

FINAL TRANSCRIPT

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SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

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Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen, and welcome to the Swedish Match second-quarter 2011 conference call. At this time all participants are in a listen-only mode until we conduct a question and answer session, and instructions will be given at that time. (Operator Instructions). And I would just like to remind you that today's call is being recorded.

Now I'd like to hand over to your chairperson, Emmett Harrison, the Senior Vice President of Corporate Communications. Please begin your meeting, sir, and I'll be standing by.

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Emmett Harrison - *Swedish Match AB - SVP, Corporate Communications*

Good afternoon. This is Emmett Harrison, Senior Vice President of Corporate Communications and Sustainability. Welcome to the second-quarter 2011 results telephone conference for Swedish Match. Lars Dahlgren, President Chief Executive Officer, is joined today by Joakim Tilly, Chief Financial Officer, and myself. The conference call should last about an hour and will include an overview by Lars Dahlgren and a review of the financials from Joakim Tilly. A question and answer period will follow.

A shortened version of our investor kit accompanies this presentation via webcast. And a complete investor kit is available in the Investor Relations section of our website, swedishmatch.com.

During today's telephone conference call we will discuss certain items which may constitute forward-looking statements. Because such statements deal with future events they are subject to various risks and uncertainties. Although management believes that its expectations are based on reasonable assumptions, it can give no assurance that its expectations will be achieved. Risk factors are outlined in the latest Annual Report, which is available on our website, swedishmatch.com. Swedish Match assumes no obligation to update information concerning its expectations.

This conference call is being recorded and the recording will be published on the Swedish Match website. With that, I would now like to turn the conference call over to Lars Dahlgren.

Lars Dahlgren - *Swedish Match AB - CEO*

Thank you, Emmett. For the second quarter of 2011 Swedish Match delivered strong comparable sales and profit growth in local currency terms. Our comparable operating profit for the second quarter increased to SEK829m, up from SEK793m previous year, an increase of 5%. In local currencies the increase was 13%.

The increase in operating profit in local currencies was driven by a very strong performance for Other Tobacco Products as well as a solid profit growth for Snus and Snuff. Comparable sales for the second quarter increased by 3% to SEK2.944b, up from SEK2.849b the previous year. In local currencies the increase was 11%.

The operating profit for the quarter, which includes the share of income from STG, reached SEK904m, down from SEK945m the previous year. In last year's number the business transferred to STG, this included before tax and interest, and it also includes the reverse of the depreciation and amortization on assets held for sale amounting to SEK13m, pending the transaction. Earnings per share for the quarter amounted to SEK2.94, an increase from SEK2.78 in the second quarter last year.

Scandinavian Snus sales were up by 12% in the second quarter versus last year. We are very pleased with the strong volumes on the Scandinavian market. Shipment volumes were up by 8%, the comparison being positively impacted due to trade loading and Easter effects. Still, when taking these effects into account shipment volumes in Scandinavia are estimated to have increased by 4% in the quarter and 3% year to date. Volumes increased in both Sweden and Norway. Operating profit for Snus in Scandinavia increased somewhat more than sales in percentage terms.

In Sweden, according to Nielson, our market share for Snus in value terms was 87.4% in the April-May period compared to 87.7% for the preceding two-month period. Our market share in volume terms was 85.2% compared to -- with 85.6% in the February-March period.

In Norway our share in value terms in the latest four-week period ending June 19 amounted to 72.6%, up from 72.5% in the previous period ending May 22. Kaliber, a new brand of value-priced Snus on the Swedish market, is in limited distribution since April and early indications are that its performance is in line with our expectations.



Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

In April our mini-pouches received a significant packaging improvement with the Swedish introduction of a new smaller and more discrete can with pouches arranged in a star formation. The cans have the same content as before and the star formation allows us to reduce the amount of plastic used for this product by 21%.

In Norway we launched two products, Nick & Johnny Crushed Ice and also Marlboro Snus. Both the Nick & Johnny and Marlboro products appear to be gaining consumer acceptance, with Marlboro outselling our competitor's product with the cigarette brand heritage.

In the US Snuff and Snus revenues in the second quarter were up by 11% in local currency on 16% shipment volumes versus year ago. During the last year second quarter there was an exceptionally low level of promotional shipments, while in this year second quarter the promotions were at a much higher level. In the third quarter we will be facing another difficult comparison as promotions in the third quarter last year were high.

Nielson reported the overall US Snuff market as being up by 7.3% for the year-to-date period ending June 11, with Swedish Match volume down 1.3%. Our analysis suggests that the real consumption of Swedish Match brands may have done somewhat better than that, caused by a skew in the Nielson sample. Nielson reports that the growth of our low-priced brand, Longhorn, was higher than the overall category, while we saw declines in the rest of our portfolio due to intense price competition.

In the most recent isolated four-week period ending June 11 Swedish Match market share was 11.0% according to Nielson. Market growth is continuing as the four-week market growth according to Nielson is 5.6% in June.

In Q2, profitability for our US Snuff and Snus businesses increased more than sales in local currency, despite higher investment spending to support the introduction of Swedish Snus on the US market and higher levels of promotional activity. The profit increase was driven by the strong volume development as well as discontinuation of sponsorship activities for Traditional Moist Snuff business, which were included in the first half of 2010.

