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Project Star

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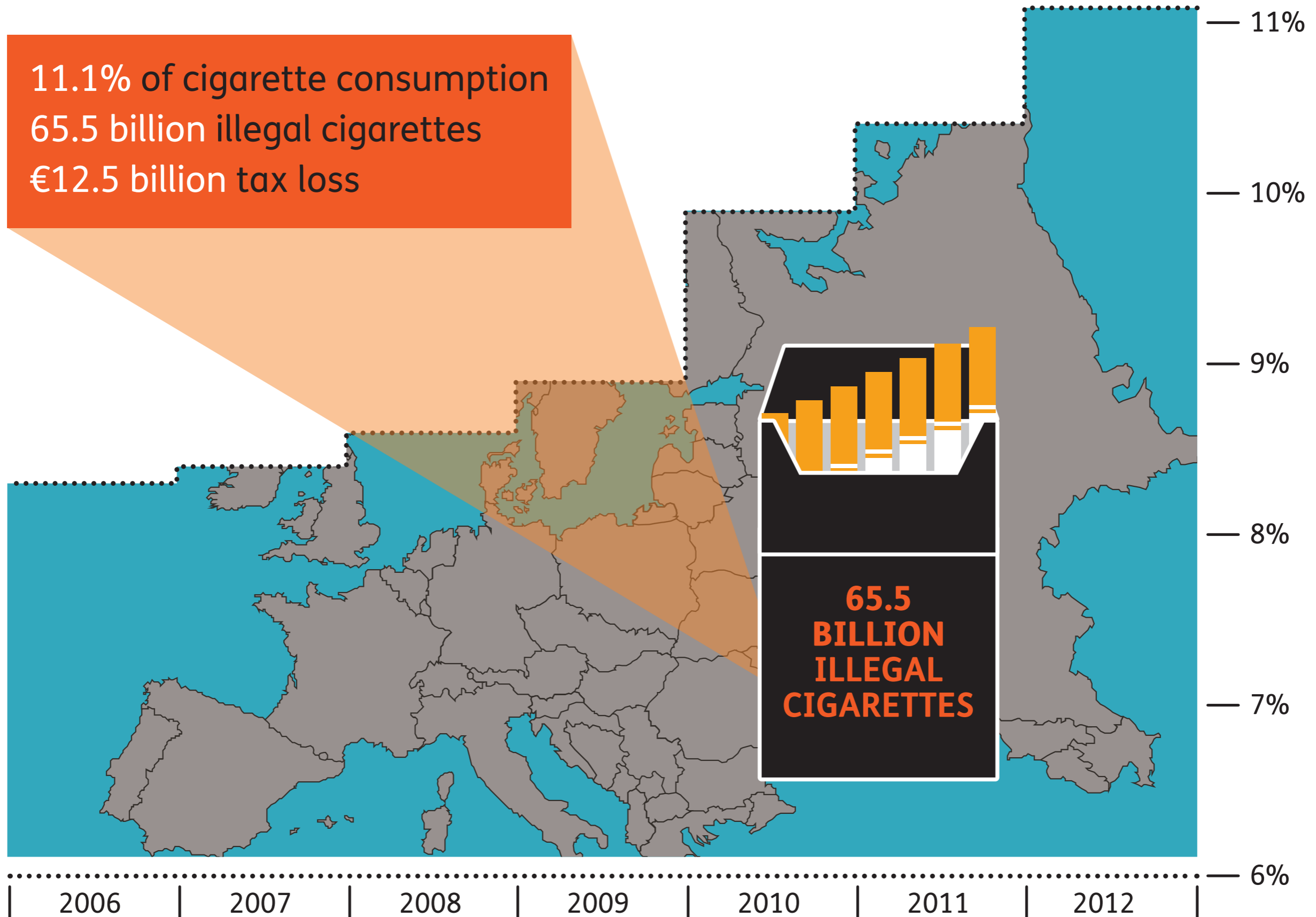
KPMG Baltics OÜ

