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SWMA.ST - Q1 2012 Swedish Match AB Earnings Conference Call

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## CORPORATE PARTICIPANTS

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## CONFERENCE CALL PARTICIPANTS

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**Stellan Hellstrom** *Nordea - Analyst*

**Anders Hansson** *Danske Bank - Analyst*

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## PRESENTATION

### Operator

Good afternoon, ladies and gentlemen, and welcome to the Interim Report January to March 2012. (Operator Instructions). Just to remind you, this conference call is being recorded.

I would now like to hand over to the chairperson, Mr. Emmett Harrison. Please, begin your meeting, and I'll be standing by.

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### Emmett Harrison - *Swedish Match AB - SVP Corporate Communications and Sustainability*

Good afternoon. This is Emmett Harrison, Senior Vice President of Corporate Communications and Sustainability. Welcome to the first quarter 2012 results telephone conference for Swedish Match.

Lars Dahlgren, President and Chief Executive Officer is joined today by Joachim Tilly, Chief Financial Officer, and myself. The conference call should last about an hour and will include an overview by Lars Dahlgren and a review of the financials from Joachim Tilly. A question and answer period will follow. A shortened version of our investor kit accompanies this presentation via Webcast, and a complete investor kit is available in the Investor Relations section of our Website at SwedishMatch.com.

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

The conference call is being recorded, and the recording will be published on the Swedish Match Website.



I would now like to turn the conference call over to Lars Dahlgren.

**Lars Dahlgren** - *Swedish Match AB - President and CEO*

Before going into the results for the first quarter, I'd like to mention that, at the annual meeting held May 2, shareholders approved an increased dividend to SEK6.50 per share, an increase of 18% for prior year. Shareholders also approved the cancellation of 7 million shares and renewed the share buyback mandate. More information about the annual general meeting can be found on our Website.

For the first quarter of 2012, Swedish Match delivered strong sales and operating profit growth, driven by solid performance for other tobacco products and Scandinavian snus. Our operating profit for the first quarter increased to SEK972 million, up from SEK793 million in the previous year, an increase of 23%. In local currencies, the increase was 21%. Excluding share of net profit from STG, our operating profit increased by 24% and by 22% in local currencies.

Sales for the first quarter increased by 10% to SEK2.917 billion, up from SEK2.646 billion in the previous year. In local currencies, the increase was 9%.

Basic earnings per share for the first quarter amounted to SEK3.27, an increase from SEK2.50 in the first quarter last year.

Scandinavia snus sales were up by 15% in the first quarter versus last year. Shipment volumes in Scandinavia were flat in the first quarter, and underlying volumes, backing out hoarding and shipment timing effects around Easter, are estimated to have been up by 1%.

First quarter operating profit and operating margin in Scandinavia increased versus the same quarter prior year.

In Sweden, according to Nielsen, our market share for snus in value terms was 83.4% in the four-week period ending March 25, compared with 83.7% for the preceding four-week period and 86.9% in the corresponding four-week period last year. Our market share in volume terms was 79.3%, compared to 79.6% in the previous four-week period and 84.9% in the corresponding period last year.

For the four-week period ending March 25, Swedish Match had a volume share of approximately 96% full-price segment and 46.6% of the value segment. The value segment accounts for approximately 34% of the Swedish market, the number of cans up from approximately 26% in the corresponding period last year. Kaliber, our newest brand of value-priced snus on the Swedish market has been in distribution since April 2011. Nielsen indicates that the brand has now achieved a 6.2% share of the Swedish market for the four-week period ending March 25, which means that Swedish Match has the leading position in the premium-price segment, as well as both the mid-priced and low-priced tiers of the value segment.

In Norway, our market share in value terms in the latest four-week period ending April 22, was 70.8%, compared with 71.1% in the previous period and 72.5% in the corresponding period last year. Our share of market in Norway in both value and volume terms has been relatively stable over the past eight months, supported by line expansions for both The Lab Series and the Nick and Johnny brand family. During the same eight-month period, according to Nielsen, The Lab Series has grown from 4.3% of the market to 6.8%, while Nick and Johnny has grown from 5.4% to 7.7%.

During the first quarter of 2012, we were engaged in an active schedule of new product launches, as well as packaging modifications for our snus products, in Scandinavia. In Sweden during the first quarter, we rolled out General strong white mini, mini pouches with the same strength as our large-pouch General white. We also began shipping products under the Catch brand with new, updated packaging design. We also continued our ongoing program of offering Catch in a limited edition variety.

As a follow-up for our summer edition of Goteborgs Rape, we offered a limited-order edition of the brand tied to the peak skiing season. In Norway, we launched a new line extension to our Nick and Johnny brand called Radical Red. Initial consumer response has been positive. We also introduced General long strong in a limited distribution, and we go nationwide for this line expansion during the month of May. In May, we have a number of new line expansions entering the market, including the Goteborgs Rape line in Sweden and, in Norway, General in a normal, white, extra strong

and General white mini. Our General Long Green Harvest, which is made from organically grown tobacco, has also been introduced on the Norwegian market.

