A Work Project, presented as part of the requirements for the Award of a Master's degree in International Management from the Nova School of Business and Economics.

PHILIP MORRIS INTERNATIONAL DELIVERING A SMOKE-FREE FUTURE – LAUNCHING A PRODUCT IN A HIGHLY REGULATED ENVIRONMENT

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17-12-2021

Abstract

The work project consists of a case study, teaching note and project evaluation report on Philip Morris International's mission of delivering a smoke-free future. The case study presents the company's transformation and introduces PMI's next-generation product IQOS that is said to have the potential to be less harmful than conventional cigarettes. The teaching note focuses on the impact of regulators on heated tobacco products. The evaluation report analyzes and provides recommendations for PMI's main challenges: widespread mistrust from stakeholders and lack of awareness for IQOS.

Keywords (Sustainable International Business, Business Transformation, Regulations, Strategy)

This work used infrastructure and resources funded by Fundação para a Ciência e a Tecnologia (UID/ECO/00124/2013, UID/ECO/00124/2019 and Social Sciences DataLab, Project 22209), POR Lisboa (LISBOA-01-0145-FEDER-007722 and Social Sciences DataLab, Project 22209) and POR Norte (Social Sciences DataLab, Project 22209).

GROUP COMPONENT

CASE STUDY

Philip Morris International delivering a smoke-free future – Engaging in a major business transformation towards sustainability.

"*It's to me very simple, we produce a product that causes diseases, and I think that the primary responsibility we have once the technology is available, and today the technology is available, is to develop products like this [IQOS] and commercialize them as soon as possible. These products hold very great promise, obviously for consumers, but also for public health, and eventually for our company, as their economies are similar to cigarettes, and in addition I believe to gain market share over time. […] First of all, we are concerned about the consumers. Secondly, even based on WHO projections, they will be, in 2025, still 1 billion plus smokers around the planet, and 9.6 million smokers in the UK, once we have the ability and innovation to offer this product to consumers, we have to offer it to them. […] I think consumers choose to use cigarettes, I don't think Philip Morris has invented cigarettes, I think for us, is to offer our consumers the best product we can in a category that we all know is addictive and causes harm, once we have the alternative, as we have it today, and I'm very happy we do, we offer them the alternative and we will do everything we can to convince them to switch to these products."* (André Calantzopoulos, BBC 2016).

"PMI aims to become a majority smoke – free business by 2025." (PMI 2021)

It was the 29th of September 2016, when André Calantzopoulos, CEO of Philip Morris International (PMI) took one last look at the headline of the speech he was about to deliver to the world, thinking about the last few exhausting months. Before delivering his speech, André thought about the long history of the company, tobacco and how cigarettes had impacted the world and the businesses he led for several years. With this in mind, he wondered how his employees, regulators, media, and consumers would receive the news of a tobacco company committing to go smoke–free. In his letter published in the "Communication on Progress 2016 United Nations Global Compact", Calantzopoulos stated that *"there is no doubt that the greatest contribution PMI can make to society is to replace cigarettes with less harmful alternatives"* (Communication on Progress United Nations Global Compact 2016). And later, in PMI's 2018 Sustainability Report, he affirmed that a tobacco company can be sustainable *"by taking every step possible to completely replace cigarettes with better alternatives, addressing its sustainability challenges across its value chain, and seizing opportunities to add value to society"* (PMI Sustainability Report 2018).

History of the company

PMI is currently one of the world's leading tobacco companies, but its history dates back to 1847, when Mr. Philip Morris opened a shop in London´s Bond Street selling tobacco and ready-made cigarettes. During the course of time, the company operated by incorporating many cigarette brands in its portfolio, including Marlboro in 1908, which eventually became PMI´s most famous and popular brand. The situation changed in 1919, when the company was acquired in the United States and incorporated in Virginia as Philip Morris & Co. Inc., and began manufacturing cigarettes in its factory in Richmond. In 1950, PMI began its worldwide expansion by introducing an internal operational division to manufacture its products around the world. Across the globe and far away from its home country, Australia becomes the first

country to host a foreign division of Philip Morris. Over the years, the tobacco giant has continued to open new production sites in Asia and Europe, expanding its influence in new markets.

One of the most significant milestones for PMI was achieved in 2009 when its facility in Neuchâtel, Switzerland, for R&D is presented as an innovation hub that brings together over 400 specialists and scientists to pioneer the development of reduced-risk products (RRPs). The road towards delivering RRPs is corroborated by the strategic approach with Altria Group Inc., which makes Altria's e-cigarettes available to PMI for commercialization outside of the United States, and, on the other hand, makes two of PMI´s RRPs available to Altria for commercialization in the United States. The introduction of RRPs as an alternative to conventional cigarettes became clearer in 2014 when PMI announced its plan to invest up to 500 million euros to build its first RRP factory in Italy. Hence, research and development efforts led to the introduction of PMI´s first smoke-free platform, IQOS, in 2014, which is piloted in Italy and Japan. After its success in the initial test markets, IQOS is later introduced in other countries such as Portugal, Romania, Russia, and Switzerland in 2015. The transition to smoke-free alternatives culminates in 2016 when PMI expresses its vision to achieve a smoke-free future, and begins allocating its resources towards the development and responsible marketing of smoke-free products supported by scientific research (PMI 2019).

Evolution & Regulations

The use of tobacco is not a recent phenomenon. In fact, more than 10,000 years ago, it was used by indigenous people in America for religious purposes, but it was not until the 1950's that tobacco started to be linked with maturity, glamour, and social life – a context in which tobacco companies and cinema played a key role in promoting such "benefits" of smoking. During the 50's, smoking was so vogue that Camel also encouraged consumers to smoke during

thanksgiving as a technique to digest food better (Castaldelli-Maia 2015). Even thoughsmoking was partially regulated in the 50's as a potential cause of fire hazard, it was not until 1964 that other concerns were raised as the Surgeon General Report on Smoking and Health was published – findings indicated that smoking was inherently related to lung cancer. This iswhen the tobacco industry started seeing new regulations coming in place.

When it comes to regulations at a national level, each country has its own approach to limit the sale of cigarettes. For instance, in the United States, Congress approved the Cigarette Labelling and Advertising Act in 1965, requiring health warning statements on all cigarette packages. The next major regulatory step occurred in 1992, when Congress introduced the Reorganization Act which mandated states implement laws prohibiting the distribution and sale of tobacco products to minors (Jacobson 1997). The European Union (EU) followed a different approach, and its most relevant initiative is the "Tobacco Products Directive" implemented in 2014 and enforced to EU countries in May 2016. This directive outlines the standardsgoverning the manufacturing, presentation, and sale of tobacco products. One of the most notable actions is Art 10.1, which specifies that each unit packet, as well as any outside packaging of tobacco products, must include combined health warnings, which should cover 65% of both exterior front and back surfaces of the unit packet as well as any outside packaging.Furthermore, Art 18.1 stipulates that member states have the authority to prohibit cross-border distance sales of tobacco products to consumers and that member states must work together toprevent these sales (Directive European Union 2014).

Urge to change

When André Calantzopoulos delivered his speech about the smoke–free future, PMI was confronting a reality in which 20% of the world´s population (Statista 2021) were smokers and lung cancer was the most common cause of cancer death worldwide.

Not only general trends of global health care were an issue, but also pressure from the financial sector was another inevitable factor. The World Health Organization (WHO) Framework Convention on Tobacco Control (FCTC) is one of the most influential conventions on tobacco–free investment, as it made finance leaders aware that it is the first legally binding health treaty. The focus of the FCTC has been to prohibit the sale of cigarettes to minors, ban tobacco product advertisements, and increase the taxes on tobacco. In addition to the FCTC, the United Nations Sustainable Development Goals (SDGs) have provided a platform on which to base the dialogue regarding tobacco-free investments. The SDG framework does not directly address tobacco companies but focuses on a broader call for action in different areas. For instance, SDG number 17, "partnership for the Goals" implies cross–sector collaboration as a key step when addressing major global issues. What is important to retain here is thatcompanies need to abide to the general guidance the SDGs provide if they intend to participatein the framework. If a financial company intends to participate in the SDG framework, for instance, it is not possible to invest in a company whose operations hinder the achievement ofSDG 3, "Good Health and Well – Being". In fact, this rationale of participation towards SDG and tobacco-free portfolios led financial giants such as AXA to divest 1.8 billion euros in assetsfrom the tobacco industry (King 2017).

Still, when talking about divestment from tobacco companies it is always necessary to open a parenthesis and think about how it contributes to solving the problem of smoking. Since many ESG investors excluded tobacco companies from their portfolios, billions of dollars were divested from the tobacco industry. However, anti-smoking investors cannot pressure companies to transform their business model and develop strategies to eliminate cigarettes – so, at this point, the question remains if whether or not investors should reward the development of less harmful smoke-free products that can cannibalize cigarette sales (Olynec 2020). What is more, in 2017, tobacco companies were excluded from the United Nations Global Compact

because their activities conflicted directly with SDG 3 and with public health policies. Therefore, tobacco companies are currently not considered an ally of the Global Compact. (King 2017)

Because of the above-mentioned reasons, it is not possible for a tobacco company to fully commit to the SDG framework if its core business operates in a way that contrasts it. Nevertheless, PMI voluntarily *"aligns with the principles and standards of the UN Global Compact (UNGC) and indicates contributions to the UN Sustainable Development Goals (SDGs) and corresponding targets."* (PMI Investor Relations, 2021). Five years after announcing its new vision, the company´s Board continues to reaffirm in its Statement of Purpose that they are committed to accelerate the phasing out of smoking. Moreover, the goal is still to transform the company to fulfil its own purpose, while also influencing the industry to follow its steps, as they seek to make a long-term positive impact that helps not only the company, but also consumers and society alike.