Maksu- ja õigusteenuste
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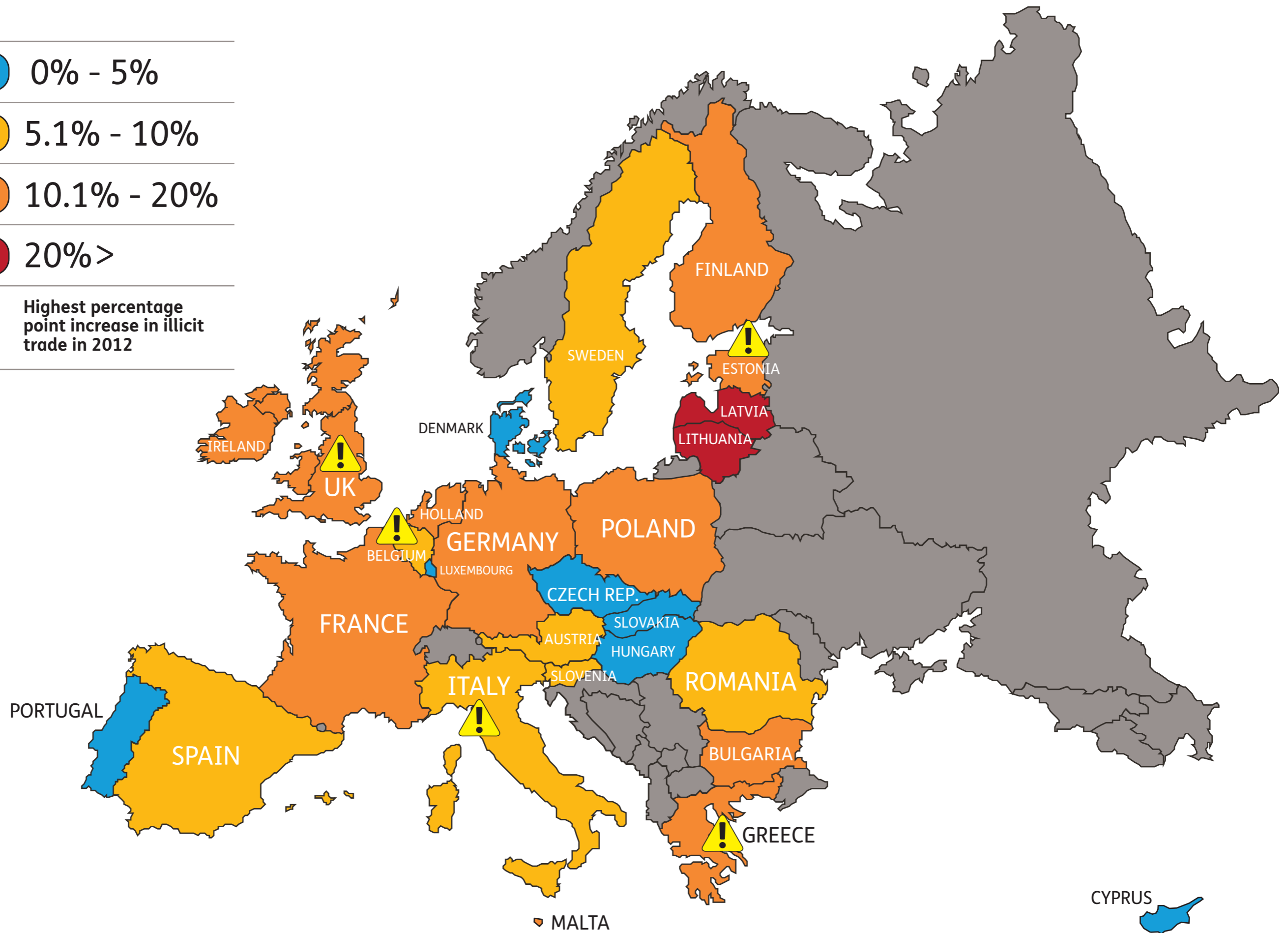
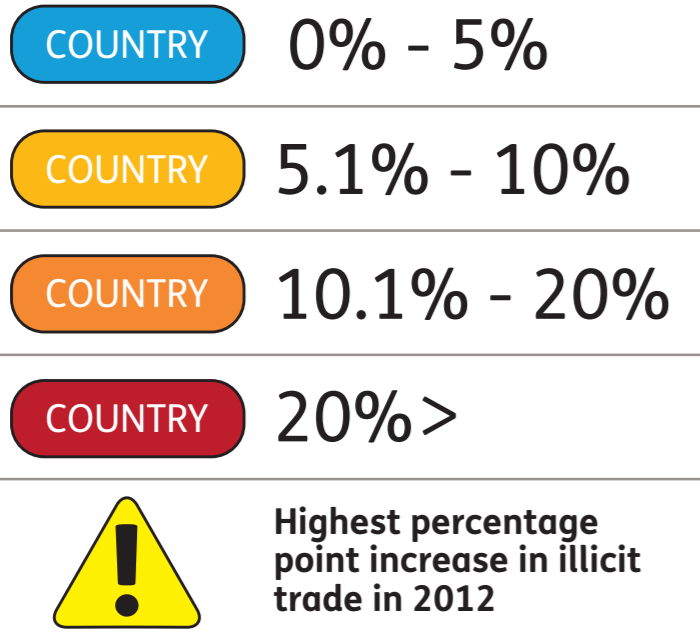
21 mai 2013



