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SWMA.ST - Q1 2019 Swedish Match AB Earnings Call

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen, and thank you for standing by. Welcome to Swedish Match Telephone Conference, Quarter One 2019 Results Report. (Operator Instructions) I must advise you, this conference is being recorded today, 9th of May 2019.

And now, I would like to hand the conference over to your first speaker today Emmett Harrison. Please go ahead, sir.

Emmett Harrison - *Swedish Match AB (publ) - SVP of IR & Corporate Sustainability*

This is the Swedish Match first quarter 2019 telephone conference and with me today are Lars Dahlgren, our President and CEO; and Tom Hayes, our CFO. In the Investors section of our swedishmatch.com website, you will find the presentation for today's call, which is intended to be viewed in conjunction with our prepared commentary. So we encourage you to follow along with that presentation. After our prepared commentary, we will be taking questions.

During today's call, there may be certain comments that constitute forward-looking statements and are subject to risks and uncertainties. Management believes that these statements are based on reasonable assumptions, but can give no assurance that expectations will be achieved. Risk factors are outlined in the latest Interim Report and Annual Report, which are available on our website. Swedish Match assumes no obligation to update information concerning its expectations. A recording of this call will be made available on the Swedish Match website. Slide 3 of this presentation reiterates the headline bullets from our interim report released this morning and we will refer you to the report, rather than repeating them on this call.

I will now turn the conference call over to Lars, who will begin on Slide 4.

Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

Thank you, Emmet and good afternoon, everyone. Let me start off with a few summary comments from the quarter, where Swedish Match delivered a solid financial result on both reported and local currency basis. It can be noted that in addition to currency translation effects, there were a number of factors that influenced our financial performance during the quarter. Calendar effects in Scandinavia, principally resulting from the timing of Easter adversely affected volumes, sales and operating profit growth. In addition, the acquisitions of Gotlandssnus and Oliver Twist in 2018 and the implementation of a new retailer merchandising program in the U.S. also affected the comparability of reported results.



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When adjusting for these items, our underlying sales development outperformed what we reported as sales growth on a local currency basis, while underlying operating profit development was largely in line with what we reported as operating profit growth on a local currency basis. The largest contributor to our sales and operating profit growth on both the reported and local currency basis came from Snus and nicotine pouches outside of Scandinavia, predominantly ZYN in the U.S. While there were some added distribution points for ZYN in the U.S. during the quarter, the majority of the sales and operating profit growth came from further increases in average sales per store. Our first production phase in Owensboro, Kentucky is operational and running smoothly and since early April, may have begun an U.S. nationwide rollout of ZYN.

Getting to our estimated 60,000 store distribution level by year-end will take some time, but we do anticipate the rapid buildup of stores gearing Q3 and Q4. In Scandinavia, overall market growth has remained strong, with volume growth at more than 5%, led by nicotine pouches and also in Sweden for pouches, somewhat lower price premium 2 segment. Through pricing and segment mix shifts, the overall value of both the Norwegian and Swedish market continued to outpace volume growth in those markets. For Swedish Match, shipment volumes were down slightly and essentially flat when adjusting for calendar and acquisition effects, as the result of segment mix shifts and share declines in certain segments. While we have been participating in the volume growth in the rapidly growing nicotine pouch segments in Sweden and Norway, our market shares in those segments are lower than our overall share of the market. For the other tobacco products or OTP segment, the U.S. mass market cigar category remained soft in the quarter, but category volumes flat to slightly down.

The decline was particularly pronounced in the HTL segment, while the natural leaf segment continued to demonstrate growth. We had anticipated another difficult quarter on quarter comparison for cigars in Q1, owing to the shortage of available leaf for rolled leaf cigars. And while the first quarter, rolled leaf cigar shipments improved sequentially over Q4 2018 levels, and rolled leaf volumes were down a bit more than 20% compared to the first quarter of 2018. With strength for other natural cigar varieties, our overall cigar shipments in the quarter were only down by 2% versus the first quarter of 2018. Despite volume declines, sales were flat and operating profit was up largely as a result of higher average pricing.

