Purchases of intangibles	(96)	(66)
Proceeds on disposal of intangibles	17	16
Purchases and disposals of investments	9	71
Proceeds from associates' share buy-backs	42	
Purchase of Tekel cigarette assets	(873)	
Purchase of ST cigarette and snus businesses	(1,243)	
Purchases of other subsidiaries and minority interests	(9)	(15)
Proceeds on disposals of subsidiaries	26	126
Net cash from investing activities	<u>(2,386)</u>	<u>(122)</u>
Cash flows from financing activities		
Interest paid	(400)	(384)
Interest element of finance lease rental payments	(3)	(3)
Capital element of finance lease rental payments	(30)	(21)
Proceeds from issue of shares to Group shareholders	3	5
Proceeds from exercise of options over own shares held in employee share ownership trusts	7	22
Proceeds from increases in and new borrowings	3,518	438
Movements relating to derivative financial instruments	(656)	(89)
Purchases of own shares	(400)	(750)
Purchase of own shares held in employee share ownership trusts	(116)	(41)
Reductions in and repayments of borrowings	(731)	(427)
Dividends paid to shareholders	(1,393)	(1,198)
Dividends paid to minority interests	(173)	(173)
Net cash from financing activities	<u>(374)</u>	<u>(2,621)</u>
Net cash flows from operating, investing and financing activities	<u>779</u>	<u>(143)</u>
Differences on exchange	261	47
Increase/(decrease) in net cash and cash equivalents in the year	<u>1,040</u>	<u>(96)</u>
Net cash and cash equivalents at 1 January	<u>1,180</u>	<u>1,276</u>
Net cash and cash equivalents at 31 December	<u>2,220</u>	<u>1,180</u>

See notes on pages 16 to 48.

ACCOUNTING POLICIES AND BASIS OF PREPARATION

The financial information has been extracted from the Annual Report and Accounts, including the audited financial statements for the year ended 31 December 2008. This financial information does not constitute statutory accounts within the meaning of Section 240 of the UK Companies Act 1985/2006.

From 1 January 2005, the Group has prepared its annual consolidated financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and implemented in the UK.

These financial statements have been prepared under the historical cost convention, except in respect of certain financial instruments, and on a basis consistent with the IFRS accounting policies as set out in the Annual Report and Accounts for the year ended 31 December 2007, except for the changes explained below.

In 2008, the Group has amended its treatment with regard to the recognition of actuarial gains and losses of retirement benefit schemes under IAS19. Following the change in accounting policy, the Group now recognises actuarial gains and losses in the period in which they occur, in the Statement of Recognised Income and Expense (SORIE), rather than using partial deferral of such gains and losses through the “corridor” method as also permitted by IAS19. The Group believes that fully recognising actuarial gains and losses where they occur results in a better presentation of the financial statements which is more in line with current market practice and expected financial reporting developments, thus providing more comparable market information. In addition, the Group also adopted early IFRIC14 (IAS19 – The Limit on a Deferred Benefit Asset, Minimum Funding Requirements and their Interaction) which clarifies the conditions under which a surplus in a post-retirement benefit scheme can be recognised in the financial statements, as well as setting out the accounting implications where minimum funding requirements exist.

The comparative period has been restated to reflect these changes, including the presentation of a SORIE which has not been required under the previous accounting policy. The impact of the changes was to reduce the Group's total equity at 31 December 2008 by £817 million (2007: £9 million) and increase the profit for 2008 by £4 million. In the year ended 31 December 2007 the profit from operations and taxation were both reduced by £1 million and therefore the profit for the year was unchanged.

In 2008, the Group also updated its accounting policy on ‘intangible assets other than goodwill’ to address trademarks acquired by the Group's subsidiary undertakings. As with other recognised intangible assets, trademarks are carried at cost less accumulated amortisation and impairment. Trademarks with indefinite lives are not amortised but are reviewed annually for impairment. Other trademarks are amortised on a straight-line basis over their remaining useful lives, which do not exceed twenty years. Consistent with the existing policy for associated companies' trademarks, impairments are recognised in the income statement but increases in values are not recognised.

The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities at the date of these financial statements. Such estimates and assumptions are based on historical experience and various other factors that are believed to be reasonable in the circumstances and constitute management's best judgement at the date of the financial statements. In the future, actual experience may deviate from these estimates and assumptions, which could affect these financial statements as the original estimates and assumptions are modified, as appropriate, in the period in which the circumstances change.

SEGMENTAL ANALYSES OF VOLUME, REVENUE AND PROFIT

For the year ended

Volume	31.12.08 bns	31.12.07 bns
Europe	253.6	245.0
Asia-Pacific	152.5	145.2
Latin America	147.2	150.5
Africa and Middle East	120.5	101.0
America-Pacific	40.8	42.3
	<u>714.6</u>	<u>684.0</u>

Revenue	External £m	31.12.08 Inter segment £m	Revenue £m	External £m	31.12.07 Inter segment £m	Revenue £m
Europe	4,720	258	4,978	3,621	225	3,846
Asia-Pacific	2,146	19	2,165	1,874	22	1,896
Latin America	2,232	615	2,847	1,979	585	2,564
Africa and Middle East	1,572		1,572	1,224	15	1,239
America-Pacific	560		560	473		473
Revenue	<u>11,230</u>	<u>892</u>	<u>12,122</u>	<u>9,171</u>	<u>847</u>	<u>10,018</u>

The segmental analysis of revenue above is based on location of manufacture and figures based on location of sales are as follows:

	31.12.08 £m	31.12.07 £m
Europe	4,745	3,655
Asia-Pacific	2,151	1,876
Latin America	2,246	1,983
Africa and Middle East	1,797	1,445
America-Pacific	1,183	1,059
Revenue	<u>12,122</u>	<u>10,018</u>

Segmental analyses of volume, revenue and profit cont...

Profit from operations

	31.12.08		31.12.07	
	Segment result	Adjusted segment result*	Segment result restated	Adjusted segment result* restated
	£m	£m	£m	£m
Europe	1,218	1,213	782	842
Asia-Pacific	802	804	667	672
Latin America	759	759	681	681
Africa and Middle East	485	536	444	467
America-Pacific	418	515	436	446
	<u>3,682</u>	<u>3,827</u>	<u>3,010</u>	<u>3,108</u>
Unallocated costs	<u>(110)</u>	<u>(110)</u>	<u>(106)</u>	<u>(106)</u>
Profit from operations	<u><u>3,572</u></u>	<u><u>3,717</u></u>	<u><u>2,904</u></u>	<u><u>3,002</u></u>

*Excluding adjusting items: restructuring and integration costs, the Canadian settlement, amortisation of trademarks and gains on disposal of businesses and trademarks as explained on pages 22 and 23.

The segmental analysis of the **Group's share of the post-tax results of associates and joint ventures** is as follows:

	31.12.08		31.12.07	
	Segment result	Adjusted segment result*	Segment result	Adjusted segment result*
	£m	£m	£m	£m
Europe	39	26	48	48
Asia-Pacific	121	121	110	110
Latin America	2	2	1	1
Africa and Middle East	2	2	1	1
America-Pacific	339	326	282	289
	<u>503</u>	<u>477</u>	<u>442</u>	<u>449</u>

*Excluding adjusting items: charges for trademark impairments, additional ST income, gain on termination of joint venture and restructuring costs as explained on page 28.

The restatement of the 2007 results reflects the change in the Group's accounting policy for recognition of actuarial gains and losses, together with the early adoption of IFRIC14, as explained on page 16.

QUARTERLY ANALYSES OF PROFIT

	31.3.08 £m	3 months to		31.12.08 £m	Year to 31.12.08 £m
		30.6.08 £m	30.9.08 £m		
Revenue	<u>2,541</u>	<u>2,916</u>	<u>3,247</u>	<u>3,418</u>	<u>12,122</u>
Europe	230	300	366	317	1,213
Asia-Pacific	193	210	199	202	804
Latin America	193	188	203	175	759
Africa and Middle East	131	128	128	149	536
America-Pacific	<u>110</u>	<u>125</u>	<u>140</u>	<u>140</u>	<u>515</u>
	857	951	1,036	983	3,827
Unallocated costs	<u>(40)</u>	<u>(11)</u>	<u>(38)</u>	<u>(21)</u>	<u>(110)</u>
	817	940	998	962	3,717
Restructuring and integration costs	(10)	(23)	(34)	(93)	(160)
Canadian settlement			(101)	(1)	(102)
Amortisation of trademarks			(12)	(12)	(24)
Gains on disposal of businesses and trademarks			<u>139</u>	<u>2</u>	<u>141</u>
Profit from operations	807	917	990	858	3,572
Net finance costs	(95)	(84)	(91)	(121)	(391)
Share of post-tax results of associates and joint ventures	<u>159</u>	<u>134</u>	<u>93</u>	<u>117</u>	<u>503</u>
Profit before taxation	871	967	992	854	3,684
Taxation on ordinary activities	(224)	(270)	(281)	(250)	(1,025)
Profit for the period	<u>647</u>	<u>697</u>	<u>711</u>	<u>604</u>	<u>2,659</u>
Earnings per share					
Basic	<u>29.92p</u>	<u>32.56p</u>	<u>33.01p</u>	<u>27.79p</u>	<u>123.28p</u>
Adjusted diluted	<u>28.44p</u>	<u>33.58p</u>	<u>33.95p</u>	<u>32.81p</u>	<u>128.78p</u>

Quarterly analyses of profit cont...

	31.3.07	3 months to		31.12.07	Year to
		30.6.07	30.9.07	restated	31.12.07
	£m	£m	£m	£m	restated
				£m	£m
Revenue	<u>2,232</u>	<u>2,493</u>	<u>2,587</u>	<u>2,706</u>	<u>10,018</u>
Europe	182	222	246	192	842
Asia-Pacific	167	168	163	174	672
Latin America	180	206	164	131	681
Africa and Middle East	124	125	105	113	467
America-Pacific	<u>80</u>	<u>112</u>	<u>128</u>	<u>126</u>	<u>446</u>
	733	833	806	736	3,108
Unallocated costs	<u>(41)</u>	<u>(4)</u>	<u>(29)</u>	<u>(32)</u>	<u>(106)</u>
	692	829	777	704	3,002
Restructuring costs	(8)	(32)	(10)	(123)	(173)
Gains on disposal of businesses and trademarks		<u>11</u>	<u>45</u>	<u>19</u>	<u>75</u>
Profit from operations	684	808	812	600	2,904
Net finance costs	(58)	(68)	(78)	(65)	(269)
Share of post-tax results of associates and joint ventures	<u>111</u>	<u>111</u>	<u>113</u>	<u>107</u>	<u>442</u>
Profit before taxation	737	851	847	642	3,077
Taxation on ordinary activities	(199)	(221)	(209)	(161)	(790)
Profit for the period	<u>538</u>	<u>630</u>	<u>638</u>	<u>481</u>	<u>2,287</u>
Earnings per share					
Basic	<u>24.24p</u>	<u>28.70p</u>	<u>29.73p</u>	<u>22.52p</u>	<u>105.19p</u>
Adjusted diluted	<u>24.31p</u>	<u>29.20p</u>	<u>28.49p</u>	<u>26.53p</u>	<u>108.53p</u>

The restatement of the 2007 balance sheet reflects the change in Group accounting policy for recognition of actuarial gains and losses, together with the early adoption of IFRIC14, as explained on page 16.