EU 27 - Illegal Cigarettes Reached Record Levels in 2012



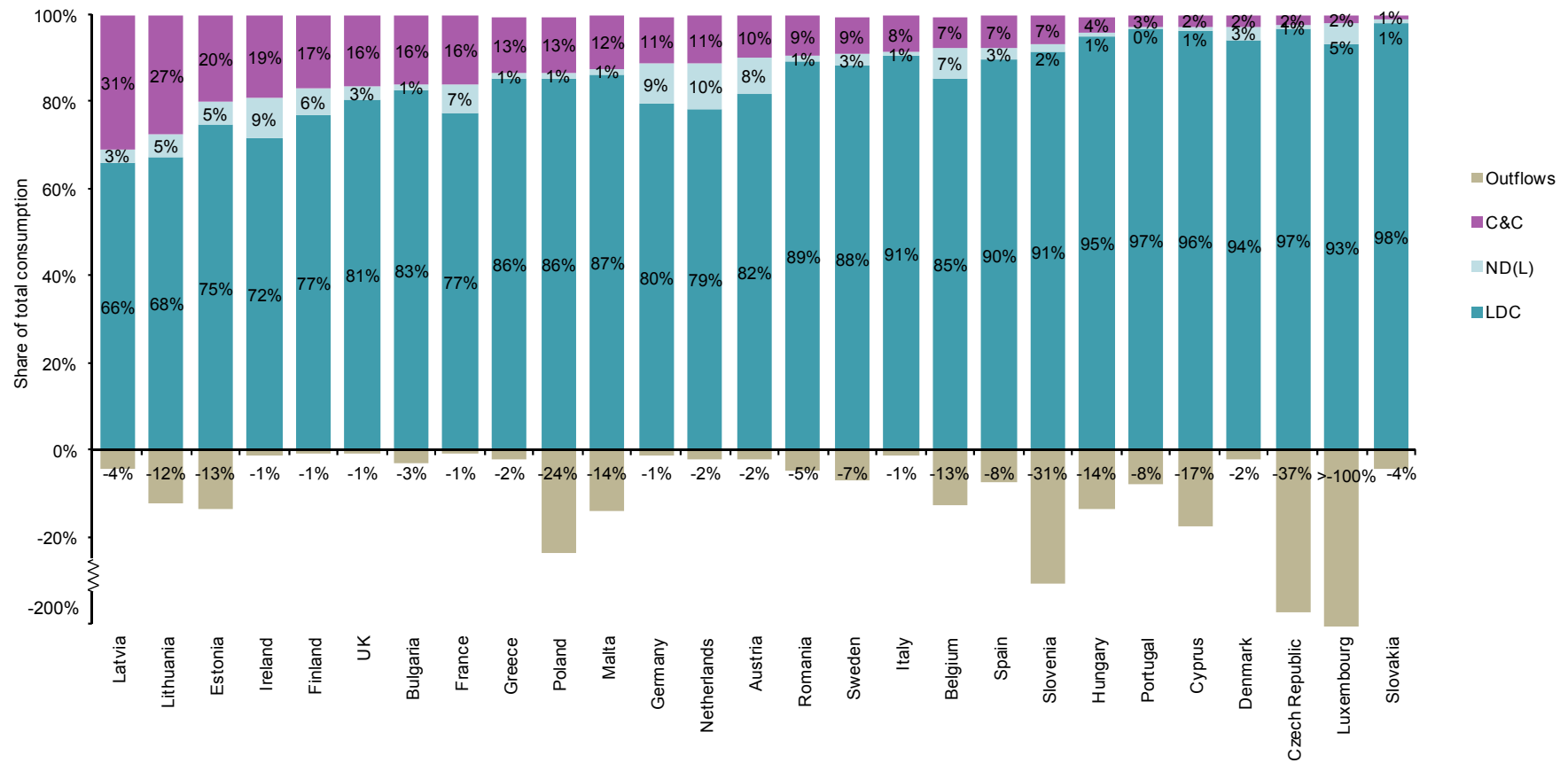
EU 27 - Illegal Tobacco Hotspots in 2012



EU total consumption

The Baltic countries had the highest non-domestic and C&C incidence as a proportion of total cigarette consumption