In May a 7% price increase was taken. On a per-count basis this was offset by a negative mix as our lowest-priced brand, Longhorn, increased its percentage of our portfolio and promotional pricing.

Swedish Match will continue to invest on its Snus program in the US with General Snus and we're very pleased with the brand's performance. General Snus is now available in more than 1,300 stores in major cities across the country. And the store expansion is continuing as we see good rotation and sell-through in our expansion stores. General typically sells at premium price compared to our -- to other Snus offerings in the US.

In June we introduced two new varieties, Classic Blend and Nordic Mint, in a new rectangular can, each holding 15 or 10 pouches of Snus. Currently these products are in limited distribution, but during the second half of the year distribution will expand into a few thousand stores in Dallas, Chicago and Philadelphia.

We're also testing Ettan Loose and Ettan Portion Pouches in Oregon and Pennsylvania in a small number of stores. Ettan is the world's oldest brand of Snus, originating in 1822. We would expect investments in the second half of the year to be higher than in the first half for our US Snus program.

With regard to SMPM International, the joint venture company for smoke-free products, we have had a small-scale launch of original Swedish Snus in Taiwan. Late in 2010 we also began testing the General Snus concept in Canada in and around the Toronto area. The product is available in a limited number of outlets and is marketed under General brand, locally adapted and researched.

We're currently scaling up the test in Canada and are now also expanding into Alberta. We continue to see positive signs from the Canadian market. There is at least one new test launch planned in 2011 and we expect investments to increase over the second half of the year.



Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

In our Other Tobacco Products business, sales for Mass Market Cigars in local currency were up by more than 20% versus the second-quarter 2010. US Mass Market Cigar volumes increased by 42% from the second-quarter 2010. Despite difficult comparisons and machinery capacity constraints we were able to temporarily produce enough product to supply the market. Additional machinery is currently coming online.

The reason for the relatively stronger growth in volume than in sales is that we've been particularly successful with our Cigarillo, our Small Cigar assortment. During the quarter we again gained market share and we have continued good success with our FoilFresh Cigars. Our Sweet Cigars in FoilFresh packaging continued to do very well. And in the second quarter of 2011 we introduced a new variant of Sweet Cigars with a [candle] wrapper, White Owl Green Sweets. Much of the volume increase was due to White Owl Green Sweets, which has proven to be very popular.

For Chewing Tobacco our market share for the year-to-date period ending June 11 was 46.1% according to Nielson estimates. This means that Swedish Match has taken some market share in the category, but Nielson estimates the decline by 7.8%.

Shipment volumes of Swedish Match brands were down by less than 4% in the quarter versus Q2 2010. In value terms our market share is above 50%. In local currency US sales were flat, while operating profit increased versus last year second quarter, as higher prices compensated for lower volumes. Last year second quarter included a SEK10m charge of the closure of the production of Piccanell brand in Sweden. Total shipment volumes in the US declined by 9% year on year, caused by steep declines in contract manufacturing volumes.

For our Lights businesses, in the second quarter in local currency terms sales decreased by 2%, while operating profit declined by 30%. In the quarter sales and operating profit on both Lighters and Matches were below prior year. The reduction in profit was due to mix effect, higher production costs and especially negative currency effect.

As regards Scandinavian Tobacco Group, the integration process is progressing well and integration costs in the second quarter were again relatively modest. A large part of the integration costs had already been taken in the fourth-quarter 2010. Swedish Match's 49% share of STG's net profit after interest and tax amounted to SEK74m for the second quarter.

The share of net profit from STG includes charges to restructuring amounting to SEK5m before tax in the quarter. For Premium Cigars, operating profit declined somewhat in the second quarter versus the prior year, mainly as a result of the weaker US dollar against the Danish krona.

For Mass Market Cigars, operating profit grew significantly as a result of synergies. For Pipe and Fine-Cut Tobacco, excluding Lane effects, operating profit was in line with prior year. While the Pipe business did very well, contract manufacturing volumes for Fine-Cut Tobacco are well below prior year.

Total Scandinavian Tobacco Group net sales for the second quarter amounted to DKK1.301b. The second quarter included a full three months of sales of EBIT -- in EBIT from the Lane acquisition, which performed in line with acquisition plan. Excluding restructuring charges the total STG operating profit for the second quarter was DKK208m and the EBITDA was DKK287m. Excluding Lane and restructuring costs operating profit increased by 14% and EBITDA increased by 10%, compared to the estimated pro forma for the second-quarter 2010.

Now I will hand over to Joakim for some more comments on the financials.

Joakim Tilly - Swedish Match AB - CFO

Thank you, Lars. To begin with, the development of exchange rates had a negative effect on our sales and operating profit comparisons due to a strengthening of the Swedish krona versus the US dollar, the Norwegian krona, the Brazilian real and the euro compared to last year's second-quarter results.



Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

The average rate of the dollar versus the Swedish krona has declined by 15.8% year to date, from SEK7.39 in Q2 2010 to SEK6.38 in Q2 2011. The Swedish krona has also strengthened against the Norwegian krona by 7%. For the second quarter the translation effect on operating profit was a negative SEK70m. For the second quarter the total translation impact on sales was a negative SEK215m, of which SEK126m for Other Tobacco Products, SEK61m for Snus and Snuff, SEK26m for Lights and SEK2m for Other Operations.