In the US market, snuff and snus revenues in the first quarter were flat versus the year ago, despite somewhat lower shipment volumes. Operating profit in the US during the first quarter was in line with prior year, as improved profitability in the US moist snuff business offset increased investments behind snus in the US. Over the past 12 months, we have stepped up our investments for Swedish snus in the US significantly.

Nielsen reported the overall US snuff market to have been up by 6.7% for the year-to-date period ending April 14 and Swedish Match volume down by 8.2%. Our analysis suggests that real consumption of Swedish Match brands have done somewhat better than that. It goes by SKU in the Nielsen sample. Nielsen reports growth of our low-priced brand Longhorn whilst declines for the rest of the portfolio.

In the most recent isolated four-week period ending April 14, Swedish Match market share was 9.7% according to Nielsen. Market growth is continuing, with four-week market growth according to Nielsen at 8.7% in the most recent period.

This month, we are introducing new packaging for US moist snuff pouch products -- the discreet disposal lid, offering added value and differentiation for our pouch product versus competition.

Swedish Match will continue to invest behind its snus program in the US with General snus. General has experienced good and proven rotation and sales in stores. The store expansion is continuing for General snus in both the traditional round can and for our two new varieties in the rectangular can format. These new varieties were launched in broader distribution in Dallas, Chicago, Philadelphia late in the third quarter and during the fourth quarter. At the end of the first quarter, we announced that we were expanding distribution of General in seven more cities, which are New York, Los Angeles, Minneapolis, Phoenix, Denver, Nashville, and throughout the state of Ohio. With this expansion, General snus is available in around 5,000 stores in either the traditional round can or the new rectangular can, and this store count continues to grow.

As we continue to build store distribution during 2012, we will expect investments in our US snus program to be substantially higher than the year earlier.

With regard to SMPM International, the joint venture company for smoke-free products, (inaudible) tests in Canada, which includes the Toronto area, as well as Alberta and British Columbia, is showing positive signs. In late November and December, we added St. Petersburg in Russia as a test market. This test is being supported by brand-building and sampling activities, where we are testing three varieties under the premium Parliament brand. While this test is in very early stages, first signs are positive. The test market in Taiwan has not met our expectations but generated valuable learning. Activities will be phased out during the year. The current plans are to add at least one additional test market during the year.

We expect incremental investments for both the US snus expansion and for the SMPM International joint venture combined to amount to between SEK60 million and SEK100 million for the full year of 2012 versus 2011.

In other tobacco products, sales for mass market cigars in local currency were up by more than 20% versus the first quarter of 2011, and volumes increased by 36%. Shipment growth due to continued volume and share gains for the White Owl assortment, including our White Owl Sweets and our new White Owl Silver cigars. We also had solid gains for our Garcia y Vega and Game small cigar assortment, our natural, rough-cut cigars. During the quarter, we gained market share. Overall volume share for Swedish Match in the US market, excluding little cigars, was 16.1% year to date through April 14, up from 13.5% in the prior year. In the latest four-week period ending April 14, volume share reached 16.3%.

While we are confident that we will continue to outpace the market in 2012, we now expect a more modest volume growth, especially during the second quarter, as we overlap the launch of White Owl Green Sweets, which occurred in the second quarter last year. There are still significant remaining opportunities to expand distribution of the sweet cigars, as well as the more recent introductions.

In January, we launched the new unflavored variety of White Owl, White Owl Silver, which we believe has great potential to help ensure continued volume growth of this brand. Initial trade reaction to this introduction has been very positive.



In April, we brought a new product, Garcia y Vega 1882 into test markets in Florida and Pennsylvania. Garcia y Vega 1882 is a line of natural-wrapped, rough-cut cigars sold in a re-sealable foil pouch for freshness.

The chewing tobacco market share for the year-to-date period ending April 14 was 44.9% according to Nielsen versus 46.2% for the year-to-date period in 2011. In value terms, our market share is above 50%. Nielsen estimates the markets have decline by 7.6% in volume terms. For Swedish Match own brands, shipment volumes in the quarter were down by 11%, while contract manufacturing volumes were up following inventory adjustments in prior quarters.

Our lights businesses have mixed results with improved performance for lighters and somewhat weaker results for matches. Lighter volumes increased, while matches were negatively affected by both lower volume and country mix effects.

Sales in other operations for the first quarter amounted to SEK687 million, compared to SEK659 million in prior year. Operating loss for other operations was SEK19 million, compared to SEK43 million prior year. During first quarter 2011, the operating loss included redundancy costs following organizational change. Operating loss in the first quarter this year was positively affected by certain, one-time adjustments relating to divested pipe tobacco operations.

