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Good morning everyone, I'm Jack Bowles, Chief Executive of BAT and I am here with Tadeu Marrocco, our Group Finance Director. We are very happy to be with you, albeit virtually for our 2020 Preliminary Results Presentation.

I hope everybody listening this morning and your families and friends are well.

Today, I am excited to update you on the progress we have made in 2020 on our journey towards a better tomorrow. Tadeu will then share more details on our performance and the 2021 outlook, before I return with more colour on our strategy moving forwards.

We are absolutely committed to transforming BAT. In 2020 we defined our corporate purpose, to Build a Better Tomorrow, which is central to everything we do. We have a clear vision to transform and grow, changing not just our portfolio, but our structures and culture. And it will fundamentally change the nature of our relationship with society. We are transforming into a high growth, multicare category FMCG business, with a reduced risk to public health, driven by evolving consumer needs.

We have already started this transformation and today we want to show you the progress we have already made, with 10% of our revenue now in Non-Combustible products, we are on track and excited by the momentum. And we have clear targets going forward.

We made excellent progress in 2020, with accelerating consumer acquisition and volume growth across all three New Categories. We have generated great momentum and we are growing share in all three New Categories as we exceed the year.

We took the opportunity to continue to invest a further £430m in the New Categories and delivered 100bps of margin expansion. This was fuelled by our continued strong performance in Combustible and £660m of cost savings.

We generated cash, free cash flow of £7.3bn, driven by operating cash flow conversion of 103%, well ahead of our 90% target.

We are proud to have delivered revenue, profit and EPS growth and strong cash flow in challenging circumstances.

While we have further to go, our transformation is well underway. We have a clear responsibility to transform our business and lead the category? Why? Because we are the largest and also the only true global tobacco and nicotine company worldwide. And we are taking this responsibility seriously.

We have strong points of difference and we are uniquely positioned, because we are the only truly international company, present in over 180 markets, including the US, which represents 40% of the global industry value. And also creates trends across our multicare category.
We are the only consumer centric, multicategory company, with the global scale to leverage our insights on consumer satisfaction and taste preferences. We are the only company present in all four New Categories, from tobacco to nicotine and beyond.

Finally, we are the only company building strong, unique, and recognised brands of the future, specifically positioned in each category.

All of this is underpinned by the quality and diversity of our people, who embrace our corporate ethos, our passion for change and speed, our transformation is already underway.

In 2020 we accelerated Non-Combustible consumer acquisition, adding another three million consumers to reach 13.5 million, with growth in every category. We added 1.1 million consumers in Q4, with sequential acceleration through the year, as our growth doubled through the second half.

Our continued investment generated tangible results and we remain very confident in achieving our 50 million target by 2030.

We have strong global brands across all three New Categories. Vuse is well on the way to global leadership and was the fastest growing Vapour brand in 2020, reaching 26% value share across our top five markets.

Glo Hyper has closed the satisfaction gap with peers, with total nicotine volume share reaching the latest February weekly share of 6.3% in Japan, this is up 100bps since August, driven by the growth of our first to world induction heating product. Although revenues were impacted by the Sens withdrawal.

THP consumable sticks volume was up 29% and across our top nine markets glo now achieves a 15% category share.

In Modern Oral, we delivered excellent growth with the volume up 62%. We consolidated our Modern Oral leadership internationally. And our US portfolio was strengthened by the acquisition of Dryft in September, with share in the US back to sequential growth in December, reaching 11% in January. We have made excellent progress, particularly in the second half.

We enter 2021 with strong volume and share momentum and a pipeline of exciting innovation. And we have further to go with the huge opportunity ahead of us to accelerate across all three categories.

Vuse and glo, with the introduction of Hyper saw strong and clear volume acceleration in H2. And Velo with the acquisition of Dryft at the end of the year is expected to accelerate this momentum in 2021.

Turning now to numbers, reported results benefited from the impact of one offs in the prior year. To better understand the key drivers of our performance we
will focus on constant currency adjusted results unless otherwise stated. And you will hear in more detail from Tadeu in a moment.

Our results show that we are delivering today, with the continued strong performance in Combustible. We gained 20bps of corporate value share in Combustible. Driven by our strategic brands, which moved 40bps, with continued strong price mix and volume ahead of the industry, demonstrating our strength and the strength of our Combustible business.

Driving growth in revenue, profit, EPS, and cash in a challenging environment. Allowing us to pay dividends of £4.7bn and to continue to de-lever the balance sheet.

I am proud of our response of our people and the teams around the world to the global pandemic. It is their resilience and agility which has delivered this result. It has already brought out the best in BAT, allowing us to build on and accelerate our new capabilities.

We have simplified the organisation, reducing management by 20%, further enhancing operational agility through Quantum. Our rapid response in our supply chain ensured no Combustible out of stock and we accelerated our transformation through new ways of working. Pivoting our business to faster grow digital platforms.

With ESG front and centre in everything that we do, we supported our employees, suppliers, farmers, and the broader community with a wide range of programmes, both financial and practical. And our COVID vaccine candidate entered phase 1 clinical trials in December. Our people have gone above and beyond, ensuring that our business performed strongly throughout the crisis and will exit even stronger.

Now over to Tadeu, who will talk you through the details of the results.

**Tadeu Marroco, Finance and Transformation Director**

Thank you, Jack. Our performance in 2020 is a great example of the journey BAT is on. We are transforming the business with strong share gains and consumer acquisition growth, powering New Categories, as well as Combustible and cost savings funding our investments while Quantum simplifies our ways of working.

We are delivering good revenue and earnings growth in challenging circumstances and excellent cash generation, enabling us to maintain our 65% dividend pay-out commitment and further de-lever the balance sheet.

We are taking this strong momentum into 2021 and we remain confident in our financial algorithm post COVID.
In 2020 we delivered revenue growth above our revised 1 to 3% guidance range and we would have been comfortably above our 3 to 5% medium term guidance range without the impact of COVID.

Combustible is the engine growth of the business and it is in great shape and we remain global leaders in volume and revenue.

In 2020 our price mix was 7.3%, which together with the strength of our brands delivered another year of both value and volume share gains, with combustibles contributing a weighted 2.3% to Group revenue growth.

Non-Combustibles added another 1% to Group growth, with an accelerated performance in the second half. This is a number we are confident to increase in the coming years. I am very pleased with the results delivered in 2020.

We are very happy with our performance in Vapour, with the standout market share performance of Vuse. We are committed to establishing Vuse as the global leader in Vapour. We are well on the way with number one positions in four of the top five markets. Our value share in the US in 2020 has nearly doubled and we are now the leader in 15 states.

In Canada we achieve leadership while migrating the brands from Vype to Vuse. And in Europe we have further strengthened our leadership positions in the top markets. With the momentum and scale we are building we are very confident in our pathway to Vapour profitability.

Looking into 2021 with our number one device share across all these markets we expect further share gains in consumables, and we’ll be piloting new launches incorporating age verification technology in key markets in quarter two.

Earlier this year we activated our Beyond Nicotine strategy with a city test of CBD vaping products in the UK. We are excited about this opportunity and we’ll keep you updated on the progress.

With the strength of our Vuse brand we are confident we can be the global leaders in Vapour, making Vuse both a high growth and highly profitable brand.

With glo we have taken a significant step forward with our induction heating product Hyper, our best performing launch yet. We have been candid that we needed to close the satisfaction gap with peers. Hyper has done this. On key consumer attributes, it scores the same or better than the competition.

Half of glo in Japan is already in Hyper, just nine months after launched, which positions us very well for the future growth.

This transformation has been borne out by sales, with good progress across all of our key THP markets.
In the end Hyper is just one step on the journey of our ambition to have the most satisfying products and the fastest growth THP brand.

We are very excited about our future innovation pipeline and where we can take this brand.

In Modern Oral in 2020 we continued to consolidate our strong leadership position outside the US. Our success in Scandinavia and across Europe showed that we have the best international portfolio of products in Modern Oral.

Beyond Europe we see very exciting prospects for Modern Oral globally. In many emerging markets consumers are familiar with other similar oral products, with no electronic device to buy this is an attractive, affordable product for consumers.