Total cigarette consumption by type 2012⁽¹⁾



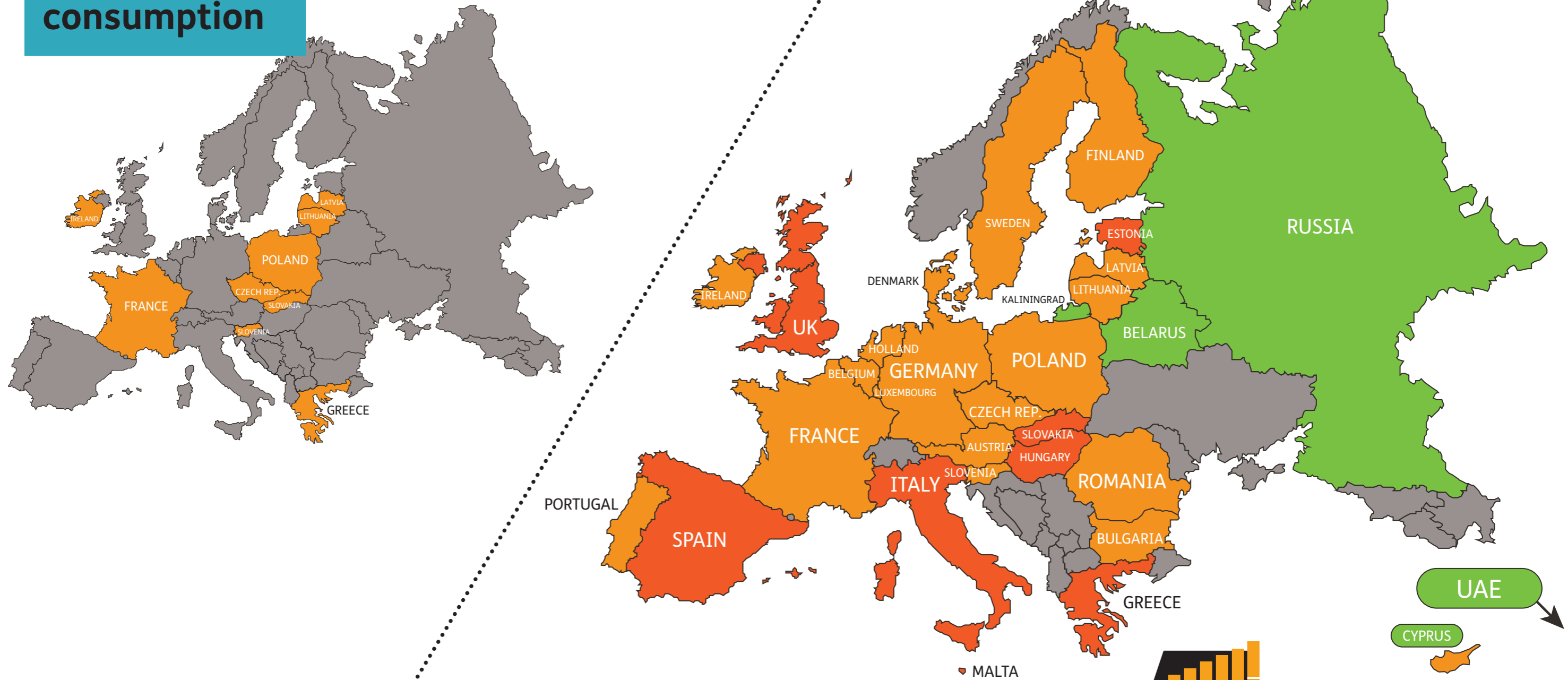
Source: (1) KPMG analysis based on EPS, LDS and ND(L) research

EU 27 - The Presence of Illicit Whites in the EU

2006

2012

2.4% of C&C consumption



- COUNTRY The presence of illicit whites in the EU
- COUNTRY Strong growth markets for illicit whites in 2012 (>30%)
- COUNTRY Main source countries of illicit whites

16.0 BILLION ILICIT WHITES IN THE EU

24.3% of C&C consumption

Source: KPMG Project STAR 2012
 C&C: Counterfeit & Contraband
 Illicit Whites: Cigarettes that are manufactured for the sole purpose of being smuggled into and sold illegally in another country