Industry Changes

The tobacco industry has been recently characterized by a wave of innovation, as established tobacco products continue to lose their appeal in an environment shaped by more health-conscious consumers, as well as tightening regulations. At a macro level, government initiatives, along with declining social acceptance of smoking, resulted in ashrink of the industry volume. The WHO, through the FCTC, is the principal force driving legislation, by encouraging public health organizations to promote increasingly stricter regulatory measures on the marketing and sale of tobacco products to adult smokers (PMI Annual Report 2020). But in a scenario where regulations play a dominant role in the tobaccoindustry, how have these really affected the market?

Currently, there is not a standard for regulation of tobacco products applicable to all nations. Even though the FCTC provides the main guidelines, they are made on a more general scale and different regions end up facing distinct regulatory environments, which means different trends in smoking (Exhibit 1). Africa, for instance, has experienced a 42% increase in the number of smokers from 2000 to 2020, and the narrative for this growth is quite simple: tobacco use in Africa has received little attention as the continent was perceived as a low smoking region compared to other developed areas, leading to low priority for tobacco control in favour of higher control of other relevant issues, such as infectious diseases (Blecher 2013). An entirely different landscape is present in both the Americas and the European Union. The former saw a decrease of 28% in tobacco use in the last 20 years - a result of higher priced cigarettes, approximately 8$ per packet (Statista 2021), which makes smoking less accessible to consumers. Furthermore, the United States Government has funded advertisements that show the adverse effects of tobacco, sometimes in a gruesome detailed manner, a measure that was also fostered by Medicaid and insurance plan programs, which required smoking cessation (American Heart Association 2018). As for the European Union, a decline of 21% in the number of smokers occurred in the same time-frame, mainly attributable to increased taxes on smoking. For instance, France increased taxes on tobacco by nearly €1 in 2018 and this contributed to a reduction of cigarette sales of 9% (OECD 2020). In contrast to the regions analysed above, in South–East Asia (SEAR) the number of smokers has remained constant, which is partially explained by the region's status as the world's largest producer and consumer of tobacco. Despite all 8 SEAR countries having signed the FCTC, they still face challenges when it comes to implementing it, mainly regarding inadequate and poor infrastructure, legislation and regulations (World Bank 2009). Lastly, the Western Pacific Region is home to one-third of the world´s population of smokers and has been targeted by campaigns to advocate for tobacco control, for which 80% of the members of the region have adhered. Even though

the campaigns have been successful in recent years, various challenges continue to appear to counteract these efforts, namely the rising popularity of electronic alternatives as potentially safer options (The Lancet, 2021).

But even if the number of smokers seems to be constantly declining across the globe (WHO 2021), tobacco companies remain profitable. In fact, the tobacco industry was valued at $932 billion in 2020 and it is predicted to expand at a compounded annual growth rate (CAGR) of 1.8%, through 2028, reaching $1.07 trillion. The international tobacco market is currently dominated by four giants: Philip Morris International (PMI), Japan Tobacco International (JTI), British American Tobacco (BAT), and Imperial Brands. While retail prices have been rising to reflect tax increases, sales volume of cigarettes have been decreasing. The transition to smoke–free products is another reason for the profitability of the industry. For instance, PMI anticipates that sales of its smoke–free products will account for more than 50% of overall sales in 2025, and in practical terms it seems to be working, as in 2020 PMI experienced a drop in sales of cigarettes of 10.7%, while sales of heated tobacco products surged by 27.9% in the same period (Forbes 2021).

Adding to the four large brands mentioned, the international tobacco market is also dominated by two manufacturers that operate in their domestic markets - The China National Tobacco Corporations (CNTC) in China and the Altria Group in the USA. When it comes to market share, the leader is CNTC with 46%, followed by PMI with 13.8%, BAT tobacco capturing 12% of the market and JT with 8% of market share. Even though the products manufactured by these companies are remarkably similar, competition relies on factors such as quality of products, brand recognition, customers´ loyalty to the brand, taste, R&D, and retail pricing. Not only that, but since the competition in the tobacco industry is quite high, tobacco companies must innovate to stay on board. Innovation has been achieved through the introduction of reduced-risk products for which the value proposition lies on offering more

choice to consumers *"towards the replacement of cigarettes with high-quality and scientifically substantiated smoke-free products for adult consumers"* (PMI 2020). First examples of reduced-risk products date back to the 1990s, but the breakthrough occurred in 2014, when PMI launched IQOS (PMI Integrated Report 2020). As the former PMI Chief Sustainability Officer mentioned: *"For PMI, or indeed any tobacco company, to credibly speak about sustainability, the purpose can be none other than to replace cigarettes with better alternatives for smokers, society, and the environment."* (PMI – Sustainability of tobacco companies 2019).

R&D in reduced-risk products

Determined to stay on board in a constantly changing environment and facing outside pressures from both the public, government and other institutions, PMI decided to reinvent its business model and committed to a major transformation. After acknowledging and informing consumers about the negative impacts of its products in an effort to tackle the lack of trust and bad reputation of the industry, PMI had to innovate and undergo internal changes and transformations to support these innovations in a sustainable way. After redesigning the company's vision, PMI defined the term Reduced Risk Products (RRP) as those products that present or have the potential to present less risk of harm to users who choose to switch to these products versus those that continue to smoke conventional cigarettes. RRPs became PMI´s focus in this transformation. The major difference between RRPs and conventional cigarettes is that RRPs do not burn tobacco or release smoke (PMI – What are RRPs 2021). Still, a question has to be made: Why do these products have potential to be less harmful than conventional cigarettes?

Scientific background on tobacco and nicotine as components of cigarettes

When lighting a cigarette, a process called combustion or burning is started, producing a complex mixture known as smoke. The burning process of tobacco generates toxicants of which around 100 have been identified as causes of most smoking-related diseases, such as lung cancer and cardiovascular diseases. (PMI – The problem with burning 2021). As a result, tobacco kills over 8 million people worldwide per year (WHO – Tobacco 2021). Nicotine, on the other hand, occurs naturally in tobacco plants. It is highly addictive which makes it the main reason for people to continue smoking, and its pharmacological effects can cause acute increases in heart rate and blood pressure. Even though nicotine is poisonous when consumed in high doses and not risk-free, it is not the primary cause of smoking-related diseases. PMI therefore argues that *"that's why we are focused on developing [reduced-risk] products that offer a flavorful nicotine-containing vapor – but with far lower levels of harmful chemicals found in cigarette smoke.*" (PMI – The role of nicotine 2017).

RRPs can be divided into two main subcategories: heated tobacco products and e-cigarettes (Exhibit 2).

Heated tobacco products - HTPs

Heated tobacco products use battery-powered heating systems to heat tobacco at temperatures lower than conventional cigarettes to produce a nicotine-infused aerosol. The products in the market come in different forms: PMI refers to its key heated tobacco product as IQOS or Platform 1, which uses an external heat source heating specially designed stick. A blade in the heater device put into the end of the tobacco-containing element heats the tobacco. Other companies use different techniques such as heated sealed chambers, like micro-ovens,

or a process in which the emission is passed over tobacco to heat it and absorb the taste (WHO – Heated Tobacco Products 2020).

E-cigarettes

E-cigarettes differ from HTPs because they do not contain tobacco. Instead, they heat a nicotine-containing liquid. Most e-cigarettes have a battery, a heating element, and a place to hold the liquid. The products create an aerosol by typically heating the nicotine-containing liquid which is being inhaled by the users. Smoking e-cigarettes is often also referred to as "vaping". While most players in the market use a similar technique, e-cigarettes come in different forms. Some are made to look like conventional cigarettes, cigars, or pipes, and others match the appearance of pens, USB sticks and other everyday items. E-cigarettes are said to be less harmful than regular cigarettes as they contain fewer toxic chemicals, yet they are not harmless (Centers of Disease Control and Prevention 2021). In the field of e-cigarettes, PMI has developed its so-called product IQOS VEEV or Platform 4.

PMI's objectives go alongside the efforts of the World Health Organization (WHO) to tackle smoking around the world, but PMI aims to achieve the defined target much faster. High standards are set and now it is up to teams of scientists, engineers, technicians, and other professionals to work towards overcoming current environmental, sustainability and harm reduction challenges to deliver innovative solutions that go beyond nicotine. (PMI 2021).

With the ambition of completely replacing cigarettes and being the sole tobacco company to have done it so far, PMI has put significant efforts and continues to invest substantial amounts in its science-based research and development to create less harmful alternatives with potential growth in markets around the world. PMI has strongly committed to science and technology as the company believes these to be the drivers of its innovation and growth. However, it is not enough to simply develop these alternatives, the company must also

ensure that adult smokers who are not willing to quit smoking, and only these, have access to these alternatives. Access means that smokers are aware of the existence of smoke-free products, the products are accepted as viable alternatives and that they are available and affordable to smokers.

Since 2008, PMI has invested over $8.1B *"in the development, scientific substantiation, manufacturing, commercialization and continuous innovation for smoke-free products"* (PMI Science 2021, 43). These investments were more vehemently observed in the opening of the R&D Center in Neuchâtel (PMI Science 2021, 44), in conducting several scientific studies and in recruiting talented scientists, engineers and specialists, who were primal to the improvement of their technological capabilities and to the establishment of 1.300 patents worldwide (PMI Science – smoke-free future 2021), ultimately helping the transformation and adaptation of PMI's value chain to serve their main purpose. This value chain transformation consists in the incorporation of new ways of thinking and working to become more digitalized, project-based and focused on customer centricity, agility, and data-driven decision-making. (PMI Science 2021). PMI is now, more than ever, committed to engage in a transparent two-way dialogue to address customers concerns and build upon their feedback. To make this transition measurable and verifiable, PMI has committed to transparent reporting through its Business Transformation Metrics. These metrics allow all stakeholders and the public to get access to all information about the pace and scale of the achievements, which contributes to the increase of trust towards the company. The approach taken by PMI has allowed the company to maintain its leadership in the conventional cigarette business, but also to become a leader in the smoke-free market.