If we go on to our (inaudible) Scandinavian Tobacco Group, total Scandinavian Tobacco Group net sales for the first quarter amounted to DKK1.334 billion, up from DKK1.179 billion in the corresponding period a year ago. In local currencies, excluding Lane effects, sales increased by 5%.

EBITDA for the total Scandinavian Tobacco Group in the first quarter amounted to DKK258 million, an increase of 6% versus prior year, excluding one-time items. The first quarter of 2012 includes the Lane business for three months, while it was included only for one month in the first quarter 2011. The first quarter of 2011 also included one month of sales and EBITDA linked to cigar brands in Australia, which were divested during that quarter. On a comparable basis, EBITDA increased by 3% for total STG.

The Swedish Match general net profit from STG amounts to SEK69 million versus SEK65 a year ago.

Sales and operating profit increased for premium and mass market cigars, while sales and operating profit declined somewhat for pipe and fine-cut combined, excluding Lane. For Lane, the US domestic development was according to expectations, while export volumes were below plan.

Apart from the increased EBITDA for Scandinavian Tobacco Group, Swedish Match share of net profit was also affected by higher net financial costs and adjustments to previous year reported periods.

On April 27, Swedish Match received its first dividend of SEK204 million from Scandinavian Tobacco Group.

After that, I will hand over to Joakhim for some further comments on the financials.

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#### **Joakhim Tilly** - Swedish Match AB - CFO

For the first quarter, the development of exchange rates had a positive effect on our sales and operating profit comparisons due to a strengthening of the US dollar versus the Swedish krona versus 2011. The average rate of the dollar versus the Swedish krona has appreciated by about 4% year to date from SEK6.5 for the year to date ending March 31, 2011 to SEK6.7 for the year to date ending March 31, 2012. The translation effect on operating profit was a positive SEK14 million in the first quarter.

For the first quarter, the total translation impact on sales was a positive SEK43 million, which consists of a positive SEK27 million for other tobacco products and positive SEK16 million for traditional snuff and positive SEK1 million for lights, and zero for other operations.

Net finance costs for the first quarter amounted to SEK134 million, compared to SEK128 million previous year. The underlying increase in the finance cost was mainly a result of higher net debt and somewhat higher interest rates due to a lower share of debt with floating interest rates.

In the first quarter, share repurchases, net, of SEK230 million were made. During the first quarter, new bond loans of SEK463 million were issued. Repayment of loans for the same period amounted to SEK759 million. As at March 31, 2012, Swedish Match had SEK9.744 billion of interest-bearing debt, excluding retirement benefit obligations, compared to SEK10.038 billion at December 31, 2011. During the remainder of 2012, SEK556 million of this debt falls due for repayment.

As of March 31, 2012, Swedish Match had SEK1.415 billion in unutilized committed credit lines.

As of March 31, the average maturity duration of the bond portfolio is 3.87 years, and the average duration of the interest-binding is 3.82 years. On March 31, the weighted average interest rates on bonds issued, including derivative effects, was 4.91% with about 2% of the portfolio exposed to variations in interest rates.

In February 2012, Swedish Match issued EUR30 million of new ten-year bonds, maturing in 2022 at an all-in rate in Swedish crowns of 5%.

In April, Swedish Match issued EUR100 million of new seven-year bonds, maturing in 2019, with an all-in rate of 4.46% in Swedish crowns.

For the first quarter, the reported tax expense amounted to SEK117 million, corresponding to a tax rate of 20%. The reported tax rate, excluding profit and loss impact from associated companies and joint ventures, was approximately 22%.

Some comments on the cash flow. Cash flow from operating activities for the first quarter amounted to SEK307 million, compared with SEK523 million for the same period previous year. The main reasons for the decrease in cash flow from operations in the first quarter of 2012 compared to the same period of 2011 are higher tobacco tax payments in the first quarter relating to the trade hoarding in the Swedish trade of both snus and cigarettes at the end of prior year before the Swedish excise tax increase.

Investments in property, plant, and equipment during the first quarter amounted to SEK39 million, compared to SEK52 million for the same period of the previous year.

Net finance cost for the first quarter increased to SEK134 million.

The net debt as per March 31, 2012 amounted to SEK8.733 billion, compared to SEK8.223 billion as at March 31, 2011.

Cash and cash equivalents amounted to SEK2.226 billion at the end of the period, compared with SEK2.533 billion as of December 31, 2011.

And, as Lars already mentioned, the first dividend from STG relating to full year of 2011 of SEK204 million was paid on April 27, 2012.