We are already seeing encouraging results from markets including Pakistan and Bangladesh. And we will continue to invest in its roll-out.

In contrast to our success in Europe, the US is the one market where we have not performed as well as we would have liked. But this is changing. Our recent Dryft acquisition really transforms our US portfolio, expanding our product range from four SKUs with only two flavours and strengths below 6mg to 28 SKUs across a range of flavours and strengths. With a great US product and entry into the key 6mg plus segment for the first time, which accounts for two thirds of the market.

After an encouraging initial period of exclusivity with one chain we are building distribution further under the Velo brand, with the latest volume share reaching 11% in January. Overall across the New Categories and beyond we are making great progress, giving us an excellent platform to further accelerate growth in the future.

This strong momentum would not be possible without the cash flow and capabilities from our Combustible business, which is industry leading.

Our Combustible business continues to perform very well across all key metrics. Overall in 2020 we grew our revenue by 2.8% with 20bps of value share gains and we continue to take strong pricing ahead of the industry and we grew volume share. This would not be possible without an excellent brand portfolio, that spans a wide range of price points. And this is concentrated around strong strategic brands in each market.

The price environment remains strong and we have seen no acceleration in downtrading in developed markets. And with our Revenue Growth Management tool we are now able to precision targets with the strong level pricing to further enhance combustibles value.
I’m really happy with the resilience demonstrated by our Combustible business throughout the year, which has shown its ability to deliver whatever the environment.

One example has been our performance through the menthol bans in the EU and Turkey. Our Combustibles portfolio over indexed in menthol, yet we significantly grew our share of nicotine. Overall we achieved 110% retention of total nicotine consumers through the menthol bans, capitalising on our unique multicategory position, adding over 300,000 new consumers in the last six months.

Now taking a look at the regions more broadly. The regions reflect the impact of COVID, particularly in the emerging markets and global travel retail and a number of additional one-off factors. Despite this we delivered a resilience performance.

In ENA we invested strongly behind New Categories to drive 50% revenue growth, led by a doubling of THP revenue from the successful launch of Hyper. And Vuse also performed strongly, as mentioned, we grew our share of total nicotine through the menthol bans.

In APME, glo volume growth from Hyper was more than offset by the Japanese excise increase and the withdrawal of Sens, our hybrid proposition. Yet we continued to take market share across the region and in the second half of the year benefited from the gradual market recovery as lockdown restrictions eased.

The team’s strong focus on our cost base drove margin expansion, despite the tough external environment.

In AMSSA, strong growth in Vuse drove New Category revenue up almost 60%. And we responded quickly to government mandated shutdowns across the region, shifting production to available sites and avoiding out of stocks.

South Africa reopened in August, although the illicit trade remains above pre-lockdown levels, we rapidly returned to market leadership.

As we said at the half year, there was a clear differentiation between emerging markets and developed market performance. We saw a significant recovery in our emerging market volume in the second half and this has continued into 2021.

While emerging markets represent around 70% of our volume, they are 25% of revenue. Despite COVID restrictions impacting consumers’ ability to access the product in many emerging markets consumption remained resilient, although impacted by global travel retail, our developed markets remained resilient throughout the pandemic.
We expect the global industry volume to recover to a decline of around 3% in 2021.

In the US we had our most successful year to date, with strong growth across revenue, value share and profits, reflecting the strength of our brand portfolio, robust pricing, and an accelerating performance in New Categories, where revenue was up by over 80% driven by Vuse.

In Combustibles we benefited from a strong portfolio across price tiers. At the premium end we had the best performing brands. In 2020 Newport and Natural America Spirit, continued to grow revenue strongly, with Newport reaching 17% value share. At this stage we are not providing US industry volume guidance for 2021, given market uncertainties.

While the positive industry dynamics in 2020 will not necessarily benefit every year we have a strong brand portfolio with lower elasticity than the industry and a targeted approach enabled by RGM. Together this gives us confidence in our ability to deliver sustainable value growth and profitability going forwards in the US.

Moving on to operating margin, we delivered a 100bps increase, reaching an overall margin of over 44%. And invested an incremental £430m to drive our growth in New Categories whilst absorbing one off costs related to COVID. This was funded by our strong value growth in Combustibles and £660m of savings driven by Quantum.

We expect to further increase our investment in New Categories in 2021 with spend weighted towards the first half. We also expect the drag from New Categories on operating margin to reduce for the full year as revenue growth offsets the additional investment.

Simplifying the business our third operational priority is driven by Quantum. We are releasing funds and creating a stronger, simpler, faster organisation. We are on track to generate at least £1bn of savings by 2022.

In 2020 we realised £660m total savings, these savings do not include any net efficiencies related to COVID. We have created a more agile, empowered, and fast organisation, we have reduced management layers and we have clear accountabilities. For example, our development pipeline has reduced from 24 months to 12 months and our speed to market deployment has improved by 40%.

We delivered robust EPS growth of 5.5% in constant currency, meeting our guidance for 2020. We could have easily delivered on our high single figure medium term guidance, had we not continued to invest behind the new categories. But this would not have been the right thing to do for the business.

Income from associates, mainly ITC was down, reflecting the impact of COVID, particularly in the second half.
Our underlying tax rate was lower at 24.9%. We expect a similar underlying rate in 2021 of around 25%.

One of the highlights of our 2020 performance was our excellent cash generation. We delivered operating cash flow conversion of 103%, well ahead of our medium-term target of over 90%. Driving our free cash flow of £7.3bn, this funded £4.7bn in dividends to shareholders, the largest payment in the FTSE.

We deleveraged the balance sheet by 0.2 times at current and 0.3 times at constant rates, with adjusted net debt falling £2.2bn at both current and constant rates, we remain confident in our target to reduce adjusted net debt to adjusted EBITDA to around three times by the end of 2021.

As mentioned, cash conversion in the period was strong at 103%. During 2020 we further strengthened our liquidity position through bond issues, including a liability management transaction, repurchasing, and redeeming debt that would have otherwise matured in 2021 and 2022, signing short term bilateral facilities and renegotiating our revolving credit facility, extending its maturity, and removing the financial covenants.

Our maturity profile improved and remains very manageable with maximum annual debt maturity moving forward no higher than £4bn, with an average maturity approaching ten years and close currency matching.

One of my priorities is maximising cash generation to fuel our transformation. We expect to generate cumulative free cash flow of around £40bn over the next five years. To drive this we expect at least 90% operating cash conversion and good profit growth, and this will be supported by Quantum savings.

In 2021 we expect gross capex of £700m broadly in line with adjusted depreciation and amortisation.

Looking forwards we remain committed to our capital allocation priorities, with a 65% dividend pay-out ratio, investing in New Categories and deleveraging to within our new corridor of two to three times adjusted net debt to adjusted EBITDA. We believe this is the right level of gearing for the Group, given our strong cash generation. And this will give us more flexibility in terms of capital allocation by the end of 2021.

We are carrying great momentum into 2021 and expect continued strong operational delivery, with revenue growth in the 3 to 5% constant currency range.

So we are confident, but we are not complacent. With COVID an ongoing challenge and uncertain US volume outlook and the continued COVID impact on our associates we retain our outlook for mid-single digit adjusted diluted EPS growth for 2021. With performance in the mid-single digit range dependent on the factors I just mentioned. We will update you as the year progresses.
With that I will now hand back to Jack.

Jack Bowles, Chief Executive
Thank you Tadeu. So we are growing our earnings and accelerated our transformation in 2020 through COVID.

We have genuine momentum, doubling our rate of Non-Combustible consumer acquisition in the second half, with a further acceleration in Q4 and we are generating the resources and cash flow to do this. From our focus on growing value in Combustibles, as well as the benefits of simplifying the company. We are led by the consumer, which is at the heart of our consumer centric, multicaregory model.

This leverages our well-established cost category consumer insights, deep understanding of product satisfaction, detailed market opportunities mapping, digital consumer, and RGM capability.

This has taken many years to build and every element is vital for multicaregory success, giving us a unique competitive advantage.