Executive summary

Project Star 2012 headlines

<p>Although manufactured cigarette consumption declined in the EU in 2012, C&C and ND(L) increased</p>	<p>Cigarette consumption declined by 5.7% to 593 billion cigarettes in the EU 27</p> <ul style="list-style-type: none"> Germany and Italy were the largest consumption markets at 103 billion and 86 billion cigarettes respectively The six largest consumption markets in the EU 27 represented over 69% of total consumption <p>C&C and ND(L) both increased in 2012, both in absolute terms and as a proportion of consumption</p> <ul style="list-style-type: none"> C&C increased by 0.4% in 2012 to 65.5 billion cigarettes and grew by 0.7 percentage points as a proportion of total consumption. If these cigarettes had been sold legally in the countries where they were identified, the tax revenue would have been worth approximately €12.5 billion ND(L) increased in 2012 for the first time since the study was initiated, by 6.5% to 24.8 billion cigarettes and grew by 0.5 percentage points as a proportion of total consumption
<p>Prices continued to rise within the EU, whilst Eastern border countries remained significantly cheaper</p>	<p>There continues to be a wide range of prices across the EU 27 countries, although prices generally increased across the majority of markets</p> <ul style="list-style-type: none"> Prices increased in Euro terms in 24 of the 27 Member States in 2012, with increases of over 5% in 13 countries The price of a pack of Marlboro varies widely across the EU, from €2.61 in Bulgaria to €9.54 in the UK; the UK experienced the biggest growth in C&C in 2012 across the EU 27 at 6.4 percentage points Prices in non-EU countries at the Eastern borders remain significantly lower; the price of a pack of premium brand cigarettes in the major source countries of Belarus, Russia and Ukraine are €1.08, €1.71 and €1.31 respectively
<p>OTP sales continued to increase, growing by 6.8% from 2011 to 2012</p>	<p>Legal domestic sales of OTP have increased every year since 2008, offsetting some of the decline in manufactured cigarette consumption</p> <ul style="list-style-type: none"> Legal domestic sales of OTP have grown at an annual growth rate of 11.4% from 2008 to 2012, reaching 145 billion cigarette equivalents, whilst legal domestic sales of manufactured cigarettes declined at an annual growth rate of 4.8% over the same period, to 540 billion sticks Price gaps between OTP and manufactured cigarettes continue to grow and range from €1.05 in Greece to €4.23 in the UK OTP represents the largest share of tobacco consumption in the Benelux markets
<p>Growth in Illicit White brands has predominantly been driven by emerging brands originating in Belarus</p>	<p>Consumption of Illicit White brands increased by 3% to 16 billion sticks in 2012, representing over 24% of total C&C volumes in the EU</p> <ul style="list-style-type: none"> The share of the three major established Illicit White brands of Classic, Jin Ling and American Legend has fallen as a proportion of total Illicit White sales, from 76% in 2009 to 33% in 2012, as the emerging Illicit White brands have gained share The largest source country for emerging Illicit White brands in 2012 was Belarus



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Estonia

Estonia – Consumption summary

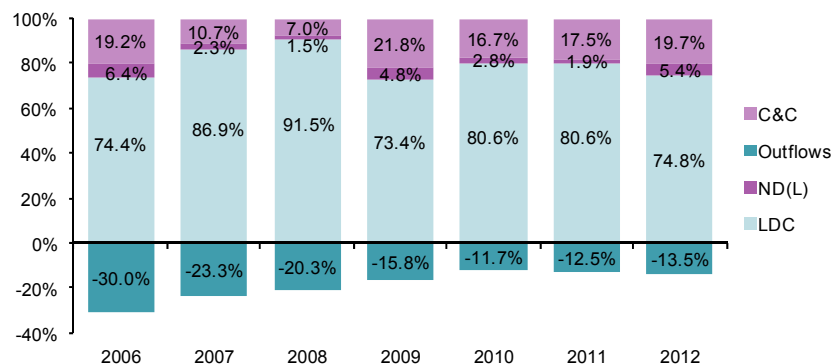
Overall consumption of manufactured cigarettes increased by 2% due to an increase in non-domestic flows, largely from Russia

Total Estonia consumption ⁽¹⁾⁽²⁾⁽³⁾								
Billion cigarettes	2006	2007	2008	2009	2010	2011	2012	Change 11/12 %
Legal domestic sales (LDS)	2.26	2.46	2.37	1.89	1.85	1.77	1.71	(3)%
Outflows	-0.65	-0.52	-0.43	-0.33	-0.24	-0.24	-0.26	10%
Legal domestic consumption (LDC)	1.61	1.94	1.94	1.55	1.61	1.53	1.45	(5)%
Non-domestic legal (ND(L))	0.14	0.05	0.03	0.10	0.06	0.04	0.10	196%
Counterfeit and contraband (C&C)	0.42	0.24	0.15	0.46	0.33	0.33	0.38	15%
Total non-domestic	0.55	0.29	0.18	0.56	0.39	0.37	0.49	32%
Total consumption	2.16	2.23	2.12	2.11	2.00	1.90	1.94	2%

The increase in total consumption is likely to have occurred as a result of higher tourist numbers travelling from Russia to Estonia taking their own cigarettes, along with more Estonian tourists travelling to Russia