REBASED REGIONAL ANALYSIS

During 2008, the Group conducted a review of the composition of its regions and, given the acquisitions of ST and Tekel, it was announced in 2008 that the regional structure would be realigned from 1 January 2009 to the following:

- Europe region splits into Eastern Europe and Western Europe
- Americas region includes the markets of Latin America, the Caribbean and Canada
- Asia-Pacific includes Japan

Although the new regional structure is only applicable from 1 January 2009, the 2008 information has been presented on the new regional basis and is shown below:

For the year ended 31 December 2008

Volume and revenue	Volume bns	Revenue £m
Eastern Europe	137.3	1,594
Western Europe	122.6	3,218
Asia-Pacific	179.5	2,717
Americas	161.0	2,863
Africa and Middle East	114.2	1,730
	<u>714.6</u>	<u>12,122</u>

Based on location of sales.

	Profit from operations £m	Adjusted profit from operations* £m
Profit from operations		
Eastern Europe	468	468
Western Europe	765	760
Asia-Pacific	922	924
Americas	956	1,052
Africa and Middle East	461	513
	<u>3,572</u>	<u>3,717</u>

*Excluding adjusting items: restructuring and integration costs, Canadian settlement, amortisation of trademarks and gains on disposal of businesses and trademarks as explained on pages 22 and 23.

All centre costs are allocated to regions in the new regional structure.

The segmental analysis of the **Group's share of the post-tax results of associates and joint ventures** is as follows:

For the year ended 31 December 2008

	Post-tax profit £m	Adjusted post-tax profit* £m
Eastern Europe		
Western Europe	39	26
Asia-Pacific	121	121
Americas	341	328
Africa and Middle East	2	2
	<u>503</u>	<u>477</u>

*Excluding adjusting items: charges for trademark impairments, additional ST income, the gain on termination of joint venture and restructuring costs as explained on page 28.

NON-GAAP MEASURES

In the reporting of financial information, the Group uses certain measures that are not required under IFRS, the generally accepted accounting principles (GAAP) under which the Group reports. This is done because the Group believes that these additional measures, which are used internally, are useful to users of the financial statements in helping them understand underlying business performance.

The principal non-GAAP measure which the Group uses is adjusted diluted earnings per share, which is reconciled to diluted earnings per share. The adjusting items that mainly drive the adjustments made, are separately disclosed as memorandum information on the face of the Income Statement and the segmental analysis.

The Group also prepares an alternative cash flow, which includes a measure of 'free cash flow', to illustrate the cash flows before transactions relating to borrowings, and provides gross turnover as an additional disclosure to indicate the impact of duty, excise and other taxes. Certain reclassifications have been made in respect of gross turnover in 2008 and as a result historical information has been represented.

Following the secondary listing of the ordinary shares of British American Tobacco p.l.c. on the main board of the JSE Limited ("JSE") in South Africa, the Group is required to present headline earnings per share and diluted headline earnings per share which are additional alternative measures of earnings per share, calculated in accordance with Circular 8/2007, 'Headline Earnings' issued by the South African Institute of Chartered Accountants. These are shown on pages 30 and 31.

FOREIGN CURRENCIES

The income and cash flow statements of overseas subsidiaries and associates have been translated at the average rates for the respective periods. Assets and liabilities have been translated at the relevant period end rates. For high inflation countries, the local currency results are adjusted for the impact of inflation prior to translation to sterling at closing exchange rates.

The principal exchange rates used were as follows:

	Average		Closing	
	2008	2007	2008	2007
US dollar	1.852	2.001	1.438	1.991
Canadian dollar	1.961	2.147	1.775	1.965
Euro	1.257	1.462	1.034	1.362
South African rand	15.132	14.110	13.292	13.605
Brazilian real	3.355	3.894	3.353	3.543
Australian dollar	2.187	2.390	2.062	2.267
Russian rouble	45.810	51.161	43.902	48.847

ADJUSTING ITEMS

Adjusting items include what we previously described as exceptional items, as well as trademark amortisation and other one-off items that distort reported results. They are excluded from earnings in calculating the adjusted diluted earnings per share.

(a) Restructuring and integration costs

The review of the Group's manufacturing operations and organisational structure including the initiative to reduce overheads and indirect costs, continued. The year ended 31 December 2008 includes a charge for restructuring and integration of £160 million (2007: £173 million), principally in respect of further costs related to restructurings announced in prior years, the reorganisation of the business in the Netherlands and costs in respect of the integration of the Tekel and ST businesses into existing operations.

Adjusting items cont...

(b) Canadian settlement

On 31 July 2008, the Group's subsidiary in Canada (Imperial Tobacco Canada) announced that it had reached a resolution with the federal and provincial governments with regard to the investigation related to the export to the United States of Imperial Tobacco Canada tobacco products in the late 1980s and early 1990s. The subsidiary entered a plea of guilty to a regulatory violation of a single count of Section 240(i) (a) of the Excise Act and has paid a fine of £102 million which was included in other operating expenses in the profit from operations for the year ended 31 December 2008.

Imperial Tobacco Canada has also entered into a 15 year civil agreement with the federal and provincial governments. In order, amongst other things, to assist the governments in their future efforts against illicit trade, Imperial Tobacco Canada has agreed to pay a percentage of annual net sales revenue going forward for 15 years, up to a maximum of Can\$350 million, which will be expensed as it is incurred.

(c) Amortisation of trademarks

The acquisitions of Tekel and ST resulted in the capitalisation of trademarks which are amortised over their expected useful lives, which do not exceed 20 years. The amortisation charge of £24 million was included in depreciation and amortisation costs in the profit from operations for the year ended December 2008.

(d) Gains on disposal of businesses and trademarks

The gain on disposal of businesses and trademarks for the year ended 31 December 2008 was £141 million, of which £139 million arose on 2 July 2008 with the disposal of its 32.35 per cent holding in the non-cigarette and snus business of ST (see other changes in the Group on page 24). This gain was included in other operating income in the profit from operations for the year to 31 December 2008.

On 20 February 2007, the Group announced that it had agreed to sell its pipe tobacco trademarks to the Danish company, Orlik Tobacco Company A/S, for €24 million. The sale was completed during the second quarter in 2007 and resulted in a gain of £11 million included in other operating income in the profit from operations. However, the Group retained the Dunhill and Captain Black pipe tobacco trademarks.

On 23 May 2007, the Group announced that it had agreed to sell its Belgian cigar factory and associated brands to the cigars division of ST. The sale included a factory in Leuven as well as trademarks including Corps Diplomatique, Schimmelpennick, Don Pablo and Mercator. The transaction was completed on 3 September 2007 and a gain on disposal of £45 million was included in other operating income in the profit from operations for the year ended 31 December 2007.

On 1 October 2007, the Group agreed the termination of its license agreement with Philip Morris for the rights to the Chesterfield trademark in a number of countries in Southern Africa. This transaction resulted in a gain of £19 million included in other operating income in the profit from operations for the year ended 31 December 2007.

OTHER CHANGES IN THE GROUP

(a) Skandinavisk Tobakskompagni (ST)

On 27 February 2008, the Group agreed to acquire 100 per cent of ST's cigarette and snus businesses in exchange for its existing 32.35 per cent holding in ST and payment of DKK11,582 million (£1,237 million) in cash, following finalisation of completion accounts. Completion of this transaction was subject to regulatory approval which was subsequently received on the condition that the Group agreed to divest a small number of local trademarks, primarily in Norway. The transaction was completed on 2 July 2008.

Until the date of the transaction, the results of ST were equity accounted as an associate undertaking and following the transaction, the results of the acquired businesses have been consolidated.

The estimated fair value of the ST Group at 2 July 2008 was £2,754 million, comprising £2,128 million for the cigarette and snus businesses and £626 million for the other operations. The Group has exchanged its 32.35 per cent existing interest in ST (estimated fair value of £891 million) and cash of £1,237 million for a 100 per cent interest in the cigarette and snus businesses (estimated fair value of £2,128 million). The transaction has been accounted for as an acquisition of 67.65 per cent of the cigarette and snus businesses' net assets of ST and a disposal of the Group's existing 32.35 per cent interest in the non-cigarette and snus businesses of ST.

The goodwill of £923 million on acquisition of the cigarette and snus businesses at 2 July 2008, stated at the exchange rate ruling at the date of the transaction, arises as follows:

	Book Value £m	Fair value adjustments £m	Fair Value £m
Goodwill	45	(45)	
Other intangible assets	8	471	479
Property, plant and equipment	83	88	171
Inventories	211	6	217
Trade and other receivables	237		237
Available for sale investments	5	(5)	
Cash and cash equivalents	78		78
Overdrafts	(82)		(82)
Retirement benefit liabilities	(3)		(3)
Deferred tax liabilities		(139)	(139)
Other provisions for liabilities and charges	(7)		(7)
Trade and other payables	(364)		(364)
Assets classified as held for sale		182	182
Net assets of cigarette and snus businesses	211	558	769
Less: fair value of 32.35% existing interest in cigarette and snus businesses			(248)
Fair value of net assets acquired			521
Goodwill			923
Total consideration			1,444

Other changes in the Group cont...

	£m
The total consideration comprises:	
- Cash	1,237
- Fair value of existing 32.35% interest in ST not retained by the Group	203
- Acquisition costs	4
Total consideration	<u>1,444</u>

The transaction also results in a revaluation of the Group's 32.25 per cent previous interest in the cigarette and snus businesses retained by the Group:

	£m
- Fair value of the existing interest in ST as retained by the Group	248
- Carrying value under equity accounting prior to the transaction	<u>(69)</u>
Revaluation	<u>179</u>

The disposal of the Group's 32.35 per cent interest in the non-cigarette and snus businesses of ST gave rise to a non-taxable gain of £139 million, after costs of £3 million as follows:

	£m
- Cash	(1,237)
- Book value, including goodwill, of existing 32.35% interest in ST not retained by the Group	(80)
- Costs allocated to disposal	(3)
- Fair value of cigarette and snus businesses acquired	1,440
- Exchange differences recycled from equity	<u>19</u>
Gain on disposal of non-cigarette and snus businesses	<u>139</u>

Included within the cigarette and snus businesses acquired from ST are £182 million of local trademarks, primarily in Norway, that are being actively marketed for sale as a condition of the regulatory approval being granted. These assets are expected to be sold within a period of one year from the balance sheet date and have been included as assets classified as held-for-sale.