To further accelerate our transformation we have put in place Quest, we announced Quantum in 2019 to deliver a simpler, faster, more agile organisation. And Quest combines Quantum with four other workstreams under Tadeu and myself. And is the catalyst to build the enterprise of the future, accelerating the move from a business that used to sell cigarettes to a consumer centric multicaregory consumer product group.

What does it all mean? Our targets are clear, with the momentum in the business we are well on track to receiving £5bn revenue with New Categories by 2025 and we have mapped a clear pathway to 2025 profitability.

And through our portfolio of products in nicotine and beyond we are confident of reaching 50 Non-Combustible consumers by 2030.

We have made excellent progress in 2020 and post-COVID we are confident in returning to our medium-term guidance, with revenue growth of 3 to 5% and EPS growth in high single figures.

We are clear that by delivering in both our ESG and financial targets we will generate significant shared value for all stakeholders, including our shareholders.

We are building a better tomorrow, we have started, we are accelerating in New Categories and we are a step ahead in multicaregory capability. And while we know we have further to go we see a huge opportunity. I am proud of what the organisation delivered in 2020. And we are carrying strong momentum into 2021, combining our growth acceleration and pathway to profitability in New Categories.
This is a pivotal year in creating the enterprise of the future. We will be sharing more with you during our presentation at the CAGNY conference tomorrow, and I look forward to taking your questions at our Q&A session at 9.30am UK time.

Thank you for listening and stay well.

Q&A Conference Call

Operator
And our first question comes from the line of Nik Oliver from USB. Nik, you are now unmuted. Please go ahead.

Nik Oliver, Analyst, UBS
Good morning guys.

Jack Bowles, Chief Executive
Hi Nik, how are you?

Nik Oliver, UBS
Thank you for the questions. Morning, yeah good thank you. Just a couple from me. Just on some of the COVID-19 headwinds that you flagged for 2020, could you just share how much of that was the global travel piece, and I guess then how much of that will spill into 2021, just to help us on the EPS bridge? And then secondly, is there any guidance you can share on what is the implicit transactional headwind baked into the constant currency EPS, because I know that transactional you absorb through the organics? That would be very helpful, thank you.

Tadeu Marroco, Finance and Transformation Director
Okay, Jack you want me to pick this one up?

Jack Bowles, Chief Executive
Sure.

Tadeu Marroco, Finance and Transformation Director
Okay, Nik, on the COVID-19 on that - we said at the middle of last year that we were expected a 3% hit on the other lines. And that being better than that, basically because of the recovery of emerging markets that went better than we first thought in the second half of the year, we ended up with a 2.5% hit in 2020 of the net turnover. So half of that is global travel retail. So 1.3% of our revenue was hit by global travel retail and we are yet to see the recovery of that in 2021.

Remember that this is one of the elements of uncertainty that we had to take into consideration when we flagged the guidance for this year in particular. Because at the end of the day we can rebound from that or we can see another
situation because we had one quarter, the first quarter of last year was still positive, we were still selling. And then all of a sudden it was completely shut down from quarter two. So this is one of the elements of the uncertainty as well.

And picking up on your second point about transaction, I would like you to remember that our guidance includes transactional FX. So when we are mid-single digit there is an element of transactional FX that is incorporated in these numbers. So that’s clear - as you saw from the presentation you have an idea because we highlight that in the operating margin waterfall. But last year it was around £30m, which equates to something like 1% equivalent of operating profit. In 2021 we’ve doubled that based on current rates.

So as we stand today, we expect to have a 2% headwind in operating profit as part of transactional FX, which again is already part of our range when we say mid-single digit range, it’s part of that, okay?

**Nik Oliver, UBS**
Okay guys, that was really clear, thanks so much.

**Operator**
Our next question comes from the line of Adam Spielman, from Citi. Adam, you are now unmuted. Please go ahead.

**Jack Bowles, Chief Executive**
Hi Adam, how are you?

**Adam Spielman, Citi**
I’m fine thank you. Good morning to you. I really wanted to get a little bit - sort of more understanding about the mid-single digit constant currency EPS guidance. I suppose going into this I had thought you’d had - globally you had a pretty easy comp because COVID was globally a negative in 2020. Also for the first time you’ve got reduced risk products turning to actually be a positive profit contribution, as I understand it, so there’s a swing in profitability from New Categories.

So I was just wondering if you could give me some of the elements that you think are leading to this mid-single digit guidance? Now as I said I would have thought your comp was easy and you’re beginning to see a positive swing in New Categories?

**Jack Bowles, Chief Executive**
Yeah Adam, thank you. I think that to start with we had a strong 2020 and we are very happy with that. We exited the year strong in Combustibles, strong in New Categories, nonetheless there are some uncertainties in front of us and frankly speaking we prefer to have guidance that is reasonable because there are some unknowns in here.

You still have the COVID that is going to bring some tension, especially in mature markets. You have uncertainties in the US, of course. Then you have our
associates that are like ITC, recovering slowly in terms of the COVID, that has been quite brutal in India - that has an impact.

So I think that we prefer to be reasonable in terms of the guidance. And then it's going to be from the top and the bottom of the guidance and we will update you as we go along across the year. Tadeu?

Tadeu Marroco, Finance and Transformation Director
Yeah, I think that you're absolutely right. We are very, very happy with the performance that we had at the beginning of 2020, we had good momentum into 2021.

You are right Adam; we expect to start reducing our P&L losses in New Categories. But we cannot ignore that the problem of the pandemic is still out there. So we expect it to be better, around a decline of 3%, most of which will probably be recovered from the emerging markets. So there will be some elements of geographic mix there that we have to take into consideration.

We are lapping strong US markets in 2020 and as you saw we haven't provided any outlook for the US market, given that is still too unclear, we're yet to see how the market develops post-COVID, that is the reason why we haven't provided the guidance.

We spoke about GTR, which still has some uncertainty there. Jack, rightly alluded to ITC, as the end of the day, we report ITC with a one quarter lag, and this means that our kickers for 2021 can be also low as it was in 2020.

So when you consider all of that we decided to take a more prudent view around mid-single digit and as we go along, we'll be updating the market.

Jack Bowles, Chief Executive
And you know Adam, we will reduce our losses in New Categories, we will be around 3 in terms of net debt to EBITDA. We will deliver in terms of Combustible. We will continue to accelerate in New Categories. And we'll simplify the company with Quantum and now the addition of Quest.

So I think that it's a pivotal year, 2021, and I want to have the possibility to invest and to make sure that we deliver on our guidance, but also that we continue to transform the company and accelerate in the great momentum that we have in New Categories, across the three categories and also beyond.

Adam Spielman, Cti
Can I ask just a couple of follow ups, and I think the answer - just talking about the guidance I think one way of saying the answer and I just want to check I've got this right. It's very clear there's more uncertainty in 2021 than pretty much any year you've seen before given COVID and all its multiple effects and because of that perhaps you've been a little bit more conservative than in previous years in your guidance. Is that a fair summary?

Jack Bowles, Chief Executive
I would agree with the first part of your comment, I would say more instead of conservative I would say reasonable. As I said we have good momentum, we continue to accelerate in 2020 and we will update you in the mid-year. I think it is the right way to go because we have momentum, and we want to continue to accelerate our transformation.

**Tadeu Marroco, Finance and Transformation Director**
But just to be clear Adam, if it were not for the uncertainty of COVID we would have been returning to the high single digit this year. There is nothing to prevent us from getting there, unless we - or until we get clear of this - you cannot ignore that, we are still living through this pandemic.

**Adam Spielman, Citi**
Okay, and then just turning to the New Categories.

**Jack Bowles, Chief Executive**
Yes.

**Adam Spielman, Citi**
... do you see 2021 ...

**Jack Bowles, Chief Executive**
Sorry Adam, we missed the beginning of your question.

**Adam Spielman, Citi**
So turning to New Categories, as you think about 2021 now compared with how you were thinking with 2021 let's say 12 months ago, would you say things are - you know in line with your plan, ahead of plan, in terms of revenue, but also the investment needed behind it?

**Jack Bowles, Chief Executive**
There are three sides to that. one is as we said at the beginning of 2020, we expected an acceleration in terms of the New Categories, we had a lot of launches, Hyper for instance, the launch of Modern Oral in the US with the acquisition of Dryft. There were a lot of things that had to materialise.

