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PRESENTATION

Operator

Ladies and gentlemen, welcome to the Swedish Match Q2 Report 2020. (Operator Instructions)

Today, I'm pleased to present Mr. Emmett Harrison. Please begin your meeting.

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

This is the Swedish Match Second Quarter 2020 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 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, Emmett, and hello, everyone. As you may recall, we have a new product segment reporting structure from the beginning of this year. And on Slide 4, we present the sales and the EBIT split under this new segmentation for the January to June period of 2020 as well as for 2019.

Due to the rapid growth of smoke-free volumes in the U.S. and most notably, ZYN nicotine pouches, the Smokefree product segment has increased its relative share of group results for the first 6 months of 2020 and accounted for nearly 2/3 of our product segment sales and nearly 3/4 of operating profit from product segments.

On Slide 5, you can see our sales split by geography as well as the geographical split for each of our product segments for the year-to-date period of 2020, and with the half year 2019 percentage split for emphasis. Approximately 2/3 of Swedish Match's sales from product segment is sourced from the U.S. Within the Smokefree segment, the U.S. is now the largest contributor to sales, having surpassed Scandinavia, which accounts for a bit more than 40% of the Smokefree total.

For Lights, a substantial portion of sales come from markets outside Scandinavia and the U.S., most notably countries in Asia and Europe, including Russia as well as Brazil.

Moving to Slide 6. Last quarter, we presented a slide on COVID-19 impact as well as our view of the outlook for the second quarter as the COVID pandemic began to take hold in our markets. During the end of the first quarter, we noted unusually high levels of orders by the trade for our products, most notably for our offerings in the U.S. We had anticipated that a high percentage of the trade [wording] would unwind in the second quarter. This was indeed the case for our U.S. moist snuff business and, to a lesser extent, for ZYN in the U.S. For our U.S. chewing tobacco business, however, our shipment volumes in the second quarter were very strong, and it does not appear that second quarter shipment volumes were impacted by the unwinding of trade inventories which could imply unwinding effects in future quarters.

For our Scandinavian Smokefree business and for our international market expansion projects, border closures and other restrictions had a notable impact on volumes as we lost the vast majority of our volumes normally delivered to Travel Retail and border shops and had to slow down planned launch activities for nicotine pouches in new markets. As a consequence of travel restrictions, however, domestic Norwegian shipments were exceptionally strong.

The pandemic also required that we put in place a number of hygiene and social distancing protocols in our factories, offices, and for our sales forces. These necessary steps resulted in extra cost during the quarter and negatively impacted production efficiencies in our manufacturing facilities. For our cigar facility in the Dominican Republic, while staffing levels gradually returned to more normal levels toward the end of April following its temporary closure, COVID-19 safety measures limited production output, resulting in relatively steep declines in natural leaf shipments and increased back orders.

Our capacity expansion projects for nicotine pouches in both the U.S. and Scandinavia are continuing according to plan. We will touch COVID-19-related impacts further in the product segment commentary, but do note that one should expect the continuation of elevated costs as well as continued shipment volatility during this pandemic period. Forecasting with any level of precision is challenging in this environment. But we have been pleased to see recent improvements to production output from our Dominican Republic cigar facility and some increased activity in the Scandinavian Travel Retail and border trade channels. With that said, our underlying markets and businesses remain strong, and I remain confident in our ability to demonstrate diligence and agility during these uncertain times, while remaining focused on the opportunities that present themselves over the long term.

Slide 7 highlights a few key points from the quarter regarding our product segments. The strong performance for Smokefree was once again the main contributor to our sales and earnings growth with ZYN in the U.S. standing out as the key driver of sales and operating profit growth. While impressive on an underlying basis, the financial performance for ZYN in the U.S. also benefited from reduced marketing spend compared to the prior year period with the comparison being impacted by reduced activity and some postponement of consumer marketing efforts in the quarter due to COVID-19 restrictions as well as costs in conjunction with the national rollout in the prior year period.



For our Scandinavian Smokefree business, aggregated shipment volumes were negatively impacted by continued border closures and travel restrictions due to COVID-19. However, positive product and country mix shifts counteracted the adverse volume effect, and both sales and operating profit grew in local currency compared to the prior year. A noteworthy consequence of the closed Swedish border trade was the dramatic increase in purchase volumes on the Norwegian domestic market. While channel and market shifts make it more challenging to get the true read on category development, we estimate that the overall Scandinavian market for snus and nicotine pouches continue to experience solid category growth.

For Cigars, our ability to produce HTL cigars in dose in Alabama in the U.S. was a distinct advantage for Swedish Match as we were able to increase our overall shipments year-on-year despite the reduced production output for natural leaf cigars from our Dominican facility. The increased shipment volumes were the result of a significant increase in sales of HTL cigars, which translated into the negative mix effects for the quarter.

Our Lights business delivered a strong financial result with a higher operating profit for both matches and lighters despite lower sales for lighters. Profits were higher as reported, but also when adjusting for restructuring charges in last year's second quarter and for the land sale that benefited the second quarter of this year. Match volumes were robust due in part to trade loading in Brazil in anticipation of an announced trade price increase.

With that, I will hand over to Tom for some additional comments on the performance for each of our product segments.

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

Thank you, Lars. On Slides 8 and 9, we've summarized some of the quarterly highlights of the Smokefree products segment, which includes snus, nicotine pouches, moist snuff and chewing tobacco.

Beginning with snus and nicotine pouches on Slide 8. ZYN in the U.S. was once again a major contributor to sales and operating profit growth for the Smokefree segment. Shipment volumes during the quarter for ZYN in the U.S. were 26 million cans, and total shipment volume during the first 6 months of 2020 has already surpassed total 2019 shipment volumes. We had previously estimated that first quarter shipment volumes benefited from 2 million cans of COVID-19 distributor hoarding and approximately 1 million cans of pipeline fill attributable to new stores added during the first quarter. While difficult to determine with precision, we estimate that the unwinding of hoarding negatively affected Q2 shipments by close to 1 million cans. And based on data measuring distributor shipments to retail, second quarter volumes of ZYN grew by 10% sequentially from the first quarter.