The book values of the acquired assets have been revalued to fair value as at the acquisition date. The main adjustments relate to the revaluations of land and buildings, recognition of cigarette trademarks and the related impact on deferred tax.

In addition to the fair value adjustments above, goodwill carried in the local books has been reversed.

The goodwill of £923 million arising on the acquisition of the cigarette and snus businesses of ST represents a strategic premium to acquire cigarette market leadership in Denmark and Norway and significant cigarette market positions in Sweden and Poland, together with a stronger snus business as a result of acquiring additional expertise and in-house manufacturing, with anticipated synergies that will arise post-acquisition. The goodwill in respect of ST on the balance sheet comprises the £923 million as a result of this transaction, together with £64 million from earlier transactions which relates to the cigarette and snus businesses.

Other changes in the Group cont...

(b) Tekel

On 22 February 2008, the Group announced that it had won the public tender to acquire the cigarette assets of Tekel, the Turkish state-owned tobacco company, with a bid of US\$1,720 million. The acquisition only relates to the cigarette assets of Tekel, which principally comprised trademarks, factories and tobacco leaf stocks. The acquisition did not include employees and the Group had directly employed the required workforce by the effective date of the transaction. Completion of this transaction was subject to regulatory approval which was subsequently received and on 24 June 2008 the Group completed the transaction, subject to finalisation of completion accounts.

The goodwill of £566 million on the cigarette assets of Tekel, stated at the exchange rates ruling at the date of the transaction, arises as follows:

Provisional values	Book value £m	Fair value adjustments £m	Fair value £m
Intangible assets		127	127
Property, plant and equipment	77	(40)	37
Deferred tax asset		1	1
Inventories	154	(24)	130
Trade and other receivables		1	1
Other provisions for liabilities and charges		(4)	(4)
Assets classified as held for sale	<u>6</u>	<u>9</u>	<u>15</u>
Net assets acquired	237	70	307
Goodwill			<u>566</u>
Total consideration			<u>873</u>
Consideration comprises:			
- Cash			866
- Acquisition costs			<u>7</u>
Total consideration			<u>873</u>

Included within the cigarette assets acquired from Tekel are certain items of property, plant and equipment that are being actively marketed for sale. These assets, amounting to £15 million are expected to be sold within a period of one year from the balance sheet date and have been included as 'Assets classified as held-for-sale'.

The book values of the acquired assets have been revalued to fair value as at the acquisition date. The main adjustments relate to the downwards revaluation of land and buildings, reduction in inventory to net realisable value and the recognition of cigarette trademarks.

The goodwill of £566 million arising on the acquisition of the cigarette assets of Tekel represents a strategic premium to acquire Tekel's significant market position in the Turkish cigarette market and significant anticipated synergies that will arise post acquisition.

Finalisation of part of the transaction is still continuing and, in addition, work in respect of identifying the appropriate fair value to be assigned to the acquired cigarette assets, has been continued since the published results for the six months to 30 June 2008. This further work has led to the goodwill increasing by £90 million compared to the provisional amount included in the six months' results. This has arisen due to more detailed on-site inspections and a review by the external valuers in determining the most appropriate fair value for property, plant and equipment and the assets disclosed as held-for-sale.

The transaction was financed from new facilities and bond issues, as described on page 34.

NET FINANCE COSTS

Net finance costs comprise:

	31.12.08 £m	Year to	31.12.07 £m
Finance costs	(658)		(405)
Finance income	267		136
	<u>(391)</u>		<u>(269)</u>
Comprising:			
Interest payable	(535)		(382)
Interest and dividend income	131		111
Fair value changes - derivatives	(521)	(143)	
Exchange differences	<u>534</u>	<u>145</u>	2
	<u>(391)</u>		<u>(269)</u>

Net finance costs at £391 million were £122 million higher than last year, principally reflecting the impact of the higher interest cost as a result of increased borrowings as well as the impact of exchange rate movements.

The net £13 million gain (2007: £2 million gain) of fair value changes and exchange differences reflects a gain of £16 million (2007: £12 million gain) from the net impact of exchange rate movements and a loss of £3 million (2007: £10 million loss) principally due to interest related changes in the fair value of derivatives.

IFRS requires fair value changes for derivatives, which do not meet the tests for hedge accounting under IAS39, to be included in the income statement. In addition, certain exchange differences are required to be included in the income statement under IFRS and, as they are subject to exchange rate movements in a period, they can be a volatile element of net finance costs. These amounts do not always reflect an economic gain or loss for the Group and, accordingly, the Group has decided that, in calculating the adjusted diluted earnings per share, it is appropriate to exclude such amounts.

The adjusted diluted earnings per share for the year ended 31 December 2008 exclude, in line with previous practice, an £11 million loss (2007: £nil) relating to exchange losses in net finance costs where there is a compensating exchange gain reflected in differences in exchange taken directly to the Statement of Recognised Income and Expense.

The Group's interest cover was also distorted by the impact of the adjusting items, shown in the adjusted diluted earnings per share calculations (page 30). It was also impacted by the acquisitions and exchange rate movements, partially offset by higher profit from operations. On an adjusted basis, based on profit before interest payable over interest payable, interest cover remains strong at 8.5x (2007: 9.4x) with the lower cover reflecting higher interest cost. Net interest cover, on the basis of profit before net finance costs over net finance costs, was 11x (2007: 12.8x).

ASSOCIATES AND JOINT VENTURES

The Group's share of post-tax results of associates and joint ventures was £503 million (2007: £442 million) after tax of £284 million (2007: £246 million). The share is after the following adjusting items which are excluded from the calculation of adjusted diluted earnings per share (page 30).

In the year ended 31 December 2008, Reynolds American modified the previously anticipated level of support between certain trademarks and the projected net sales of certain trademarks, resulting in a trademark impairment charge of which the Group's share amounted to £20 million (2007: £7 million) (net of tax).

The year end of ST, an associate of the Group to 2 July 2008, was 30 June, and, for practical reasons, the Group had previously equity accounted for its interest based on the information available from ST which was 3 months in arrears to that of the Group. As explained on page 24, the Group acquired 100 per cent of ST's cigarette and snus business on 2 July 2008. Consequently, in order to account for the Group's share of the net assets of ST at the date of the acquisition, the results of ST for the period up to 2 July 2008 have been included in the results from associates for 2008, resulting in one additional quarter's income in 2008. This contributed an additional £13 million to the share of post-tax results of associates and joint ventures.

On 21 February 2008, Reynolds American announced that it would receive a payment from Gallaher Limited resulting from the termination of a joint venture agreement. While the payment will be received over a number of years, in the year ended 31 December 2008 Reynolds American recognised a pre-tax gain of US\$328 million. The Group's share of this gain included in the results for the year amounted to £45 million (net of tax).

On 9 September 2008, Reynolds American further announced planned changes in the organisational structure at Reynolds American Inc. and its largest subsidiary, R. J. Reynolds Tobacco Company. The charge to the year's results amounted to US\$90 million. The Group's share of this charge included in the results for the year amounted to £12 million (net of tax).

Following the change in the Group accounting policy for retirement benefits, noted on page 16, the Investment in Associates and Joint Ventures on the Group balance sheet at 31 December 2007 has been increased by £47 million, with a corresponding entry to equity. The change in the Group's accounting policy did not have any impact on the results from Associates for 2008 and 2007.

TAXATION

	Year to 31.12.08 £m	31.12.07 £m restated
UK corporation tax		
Overseas tax	959	816
Adjustment in respect of prior periods	(14)	(51)
Current tax	945	765
Deferred tax	80	25
	<u>1,025</u>	<u>790</u>

The tax rates in the income statement of 27.8 per cent in 2008 and 25.7 per cent in 2007 are affected by the inclusion of the share of associates' post-tax profit in the Group's pre-tax results and by adjusting items. The underlying tax rate for subsidiaries reflected in the adjusted earnings per share below was 30.8 per cent in 2008 and 29.6 per cent in 2007. The increase arose primarily from a change in the mix of profits and as a result of one-off prior year adjustments included in 2007. The charge related to taxes payable overseas. The tax charge for 2008 also included a one-off deferred tax charge of £26 million as a result of the acquisition of the cigarette assets of Tekel. This has been excluded from the adjusted diluted earnings per share and consequently from the underlying tax rate above. The restatement of 2007 reflects the change in the Group's accounting policy as explained on page 16.

EARNINGS PER SHARE

	Year to 31.12.08 pence	31.12.07 restated pence
Earnings per share:		
- basic	123.28	105.19
- diluted	122.54	104.46
Adjusted earnings per share		
- basic	129.55	109.29
- diluted	128.78	108.53
Headline earnings per share		
- basic	114.80	103.46
- diluted	114.11	102.75

Basic earnings per share are based on the profit for the year attributable to ordinary shareholders and the weighted average number of ordinary shares in issue during the year (excluding treasury shares).

For the calculation of the diluted earnings per share, the weighted average number of shares reflects the potential dilutive effect of employee share schemes.

The presentation of headline earnings per share is mandated under the JSE Listing Requirements. It is calculated in accordance with Circular 8/2007 'Headline Earnings', as issued by the South African Institute of Chartered Accountants.

Earnings per share cont...

Earnings have been affected by a number of adjusting items, together with certain distortions to net finance costs under IFRS (see page 27) and to deferred tax (see page 29) in 2008, and to illustrate the impact of these items the adjusted diluted earnings per share are shown below:

	Diluted earnings per share	
	Year to 31.12.08 pence	31.12.07 pence
Unadjusted earnings per share	122.54	104.46
Effect of restructuring and integration costs	6.08	6.48
Effect of Canadian settlement	5.09	
Effect of amortisation of trademarks	0.90	
Effect of disposals of businesses and trademarks	(6.38)	(2.75)
Effect of net finance cost adjustment	0.55	
Effect of associates' trademark impairments, restructuring costs and termination of joint venture	(0.65)	0.34
Effect of additional ST income	(0.65)	
Effect of deferred tax adjustment	1.30	
Adjusted diluted earnings per share	<u>128.78</u>	<u>108.53</u>

Similar types of adjustments would apply to basic earnings per share.

The earnings per share are based on:

	31.12.08		31.12.07	
	Earnings £m	Shares m	Earnings £m	Shares m
Earnings per share				
- basic	2,457	1,993	2,130	2,025
- diluted	2,457	2,005	2,130	2,039
Adjusted earnings per share				
- basic	2,582	1,993	2,213	2,025
- diluted	2,582	2,005	2,213	2,039
Headline earnings per share				
- basic	2,288	1,993	2,095	2,025
- diluted	2,288	2,005	2,095	2,039

Earnings per share cont...