During the first quarter, Swedish Match, repurchased 1.4 million shares for SEK367 million at an average price of SEK250.52, following authorization from the annual general meeting held in 2011. During the first quarter, the Company sold 0.9 million treasury shares at an average price of SEK144.71, totaling SEK137 million, as a result of option holders exercising options.

As per March 31, 2012, Swedish Match held 9.3 million shares, corresponding to 4.39% of the total number of shares. The number of shares outstanding, net, as per March 31, 2012, amounted to SEK203.7 million. In April 2012, a further 123,000 shares have been repurchased for SEK33 million at an average price of SEK267.66.

At the annual general meeting, shareholders authorized the cancellation of 7 million shares currently held in treasury. When the cancellation is completed, the total number of registered shares in the Company will amount to 206 million shares.

At the annual general meeting, shareholders also approved a renewed mandate to repurchase shares up to a holding in treasury not exceeding 10% of the number of registered shares in the Company until the next annual general meeting in 2013.



The net debt was SEK8.7 billion as per March 31. The net debt generation to EBITDA, excluding share of profit in STG, was 2.4 for the 12-month period ending March 31, 2012.

And I will now turn the conference call over to Lars.

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

And I will turn it over to the operator, and we can open the floor to questions and answers.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions). Andreas Lundberg.

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**Andreas Lundberg** - *ABG Sundal Collier - Analyst*

I have a question on STG. It seems that you have a positive adjustment for DKK17 million for the full entity. Does this mean that Q4 should have been stronger than Q1, lower than reported? That's the first question.

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**Joakhim Tilly** - *Swedish Match AB - CFO*

For Q1, there's (technical difficulties) lower. That's clear. The DKK17 million in adjustments comes from the prior period. For Q4, there was a little, similar adjustment also coming from the Q3. So it's a very small effect on Q4, isolated, actually.

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**Andreas Lundberg** - *ABG Sundal Collier - Analyst*

Okay. Thank you. And, just to get some more color here on the drivers, because, if you add or subtract that back, you will get earnings decline year on year in STG in the first quarter. That's correct. Right?

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

In terms of EBITDA on a comparable basis, it was up 3%. And then the financial, net, is (inaudible).

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**Andreas Lundberg** - *ABG Sundal Collier - Analyst*

Okay. But, if you add or subtract those positive adjustments in the first quarter, earnings would have been down year on year. Is that correct?

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**Joakhim Tilly** - *Swedish Match AB - CFO*

Well, if you look -- as we have said, the comparable EBITDA increased slightly, but then that was offset by higher net financial costs. That increase in the financial cost has to do with the increase in loans due to the Lane acquisition last year and also due to the fact that they were a bridge finance for a very large part of the first quarter last year. So the interest rates have gone up. And we also have a higher net debt.



**Andreas Lundberg** - *ABG Sundal Collier - Analyst*

Okay. So the 3% increase in EBITDA is adjusted for this positive adjustment. Is that correct?

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

Yes.

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**Joakhim Tilly** - *Swedish Match AB - CFO*

Yes.

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**Andreas Lundberg** - *ABG Sundal Collier - Analyst*

Okay. Thanks. They were all my questions.

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**Operator**

Jon Fell.

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**Jon Fell** - *Deutsche Bank - Analyst*

A couple of questions on snuff. Firstly, could you give us a bit more feel for your underlying volume performance in Norway? You talk in the statement about strong shipment volumes to Norway in the quarter. Does that imply that you shipped a bit ahead of what your consumer off-take was, or was it actually a normal figure that you shipped to Norway this quarter?

And then, on US pricing, flat sales, volumes down (inaudible). Your net price mix was up [4]. Could you talk us through a little bit the dynamics there in terms of your actual price increases, negative mix, and any shifts in discounting that happened versus last year? Thanks.

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

I'll start off with Norway, and then Emmett can begin on the US side.

Yes. We did have higher shipments than the underlying performance into the Norwegian markets. This is -- there are natural timing differences. And then the hoarding effects have actually worked the opposite way for Sweden and Norway. In Sweden, we had hoarding at the end of last year, and we had unusually low shipments to the Swedish markets, whilst, Norway, we had a hoarding at the end of 2010, which resulted in an unusually weak first quarter of 2011. So, on a comparable basis, that means that the shipment growth to Norway is clearly higher than the overall market or our consumption.

And, when it comes to Nielsen, for the year-to-date period, do you remember, Emmett, what it is, because we just got the most recent data for Norway. But it's well above 10% year to date for the category. And, as you know, we have also limited market share, but it's been fairly stable the last eight months. But that means that we are not quite up to the category growth on the consumption level, but, still, very healthy growth for Swedish (inaudible) product in the Norwegian market during the first quarter (inaudible).

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**Emmett Harrison** - *Swedish Match AB - SVP Corporate Communications and Sustainability*

And I will get the volume growth rate for Norway in just a moment.