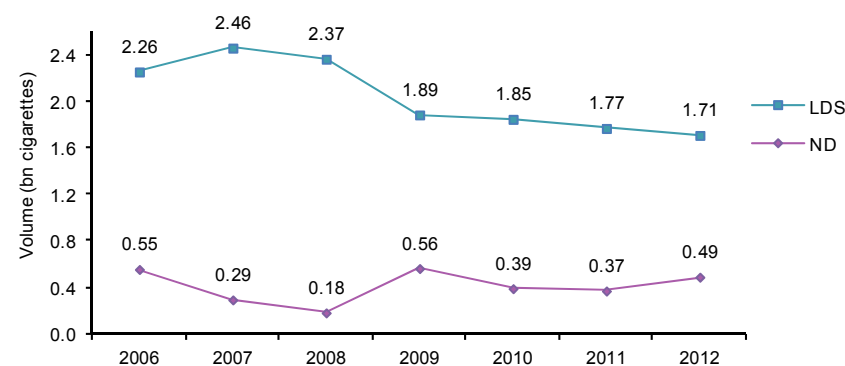
- The 5% fall in legal domestic consumption has been offset by a 32% increase in non-domestic consumption
- There appears to have been a significant increase in the number of Russian visitors on shopping trips, which has had a significant impact on the total level of ND(L) within the country⁽⁴⁾
- The OTP market is small and therefore is likely to have a negligible impact on overall consumption

Share of Estonia cigarette consumption by type 2006-2012⁽¹⁾⁽²⁾



Sources: (1) KPMG EU Flows Model 2006 - 2012
 (2) Synovate/Ipsos ND(L) research 2006 - 2012 (Ipsos acquired Synovate in 2011)
 (3) LDS/IMS data provided by PMI
 (4) Interview with PMI local management

Estonia total manufactured consumption (bn sticks) 2006-2012⁽¹⁾⁽²⁾



Estonia – Country flows summary

The Estonian market experienced 26% rise in inflows from Russia, its main non-domestic source market, and a small increase in outflows to Finland

Key inflows and outflows (billion sticks)^{(1)(2)(a)}



Inflows to Estonia

	2006	2007	2008	2009	2010	2011	2012	Change 11/12
Billion cigarettes								
Russia	0.22	0.23	0.14	0.51	0.36	0.30	0.38	26%
Belarus	0.00	0.00	0.00	0.00	0.00	0.03	0.05	81%
Other countries	0.34	0.06	0.04	0.05	0.02	0.04	0.05	49%
Total inflows	0.55	0.29	0.18	0.56	0.39	0.37	0.49	32%

Outflows from Estonia

	2006	2007	2008	2009	2010	2011	2012	Change 11/12 %
Billion cigarettes								
Finland	0.43	0.25	0.25	0.27	0.21	0.20	0.21	4%
Other countries	0.22	0.27	0.18	0.06	0.03	0.03	0.05	48%
Total outflows	0.65	0.52	0.43	0.33	0.24	0.24	0.26	10%

Inflows to Estonia have increased from its main source country Russia, as well as rise in inflows from Belarus

- Russian inflows have increased as a result of a growing number of tourists travelling between each country
 - Tourist flows from Russia increased by 49% in 2012 as Russians take advantage of the choice of shops in Estonia, whilst tourists from Estonia to Russia have increased at an average of 47% in the past three years⁽³⁾
- Belarus inflows have increased, a pattern seen by many countries within the EU, as illicit cigarettes are increasingly transported through this channel

Outflows to Finland increased by 4%, as a result of increased tourist flows from Finland to Estonia

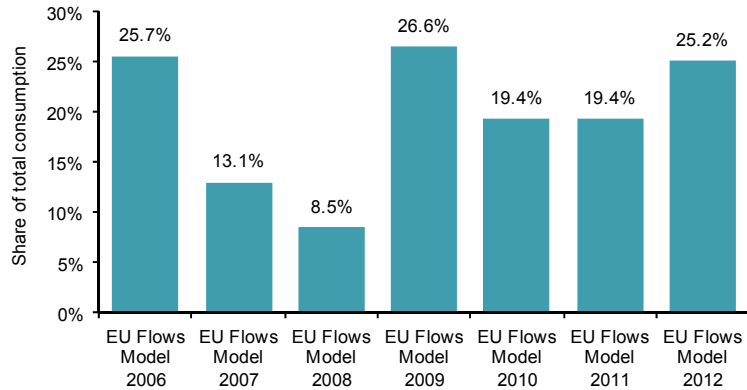
Notes: (a) Map shows flows over 1% of consumption, or top flow if none are greater than 1% of consumption. Countries which are both source and destination countries are coded according to the larger flow

Sources: (1) KPMG EU Flows Model and interviews with PMI Local Management
 (2) Synovate/Ipsos ND(L) research 2006 - 2012 (Ipsos acquired Synovate in 2011)
 (3) Statistics Estonia, Inbound and outbound tourist trips, February 2013