Headline earnings per share are calculated by taking the following adjustments into account:

	Diluted headline earnings per share	
	Year to	
	31.12.08	31.12.07
	pence	pence
Unadjusted earnings per share	122.54	104.46
Effect of impairment of goodwill and property, plant and equipment	0.25	0.84
Effect of gains on disposal of property, plant and equipment	(0.45)	(0.19)
Effect of gains on disposal of businesses and trademarks	(6.68)	(2.75)
Effect of (gains)/losses reclassified from the available-for-sale reserve	(0.30)	0.05
Effect of share of associates' trademark impairments and termination of joint ventures	(1.25)	0.34
Headline earnings per share	<u>114.11</u>	<u>102.75</u>

CASH FLOW

a) The IFRS cash flow includes all transactions affecting cash and cash equivalents, including financing. The alternative cash flow below is presented to illustrate the cash flows before transactions relating to borrowings.

	Year to	
	31.12.08	31.12.07
	£m	£m
Net cash from operating activities before restructuring costs and taxation	4,692	3,656
Restructuring costs	(210)	(190)
Taxation	(943)	(866)
Net cash from operating activities <i>page 15</i>	<u>3,539</u>	<u>2,600</u>
Net interest	(280)	(280)
Net capital expenditure	(482)	(436)
Dividends to minority interests	(173)	(173)
Free cash flow	<u>2,604</u>	<u>1,711</u>
Dividends paid to shareholders	(1,393)	(1,198)
Share buy-back	(400)	(750)
Purchase of Tekel cigarette assets	(873)	
Purchase of ST cigarette and snus businesses	(1,243)	
Other net flows	(227)	152
Net cash outflows	<u>(1,532)</u>	<u>(85)</u>

The growth in underlying operating performance, as well as the timing of working capital movements and higher dividends from associates, partly offset by the adverse impact of the £102 million cash outflow from the Canadian settlement, explained on page 23, resulted in a £1,036 million increase in cash flow before restructuring costs and taxation to £4,692 million. Although there was a £77 million increase in tax outflows reflecting higher profits and the timing of payments, with the above operating cash flows and higher restructuring costs, the Group's net cash flow from operating activities was £939 million higher at £3,539 million.

Free cash flow is the Group's cash flow before dividends, share buy-back and investing activities. With higher capital expenditure, the free cash flow was £893 million higher than 2007 at £2,604 million. The free cash flow exceeded the total cash outlay on dividends to shareholders and share buy-back by £811 million.

The ratio of free cash flow per share to adjusted diluted earnings per share was 101 per cent (2007: 77 per cent), with free cash flow per share increasing by 55 per cent.

Cash flow cont...

During 2008, the cash outflows of £873 million and £1,243 million respectively on the purchase of Tekel assets and ST businesses comprised the purchase price, part of the acquisition costs less acquired net cash and cash equivalents and overdrafts.

The other net flows in 2008 principally reflect the impact of the level of shares purchased by the employee share ownership trusts, together with the impact of outflows in respect of certain derivative financial instruments. The comparative figure for 2007 largely relates to the sale of the Belgium cigar factory and associated brands, as well as the disposal of the pipe tobacco business.

The above flows resulted in net cash outflows of £1,532 million (2007: £85 million outflow). After taking account of transactions related to borrowings, especially net new borrowings, the above flows resulted in a net increase of cash and cash equivalents of £779 million (2007: £143 million decrease) as shown in the IFRS cash flow on page 15.

b) The movements in net debt (borrowings including related derivatives, less cash and cash equivalents and current available-for-sale investments) and the maturity analyses of net debt are as follows:

	31.12.08	31.12.07
	£m	£m
Reconciliation of movements in net debt		
Net debt 1 January	(5,581)	(4,994)
Exchange*	(2,622)	(466)
Free cash flow	2,604	1,711
Dividends	(1,393)	(1,198)
Share buy-back	(400)	(750)
Tekel acquisition	(873)	
ST acquisition	(1,243)	
Other net flows	(227)	152
Other non cash items	(156)	(36)
Net debt 31 December	<u>(9,891)</u>	<u>(5,581)</u>
*Including movements in respect of debt related derivatives		
Maturity analysis of net debt		
	31.12.08	31.12.07
	£m	£m
Net debt due within one year:		
Borrowings	(2,724)	(861)
Related derivatives	(91)	(90)
Cash and cash equivalents	2,309	1,258
Current available for sale investments	79	75
	<u>(427)</u>	<u>382</u>
Net debt due beyond one year:		
Borrowings	(9,437)	(6,062)
Related derivatives	(27)	99
	<u>(9,464)</u>	<u>(5,963)</u>
Total net debt	<u>(9,891)</u>	<u>(5,581)</u>

The Group remains confident about its ability to successfully access the debt capital markets and reviews its options on an ongoing basis.

Cash flow cont...

c) Cash generated from operations (page 15)

	31.12.08	Year to 31.12.07 restated
	£m	£m
Profit from operations	3,572	2,904
Adjustments for:		
Amortisation of trademarks	24	
Gains on disposal of businesses and trademarks	(141)	(75)
Depreciation and impairment of property, plant and equipment	350	293
Amortisation and write off of intangible assets	56	43
(Increase)/decrease in inventories	(367)	170
Decrease/(increase) in trade and other receivables	19	(83)
Increase in trade and other payables	746	61
Decrease in net retirement benefit liabilities	(99)	(119)
Decrease in provisions for liabilities and charges	(31)	(16)
Other non cash items	27	3
Cash generated from operations	<u>4,156</u>	<u>3,181</u>

The restatement of the 2007 results reflects the change in the Group's accounting policy for recognition of actuarial gains and losses, together with the adoption of IFRIC14, as explained on page 16.

Cash generated from operations includes an outflow of £102 million (2007: £nil) relating to the Canada Settlement as explained on page 23.

d) IFRS Investing and financing activities

The investing and financing activities in the IFRS cash flows on page 15 include the following items:

In 2008, the £17 million cash inflow on disposal of intangibles comprises the cash received on the termination of the license agreement described on page 23, while in 2007, the £16 million cash inflow reflects the pipe tobacco trademarks, explained on page 23.

Purchases and disposals of investments (which comprise available-for-sale investments and loans and receivables) include an inflow in respect of current investments of £8 million (2007: £65 million inflow) and £1 million sales proceeds of non-current investments (2007: £6 million).

In 2008, the cash proceeds on associates' share buy-back of £42 million principally reflects the cash received in respect of the Group's participation in the share buy-back programme conducted by Reynolds American Inc.

In 2008, the cash outflow of £873 million on the purchase of Tekel assets comprises the purchase price and the acquisition costs as shown on page 26. The cash outflow of £1,243 million on the purchase of ST cigarette and snus businesses comprises the purchase price less acquired net cash and cash equivalents of £78 million and overdrafts of £82 million as shown on page 24.

In 2008, the purchase of other subsidiaries and minority interests arises from the acquisition of minority interests in the Group's subsidiaries in Africa and Middle East and Europe, while in 2007 it arises from the acquisition of minority interests in the Group's subsidiaries in Africa and Middle East, Europe and Asia Pacific.

In 2008, the cash inflow on disposal of subsidiaries reflects the net proceeds on the sale of a non-core business in the Asia Pacific region, while for the year ended 31 December 2007 the cash inflows principally reflected the proceeds from sale of the Belgian Cigar factory and associated trademarks.

Cash flow cont...

The movement relating to derivative financial instruments is in respect of derivatives taken out to hedge cash and cash equivalents and external borrowings, derivatives taken out to hedge inter company loans and derivatives treated as net investment hedges. Derivatives taken out as cash flow hedges in respect of financing activities are also included in the movement relating to derivative financial instruments, while other such derivatives in respect of operating and investing activities are reflected along with the underlying transactions.

Dividends paid for the year to 31 December 2008 include £1,393 million (2007: £1,198 million) of dividends to Group shareholders and £173 million (2007: £173 million) to minority shareholders.

e) Net cash and cash equivalents in the cash flow statement comprise:

	31.12.08	31.12.07
	£m	£m
Cash and cash equivalents per balance sheet	2,309	1,258
Accrued interest	(3)	
Overdrafts	(86)	(78)
Net cash and cash equivalents	<u>2,220</u>	<u>1,180</u>

f) Liquidity

In the year ended 31 December 2008, the €1.8 billion revolving credit facility arranged in December 2007 was cancelled and replaced with the issue of €1.25 billion and £500 million bonds maturing in 2015 and 2024 respectively. In addition to this, the Group increased its €1 billion (5.375 per cent, maturity 2017) bond by an additional €250 million, bringing the total size of the bond to €1.25 billion.

During the year the Group also issued US\$300 million and US\$700 million bonds, maturing in 2013 and 2018 respectively, pursuant to Rule 144A and RegS under the US Securities Act. The Group also repaid US\$330 million and £217 million bonds upon maturity in May and November respectively. In addition, on 22 September 2008, the Group repurchased its maturing Mexican 2011 MXN1,055 million UDI bond and refinanced it with a floating rate borrowing of MXN1,444 million.

On 13 February 2008, the Group entered into an acquisition credit facility whereby lenders agreed to make available an amount of US\$2 billion. On 1 May 2008, this facility was syndicated in the market and was redenominated into two euro facilities, one of €420 million and one of €860 million. These facilities expire on 31 October 2009. There was a net draw down on these credit facilities of €1.15 billion during the year ended 31 December 2008 (2007 €nil).

In March 2007, €800 million of €1.7 billion bonds with a maturity of February 2009 were replaced by €1 billion bonds with a maturity of 2017. In March 2007 the Group's central banking facility at £1.75 billion was extended on existing terms under a one year extension option with final maturity dates between March 2011 and March 2012, and was undrawn as at 31 December 2008.

RETIREMENT BENEFIT SCHEMES

The Group's subsidiaries operate around 150 retirement benefit arrangements globally. The majority of the scheme members belong to defined benefit schemes, most of which are funded externally and are closed to new entrants. The Group also operates a number of defined contribution schemes.

The overall net liability for all pension schemes and healthcare schemes amounted to £773 million at the end of 2008, up from £323 million at the end of 2007. The present total value of funded scheme liabilities was £4,647 million (2007: £4,265 million), while unfunded scheme liabilities amounted to £248 million (2007: £232 million).

The increase in the scheme liabilities and deficit in the schemes, were largely due to an increase in life expectancy and the fall in asset values on world markets, partly offset by higher discount rates for liabilities.

Contributions to the defined benefit schemes are determined after consultation with the respective trustees and actuaries of the individual externally funded schemes, taking into account the regulatory environment.