**Jon Fell** - Deutsche Bank - Analyst

Could you remind us also, while that's happening, roughly what sort of proportion of your Scandinavian volumes Norway is now?

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**Lars Dahlgren** - Swedish Match AB - President and CEO

Roughly 15%.

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**Jon Fell** - Deutsche Bank - Analyst

15%. Okay.

(multiple speakers)

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**Emmett Harrison** - Swedish Match AB - SVP Corporate Communications and Sustainability

The other thing on the Norwegian market -- you have to remember that last year, the first half of the year, there was a destocking of warehouse inventories from our old distribution system that we had versus, this year, we are shipping directly from our factories out to the Norwegian market. So that also impacted the year-on-year volume growth numbers for Norway versus prior year. So there was a double effect there.

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**Jon Fell** - Deutsche Bank - Analyst

Okay.

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**Emmett Harrison** - Swedish Match AB - SVP Corporate Communications and Sustainability

I don't see the Norwegian market growth number right in front of me, but, as I recall, it was well above 10%.

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**Jon Fell** - Deutsche Bank - Analyst

That will do. Thanks.

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**Operator**

Stellan Hellstrom.

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**Stellan Hellstrom** - Nordea - Analyst

Just a question, first, on the Kaliber now that you have some 6% volume share. I'm just wondering where you see the potential here, given that you had more limited distribution. I know (inaudible) peaked at 13% volume share. I guess that's not really what can be achieved with Kaliber. What do you think?

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**Lars Dahlgren** - Swedish Match AB - President and CEO

We will have to wait and see and assess the market dynamics. But the important thing for us, which we've been fairly clear about this, but we are the biggest player in all price segments in the Swedish markets. So we offer very competitive and good, high-quality products for all consumers. Now, according to the latest Nielsen measures, we are the biggest in premium, of course, but then also in the mid-price and in the low-price segments. It depends a little bit on the market dynamics and how the overall value segment is going to develop going forward.

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**Stellan Hellstrom** - Nordea - Analyst

From what you see now, are you planning on increasing distributions?

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**Lars Dahlgren** - Swedish Match AB - President and CEO

Right now, I'd say, based on the current market dynamics, we don't see a need to increase distribution for Kaliber. That can be give or take some additions and some delistings and so forth. We are definitely well in line with our objectives when it comes to Kaliber. It's going the right way.

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**Stellan Hellstrom** - Nordea - Analyst

Also a question on your cost increases for your initiatives on snus, if you can give some idea on the phasing of your costs in the next few quarters.

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**Lars Dahlgren** - Swedish Match AB - President and CEO

Yes, I will, because you should be aware that, in the first quarter, it was a fairly low increase. It was below SEK10 million. So we secured a lot of new distribution in the US in these seven new cities. But we actually haven't started supporting (inaudible) in that aspect in the second quarter. So we still stand by our, as was said, the full-year estimates of SEK60 million to SEK100 million in additional international snus spending. But, while the delta was very small in the first quarter, it will be substantially higher in the second quarter.

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**Stellan Hellstrom** - Nordea - Analyst

Great. Thanks. Also, finally, on STG, coming back to that, and the 3% increase in comparable EBITDA, I was under the impression that you saw at least some synergies coming in this year as well. I'm just wondering if there some to expect further on or if that's sort of offset by weak market fundamentals.

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**Lars Dahlgren** - Swedish Match AB - President and CEO

What we have said about STG is that we estimate realized synergies in 2011 to EUR17 million, and we estimate it is around EUR20 million for the full year 2012.

And, when it comes to the relatively modest comparable EBITDA growth, you should be aware of -- when it comes to Scandinavian Tobacco Group stats, this is a combination of a lot of businesses that actually are light in the first quarter. In our premium -- our former premium cigar business and European cigar businesses, they are all businesses that have a relatively little proportion of their sales in the first quarter.

So we definitely expect improved run rate, so to say, of the operating profit and EBITDA going forward for the remainder of the year because this is a relatively light quarter, in combination with some investments that we have done on the central side, like, for example, a new ERP system for the consolidated unit that has driven some costs. That means that the overall EBITDA comparison is not that impressive.



**Stellan Hellstrom** - *Nordea - Analyst*

Okay.Thanks.

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**Operator**

Anders Hansson.

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**Anders Hansson** - *Danske Bank - Analyst*

The first one, coming back to STG, where sales up 5%, underlying EBITDA up 3%. As you were talking about the synergies you took out in 2011, is it just that you've driven some costs? Or what has happened to underlying margins in European cigars, for example?

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

As I just explained, it's a combination of -- the European cigars have increased profit. The premium cigars have increased profit. And, in the combination of fine, custom pipe tobacco, there is a slight decline but not a material one. And then, given that there are some higher central costs, that's why the EBITDA comparison is up by 3%.