Estonia – Comparison of external sources for non-domestic estimates

Non-domestic incidence rose in Estonia by 5.8 percentage points in 2012, from 19.4% to 25.2%

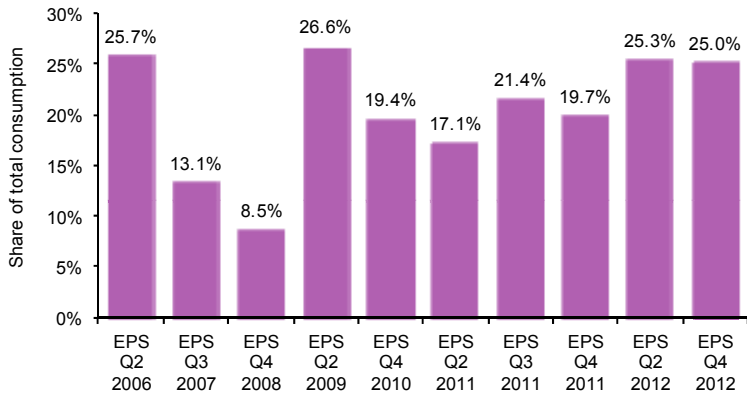
Non-domestic market estimates 2006-2012^{(1)(2)(a)}



The EU flows model calculates non-domestic incidence by inputting the empty pack surveys results from each quarter

- For Estonia, each EPS quarterly wave is weighted equally, as there were no inconsistencies or specific issues or events that may have distorted a quarterly result
- Each pack collected was weighted in order to obtain a sample representative of the population of each town sampled
- No additional re-weighting or analysis was undertaken

Other non-domestic market estimates 2007-2012^{(2)(a)}



Sources: (1) KPMG EU Flows Model 2006 - 2012

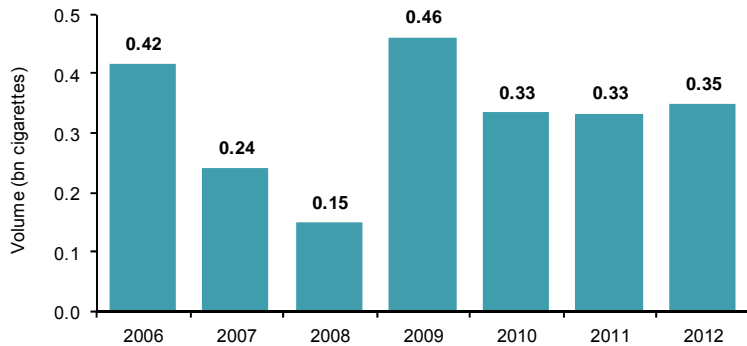
(2) PMI Empty Pack Surveys 2007 – 2012

Notes: (a) Non-domestic incidence for the 2012 EPS and EU flows model results has been calculated on a sticks basis. For more detail please see Appendix [x].

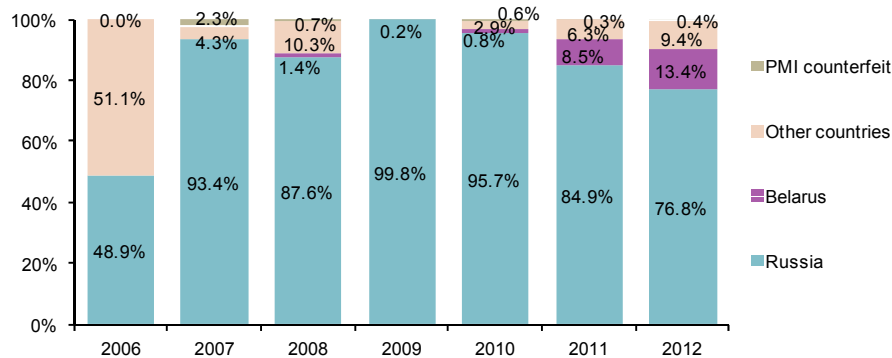
Estonia – C&C summary

The majority of C&C continues to come from Russia, however C&C inflows from Belarus are increasing, as illicit supply chains appear to be growing from Belarus across the EU

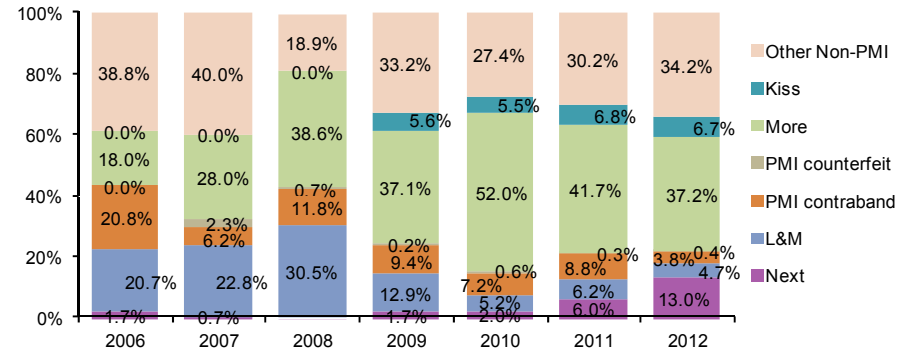
Total inflows of C&C
2006-2012^{(1)(2)(a)}