Thomas Hayes - Swedish Match AB (publ) - Senior VP & CFO

On Slide 5, we've summarized some of the quarterly highlights of the snus and moist snuff product segment. Despite the negative impact on volumes due to the timing of the Easter, Swedish Match grew both sales and operating profit in Scandinavia, from a combination of higher pricing, the impact of the Gotlandssnus acquisition and a stronger NOK versus the SEK. In the U.S., as noted earlier, ZYN was the major growth driver. Shipment volumes in the quarter for our Snus to nicotine pouch business in the U.S. doubled compared to the prior year, driven by ZYN, which had a notable impact on our improved operating profit performance.

Our U.S. moist snuff business can experience quarterly fluctuations due to changes in promotional phasing. Following an exceptionally strong fourth quarter, U.S. moist snuff shipment volumes declined 11% versus Q1 2018, with sales and operating profit from this business declining at a more pronounced rate. There was also a change in our U.S. cost allocation methodology during the quarter for shared operating expenses for our U.S. businesses. This has impacted operating profits and EBIT margins for our snus and moist snuff and OTP segments. The change recognizes the designation of ZYN as a more established business, within our U.S. portfolio. The effect was negative for the snus and moist snuff product segments by SEK16 million and positive for the other tobacco products by the same amount.

On Slide 6, we've provided our estimates of trended total market and Swedish Match volume growth in Scandinavia, adjusted for hoarding and calendar effects, as well as Swedish Match underlying currency adjusted price mix effects by quarter. The market growth is being sourced from both Norway and Sweden, but we have noted that some of the growth has shifted somewhat from Norway to Sweden, influenced by increased purchases in the tax free and border trade channels along with e-commerce.

Our volume development relative to the overall market reflects the segment's market share challenges we face. Our underperformance to the market has been worsening in recent quarters as a result of relatively sharp increases in market segments where our share significantly under squeezed our overall category share as well as market share losses will be attractive premium 2 segment and Sweden. The price mix effects remains positive at similar levels to previous quarters, supported by the higher pricing and segment shifts.

On Slide 7 and looking specifically at Sweden, you can see that based on Nielsen measures, overall market growth remains robust. Since 2017, the retail value of the market has grown at a somewhat faster pace than market volumes. This is a result of tax and pricing changes supported by a



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stable premium segment versus the value segment, as well as growth of nicotine pouches where products are premium priced. Comparing the first quarter with both Q1 2018 and Q4 2018, our share declined in both the value and premium segments. Approximately half of the overall market share decline is due to segment mix. Our market shares for both premium loose and traditional premium 1 pouches, segments that are declining are significantly higher than our overall market share, while we are under-represented in market share in a rapidly expanding nicotine pouch segment.

While we have been successful in gaining year on year market share in this attractive segment, the segment trends continue, we need to capture a higher percentage of growth within this segment to markedly stem overall market share losses. To that end, one of our key priorities is to capture a greater share of the growth in both the nicotine pouch segment and in the growing premium 2 segments.

These are challenging and fiercely competitive segments, with all major competitors working to expand their presence. While these trends from a category perspective are encouraging, the premium 2 and nicotine pouch segments are dynamic and less reliant on traditional formats and brands. But we have historically enjoyed market share advantages. Supported by strong competitive activity in terms of product launches and in-store visibility, the nicotine pouch segment has doubled in size over the past year and now represents 2.8% of the Swedish market, according to Nielsen. We believe that nicotine pouches has an even larger share of this market, as e-commerce and certain high volume independents are not taken into account in the Nielsen figures.

Turning to Slide 8, our market share declines in Norway, based on Nielsen measures are almost exclusively attributable to the segment shifts in the overall market, with loose snus declining in importance and the nicotine pouch segment rapidly growing. Our shares are relatively stable in both the loose segment and the regular tobacco portion segment, but in the most rapidly growing sub segment, nicotine pouches our share, while growing year-on-year is far below our average market share. The nicotine pouch segment in Norway has grown dramatically over the past 2 years and now represents over 13% of the total market or nearly double the size of the entire loose segment.