The pace of new store distribution slowed during the second quarter, and distribution build through the remainder of the year will be limited somewhat due to overall production capacity constraints. With regard to our Scandinavian business, we estimate that the decline in shipment volume was exclusively attributable to COVID-19 effects. With borders closed, as Lars mentioned, Norwegian domestic volume was exceptionally strong as consumers did not have the option of buying their products in Sweden. When comparing Nielsen data to deliveries, it appears that Swedish Match Q2 shipments to Norway were further elevated as the Norwegian trade inventories at the close of Q1 were at normally low levels.

The high Norwegian volumes were positive to our price and portfolio mix. Unfortunately, the depreciation of the NOK compared to the SEK eroded much of that added benefit. Outside of Scandinavia, we were successful in adding 2 countries to the geographies where ZYN and nicotine pouches are available at points of trade. However, due to lockdowns, travel restrictions and store closures in a number of markets, we had to modify and, in some cases, defer our sales and marketing activities in new markets.

Turning to Slide 9. In moist snuff in the U.S. where we reported improved shipment volumes despite trade unwinding for the first quarter COVID-19 hoarding, in large part due to our simplified pricing promotion strategy for Longhorn. Both sales and operating profit were down, however, due to both portfolio mix shifts and higher manufacturing costs related to COVID.

We once again gained market share in the faster-growing pouch segment of the market. In this quarter, our share within the moist snuff pouch segment surpassed our overall share within the moist snuff category.



For U.S. chewing tobacco, like for moist snuff, we noted increased orders in Q1 from wholesalers and retailers likely tied to the COVID-19 hoarding. Unlike moist snuff, however, we cannot see any discernible unwinding of trade inventory during the second quarter, and shipment volumes increased compared to the prior year. The long-term decline trend of chewing tobacco category is likely to continue, so one should consider the year-on-year volume growth during the quarter to be an exception rather than the norm.

For chewing tobacco outside the U.S., our chew bags and chew bits, shipment volumes for the quarter declined compared to the prior year, most notably in Germany, where a recent court verdict adversely impacted future growth opportunities for chew bags in that market.

On Slide 10, we show the volume trend for the combined snus and nicotine pouch category for Sweden and Norway together, as measured by Nielsen. With border closures and changes in purchasing patterns, it is much more difficult to properly assess market dynamics in individual markets. But when looking more on an aggregated view, we believe that combined category is demonstrating continued strong growth in consumer offtake led by the rapid growth of nicotine pouches.

On Slide 11, we presented a standard slide to depict the market trend for the snus category on a volume and value basis as well as market shares in Sweden according to Nielsen. While Nielsen measures have experienced more volatility and should therefore be viewed more directionally within the COVID context, 2 points are worth commenting on are the decline in rate of year-on-year growth for the snus category and the weaker relative performance in retail value development in Sweden. The decline in snus growth rate is at least in part attributable to travel restrictions, while the decline in retail value is attributable to channel shifts within Sweden where we saw significant volume declines in the more premium-priced channels like convenience, with stronger volumes in more price-sensitive channels like grocery. The value price segment share of the market remained relatively stable compared to the prior year, and Swedish Match's total market share in the category declined 1.2 points compared to the prior year, principally due to segment mix shifts and 0.9 points sequentially, primarily due to market share losses in the value and Premium 2 segments.

On Slide 12, we have presented the market share trend -- the market trend and market shares for nicotine pouch category in Sweden according to Nielsen. Supported by strong competitive activity in terms of product launches and in-store visibility, the nicotine pouch category has doubled in size over the past year and is now roughly 8% relative to the snus category. Swedish Match's share in the nicotine pouch category has remained relatively stable and our continued objective is to capture a higher percentage of growth within this attractive category. And recall that in terms of pricing during nonpromotional periods, nicotine pouches are typically priced in line with or above the Premium 1 snus products, and the dramatic growth of nicotine pouches have therefore contributed to a positive price/mix effect in the combined category.

Now turning to Slide 13. And to the left, we have presented total combined snus and nicotine pouch category, volume and retail value development on a trended basis for the Norwegian market according to Nielsen. The impact of border closures between Norway and Sweden is quite evident and dramatic in the quarter. Once the borders reopen and Norwegians are more freely able to travel to Sweden, we should expect the extreme level of in-country purchases to revert to more normal levels. Given that Norway is an all-premium market, this shift from Swedish border purchases to our Norwegian domestic purchases provided Swedish Match with price/mix benefits during the quarter that more than compensated for the lost Swedish border trade volumes. Swedish Match has gained market share within the snus category. And although we have lost market share within the nicotine pouch category compared to the prior year, our market share has remained relatively stable on a sequential basis.

On Slide 14, you can see that the nicotine pouch segment in Norway has grown dramatically over the past 2 years. And in the nicotine pouch segment, even with our own strong volume growth, our share progression remains a challenge.

On Slide 15, the chart illustrates the dramatic growth of ZYN nicotine pouches in the U.S. on a trailing 12-month basis. Please bear in mind that shipment volumes do not always fully align in timing or magnitude with consumption volumes, particularly in periods of significant store distribution build due to inventory stocking or destocking effects at the wholesaler or retailer level. In our last interim report conference call, we noted that shipment volumes during the first quarter benefited from both pipeline and COVID-19 effects.

On Slide 16, we have summarized trended volume and market shares by brand within the nicotine pouch category in the U.S.-based on distributor shipments to retail. ZYN is now available nationally in the U.S., and despite being in fewer stores than another nicotine pouch competitor and expanding distribution and aggressive price promotion by other competitors, ZYN's market-leading share has remained resilient. As competition



increases and the market expands, our ability to maintain market shares at these levels will become increasingly difficult, but the trend so far is very promising. And with a rapidly growing category, it is still possible to deliver continued volume growth despite market share losses. I would like to remind you, however, that until the next phase of capacity expansion is operational continued volume growth could be limited by capacity constraints.

On Slide 17, you can see the size of our ZYN brand in the U.S. relative to a number of benchmarks in the established western region as well as for all national launch markets on a trended basis based on distributor shipments to retail. The trend rate can experience fluctuations due to distributor ordering patterns as well as promotional activities, but moist snuff -- backed by moist snuff and nicotine pouch competitors. While the growth trend for some of the benchmark has softened, we are encouraged that we continue to see growth in both the western region and regions outside the west despite aggressive promotional pricing and distribution efforts by nicotine pouch competitors in the second quarter.