MOVEMENTS IN TOTAL EQUITY

	31.12.08	31.12.07 restated
	£m	£m
Total recognised income and expense for the year <i>page 12</i>	2,147	2,615
Employee share options		
- value of employee services	51	37
- proceeds from shares issued	10	27
Dividends and other appropriations		
- ordinary shares	(1,393)	(1,198)
- to minority interests	(176)	(173)
Purchase of own shares		
- held in employee share ownership trusts	(116)	(41)
- share buy-back programme	(400)	(750)
Acquisition of minority interests	(5)	(9)
Other movements	8	(3)
	<u>126</u>	<u>505</u>
Balance 1 January	7,089	6,584
Balance 31 December	<u>7,215</u>	<u>7,089</u>

Total equity was £126 million higher at £7,215 million. The profit retained after payment of dividends exceeded the level of the share buy-back by £664 million. In addition, exchange movements had a £937 million positive impact on shareholders' funds, reflecting the general weakness of sterling at the end of 2008 compared to 2007.

The restatement of the 2007 results reflects the change in the Group's accounting policy for recognition of actuarial gains and losses, together with the adoption of IFRIC14, as explained on page 16.

LITIGATION: FRANKED INVESTMENT INCOME GROUP LITIGATION ORDER

British American Tobacco is the principal test claimant in an action in the United Kingdom against HM Revenue and Customs in the Franked Investment Income Group Litigation Order ("FII GLO"). There are over 20 companies in the FII GLO. The case concerns the treatment for UK corporate tax purposes of profits earned overseas and distributed to the UK. The claim was filed in 2003 and the case was heard in the European Court of Justice in 2005 and a decision of the ECJ received in December 2006. In July 2008, the case reverted to a trial in the UK High Court for the UK Court to determine how the principles of the ECJ decision should be applied in a UK context.

The High Court judgment in November 2008 concluded, amongst many other things, that dividends received from EU subsidiaries should be, and should have been, exempt from UK taxation. It also concluded that certain dividends received before 5 April 1999 from the EU and, in some limited circumstances after 1993 from outside the EU, should have been treated as franked investment income with the consequence that advance corporation tax need not have been paid. Claims for the repayment of UK tax incurred where the dividends were from the EU can be made back to 1973. The case will now proceed to the Court of Appeal.

The tentative conclusion reached in the judgment would, if upheld, produce an estimated receivable of about £1.2 billion for British American Tobacco.

The potential receipt of some or all of the amount referred to above has not been recognised in the results of the Group due to the uncertainty of the amounts and eventual outcome.

CONTINGENT LIABILITIES

The Group is subject to contingencies pursuant to requirements that it complies with relevant laws, regulations and standards. Failure to comply could result in restrictions in operations, damages, fines, increased tax, increased cost of compliance, reputational damage, or other sanctions. These matters are inherently difficult to quantify.

In cases where the Group has an obligation as a result of a past event existing at the balance sheet date, it is probable that an outflow of economic resources will be required to settle the obligation and the amount of the obligation can be reliably estimated, a provision would be recognised based on best estimates and management judgment.

There are, however, contingent liabilities in respect of litigation, taxes in some countries and guarantees for which no provisions were made.

The Group has exposures in respect of the payment or recovery of a number of taxes. The Group is and has been subject to a number of tax audits covering amongst others, excise tax, value added taxes, sales taxes, corporate taxes, withholding taxes and payroll taxes.

The estimated costs of known tax obligations have been provided in these accounts in accordance with the Group's accounting policies. In some countries, tax law requires that full or part payment of disputed tax assessments be made pending resolution of the dispute. To the extent that such payments exceed the estimated obligation, they would not be recognised as an expense. In some cases disputes are proceeding to litigation.

While the amounts that may be payable or receivable could be material to the results or cash flows of the Group in the period in which they are recognised, the Board does not expect these amounts to have a material effect on the Group's financial condition.

Contingent liabilities cont...

Product liability litigation

Group companies, notably Brown & Williamson Holdings, Inc. (formerly Brown & Williamson Tobacco Corporation) (B&W) as well as other leading cigarette manufacturers, are defendants, principally in the United States, in a number of product liability cases. In a number of these cases, the amounts of compensatory and punitive damages sought are significant.

Indemnity

In 2004, B&W completed the combination of the assets, liabilities and operations of its US tobacco business with R.J. Reynolds Tobacco Company (RJRT), a wholly-owned subsidiary of R.J. Reynolds Tobacco Holdings, Inc., pursuant to which Reynolds American Inc. was formed (the Business Combination). As part of the Business Combination, B&W contributed to RJRT all of the assets and liabilities of its US cigarette and tobacco business, subject to specified exceptions, in exchange for a 42 per cent. equity ownership interest in Reynolds American. As a result of the Business Combination:

B&W discontinued the active conduct of any tobacco business in the United States;

B&W contributed to RJRT all of its assets other than the capital stock of certain subsidiaries engaged in non-US businesses and other limited categories of assets;

RJRT assumed all liabilities of B&W (except liabilities to the extent relating to businesses and assets not contributed by B&W to RJRT and other limited categories of liabilities) and contributed subsidiaries or otherwise to the extent related to B&W's tobacco business as conducted in the US on or prior to 30 July 2004; and

RJRT agreed to indemnify B&W and each of its associates (other than Reynolds American and its subsidiaries) against, among other matters, all losses, liabilities, damages, expenses, judgments, attorneys' fees, etc., to the extent relating to or arising from such assumed liabilities or the assets contributed by B&W to RJRT (the RJRT Indemnification).

The scope of the RJRT Indemnification includes all expenses and contingent liabilities in connection with litigation to the extent relating to or arising from B&W's US tobacco business as conducted on or prior to 30 July 2004, including smoking and health tobacco litigation, whether the litigation is commenced before or after 30 July 2004 (the Tobacco Litigation).

Pursuant to the terms of the RJRT Indemnification, RJRT is liable for any possible judgments, the posting of appeal bonds or security, and all other expenses of and responsibility for managing the defence of the Tobacco Litigation. RJRT has assumed control of the defence of the Tobacco Litigation involving B&W, to which RJRT is also a party in most (but not all) of the same cases. Accordingly, RJRT uses or plans to use the same law firm or firms to represent both B&W and RJRT in any single or similar case (except in certain limited circumstances) as RJRT's interests are typically aligned with B&W's interests, as RJRT has substantial experience in managing recognised external legal counsel in defending the Tobacco Litigation, and external counsel have independent professional responsibilities to represent the interests of B&W. In addition, in accordance with the terms of the RJRT Indemnification, associates of B&W have retained control of the defence in certain Tobacco Litigation cases with respect to which such associates are entitled to indemnification.

Contingent liabilities cont...

US litigation

The total number of US product liability cases pending at 31 December 2008 involving B&W and/or other Group companies was approximately 3,251 (2007: approximately 3,323). At 31 December 2008, UK-based Group companies have been named as co-defendants in six of those cases (2007: six). In 2008, no US cases were tried against B&W. No US cases involving the UK-based Group companies were tried in 2008. No product liability case in which a UK-based Group company is a defendant is currently scheduled for trial in 2009.

Since many of these pending cases seek unspecified damages, it is not possible to quantify the total amounts being claimed, but the aggregate amounts involved in such litigation are significant. The cases fall into four broad categories:

(a) Medical reimbursement cases

These civil actions seek to recover amounts spent by government entities and other third party providers on healthcare and welfare costs claimed to result from illnesses associated with smoking. Although B&W continues to be a defendant in healthcare cost recovery cases involving plaintiffs such as hospitals and Native American tribes (see below), the vast majority of such cases have been dismissed on legal grounds.

Further, on 23 November 1998, the major US cigarette manufacturers (including B&W and RJRT) and the attorneys general of 46 US states and five US territories executed the Master Settlement Agreement (MSA), which settled recoupment lawsuits that had been brought by these states and territories. Under the terms of the MSA, the settling cigarette manufacturers agreed, among other things, to pay approximately US\$246 billion to the settling states and territories (and to four states that had reached separate settlements of their recoupment actions) over 25 years, and agreed to various restrictions on US tobacco advertising and marketing. The MSA includes a credit for any amounts paid by participating tobacco manufacturers in subsequent suits brought by the states' political subdivisions.

At 31 December 2008, a reimbursement suit was pending against B&W by an Indian tribe in Indian tribal court in South Dakota, and another reimbursement case (City of St. Louis) was pending against B&W and a UK-based company. In City of St. Louis, plaintiffs consist of more than 60 public and non-profit hospitals in Missouri seeking reimbursement of past and future alleged smoking related healthcare costs. Summary judgment motions are pending and discovery remains ongoing. A trial date for this case has been set for 11 January 2010.

(b) Class actions

At 31 December 2008, B&W was named as a defendant in some 10 (2007: 12) separate actions attempting to assert claims on behalf of classes of persons allegedly injured or financially impacted through smoking or where classes of tobacco claimants have been certified. Even if the classes are or remain certified and the possibility of class-based liability is eventually established, it is likely that individual trials will still be necessary to resolve any actual claims. Class-action suits have been filed in a number of US state and federal courts against individual cigarette manufacturers and their parent corporations, alleging that the use of terms such as "lights" and "ultralights" constitutes unfair and deceptive trade practices.

A class action complaint (Schwab) was filed in the US District Court for the Eastern District of New York on 11 May 2004 against several defendants, including B&W and certain UK-based Group companies. The complaint challenges defendants' practices with respect to the marketing, advertising, promotion and sale of "light" cigarettes, and seeks billions of dollars in economic damages. The district court granted plaintiffs' motion for class certification on 25 September 2006. On 3 April 2008, the Schwab class was decertified by the Second Circuit Court of Appeals. The mandate returning the case to the district court was issued on 29 May 2008.

Contingent liabilities cont...

Other types of class-action suits assert claims on behalf of classes of individuals who claim to be addicted, injured, or at greater risk of injury by the use of tobacco or exposure to environmental tobacco smoke, or the legal survivors of such persons.

In *Engle* (Florida), filed on 5 May 1994, a jury rendered a punitive damages verdict in favour of the Florida class against all defendants, with US\$17.6 billion in punitive damages assessed against B&W. After various post-trial and appellate proceedings, the Florida Supreme Court, among other things, affirmed an intermediate appellate court's decision to decertify the class, vacated the jury's punitive damages award and permitted putative *Engle* class members to file individual lawsuits against the *Engle* defendants within one year of the Court's decision (subsequently extended to 11 January 2008). As of 31 December 2008, B&W has been served individually in approximately 54 *Engle* progeny cases pending in Florida courts. These cases include approximately 110 plaintiffs.