Share of C&C by origin
2006-2012^{(1)(2)(a)}



Share of C&C by brand
2006-2012^{(1)(2)(a)}



Notes: (a) KPMG calculates the split between C&C and ND(L) by analysing consumer research which records the volume and brands purchased legally from other countries.

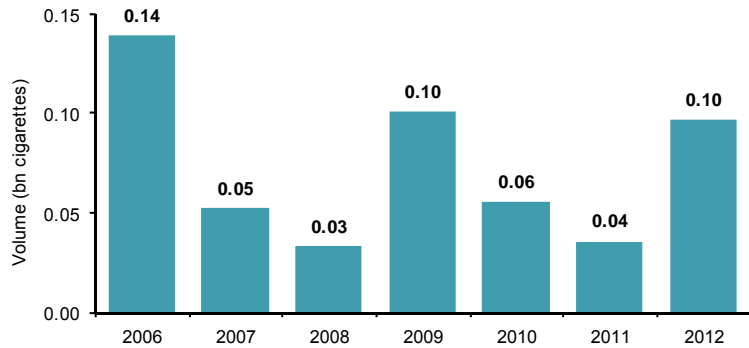
Sources: (1) KPMG EU Flows Model and interviews with PMI Local Management

(2) Synovate/Ipsos ND(L) research 2006-2012 (Ipsos acquired Synovate in 2011)

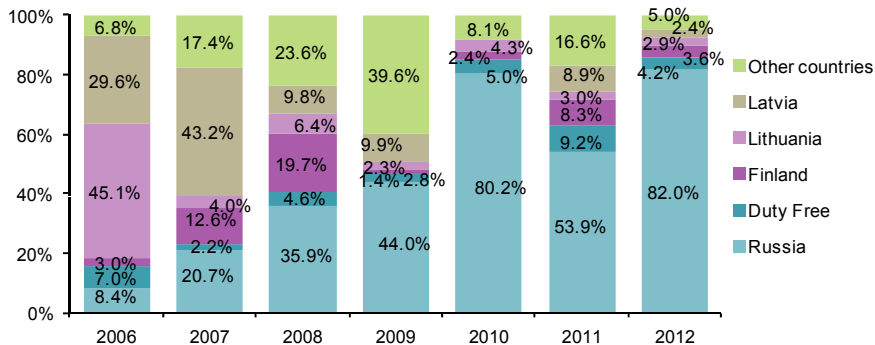
Estonia – ND(L) summary

ND(L) continued to increase from Russia, as inbound and outbound tourist flows increased by over 50% in 2012

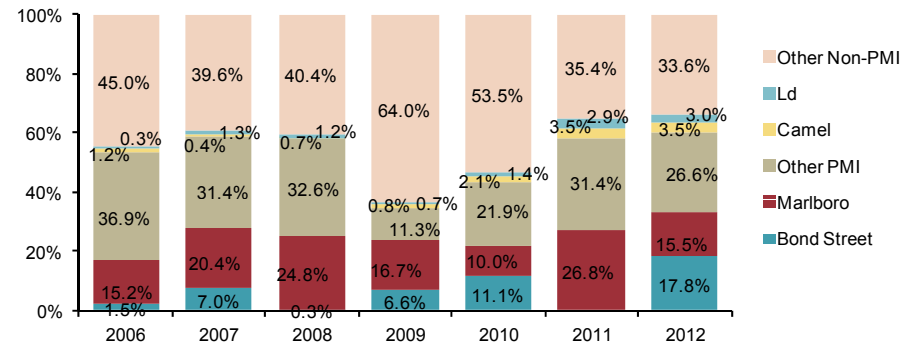
Total inflows of ND(L)
2006-2012^{(1)(2)(a)}



Share of ND(L) by origin
2006-2012^{(1)(2)(a)}



Share ND(L) by brand
2006-2012^{(1)(2)(a)}



Notes: (a) KPMG calculates the split between C&C and ND(L) by analysing consumer research which records the volume and brands purchased legally from other countries.

Sources: (1) KPMG EU Flows Model and interviews with PMI Local Management
(2) Synovate/Ipsos ND(L) research 2006 - 2012 (Ipsos acquired Synovate in 2011)

Aitäh!

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