Introducing IQOS

The first thing that should be noted about IQOS is that it is a HTP and not an e-cigarette. Even though they share some commonalities in regard to both being alternatives to conventional cigarettes and having slender, battery-powered devices, IQOS vaporizes actual tobacco, instead of vaporizing nicotine-containing liquid (Belluz J 2018, Exhibit 3). An IQOS device can be divided into three main components: a heated tobacco unit, the IQOS holder (which looks like an e-cigarette), and a charger. To use it, users must insert the tobacco unit into the IQOS holder, press a button to turn on a battery-powered heater, and then inhale the nicotine-containing vapor. This smoking experience lasts for about six minutes, or 14 puffs, before the tobacco unit is exhausted and the IQOS device needs to be recharged once again (PMI 2014).

IQOS is highly adaptable to consumers' tastes. In fact, several types of HEETS (heated-tobacco sticks) are available across many markets, with ones being exclusive to certain regions and others being more commonly found. However, due to legislations in the US and Europe, which forbid the manufacture of flavoured tobacco, the major difference between all variants relate to their intensity, with the menthol flavour being an exception.

All this mimicking of traditional tobacco-smoking has a finality: to potentially reduce harm and the risk of smoking-related diseases. To achieve that, the difference lies on how the tobacco is treated inside the IQOS device – rather than being burnt at temperatures from 600ºC to 900ºC like traditional cigarettes, it is instead heated below 350ºC (PMI Integrated Report 2019). In fact, and like it was already conveyed in a previous section, scientific research states that extreme temperatures seen in traditional cigarettes can certainly be the main factor for the release of dozens of chemicals that are harmful for consumers' health and may be associated with eventual tobacco-related diseases (PMI 2014).

The lower heating temperature in the IQOS platforms is achieved via a heating blade and acts as both a heater and temperature sensor. The blade constantly monitors and controls the temperature of the tobacco while the device operates, which is one of the main factors contributing to the core of the innovation. The 350ºC as the maximum limit of the tobacco heating process guarantees that no combustion occurs, leading the aerosol generated to have on average 95% less Harmful and Potential Harmful Constituents (HPHCs) than those found in conventional cigarettes (PMI Science 2019). The processes described seem to indicate that switching from conventional cigarettes to IQOS has a positive impact on smokers' health. (PMI Science 2018). However, an often-emphasized aspect by PMI is that, although a better alternative to conventional cigarettes, IQOS devices are not fully risk-free. The toxics released in the process of heating are greatly reduced, but not eliminated entirely, while there is always still the presence of nicotine to account for, which, as already said, is addictive (Healthline, 2021).

Test Market Strategy

As the time to finally deliver IQOS to consumers arrived, PMI figured that testing the product in a select number of markets would be beneficial for the "reconnaissance" phase of the product launch. Thus, in the end of 2014, Milan (Italy) and Nagoya (Japan) served as the first IQOS test markets. These markets were selected because of their reputation as large metropolitan areas that usually welcome innovation, reasons that are important for the product to be tested and explained to retailers and consumers (Tobacco Journal International 2015).

In Japan, the goal was to take advantage of the heavy regulatory environment on e-cigarettes that contained nicotine-laced liquid. IQOS would not face these regulations as the devices heat tobacco and use HeatSticks as a refill (Reuters 2016). As such, an opportunity to capture the

market share of the fast-growing Japanese e-cigarette business was presented to PMI, while tax benefits also arose because of the potential lower risk nature of heated-tobacco products. Furthermore, due of the higher excise tax, the profit margins of smoke-free products are comparable to or exceed those of cigarettes. (PMI Progress Report 2016).

In Italy, the strategy was more of a forward-looking one. Even though the Italian government had a more uniform approach towards tobacco products, be it heated or burnt, PMI was confident that less regulations for IQOS would be put in place once legislators understood the benefits the product would bring to Italian consumers (Euromonitor 2021). Additionally, the fact that heated-tobacco products were not subject to any indoor smoking bans or advertisement legislations brought PMI confidence that the eventual success case in Italian grounds could inspire other developed economies to follow (Liu 2018).

Still, it was the Japanese play that ended up being fruitful in a more quickly manner, setting it as the standard test market and the backbone of PMI's enormous transformation. The cultural aspects played a key role in guaranteeing the success of the experiment – indeed, Japanese consumers' savvy preferences towards cleanliness meant that smoking with no ashes, less smell and no impact on indoor air quality would perfectly bridge the experience of smoking with the cultural standpoint. Hence, only a few months were needed for an expansion to other Japanese prefectures to happen, followed by a national spread of the brand in April 2016, a move that cemented the Nippon country as a global standard for the desired IQOS transition.

Commercialization Strategy

After defining which markets to enter and what strategy to follow, consolidation in those and other markets would be the next logical step for PMI to think about. To do so, the company focused on invoking its own smoke-free vision to consumers and critics' minds. An

example of this is the numerous participations in seminars, conferences, music festivals and art exhibitions (PMI Sustainability Report 2020). Moreover, there was a focus on connecting with IQOS-friendly restaurants and bars, a move that enhances the potential difference in harm to consumers' health that separates both types of smoking (Reuters 2020).

These efforts reflect PMI´s commitment to sustainability through engagement with stakeholders, which might ultimately deliver the envisioned smoke-free future. More than ever, social support is required to enable the implementation of legal frameworks that would rapidly stop cigarette smoking by encouraging smokers to become aware of smoke-free alternatives. (PMI Sustainability Report 2018).

Nevertheless, in the eyes of many, IQOS seemed like an attempt to sanitize PMI's product line, and one that is not always successful at that. A notable marketing failure by PMI concerned the use of IQOS ambassadors in some countries around the world, many of whom were reported to be younger than 25 years old. The problem here lies on the fact that the company's internal guidelines prohibit influencers who are or appear to be under 25 years old to promote its brands, leading it to violate its own policy towards social media communication (Reuters 2019). As an answer to this, PMI has stated quite transparently that, even if parts of the reports were true, there was never the intent to violate their guidelines and there were insufficient controls put in place to ensure compliance (Responsible Marketing Practices at PMI 2019). Ultimately, this incident led the company to shy away from engaging with anyone for the purpose of creating social media posts promoting their products. However, this type of transgression against company's standards and overall misalignment between its branches around the world induced many to believe that PMI is not yet prepared to let go the past and go fully sustainable.

Communication

When assessing how to communicate and reach consumers in an effective way, tobacco companies must innovate since most of the usual marketing channels are restricted by tight regulations implemented in the last decades. PMI has relied and continues to rely on its reputation to ensure word-of-mouth as an effective means of getting consumers to know about their products. To support this process, PMI launched a global campaign called "Unsmoke" in 2019, which was rolled out across various online and offline channels. Given widespread misconception and mistrust towards PMI's intentions, the campaign's goal was to move smoke-free products and their potential benefits for public health into the center of attention and clear up misunderstandings. The campaign followed a clear message: *"If you don't smoke, don't start. If you smoke, quit. If you don't quit, change."* (Unsmoke your World, 2019). To target specific groups, the campaign addressed the general public with the claim "Unsmoke Your World" (UYW) while "Unsmoke Your Mind" (UYM) was aimed to reach opinion leaders. UYW targeted individuals and had the goal to inform them about the existence of better alternatives as well as encourage the general public to call for regulations that improve access to information. UYM rather addressed general misconceptions on smoke-free products and demanded for an open conversation between tobacco companies and regulators as well as other stakeholders (PMI Integrated Report 2020). The key focus of the campaign was on the concept of harm reduction with the goal to reduce the negative impact of people's choices (Unsmoke your World 2019).

Sales

From a selling standpoint, with the IQOS launch came a transition from a conventional B2B model to a more Direct-to-Consumer (D2C) approach. This meant that much focus would

be given to IQOS unique points-of-sale (POS), examples of which are specialty stores, kiosks, pop-up stores and "corners" in convenience stores (Israel Journal of Health Policy Research, 2019). Even though the strategies employed to promote IQOS-related products are different according to the type of POS analysed, one common practice seems to apply to all of them: the products sold should not be directed for young consumers. The company is taking this strategy so seriously that by 2023, it hopes to have its whole array of electronic smoke-free products outfitted with age-verification technology. (PMI Integrated Report 2020).

As it was already stated, the launch of IQOS resulted in a more customer-centric approach based on a D2C business model. Further, as HTPs require detailed explanation and sharing of clear information to help consumers in their decision-making, the company opened both stationary boutiques as well as temporary stores.

The adoption of this new model of doing business also led to a shift in the company's strategies to get closer to consumers. At this time, the company took in a lot of efforts to gather reliable data that could be used in planning certain aspects, such as IQOS store locations and the interior materials of these stores (Go-Popup, 2021). These stores allowed PMI to get closer to the customer, and show and explain the new product on site, which played a key role in the branding of IQOS. In fact, a product like IQOS, which did not exist before, requires that all the aspects surrounding it, including the innovation itself, be transmitted in a clear way to consumers, and this direct interaction becomes a primal form of doing so.

With a minimal, modern and product-focused design, PMI aims to create a warm and welcoming atmosphere in which adult smokers have the chance to experience and test the new product (Exhibit 4). The personal contact with consumers during both the buying and after-sale process is one that PMI has never had before. Now, this offers it the opportunity to not only receive direct feedback on the product, but also follow up with consumers on their journey,

therefore contributing to IQOS' so called "customer experience". In general, IQOS stores play an important role in PMI's sales strategy, as they are the main marketing funnel to create awareness of the brand (Go–PopUp, 2021). PMI operates 24 consumer call centers that help consumers in the case that questions arise about the use of the product. Gathered insights are being collected and used for improvements in product development. By the end of 2020, there were a total of 259 IQOS stores and 2,200 exclusive IQOS retail touchpoints worldwide, offering support to adult smokers that are interested in learning about and experiencing heated tobacco technology.