We saw a strong acceleration in the second half of the year, with an additional 2 million consumers - across the world 13.5 million consumers, but 2 million in the second half, and 1.1 million in the last quarter. So we had strong acceleration.

As I said earlier in the second half the three categories in terms of volume grew around 50% in volume. So we are getting where we want to be, we still have a lot of developments to be done in terms of geo expansion. Still a lot of things to be done in terms of putting our products in front of the consumers, and I think that it is a strong start, with Q4 and the beginning of the year and it will continue to accelerate greater to that.
That is what we wanted; I think that we have to sustain the investment in terms of new categories. As I said before it is more now that we have built the capabilities, it has taken us three years to get there with our multicategory consumer centric approach. We are the only one to have that and to have been present in the New Categories, the three categories and beyond. We have already started with CBD in the UK and other developments as you saw in the presentation. so I'm happy with the development.

Now we can continue to accelerate. So we are on the journey and accelerating on the journey.

Tadeu do you want to add something?

Tadeu Marroco, Finance and Transformation Director
No I think that you’ve said it all. I think that we - the plans - I think that we have addressed the major points that we had around New Categories. First, we knew about the satisfaction problem we had in THP and glo Hyper is proving we have addressed this gap and given the performance and not just in Japan, but outside of Japan which is quite exciting.

We know that we had a problem in Modern Oral in the US, which the acquisition of Dryft puts us back in the competition, in the fight, because in the end we moved from four SKUs to 28 SKUs. And we knew that we had to address the profitability that we had in Vapour. And we have made big inroads with that, we have a clear roadmap to profitability in Vapour.

And so that's the reason why we are very confident to start reducing the losses also in the P&L from 2021 onwards.

Jack Bowles, Chief Executive
So we're on a very good track for the £5bn by 2025 and we'll accelerate as we go along. So we'll go step by step. You know me, I'm more of a farmer somewhat, we do what we say, and we say what we do, and we deliver, and we'll continue to do so.

The pivotal moment is the year 2021 where we continue to invest, as Tadeu said, reduce the losses in New Categories, despite the additional investment and continue to plough forward. We have the cash, why? Because we have a very strong Combustible business. And we are migrating the consumers from Combustibles to New Categories. And there is a lot of space.

Also we are present internationally, but also in the US, and we are the only ones like that. And that gives us the possibility to continue to plough through.

In the US for instance on Vapour, we have already 15 states where we are leaders in Vapour. In Canada we took the leadership in Vapour. And we are continuing to accelerate on THP and in Modern Oral we are the leader worldwide. And now through the acquisition of the products that we did now we went from 8 to 11.1, 11.2% share and we’re just in the expansion of distribution.
As you know all these products, including e-cigarettes in the US for instance are going more and more into general trade, which means lower trade margins by far. And also the volume gives us reduction of COGs and all our innovation is not only geared at satisfaction to the consumer, but also the reduction of COGs and scale.

So I think that we are on the right path. We will continue to accelerate.

Adam Spielman, Citi  
Okay, thank you very much.

Jack Bowles, Chief Executive  
Thank you, Adam.

Operator  
Our next question comes from the line of Gaurav Jain from Barclays. Gaurav, you are now unmuted. Please go ahead.

Gaurav Jain, Barclays  
Good morning and thank you. I have three questions, so one is ...

Jack Bowles, Chief Executive  
Please can you start with one and then go to the next one and then go to the next one, I'm French, so I don't have the time to digest? Thank you.

Gaurav Jain, Barclays  
No worries Jack. First can you tell us about THP plans over the next few years, you are still in a limited number of markets, how many markets should we expect that to launch in over the next three years, is Europe going to be a big focus? I don't think you're in Germany. So how are you think of this number?

Jack Bowles, Chief Executive  
Yeah, I think that you have always to go back to what we said in terms of the way we look at the full portfolio in terms of New Categories. There are some markets where we will emphasise on one category and then reduce the investment on the other categories. Because the consumers are different from geographies, but also taxation, but also regulation.

So we will have an expanded footprint in terms of THP, but we will not put THP everywhere. We will have an expanded footprint on THP where we feel that the category has legs for the future, i.e. the current markets plus others that we determine as additional markets for THP. So it's an approach by category because we have these three categories that we can navigate.

Gaurav Jain, Barclays  
Sure thank you. The second is on the £400m charge in relation to the MSA liability that you have booked in relation to the brand that you sold to Imperial. So how should we think about this because now you have booked the charge, so how should we think about it?
Jack Bowles, Chief Executive
Tadeu, you take that one.

Tadeu Marroco, Finance and Transformation Director
Yeah, look this is an old litigation that we had which comes back to the transaction that involved Florida in the past, as you know, and I don't want to make much comment about this because the litigation is ongoing. We booked the charge because we had a request from the Florida state to pay for both the MSA related to the products that we sold to Imperial, or to Reynolds at that time, so to Imperial at the back of the transaction. So we had to book a charge and we pay, actually some of that has already been paid.

And we've made a provision based on the best estimate for the other three states that are pending. And we have a final court judgement in Delaware so I will prevent making any further comments on that, but the important thing is that it is already booked in our results. Some of that we have paid and some of it in terms of provision.

Gaurav Jain, Barclays
Sure thank you. Just the last question on the staff, look since April 2019 [audio jumps] was around 17% and there is a lot of value within that company, either through your stakes in other companies, now the NGP business is growing very fast and the cigarette company less tech like valuations whether it is Hong Kong or wherever. So is there a way for you to approach the unlocking of the value which resides within BAT?

Jack Bowles, Chief Executive
Let me tell you, I mean very clearly, you know, a few years ago when Tadeu and myself took the two jobs that we have now we were told that in terms of New Categories we were nowhere, and we had a lot to do. We have created capabilities; we have taken a position in three different categories and we are growing strongly.

So I think what is important to consider is that we have a lot of potential moving forward, because we are already three years on the journey of multicategory and we will continue to accelerate on that journey. Tadeu?

Tadeu Marroco, Finance and Transformation Director
Yeah, I think that is right, I don't have much more comments to take. The question is about exactly what Gaurav because I missed the first part of the question?

Gaurav Jain, Barclays
What I was asking is that your NGP business is growing very fast and that we see the standard on e-cigarette companies, they are trading at tech like valuations?

Jack Bowles, Chief Executive
You know the reality is there was a bubble with e-cigarettes, there was a bubble with other companies in New Categories, the reality is you have to have a very
strong foundation in terms of international footprint, you have to have the capabilities, i.e. the distribution in the 180 markets that we are in. And then you have to have the legs and the possibility and the understanding in terms of consumers in terms of regulation, in terms of pricing and in terms of distribution to be able to be there on the long run. And that's what I think we've demonstrated.

We've created the capabilities and we go forward. We are not a hey, hi there, we are there building capabilities on the long term for accelerating our transformation. We are a global consumer, multicategory company and we are the only one. And that is our point of difference and it is paying off. H2 2020 has been the testament to that. And that gives us a strong springboard for 2021 and we'll continue to grow.

I am very confident in the £5bn, I'm very confident in the 50 million consumers that we want by 2030. It's a long journey. It's not a sprint it's a marathon and we are winning the marathon, multicategories and all of the elements of the puzzle are coming together as we speak.

**Tadeu Marroco, Finance and Transformation Director**
I fully agree with Jack, I think we need to persevere, it's a question of time, we have created the right foundations, we are already seeing the benefits. It's time, that's why Jack referred to 2021 being a pivotal year, we agree with that and this will continue the progress.

**Gaurav Jain, Barclays**
Okay, thanks for that.

**Operator**
Our next question comes from the line of Richard Felton, from Goldman Sachs. Richard, you are not unmuted. Please go ahead.

**Richard Felton, Goldman Sachs**
Good morning. My first question is on NGP margins, so at your capital markets day in March last year you showed a very interesting slide with gross margins for each of your NGP categories and an indication of whether you were facing headwinds or tailwinds.

So my question is whether things have developed as you had anticipated, in particular for Vapour you called our various regions for gross margins to improve. Have you actually seen that in your FY20 numbers? That's my first question.