Looking at U.S. moist snuff on Slide 18, we've summarized trended quarterly category and Swedish Match growth rates based on distributor shipments to retail. It is fairly evident that Q1 2020 growth rates have been favorably influenced by COVID-19 porting activities and an unwinding occurred during the second quarter. MSA data indicates that Swedish Match volumes continue to outpace the category, led by pouches in the second quarter. As noted earlier, we are seeing favorable trade and consumer response to our simplified price promotion strategy for Longhorn contributing to the year-on-year share gains for our moist snuff portfolio.

Looking at U.S. chewing tobacco on Slide 19, where we once again outperformed the overall category in both the premium and value segment. Earlier in this presentation, we noted that shipments in the quarter for our own brands were up versus the prior year. For longer periods, there has generally been mid single-digit volume declines annually for both the market and for Swedish Match with a shift from premium products more toward value-priced brands. Our year-to-date shipment volume growth of 1% is likely an anomaly of COVID-19-related distributor purchasing behavior which could result in distributor destocking in future quarters.

On Slide 20, we've presented some of our recent new product and market activities for snus and nicotine pouches. In the U.S. through 2019, the 3 depicted U.S. ZYN varieties, which include the citrus-flavored SKU, in addition to 2 unflavored varieties had only been available in the western region. During this year and especially during Q2, we have expanded the availability of these products nationally. In May of this year, we relaunched our 1 range of products on the Swedish market, which provides consumers with a powerful taste experience, featuring large well-filled pouches and center pouch paper for an improved mouth fill, all packaged in a more contemporary design. Early indications are that this overhaul and brand transition has been successful with One gaining share within the attractive Premium 2 segment in Sweden.

In addition to the One range of products, we also expanded our assortment for ZYN in Sweden and G4 nicotine pouches in both Sweden and Norway. Our activities in new markets for ZYN outside of Scandinavia and the U.S. have been limited recently due to COVID-19 restrictions. But we were successful in launching ZYN into a number -- limited number of stores in both Bosnia and Poland since the first quarter.

Moving to Slide 21 in cigars. Swedish Match cigar shipment volumes increased 2% compared to the prior year as our shipments for HTL cigars more than offset declines for our natural leaf varieties, which resulted from our inability to meet customer orders following the closure and subsequent phased reopening of our Dominican Republic manufacturing facility. The overall cigar category appears to be very strong right now, possibly impacted by COVID-19-related changes in consumption patterns. Operating profit and operating margin were down due to both mix shifts and higher manufacturing costs, heavily influenced by COVID-19-related factors.

On Slide 22, we've presented a quarterly trend of Swedish Match cigar shipment volumes as well as our estimate of the U.S. mass market cigar category and segment volume development based on distributor shipments to retail. Swedish Match utilizes the externally developed MSA data set and revisions to historical reporting periods are common as retail stores and distributors are added to the data set. Based on NSA measures of distributor shipments to retail, total cigar category volumes increased by more than 10% for the first 6 months of the year compared to a category growth rate of slightly more than 2% for full year 2019. Swedish Match's volume under this same measure increased by 15% in the first 6 months of 2020, and with Swedish Match significantly outperforming the category and the HTL segment while growing at a slower rate than the category for natural leaf cigars, influenced markedly by COVID-19 production constraints.

On Slide 23, you can see a split of cigar volumes for Swedish Match in the comparable market during the second quarter, and on the right side of the slide, you can see our shipment volume trends. The production constraints experienced by our Dominican Republic facility is evident by the sharp decline in trended natural leaf varieties as well as the composition of our portfolio in the quarter. Normally, close to 2/3 of our portfolio is comprised of natural leaf cigars if these cigars represented only 55% of our shipments during the quarter.

Moving on to Slide 24 in our Lights product segment. Adjusted for currency translation effects, sales for the segment were up 14% and operating profit was also sharply higher. Match has benefited most notably from strong volumes, but also from an improved product mix. In one of our larger markets, Brazil, there was the benefit of trade loading of matches in anticipation of an announced price increase. We sold some land in Brazil this quarter for a gain of SEK 6 million, and last year's second quarter results included restructuring charges of approximately SEK 12 million, both related to matches. Excluding these items, the operating profit for matches was also considerably higher year-on-year.

For lighters, volumes were down, but with improved positive product mix, tight control, cost controls and reduced raw material pricing, most notably for nylon, operating profit also improved compared to the prior year.

On the regulatory front, on Slide 25, you can see some of the more notable regulatory events, which have occurred during the second quarter. With regard to the FDA and cigars, we note that the filing deadline for SE applications has been extended to September, and we are well positioned to meet this filing deadline.

For chewing tobacco in Germany, the federal administrative court has decided not to grant leave to appeal, a lower court decision on Thunder chew bags. So that decision is now final. This is a product-specific ruling. But nonetheless, we anticipate that there may be a cessation of sales of most chew bags in their current form in Germany. Sales of chew bags on the German market during the 6-month period ended June 30, 2020, amounted to SEK 46 million and are included within other markets in the Smokefree products segment specification.

On Slide 26, we've summarized relevant metrics from our interim report relating to finance costs, our financial position and earnings per share. Net finance costs during the quarter increased relative to the levels that we've experienced in the past, principally due to higher debt levels as well as lower returns on our surplus cash position. The weighted average interest rate of our loan portfolio at June 30 was 2.05% compared to 2.08% at the end of 2019.

Our net debt-to-EBITA for the 12-month period ended June 30 was 2.1. During the first 6 months, new bond loans of SEK 3.175 billion were issued and repayments of bond loans amounted to SEK 500 million. During the remainder of 2020, SEK 800 million of this debt falls due for payment.

As of June 30, 2020, Swedish Match had SEK 1.5 billion in unutilized committed credit lines and cash and cash equivalents amounted to SEK 3.907 billion at June 30, 2020, compared to SEK 2.37 billion at December 31, 2019.

The net debt as of June 30 amounted to SEK 13.384 billion compared to SEK 11.925 billion at December 31, 2019. The capital duration was 4.2 years with 98% of the portfolio subject to fixed interest rates.

The EPS bridge illustrates the components of our 28% year-to-date growth in EPS, and apart from the after-tax effect of our increased operating profit, the reduced number of shares had a meaningfully positive impact.

During the first half of the year, we made share repurchases in the amount of SEK 1.435 billion, buying 2.4 million shares at an average price of about SEK 596 per share, and during the second quarter, an ordinary dividend of SEK 2.20 billion for the 2019 financial year was paid out to shareholders.