PMI has invested heavily in training their IQOS coaches, who are instructed to follow the company's Good Conversion Practices. The stores do not only follow the purpose of selling IQOS to new consumers, but also serve as a service point for cleaning and replacing devices, as well as an opportunity to upgrade for current users. The latter includes sales of new device ranges and accessories that offer users the option to personalize their IQOS device.

Adding to the personal contact in the stores, PMI has developed its digital services to better serve customers. Particularly, the company has provided virtual sessions with IQOS coaches and built a customer relationship management system that offers tailored communication and gathers relevant data on switching rates (PMI Integrated Report 2020).

Switching consumers to IQOS

PMI has made significant progress towards its ambitious objective of having at least 40 million smokers transition from traditional cigarettes to PMI's smoke-free products by 2025, since the debut of IQOS. By the end of 2020, an estimated 12.7 million smokers have transitioned to IQOS and quit smoking. The total number of IQOS users amounted for 17.5 million in 2020, of which 72% stopped smoking cigarettes. Following the 2016 announcement

of a smoke-free future, and the fact that IQOS has been made available for sale in 64 markets so far, the volume of smoke-free products shipped by PMI increased tenfold until 2020, while the shipment volume of combustible products decreased by almost 200 million units over the same period of time. As a result, smoke-free products accounted for 10.4% of total shipment volume in 2020. Moreover, smoke-free products contributed 23.8% of total net revenues in 2020, up from 2.7% in 2016. This can be explained by a marketing overspend of 76% for smoke-free products (Exhibit 5). While consumer acceptance of IQOS varies in different markets, the biggest success story emerged in Japan, which became the first country where the shipment volume of heated tobacco units exceeded that of cigarettes (PMI 2021).

According to PMI, the number of smokers switching to IQOS could be much higher if more adult smokers had better access to its smoke-free products. “Access” is defined along four variables: (1) awareness of the benefits of smoke-free products, (2) acceptance of products by smokers as a viable alternative to cigarettes, (3) availability of products for sale to smokers and (4) affordability of smoke-free products. But how can access be achieved? When raising awareness, PMI wants smokers to understand the differences and benefits of smoke-free products compared to combustible cigarettes, while also stressing out the fact that smoke-free alternatives are not risk-free. Awareness is strengthened by information, and PMI puts in place an internal process to ensure that messages to consumers concerning smoke-free alternatives are clear through comprehension research in various markets. Smokers will stop smoking cigarettes and switch to better alternatives only if they prefer them, and this process is defined as product acceptance. Acceptance is measured by the full-switching rate, which is defined as the percentage of IQOS users who have stopped smoking traditional cigarettes compared to the total of IQOS users. According to PMI, a switching rate of 100% will make conventional cigarettes obsolete. Availability is a particularly important component as it refers to the possibility of making smoke-free alternatives available to smokers, and this depends on

countries regulatory framework. Finally delivering a smoke-free future will be highly dependent on making better alternatives to smokers affordable. Economies of smoke-free alternatives are different from those of traditional smoking and require customers to buy a device to heat tobacco. The retail price for IQOS ranges from 29 to 49 euros depending on the model. To address cost barriers, PMI has implemented actions, such as lending the device or payment over time (PMI 2020).

To achieve this, PMI calls for a regulatory framework driven by governments, policy and regulators that allows smoke-free products to be sold and adult smokers to be informed about the existence and availability of these products (PMI 2020). *"We're optimistic about the future as we work to progressively transition PMI's existing cigarette business to potentially less harmful alternatives. There is tremendous opportunity to positively impact public health with the availability of better choices than continued smoking, and we can't do it alone. Contributions from public-health experts, the scientific community and regulators will greatly accelerate switching from cigarettes to smoke-free products.",* said Tony Snyder, PMI's former Vice President of Communications (PMI 2019).

Engaging stakeholders

PMI is aware that the success of its strategy depends not only on consumers acceptance of the new products, but also on other external stakeholders such as regulators, the scientific community, investors, and NGOs. However, engaging stakeholders has been challenging, and the public debate on smoke-free products has been controversial. In response to the launch of IQOS, for instance, health charity "Action on Smoking and Health" called for independent evidence to prove that IQOS is significantly less harmful than smoking, as well as for further investigation of risks of youth uptake and research on economic and social cost of dependence

(ASH 2016). In 2017, PMI and other tobacco companies were excluded from the United Nations Global Compact (UNGC), following a letter signed by over 200 organizations calling for a permanent participation ban for tobacco companies. Critics have claimed that the UNGC serves as a point of entry for multinationals seeking to expand their policy influence over the UN and its agencies (Tobacco Tactics, 2021). UNGC argues that *"the decision recognizes that tobacco products are in direct conflict with UN goals, particularly with the right to public health, and undermines the achievement of SDG 3"* (United Nations Global Compact 2021).

Moreover, in 2020, the U.S. Food and Drug Administration (FDA) approved the marketing of IQOS tobacco heating device, with information about "reduced exposure" (FDA 2020), although the University of California Center for Tobacco Control Research and Education and the US Tobacco Products Advisory Committee recommended against such authorization (Center for Tobacco Control Research and Education UCSF 2020, Reuters 2018). The authorization allows the use of claims in the scope of "exposure modification" in the U.S. – however, *"the FDA determined that the evidence did not support issuing risk modification orders"* (FDA 2020). Nevertheless, PMI communicated FDA´s authorization as a major achievement for the company, hailing the decision as a *"milestone for public health"* (PMI 2020). Thereupon, WHO published a statement reminding its member states of the prohibition of false, misleading, or deceptive tobacco advertising and that *"reducing exposure to harmful chemicals in HTPs does not render them harmless, nor does it translate to reduced risk to human health"* (WHO, 2020). To avoid potential misinterpretation of the FDA authorization, the Tobacco Control Research Group at the University of Bath published a briefing summarizing the scientific findings on IQOS and calling for caution and close monitoring of PMI's marketing activities. (TCRG 2020).

Further, the regulatory landscape for cigarettes, and particularly for new generation products, varied significantly around the world (Exhibit 6). Following the introduction of HTPs

and e-cigarettes, several regulations were enacted, ranging from no bans to complete bans in certain markets. For instance, countries like Hong Kong and Singapore banned e-cigarettes and HTPs with the reasoning that they encourage smoking among young people (South China Morning Post 2021, Ministry of Health Singapore 2020). According to Calantzopoulos, regulators are one of the most important stakeholders and key players in achieving the success of a smoke-free future: *"On our side, we can develop a portfolio of products, put our money into commercial efforts, but we need the government to play the game as well; for consumers to change their behavior, you need products, but you also need incentives and differentiation...taxation, labelling, are all important."* (Barron's 2019).

Looking ahead

Despite all the efforts over the past years, PMI still faces widespread mistrust from institutions, regulators and consumers, a fact that the company sees as the biggest challenge on the way to achieve the goal of becoming a predominantly smoke-free company by 2025. Tight regulations and marketing bans for smoke-free products reduce opportunities for PMI to create awareness for IQOS and its potential benefits, and the less opportunities there are for PMI to spread information among current consumers, the less smokers switch to IQOS. Will enough smokers switch to IQOS or is the smoke-free future at risk? Can trust be regained with a product that, while potentially less harmful, remains highly addictive? As a second area of activity, PMI started to explore business areas beyond tobacco and nicotine, and formulated a second goal of generating *"at least $1bn in net revenues from Beyond Nicotine products by 2025"* (PMI 2021), a move that will help it evolve into a broader lifestyle and consumer wellness company. The first step in that direction was the acquisition of Vectura, a UK-based inhaler company, in September 2021, which Calantzopoulos described as *"that missing capability in*

order to develop products that have nothing to do with nicotine" (Financial Times 2021). However, also in this case, PMI is accused of false intentions. In fact, the public debate on the deal was controversial, and public health and anti-smoking charities called it *"an unresolvable ethical conflict"* (British Thoracic Society 2021). In particular, they refer to the fact that PMI currently still generates most revenues with combustible cigarettes, raising once again the issue of trust. Even if only for the transition phase, can the two business areas coexist?

***

As a young professional, you are thinking about investing your money in stocks. PMI is also on your watchlist, but you are unsure whether it is the right decision to invest in the company. Big questions are buzzing in your head: Should you reward PMI's approach to reinvent themselves and address the problems they helped created or do you choose not to engage with tobacco companies? Do you trust PMI's intentions, and do you believe in a smoke-free future and the Beyond Nicotine strategy? What would you expect from PMI as a shareholder?

Field Lab in Partnerships for

Sustainable Development

Project Evaluation Report

1. Philip Morris International

Key facts

- Philip Morris International is a Swiss American multinational company leading the **cigarette and tobacco market**.
- It is listed on the New York Stock Exchange (NYSE: PM) since 2008 and employs **71,000** people around the world.
- PMI is present in **over 175 markets** around the world and serves **150M consumers**.
- 5 of the top 15 international cigarette brands in the world are theirs, including Marlboro.

Current market position of the company: Leading company in the cigarette & tobacco industry.

Competitors: British American Tobacco, Japan International Tobacco.

First mover advantage: PMI first began selling the heat-not-burn device in Japan and Italy in 2014 in limited test markets. After a great response, it rolled it out into more markets and started selling IQOS throughout Japan, Italy, Portugal and more. PMI is the first and only tobacco company stating that they want to end conventional cigarette sales.