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**Anders Hansson** - *Danske Bank - Analyst*

Yes. But one could assume, given that all the synergies you took out in 2011, profits are up in European cigars, for example. If that is purely driven by synergies, what's happened to -- ? What's your take on gross margin

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

In the European cigars, it's synergy-driven. In premium cigars, there are some synergies, but, actually, the main source there is volume growth, where the market has done better in the first quarter.

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**Anders Hansson** - *Danske Bank - Analyst*

Okay. Thanks. One other thing, on mass market cigars, where you're more positive on full-year volumes. Is that just because Q1 was so great or because you have a big portfolio coming with further product launches during the rest of the year? Why a more positive now compared to after Q4?

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

We were fairly positive after Q4 as well. Now we're three months into the year, and we know a little bit more. And, as we explained, the recent introductions, like the White Owl Silver, have performed very well. So we have been positive all along. But we know more, and maybe we're a little bit more positive now.

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**Anders Hansson** - *Danske Bank - Analyst*

Okay.Thanks. One final one, which I may have missed. Did you explain the unusually high negative net working capital in Q1?

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**Joakhim Tilly** - *Swedish Match AB - CFO*

As I said when I mentioned the cash flow for the quarter, the reason is that we had very high tobacco tax payments in Q1, since there was a hoarding of both snus and cigarettes in Q4 last year.

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**Anders Hansson** - *Danske Bank - Analyst*

Yes. Sorry I missed that. Thanks.

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**Operator**

Peter Wallin.

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**Peter Wallin** - *Handelsbanken - Analyst*

I have a follow-up question on US mass market cigars in terms of what we should be expecting in the relationship between volumes and sales growth for the coming quarters, since this quarter, again, we had a fairly large discrepancy between volumes and sales.

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

Yes. I think you should expect that there will be an element of a mix shift, and these new introductions are supported by promotions. So it's wise to expect a little bit stronger volume growth than net revenue growth.

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**Peter Wallin** - *Handelsbanken - Analyst*

Okay. Thank you. And then, going to another area, which also has been discussed fairly much already, STG. And you've now received your first, at least, technically, formal dividend. Just to see that I have understood things correctly, they are supposed to pay dividends twice per year. Could you give an indication of whether you think that, if things develop according to what you see right now, that you will see an equally large or potentially larger dividend in the second half of this year?

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

I think we -- when it comes to dividends from STG, the important thing is to understand the dividend policy, which stipulates that, normally, the minimum dividend is two-thirds of the net profit.

But, then, as you recall, we also have a financial policy of STG that regulates that they should maintain a net debt in relation to the EBITDA of below three times -- between two and three times, which means that any excess free cash flow -- and, of course, there could be some timing there, but the dividend is used to regulate the capital structure within that agreed range.

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**Peter Wallin** - *Handelsbanken - Analyst*

Okay. And then, also, following up in terms of this comparable EBITDA growth of 3% in the quarter, you also said in your report that, to some extent, STG's earnings have suffered from the strike during the quarter also on the introduction of the smoking ban in Belgium. Did the strike, for example -- ? Was that impact material, or was it, basically, just having a fairly small, negative

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

I'm able to say it's material. European volumes were down by around 3%. And then the weighted average of the markets, as far as we can read, was down more. So it took market share -- STG took market share in those key markets. And a very rough assessment is that 1 percentage point of that 3% decline was attributable to inability to deliver during a short period.

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**Peter Wallin** - *Handelsbanken - Analyst*

Okay. Thank you very much. And then just a final, more of a big-picture question. Just if you have any comment on -- well, a week ago or slightly more, we had some headlines on the British tabloids regarding the coming European new tobacco directive and, potentially, that the ban of flavor additives also impacting snus or snuff. Do you have any kind of color to give on that?

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

Once again, (inaudible) told us that -- she said it was a tabloid that published this. And there is no official proposal out there yet from the European Commission. But everybody knows that packaging and ingredients are part of the options that the European Commission is thinking of regulating. And, since (inaudible) is also a topic, it could potentially spill over effects to the smoke-free market.

But, as you saw, being in Sweden, the Swedish politicians very firmly expressed their standpoint in terms of defending the Swedish snus product in the Swedish market, especially in view that the product is banned in the rest of the European Union. It would be a little bit absurd to have any regulation affecting a product that can't move freely in the market. And, also, the public reaction has been of such magnitude that I am pretty sure that it has reached the ears of the Commission.

This is where we cannot neglect -- the regulatory development is a little bit unclear, so we cannot neglect that that's a risk. But we would be very surprised if there will still be a regulation to the core Swedish snus portfolio.

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**Peter Wallin** - *Handelsbanken - Analyst*

Okay. Well, thank you very much. That's all for me.

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**Operator**

Daniel Ovin.