Lars Dahlgren - Swedish Match AB (publ) - President & CEO

On Slide 9, you can see some of our more recent new product launches, for snus and nicotine patches in Scandinavia and in markets outside of Scandinavia. After a relatively quiet fourth quarter in terms of new product activity in Norway and Sweden, a number of launches more recently for nicotine pouches in Norway under our G4 brand and in Sweden for ZYN. We also introduced the pure white variety of Onico, which is our pouch product that delivers great taste, with neither nicotine nor tobacco. We've added a new variety to our XR series, with Goteborgs Rape Sparkling and have launched several limited editions including in addition to Jacobssons from our acquired Gotlandssnus business. Outside of Scandinavia, we are now marketing ZYN in a number of varieties, both slim and mini dry format in Czech Republic and also in Scandinavia and Denmark, where we have now established a new sales force.

Turning to moist snuff and Slide 10, for the first 3 months of the year, we established -- we estimate that the U.S. moist snuff market declined slightly. In value terms however, the market was more robust, a result of manufacturer pricing as well as some increased excise taxes. Looking at deliveries from wholesalers to retailers, the value growth of the market during the first quarter was roughly 5% compared to the prior year, while Swedish Match value growth increased at a somewhat faster pace. The pouch segment in the U.S. continues to grow as a share of the overall market and Swedish Match has been gaining share within this attractive segment. Based on our measure of distributor shipments to retail, the pouch segment grew in most parts of the U.S. and was up nearly 2% in the first quarter nationwide. Based on these same measure, Swedish Match volumes on pouch products grew by more than 10% in the quarter.

On Slide 11, the 2 charts illustrate the impressive growth of snus and nicotine pouches outside of Scandinavia. ZYN volume in the U.S. account for substantially all of this growth. U.S. shipment volumes growth achieved a new milestone in the quarter at over 6 million cans. This was more than 40% above the Q4 level and almost 3 times higher than the level in the first quarter of 2018. You will note on the graph on the right hand side of the slide that the store count has been growing at a fairly steady pace since 2016. Despite this built-in distribution, in store velocity rates measured on cans per store on a week basis have continued to increase.

More of the volume growth over the periods presented as resulted from increased velocities rather than distribution gains. And in the coming quarters, with a more rapid store distribution plan, a larger portion of volume will represent pipeline volume into new stores. While there may



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continue to be good growth in velocity rates in established stores, the growth in average velocity rates may not follow the same upward curve and the same slope as we now are experiencing. At the end of the first quarter, ZYN was available in slightly less than 15,000 stores in the U.S. And since April, availability of ZYN has been rapidly increasing and we anticipate, as I earlier said that, at the end of the year, will be in approximately 60,000 stores.

On Slide 12, we have presented our estimate of the development of total moist snuff category and moist snuff pouch segment volumes by region. The development represents first quarter distributor shipments to retail for 13-week period ending March 17, 2019 versus the comparable 13-week period in the prior year. While the moist snuff category has experienced general softness due in part to the higher pricing that I commented on, the decline in the moist snuff category volumes is even more pronounced in the Western region where we are present with ZYN.

You see a similar effect when looking more specifically at the development of the moist snuff product segment, where the western region was the only region experiencing a decline in year-on-year segment volumes in the 13-week measurement period. It should be noted that this differential in moist snuff regional growth rates may not completely be attributable to the progress we're seeing for ZYN and as ZYN consumers are not exclusively sourced from moist snuff users, but this does indeed demonstrate the exciting opportunity that ZYN can play in transforming the nicotine landscape.

Thomas Hayes - Swedish Match AB (publ) - Senior VP & CFO

Moving on to Slide 13 and our other tobacco products or OTP segment. Within OTP, cigars delivered a solid financial performance in the first quarter, where sales were flat and operating profit improved in U.S. dollars on somewhat lower volumes. The financial performance of our U.S. cigar business benefited from the chain segment methodology for shared operating expenses in the U.S., but much of the favorable performance was attributable to higher average pricing. Cigar growth continued to be constrained by leaf supplies for our rolled leaf cigar assortment. Alternative supply measures have been implemented and we should be able to increase our deliveries of rolled leaf cigars going forward.

It's worth noting that Q2 represents the most challenging quarter for year-on-year volume comparison perspective, but the comps get easier in the second half of the year and especially in Q4. In our chewing tobacco businesses, the first quarter was rather soft, with lower volumes in the U.S. and some pressure on sales and costs outside of the U.S., which are of a temporary nature largely related to the establishment of a sales office in Denmark.