Slide 27 simply restates our 2020 outlook from the interim report, which remains unchanged. Our CapEx plans remain on track to be considerably above the 2019 level, and we continue to foresee good market growth for Smokefree nicotine products. While we continue to expect the effective corporate tax rate for the full year to fall within the 22% to 23% range noted in the outlook, the strengthening of the U.S. dollar or a more rapid growth of the U.S. businesses compared to our Scandinavian businesses could place added upward pressure on our consolidated group effective tax rate. And finally, as always, fluctuations in currency rates will affect our future reported results, and you may want to take note of some of the

more important average exchange rates versus the SEK. The average exchange rate in the third quarter of 2019 for the U.S. dollar was SEK 9.6; the NOK, it was SEK 1.08 and the Brazilian real was SEK 2.42.

With that, operator, please open up the line for questions.

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

We can open the line for questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) So the first question is from Niklas Ekman from Carnegie.

Niklas Ekman - *Carnegie Investment Bank AB, Research Division - Head of Consumer Discretionary & Staples and Financial Analyst*

A couple of questions. Firstly, a question on ZYN and the current operating margin. Counting backwards, it sounds like you are looking at an operating margin right now that is kind of in the upper end of the 50% to 55% range. Can you confirm this? And can you also elaborate a bit on where you expect this could go going forward? On the one hand, hampered by increased marketing and maybe price pressure. On the other hand, the positive scale effects and fewer kickbacks to newly launched retailers. If you could just elaborate on that? That's my first question.

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

Okay. Niklas, I'd say your estimate is good and that the margin that we're experiencing for ZYN in the U.S. right now is heightened -- expected heightened relative to what our expectations were. I would point out that the extent of marketing that we have been able to do, whether it's due to COVID-19 effects or similarly due to the fact that the general production constraints. We've been less aggressive in looking to match some of our competitor activities on price promotion in market.

So I guess in sum, yes, we do have a operating margin for ZYN in the U.S. that is within kind of -- at or above slightly the range that you specified. But we would expect that margin to moderate as production quantities come online and as our marketing efforts that were curtailed in the second quarter are able to be put in place.

Niklas Ekman - *Carnegie Investment Bank AB, Research Division - Head of Consumer Discretionary & Staples and Financial Analyst*

Okay. And sticking to ZYN, but looking at the European rollout. Obviously, a difficult quarter in terms of rolling out to new markets. But can you still elaborate a little bit on what kind of volumes you are seeing in Europe? Are there any markets where you're seeing any similar performance per store as what you've seen in the U.S. rollout?

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

This is Lars. I mean, when you look at very early store velocity developments, we have seen some similarities. But then typically leveling off with, albeit, future growth, indicating that it takes a longer time in the European market to build the business.



Niklas Ekman - *Carnegie Investment Bank AB, Research Division - Head of Consumer Discretionary & Staples and Financial Analyst*

Okay. And can you also say something more about the regulatory environment? You mentioned here the FDA regulation on flavors, and you mentioned the date, the 9th of September. What do you think the likelihood is? Are you seeing any indications of a flavor ban actually coming in place by the 9th of September?

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

The 9th of September is the deadline as it stands right now for filing of SE applications or PMTA applications for these newly deemed products. As you know, we already find our PMTA applications for ZYN, and we stand well equipped to file for our cigar assortment by this deadline.

FDA has indicated themselves that in terms of labor enforcement, they will avail of the SE process. Exactly what that means remains to be determined, whether they will -- it becomes a bit speculative, but whether they put higher thresholds, so to say, on what is actually considered to be a substantially equivalent product, if it is a flavored product, compared to an unfavorable product, that remains to be seen.

But in terms of federal flavor regulation across all assortment, there seems to be a delay if you listen to what FDA communicates in terms of prioritizing their agenda. So not too long ago, they talked about coming out with a proposed rule in March of this year. And based on recent communication, at the earliest, I would say, toward the end of the year.

Niklas Ekman - *Carnegie Investment Bank AB, Research Division - Head of Consumer Discretionary & Staples and Financial Analyst*

Excellent. And on the same topic but for the European market, as I understand, nicotine pouches is more or less entirely unregulated today and that might change with the new implementation report from May 2021. Are you seeing any indications there where the market is heading? And for specific countries like Sweden, Norway, Denmark, what are the moves in terms of regulation for nicotine pouches?

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

Yes. I mean, if you take -- first of all, if you talk about the evaluation and the subsequent revision of the tobacco directive, as you point out, that is a possibility, that nicotine pouches would be folded in, in the tobacco directive, similar to what e-cigarettes were in the last round, albeit that ZYN today is not a tobacco product. But we think that a common regulation within the tobacco directive could potentially be relatively good for the category. As sort of say, in one go, you would have a consistent approach on how to regulate the product. Because as you point out right now, it's kind of more country specific. And there are various examples there.

I mean, if you take the Czech Republic, as we understand it, there is a proposal to regulate nicotine pouches in what we consider a reasonable and rational manner. If you take Sweden, the government has appointed an inquiry that will evaluate the macro regulation, including looking at nicotine pouches. But -- and the report there is not due until in 2021, and then we need to see what kind of proposals come after that. In Sweden, though, the product is taxed. So it's, in that sense, recognized by the regulators. And similar in Denmark, there was a political compromise regarding tobacco products. And I think it was at the end of last year or the very beginning of this year where nicotine pouches were singled out. And at least for a 2-year period where they would where they would monitor the development in terms of consumption uptake and so forth and the youth prevalence that planned flavor ban would not be included in such regulation for nicotine pouches, while, for example, our June tobacco product, as the proposal read, would be included. However, we haven't seen -- and that could be COVID-related, just in terms of political agenda. We haven't seen any sharp proposal yet. We had expected to see that by now. But as we understand it, it's pushed at least over the summer.

Operator

So we have the next question from Mr. Adam Spielman from Citi.



Adam Justin Spielman - Citigroup Inc., Research Division - MD, Head of EMEA Consumer Staples Research and European Tobacco & Beverage Analyst

Yes, I have 2 questions. The first question refers to Slide 16 and 17 of the presentation. And in both those slides, presented in different ways, but nonetheless, is absolutely common in both, that the growth of nicotine pouches as a category and, indeed, yours, has slowed according to shipments in the MSAi data. And I was wondering what you should read into that. Certainly, you could make the argument that, actually, demand is slowing. Because if you were capacity constrained and everybody really wanted this product, I would expect Velo to at least remain stable as opposed to decline.