**Jack Bowles, Chief Executive**

Yeah, I think what's important to note is that we have improved in terms of our COGs, we have improved in terms of our distribution costs and we have improved in terms of efficiency of marketing. That's why we say that for 2021 we will not only continue to invest at the high level in New Categories, but we will start to reduce our losses in terms of New Categories.
I think that is a very important testament to the journey that we are going through in terms of financial efficiency in New Categories. Tadeu, maybe you want to add something?

**Tadeu Marroco, Finance and Transformation Director**
Yeah, just going back to the CMD and what we see today, look on the Modern Oral the margins are even higher than what we showed before. So the payback, we always said that with a payback on Modern Oral once we’ve launched in all markets is not more than 15 months. So it’s a product - there is no device, there is a very good margin, and we are very satisfied with that.

On the THP we both said there would be probably some headwinds ahead, we have seen already some governments taking excise up, which means that there will be come margin headwinds that will be facing. But overall the impact in our case that we use most of our cigarette machines adapted to our consumables I think that give us space to reduce the cost for our consumers and keep our market as attractive, if they are in cigarettes, if not more.

The only problem that we have been facing and you know that's around Vapour and the [audio jumps] industry made in 2020 it's around trade margins, because as big as you get you start having more negotiating power. So we are seeing this in front, so we have been renegotiating trade margins with some of the key accounts, the main accounts.

The other element that we are leveraging is e-commerce, we now have already 20,000 subscriptions and the subscriptions have more than double over normal buyers. And e-commerce has more than twice the standard one you sell in convenience stores. So we grew our e-commerce by more than 60% and it's doing extremely well.

And the other element that we are now introducing in Vapour and in New Categories in general is our Revenue Growth Management Tool. That is doing extremely well in Combustibles and we can now take price in some areas with no negative impact on volume. So we can be very clever in terms of elasticity across the New Categories, so we have been doing that in the UK for example with very good results.

And finally we introduced more, with the return of investments, in terms of marketing investment spend, so determine exactly the effective touchpoints behind the investment to allow us to do better resource allocation procedures.

So all in all we are progressing, for sure that when you see one particular effect is the combination of markets where you just starting and markets that are mature. But we are registering the result of all these initiatives coming through in more mature markets.

**Jack Bowles, Chief Executive**
You know what makes the difference at the end of the day is all the points that Tadeu spoke about and scale. And scale in terms of e-cigarettes were growing
in the second half 59% in terms of THP we're growing 45% and in terms of Modern Oral we're growing 56%.

So that plus all the points that Tadeu said, I mean that's why we're saying that we will reduce our losses in 2021. So that's the pathway and we'll continue to plough through.

Richard Felton, Goldman Sachs
Great thank you that's very clear. My second question is on the outlook for US cigarettes. I appreciate you haven't given any specific guidance or industry volumes. But could you maybe outline some of the scenarios you're thinking about for the US in FY21 which underpins your Group guidance for 3 to 5% constant currency growth?

And related to that are you expecting a more challenging tax environment in FY21 than you would expect in a normal year? Thank you.

Jack Bowles, Chief Executive
First of all, in terms of the US, yes, we are not giving guidance. What you have to start with is 2020, we had a very strong performance in the US, why because we have an extremely strong portfolio, we're much better in pricing than anybody else. We led pricing twice during the year and we took more pricing than the competition.

We grew volume share, and we grew value share, we didn't see any acceleration of our downtrading. So we have a very strong portfolio.

On the back of that you will have also the consequences of the COVID that will still be there in 2021. You will have also all the impact in terms of taxation, in terms of regulation. But you know already in the US you have prices that are ranging from $5 in Houston Texas, to $10 in New York. So there is a lot of space. And because we have a very strong portfolio, we will be certainly able to navigate all of this.

We don't give guidance for the US because there is uncertainty and Tadeu might elaborate a little bit about that later. But the reality is we see that our performance in the US is going to have an increase in revenue because the market will be good, but to what level these external factors will impact the business moving forward, we're very well positioned in the US market and we will be the ones that will be benefitting more.

But Tadeu, do you want to add something.

Tadeu Marrocco, Finance and Transformation Director
Yeah, I think it's important to - when you think about the US market you should bear in mind that there is a historic decline of around 3 to 4% in the markets. Now last year we had an up - the industry was up 1.5%, because there were these factors that Jack alluded to, inventories was a big factor, we noticed that retailers and wholesalers in general they increase their levels of inventories to cope with the uncertainties around lockdown throughout the pandemic.
We saw that there were more consumer moments, and these generate more, if anything that’s likely up in the US for example. We also saw that the flow back that we have seen in Vapour in the years in the over 18s, they reduce, and it actually contributes to positive momentum in the cigarette business at the back of the value crisis, and then the regulation that they are stripping out flavours, part of tobacco and menthol out of the cigarette business in January 2020.

So there are a number of factors and that’s exactly what we mean about uncertainties, because we don’t know how the pandemic will develop and hence all these elements, I was referring to will actually impact the markets in 2021. The markets will perform, the macroeconomic environment, how the Vape in particular, we saw already some uptick on Vapour from the last quarter, the last two quarters last year, whether it will continue or not.

So that’s why when we talk about our guidance we always talk about a range, we say mid-single digits. But there is a range there that would be higher or lower, it is exactly what of the elements that is part of the uncertainties that we are taking.

**Jack Bowles, Chief Executive**
What’s important is that we have a very strong portfolio in the US, both in Combustibles and in New Categories and we are ploughing forward. So what is very important to consider is that we know how to navigate all these things, but yet it’s too early, especially with the competition not giving guidance, I’m not feeling interesting in giving guidance at this stage. We’ll see more towards the half year what has developed in the US and we’ll take it from there, but the start is strong.

**Richard Felton, Goldman Sachs**
Okay thank you very much.

**Operator**
Our next question comes from the line of Alan Erskine from Credit Suisse. Alan, you are now unmuted. Please go ahead.

**Jack Bowles, Chief Executive**
Hi Alan, how are you?

**Alan Erskine, Credit Suisse**
Hey, good morning, I’m very well, I hope you’re well as well. Three questions from me, so I’ll ask them one by one.

**Jack Bowles, Chief Executive**
Thank you.

**Alan Erskine, Credit Suisse**
The first question is on heated tobacco in Japan and two parts to that, you say you exited the year with 6.3% share, could I just check how much of that, or what proportion of that is Hyper?

And then my second question is if I look ...

**Jack Bowles, Chief Executive**
Let me start with that, one if you don't mind. So the answer is 50%. And what is interesting is that we don't see a next generation of decline of the products that were there prior to the launch of Hyper. What we see is that some consumers are very happy with the super slim segment, with the super slim product that we have in the market. It plays to older consumers. And for the younger consumers now we have the glo Hyper, that complements the portfolio if you want. And it is the first to world induction heating that we launched a few months ago.

So I think that we're in a good position in a very, very competitive market where everybody throws everything in, Phillip Morris and JPI are throwing everything in, we have grown since August 100bps in terms of market share. So we had a difficulty in terms of products at the beginning of last year and now with glo Hyper we have a portfolio that resonates very well with the consumers.

We have also extended our capabilities in terms of digital and in terms of consumer activation. Digital especially during the COVID, so there was a lot of closure of shops in the first half of the year and we have accelerated strongly in the second half of the year.

As I said, you know THP in Japan we make money, we're happy about that and we'll continue to do so, it represents more than 50% of our revenue in Japan. But our Combustible business also in Japan is doing very well and we continue to have these two engines of growth in Japan.

That was for the first question.

**Alan Erskine, Credit Suisse**
I think to be fair you've covered most of my second part as well. But I was just going to say clearly it is a pivotal ...

**Jack Bowles, Chief Executive**
I'm not a mind reader but I'm trying to give complete answers.

**Alan Erskine, Credit Suisse**
It is a key battleground I guess and given the momentum that you have going into the year, would you be confident - would your ambition be to grow share of the heated tobacco category in 2021 in Japan. I'm conscious PMI have got some innovations coming. But would you aspire to grow in share '21 on '20 in Japan heated tobacco?