Market leader: With the introduction of new products and more market exposure to these new products, PMI will face increasing competition but having stepped so far ahead of the competitors it will be challenging for rivals to catch up.

1.1 Philip Morris International's vision of a smoke-free future

Smoke-free Future refers to PMI´s vision for 2025 and beyond, in which most of their clients will consume non-combustible tobacco – IQOS. These smoke-free products, while not risk free, are a "far better choice than cigarette smoking" (PMI, 2021)

PMI´s Goals

To generate +50% of total net revenues with smoke-free products by 2025.

Commercialize IQOS in 100 markets by the end of 2025 – up from 64 markets at the end of 2020.

How to achieve it? – Strategies

- Investments to develop, market, and sell smoke-free alternatives.

- Create awareness to switch adult smokers to these alternatives as quickly as possible.

- Transition their resources from cigarettes to smoke-free products through sustainability programs across the entire value chain.

- Propose favorable regulatory policies that stimulate the substitution of cigarettes and gather support from civil society.

- Engage with stakeholders (employees, communities, etc.) to speed the transformation while mitigating negative consequences.

- Increase transparency in the progress, share scientific findings and encourage others to review them.

PMI´s success so far: 18M IQOS users by end of 2020. Successfully passed the bar of FDA-PMTA authorizing the marketing of IQOS as a Modified Risk Tobacco Product.

2. Problem statement

- On the way to a smoke-free future, PMI has two main challenges: Firstly, there is a **lack of awareness for the new product IQOS**. Creating awareness for IQOS is needed to switch current smokers to an alternative product. Secondly, the company faces **widespread mistrust from stakeholders**. Regaining trust and cooperation with stakeholders, however, is critical for achieving its ambitious goals. Even though mistrust towards PMI has also been found among consumers, regaining trust from regulators and other stakeholders has priority to influence more favorable regulations for smoke-free products.

- It is essential to focus on both challenges in this report, as the two parts are highly interrelated. In many countries, tobacco products, including reduced-risk products, are highly regulated. Tobacco companies are calling regulators for more favorable regulations for reduced-risk products. To support this process, PMI must regain lost trust. Only if regulators would introduce more favorable regulations for reduced-risk products, tobacco companies will have more opportunities to create awareness for IQOS.

- Retrieved from the abovementioned challenges, the report will answer the following research question: **Is a smoke-free future attainable and which actions are needed in order to achieve this goal?**

3.1 Literature review – Generic information on trust

Sucher/Gupta found that trust plays a major factor for a company's success. Trust develops when a company creates products and services that work, has good intentions, and takes responsibility for all impacts the organization has, be it intended or not.

Three steps to regain trust

1. Take responsibility

Companies should first take responsibility for the harm that has been created and apologize for it.

2. Fix accountability

Secondly, companies should fix accountability for what was wrong. What people care about is that the person who is responsible for what goes on be held accountable.

3. Present long-term strategy

Finally, they should present a long-term strategy for trying to fix what caused the damage in the first place.

Two promising tactics

Sustainability reporting

Sustainability reporting can play an important role in getting a company's story out. Companies win over consumers' trust by transparently presenting the strategy, the actions taken, the stakeholders that the company is trying to satisfy, measurable progress that it is making, and all activities that still need to be done.

The first audience is inside the organization

If trust is built from the inside out, the people who really need to understand what the company has done, and what it is doing to make good on what happened, are the people inside the company. They are the first ones that can carry the transformation story to the outside (Sucher/Gupta, 2021).

3.2 Self-Developed Trust building framework (1/2)

Disclaimer: There is a lack of trust building frameworks with regulators for the tobacco industry and a lack of applicability of existing trust frameworks for other industries. This is due to the fact that leading organizations recommend regulators not to engage with tobacco companies because of the fundamental conflict of interest between tobacco companies' interests and public healthpolicy interests. The regulators follow the WHO Framework Convention for Tobacco Control (FCTC), aiming to align memberstates' interactions with tobacco companies (further explained in page 8). Our self-build framework has been developed based on Guidelines for Implementation of Article 5.3 of the WHO FCTC, which delivers guidelines for regulators on how to interact with tobacco companies. Based on given recommendations for regulators following these guidelines, we retrieved implications and best practices for tobacco companies by claiming that tobacco companies should voluntarily align to the principles of FCTC. The idea is,if tobacco companies follow the provided best practices, they might be able to regain trust from regulators and win a seat at the table.

Nevertheless, we are aware of both the practical and ethical limitations of this framework. In practice, it will be extremelychallenging for tobacco companies to regain trust, no matter how much effort they put into this issue. As long as tobacco companies sell a deathly product, regulators will meet them with mistrust, monitor them closely and regulate their actions.

3.2 Self-Developed Trust building framework (2/2)

WHO FCTC Guideline	**Principle 2:** Accountability and transparency in interactions between regulators and the tobacco industry.	**Principle 3:** Accountability and transparency in operations of the tobacco industry.	**Principle 4:** Discouragement of incentivization of/and collaboration with the tobacco industry.
Recommendation for regulators	Regulators are recommended to require the information provided by tobacco industry to be transparent and accurate.	Regulators are recommended to denormalize and regulate tobacco companies' CSR activities.	Regulators are recommended to reject partnerships with the tobacco industry and do not provide special treatment to the industry in general.
Implication for PMI and Best Practice	The tobacco industry should be accountable as well as transparent in interactions with tobacco control and public health officials and voluntarily provide required information.	The tobacco industry should be accountable and transparent in all operations. PMI is recommended to continue improving sustainability actions along the value chain.	PMIs engagement in public affairs is not wanted. Regaining trust is extremely challenging, however, transparency and products that might actually improve public health helpthe industry to make its point.

Based on: WHO FCTC Guidelines for Article 5.3 (WHO, 2021).

3.3 Literature review – Tobacco Control and Regulations

Tobacco is one of the few products on the legal market which, when used explicitly as the manufacturer intended, leads to untimely death and disability. Had the product been released on the market today, it could never meet the regulatory requirements for sale. However, due to the important role that tobacco now plays in many communities, no country has sought to delegalize any tobacco-related product. The preferred public policy has been to use public monies to convince citizens not to smoke (National Research Council, 1997).

This policy is broadly referred to as tobacco control.

Objectives

1. Protect non-smokers in society
2. Reduce prevalence by encouraging smokers to quit and discouraging non-smokers from starting to smoke

In 2003, the **Framework Convention on Tobacco Control (FCTC)** is almost universally adopted as a treaty that establishes certain global standards for tobacco control policies. These policies seek to manipulate the price of cigarettes, limit the access of the young, and encourage places where non-smokers will be protected from the harmful effects of tobacco smoke. Further, mass media can also be used as a channel for tobacco counter advertising.

Countries have developed and strengthened their regulations based on the FCTC, leading to smoking reduction as the framework helped keeping tobacco control at the top of political agendas.

Lobbyism, litigation and trade disputes to delay and prevent governmental action on smoking become inherent to the tobacco industry, but eventually companies realize that these practices are not ethical nor sustainable in the long-run.

3.3 Literature review – Tobacco Control and Regulations

How Tobacco Companies have evolved

1. **Partnering with Science**

   Increasing collaborations with scientists and researchers led to the emergence of more innovative smoking alternatives, which are more difficult to control and regulate. In fact, doing so would almost mean turning a back on science.

2. **WHO continues to classify HTPs as conventional tobacco**

   Because of the strict definitions of 'tobacco products', health authorities continue to put Heated Tobacco Products (HTPs) in the same basket as combustible tobacco (further explained in page 22). However, WHO is reportedly collecting data to evaluate the evolution of trends so that a more specific regulative framework can be applied to HTPs (Gruszczynski/Melillo, 2020).

Science-based solutions that envision the reduction of harm in consumers' health have been the priority to bypass tobacco control policies.

This increasing innovation in less harmful products means a constant adaptation of public policies in formulating new regulatory measures to meet these solutions.

Which would be preventable had HTPs and other smoke-free products been regarded as different products than traditional tobacco in regulatory frameworks.

3.4 Literature review: Harm reduction as a communication tool

In 1974, Michael A.H. Russell, a British tobacco addiction expert, publishes an article citing the dangers of tobacco and nicotine for consumers' health. However, Russell believed that "the goal of abstinence and the abolition of all smoking is unrealistic and doomed to fail" (Rodu/Godshall, 2006). As a result, the solution does not lie on trying to eradicate smoking-related issues, but to reduce them.

Tobacco Harm Reduction: It involves the use of alternative less harmful sources of nicotine, including HTPs, by those smokers who are unable or unwilling to quit tobacco and nicotine entirely.

For HTPs specifically, manufacturers claim that levels of toxicants and hazardous compounds are significantly reduced, implying that inhalation of the modified aerosol is less harmful to the user's health compared to conventional cigarettes (Mallock, 2019).

Do not Want Vaping*

HTPs offer 50% to 90% less exposure of harmful compounds seen in cigarettes

HTPs

Accept Vaping

HTPs offer less harm reduction than e-cigarettes (UK Government, 2018)

HTPs should be the first smoking-alternative only for those who do not like vaping devices as substitutes of conventional cigarettes

*vaping = using e-cigarettes

3.4 Literature review: Harm reduction as a communication tool

The Path to a Smoke-Free Future

1st Step: Researching and developing better non-combustible alternatives that are scientifically substantiated.

2nd Step: Broadening access for adult smokers, while simultaneously working to phase out cigarette smoking.

But is it even possible to advertise this harm reduction to consumers with so many communication channels blocked?

Here, a priority should be given to assuring consumers that these products would only be targeted for smokers.

According to PMI: *"Smoke-free products are for adult smokers who would otherwise continue smoking. The best choice any smoker can make is to quit cigarettes and nicotine altogether."* (Smart Brief, 2021)

Ordinary communication channels are very limited

Regulatory frameworks protect consumers from tobacco products that, even being less harmful, still produce damage to users' health.