Anyway, I'd just like to comment on the apparent slowdown or the actual slowdown shown in Slides 16 and 17. That's my first question.

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

Yes. I mean, first of all, Adam, I would urge you to be a little bit careful with quarterly comparisons this year due to the kind of extraordinary circumstances in the marketplace caused by COVID-19.

So I mean, the number, in terms of volumes in the MSA data, as Tom stated, is a sequential growth of 10% on shipments from distributors to the retail. And when you look at that more closely on a weekly data, you also see that similar to shipments that we reported that then go into distributors, the MSA data indicates that there was COVID-related hoarding toward the end of the first quarter and unwinding of the -- some of the hoarding in the second quarter. So in that sense, you can say that the underlying MSA growth is actually stronger on a sequential basis.

But again, you need to be careful, and there are kind of seasonal factors in here. So even for some other categories, the second quarter normally is a little bit stronger. So I think one has to see in these very special times, it's extra important to look a little bit more on the long term. And what is clear to us is that the category has continued growing nicely, and that it has continued to -- the growth has been, at least in our case, been driven by increased velocity rather than expanded distribution and the introduction or the availability, national availability of new SKUs, including these unflavored products.

And on the next slide where -- when you look at these benchmarks, I mean, then you get into further details and you have kind of 2 categories to play with. So here, it becomes extra susceptible to quarterly fluctuations. And you need to bear in mind that we're only reporting here ZYN volumes relative to the moist snuff category. And if you take the regions outside the west, there, we have seen -- although our overall market share is more or less stable between the first and the second quarter, overall market share in the -- what we can call the expansion markets, has declined a bit. So you need to add competitive volumes, so to say, to those benchmarks if you want to evaluate the whole category. And when you're into the west, you're into an even smaller data set, and therefore, additionally vulnerable to kind of quarterly fluctuations in ordering patterns.

So long story short, we feel very good about the continued growth. And even if there is a slowdown on a sequential basis, it's very strong. And we have seen some of this very strange demand in other categories. So to the extent that some of this, for example, if you smoke more cigars because you're not in a workplace where it's a smoking ban. Well, maybe when you get back to your workplace, you go back to using your ZYN instead.

Adam Justin Spielman - Citigroup Inc., Research Division - MD, Head of EMEA Consumer Staples Research and European Tobacco & Beverage Analyst

Can I turn to another question, which is, clearly, in some small markets in the United States, it is illegal for you to sell flavors. So let's say, San Francisco City, Boston, I believe. And can you just talk about how the growth of ZYN where you're selling Chill and Smooth compares with equivalent cities, let's say, or equivalent geographies where you have a full range of flavors available to you?



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

Yes. I would say that what we're seeing -- I mean, we have obviously, pockets of localized labor bans. We have more recent example of a statewide flavor ban in Massachusetts that only went in force 1st of June of this year. And in that market, what we saw was, once again, based on distributor shipments to retail, was in essence, a replacement of the velocities of a broader assortment, including flavored SKUs of ZYN with our unflavored varieties.

Now I think it's probably still somewhat early to draw firm conclusions that it's a complete replacement of those SKUs, because some of that, obviously, is selling those unflavored SKUs into those points of retail.

I mean, California, kind of more broadly, is not one of our highest-performing velocity states. So -- and then if you look more specifically at counties or cities within California, it becomes that much more challenging to capture a read on what you see because it's not that difficult if you're talking about a county or local flavor ban measure for consumers to travel within the states beyond the bounds of that flavor ban to get their unflavored product.

But I would say in those jurisdictions where we do have flavor bans, we see a nice, attractive velocities. And we're not seeing market declines in overall velocities affected by those regions.

Operator

The next question is from Mr. Fredrik Ivarsson from ABG.

Fredrik Ivarsson - *ABG Sundal Collier Holding ASA, Research Division - Research Analyst*

A few questions from me as well. First one, on product mix maybe in Sweden in particular. Given the current macroeconomic uncertainties that we're currently seeing, I would assume that some consumers might trade down. But on the other hand, you might see some strong growth within nicotine pouches. So curious, can you say anything about what you saw in terms of underlying product mix, particularly in Sweden? And maybe what your expectations are going forward?

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

Yes. I mean we haven't seen any abnormal swings to the product mix in Sweden, I would say. Actually, I mean, I would point you to the slide we had in our presentation where you can see the market share is measured by Nielsen. Overall, we consider Nielsen to be -- in terms of market shares and therefore, also segment market shares, the trends there relatively reliable despite what's going on. And the reason for that is that also that Nielsen doesn't capture the border trade that well. So there, you see that the value segment has remained relatively stable. It's -- we think it's fairly accurate.

And when you look within Premium segment, we have seen continued strong growth of the Premium 2 segment and potentially a little bit steeper decline than normal in the Premium 1 segment. But that is actually also a little bit influenced by lack of Norwegians coming over to Sweden and buying some of our products, but also one of our competitors. We see that on the shares within Premium 1.

Fredrik Ivarsson - *ABG Sundal Collier Holding ASA, Research Division - Research Analyst*

Okay. And second question, a little bit more short term, I guess, into looking into Q3 and Q4. How should we think about marketing spend for ZYN in the U.S.? Should we just assume that a fair part of the cancel or marketing spend won't come back? Or should we think like it's more postponed into H2?



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

No. It's -- what I would view it is our -- our second half plans are largely consistent with what we had planned for pre-COVID. So the kind of the savings that we experienced in Q2 is more so a kind of loss spend.

Operator

The next question is from Mr. Gaurav Jain from Barclays.

Gaurav Jain - Barclays Bank PLC, Research Division - Research Analyst

So I have 3 questions. One is on ZYN shipments. So you have shipped 26 million. And in the comments, I think you mentioned that 1 million is the pantry unwind. So that means that 27 million is the sell-through over which there will be little sequential growth in Q3 and Q4 because of the capacity constraints that you have highlighted. Is that the right way to think about ZYN's volume numbers?

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

Yes. I mean, we shipped 26 million. And yes, we think that, that 1 million is -- we were not 0 on inventory at the end of the quarter. So in that sense, we -- without the reversal of the hoarding, our estimate is that we would have sold about 1 million more.