Net finance cost for the second quarter amounted to SEK131m compared to SEK129m the previous year. The net finance cost for the first six months increased to SEK259m compared to SEK235m in the first six months of 2010. The net finance cost for 2010 includes bondholder consent fees of SEK21m related to the STG transaction. The underlying increase in the finance cost was mainly a result of the higher net debt and higher interest rates. During the period a loan repayment of SEK140m was received from STG following final transaction adjustments.

In the first half of the year Swedish Match paid dividend totaling SEK1.152b and repurchased shares net in the amount of SEK1.114b (sic - see presentation). During the first six months new bond loans of SEK133m were issued. Repayment of loans for the same period amounted to SEK497m, including repurchase of SEK141m of bond loans with shorter maturities.

As of June 30, 2011 Swedish Match had SEK9.524b of interest bearing debt, excluding retirement benefit obligations, compared to SEK9.885b at December 31, 2010. During the remainder of 2011 SEK187m of this debt falls due for repayment. As of June 30, 2011 Swedish Match had SEK1.468b in unutilized committed credit lines.

The average maturity duration of the bond portfolio is 3.8 years and the average duration of the interest binding is 3.7 years. The weighted average interest rates are on bonds issued, including derivative effects, is currently 4.92% and about 5% of the portfolio is exposed to variations in interest rates.

As of June 30, 2011 Swedish Match had SEK1.8b of cash and cash equivalents. For the first half of the year the reported tax expense amounted to SEK290m, corresponding to a tax rate of 20.1%. The reported tax rate, excluding one-time items as well as profit and loss impact from associated companies and joint ventures, was approximately 22%, which is the same as in 2010.

Some comment to the cash flow. Cash flow from operating activities for the first six months amounted to SEK1.228b compared with SEK1.116b for the same period the previous year. The main reasons for the increase in cash flow from operations in the first half of 2011 compared to the same period in 2010 are somewhat lower taxes paid, improved cash flow from changes in working capital and the timing of interest payments.

Investments in property, plant and equipment during the first six months amounted to SEK132m compared to SEK197m in the first six months of 2010, whereof, SEK25m pertained to businesses now transferred to STG.

During the first quarter Swedish Match repurchased 5.9m shares for SEK1.180b at an average price of SEK199.60 per share, following authorization from the annual general meeting held in 2010. No shares were repurchased during the second quarter. During the first quarter the Company sold 0.5m treasury shares at an average price of SEK127.10, totaling SEK67m, as a result of option holders exercising options. No options were exercised during the second quarter.

In accordance with the resolution at the annual general meeting on May 2, 2011, 18m shares held in treasury have been cancelled. The total number of registered shares in the Company after the cancellation of shares is 213m.

The net debt was SEK8.7b as per June 30. The net debt in relation to EBITDA, excluding businesses transferred to STG, share of profit in STG and other one-time items was 2.6 for the 12-month period ending June 30, 2010.

I will now turn the conference call over to Lars.



Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Lars Dahlgren - Swedish Match AB - CEO

Yes, and, operator, I think we can go ahead and open the floor to questions and answers.

QUESTIONS AND ANSWERS

Operator

Thank you, sir. (Operator Instructions). Our first question comes from the line of David Hayes. Please go ahead, announcing your company.

David Hayes - Nomura - Analyst

Afternoon, gentlemen, it's David Hayes calling from Nomura. Just first, if I can, on the Cigar business, obviously, a fantastic volume number again in the quarter, despite the compound and the capacity constraint that you mentioned. Just three things on that really. Firstly, as we've got it on the run rate of the absolute volumes it looks like for us at the second half you could be doing a similar 40% volume growth. I just wonder whether you can comment on whether that's realistic.

Just in terms of the capacity constraint, I just wonder whether you can quantify what 42% could've been if you had no capacity constraint.

And then, thirdly, just in terms of the market, can you give us an update on your market share, in particular in the Sweets category, and how that moved over the second quarter? Thanks very much.

Lars Dahlgren - Swedish Match AB - CEO

Hi, David, this is Lars. I'm starting while Emmett is looking on the market shares there. When it comes to, first of all, the capacity constraints in the second quarter, I think it's fair to say that thanks to an enormous effort by our organization done in the factories we managed to work around them. So you shouldn't factor in any big backlog there from the second quarter.

And when it comes to the second half of the year it is very clear that we have taken a lot of market share for quite a period now. So, of course, for every period when we look back, compare, let's say, July '11 versus July '10, we have a significantly higher market share. So we -- everything can happen out there on the market, but our own estimates are that we should continue to deliver strong double-digit growth throughout this year. And then let's see how it plays out.

The new machinery is online now, so we don't have any constraints going into the third quarter. And I think we have clearly more visibility in the third quarter and that should be very strong. Given the fewer number of delivery days and the strong ending last year I think the comparison will look a little bit weaker in the fourth quarter, but still look very good.

David Hayes - Nomura - Analyst

Okay. Thank you.

Emmett Harrison - Swedish Match AB - SVP, Corporate Communications

Okay. And in terms of market shares for Sweet Cigars, what I have is not the Nielson data but the CMPC data. So the numbers might differ a little bit if I had the Nielson numbers, the exact AC Nielson numbers there. But for the -- the year-to-date share for Swedish Match is about 17%; 16.9% of that segment.