In the first trial of an individual *Engle* class member (*Lukacs*), the jury, on 11 June 2002, awarded plaintiff US\$37.5 million in compensatory damages (B&W's share: US\$8.4 million). After post-trial proceedings, on 12 November 2008, the trial court entered judgment for plaintiff in the amount of US\$24,835,000 (plus interest), for which defendants were jointly and severally liable. Defendants filed an appeal from the judgment on 1 December 2008.

In a case filed on 24 May 1996 by a class of Louisiana smokers (*Scott*) in Louisiana state court against several US cigarette manufacturers (including B&W), the jury, on 28 July 2003, returned a verdict in defendants' favour on a medical monitoring claim, but made findings against defendants with respect to claims relating to fraud, conspiracy, marketing to minors and smoking cessation. On 21 May 2004, the jury returned a verdict in the amount of US\$591 million on the class's claim for a smoking cessation programme. On 7 February 2007, an intermediate appellate court, among other things, affirmed class certification and upheld the smoking cessation programme for certain smokers who began smoking before 1988, but reduced the US\$591 million jury award by US\$312 million and rejected any award of prejudgment interest. On 21 July 2008, the trial court entered judgment in the case, finding that defendants were jointly and severally liable for funding the cost of a court-supervised smoking cessation programme, and ordering defendants to deposit approximately US\$264 million together with interest from 30 June 2004 into a trust for the funding of the programme. On 15 December 2008, the trial court entered an order permitting defendants to take a suspensive appeal, thereby staying enforcement of the judgment pending the resolution of defendants' appeal.

A class action complaint (*Cleary*) was filed in state court in Chicago, Illinois on 3 June 1998 against several defendants, including B&W, B.A.T Industries p.l.c. (Industries) and British American Tobacco (Investments) Limited (Investments). Industries was dismissed on jurisdictional grounds by an intermediate appellate court on 17 March 2000. The second amended complaint, filed on 8 April 2005, alleges, among other things, that defendants fraudulently concealed facts regarding the addictive nature of nicotine and that certain US defendants marketed tobacco products to underage consumers, and seeks, among other remedies, disgorgement of profits. On 11 July 2006, plaintiffs filed a renewed motion for class certification, which remains pending. The case is currently in class certification discovery.

(c) Individual cases

Approximately 3,238 cases were pending against B&W at 31 December 2008 (2007: approximately 3,307) filed by or on behalf of individuals in which it is contended that diseases or deaths have been caused by cigarette smoking or by exposure to environmental tobacco smoke (ETS). Of these cases, approximately: (a) 2,620 are ETS cases brought by flight attendants who were members of a class action (*Broin*) that was settled on terms that allow compensatory but not punitive damages claims by class members; (b) 490 of the individual cases against B&W are cases brought in consolidated proceedings in West Virginia; (c) 54 are *Engle* progeny cases that have been served upon B&W, and (d) 74 are cases filed by other individuals.

Contingent liabilities cont...

There are three verdicts against B&W that remained subject to appeal in 2008:

In December 2003 and January 2004, a New York state court jury (Frankson) awarded an individual plaintiff compensatory and punitive damages against B&W and two industry organisations. After post-trial and appellate proceedings, the trial court entered judgment on 26 June 2007 in the amounts of US\$175,000 in compensatory damages and US\$5 million in punitive damages. Defendants subsequently appealed from the judgment to an intermediate appellate court. Appellate oral argument was heard on 26 January 2009. A decision remains pending.

In February 2005, a Missouri state court jury (Smith) awarded an individual plaintiff US\$500,000 in compensatory damages and US\$20 million in punitive damages against B&W. On 16 December 2008, an intermediate Missouri appellate court affirmed the compensatory damages award, but remanded the case for a new trial on issues relating to punitive damages. B&W filed a motion for rehearing on 31 December 2008, which was denied on 27 January 2009.

On 18 March 2005, a New York state court jury (Rose) awarded an individual plaintiff US\$1.7 million in compensatory damages against B&W. On 10 April 2008, an intermediate state appellate court reversed the judgment and ordered that the case be dismissed. On 16 December 2008, the New York Court of Appeals affirmed the intermediate appellate court's ruling. Plaintiff filed a motion to reargue to the Court of Appeals on 14 January 2009, and defendants filed a response on 9 February 2009. A decision on this motion remains pending.

(d) Other claims

The Flintkote Company (Flintkote), a US asbestos production and sales company, was included in the acquisition of Genstar Corporation by Imasco Limited in 1986 and became a Group subsidiary following the restructuring of Imasco Limited (now Imperial Tobacco Canada Limited (Imperial), the Group's operating company in Canada) in 2000. Soon after this acquisition, and as part of the acquisition plan, Genstar began to sell most of its assets, including the non-asbestos related operations and subsidiaries of Flintkote. The liquidation of Flintkote assets produced cash proceeds and, having obtained advice from the law firm of Sullivan & Cromwell LLP and other advice that sufficient assets would remain to satisfy liabilities, Flintkote and Imasco authorised the payment of a dividend of US\$170.2 million in 1986 and a further dividend of US\$355 million in 1987. In 2003, Imperial divested Flintkote and then, in 2004, Flintkote filed for bankruptcy in the United States Bankruptcy Court for the District of Delaware. In 2006, Flintkote, representatives of both the present and future asbestos claimants, and individual asbestos claimants were permitted by the bankruptcy court to file a complaint against Imperial and numerous other defendants including Sullivan & Cromwell LLP, for the recovery of the dividends and other compensation under various legal and equitable theories. Sullivan & Cromwell LLP and Imperial have since filed cross complaints against each other. The parties are presently engaged in case management discussions to establish the scope and manner of discovery in this case.

In Wisconsin, the authorities have identified potentially responsible parties (PRPs) to fund the clean up of the Fox River, Wisconsin. The pollution was caused by the alleged discharges of toxic material from paper mills operating close to the river. The cost of the clean up work has been estimated to be in the order of US\$600 million. Among the PRPs are NCR Corporation (NCR) and Appleton Papers Inc. (Appleton) who may be liable for a proportion of the clean up costs. In 1978, Industries purchased what was then NCR's Appleton Papers Division from NCR. In 1978, Industries also incorporated a US entity by the name of BATUS, Inc. (BATUS), which in 1980 became the holding company for all of Industries' US subsidiaries, including Appleton. As the holding company, BATUS obtained insurance policies for itself and its subsidiaries that included coverage for certain environmental liabilities. Industries/BATUS spun off the Appleton business in 1990 to Wiggins Teape

Contingent liabilities cont...

Appleton p.l.c. and Wiggins Teape Appleton (Holdings) p.l.c., now known as Arjo Wiggins Appleton Ltd. and Arjo Wiggins US Holdings Ltd. (collectively, the AWA Entities), obtaining full indemnities from AWA Entities for past and future environmental claims. Disputes between NCR, Appleton, the AWA Entities, and Industries as to the indemnities given and received under the purchase agreement in 1978 have been the subject of arbitrations in 1998 and 2006. Under the terms of the arbitration awards, Industries and Appleton/the AWA Entities have an obligation to share the costs of environmental claims with NCR, but Industries has never been required to pay any sums in this regard because Appleton and the AWA Entities have paid any sums demanded to date, and the authorities have not identified Industries or BATUS as PRPs. It is believed that all future environmental liabilities will continue to be met directly by Appleton and the AWA Entities by self-funding or insurance cover and no demand will be made upon Industries. However, the risk for Industries in respect of the Fox River clean up is that Appleton and the AWA Entities will exhaust insurance policies beyond that which Industries believes Appleton and the AWA Entities are entitled to under the demerger agreement, potentially leaving Industries with no insurance to call on should it be called on to contribute. There is currently a tolling agreement in place with regard to the differing interpretations of the provisions of the demerger agreement in this regard, which preserves the parties' rights to litigate the issue even though the limitation period has expired. Given the likelihood that the case will not be resolved for some time, Appleton, the AWA Entities, Industries and BATUS have agreed to extend the tolling agreement until 31 December 2009.

UK-based Group companies

At 31 December 2008, Industries was a defendant in the US in one class action, the Schwab case mentioned previously. In that case, Industries was substituted for British American Tobacco p.l.c. as a defendant. Investments had been served in one reimbursement case (City of St. Louis), the Department of Justice case (see below), one anti-trust case (Daric Smith, see below), two class actions (Cleary and Schwab) and two individual actions (Eiser and Perry).

Conduct-based claims

On 22 September 1999, the US Department of Justice brought an action in the US District Court for the District of Columbia against various industry members, including B&W, Industries and Investments. Industries was dismissed for lack of personal jurisdiction on 28 September 2000. The Government sought, among other relief, the disgorgement of US\$280 billion in past profits pursuant to the federal Racketeer Influenced and Corrupt Organisations Act (RICO) statute. On 4 February 2005, the DC Circuit Court of Appeals ruled that the Government could not claim disgorgement of profits under RICO. On 17 August 2006, the district court issued its final judgment in favour of the Government, and against certain defendants, including B&W and Investments. The court also ordered a wide array of injunctive relief, including a ban on the use of "lights" and other similar descriptors. Investments' compliance with the court-ordered remedies may result in potentially significant financial exposure. Defendants, including B&W and Investments, filed notices of appeal to the DC Circuit Court of Appeals on 11 September 2006, and thereafter obtained a stay of the district court's judgment. Appellate briefing has been completed and oral argument took place on 14 October 2008. A decision remains pending.

In the Daric Smith case, purchasers of cigarettes in the State of Kansas brought a class action in the Kansas State Court against B&W, Investments and certain other tobacco companies seeking injunctive relief, treble damages, interest and costs. The allegations are that defendants participated in a conspiracy to fix or maintain the price of cigarettes sold in the US, including the State of Kansas, in violation of the Kansas Restraint of Trade Act. Discovery is continuing.

Product liability outside the United States

At 31 December 2008, active claims against the Group's companies existed in 18 (2007: 18) markets outside the US but the only markets with more than five active claims were Argentina, Brazil, Canada, Chile, Italy, Nigeria, and the Republic of Ireland. There has been new litigation in Bulgaria and Israel, where class actions have been filed, and in Russia where the Ministry of Health commenced a consumer protection claim. In 2008, judgments in favour of the defence were rendered in individual smoking and health cases in Finland, the Netherlands and Chile. The following is a description of the major developments since the last report in cases pending outside the United States that fall into four broad categories:

(a) Medical reimbursement cases

Argentina

ATLA (Argentine Tort Law Association) in June 2007 instigated a lawsuit stating damages and medical recoupment claims as against Nobleza-Piccardo S.A.I.C.y F. (Nobleza Piccardo). ATLA sought to have certain public entities joined as plaintiffs. On 23 December 2008, the court allowed intervention by the national government and declined to accept in full certain defences asserting legal invalidity of the claims. Nobleza Piccardo will appeal this ruling.