On Slide 14, we have presented our estimate of overall U.S. mass market category and segment development based on distributor shipments to retail. The overall category declined slightly as continued growth in the natural leaf segments could not fully compensate for the declines in the larger HTL segment. Based on the same measure, Swedish Match grew while the market was down. Our growth resulted from our portfolio mix versus the overall category as well as market share gains within the decline in HTL segment. And when ignoring pipe tobacco cigars, which is a segment where we have a very nominal participation, natural leaf cigars comprise approximately 60% of our portfolio compared to about 40% of the category as a whole. Our underperformance relative to the market in the first quarter within the natural leaf segment is exclusively attributable to our production constraints within the rolled leaf sub segment.

Turning to U.S. chewing tobacco, on Slide 15, Swedish Match is well positioned in both the premium and value segments and based on our measure of distributor shipments to retail, we once again outperformed the category as well as both segments. While the shift in the portfolio toward more value-priced products places pressure on average selling prices and margin, on moderating rate of volume declines mitigates this development somewhat. And while shipment volumes of Swedish Match brands declined notably in the first quarter versus the prior year, shipment volumes can be volatile and it's perhaps better to look at longer periods. And for the 12-month period ended in March, volumes were down for Swedish Match brands by 4%, while price mix effect was plus 3%.

Moving on to the lights and Slide 16, reported operating profit improved by 40%. This improvement primarily reflects restructuring charges that were incurred in the first quarter of 2018. When excluding the effects of those charges, operating profits increased slightly. It was a good quarter for volumes, especially for lighters, but match volumes also good. For lighters, the market mix was favorable. For matches, price mix effects were rather weak, however, realized pricing was strong supported by the currency benefit of export sales from our Swedish based match businesses -- business priced in U.S. dollars and euros. As we have mentioned in prior quarters, we have been facing significant cost pressures on nylon, on of



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the key input materials for our lighters. This had an adverse effect on profits as raw material costs have substantially offset the benefits of stronger lighter sales.

We are now on Slide 17, and we're looking at the regulatory landscape and in mid-March, the FDA released the draft guidance document with the intent to move forward with a proposed rule to ban all flavored cigars. As a manufacturer of cigars, we are not alone in voicing our concern about the FDA's approach outlined in the draft guidance. The FDA has specified an acceleration of substantial equivalence filings for flavored cigars and a 30 day compliance period following the issuance of final guidance. The 30 day filing and review period for cigar SEs will be Herkyland in the normal course. But what makes the draft guidance even more impractical is that the FDA has not yet provided manufacturers with the SE filing requirements for cigars. The final form of the guidance and its implementation timeline remain uncertain.

As we mentioned in our conference call after the fourth quarter, the TPSAC hearing to the FDA on our MRTP application related to general snus took place on February 6. On April 12, the FDA announced the closing date for the MRTP docket, with comments needed to be submitted by May 13. Sometime after that, the FDA will make its decision on whether general snus receive the approval on its MRTP application. And while we are optimistic about the outcome of their decision, there has been no communication as to the timeline.

On Slide 18, we've summarized relevant metric from our interim report relating to finance cost, our financial position and earnings per share. Net finance costs during the quarter were in line with levels that we experienced during the past few quarters. The weighted average interest rate of our loan portfolio at March 31 was 2.24% compared to 2.18% at the end of 2018. The capital duration was 4.1 years, with 98% of the portfolio subject to fixed interest rates. And on April 3, the debt reflecting has been due in 2019 was repaid and in January of this year, we secured SEK1 billion of borrowing with -- via a private placement of 7-year tenure, with 2.73% in anticipation of this repayment. After the repayment, the weighted average interest rate of our bond portfolio was reduced to approximately 2.1%. Our net debt to EBITDA for the 12-month period ending March 31 was 2.1. As of March 31, 2019 Swedish Match had SEK13.832 billion of interest-bearing debt, which excludes retirement benefit obligation, but includes the recognition of lease obligations of SEK269 million from the adoption of the new lease accounting standard.