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**Daniel Ovin** - *Chevreux - Analyst*

I have a question on the price increases in Scandinavia in the first quarter. They were a little bit higher than what I expected. I just wonder how I should think of this for the rest of the year. Is there is any reason to expect that it would drop in the second quarter? Or should we assume it's going lower and then not assume a drop off from the second half? Or how should we think about the price increases?

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

There are quite a few dynamic pieces in there, and one of them actually being the first question addressed there on the Norwegian shipment. Norway is a high-cost country with also high -- somewhat higher snus prices than in Sweden. So Norway, being a relatively larger part of the overall shipment portfolio, brings up the average price.



And then you need to remember that we had a price adjustment in the Swedish market in early June last year and one in the first of January this year, which means that, for the first quarter, on a comparable basis, you see the effect of two price adjustments. And that will not be fully the same effect in the second quarter and beyond that. There is only one of those changes on a comparable basis, assuming things still remain unchanged. And there is a similar effect in the Norwegian market, with a month difference you can say.

So the relatively strong price/mix component of 15% in the first quarter -- you should expect that to be lower in the second quarter and going forward.

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**Daniel Ovin** - *Chevreurx - Analyst*

Okay. Thank you. And then just one final question on the mass market cigars. I wonder if you can give some indication of how much of that strong volume growth, 36%, was driven by the new launch of the White Owl Silver product.

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**Emmett Harrison** - *Swedish Match AB - SVP Corporate Communications and Sustainability*

It's partly with the White Owl Silver cigar, but we also had continued strength and growth of the sweet cigars, both the original sweets that we launched nearly two years but also the green sweets that we launched last year. We also had a small product launch that we had announced, the 1882. That's a fairly small number. But it really was a combination of the Silver, which did very well, along with the expansion of sweets, both continued consumption growth and some more distribution gains there.

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**Daniel Ovin** - *Chevreurx - Analyst*

Okay. That's all for me. Thank you.

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**Operator**

David Hayes.

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**David Hayes** - *Nomura - Analyst*

Just picking up on the front page of the release, you made, for the first time, I think, the point about the promising activities in the joint venture in Canada and Russia. I just wonder whether you can sort of say whether that was deliberately put in there because you are seeing some real traction in those test markets.

And then, related to that, I just wonder whether you could remind us of what sort of costs you'll incur in your share of that for this year. Thanks very much.

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

We deliberately put it in there because we wanted to communicate it. I don't know if it's the first time. I think I've been saying the same type of thing in investor meetings, because we remain encouraged with the early signs from Canada and Russia.

Having said that, you need to remember that it's still a very small-scale, test launch. It's been in, roughly, 600 stores in Canada. And we're in, roughly, 200 stores in the St. Petersburg area. But early signs are positive.



But then, on the other hand, as we -- as I spoke about, we decided to phase out the test market in Taiwan. So this is the nature of having several test markets ongoing at the same time.

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**Joakim Tilly** - *Swedish Match AB - CFO*

And, on the spend, when we talk about SEK60 million to SEK100 million to span for the full year incrementally, that includes both the JV with PMI and the US. A substantial part of that, though, is for the US market.

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**David Hayes** - *Nomura - Analyst*

That's great. Thank you very much.

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**Operator**

Adam Spielman.

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**Adam Spielman** - *Citigroup - Analyst*

I'm interested to find out if there has been any decline in your premium snus brand in Sweden following the -- basically, following the price rise in Sweden. Any light you can give on that, please?

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

As you know, we talk about the entire Scandinavia because of the moving pieces. But, basically, what I said before. It's clear that Norway grew very strongly, and Sweden declined, partly related to the hoarding. So it's hard to get an exact read on only three months around the yearend. But, yes, we have a decline in our full-priced portfolio. And Nielsen also reports that there is a slight decline of the full-priced brands (inaudible).

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**Adam Spielman** - *Citigroup - Analyst*

And, if you look at the Nielsen, because I'm more interested in consumer off-take than sort of worrying about the hoarding effects, are we talking about 1% or 2% decline in the full-priced brands, or are we talking something more substantial than that.

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

The issue with Nielsen is that Nielsen reports 6% growth for the entire market for the first three months, 6.4%. But I don't believe that. That is overstating the market growth. There are swings in Nielsen. And I think the number in Nielsen -- if I recall, the number, I think, is 3% down for full-priced brands or something like that.

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**Unidentified Participant**

(Inaudible).



**Lars Dahlgren** - *Swedish Match AB - President and CEO*

Like I said, you have to take those -- there are swings in the Nielsen data, so you have to take those numbers with a little bit grain of salt and look for longer periods.

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**Adam Spielman** - *Citigroup - Analyst*

Okay. Thank you.

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**Operator**

(Operator Instructions). James Bushnell.