Brazil

The São Paulo State Public Prosecutor instigated a lawsuit in July 2007 comprising product liability, ETS and medical recoupment claims. On 7 October 2008, Souza Cruz S.A. (Souza Cruz) filed an objection to a motion to intervene as an additional plaintiff by ACTbr, a private anti-tobacco group. On 17 October 2008, the court issued an order to plaintiffs to respond to certain of defendants' procedural requests, as well as certain defences and objections.

Canada

The government of the Province of British Columbia brought a claim pursuant to the provisions of the Tobacco Damages and Health Care Costs Recovery Act 2000 (the Recovery Act) against domestic and foreign manufacturers seeking to recover plaintiff's costs of health care benefits. Investments, Industries, Imperial and certain former Rothmans Group companies are named as defendants. The constitutionality of the Recovery Act was challenged by certain defendants. Ultimately, in September 2005, the Supreme Court of Canada declared the Recovery Act to be constitutionally valid. The defendants joined the federal Government of Canada as a defendant and the federal Government, in turn, filed a motion to strike the claim. The Supreme Court of British Columbia found in favour of the federal Government, dismissing it from the action. Defendants' subsequent appeal of that order has been consolidated with a similar appeal in the Knight case (see below). The appeals are scheduled to be heard in the week of 1 June 2009. Non-Canadian defendants, including Investments and Industries, sought to dismiss the action on the ground that the British Columbia court lacked personal jurisdiction over them. These motions were subsequently denied, and defendants' appeal of these decisions was ultimately unsuccessful. The claim is now set down for trial in September 2011.

In another Canadian recoupment case, the government of the Province of New Brunswick has brought a health care recoupment claim against domestic and foreign tobacco manufacturers, pursuant to the provisions of the Recovery Act passed in that Province in June 2006. The Company, Investments, Industries, Imperial and certain former Rothmans Group companies have all been named as defendants. The government filed a statement of claim on 13 March 2008. The Group defendants were served with the Notice of Action and Statement of Claim on 2 June 2008.

Colombia

British American Tobacco (South America) Limited was served on 18 July 2008 in a public interest action that has a recoupment component. The case was brought by two Colombian citizens alleging that the defendant violated numerous "collective" interests and rights of the Colombian population. In addition to equitable and injunctive relief, plaintiffs are seeking 25 per cent. of smoking-related health-care costs since the time that the Group has been operating in Colombia.

Israel

Clalit, one of the main healthcare providers in Israel, filed a recoupment claim on 28 September 1998 in the Tel Aviv District Court against several local and international tobacco companies. Clalit seeks NIS 7.6 billion (approximately US\$1.9 billion) in damages and injunctive relief. Following a series of procedural negotiations between the parties, the Group companies currently named as defendants in the action are Industries, B&W, B.A.T (U.K. and Export) Limited (BATUKE) and Investments. In 2003, the Group company defendants except for Industries, and others, filed motions to strike the Statement of Claim on the ground that Clalit's claims are remote and derivative, and therefore cannot be brought as direct claims. On 16 February 2004, the District Court judge issued a consolidated decision denying defendants' motions. Defendants have appealed this decision to the Supreme Court. The outcome of the Supreme Court ruling on defendants' appeals is still awaited. Additionally, in 2002, Industries filed a motion to set aside service as improper due to its lack of contacts with the jurisdiction. That motion was denied in or about November 2005, and Industries subsequently filed a motion seeking leave to appeal that decision to the Supreme Court. A decision on Industries' motion is stayed pending a ruling on the other defendants' motions to strike.

Nigeria

In 2007, four Nigerian states (Lagos, Kano, Gombe, and Oyo) and the federal government of Nigeria filed separate health care recoupment actions, each seeking the equivalent of billions of US Dollars for costs allegedly incurred by the state and federal governments in treating smoking-related illnesses. British American Tobacco (Nigeria) Limited, the Company and Investments have all been named as defendants, and have filed preliminary objections in each of the pending cases. In 2008, a healthcare recoupment claim was also filed in Akwa Ibom state. The Company and British American Tobacco (Nigeria) Limited have been served with notices in that action. A healthcare recoupment claim has reportedly also been filed in Ogun state. No Group companies have been served with that claim.

On 21 February 2008, the initial Lagos action was voluntarily discontinued by plaintiffs and replaced on 13 March 2008 with a substantially similar action. British American Tobacco (Nigeria) Limited, the Company and Investments have all been served in the new action and have filed preliminary objections. On 8 July 2008, the High Court of Gombe State ruled on the preliminary objections filed by the Company, Investments and other defendants in the case, setting aside service on all defendants and striking out the claim. Plaintiff has since filed a renewed action and the court has granted plaintiff's application for leave to issue and serve a writ of summons outside the jurisdiction. In Kano and Oyo States, proceedings are currently concerned with determining the parties' preliminary objections to jurisdiction. Matters in the Akwa Ibom and Federal claims stand adjourned for reports on service.

Saudi Arabia

There are reports that the Saudi Ministry of Health is pursuing a health-care recoupment action in the Riyadh General Court against a number of tobacco distributors and agents. At 31 December 2008, no Group company had been served with process. The Ministry of Health is reportedly seeking damages of at least 127 billion Saudi Riyals. In addition, a separate recoupment action has reportedly been filed by the King Faisal Specialist Hospital in the Riyadh General Court, naming 'BAT Company Limited' as a defendant. At 31 December 2008, no Group company had been served with process.

Spain

The Junta de Andalucía, together with the Health Service of Andalucía (hereinafter "Junta") filed, on 20 September 2007, a recoupment action against the Spanish State and six tobacco companies, including British American Tobacco España, S.A. (BAT España). The Junta seeks the reimbursement of €1,769,964 allegedly spent in healthcare costs for treating patients with smoking-related diseases. The Court upheld the State's preliminary objections to the claim and dismissed the claim on 14 November 2007. On 4 March 2008, the Junta filed a notice of its intention to appeal that decision. The Junta's appeal remains pending. On 23 July 2008, BAT España was served with notice of a new claim by the Junta asserting essentially the same claims as in the prior action.

Contingent liabilities cont...

(b) Class actions

Brazil

In 1995, a class action was filed by the Association for the Defence of the Health of Smokers (ADESF) against Souza Cruz and other tobacco manufacturers in the São Paulo Lower Civil Court alleging that defendants are liable to a class of smokers and former smokers for failing to warn of cigarette addiction. Plaintiffs seek monetary damages and injunctive relief. The case was stayed in 2004 pending defendants' appeal from a decision issued by the lower civil court on 7 April 2004. On 12 November 2008, the São Paulo Court of Appeals overturned the lower court's unfavourable decision of 2004, finding that the lower court had failed to provide defendants with an opportunity to produce evidence. The case now returns to the lower court for production of evidence and a new judgment.

The Brazilian Association for the Defence of Consumers' Health (Saudecon) filed a class action against Souza Cruz in the City of Porto Alegre, Brazil on 3 November 2008. Plaintiff purports to represent all Brazilian smokers whom, it alleges, are unable to quit smoking and lack access to cessation treatments. Plaintiff is seeking an order requiring the named defendants to fund, according to their market share, the purchase of cessation treatments for these smokers over a minimum period of two years. Souza Cruz filed its Statement of Defence on 26 January 2009.

A consumer association known as ACODE (Association of Exploited Consumers of the Federal District) instigated an action in essence seeking a court order to stop Souza Cruz from marketing cigarettes in Brazil. In December 2006, the 4th Chamber of the Federal District Court of Appeals confirmed a lower court decision that ruled the claim groundless and unlawful. Plaintiff filed an appeal before the Superior Court of Justice which has been pending final review since May 2007.

The State of Sergipe instigated in 2004 a class action seeking compensation for smokers in Sergipe State who purportedly sought to quit smoking. The lower court denied plaintiffs' request for early relief and determined that all Brazilian tobacco companies and ANVISA be ordered to join the case as co-defendants. Since then all the parties involved have yet to be served process.

Bulgaria

In March 2008, a collective claim was filed in the Sofia City Court of Bulgaria against 21 defendants, including British-American Tobacco Polska S.A., British-American Tobacco (Romania) Trading SRL, and House of Prince A/S. Plaintiff seeks recovery of roughly 17,000 Leva (approximately US\$12,000) in damages per class member and injunctive relief. The claim was dismissed twice on procedural deficiencies, but re-instated both times on appeal. On 2 December 2008, the Sofia City Court dismissed the youth advertising claim and required plaintiff to meet various evidentiary and procedural conditions in order to proceed with the claim.

Canada

In the Knight class action in Canada, the Supreme Court of British Columbia certified a class of all consumers of cigarettes bearing "light" or "mild" descriptors since 1974 manufactured in British Columbia by Imperial. The British Columbia Court of Appeal affirmed the certification of the class but has limited any potential financial liability to the period from 1997. This is a "lights" class action in which plaintiff alleges that the marketing of light and mild cigarettes is deceptive because it conveys a false and misleading message that those cigarettes are less harmful than regular cigarettes. Plaintiff seeks compensation for amounts spent on "light and mild" products and a disgorgement of profits from Imperial. Imperial joined the federal Government of Canada as a defendant and the federal Government, in turn, filed a motion to strike the claim. The court subsequently dismissed the federal Government from the action. Imperial appealed that order, and its appeal has been consolidated with a similar appeal in the British Columbia recoupment litigation (see above). Hearings are scheduled for the week of 1 June 2009.

Contingent liabilities cont...

A similar "lights" and "mild" class action claim has been filed in Newfoundland. Imperial has filed a third party notice against the Federal Government. The certification hearing took place in September 2007. Certification was denied on 29 December 2008 and Imperial subsequently received plaintiffs' notice for leave to appeal.

There are currently two class actions in Quebec. On 21 February 2005, the Quebec Superior Court granted certification. The court certified two classes, which include residents of Quebec who suffered from lung, throat and laryngeal cancer or emphysema, and residents who were addicted to nicotine at the time the proceedings were filed and who have since remained addicted. Plaintiffs have served a Statement of Claim.

On 12 May 2008, the Ontario Court of Appeal dismissed plaintiffs' appeal in the Ragoonanan class action. The proposed class action sought to certify as a class "all persons who suffered bodily damage or property damage as a result of fires commenced by cigarettes that did not automatically extinguish upon being dropped or left unattended". Certification was denied in first instance and leave to appeal was denied in the 12 May 2008 decision. In summary, the court decided that there was no rational relationship between the class definition and the proposed common issues and that a class action was not a preferable procedure.

Israel

In May 2008, nine smokers of low yield cigarettes filed a class action in Israel, known as Numberg, before the Tel Aviv District Court against various defendants including the Group's Israeli distributor, Globbrands Agencies 2007 Limited. Plaintiffs allege that since December 2004, defendants have fraudulently marketed and sold low yield cigarettes in Israel, in contravention of what they interpret to be an express ban on the sale of such products following the prohibition on the use of "lights" descriptors, by using methods such as marking cigarette packages in a special colour, using descriptors such as "slim" or "super slim", and displaying text that describes the amount of tar and nicotine yields. In addition to injunctive and declaratory relief, plaintiffs seek 78.5 billion NIS (approximately US\$20.3 billion) in monetary damages.