Need to innovate in communicating harm reduction

Points to Consider Going Forward

- Proven policy drivers – such as taxation, advertising bans, smoke-free public spaces, and graphic health warnings – that reduce tobacco use, must continue to be at the core of tobacco control efforts (Bialous & Freeman, 2021)
- Word of mouth as a means of advertising tobacco between consumers who are already smokers.

4. Methodology

To obtain primary data, and identify some principles and information about our samples, **survey** and **individual interviews** were used as our methodology.

The survey methodology aimed to assess the **prevalence of tobacco users**, as well as the factors leading current tobacco consumers to switch to smoke-free alternatives such as IQOS. We also aimed to assess the **general awareness of the harm** caused by tobacco and the benefits associated with a **transition to Reduced Risk Products**. Lastly, we tried to understand the **public trust factor** and its implications for tobacco companies and for the tobacco industry.

- **Participants:** 205 over the age of 18 responded to the survey online.
- **Sampling method:** Random selection (Criteria: +18 years old). We have grouped the respondents into three different categories for a more detailed analysis of each group: smokers of conventional cigarettes, IQOS users, and non-smokers.
- **Type of data:** Quantitative, primary descriptive data in which we gathered information without intervening.
- **Validity:** Carefully designed survey that can be replicated by other researchers. Open ended questions in the survey increase validity.
- **Limitations:** Small sample especially for each sub-group.

4. Methodology

The individual interviews methodology aimed to understand the key reasons that led tobacco users to switch to IQOS, as well as the reasons preventing them from switching. A deeper understanding of these determinant factors will contribute to maximize the number of smokers that do not intend to quit smoking to transition to a less harmful alternative.

- **Participants:** 10 respondents over the age of 18 were directly contacted to respond to the interview questions online (note taking).
- **Sampling method:** Non-random selection. Participants were selected based on predetermined criteria and divided into two sub-groups: smokers of conventional cigarettes and IQOS users who do not intend to quit smoking. All participants have a shared background of smoking.
- **Type of data:** Qualitative in order to obtain real world knowledge about consumers' preferences and perceptions. This is a less controlled methodology but more interpretative, in which answers were given in real-time to us.
- **Validity:** Structured interviews that result in concrete answers about the topic to measure.
- **Limitations:** Small sample, accessibility of respondents

5.1 Hypotheses

With the goal of achieving a smoke-free future, PMI still faces widespread mistrust from stakeholders and a general lack of awareness for its product. Garnering further insights about these two factors will be critical for the company to achieve its ambitious goals for 2025 and beyond.

PMI's Status Quo

Focus on becoming a sustainable company by focusing in two main areas:

- Sustainability actions along the **value chain** (eg: Diversify productions of tobacco farmers).

- Sustainability actions related to the **product** ((eg: Development of Reduced-Risk-Products (RRP)).

Hypotheses

- There is a general lack of awareness for IQOS;
- Widespread public mistrust towards tobacco companies is still present.

5.2 Evaluation Status – Main findings from Survey (smokers/non-smokers/IQOS users)

- Smokers are aware of the health implications but not of alternatives that can mitigate smoking damages, 50% are not aware of technology and potential benefits of IQOS.
- Arguments in favour of converting to IQOS are linked to **less smoke, no ash and cheaper prices**.
- Negative connotations of smoking are linked to **health damages** and **high financial burden,** while negative perceptions of IQOS are linked to **addictions**, **battery duration**, and the possible long-term health consequences.
- 36% of participants still believe that IQOS is a good alternative to quit smoking.
- Arguments in favour of IQOS relate to **less smell** and better feeling compared to traditional cigarettes.
- 50% believe **Governments should invest** in technology that promotes the development of less harmful alternatives.
- 67% think **more regulation and taxation** should be implemented to further pressure tobacco companies.
- Generally, consumers believe tobacco companies should be **more transparent** and **cooperative with public entities**.
- Respondents are divided between believing in the achievement of a smoke-free future, yet most seem to agree that **it is not attainable by 2025**.

5.2 Evaluation Status - Main findings from interviews – IQOS Users

- The switch to IQOS from cigarettes primarily relates to **health concerns**.
- IQOS awareness comes predominantly from **word-of-mouth**.
- In terms of impacts of IQOS in interviewees' health, they almost unanimously state that, even though there is still a bad feeling towards using IQOS, health seems to improve, especially apparent in doing sports and less coughing.
- Regarding what interviewees dislike about IQOS, answers seem to differ a lot: some state the need to charge as troublesome, the fact that they smoke more and the expensive nature of the machine and HEETS.
- Most users are not aware of the characteristics that make IQOS a less harmful alternative, and those who are aware do not know the details about it. Some argue that **more independent research** should be conducted.
- All interviewees say that they will never go back to smoking cigarettes.
- Respondents who used IQOS customer service say it was acceptable and all requests were complied, but most didn't even need it.
- No respondent trusts tobacco companies, they feel they take use of an addiction as a profit-making consumer characteristic.
- To correct this trust, most suggest being more transparent in terms of the science behind the new products PMI releases. Not only that, but they also think that most information is made available by PMI and not independent researchers/media outlets.
- As for the Smoke-free initiative, participants think it is a step in the right direction, but it is difficult to attain because of the need to change consumers' perception of the company and of smoke-free products in general.

5.2 Evaluation Status - Main findings from interviews – Smokers

- All participants are **aware of IQOS as an alternative** for conventional cigarettes but not all are aware of how it works.
- Main factors preventing people from switching to IQOS are the **taste**, **smell**, and **little knowledge** about the product.
- The **design of IQOS appeals to most respondents**. One respondent mentioned that it looks very electronic and technical, and that its larger size makes it less easy to smoke.
- If the **benefits of IQOS were more readily available** consumers would probably switch also due to the **cheaper price**. One respondent mentioned that increased prices for traditional cigarettes would convince her to switch to IQOS.
- In general, **mistrust** is a factor preventing people from switching to IQOS. Consumers know that it is a better alternative but recognize it is **still harmful** and the **long-term health impact cannot yet be proved**.
- Regarding the correlation between a better access to information and consumers switching to IQOS, responses are different. For some, a **better communication would probably impact their decision**, while for others, their **social context is a no go** for IQOS.
- All respondents mentioned that **regulators should allow better access to information** on alternatives to smoking.

5.2 Evaluation Status - Main findings from interviews – Both Groups: Smokers & IQOS users

- Most people **do not trust tobacco** companies because they believe **profit is their ultimate driver** just like any other company, but the difference here is that they are profiting with a product that is **highly addictive** and **kills people**.
- Respondents mentioned that **governmental verification of manufacturing processes** to guarantee **standards** and more **transparent information** would increase their trust on tobacco companies.
- People think that the information made available to the public by tobacco companies is **not clear nor transparent and** suggest **more state control** to improve it. Others mention the **lack of scientific proof** that IQOS is less harmful and therefore should not be promoted as an alternative.
- The majority believes PMI´s goal is **not attainable** since people will keep smoking even though they are aware of negative health consequences. Disruptive events/actions needed to take place for people to stop smoking. Others see IQOS as a greenwashing strategy only.

5.3 The challenge of awareness creation and the role of regulations

After having better understood the consumer perception and the general awareness of IQOS as well as the public trust factor in the survey, four main points of criticism that consumers mentioned have been identified:

- Lack of clear and transparent communication by PMI.
- Limited opportunities for PMI to create awareness for IQOS and the need of regulators to allow better access to information.
- Tobacco companies should be more cooperative with regulators and governments.
- Lack of trust towards tobacco companies

The current unfavorable regulations for smoke-free products result in few opportunities for the company to create awareness for IQOS. As a result, the company's communication might be perceived as less clear and transparent. To influence regulations to be more favorable, however, the company must regain trust of regulators and other stakeholders. This topic will be further explored in the upcoming pages.

5.4 Origins of mistrust (1/2)

To better understand the trust issue that PMI is facing, it is crucial to identify the reasons for mistrust. It has been found that mistrust towards tobacco companies has diverse origins that, in combination, all contribute to the overall skepticism regulators have. The below mentioned serves as an overview of possible origins but is not limited to it.

The past: Tobacco companies are known as pioneers of fake news, after largely spreading misinformation to protect revenues in the face of mounting evidence of links between tobacco smoke and serious illnesses. The industry has been accused of dark money lobbying and sponsoring questionable academic studies.

The product: The industry has been selling a highly harmful and addictive product killing 8.1 million people worldwide annually. Despite efforts towards better alternatives, the business model remains on selling addictive products. Therefore, critics question how much such an industry should be trusted when it says it is interested in consumers' health.

Little independent research on smoke-free products: As PMI's smoke-free products are rather new in the market, there have been few independent scientific studies on the actual risk of the products so far. Due to a general mistrust in research conducted by tobacco companies, people are uncertain on how to assess the new products.

5.4 Origins of mistrust (2/2)

Misleading communication: The term "smoke-free future" might be misleading as it might insinuate that the company will stop selling tobacco and nicotine products once and for all. However, IQOS presents a large pillar of the smoke-free vision. Such misleading communication does not help in building trust.

Contradicting actions around the world: While committing to a smoke-free future on one hand, PMI was still marketing cigarettes heavily in many medium and low-income countries on the other hand, where about 80 per cent of the world's smokers now live. Critics, therefore, question the true intentions for the new strategy.

Acquisitions that follow the company's Beyond Nicotine strategy: Recently, PMI acquired UK inhaler group Vectura. Even though PMI justifies the merger as part of its plan to become a "healthcare and wellness company", the two business areas are not necessarily perceived as following the same strategic direction. Critics call it a cynical form of vertical integration.