The EPS bridge illustrates the components of our 19% growth in adjusted EPS for the first quarter and then apart from the after-tax effect of our increased operating profit, the reduced number of shares had a positive impact. And during the first quarter, we made share repurchases in the amount of SEK449 million and on April 16, a total of SEK1.770 billion was paid out to shareholders in dividends, at SEK10.5 per share.

And finally on Slide 19, we repeat our outlook for 2019, which is unchanged from what we presented in February of this year. I will point out that our outlook statement regarding our expectations for the U.S. cigar market continues to be without any overarching consequences of what the FDA may or may not be able to implement, under its draft guidance on flavored cigars. And finally, as always, fluctuations in currency rates will affect our future-reported results, and you may want to take note of the more important average exchange rates versus the SEC. The average exchange rate in the second quarter of 2018 for the U.S. dollar was 8.66, the NOK, it was 1.08 and the Brazilian real was 2.41.

And with that operator, please open up the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from the line of Owen Bennett from Jefferies. Please go ahead.

Owen Michael Bennett - Nomura Securities Co. Ltd., Research Division - Research Analyst

Hope all are well. And couple of questions, please. First of all, just on the industry trends in Scandinavia and they continue to be very strong. I was just wondering if you could give some guidance in terms of, what you expect those volumes to be for the full year. And then secondly, on the potential regards to any legal challenge and would this delay any possible implementation around the flavored ones. Thank you.



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Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

Owen, this is Lars. I'll start with your second question, that type of question, that we don't comment on. But obviously, we have provided our comments to the draft guidance and we think that there is a lot to be commented upon in that guidance. When it comes to the industry trends, we see very encouraging trends in Scandinavia for a long time. And what's very positive when we look now is that we see new users coming in to the category, which also, it's a reflection of the more intense innovation in the category, including nicotine pouches that we included in the definition of the snus market and so, there is no -- we haven't seen anything here now that suggests that the current trends should stop. But on the other hand, predicting the future is very difficult, so we don't give any specific guidance of, what we think. As Tom pointed out, we have seen a little bit softer growth in the Norwegian market, but predominantly, that is sort of on the domestic side, while we've seen a stronger border trade in Sweden and also very high volumes in tax free channels. And in some of the tax-free channels, just to be clear are -- that cater to Norwegian citizen, they are in plain packaging and some are not depending on which jurisdictions that apply.

Operator

Your next question comes from the line of Adam Spielman from Citi. Please go ahead.

Adam Justin Spielman - *Citigroup Inc, Research Division - MD and European Tobacco and Beverage Analyst*

A couple of questions if I may. To start with you said, very clearly you need to gain more market share or more segment share within the nicotine pouch segment in both Norway and Sweden. And I was wondering what that means and also in premium 2, does it mean to say, enhance innovation or have you got any other plans or are you thinking of lower price products, but that came across very loud and clear. So that's my first question, but I do have others. Thank you.

Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

Adam, as you will understand, we're a little bit careful on what we talked about in a call like this in terms of how we intend to grow our business. And -- but I'd say it varies, this -- first of all, the competition that we're seeing in this segment that's not have to do so much with price, I would say, it's more about innovation. With that said, there are kind of temporary deals in certain channels and so for that an increasing extent also in the Swedish market, not the least in the e-com channel. But there are also distribution opportunities. It is a fact that we have been very capacity constrained and to some extent, are on especially parts of our ZYN assortment coming from the U.S. market and that has affected the pace of our initiatives also in Sweden and in other European countries. So distribution build is one clear parameter but then of course innovation is another important part. And I think just to add one comment to the first question and it's reminding me that we sit in a room here without window so, and we don't see the sun and we haven't seen much of the Sun so far in May and yes, the reminder for everybody that the summer last year was extremely warm in Scandinavia. And we do think that provided some extra growth in 2018 to the snus category. So it unfortunately looks right now in the weather forecast we have tough weather comps in (inaudible).

Adam Justin Spielman - *Citigroup Inc, Research Division - MD and European Tobacco and Beverage Analyst*

And very sort of a minor question. I see you're -- here you're expanding your nicotine pouches into Denmark. How big an opportunity do you think that is, because obviously, a lot of [danes] go cross the bridge, so they're fully familiar with Swedish culture. It's always seemed to me that the most likely place that would adopt snus in the European Union would be Denmark. Is that something you would -- I mean, how would you quantify that opportunity?