So -- and then going forward, as Tom highlighted, we are, based on current trends, capacity-constrained for the remainder of the year. And then we do everything we can to supply the market, and we've been successful throughout the history and then driving efficiencies out of our factory. And then we also support the U.S. market with a bit of production from Sweden, and we can potentially do a little bit more there in the second half compared to the first just based on some of the investments in Sweden coming onboard. But we're talking small increments here.

Gaurav Jain - Barclays Bank PLC, Research Division - Research Analyst

Okay. That's very helpful. Now my second question is on the flavor ban question that was asked previously and specifically on California. So there is a bill which has passed the California Senate recently, SB 793, and now it's in the house, which is looking to ban flavors, which will impact ZYN. And I think in the filing, you have also filed your comments. So can you just help us think how big the impact can be? How big is California for ZYN?

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

Are you talking store counts or...

Gaurav Jain - Barclays Bank PLC, Research Division - Research Analyst

Just the overall volumes in California as a percentage.

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

So it's about 10% of our store base albeit with velocities that are not near what they are for the balance of the states within the West and even probably some of the states that we have right now within our national launch markets. What is encouraging with a flavor ban is that with what we've seen is this kind of transition to the nonflavored varieties, and we are -- but for a handful of other competitors alone, with having unflavored varieties at our disposal. So I think in that respect, what we did see in Massachusetts, you basically went from a 3- or 4-player game to roughly a 2-player game at this point.



Gaurav Jain - Barclays Bank PLC, Research Division - Research Analyst

Right. And did you see a lot of e-cigarette consumers on flavors switching to your unflavored ZYN varieties in Massachusetts?

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

I'm not sure. We're not tracking the consumer migration or transition at that granular a level. So I would say it would be -- I could speculate in that respect, but I'd rather not do that.

Gaurav Jain - Barclays Bank PLC, Research Division - Research Analyst

Sure. And then one last question on this. So we have spoken of an MRTP on ZYN before, and I don't think you have filed any. But if you get an MRTP, do you think that will protect you from any of these flavor bans which are being proposed in different parts of the U.S. and also maybe create a better tax architecture for you?

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

Yes. I think that I'm more positive in terms of states having a more favorable stance on tobacco taxes. I think you seem to be fairly familiar with the California proposed bill, and that one does not have a carve-out for MRTP.

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

And I mean, the difference between a PMTA and an MRTP boils down to what you're allowed to tell consumers from the manufacturing side. Also, the standards set in the PMTA process are fairly high in terms of the FDA concluding that it's appropriate for public health. So if you look into, for example, when we first received our PMTAs for General Snus, already then, they were very explicit on the relative risk for General Snus compared to cigarettes. But we are not allowed to tell consumers. So in that sense, I'd say the PMTA process there is probably more important.

Operator

So we have a question from Mr. Sanath Sudarsan from Morgan Stanley.

Sanath Sudarsan - Morgan Stanley, Research Division - Research Associate

It's Sanath here from Morgan Stanley. A couple of questions from my end. First, have you seen any difference in the consumer profile when you move from the western part of the U.S. to the rest of the U.S. in terms of maybe from where you're sourcing consumers from or maybe getting, recruiting more female consumers, et cetera. Is there any kind of a mix shift you've seen?

And secondly, in terms of the environment right now with COVID, people are probably traveling less to stores, et cetera. And you guys marketing less, of course. How do you think -- what's kind of stimulating the demand for nicotine pouches or the continued demand for nicotine pouches in this market?

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

Well, I mean, on the latter -- last question, the -- it's good established and made available ZYN nationally prior to the COVID-19 pandemic hitting the country. And so many consumers have already tried it or they have friends and so forth to have a good experience with the product. And it's



a good product, and people don't stop consuming good products even in, sort of say, bad times, albeit unless they are kind of directly hit by restrictions and so forth.

And in terms of mix on consumer profiles and so forth, that's kind of it's a the detail level that we don't go into this call. But I mean, we track our consumer base and so forth. But it's data that we speak more generally about when we decide to do so.

Sanath Sudarsan - *Morgan Stanley, Research Division - Research Associate*

And if I may just ask, just going back to your comment about limited distribution build and production limitations within in the U.S. Could you just still, again, jog our memory on what amount of -- or what's the level of distribution you expect in the U.S. given, at current levels you are about, you're very close to your biggest distribution-led competitor in nicotine pouches? And in terms of timing on capacity, when could we expect that to come on board in the U.S.?

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

Yes. So I'm going to start with the capacity question first in that regard. What I would say is when you look at our Q2 shipments, it was that the vast majority of what we shipped in Q2 was produced at our Owensboro facility. So the extent of supplemental volumes that we source from our Swedish manufacturing site was somewhat limited. And I think Lars had mentioned, obviously, that there does present opportunities for incremental levels of support as market demand in our established distribution base in the U.S. expands over the course of 2020. And that will give you a pretty good sense of our current manufacturing capacity. And the third phase of the broader ZYN capacity plan would have lines coming online toward the tail end of this year. Or one, it's kind of more of a phased basis for the multiple lines we're putting in place. So we will have a line or 2 that is turned on. That's not fully operational in producing product at the levels that we're experiencing right now for our previously implemented lines. But I would look at that as kind of that future installation in Owensboro to be more of a benefit for 2021. And that expansion is to essentially double what our current annualized capacity is in Owensboro.

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

This is Emmett. Just to add a little bit to that, going into the production increase toward the end of this year and, really, getting going in 2021, we will have some added costs going into that in terms of manning and preparation for that before actual production goes out. So one should bear that in mind a little bit as well.

Sanath Sudarsan - *Morgan Stanley, Research Division - Research Associate*

Okay. Anything on the stores, if you have any?

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

Yes. And I would look at -- we talked about being in 85,000 stores currently. And as we expand capacity, so without capacity restrictions, so let's now think about 2021 and beyond, the store set for tobacco in the U.S., the 85,000, 90,000 stores is about the number of stores that we have shipments to for our Longhorn moist snuff brand. If you look at brands kind of more -- the market-leading brands within moist snuff, you have -- they may be shipping to 150,000 stores. But really, it's more closer to 125,000 is a big good number to use in terms of the universe of convenience stores that could be potential market for convenience. And bear in mind, we talked about in Q1 that our 85,000 stores includes a large number of stores within the drug channel, which is kind of outside that 125,000 stores I mentioned for the market-leading moist snuff brands.

Operator

So the next question is from [Mr. Patrick Fullen] from [Brickburn.]