Implications for PMI: The analysis shows that every single action PMI takes contributes to how they are perceived as a company. Influenced by the past, critics will always watch tobacco companies more closely which is why they must avoid controversies.

5.5 Evaluation Status Quo: regulatory dilemmas examples for HTPs

Even though countries regulate tobacco products differently, new innovative products such as HTPs pose major challenges on international frameworks on tobacco control, more importantly regarding the FCTC.

Tobacco regulation mainly focuses on cigarettes. Still, the FCTC tries to cover a broader array of tobacco products and defines them as "products entirely or partly made of the leaf tobacco as raw material, which are manufactured to be used for smoking, sucking, chewing or sniffing" (Art. 1(f)). When HTPs were introduced, regulators faced the dilemma on whether they should have been regulated by the FCTC. Because HTPs contain tobacco, they can be regarded as "partially made of tobacco leaf". However,for regulators it can be tricky to address if HTPs are made for "smoking, sucking, chewing or sniffing", as the tobacco industry claimed that the emissions produced are not smoke but vapor, leading regulators to re-think whether to include newer tobacco products and how to classify them. Nevertheless, the WHO states that HTPs are tobacco products and should be regulated in line with the FCTC.

Regulators struggled on addressing the electronic components of HTPs used for tobacco sticks. The tobacco stick clearly is in the category of tobacco products. This loop in legislation poses a challenge to regulators, as tobacco companies might be able to advertise the electronic device by placing posters in strategic sectors.

Other challenges link to ensuring regulations are applied to tobacco products and devices, which can be attractive for consumers. Turkey faced this problem with shishas and was praised when it implemented laws requiring health warnings on devices.

Gruszczynski/Melillo, 2020)

5.5 Recent decisions on HTPs by governments and complex regulatory situation

Due to the novelty of the HTP category, the regulatory situation is unclear and varies around the world. Following applications to authorize IQOS in a certain way, different countries have made different decisions. The following three examples represent the controversial regulatory decision-making on HTPs:

United States: The US Food and Drug Administration (FDA) authorized the marketing of the IQOS tobacco heating system with "reduced exposure" information in August 2020, allowing claims that switching fully from cigarettes to IQOS minimizes exposure to dangerous chemicals. The FDA, however, denied PMI's claim that IQOS users have a lower risk of disease. (FDA, 2020).

Italy: The Italian Ministry of Health denied an application by PMI to certify IQOS and HEET sticks as reduced-risk products in March 2020. Based on the information presented by PMI, the ministry has called for more independent research and has classified the new HTP technology as a "public health issue." (Ministero della Salute, 2020).

Australia: The Australian Department of Health's Therapeutic Goods Administration (TGA) rejected PMI's request to change the country's Poisons Standard with respect to nicotine in favor of HTPs in August 2020. As a result, the sale of HTPs in Australia will be prohibited indefinitely. HTPs, according to the TGA, will not make a major contribution to harm reduction. (TGA, 2020).

Implications for PMI: The disunity of global regulations for HTPs poses a high level of regulatory risk for PMI. The success of IQOS is dependent on the regulatory framework in each country, which currently is highly dynamic and inconsistent.

5.5 Overview and trends of the regulatory environment for HTPs around the world

A look at the regulatory frameworks and measures for HTPs shows trends and implications for the future.

Countries where HTPs fall under existing tobacco control laws

Due to the novelty of HTPs, many countries have not yet introducedspecific regulations for the category. As a result, existing tobacco control lawsapply, yet the regulatory environment is often not comprehensive. Advertising law for HTPs vary across Europe – the plain packaging law, for instance, does not apply in France and the UK.

Countries taking specific regulatory actions on HTPs

More and more countries have amended existing legislation to include HTPs or introduced entirely new legislation. Canada, for instance, amended its law to include the heating device within the definition of "tobacco product", meaning that all components of HTPs are covered by advertising bans and the plain packaging law (TPVA, 2018). Moreover, the Portuguese regulator has included HTPs under thesmoke-free law and extended its law on tobacco advertising to include heating devices (Law No. 63/2017 Portugal, 2017). The United Arab Emirates passed an Electronic Nicotine Products standard, which controls HTPs and requires to specify the product's production, import, retail and display. As a result, HTPs are now covered by the same regulatory framework as tobacco products (European Commission, 2020).

Implications for PMI: In recent years, an increasing number of countries have reacted to the novel products in the market by adopting new laws to specifically regulate HTPs. That way, regulators closed loopholes to the detriment of tobacco companies that have been using them to create awareness for HTPs. With this example, it is likely that more countries will follow this trend.

5.5 Outlook of regulatory scenario for HTPs

The regulatory environment for HTPs might change in the future once sufficient scientific evidence emerges. According to the literature, three possible scenarios might emerge, calling for specific actions accordingly.

HTPs do not reduce health risks for users (ex-smokers)

- Total sales ban. This approach will limit the variety of products on the market and decrease attractiveness of tobacco products to consumers.
- Ban on deceptive descriptors on packages such as 'light' or 'ultra-light'.
- The preliminary rational is that if the product is not less harmful it should not be in the market.

HTPs reduce health risks, but some potential systematic risks are real and difficult to regulate

- HTPs should remain under classification of tobacco products, therefore subject to traditionaltobacco control. This will allow consumers to switch to HTPs, but still will not undermine existing tobacco regulation aimed at tobacco eradication.

HTPs reduce health risks and do not pose systematic risks

- No regulation is unadvisable as HTPs are still addictive.
- Regulations should maximize benefits of switching to HTPs.
- Keep advertisement and age restrictions.
- Allow only commercial communication concerning relative risks of HTPs (Gruszczynski/Melillo, 2020).

Implications for PMI: Even if HTPs are not considered harmful, regulations might still be in place, limiting advertisement

5.5 Regulatory outlook and expert opinions

Future regulations for HTPs are unclear. Science serves as the groundwork and leading government agencies provide guidance for regulators. Current findings might give an outlook on how regulations for HTP will develop.

Extract of research findings on IQOS

- IQOS reduces exposure to harmful and potentially harmful constituents (HPHCs) compared to standard cigarettes.
- When IQOS emissions are compared to combustible cigarette smoke, PMI's research indicates much higher amounts of numerous substances that are not recognized as HPHCs by the FDA. The consequences of these chemicals are unknown. (St Helen et al, 2018).
- IQOS could cause organ toxicity that has never been linked to cigarettes before. (Chun et al, 2018).

Expert opinion from World Health Organization

- WHO states that there is insufficient evidence to support the claim that HTPs cause less harm than conventional cigarettes. Additional research is needed to confirm any claims related to less risk/less harm.
- The link between exposure and health effects is complex. Less exposure to harmful chemicals does not imply that the risk level for a human body decreases.
- PMI has not been able to prove that IQOS will reduce tobacco-related diseases. (WHO HTPs, 2020)

Implications for PMI: As long as there is no evidence demonstrating that HTPs are less harmful than conventional cigarettes, leading organizations such as WHO will recommend regulators to regulate HTPs as conventional cigarettes.

6. Summary of main challenges

The previously mentioned analysis can be concluded by the following main challenges for PMI:

- Due to widespread mistrust, cooperation with governments is challenging. Nevertheless, PMI is highly dependent on their decisions regarding taxation and regulations, especially in terms of awareness creation.
- Old misdoings and bad perception of tobacco companies are difficult to forget in consumers and regulators' minds.
- Terms (RRPs, smoke-free) that the company uses are misleading and contribute to mistrust.
- IQOS (unintentionally) reaches ex-smokers, non-smokers and youth.
- The company has not yet managed to demonstrate that IQOS is less harmful compared to conventional cigarettes. The lack of research results weakens its line of argumentation.
- PMI faces difficulties in making the message that IQOS is the better alternative easy to understand for everybody.
- Due to regulations, the company has few opportunities to create awareness for IQOS.
- PMI's communication is perceived as not being clear and transparent.
- People feel that information on smoke-free alternatives is largely provided by PMI and wish for more independent sources.
- The goal to become a predominantly smoke-free company by 2025 is perceived as very ambitious, not attainable and profit-driven.

7.1 The recommendations are ranked by two criteria and cover two scenarios.

To better assess the relevance of our recommendations, we ranked them by two criteria and developed two possible scenarios.

Prioritization of recommendations based on two dimensions:

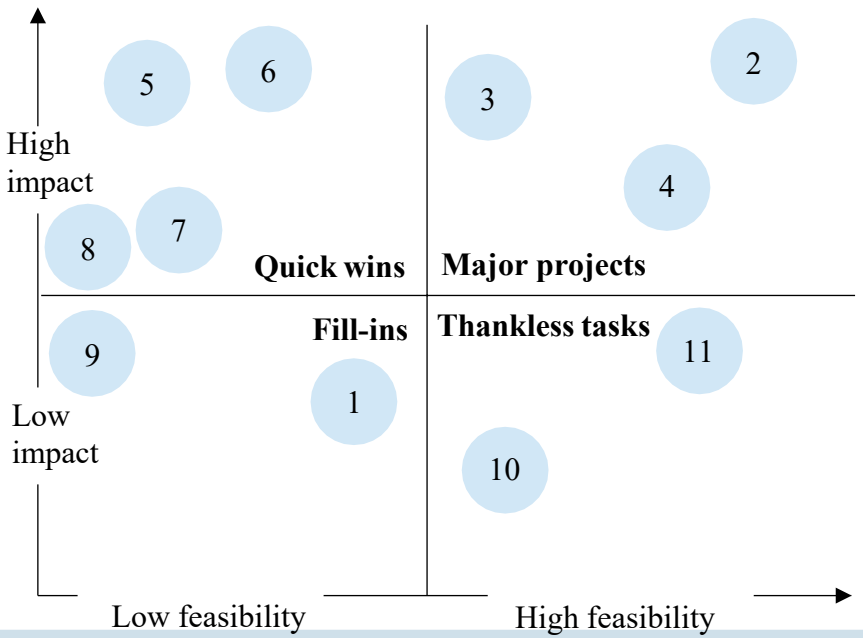
The given recommendations will be ranked according to an Action Priority Matrix based on two components: Feasibility and impact. Feasibility is defined as the degree of recommendations being easily implemented. This includes effort, costs and capacity needed to implement the recommended action. Impact, on the other hand, is defined as the effect the recommendation has for PMI's goal of delivering a smoke-free future.