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Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

I would quantify it as relatively significant opportunity and we also do -- we do think that nicotine pouches in Europe, it's reasonable to expect that we will see a blend of chew bags and nicotine pouches in the European market and you're right about your comment on going across the bridge. And I think it's also fair to say that some products has gone, not only consumers have gone over the bridge, but some products have gone over the bridge as well before, so there seem to be a fairly strong interest in the Danish market when it comes to White type of chewing tobacco products and nicotine pouches and there is another competitor of ours who is bigger than we are at the moment.

Adam Justin Spielman - *Citigroup Inc, Research Division - MD and European Tobacco and Beverage Analyst*

Quickly turning to ZYN, can you say just at the moment, as in sort of early May, how many stores you have distribution in?

Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

In Denmark?

Adam Justin Spielman - *Citigroup Inc, Research Division - MD and European Tobacco and Beverage Analyst*

No, no, no in the U.S., sorry.

Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

Yes, we, I mean, we ended the first quarter around just shy of 15,000 stores and during April, we have basically gone into 18,000 more stores, whereas that leads to -- we got on the point of sales, the material and so forth, and then where the product physically went into all of those stores at the end of the month and not updated on, but that's the magnitude we're talking about.

Adam Justin Spielman - *Citigroup Inc, Research Division - MD and European Tobacco and Beverage Analyst*

So just to be clear, you said 18,000 more, so we're talking a total of 33,000 or have I misunderstood you?

Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

That you have correctly understood me.

Thomas Hayes - *Swedish Match AB (publ) - Senior VP & CFO*

Just Adam, one second in that. A point of clarification on the kind of prepared commentary before the Q&A, in terms of the rapid expansion in the U.S., it's Q2, Q3 and not as it was communicated Q3, Q4, I just want to make sure that's clear.

Adam Justin Spielman - *Citigroup Inc, Research Division - MD and European Tobacco and Beverage Analyst*

And then my very final -- well, 2 sort of detailed questions, if you look at the Western region alone, what sort of market share do you think you have? I'm talking about ZYN as a percentage of smokeless tobacco?



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Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

I mean we -- you saw the charts there where we compare it to -- or where we look at the moist snuff category and it's fairly clear to us that there is a meaningful impact on moist snuff category and especially and pouches. I haven't run the market share if you include snus as well, but then, if you look -- if you take it -- if you would make a market out of total moist snuff and ZYN represented a bit more than 10% of that market in the third quarter.

Adam Justin Spielman - *Citigroup Inc, Research Division - MD and European Tobacco and Beverage Analyst*

And the very final question, I'm not asking a lot. You said you did more than 6 million cans in Q1. Was there any pipeline effect in that? Not necessarily in your new stores, but perhaps to distributors, or was that entirely representative of a sellout if you like?

Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

No, that was the -- those were normal shipments to the Western region and we did not start to ship anything to distributor in anticipation of the national launch in the first quarter.

Operator

(Operator Instructions) And your next question comes from the line of Stellan Hellstrom. Please ask your question. You're calling from Nordea.

Stellan Hellström - *Nordea Markets, Research Division - Senior Analyst of Retail and Consumer Goods*

I'd like to ask you about the Swedish snus market and you lost some market share here, you say it's not a question of price really, but are we to be concerned about your ability to raise prices this year or --?

Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

I mean, if you look at Slide 6 that we included in the presentation, and we do provide a fair amount of details on the realized pricing and we don't comment there with specificity on our pricing action. And I think it's fair to say that the picture is getting increasingly complex with all these mix shifts between segments and so forth. I mean, it goes both ways in terms of, you have very good growth in nicotine pouch segment with higher pouches, you have very good growth in the premium 2 segment, which is obviously better than the value segment and much better than value segment in terms of pricing. But it's shy of the premium 1 segment. And if you look in the history, the recent history, we have seen consistently that the value of the market has outperformed volume and -- but the numbers are, I'd say basically covering inflation historically and I think it's reasonable also that you will some adjustments in 2019, to cover the increased salary cost et cetera, but after each quarter, we will continue to providing the details of the realized price mix effects.

