# $2^{ND}$ QUARTER, 2008, EARNINGS CALL

**NICK ROLLI**

**(1)** Hi and thank you for joining us. Earlier today we issued a news release which contains detailed information on Philip Morris International's 2008 second quarter results. If you do not have a copy, you may access one on our web site at www.pmintl.com.

Following the completion of the spin-off, historical basic and diluted earnings per share amounts were recalculated based on the actual number of shares distributed by Altria Group, Inc. on the distribution date. In our first quarter earnings release, we provided a reconciliation of 2007 reported results to 2007 pro forma adjusted results by quarter and for the full year. This document is also available on our website.

**(2)** As we take you through our second quarter results today, please note that we will refer to certain results as being "after adjustments". This will imply that this data has been adjusted for the impact of currency and acquisitions. Furthermore, to provide you with a pure organic comparison, we will also exclude the impact of the transfer of our US duty-free business to PM USA in August last year. This latter adjustment is not included in the numbers in our press release.

Please also note that, unless otherwise stated, we will be talking about results in the second quarter 2008 and comparing them with results in the same period in 2007. References to international tobacco market shares are PMI estimates based on a number of sources.

**(3)** Today's remarks contain forward-looking statements and projections of future results, and I direct your attention to the Safe Harbor Statement in today's presentation and news release for a review of the various factors that could cause actual results to differ materially from projections.

It's now my pleasure to introduce Hermann Waldemer, Chief Financial Officer for Philip Morris International. Hermann.

**HERMANN WALDEMER**

Thank you, Nick. Hello, everyone.

**(4)** As you have seen from our press release, we have reported excellent second quarter results. These results, combined with our continued strong business momentum, currency favorability, higher pricing in a number of markets such as Italy and Russia, and planned reinvestments in key markets, have enabled us to raise our annual guidance.

Our revised adjusted full year diluted EPS guidance for 2008 is between $3.32 and $3.38, representing a growth rate of between 19 and 21%.

**(5)** Diluted earnings per share were 86 cents, up 22.9% or 16 cents per share. Of this increase, 6 cents, or about 40% of the increase, reflects the strength of our business and favorable currency accounts for the other 10 cents. In the first half of the year, reported EPS was up 26% or 36 cents per share, with business growth and currency each accounting for about half.

**(6)** Net revenues excluding excise taxes were 15.0% higher at $6.7 billion, representing an increase of $874 million. After adjustments, net revenues increased by 4.4% driven by higher prices as well as improved volume and mix in several key markets.

**(7)** Reported operating companies income, or OCI, increased by 23.7% to $2.8 billion. After adjustments, OCI was 9.8% higher. We achieved double-digit OCI growth in EEMA, Asia and Latin America.

**(8)** Our cigarette volume reached 223.2 billion units, an increase of 1.0%. Organic volume increased by 0.6%. Strong growth was achieved notably in Argentina, Egypt, Indonesia, Korea, Mexico, Russia and Ukraine. This is an improved performance that reinforces our confidence that we can achieve our longer term goal of 1 to 2% volume growth.

**(9)** *Marlboro* shipment volume declined by 2.4% to 79.1 billion units. After taking into account the impact of the transfer last year of our US duty-free business, *Marlboro* shipments were up in all geographical regions except the EU. The brand continues to perform strongly in Argentina, Egypt, Indonesia, Korea, Mexico, Romania, Russia and Ukraine. Our innovative line extensions are helping to strengthen the vitality of the brand and its overall equity.

**(10)** Increased shipments of *Parliament* and *Virginia Slims* have reinforced PMI's leadership position in the premium segment. *Parliament* shipments were up 28.1% thanks to tremendous momentum in Korea, Russia, Turkey and Ukraine. *Virginia Slims* shipments increased by 12.2%, reflecting both volume growth in existing key markets, such as Japan and Korea, as well as the penetration of new markets, such as Greece and Romania.

**(11)** Our two key brands in the mid price segment are *L&M* and *Chesterfield*. Outside of the EEMA Region, the volume of *L&M* grew by 3.4%, driven by France, Germany, Netherlands and Poland. *L&M* is the second largest brand in the cigarette industry in the EU Region behind *Marlboro* and, over the last 12 months, has been the fastest growing brand in Germany.

As you know, we have revamped the brand in Russia and Ukraine. While *L&M* shipments continued to decline in these markets, we were able to more than offset this volume decline through higher shipments of *Chesterfield*. *Chesterfield* sells at a premium to *L&M* and consequently generates higher margins. Globally, we are delighted by the performance of *Chesterfield* as it maintained its very strong momentum with an increase in shipments of 18.0%.

**(12)** Our key brands are in good shape and we are continuing to strengthen our international brand portfolio leadership through the development of a successful innovation pipeline. We've talked to you previously about the success of *Marlboro Filter Plus* in a number of markets. Let me share with you some other examples.