**Jack Bowles, Chief Executive**
Yeah, I think that our position is strong, we have momentum. I think that innovations have been launched by everybody in the course of 2019 and 2020 and now we have the right portfolio, and we'll continue to plough through.

**Alan Erskine, Credit Suisse**
Thank you, my second question, and forgive me this may be a stupid question. But my understanding of transaction issues, a large part of that was you’re buying tobacco leaf often in dollars and then selling the cigarettes in obviously the currencies of the end markets. But just looking, obviously the dollar has weakened against the euro quite materially, so maybe just for my understanding can you just very simply why the transaction headwind is greater in ’21 than in ’20?

**Jack Bowles, Chief Executive**
Well the Finance Director, Tadeu that’s for you.

**Tadeu Marroco, Finance and Transformation Director**
Well Alan, it’s basically our exposure to emerging markets. There is a massive devaluation of currencies. For example, if you go to Russia, you’re absolutely right, you have to pay your leaf in dollars. And then all of a sudden you have a massive devaluation of the rouble - your starting last year. But I think the average last year compared with the spot rate this year is a much stronger devaluation than the average.

So that’s what makes - the same happens in Brazil, the same happens. So it’s exactly the exposure more to us in the emerging markets that makes this a big hit.

**Alan Erskine, Credit Suisse**
Thank you. And then my last question is just conceptual really. I mean as we look to the journey on NGP products to break even and the profitability at some point can I just ask, which of the two categories, Vapour and Heated Tobacco do you think will go through, breakeven first?

**Jack Bowles, Chief Executive**
Well they’re all improving sequentially, which is very good. Then it will all depend on the taxation environment. We see that there is more taxation acceleration in THP at the moment, but we’ll have to see through the years.

What is most important to us is that we want to reduce our losses as of this year in terms of New Categories and then clear all to profitability.

As I said before, the scale is very important and we’re expanding dramatically because we have the right capabilities, and we have the right portfolio. We have innovation today and we’ll have innovation this year and next year coming to the market, so I think that we have a clear pathway. After that, that’s the beauty of being in multicategory.

As I said, THP has more acceleration in terms of taxation. Well, we are in three categories so we can balance our activities. And remember always that in terms
of Combustible, we have the best performing business. We’re growing share, we’re growing value share and we’re the biggest in volume.

So, I mean the fact of having all these artillery in our weaponry, if you want, gives us a very strong position. And I think that also you cannot forget the fact that we have a team in BAT across the different levels of the organisation because we have the uniqueness of being entrepreneurs at core, and because we have simplified our organisation, we’re taken out 20% of the management of the company.

And also, we have a change - I and Tadeu have changed most of the management board with new responsibilities and new people and we’ve changed 120 below. We’ve changed something around three quarters of the jobs of the different people that were there including the replacements. So we have taken a lot of people from outside.

So, I think that we have a clear path in terms of development. Tadeu?

**Tadeu Marroco, Finance and Transformation Director**

Yeah, I agree with you. I think that we cannot forget that it depends a lot in terms of the mapping that we’ll be doing in terms of expansion, in terms of consumer needs. And we have all the tools necessary to identify that.

And so at a global scale it’s always tricky to answer your questions like that because at any point in time in entering new markets and you have some mature markets, but the dynamic behind a category like Jack said, we’ll have to see how this pans out.

**Jack Bowles, Chief Executive**

We have a clear pathway for each category in terms of profitability. And we have a very clear pathway in terms of geo expansion. We said that one year ago and we continue. We’ll do what we said one year ago basically. And we are accelerating in our transformation and that makes us successful.

Now, is it to the point where we are already reaching the £5bn? The answer is no, but we are on the very strong acceleration. And that is why we’re in the situation in which we are, which is the base is extremely strong, the foundation is extremely strong. We have the right strategy. We’re expanding on that portfolio. We have the right innovations, the right capabilities and a radical cost and resources allocation. And we go very, very close to the cash and to the dividend in order to make sure that we’re able to deliver as we transform the company.

It’s a pivotal year in 2021 where the investments that we’ve made in the last three years, the momentum that we have at the end of 2020 will take us through to a next phase of the development when we start Quantum and really growing the company in a very different way going forward.

**Alan Erskine, Credit Suisse**

Super. Thanks a lot, guys.
Jack Bowles, Chief Executive
Super. Thank you.

Operator
Our next question comes from the line of John Leinster from Société Générale. John, you are now unmuted, please go ahead.

Jonathan Leinster, Société Générale
Thank you very much. And good morning.

Yeah, a few questions. I'll go one at a time as well.

Jack Bowles, Chief Executive
Thank you.

Jonathan Leinster, Société Générale
So first of all on the NGP, I mean clearly the targeting implies 25%, 30% sales growth. Is that something we should write in, is that going to be exponential or should we assume that for 2021?

Jack Bowles, Chief Executive Officer
It's a very good question. And again, I think that there is a lot of moving parts in development of New Categories. There is taxation, there is regulation, there's geographical footprint, there's consumer choices. As you saw, launched Sens because we wanted to experiment in hybrid between the kind of e-cigarettes and THP. It was not successful but yet we took a lot of learning. So the portfolio will evolve as we go along and there are lots of things that will happen.

So, I think that it's going to be a journey where I'm telling you now that we're very confident with the £5bn and we are continuing to develop our business. We will invest strongly in 2021 to continue to benefit from the acceleration that we have.

Again, I insist it's the first time that we have in a half year 2 million more consumers, and this is massive. That's 1.1 million in Q4 only, so we are in best in class. And that's great because we need to continue to do so. And because we are edged between our three categories plus beyond nicotine that we have already explored since more than a few years now and started with the pilot in terms of CBD, we'll continue to accelerate in that category also.

So it's a question of deploying all this and making sure that we make the right calls. That's why I want to have space, I want to make sure that I do the right things for the business with Tadeu and making sure that we the right resources in place.

Jonathan Leinster, Société Générale
Right, okay. Just following on from that, I mean the £5bn target for 2025, I mean clearly one of your competitors is talking half of revenues by the same period which implies a business or an NGP business sort of two to three times bigger. I mean, is £5bn ambitious enough?
Jack Bowles, Chief Executive Officer
You know as I said, I'm a farmer. We take it step by step. We have a very strong start, we're happy with that and then we'll navigate as we go along.

I think that our strategy is the right one. I'm sorry, I'm repeating myself, but I think our strategy is the right one and we'll continue to accelerate.

So they did not - that's fine, that's fine. It's for them it's fine. It's perfect, very good.

Our numbers are our numbers, and we'll continue to develop as we go along.

Jonathan Leinster, Société Générale
Okay. And just a more technical one. I mean the FDA has begun to issue sort of notices to - some of the non-PMT compliant vaping. I think in the past you've talked about a contestable space of a couple of billion dollars. Is that beginning to show or are the FDA measures as we speak still very limited in terms of US vaping?

Jack Bowles, Chief Executive Officer
The way it works in the US, you know, is that it has been slowed down a bit by the COVID. As you saw, the date was moved back a bit about nine months ago. But the reality is the market is going very clear directions.

One, it is from open system to closed system. Two, from vapour shops to general distribution. And three, from products to brands because people need to be reassured by the quality of their brands.

And we've doubled our position in the US in the last 12 months, so we'll continue to do so. I think that all our products are where they should be in the PMTA process and I call to you to believe that there is for the two years to come a contestable space of £1.5bn.

Now, how will that materialise in terms the implementation of the PMTAs? We'll have to see, that's going to be the starting element. But already the fact that they're producing a list of products that are not going through the process in the right way gives you some idea that the ball has stated to roll. But we'll have to see as we go along, you know, let the whole thing unfold.

And we still consider that there is a contestable space of £1.5bn moving forward.

Tadeu, do you want to add something?

Tadeu Marroco, Finance and Transformation Director
Yeah, look Jack, I just want a point on the £5bn. I think that's more important for sure that we are confident, we clearly have the momentum. 2020 was a very unique year and we had to face a number of headwinds as you probably have noticed from what we've disclosed.
But more important are the transformations that have already happened. They won’t change. So our footprint is our footprint. It’s unique. No other company will be comparable with each other because they are different, so we have a footprint that is different.