Stellan Hellström - *Nordea Markets, Research Division - Senior Analyst of Retail and Consumer Goods*

I think last time this year, you did provided up with an update for the current year, but this time, no.

Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

Yes, it's that -- we take that after each quarter and also you can look in the Nielsen data, so you see -- if you look in the Nielsen data, you will see that in Norway, that was a price increase at the beginning of the year. And then for the Swedish market, you can follow the Nielsen data.



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Stellan Hellström - *Nordea Markets, Research Division - Senior Analyst of Retail and Consumer Goods*

Then on the ramp up of ZYN now in the coming quarters of the distribution. Is this going to be something to think about in terms of costs for you, even potentially unusually high deliveries as you fill the pipelines in Q2?

Thomas Hayes - *Swedish Match AB (publ) - Senior VP & CFO*

No, I would look at the increased cost in support of the expanded national footprint, more so as a Q2, Q3 phenomena in that -- I mean Q2 and into Q3 as we're expanding distribution, there is a fairly sizable cost in and around point of sale material, merchandisers just getting those added stores in place. Q3 would also once the product is in place, you'll probably see more of an increase in consumer marketing spend in support of just getting the product in the brand in the front of the eyes of consumers. So you should expect to see from a cost perspective, Q1 was relatively light with respect just to our Western region footprint. Q2 would be -- Q2 and Q3 would include those kind of more national distribution marketing cost and then, obviously Q4 would be less than the marketing spend way.

Stellan Hellström - *Nordea Markets, Research Division - Senior Analyst of Retail and Consumer Goods*

Also, is there anything to that can be seen in terms of competitors, their activity on the sides of obviously between pouches in the U.S.?

Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

No particular news, but I mean, you all have seen one major competitor speaking about the coming products, but we haven't seen the actual products then, we have no more information than you have on their plans.

Operator

Your next question is from the line of Karri Rinta from SHB. Please go ahead.

Karri Rinta - *Handelsbanken Capital Markets AB, Research Division - Research Analyst*

A quick question on your manufacturing capacity when it comes to ZYN. Can you give us an update on [the app] when are the sort of the next lines coming on stream during the upcoming 18 months and then, some indication of what kind of quarterly -- what is your quarterly capacity maximum at this point and is that a relevant constraint in the second quarter or more towards the, towards the end of the year?

Thomas Hayes - *Swedish Match AB (publ) - Senior VP & CFO*

Yes, and I would say one thing to keep in mind is, all of our volumes in 2018 and then even the volumes for much of the first quarter of 2019 were supported by volumes manufactured in Sweden. So we still have the capability of producing the dry ZYN product in Scandinavia in support of our efforts in the U.S. But as mentioned our initial lines, that were part of our capital approved in the middle of 2017 came online in parts and pieces from very late 2018 into the first quarter of 2019. And what we've communicated previously is that, that our first 2 investment plans for ZYN would provide production capacity equivalent to what is the U.S. category for snus. So roughly -- and we said more than 60 million cans. So, those first 2 capital projects should be the first, the first one is completed. The second one should complete itself, towards the end of the third and into the fourth quarter of this year. In February of this year, we talked about a doubling of that capacity. So slightly more than our -- more than 60 million cans to a doubling of that, that capacity will not come in line until the latter part of 2020.



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Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

And yes, a point of clarification. We are still supporting and as we build up and get that speed of the machine are up in the U.S. to its optimized levels, we are supporting and the volumes from Sweden as well. And that has put a little bit of a restriction in timing in terms of the initiatives that we can do in other markets.

Karri Rinta - *Handelsbanken Capital Markets AB, Research Division - Research Analyst*

Okay. So more specifically, could you, could you deliver 10 million cans in Q2 from a capacity standpoint?

Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

I think, we'll talk about Q2 after Q2.

Operator

(Operator Instructions) There are no further questions, please continue.

Lars Dahlgren - *Swedish Match AB (publ) - President & CEO*

Okay. Then we thank everybody for listening and asking good questions. And I'd like to inform you that the release of our Q2 report will be on July 18. Thank you.

Operator

Ladies and gentlemen, this does conclude your conference for today. Thank you very much for participating. You may now all disconnect.

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