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

David Hayes - Nomura - Analyst

Okay. And do you have what it was going into the quarter? I'm just trying to get a feel for the run rate that you're picking up.

Emmett Harrison - Swedish Match AB - SVP, Corporate Communications

Yes, if I -- let's see here. If I take a look at the four-week period of total Swedish Match according to Nielson, we gained about two-tenths of a point between May 14 and June 11.

David Hayes - Nomura - Analyst

Okay, perfect. Okay. Thank you very much, guys. Thank you.

Operator

Our next question comes from the line of Stellan Hellstrom. Please go ahead, your line is now open, announcing your company.

Stellan Hellstrom - Nordea - Analyst

Hi, Nordea. Yes, another question on machine-made cigars in the US. It seems from your -- the result in Other Tobacco Products that your margin was quite high and, perhaps, even for the machine-made cigars. I'm just wondering how the extra shift has affected your profitability and to what extent and what -- if that should lift profitability in the -- in the comparable number next year.

Lars Dahlgren - Swedish Match AB - CEO

It's not a major impact because, of course, these cigars on the margin they contain, relatively speaking, higher labor costs since they have to run a lot of overtime and so forth. But at the same time they are pure marginal volumes. So the underlying margin for the other tobacco product segment is really -- for the quarter is really illustrative of what that business is doing with these type of volumes. And we had a good first half of the year. We were encouraged with the Chewing Tobacco performance also for the first six months of 2011.

Stellan Hellstrom - Nordea - Analyst

All right. Speaking about the Chewing Tobacco then, your market share has been very stable for a very long time and now you seem to be gaining perhaps even more than what Nielson is showing. Is there an explanation for this?

Lars Dahlgren - Swedish Match AB - CEO

There can always be some differences between shipments and Nielson and so forth. There is some promotional phasing effects on Chewing Tobacco as well, but much less pronounced than on Chew. And we are -- it's safe to conclude that we are definitely doing better than the overall category. And it's very good to be the largest player and have the biggest brands in a declining category. And we get very good service by the trade, and they like our products, and the consumers like our products. So we like that business a lot.

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Stellan Hellstrom - *Nordea - Analyst*

All right. Also a question on your -- on the 4% growth in Scandinavian Snus volumes. Could you care to give any split here on Norway and Sweden?

Lars Dahlgren - *Swedish Match AB - CEO*

There are a lot of moving pieces. And 4% is, of course -- that's our underlying estimate for the second quarter and it's a little bit difficult to strip out Easter and so forth. But we're relatively confident on 3% volume growth year to date underlying. And that's, of course, very positive since it's a little bit stronger than the recent history. And the split is the usual one where Sweden is up a little bit and Norway is up more and then driving the overall category growth. But Sweden is up as well year to date on underlying volumes as far as we can see.

Stellan Hellstrom - *Nordea - Analyst*

Okay. But it's fair to say that this sort of improvement here comes mainly from a better performance in Sweden then, or --?

Lars Dahlgren - *Swedish Match AB - CEO*

Yes.

Stellan Hellstrom - *Nordea - Analyst*

All right. Thanks.

Operator

Our next question comes from the line of Peter Wallin. Please go ahead, announcing your company.

Peter Wallin - *Handelsbanken Capital Markets - Analyst*

Thank you, Handelsbanken. I would like to start off with a follow up on the Scandinavian Snus volumes. Considering the delivered volumes of 8% in the quarter and you're only seeing somewhat higher margins, is this some kind of promotional spending behind Kaliber in the quarter? Or why don't you get a better margin kickback from the good volumes?

Lars Dahlgren - *Swedish Match AB - CEO*

In an isolated quarter you have some fluctuations of cost versus prior year and so forth. And then you have a little bit of a -- a little bit of the price effect has been offset by negative translation on the Norwegian krona as well. But the underlying profitability is very strong in the Scandinavian Snus business and it's up also year to date more than sales, so we're very pleased with it.

And then we've had quite a bit of new product activity, as you are aware of, in terms of Kaliber. Of course, it's a low-price product, although it's absolutely no material impact on the profitability for the quarter. And then we have had new product launches in Norway and we have had a few during the spring here in Sweden as well. So we continue to invest in the business as we continue to grow it.

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Peter Wallin - *Handelsbanken Capital Markets - Analyst*

Okay. Thank you. And then I've seen in the interviews flashing in the screen in the morning about the US Mass Market Cigars, where you've said that, going forward, you will probably put more focus on increasing profits rather than improving margins. How should I interpret that? Should you be investing more in expanding your sales force?

Lars Dahlgren - *Swedish Match AB - CEO*

No, you should -- I think that was a question on what will the margin be for the full year. And, for us, we focus a lot on making sure we grow the business and the profits. And whether the margin moves up one or two points is not the main focus, as long as we can continue to drive cash flows and profitability. So it was more a way to say that I don't have a fixed margin guidance ahead of me.

Peter Wallin - *Handelsbanken Capital Markets - Analyst*

Okay. And then I have one question on the STG, where you're seeing a clear effect of your ongoing and for synergies in your Mass Market operation there. What's your view on potential cash distributions from STG to Swedish Match for the second half of 2011, considering that a major part of your synergies already seem to be coming in, in your Mass Market Cigars?