So if you see below the group-level, at market level, you go to Japan more than 40% of our revenue is arriving in the what we call Non-Combustible. You go to Sweden, it’s more than 60%. You go to UK, it’s 30%.

So this is happening in a number of markets. But for sure we are present in - we have a very strong footprint across the world. So I think that that’s what is important people to have their own pace. We are very confident we can deliver the £5bn, and it’s a transformation and that’s what it is in my view.

Jonathan Leinster, Société Générale
Okay. Lastly, can I ask - I mean you’ve tried the Modern Oral category in a number of - a couple of emerging markets and I was just wondering whether there’s any update on whether that had proved successful or not?

Jack Bowles, Chief Executive Officer
Yeah, it’s a very good question. The answer is yes and we’re taking learnings from there, because there are a lot of countries in emerging markets where the return of chewing these kind of products is there already.

And also, always remember, you don’t need to buy a device to go to Modern Oral. So the cost barrier is not there. And there is a lot illicit in these different markets and this is a product that will be with taxation. So it’s all beneficial to both the governments in terms of revenue, the consumers in risk reduction because they cannot accord a device, and to us because we have the geographical footprint to support that.

So, we’re taking the learnings as we speak in these different markets and we’ll continue to move forward.

I strongly believe that we have a major strength in our geographical footprint and our revenue. 75% Of our revenue globally is in developed markets, 25% of our revenue is in emerging markets, but yet on the volume side 60% of our volume is in emerging markets. So we have the distribution in all these markets that we can leverage.

Tadeu, do you want to add something?

Tadeu Marroco, Finance and Transformation Director
Yeah, I would just add it that COVID didn’t help us at all. In a year like that in those type tests we were referring to, but I think that clearly it is there. A number of those markets are stick markets so we can sell not even [audio jump] can sell sachets of Modern Oral with very few pouches. For example, four or five make it very affordable. So clearly it’s - and it’s a way that we came to democratise the journey to add reduced risk products. So we will see but we
believe that there is a potential there and it’s the right thing to do for society as well.

Jonathan Leinster, Société Generale
Okay, thank you very much.

Operator
Our next question comes from the line of Rey Wium from SGB Securities. Rey, you are now unmuted, please go ahead.

Jack Bowles, Chief Executive Officer
Hi Rey, how are you? Long-time no-see.

Rey Wium, Standard Bank Group
Hi Jack, Tadeu. No, all good. Just a couple of questions from my side as well.

I just noticed the net debt to EBITDA corridor; I think you’ve now said two to three times as opposed to the previous guidance. I think it was one and half to two and a half. So I was just curious what has led to the thinking of increasing it a bit?

And to follow on from that is you know, if you get to a net debt EBITDA of around about three times is the share buybacks maybe something on the radar screen for 2022?

Tadeu Marroco, Finance and Transformation Director
We’re just …

Jack Bowles, Chief Executive Officer
Tadeu, I’ll start off.

What's very important to me is that we go to around three, because that gives us then a straitjacket that is unleashed and then we can re-look at the way we do our capital allocation. That is going to be by the end of the year. But Tadeu?

Tadeu Marroco, Finance and Transformation Director
Yeah, look Rey, we have set this new leverage corridor for the company of three to two because this if that aligned with our private rating ambitions and our business needs as well.

We have clearly expressed in terms of priorities for capital allocation that we are committed to the dividends pay-out ratio, continue investment in the New Category space and deleverage in line with our targets.

We have a very high cash-generative company even in a difficult year like 2020 as we saw in our results, we were able to generate cash. Hence, we expect to generate around £40bn plus in terms of free cash flow, the next five years which is two thirds of the [audio jumps] of BAT to date.
So once we’ve reached this level or this corridor, we will have more flexibility to assess the areas as share buyback like you allude to if the circumstance are the right one or bear in mind, that our purpose continues to be invested in the New Categories of business and beyond nicotine space as well.

Rey Wium, Standard Bank Group
And just in terms of your industry volume guidance, I think you’re saying are roughly around about 3% lower. So now obviously, would it be far off to, given that you’ve always gained a bit of market share, to think that you may do a little bit better than that? I just want to get a bit more colour on your own specific volume number target?

Jack Bowles, Chief Executive Officer
Now, we do believe that in 2021 the emerging markets will recover a bit in terms of volume. And as you rightly say, we grow share, and we grow value share. So that’s what we said for the size of the market.

We always aim of course to do better than the market.

Rey Wium, Standard Bank Group
And maybe if I can just throw in the last one there.

Jack Bowles, Chief Executive
Sure.

Rey Wium, Standard Bank Group
Just in terms of the Canada litigation. It’s now two years basically that this stay has been in place. I mean, I know you’ve provided just an update in the release. But I mean, how much longer can we expect this to continue? I mean any sort of evidence that we can maybe get to some finality on that?

Jack Bowles, Chief Executive Officer
Yes, I think first of all it’s a legal case, so we have to be cautious in the way we speak about that. A second one, there has been some parts that has been covered in the last two years, but I think that looking at it through the lenses of legal it will take some time. And it takes a lot to tango, a lot of people to tango. And it will take some time.

So it’s known it’s taken care of, but we’ll have to be patient, I think.

Rey Wium, Standard Bank Group
Okay, excellent. Thank you so much.

Jack Bowles, Chief Executive Officer
Thank you. Have a nice day. Next question?

Operator
Our next question comes from the line of Sanath Sudarsan from Morgan Stanley. Sanath, you are now unmuted, please go ahead.
Jack Bowles, Chief Executive Officer
Hello, Sanath.

Sanath Sudarsan, Morgan Stanley
Good morning Jack. Good morning, Tadeu. I hope you’re well.

Jack Bowles, Chief Executive Officer
Yes.

Sanath Sudarsan, Morgan Stanley
Great. So a few from my side.

Starting off, I just wanted to understand what’s the kind of split we are thinking about or we should be thinking about in terms of your investment in NGP with the various promotions, what’s the score platform investment?

And you know, what I’m more keen to understand is what’s the impact you’ve seen in all the markets as you’ve kind of lifted your promotions in terms of the sales growth or consumer attention? That’s the first question.

Jack Bowles, Chief Executive Officer
Yeah, I’ll take the second part. Tadeu will take the first part. I think what we see is that the efficiency that we have in terms of converting consumers is increasing. I think that the quality of the portfolio resonates very well with the consumer. And I think that there has been a lot of places where there has been either heavy promotions done by competition like NJOY in the US where you have to the resources in order to follow and in order to make sure that you’re in the game, and we did so.

So, of course we are for value. Value, I mean growing value of the category. But we will take the actions that are necessary when necessary.

I think that the pathway is clear. We have the right platforms in three different categories, and we are accelerating.

I think that the road to profitability in terms of these three categories is clear and we’ll start to reduce our losses in 2021.

Tadeu, do you want to take the first part of the question?

Tadeu Marroco, Finance and Transformation Director
Yeah. So on the promotion side we are if you take the year 2020 - 20% of the investment was around promotions. And for sure, this is just a reminder, no these are any initiatives that we put through our turnover. So when you see our numbers, these are at net of those, let’s put it that way.

And we have a clear way to track the return of those promotions. And we have a very clear payback time in each of those markets and we track them very diligently as you can imagine.
And then, I spoke about the marketing that we have put in place, that is completely linked with consumer funnel. So we can identify exactly basing our plan to in terms of numbers of buyers, loyalty, in terms of consumers that want to generate how much we need to invest in each of their touch points, which is the other aim.

So ...

**Jack Bowles, Chief Executive Officer**
I must insist on the point that Tadeu raised which is the price promotions. The promotions are already in the NTO already in the revenue line.

**Sanath Sudarsan, Morgan Stanley**
Great, thank you very much. And the second one I want to understand is in terms of your global cigarette user pool, of course people have been staying at home probably smoking more, but you’ve had lockdowns especially in emerging markets to deal with.

But as you exit 2020 how have you seen your consumer pool evolve? Have they kind of been more sticky, remaining the same with you or you’ve seen the normal rate of decline in users which you traditionally see in emerging markets? I just want to understand your user pool, how that has kind of evolved.