Unidentified Analyst

Three questions from me, if I may. First, you mentioned in July, you're beginning to see recovery in volume trade in Travel Retail. How much of recovery have you seen relative to pre-COVID levels in Scandinavia?

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

Yes. Very little. But what we are seeing is that the Finnish border, which is the smaller of the 2 borders, there, trade has opened up. And then travel out of Sweden and so forth and airports, the traffic is starting to operate again, but at a reduced the level. And the ferries on the Baltic sea, while the overall capacity has been reduced because of one of the operators running into financial difficulties, as I understand it, those cruises are starting to run, which is kind of very positive from -- in terms of being able to supply to the Finnish consumers.

But the big one here is the Norwegian one, if we talk volumes. And so far, Norwegians that travel to Sweden -- to those parts of Sweden, they need to quarantine if they go back to Norway. So I think we have to expect that it -- the third quarter will definitely include a clear impact in terms of the shipment volumes as well. And then nobody knows exactly how long this will go on.

Unidentified Analyst

Okay. That's clear. And then on the U.S., in terms of customer acquisition for ZYN, it builds off to another question. But have you seen any noticeable drop off during Q2? I'm assuming you have. Or has it remained relatively flat? Can you provide any color there?

And then one more on the U.S. just on moist snuff and chewing tobacco. Your pricing was down and there was a shift towards value price offerings and the year-to-date chewing tobacco declined in Premium segments. So have you seen any elements of accelerated downtrading during Q2 and can the same be said about moist snuff?

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

The one question that you said in terms of customer acquisition, I presume you mean -- are you talking store build there?

Unidentified Analyst

Yes.

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

Yes. So we finished Q1 at 83,000 stores, and we finished Q2 with 85,000 stores. So there wasn't much in the way of incremental store build during the quarter nor is there expected to be much in the way of incremental store build as we look out over the second half of 2020. And from a downtrading, our -- kind of our pricing, what I would say is, I mean, Longhorn is the lion's share, significant portion of our total moist snuff portfolio. So we have 2 other moist snuff brands in Timber Wolf and Red Man moist snuff, but those are not necessarily large contributors to our overall portfolio mix.

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

For chewing tobacco, the trend has been, for a number of years, moving from premium-priced products to value-priced products. And we have a very strong share in the premium segment and a very good and growing share within the value price segment. And that trend is a longer-term trend, and we would expect that to continue.

I don't believe that there's any acceleration of that trend. But in the second quarter, it was a bit of an odd quarter with quite strong shipments in it. The EDLP program that we have for Longhorn, the new pricing promotion strategy we have for Longhorn is helping us quite a bit. If there were any effects of downtrading from moist snuff, that would benefit Swedish Match as our portfolio is more skewed toward value-priced products than our competitors' portfolios.

Operator

Next question is from Mr. Karri Rinta, Handelsbanken.

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

Two questions. Firstly, a follow-up on the potential flavor ban in California. You mentioned that California is roughly 10% of your store count, but it's also the largest state in the western region where you have been for quite some time. So can you give us any more color on the -- how much of your volumes, ZYN volumes California is? And maybe if it's more or less than 20%? And then secondly, if this ban were to be implemented, would online sales still be allowed into the state of California? That's my first question.

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

The -- my understanding is that online sales would be allowed. the challenge there is to what extent would that then result in increased regulations around and whether it's a disallowance and/or an age requirement restriction placed on online sales. And there has recently been a federal regulation that would expand the PACT Act to also cover e-cigarettes that has not, to this point, addressed nicotine pouches.

And we don't provide specific volumes on a state-by-state basis. So -- but I think that with what I had mentioned, you get a sense of the number of stores that we have, and roughly 10% of it is the distribution base we have in California, a little less, I'd say arguably less than 10%.

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

All right. And the ZYN capacity expansion in Sweden, I think it was -- you earlier commented that it would be operational sometime this summer. So can you give us an update on whether it's up and running? And I think you have also mentioned that it would be a sort of on an annual basis, a net increase of SEK 25 million cash? Is that correct?

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

And the machines have been installed and started to produce some output but at very low initial levels. There will be a gradual ramp-up there in terms of getting the equipment fully operational. And it's roughly max capacity of 18 million to 20 million cans we're talking about in the first round. But it's also designed for products that don't go to the U.S. market. So it's -- if it's the U.S. market, you're thinking of it -- it's more for international expansion.

Operator

So the next question is from Mr. Adam Spielman from Citi.



Adam Justin Spielman - Citigroup Inc., Research Division - MD, Head of EMEA Consumer Staples Research and European Tobacco & Beverage Analyst

I just -- following up. At the time of the 1Q results, you gave a whole load of sort of comments about what you think would happen in 2Q, bearing in mind the virus and the crisis. I think you've said -- and so the question is, is there anything specific we should be thinking about in terms of 3Q? You've already highlighted that the situation in Scandinavia is eased a bit, but not that much. Norwegians will find it very hard to buy in Sweden, across the border. Are there any other sort of things we should be thinking about around your business that may be distorted in Q3 because of the virus?

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

Yes. So I would look firstly to what we talked about as being those volumes that we did not see unwind in Q2. So that's within the chewing tobacco space as well as those roughly 1 million cans within ZYN that will likely come down in Q3.

Adam Justin Spielman - Citigroup Inc., Research Division - MD, Head of EMEA Consumer Staples Research and European Tobacco & Beverage Analyst

And sorry, did you say 1 million? Because I thought it was 2 million sort of that was the bill -- well, I thought there was a 3 billion build in Q1. And a 1 million unwind in Q2, which implies sort of still 2 million to go. But maybe I misunderstood that.

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

Yes. And my math is more specifically around the Q1 hoarding. And the reversal that we could as best determined from that hoarding in Q2. I mean, we have -- the pipeline, whether it's stores receiving product for the first time, whether it's stores receiving expanded varieties of product for the first time, that's more challenging to understand the placement and reversal of that in market on a quarterly basis. So I was talking more so specifically about the level on hoarding.

Adam Justin Spielman - Citigroup Inc., Research Division - MD, Head of EMEA Consumer Staples Research and European Tobacco & Beverage Analyst

Consumer level. And that -- so just to be absolutely crystal clear, I think you said, and I'm trying to check, that you expected consumer pantry loading, sort of inventories in people's houses, to fall by maybe 1 million cans during Q3. I mean, none of us have a crystal ball, but that's, I think, what you said, am I correct?