Lars Dahlgren - *Swedish Match AB - CEO*

Yes, but also some of the costs that were booked in the second quarter of 2010 -- or the fourth quarter of 2010, some of that cash flow is coming through this year and then maybe the Lane acquisition. So we'll have to wait and see on how the cash situation looks during the second half. And then when we sum up the full year we'll see. We have a -- the net debt to EBITDA of the STG Group is -- was at the time of incorporation 2.5, so this was in the middle of the range of what the financial policy stipulates.

Peter Wallin - *Handelsbanken Capital Markets - Analyst*

Okay. Well, thank you very much, that's all from me.

Unidentified Company Representative

(Inaudible).

Operator

Our next question comes from the line of Anders Hansson. Please go ahead, announcing your company.

Anders Hansson - *Danske Markets - Analyst*

Hi, Anders Hansson at Danske Markets. First of all, on STG and EBIT margins that were up, I think it was 13% in Q1 and 16% in Q2. And since we don't have that much history can you help me understand what is seasonal, what is mix changes from Lane and what is cost cutting?

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Lars Dahlgren - *Swedish Match AB - CEO*

Q2 is normally a stronger quarter than Q1, so there is a seasonal effect. And Q3 and Q4 are typically the strongest in the Cigar business. There is an element of that. And then, of course, you have the relative sizes of the different segments as well. And then we don't have a 100% analysis on the STG results, given that we have a tight reporting and we're in the middle of the summer. We have, to some degree, work with some estimates and on the commentary side there.

Anders Hansson - *Danske Markets - Analyst*

Okay. More and more [is] buying Other Tobacco Products. Can you help us in any way with the split between Mass Market and Chewing Tobacco in Q2, at least some comment? Was it a big difference between Mass Market and Chewing or rather no span?

Lars Dahlgren - *Swedish Match AB - CEO*

When it comes to operating profit it's fair to say that the Cigars are quite a bit bigger now than the Chewing Tobacco.

Anders Hansson - *Danske Markets - Analyst*

Okay. Finally, just on Scandinavian Snus, do you have a good idea on what's causing the acceleration in market growth right now, or is it just normal fluctuations?

Lars Dahlgren - *Swedish Match AB - CEO*

It's excellent products out there in the market. I still -- I think we still see a little bit of recovery from these states when there were draconian tax increases on the Swedish market. We have had pretty good trends since then; the market turn around then. And of course -- and then you have -- the continued growth in Norway is very positive.

Anders Hansson - *Danske Markets - Analyst*

Okay, thanks.

Operator

Our next question comes from the line of Robbie Aitken. Please go ahead, announcing your company.

Robbie Aitken - *RBS - Analyst*

Yes, it's Robbie Aitken from RBS. I just noticed I was right; it sounded like a launch of Marlboro Snus in Norway. I was just wondering, given the fact that it's a truly international brand, what sort of capacity there may be to launch this through the joint venture in some of the test markets, so in Canada and Taiwan and that sort of thing, where it's probably slightly more recognizable.

Lars Dahlgren - *Swedish Match AB - CEO*

Yes. It's of course recognizable in Norway as well. The joint venture can use the brands of Swedish Match and the brands of Philip Morris, so it's absolutely possible to use the Marlboro brand name in the JV markets.

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Robbie Aitken - RBS - Analyst

And I guess a bit of a follow up. Does that represent a change in thinking, given that it's usually been about traditional heritage brands in terms of launching the Swedish product overseas? I guess this marks a bit of a -- well, not necessarily reversal, but certainly a change in thinking with launching a Cigarette brand into Norway.

Lars Dahlgren - Swedish Match AB - CEO

No, it doesn't. The products that the JV has launched so far are under the General brand.

Robbie Aitken - RBS - Analyst

Right.

Lars Dahlgren - Swedish Match AB - CEO

And when it comes to Norway it's the license agreement, so it's not a JV launch. It's a Swedish Match launch. We have that brand name and there are Cigarette competitors out there with some Cigarette brands, although they have had limited traction. We wanted to see what that brand can do for us in that market.

Robbie Aitken - RBS - Analyst

Okay, thank you. Maybe the last thing is, I think you reminded us last time on the first-quarter call about the incremental spend and the joint venture. I wonder if you could just maybe update us on that.

Lars Dahlgren - Swedish Match AB - CEO

What we've said is that this whole year we are accelerating our Snus investments internationally. That goes for the US and that goes for JV markets as well, and also that they are relatively back-half heavy. So I think after the first quarter I spoke about SEK50m to SEK100m incremental investments -- marketing investments over 2010 levels for JV markets and the US combined.

For the first six months we are actually only up SEK20m, but it will be much heavier in the second half. But practically speaking, just having everything ready on time in terms of getting the fridges delivered and so forth, I have a little bit hard time to see that we'll reach all the way to SEK100m. So I think right now I'd say SEK50m to SEK80m is probably a better estimate in terms of incremental spending. But if we can do the SEK100m or even more than SEK100m, if we deem that to be the right thing, we will, of course, that. We basically do as much as we can right now, since we see the momentum.