We didn’t see any acceleration or reduction of the user rate of the products. What we saw more is the fact that the borders were closed as this reduced illicit in a certain number of countries. But also, consumers did not move.

For instance in Germany, a market that is historically going down by 2% or 3%, has grown by more than 4% because the Germans stayed in Germany, and Germany is a high value market. So it’s more these kinds of things that have influenced the thing, rather than consumption by consumers. No change in the patterns.

**Sanath Sudarsan, Morgan Stanley**
Right. And then the last one I would say this is probably for Tadeu. Just trying to kind of deconstruct that £40bn cumulative cash flow over the next five years, you did about £7.5bn in 2020, even though you had some payments to be made. But you have a guidance of mid-single digits 2021, high-single digits thereafter you know, but just mathematically puts you more at £45bn. Should we be thinking about cash generation differently post 2021?

**Tadeu Marroco, Finance and Transformation Director**
No, at the end it’s we are saying £40bn+ to be precise. But this is predicated in our ability to continue to raise a lot of cash out of the pot. So that conversion has been exceptionally good in 2020, with targets as you know above 90% but the reality is that we had been above 95% over the last year because the focus that we have given on the cash side.
I don’t know if you remember but we decided also to make some calls in terms of capex. We fixed our capex to levels of depreciation and they started to kick in in 2020. This is one of those explanations why our conversion has been so high. So the £40bn+ and our ability to continue to generate and convert as much as possible cash. And also in our algorithm, financial algorithm of mid-single digit and going back to high-single digit as soon as we [audio jumps].

So that’s all together. And considering all those one offs that we have here and there.

Sanath Sudarsan, Morgan Stanley
All right, thank you. Can I just ask you on the 2021 cash flow please if I may, I’m trying to just think through your deleveraging target of around three turns by 2021, I mean you have a normal deleveraging run rate of about .4 turns and given how the GB has moved versus dollar, maybe it’s a year where it’s actually beneficial to you.

So is it a more conservative guidance of around three rather than let's say more like 2.8, which should be a more normal run rate?

Tadeu Marrocco, Finance and Transformation Director
No, I don’t think so. Look, in terms of the deleverage you’re right, we have been able to deleverage at .4 the last three years. These are the year 2020 at constant, it’s all constant FX, at the 2020 - deleverage at .3, but the currency is not helping us in the past. So in 2020, it’s a good example, we managed to deleverage [audio jump] because of the headwinds that we faced which is basically the difference between 31st December year end position and throughout the year.

So if you see 2021 for sure that our net debt, it will stay as it is now for the end for the year, which is long – it’s a stretch to imagine that because there's still a year to go. For sure, the net debt will be reduced.

On the other hand [audio jump]. So you have to balance out this. So we'll have to see. It’s too early to speculate how it will be this. But our ambition is to get around three times. There was a certain stage last year an ambition to get below three times, but we’ve moved that today with the provided guidance from high to mid-single digits last year because of the earnings estimate.

So we still believe that we’re on track to get to around three times by the end of the year.

Jack Bowles, Chief Executive Officer
And you know, I mean the important point, we of course continue to pursue our approach in terms of dividend at 65%. Last year we had more than £2bn in terms of free cash to take care of this.

I think that the company is in a good situation. We'll go step by step; we'll go step by step.
Sanath Sudarsan, Morgan Stanley
Great. Thank you very much.

Operator
Our last question for today comes from the line of Gaurav Jain from Barclays. Gaurav, you're now unmuted, please go ahead.

Gaurav Jain, Barclays
Yes, thank you for taking the follow-up. And it actually follows on from that question on leverage.

So how would you calculate leverage because you know, the comments I have heard from Phillip Morris and the others is that - they saying agencies are taking a very conservative view of tabaco companies' leverage and doing all sorts of adjustments. And they are planning every repurchases at a much lower level of leverage than what - than 3x. So how should we think about how rating agencies are looking at leverage?

Tadeu Marroco, Finance and Transformation Director
You are a bit cut Gaurav. I don't know if you're [audio jump] now. But anyway, you want to know how we calculate. Look, at the end of the day ...

Gaurav Jain, Barclays
Sorry ...

Jack Bowles, Chief Executive Officer
... at the core of the question, I'm not sure I heard everything also because the line was not so good. But I think what's important is what we said is that we'll go to around three and net debt to EBITDA. Then we'll review our capital allocation. But Tadeu, from what you understood from the question, I'm sorry it was not very clear. The line was broken.

Tadeu Marroco, Finance and Transformation Director
Well the calculations were - the net debt is basically a conversion back to sterling on 31st December. It's a balance sheet conversion, rate one. So if given the fact that most of our debt is US dollar nominated if there is a strength in pounds at that point in time, we'll benefit it because it's less pounds at 31st December. So that's one element.

So if the currency stays as it is today compared with the previous year clearly, there'll be a lower net debt figure.

On the other hand they did calculate throughout with the average, the exchange rate, how much profit we translate into cash at the cumulative rate, average rates throughout the year. And this also suffers an impact. So we'll have to see how this performs throughout the year.
Remember that the correlation between FX to pounds and dollars is important for the debt but not that much for EBIT - it can also get impacted by emerging markets currencies from all that.

So and then we get to the year-end figure. Now for this, I can explain all that, the constants of FX and all that, but what matters is what is the headline number.

We don’t incorporate ITC in those numbers. So if you want to know, so our EBIT that doesn’t count with ITC despite the fact that ITC is part of our investment. But that’s basically the way we calculate.

**Gaurav Jain, Barclays**
Sure. What I was asking you, how do rating agencies do any adjustment to those numbers?

**Tadeu Marroco, Finance and Transformation Director**
Okay, now I’ve got it. Okay. Well it depends. It depends on the rating and some of them use a broad debt as opposed to net debt. Some others, they’re just for PPA. Some are, you see - so depending on the agents, but they’re slightly different from basically what we calculate.

**Gaurav Jain, Barclays**
Sure, but is there a range of how much higher is your leverage in the eyes versus the number that you have? Like is it .3 times, .4 times higher than what we are seeing?

**Tadeu Marroco, Finance and Transformation Director**
Our corridor, three to two is in line with our credit rating ambitions. We have a BBB+, and which is exactly where we want to be. We are BAA1 so 2, so we want to be BAA1. So I think that is what we want to achieve of the new corridor because this aligns our credit rating ambitions.

**Gaurav Jain, Barclays**
Okay, brilliant. Thanks a lot.

**Tadeu Marroco, Finance and Transformation Director**
Thank you very much.

**Operator**
I will now hand the call back to your host, Jack Bowles for any closing remarks.

**Jack Bowles, Chief Executive Officer**
Thank you very much.

Thank you very much for all your questions and your support during the year. I mean what’s important for me is that we deliver, we transform, and we have a strong acceleration in 2020.
We have a strong 2020 in Combustible and in NGP we really take the steps forward. We have routine volume in all three categories in the second half by around 50%.

We have 2 million more consumers in H2 alone. Dividend cash flow and deleverage we’re taking care of. Tadeu does that very well.

So 2021 is really a pivotal year. We have momentum, we have strong foundations, and we have the right multicategory strategy.

We are the only global consumer multicategory company, and we’re accelerating our transformation. That has nothing to do with stand still. We have an accelerating path, and we’ll continue to do so.

By doing so we will also reduce our loss in New Categories. We will go around three net debt to EBITDA. We will deliver on Combustibles and on value on Combustibles specifically, continue to accelerate on our momentum of New Categories.

We will simplify our busines with Quantum and now we added Quest, which is the enterprise of the future and the next step of our transformation. This is a pivotal year in 2021. We will deliver, we’ll transform, and we’ll accelerate.

So thank you very much for your questions and thank you very much for your patience. Have a nice day and stay safe. And also, I’ll remind you that tomorrow we will be at CAGNY, so some of you, or the ones that can participate and join that will be absolutely fantastic. So see you all tomorrow at the CAGNY conference, Tadeu and myself will be there doing a presentation and Q&A. thank you very much, have a nice day.

**Tadeu Marroco, Finance and Transformation Director**

Thank you.

**Operator**

Thank you for joining today’s call. You may now disconnect your handsets. Hosts however, please stay on the line and await further instructions.

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