*Marlboro Intense* is a rich, flavorful, usually shorter cigarette in a red pack. It was launched initially in Turkey, and more recently in Belgium and the Netherlands. In Italy, a lighter tasting version was launched in March as *Marlboro Compact* in a silver pack.

To support our leading position in the growing menthol segment, we have launched *Marlboro Crisp Mint*, *Marlboro Fresh Mint* and *Marlboro Ice Mint* in a number of markets in Asia and Latin America. These refreshing products are performing well. For example, *Crisp Mint* reached a 1.4% share in Hong Kong, *Fresh Mint* 0.4% in Malaysia and *Ice Mint* 0.3% in Japan. I will discuss our latest menthol innovation, *Marlboro Black Menthol*, when I talk specifically about Japan later.

We have successfully developed a number of new products in response to an increasing demand in several markets for cigarettes with a slimmer diameter. Premium priced *Virginia Slims Uno* has notably achieved a 0.3% market share in Greece and Romania in May and a 0.2% share in Japan in the quarter. Mid priced *L&M Link* has achieved a 1.5% market share in Poland.

**(13)** Let me now take you through the results and key business developments in our four regions.

Industry volume in the EU Region is estimated to have declined by 3.7% during the second quarter, driven by the one time impact of recent public smoking restrictions, higher prices and a long term decline in smoking incidence. Our shipment volume decreased by 4.4% to 64.8 billion units and our estimated market share was down slightly to 39.4%.

Revenues net of excise taxes after excluding the very positive currency impact declined by 1.7% and OCI was essentially stable. These results were impacted by the total market declines and the need to temporarily absorb some tax increases in the Czech Republic and Poland, where we had shorter inventory durations of old tax products than our competitors. During the first half of the year, revenues net of excise taxes in the region were essentially stable and OCI increased by 5% net of currency.

Business fundamentals in our four key EU markets continue to strengthen. In Germany, our adjusted cigarette market share was up 0.3 points to 37.0%. *L&M* is growing and *Marlboro* is sequentially improving its share. We also expanded our position in the important German fine cut category with a market share increase of 4.8 points to a record quarterly level of 16.5% thanks to our innovative *Tobacco Block* and the strength of the *L&M* and *Next* brands. Our profitability in Germany is up both in the quarter and the first half of the year.

In Italy and Spain, we continued to improve our profitability during the quarter. Our share is up in the first half in both markets. *Chesterfield* is performing very well and *Marlboro* is resilient. In France, while share is down on a year-on-year basis by 2.5 points due to the impact of a less favorable price point for *Marlboro*, our market share of 40.9% has been stable since the fourth quarter of last year.

The outlook for the EU region is improving. We have recently announced price increases in Italy, the Netherlands and Switzerland and have strengthened our competitive position in the important German market. Public smoking bans have now been implemented across most of the EU and we expect the one time impact on total industry volume to have been largely absorbed by year end. The very large tax driven price increases in Central Europe relating to EU accession are moderating. The Czech Republic has now reached the excise tax level currently required in the EU. Hungary, Poland and Slovakia should reach it next year.

In this context, I would like to comment on the update to the tobacco excise directive that the EU Commission is proposing. First, I would like to emphasize that we welcome the review as it is an opportunity to improve the framework for excise taxes in the EU. Second, the proposal is essentially in line with what we had expected, following a broad consultation. The next step is for the EU Commission to discuss the proposal in detail with the member states, a process that will allow individual countries to convey their views on each element of the proposal. As a unanimous agreement is needed on every proposed change to the current directive amongst the 27 EU member states, we expect that the proposal will be modified prior to its finalization, which is foreseen during the second half of next year. We are pleased that the EU Commission recognizes that there is little justification for significant differences in the taxation level for cigarettes and fine cut products. We also welcome the proposed increased flexibility to be given to Governments in terms of the excise tax structure and the level of the Minimum Excise Tax. We however regret that the Commission has not taken this opportunity to propose an abolition of the excise incidence rule and are concerned that tax increases resulting from the proposal could have unintended consequences in certain EU countries if implemented as currently proposed.

**(14)** During the second quarter, the EEMA Region continued to achieve very strong results with volume up 3.2%, net revenues excluding excise taxes and currency 10.2% higher, and OCI excluding currency increasing by 22.9%. We are benefiting from the premium skew of our portfolio as consumers continue to trade up. The resulting volume growth and improved product mix has been further boosted by price increases, thus driving profitability to record levels.

Russia is central to these excellent results with PMI shipments increasing by 8.3%. Continued strong consumer uptrading has benefited *Chesterfield*, *Marlboro* and *Parliament*. Revenues net of excise taxes and currency rose by 24% driven by favorable volume and mix and higher prices. This has enabled us to increase profitability to record levels.

Our shipments grew by 2.9% in Turkey. While our share was essentially stable, we benefited from consumer uptrading with very strong *Parliament* growth. This more favorable mix, along with higher prices, has been driving profitability.