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

No. I think what I'm saying is that there -- we, at this point, still see levels of inventories and distributors that, on a kind of a weeks-on-end basis, is higher than pre-COVID levels. So it's really the shipment of those levels out to points of trade for sale through. And those spiked quite markedly in and around the end of Q1.

So the reversal of the hoarding consequences that have yet to unwind is one element. We also talked about the challenges that we've had in our Dominican Republic facility on the -- what was the closure and the phased reopening. We are not yet at kind of pre-COVID production levels. So we will continue to see levels of increased cost and likely adverse -- elements of adverse mix shifts as we bring on -- kind of return to more normalized levels at our Dominican facility. And we expect to kind of get to pre-COVID levels by the end of Q3.

Those are the 2 larger pieces. We talked also about this relationship of shipment volumes in Norway in Q2 versus what underlying Nielsen may otherwise suggest with a view that a portion of our shipments into Norway in Q2 helped to replenish what were depleted levels at the end of Q1. So there could be some level of unwinding of that effect in Q3.

That's kind of a view of the larger pieces. There likely could also be some headwinds within lighters and international markets as well as even our U.S. -- our Swedish distribution business, but those are kind of on the margin.

Operator

(Operator Instructions) So for now, we have the next question. I think it's again from Mr. Fredrik Ivarsson from ABG.

Fredrik Ivarsson - *ABG Sundal Collier Holding ASA, Research Division - Research Analyst*

A quick follow-up from me as well. On the capacity for ZYN in the U.S., just make sure you're talking about doubling next year, but that you did also, in the end of 2019, and that was on a run rate of 20 million, I think, on a quarterly basis. And now you say doubling as well, but now you're in a run rate of 25 million. So are we looking for 160 million or 200 million?

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

Now I will say that during Q2 and during the challenges that we were facing with COVID, we were particularly focused on ZYN and our ability to meet volume demands. So you get to some level, whether the 25-ish million of production in our Owensboro facility is sustainable for all repeatable quarters. So there was -- I think we've talked historically about installed capacity of roughly -- or above 80 million cans. And that would be then doubled to greater than 160 million cans once the Phase III implementation build is fully up and operational. But there are opportunities to kind of flex, and we are continuing, as we become more familiar with the equipment, of increasing and improving manufacturing efficiencies with that equipment.

Operator

So we have another question from [Robbie] Rampton from UBS.

Robert Amos Rampton - *UBS Investment Bank, Research Division - Associate Analyst*

Just my first question is on capacity in Scandinavia for the U.S. variant of ZYN. I think previously, you've talked about 15 million annualized. It sounds like you're getting another 18 million to 20 million annualize online imminently? Any additional color there?

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

Yes, I'd say that's -- that's not entirely realistic going forward. I mean, in the very initial ramp-up phase of the U.S. market, the Swedish factory were under extraordinary circumstances to help supply the market and in a manner that isn't sustainable over the longer term. So that equipment does not have kind of an ongoing capacity of 15 million. And the capacity that is being installed now in -- the new equipment that is being installed and has just started to become operational in Sweden. That one is designed for producing the can for European markets, which differs from the U.S. market. It can, of course, with investments and so forth and the retooling of the equipment, be altered and serve as a back up or under extreme circumstances. But it's kind of more complicated than normal changeover. So one shouldn't kind of think of that as additional U.S. upside. Then I would say, in that respect, what Tom highlighted that we've been very successful in our store in terms of utilizing the equipment that an operating efficiency level that has exceeded a little bit our initial projections based with this -- on this new technology probably represent more of a potential upside opportunity than kind of any material support from Sweden.



Robert Amos Rampton - UBS Investment Bank, Research Division - Associate Analyst

Great. So my next question is on the -- previously, you've given us an indication of the shipment numbers to the core region or at least giving us the tools to work it out. Can you give us that number?

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

Yes, we did not present that slide. I would say that we did see a continuation of store distribution in the West as well as increased velocities in the West. And when you look at the source of growth, be it store distribution or increased velocities, the increased velocities represented roughly 2/3 of the growth.

Robert Amos Rampton - UBS Investment Bank, Research Division - Associate Analyst

Apologies. My next question is, you commented that share was down outside the West. Can you tell us -- can you give us some color around what your share is and how that changed? I appreciate that the overall category grew, and so it's not affected your growth, so to speak.

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

Yes. I think that one should look at it, given our first-mover advantage in the western region, we provide kind of the total U.S. share numbers in the materials. The -- our market shares -- and these are broad numbers, but our market shares within the west, specifically, are mid-80s or so. And market shares for the -- for the balance of the U.S. are slightly less than 70%. And holding reasonably firm despite the aggressive promotional pricing activities that have been put in place by certain of our competitors.

Robert Amos Rampton - UBS Investment Bank, Research Division - Associate Analyst

Great. Apologies, another question for me. In terms of the velocity in some of your earlier installs, you've previously mentioned that some of the 2016, '17 ones were -- the ones above the 60% to 70% mark were slowing. Any update there? Is that still the case?

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

No. I'd say if you look at the developments over Q2, if you go back to our 2016 installs, so Q3 and Q4 of 2016, we're continuing to see kind of -- and there's roughly 3,500 stores, I believe, that we installed in the back half of 2016, we're continuing to see increases in velocities from those stores. So we have not kind of hit the peak or the plateau even for our earliest installs.

Robert Amos Rampton - UBS Investment Bank, Research Division - Associate Analyst

Great. That's very encouraging. And apologies, one final question for me. You've previously given the price/mix in Scandinavia. You've not given it this quarter. I assume it was high single digit, mid-single-digit driven primarily by the shift to Norway? Or is my (inaudible)

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

Yes. I mean, you get the good indication by our new and we like to think improved interim report where we published the sales for Scandinavia, and total Smokefree, of course, snus and nicotine pouches representing vast majority and where you also have the volumes. But there is a strong price/mix component, as you point out and offset by the -- or partially offset, I should say, by the weakened Norwegian krone.



Operator

Okay. So there's any further questions at this time. So please go ahead, speaker.

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

Okay. Then we would like to thank everybody for listening today and asking good questions and inform you that the release of our third quarter results will be on October 27. Thank you.

Operator

This now concludes our conference call. Thank you all for attending. You may disconnect your lines.

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