Robbie Aitken - RBS - Analyst

Right, thanks very much, guys.

Lars Dahlgren - Swedish Match AB - CEO

Thank you.



Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Operator

Our next question comes from the line of Erik Bloomquist. Please go ahead, announcing your company.

Erik Bloomquist - *Berenberg Bank - Analyst*

Yes, hi, Erik Bloomquist from Berenberg Bank. I wanted to stay on the US for a moment. Could you update us on where you're at in terms of new retail locations as you're expanding out the General launch? And when do you expect to be at the new targeted distribution level?

Lars Dahlgren - *Swedish Match AB - CEO*

Yes. Right now we are in just below 1,400 stores with the original Swedish round-can offering, which is basically available nationally in the US. But of course there might only be one store per city and so forth if it's not a big city. And we'll continue to expand that offering throughout the year. And a rough number is that we could be in around 2,000 stores with that proposition at the end of the year.

And then we are just entering the market now, you can say. We made a very small-scale launch in restaurants and bars of a new General offering in a square can with fewer pouches in the can, so a little bit more of a Mass Market product but still priced on premium compared to the existing Snus offerings in the US.

And there we will go in more focused geographically. So it will be a more concentrated test launch, you can say, in Dallas and in Philadelphia and in Chicago. And the goal there is to be around 3,000 stores by year end. And again it's more of the practicalities that decide whether it's going to be 2,500 or 3,500 by year end.

So a rough number is that we should be -- basically, we started the year with 2,000 stores and we should be in and around 5,000 stores with General Snus in the US, in addition, of course, to the availability over the e-commerce channels.

Erik Bloomquist - *Berenberg Bank - Analyst*

Okay. I assume the new 15 pack square can has tested well, again, competitors from, say, Reynolds American and Altria. Is that -- is your expectation that that's going to go head to head against those products?

Lars Dahlgren - *Swedish Match AB - CEO*

To some extent, yes. Of course, we expect to attract existing Snus users and existing cigarette smokers, and maybe some existing dippers.

Erik Bloomquist - *Berenberg Bank - Analyst*

Okay. And then, just in terms of STG, when will we start to see the impact of the Lane acquisition in the numbers, because it doesn't appear that it's made much difference in this quarter? Is that something that we'll see more of in the second half?

Lars Dahlgren - *Swedish Match AB - CEO*

Lane has performed in line with the acquisition plan and, basically, on historic profit levels in the quarter.

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Erik Bloomquist - *Berenberg Bank - Analyst*

So it's fully in Q2?

Lars Dahlgren - *Swedish Match AB - CEO*

Yes.

Erik Bloomquist - *Berenberg Bank - Analyst*

Okay, all right. Thank you.

Lars Dahlgren - *Swedish Match AB - CEO*

Thank you.

Operator

(Operator Instructions). Our next question comes from the line of Daniel Ovin. Please go ahead, announcing your company.

Daniel Ovin - *Chevreurx - Analyst*

Yes, Daniel Ovin here from Chevreurx. I wonder about STG and the contribution we see from this associate. So SEK74m, now SEK65m last quarter, and I wonder a bit of where we are in terms of realizing the synergies. Are we already now starting to see full synergies and, if not, when do you expect this to happen?

Lars Dahlgren - *Swedish Match AB - CEO*

Yes, this is Lars again. The synergies are coming in gradually, so we don't see -- we estimate the total synergies to around EUR30m and we will not see those not even for our full-year 2012, but we will see a good part of it for the full-year 2012.

And when you look at -- compare the SEK65m in the first quarter to the SEK74m in the second quarter, what you need to account for as well is that at the beginning of the year the Company had only temporary bridge financing at extremely low variable rates. So the financial net is quite a bit more negative in the second quarter than the first quarter. That's why you get the relatively little improvement on our share income whilst there was a clear improvement in terms of the EBITDA and the EBIT from the STG Group.

Joakim Tilly - *Swedish Match AB - CFO*

I think I can add to that slightly. This is here Joakim. They have a bit in excess of DKK3b in debts and the interest rates now that they have to pay when their permanent financing is in place is a bit below 4%, so that gives you a better estimate on the financial debt of the Company.

Daniel Ovin - *Chevreurx - Analyst*

Okay, perfect, thank you very much.



Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Operator

Our next question comes from the line of Kevin Dreyer. Please go ahead, announcing your company.

Kevin Dreyer - *GAMCO Asset Management - Analyst*

Hi, there. Good afternoon, Kevin Dreyer from GAMCO Asset Management. Just wondering about the US Snuff environment. We'd obviously seen a lot of competitive activity, primarily from Altria, in recent quarters. Have you seen that continue? Has it abated at all? In their press release they said they had some net price realization in their smokeless segment.

Lars Dahlgren - *Swedish Match AB - CEO*

Yes, we definitely see it continue, I'd say, intensely as ever. It is true, of course, that for a few years in a row now we have had price increases on the markets in May, so that's a positive thing. But then a lot of it is poured back into the category in terms of temporary price reductions and then, notably, our course these premium brands and offerings or new line extensions of premium brands at value price list levels.

If you consider these line extensions of the premium brands that are list price and the value price levels as value price, the value share of the US market continues to go up and is close to 56% of the total market in the latest Nielsen period. And, if anything, that's actually an acceleration.