Venezuela

FEVACU (Venezuelan Federation of Associations of Users and Consumers) instigated a purported class action that was admitted by the court on 22 October 2008 seeking, among other relief, that defendant be required to fund a trust for the treatment of alleged smoking-related diseases. On 19 January 2009, C.A. Cigarrera Bigott Sucs. appeared as a third party whose rights may be affected by the proceedings, as provided under the procedural law.

(c) Individual cases

Brazil

As of 31 December 2008, there were approximately 310 individual cases that remain pending in Brazil against Souza Cruz in which it is contended that the smokers' diseases or deaths were caused by cigarette smoking. Since 1995, approximately 530 individual cases have been filed in Brazil against Souza Cruz. Approximately ten of these cases have resulted in court decisions favourable to plaintiffs in either the civil court or court of appeal, all of which remain on appeal.

Canada

Three individual smoking and health cases have been filed in Canada. Of these, two (Battaglia and Landry) have been in abeyance since 2004 and 2003 respectively. The third (Spasic) is active and currently at a preliminary stage. One smoking and health case (Stright) has been filed in Nova Scotia but has been in abeyance since 2005.

Contingent liabilities cont...

Chile

On 16 December 2008, the Civil Court of Santiago dismissed an individual smoking and health action filed by Mr Andres Javier Rada Meza against Compania Chilena de Tabacos S.A. (Chiletabacos) and other tobacco manufacturers in 2006. Plaintiff can challenge this decision before the Court of Appeal with ten days of being notified of the decision. In addition to Rada, there are eight smoking and health claims pending against Chiletabacos that have not been decided yet.

Finland

On 10 October 2008, following a consolidated trial, the Helsinki District Court dismissed three individual smoking and health actions that were brought against British American Tobacco Nordic Oy (BAT Nordic), amongst others, and ordered each plaintiff to pay BAT Nordic costs of €125,000. In December 2008, plaintiffs appealed the District Court's decisions in their entirety but one plaintiff, Lindroos, has subsequently withdrawn her appeal. Briefing of the substantive appeals is ongoing.

Ireland

Fifteen individual smoking and health cases are ongoing in the Republic of Ireland, in which plaintiffs seek compensation for various alleged tobacco-related injuries. The Group defendants involved in these claims are PJ Carroll & Co. Ltd and Rothmans of Pall Mall (Ireland) Ltd, although both Group companies are not named in every action. One case, McCormack, was dismissed by judgment perfected on 17 July 2008 but plaintiff has filed a notice of appeal. Dismissal motions in 13 other cases are pending the decision of the Supreme Court in McCormack. The fifteenth case is currently dormant.

Italy

As of 31 December 2008, there were approximately 1,672 (2007: 3,478) individual "lights" cases in Italy pending against British American Tobacco Italia S.p.A. Almost all of the individual "lights" cases filed in Italy are pending before lower level (Justices of the Peace) courts. Because of the type of court involved, the maximum possible recovery in damages is €1,033. In 2007, 2,230 "lights" cases were filed by a single plaintiffs' counsel in the jurisdiction of Pescopagano. In 2008, all of these claims were withdrawn. As of 31 December 2008, 1,026 (2007: 950) cases (not including the Pescopagano cases) have been suspended or dismissed. There are 38 (2007: 33) individual smoking and health cases pending before Italian Civil Courts, in which it is contended that the smokers' diseases or deaths were caused by cigarette smoking. There are three (2007: two) labour cases for alleged occupational exposure.

Netherlands

On 17 December 2008, the District Court of Amsterdam dismissed an individual smoking and health action filed in June 2005 by Peter Josef Romer against British American Tobacco The Netherlands B.V. and British American Tobacco Manufacturing B.V. Plaintiff has until 18 March 2009 to appeal the dismissal.

(d) Consumer protection litigation

Russia

On 8 September 2008, a consumer fraud action was filed in the Savelovsky District Court of Moscow by the Ministry of Health and Social Development in Russia against OJSC British American Tobacco - Yava (Yava) and its retail distributor, CJSC International Tobacco Marketing Services. The claim seeks a declaration from the court that the use of the words "light, superlight, and 1mg light" on cigarette packets of Yava's low tar cigarettes are misleading and unlawful, and further seeks the removal of these descriptors. In November 2008, the action was dismissed for lack of jurisdiction, but the dismissal was reversed on appeal. Grounds are awaited to determine whether a further appeal can be launched. In the meantime, the case file has been returned to the court of first instance where a hearing on the merits will be scheduled.

Contingent liabilities cont...

Other litigation outside the US

In July 2008, Imperial entered into a plea of guilty to a violation of a single count of section 240(1)(a) of the Canadian Excise Act and paid a fine of C\$200 million. Imperial thereafter obtained full immunity from further prosecution and civil proceedings from the federal and all 10 provincial governments in Canada. Imperial also entered into a 15-year civil agreement with the federal and provincial governments of Canada, under which Imperial, the federal government, the provinces and others will work together on initiatives to fight the growth of illegal tobacco products. The agreement further requires a payment of C\$50 million in 2008 and a percentage of Imperial's annual net sales revenue going forward for fifteen years up to a maximum of C\$350 million.

Conclusion

While it is impossible to be certain of the outcome of any particular case or of the amount of any possible adverse verdict, the Group believes that the defences of the Group's companies to all these various claims are meritorious on both the law and the facts, and a vigorous defence is being made everywhere. If an adverse judgment is entered against any of the Group's companies, an appeal will be made. Such appeals could require the appellants to post appeal bonds or substitute security in amounts which could in some cases equal or exceed the amount of the judgment. In any event, with regard to US litigation, the Group has the benefit of the RJRT Indemnification. At least in the aggregate, and despite the quality of defences available to the Group, it is not impossible that the Group's results of operations or cash flows in particular quarterly or annual periods could be materially affected by the final outcome of any particular litigation.

Having regard to all these matters, the Group (i) does not consider it appropriate to make any provision in respect of any pending litigation and (ii) does not believe that the ultimate outcome of this litigation will significantly impair the Group's financial condition.

Guarantees

Performance guarantees given to third parties in respect of Group companies were £1 million (2007: £1 million).

SHARE BUY-BACK PROGRAMME

The Group initiated an on-market share buy-back programme at the end of February 2003. During the year to 31 December 2008, 22 million shares were bought at a cost of £400 million (31 December 2007: 45 million shares at a cost of £750 million), bringing the total of the above buy-back programme to 313 million shares, at a cost of £3,342 million.

RELATED PARTY DISCLOSURES

The Group's related party transactions and relationships for 2007 were disclosed in the British American Tobacco Annual Report and Accounts for the year ended 31 December 2007. During 2008, there were no material changes in related parties or related party transactions, other than in relation to the ST Group (see page 24), Reynolds American Inc. (see page 33) and in respect of the shareholding by R&R Holdings S.A. in the ordinary shares of the Group. In November 2008, the controlling companies of R&R Holdings S.A., Compagnie Financière Richemont SA and Remgro Limited, distributed the 30 per cent interest in the shares of British American Tobacco that they indirectly held, to their shareholders. A new subsidiary company of Richemont, Reinet Investments S.C.A., now owns around 4 per cent of the Company's shares, while the rest are owned by non-related individuals and institutions.

ANNUAL REPORT

The financial information in this preliminary announcement does not constitute statutory accounts within the meaning of section 240 of the Companies Act 1985 (as amended).

The figures contained herein have been extracted from the Group's Annual Report, including the audited financial statements for the year ended 31 December 2008, which will be delivered to the Registrar of Companies. The Annual Report and Accounts for the year ended 31 December 2007 have been delivered to the Registrar of Companies. The auditors' report on both these sets of financial statements were unqualified and did not contain a statement under section 237(2) or section 237(3) of the Companies Act 1985.

The Annual Report will be published on bat.com at the end of March 2009. At that time, a printed copy will be mailed to shareholders on the UK main register who have elected to receive it. Otherwise, such shareholders will be notified that the Annual Report is available on the website and will, at the time of that notification, receive a Performance Summary (which sets out an overview of the Group's performance, headline facts and figures and key dates in the Company's financial calendar) together with a Proxy Form and Notice of Annual General Meeting. Specific local mailing and/or notification requirements will apply to shareholders on the South African branch register.

FINANCIAL CALENDAR 2009

30 April Annual General Meeting
The Mermaid Conference & Events Centre
London
EC4V 3DB

6 May Interim Management Statement

30 July Interim Results

28 October Interim Management Statement

CALENDAR FOR THE FINAL DIVIDEND 2008

2009

26 February Dividend announced (including amount of dividend per share in both sterling and rand; applicable exchange rate and conversion date)

6 March Last Day to Trade (JSE)

9 March to
13 March No transfers between UK main register and South African branch register; no shares may be dematerialised or rematerialised.

9 March Ex-dividend date (JSE)

11 March Ex-dividend date (LSE)

13 March Record date (LSE and JSE)

6 May Payment date (sterling and rand)

LISTINGS AND SHAREHOLDER SERVICES

Primary listing

London Stock Exchange (Share Code: BATS; ISIN: GB0002875804)

Computershare Investor Services PLC
The Pavilions, Bridgwater Road, Bristol BS99 6ZZ, UK
tel: 0800 408 0094 (UK); +44 870 889 3159 (overseas)
e mail: web.queries@computershare.co.uk

Secondary listing

(since 28 October 2008) – JSE (Share Code: BTI)
Shares are traded in electronic form only and transactions settled electronically through Strate

Computershare Investor Services (Pty) Ltd
PO Box 61051, Marshalltown 2107, South Africa
tel: 0861 100 925 (SA); +27 11 870 8222 (overseas)
email: web.queries@computershare.co.za

DISCLAIMERS

This announcement does not constitute an invitation to underwrite, subscribe for, or otherwise acquire or dispose of any British American Tobacco p.l.c. shares or other securities.

This announcement contains certain forward looking statements which are subject to risk factors associated with, among other things, the economic and business circumstances occurring from time to time in the countries and markets in which the Group operates. It is believed that the expectations reflected in this announcement are reasonable but they may be affected by a wide range of variables which could cause actual results to differ materially from those currently anticipated.

Past performance is no guide to future performance and persons needing advice should consult an independent financial adviser.

Copies of this announcement may be obtained during normal business hours from the Company's Registered Office at Globe House, 4 Temple Place, London, WC2R 2PG and from our website www.bat.com

Nicola Snook
Secretary
25 February 2009