In Ukraine, shipments increased by 8.2% driven by *Chesterfield, Marlboro, Parliament* and *Virginia Slims*. As a result, our market share reached a record level of 35.2%. Our profitability will be further boosted by the recent retail price increases in this important market.

**(15)** Cigarette shipment volume in Asia grew by 1.9% to 56.8 billion units, with growth in Indonesia and Korea more than offsetting a decline in Japan. *Marlboro* is performing very well across the Asia Region with a volume increase of 1.8%. *Marlboro Filter Plus* and *Marlboro Mix 9* (kretek) have reinforced the brand's equity, helping to drive the brand family to record levels in Korea and Indonesia, and *Marlboro* continues to perform strongly in the Philippines. *Marlboro*'s success is complemented by the tremendous performance of *Parliament*, driven by Korea, whose shipments were up over 50% in the region, and *Virginia Slims*, which experienced double-digit growth.

Revenues net of excise taxes were up by 4.9% excluding currency. We achieved a 15.2% increase in OCI net of currency in Asia as excellent results, notably in Australia, Indonesia and Korea, more than offset a decline in Japan.

We are very pleased with our results in Indonesia. Our shipments there were up 14.9% as our entire portfolio grew with *A Mild* and *Marlboro* performing particularly well.

**(16)** Let me focus for a moment on Japan. During the second quarter, industry volume was down by 1.6%, helped by trade purchases in advance of the implementation of the new vending age control mechanism. PMI shipments, meanwhile, declined by 7.0% due to the declining total market and an optimization of stock coverage levels. Our share reached 23.9%, which was 0.3

points below the prior year's level, but stable compared to both the first quarter of this year and the last quarter of 2007.

*Marlboro*'s share remained stable at 9.8%. We are launching *Marlboro Black Menthol* during the first week of August to reinforce the brand's performance. This innovative new product has a unique refreshing mint flavor and provides a bold cooling sensation.

*Lark*'s share of 6.8% was marginally down from last year but slightly up compared to the first quarter of 2008. Recently launched *Lark Menthol X* has achieved a market share of 0.3% and the new *Lark Classic* is doing well in test market. *Virginia Slims* has continued to expand to reach a market share of 2.1%, driven by the successful launch last year of *Virginia Slims Noire*.

These results show that our increased focus on innovation is starting to have a positive impact and we expect improved results going forward, fuelled by additional marketing investments. While we are focused on restoring share growth momentum, we are also very conscious of the pressures on profitability from a declining market which is subject to price controls. While we oppose the recent call for a massive tax and price increase, we believe that this debate may encourage the Government to consider revising the Tobacco Law to allow pricing freedom.

**(17)** Latin America had another very strong quarter on all counts. Our cigarette shipment volume was up 7.9%, and 1.3% excluding acquisitions, driven by strong results in Argentina and Mexico, partly offset by Colombia.

In Argentina, our shipments increased by 8.8% and we gained 1.9 points to reach a market share 70.3%, driven by *Marlboro* and the *Philip Morris* brand. In Mexico, the total market remained stable while we were able to increase our market share by 3.0 points to 67.2%, driven by *Benson & Hedges, Delicados* and *Marlboro.*

In Latin America as a whole, our revenues net of excise taxes increased by 8.0% excluding currency and acquisitions, while our OCI was 15.0% higher on the same basis.

**(18)** Let me say a few words about our actions to enhance shareholder value.

On May 1st, we started our two year share repurchase program. Since then, we have spent \$2.1 billion out of the \$13 billion approved by the Board of Directors. In total, we have so far purchased 41.4 million shares at an average price of \$51.48. On June 18th, we announced our first quarterly dividend as a public company of 46 cents a share. As stated previously, we expect to return a total of \$21 billion to shareholders over the next two years, which reflects about 20% of our current market capitalization.

In order to help finance these and other business requirements, we successfully raised $6 billion in May in a US Dollar bond offering at what we believe are attractive rates. During the second half of the year, we intend to continue to access the capital markets provided financing conditions are suitable.

**(19)** To sum up:

- Our businesses in EEMA, Asia and Latin America are performing very well with strong volume growth, an improved mix and higher prices and margins;
- The outlook for the EU Region is improving with pricing power remaining strong and an enhanced competitive position notably in Germany;
- Japan remains a challenge due to continued price controls in a declining market. We have however stabilized our market position and have the strategies in place which we believe will enable us to grow share again;
- Enhanced innovation is driving better organic volume; and
- We are on track with our productivity saving programs and our financial measures to return significant cash to our shareholders.

As you can see, we are delivering against the targets that we established and shared with you in March.
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**(20)** I will now be happy to take your questions.

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**NICK ROLLI**

Thanks everyone. The Investor Relations team is available in Lausanne should you have any follow-up questions.