Kevin Dreyer - *GAMCO Asset Management - Analyst*

Okay. And also on the expansion of Snus in the US, obviously, you're going into more and more stores. This started out as a specialty shop item. Are you now going from the connoisseur consumer to more of a mainstream consumer and taking -- and where are you getting new consumers from? Are they current snuff users, are they smokers, a combination?

Lars Dahlgren - *Swedish Match AB - CEO*

It's a combination. Naturally, the more we expand -- I say if we go back to the very initial launch when we used to speak about 112 stores, those are very metropolitan and quite a few of the consumers are Scandinavian expats and so forth, and then it's gradually become more and more of a broader offering.

But I think it's fair to say that the existing consumers where we sell in close to 1,400 stores is mostly the highly involved consumers that really know what Snus is about and have read up on the Swedish experience and so forth. But when it comes to the new complement here in the fall with General in the 15 pouch, where we go a little bit more Mass but in concentrated geographies, that is more catering to those people who may not be fully converted Snus users at this point, but maybe using some competitive brands and maybe Cigarette smokers.

So we expect to attract, and we do attract. In the existing offering we definitely attract some from the dippers, but -- and some just to start with the Snus directly, because they like the product, and some former Cigarette smokers. And I think it's likely that the broader we go the more it caters to Cigarette smokers and the use of competitive brands.

Kevin Dreyer - *GAMCO Asset Management - Analyst*

Great, thank you.

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Lars Dahlgren - Swedish Match AB - CEO

Thank you.

Operator

Our next question comes from the line of Mikael Holm. Please go ahead, announcing your company.

Mikael Holm - Erik Penser - Analyst

Hello, Mikael Holm, Erik Penser. First of all, a question on the US Mass market. Could you say anything about the competitive response to your significant market share gains in the latest year?

Lars Dahlgren - Swedish Match AB - CEO

Yes, they do a lot of things. They do pre-price promotions. They try to copy the Green Sweets and they copy the FoilFresh packaging, and there is a lot of competitive activity going on, but we have very strong momentum with the consumers and the trade and we continue to improve all the time.

Mikael Holm - Erik Penser - Analyst

Okay. And also just on the Scandinavian Snuff volumes, where you are a bit more optimistic, in contrast to AC Nielsen consumption data, which actually are decelerating, why do you -- what do you believe is the difference between what you are experiencing and the AC Nielsen, the consumption data numbers?

Lars Dahlgren - Swedish Match AB - CEO

We don't know. Nielsen is suggesting a slight, slight decline on the Swedish markets. But we deliver not only our own volumes. We have full transparency of the total deliveries also for competitors, but not by competitor.

But we can see all the Snus at Swedish Match. We know the volumes of all the Snus deliveries from the Swedish Match distribution on the Swedish market. And, Snus, being a fresh product that needs to stay refrigerated and so forth, we simply think that our own numbers are more reliable, quite frankly, than what Nielsen reports as market growth.

Mikael Holm - Erik Penser - Analyst

Okay. And, lastly, do you have any update on the EU tobacco directive with regards to risk for flavored products or potential for you expanding into Europe?

Lars Dahlgren - Swedish Match AB - CEO

I think we have to wait and see, but I consider the risks for Snus to be very limited. It's more of upsides when it comes to Snus. The latest is really that the Swedish government's continuing to advocate that the ban should be lifted and they think that this is an important matter, and they're continuing their dialogue with the Health Commission on a ministry level.

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

And also that the rumors is that the publication of the proposal for the revised tobacco directive will now be postponed until 2012 instead of end of 2011, as there have been quite a lot of comments to the impact assessment done by the commission. But there is no major news, but -- because it is more of an upside than a risk.

Mikael Holm - *Erik Penser - Analyst*

Okay, thank you.

Lars Dahlgren - *Swedish Match AB - CEO*

Thank you.

Operator

Our next question comes from the line of Rogerio Fujimori. Please go ahead, announcing your company.

Rogerio Fujimori - *Credit Suisse - Analyst*

Hi, everyone. It's Rogerio here from Credit Suisse. I just have a quick question on Snuff margins, given your first-half performance. I was just wondering if you could update us on your indications for the full year, which you previously hinted to be a [doubling] line of last year. Thank you.

Emmett Harrison - *Swedish Match AB - SVP, Corporate Communications*

Rogerio, it's Emmett. We had indicated that the 2011 operating margin, the best indication would be 2010's full year operating margin as a base line, and that was around 46%. Now, currency fluctuations and mix and so forth affect that a little bit, but we still hold to that. And Lars talked about incremental spending for our Snus projects in the US. We have -- looking at adding at least one more new market with the PMI joint venture and so forth. So there is more spending going into the businesses in the second half of the year.

In the first half of the year I think the margin was around 44.5% or so. So that would imply a somewhat higher margin in the second half of the year than in the first half of the year. But because of the timing and spending you may find that some of the historical patterns we've had in terms of margin progression from quarter to quarter may be a bit different this year, maybe a bit more balanced.

Rogerio Fujimori - *Credit Suisse - Analyst*

Thank you, Emmett.

Operator

We have a follow-up question from the line of Andreas Lundberg. Please go ahead, your line is now open.