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**James Bushnell** - *Exane BNP Paribas - Analyst*

I have two questions, please. The first, and this has already been skirted around a fair bit, but I'll try anyway. On the price mix in Sweden -- obviously, it's 15% for Scandinavian snus overall. I just wondered what that number would be like for Sweden. I think you had maybe a gross increase of around 15%. I'm just interested as to how much that was offset by negative mix and/or discounting. That's question one.

And my second question is -- you mentioned some one-offs in your other operations segment, both in the prior year and the current quarter. I wondered if you could just give us some numbers around those, so we can get a feel for the actual year-on-year impact and, therefore, the underlying performance. Thank you.

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**Emmett Harrison** - *Swedish Match AB - SVP Corporate Communications and Sustainability*

Of the 15% price/mix effect, a few percentage points of that, actually, is the Norwegian effect, which is fairly big. You have to recall that, this year, in the first quarter, we had the regular Norwegian shipment volumes plus a little restocking effect. And then, last year in the first quarter, there was less shipments than the consumption going on because of a destocking effect.

On the Swedish market, you have a price/mix effect because of the growth of Kaliber relative to the full-priced products. So I think you can take that 15% and drop it down by a few percentage points. We won't give specifics on country by country.

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**Joakhim Tilly** - *Swedish Match AB - CFO*

On the second question on one-time in other operations, the delta between the quarters is about [SEK15 million] in one-timers.

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**James Bushnell** - *Exane BNP Paribas - Analyst*

[SEK15 million]?

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**Joakhim Tilly** - *Swedish Match AB - CFO*

Yes.





**James Bushnell** - *Exane BNP Paribas - Analyst*

Okay. Thank you very much.

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**Operator**

Toby McCullagh:

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**Toby McCullagh** - *Morgan Stanley - Analyst*

Just two quick questions. One is a clarification, really. On the incremental snus investment of SEK60 million to SEK100 million that you have talked about, could you just give us an indication of how that ought to be -- how we ought to think that's going to flow through the year?

And the second question is just on your US moist snuff business. Obviously, that's continuing to suffer from negative mix and (inaudible) market share. I wonder if you could just maybe give us an update on how you're trying to -- what your ambition is for that or what your strategy is to turn that around. Thanks.

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**Lars Dahlgren** - *Swedish Match AB - President and CEO*

On the snus spending, as I said, it's just below SEK10 million increase in the first quarter, so it is going to be substantially higher. And then the timing can, of course, vary a little bit on exactly when the planned activities take place and so forth. But, as it looks now, the delta might actually be the biggest during the second quarter. We should expect a substantial increase over prior year in terms of snus spending in the second quarter.

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**Emmett Harrison** - *Swedish Match AB - SVP Corporate Communications and Sustainability*

And on the US moist snuff side for market share, the Nielsen numbers are showing around 9.7% share of market the latest four-week period; I think, 9.9% year to date. They are showing volume declines that we think are a little bit more dramatic than our actual volume decline, partly just because of the way Nielsen reads the numbers and expands them out totally. We tend to do a little bit better in some of the stores that they might be under-representing a little bit.

We also have a little bit of difficulty against Nielsen because we're selling Longhorn in tubs, which, we talked about in the previous quarterly report. Each tub has about 12 cans worth of product in it. So, if someone were to buy two less cans of Longhorn and buy one tub, Nielsen would show that as a volume decline and a share decline, and we would have an extra 11 cans of sales for it. So it makes it a little bit tough.

Some of the things that we're doing? Longhorn tubs that I talked about. Also, we mentioned, for our pouch products for all of our brands in the US, we are introducing a product improvement, which is a disposal lid on the product, which is new for pouch products and should differentiate us against the competition. It is a very competitive market in the US. But we did see already in the first quarter, even though we had a volume decline of around 4%, our sales were flat. Our operating profits were up only looking at moist snuff business.

So it's managing our product portfolio, as well as our marketing mix, in order to have good profitability in that business.

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**Toby McCullagh** - *Morgan Stanley - Analyst*

Okay. That's helpful. And with the effect of positive pricing, do you think that's down to the sort of innovations and the things that you're doing, or is it a change in the degree of discounting in the quarter?



**Lars Dahlgren** - *Swedish Match AB - President and CEO*

There are some timings on the promotional schedules that always can affect the comparison in short phases. You remember we had to pull back -- although we disagree with FDA, we had to pull back on some of the promotions on Timber Wolf products. We had a fairly low amount of promotions in the quarter.

**Toby McCullagh** - *Morgan Stanley - Analyst*

Okay. That's great. Thanks very much.

**Operator**

And we appear to have no further questions.

**Lars Dahlgren** - *Swedish Match AB - President and CEO*

Okay. Then I'd just like to, finally, inform everybody that the release of our first half results will be on July 20. Thank you very much.

**Operator**

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

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