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Andreas Lundberg - ABG Sundal Collier - Analyst

Yes, thank you. It's Andreas Lundberg with ABG in Stockholm. Just a question on the Lights situation. Could you give some more color on the outlook? And given what you see now in terms of spot rate for FX and the raw material was the second quarter the worst from a margin perspective? Thank you.

Lars Dahlgren - Swedish Match AB - CEO

Of course, a lot of things have gone against us in the recent history. And right now the spot rate looks slightly better, but they keep on changing every day. But, yes, when it comes to some of the raw material prices we think that we have the worst behind us and we also see a little bit of an improved country mix going into the third quarter.

So we think that the third quarter will look better than the second quarter and, generally speaking, the second half will be a little bit better. But we may not reach up to prior-year levels for the second half, or we probably won't, but hopefully the difference should be smaller than what we've seen in the first six months.

Andreas Lundberg - ABG Sundal Collier - Analyst

Okay, thank you. I have a follow up on the Snuff margin. Have you had any positive effects from lower cost of goods sold from the fact that none of your input materials are purchased in US dollars?

Lars Dahlgren - Swedish Match AB - CEO

Yes, there is a US dollar affect on the Tobacco and a little bit of a euro effect on some of the other material. But largely I can say that we don't have any major fluctuations in our cost of goods sold per can in the Scandinavian Snus operation. This is basically a mixed bag of-- some raw materials have gone up, underlying prices, some have been offset by currency. There are productivity improvements in the production.

At the same time we produce a larger variety, and including some smaller skews than for [other] JV markets and so forth, unlike the new launch for US. So the complexity has increased a little bit, but on balance, then, we basically manage to keep the cost per can constant.

Andreas Lundberg - ABG Sundal Collier - Analyst

Okay, thank you. And a last one. What's your consumer response for the new smaller cans in Sweden?

Lars Dahlgren - Swedish Match AB - CEO

Well, we have only heard. We don't see anything in the numbers. It's a relatively small segment, but the consumer responses here is more of anecdotal in character, and also from the trade, and then it's very positive. And I've seen some bloggers also expressing their appreciation of this very slick and nice packaging, and I understand them. It looks very good.

Andreas Lundberg - ABG Sundal Collier - Analyst

Okay, thank you, Lars.

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Lars Dahlgren - *Swedish Match AB - CEO*

Thank you.

Operator

(Operator Instructions). We have a question from the line of Mathias Svensson. Please go ahead, announcing your company.

Mathias Svensson - *Keel Capital - Analyst*

Hi, Mathias Svensson, Keel Capital. I just wanted to hear if you have any longer-term goals when it comes to the Swedish Snus in the US and how quickly you will be getting there. And also how much spending you are prepared to give to go there as well.

Lars Dahlgren - *Swedish Match AB - CEO*

Nothing that we have published, but I think we are in the investment mood for a few years now, because we see this being very big potential. I think that the very long perspective is that the US is going to resemble a little bit the Scandinavian development, where there was an established tradition of oral tobacco and in Sweden and Norway the loose Snus, but then were substituted by a more modern way of consumer smoke-free tobacco.

So I wouldn't be surprised if -- long term if we start to see a little bit of decline in the Moist Snuff segment compared to the growth numbers we see now, and this is compensated for by a growth in more modern varieties, like Swedish Snus.

Mathias Svensson - *Keel Capital - Analyst*

So you think that it would be a similar size in a 10-year period?

Lars Dahlgren - *Swedish Match AB - CEO*

No, I think to get up to Swedish or Norwegian penetration in 10 years I don't think is realistic (multiple speakers).

Mathias Svensson - *Keel Capital - Analyst*

No, but I'm thinking number of cans in the US on the Moist and the Snus side.

Lars Dahlgren - *Swedish Match AB - CEO*

I hope so.

Mathias Svensson - *Keel Capital - Analyst*

Good. Thank you.

Lars Dahlgren - *Swedish Match AB - CEO*

Thank you.

Jul. 20. 2011 / 12:00PM, SWMA.ST - Q2 2011 Swedish Match AB Earnings Conference Call

Operator

We have a follow-up question from the line of David Hayes. Please go ahead, your line is now open.

David Hayes - Nomura - Analyst

Sorry, just a quick follow on that point. As I understand it you're still shipping in the Snus to the US from Sweden. Do you see at some point the need and the want to put a plant in the US, and what timeframe do you think that would be in terms of stepping that up again in terms of production? Thank you.

Lars Dahlgren - Swedish Match AB - CEO

Yes, that's our hope, that we will have to take that decision in the not too distant future. But it's -- and then, of course, we can do it -- we can send almost any finished products and so forth for some time. For the next couple of years we think that the most rational thing is to keep the production in Sweden and to ship it over, and then we'll have to see how volumes develop. But in the not too distant future we think that an investment decision in the US will be required.

David Hayes - Nomura - Analyst

Very good, thank you.

Operator

We have no further questions from the phones at this time, sir. Now I'll hand the conference back to you.

Lars Dahlgren - Swedish Match AB - CEO

Okay, thank you. Just to remind everybody that the release of our Q3 results will be on October 26. Thank you.

Operator

Ladies and gentlemen, thank you for your participation today. This concludes today's conference and you may now disconnect your lines. Thank you.

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