Scenario analysis:

The company's main challenge, to regain trust, is a long-term process. It is not foreseeable which direction regulators will follow in the future since their decisions are highly dependent on new scientific findings. This situation creates uncertainty for PMI. In order to still deliver value with our recommendations for any development in the future, we provide recommendations for two scenarios. **Scenario one** projects a future in which the regulations will not change much, thus being more unfavourable for PMI and creatingfew opportunities to create awareness for IQOS. **Scenario two** assumes that new studies will find that IQOS poses less risk comparedto conventional cigarettes. As a result, regulators would introduce more favourable regulations and therefore more opportunities to communicate IQOS.

7.2 Recommendations for scenario 1: Current unfavorable regulations

1. Align company's actions voluntarily with FCTC, namely proven policies like taxation and graphic health warnings. (a)
2. Further build on Word of Mouth and use IQOS users as their main marketing channel, including "refer a friend" mechanisms. (b)
3. Increase the number of IQOS stores in strategic locations to create brand awareness. (b)
4. Communicate the science and concept behind IQOS clearly, transparently and easy to understand. (a/b)
5. Acknowledge and take responsibility for what mistakes happened in the past. (a)
6. Invest in R&D to prove that IQOS is less harmful compared to cigarettes and encourage independent research. (a/b)
7. Continue making IQOS accessible in terms of price. (b)



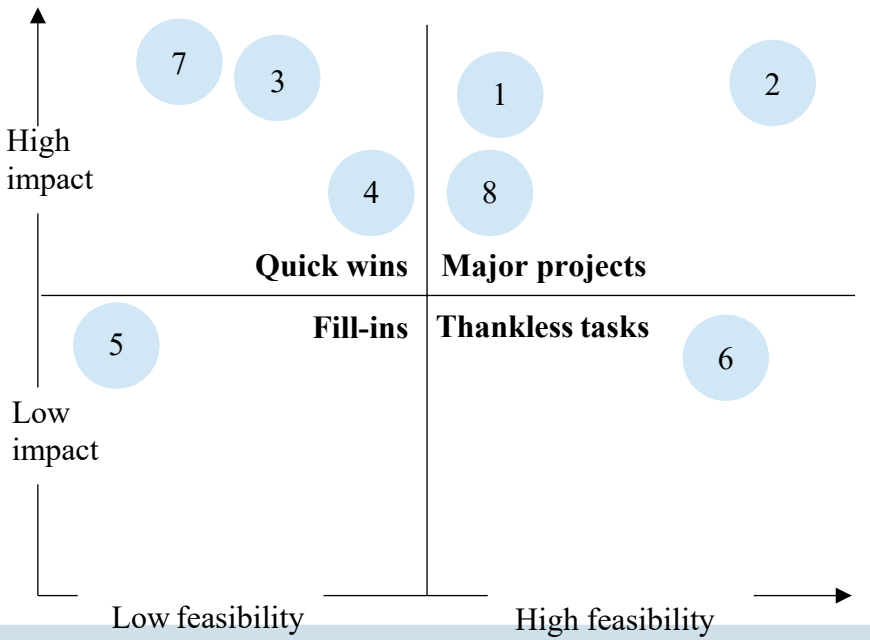
8. Voluntarily implement plain packaging in markets in which they are not required by law. (a)
9. Stop selling cigarettes now. (a)
10. Monitor the trend of unintentionally reaching people outside the target group and act accordingly. (a)

(a) = Recommendations related to trust
(b) = Recommendations related to awareness creation

7.2 Recommendations for scenario 2: Favorable regulations

Disclaimer: This scenario assumes that PMI was able to demonstrate that IQOS is less harmful than traditional cigarettes.

1. Use traditional marketing channels to market IQOS to maximize awareness of benefits of HTPs. (b)
2. Specifically target cigarette smokers via direct marketing. (b)
3. Keep current market prices of IQOS to not attract new non-smoking customers and increase prices of cigarettes. (a/b)
4. Improve Search Engine Optimization to clearly inform consumers about PMI Science. (b)
5. Cooperate with independent researchers to build trust and awareness. (a/b)
6. Establish IQOS as a lifestyle brand that helps smokers to live healthier. (b)



7. Engage regulators in informing smokers about the concept of harm reduction and creating awareness for IQOS. (a/b)
8. Engage passive smokers and doctors in campaigns for IQOS to not engage with the product and convince cigarette smokers to switch to IQOS. (a/b)

(a) = Recommendations related to trust
(b) = Recommendations related to awareness creation

8.1 Implementation plans

Since scenario 1 is most likely to happen in the upcoming years, the implementation plans will focus on this scenario only.

According to the Action Priority Matrix, we identified three Major Projects:

1. **Further build on Word-of-Mouth and use IQOS users as their main marketing channel, including refer a friend mechanisms.**

It is imperative that it is specified who the target consumers are exactly: adult smokers who are not willing to quit. As such, strategies will need to be employed in order to ensure that the word-of-mouth tactic is applied with that directive in mind.

2. **Increase the number of IQOS stores in strategic locations to create brand awareness.**

Some criteria's need to be considered here, so that the locations chosen are aligned with the type of consumer PMI is trying to attract. Also, other factors like the level of innovation welcomed in the area and the ratio smokers/IQOS users should also be taken into account when following this project plan.

3. **Communicate the science and concept behind IQOS clearly, transparently and easy to understand.**

As it was previously addressed, partnering with science may prove to be a winning strategy in combatting tobacco control policies. However, showcasing the benefits developed should be prioritized as something advertised by independent research and not risking being seen as unbiased findings had the research been developed by PMI itself.

The following slides will present implementation plans for these three projects.

8.2 Implementation plan – Word of Mouth

Goal: Make use of one of the only marketing channels PMI has in order to create awareness for IQOS.

Implementation

1. Create a referral program and offer valuable incentives, e.g., free IQOS accessorizes or 15€ per customer acquired
2. Identify top consumers and use them as point of contact for undecided cigarette smokers (e.g., as a chat on website).
3. Create a community in which IQOS users can share their experience and convince cigarette smokers to follow.

Opportunity & Risks

Opportunities: People trust recommendations from friends and family above any other form of advertising. For PMI, Word of Mouth presents one of the only opportunities to create awareness for IQOS.

Risks: Word of Mouth cannot be controlled by the company and negative feedback might be easily transmitted without noticing.

Limitations

The audience is limited to those that the current consumers can reach, and the message can only be spread slowly.

Costs

The costs are low, refer a friend mechanisms, however, do come with costs for incentivizing consumers to do so.

8.2 Implementation plan – IQOS stores

Goal: Create more opportunities to explain IQOS, provide information on R&D and build the brand

Implementation

1. Set up new permanent stores in highly frequented and strategic locations, which openly welcome innovation.
2. Open temporary lounges at events, festivals, fairs, airports and in restaurants/bars (depending on regulations).
3. Train IQOS coaches to comply with Good Conversion Practices to avoid reaching non-smokers and youth.

Opportunity & Risks

Opportunities: Create a space that fully conveys what IQOS stands for and have close contact with potential customers in order to gather feedback on the product. These customers must exclusively be adult smokers who are not willing to quit.

Risks: Stores in highly frequented locations will result in high scatter losses and might attract non-target consumers.

Limitations

The audience is limited to walk-in customers and people that intentionally plan to visit an IQOS store.

Costs

Opening new stores comes with expenses for rent, furniture and salaries for IQOS coaches which can be classified as expensive.

8.2 Implementation plan – Clear and transparent communication

Goal: Build trust by communicating clearly and transparently

Implementation

1. Clearly explain the current findings on IQOS and do not exaggerate its potential benefits.
2. Avoid misleading terms such as “reduced-risk products” and “smoke-free future” since they end up confusing consumers on the actual vision PMI is trying to bring.
3. Use easy to understand infographics to explain IQOS.

Opportunity & Risks

Opportunities: Enhance trust from consumers and regulators by using independent research to convey that transparency is at the forefront of the company’s renovated strategic vision. Also, this guarantees that benefits are communicated in an unbiased way.

Risks: Transparent communication might weaken the line of argument stating that IQOS is a better alternative.

Limitations

In scenario 1, this strategy is limited by marketing bans and few opportunities to reach consumers.

Costs

Developing a communication strategy can be costly when external consultants are needed to hire.

9. Conclusion (1/2)

Is a smoke-free future attainable?

Yes, it is

- Good market position with first-mover advantage.
- So far, successful transition rates in developed markets.
- Increasingly health-conscious consumers.
- IQOS users like the benefits of the products and the majority does not want to go back to smoking conventional cigarettes.

No, it is not

- Due to widespread mistrust and unwillingness to cooperate of stakeholders, PMI struggles to spread information on IQOS and its benefits around consumers. The less people have access to information, the less will switch.
- It is rather difficult to imagine a tobacco industry without regulations which might delay the 2025 vision.
- Consumers who do not want to switch, will always continue smoking cigarettes. If PMI stopped selling cigarettes, illicit trade might become an issue.

A smoke-free vision seems attainable, with uncertainty arising on how much time it will take. It seems that the quicker PMI regains consumers' trust and the more effective it is at achieving and communicating the benefits of reduced-risk products, the sooner this ambitious goal will set forth.

9. Conclusion (2/2)

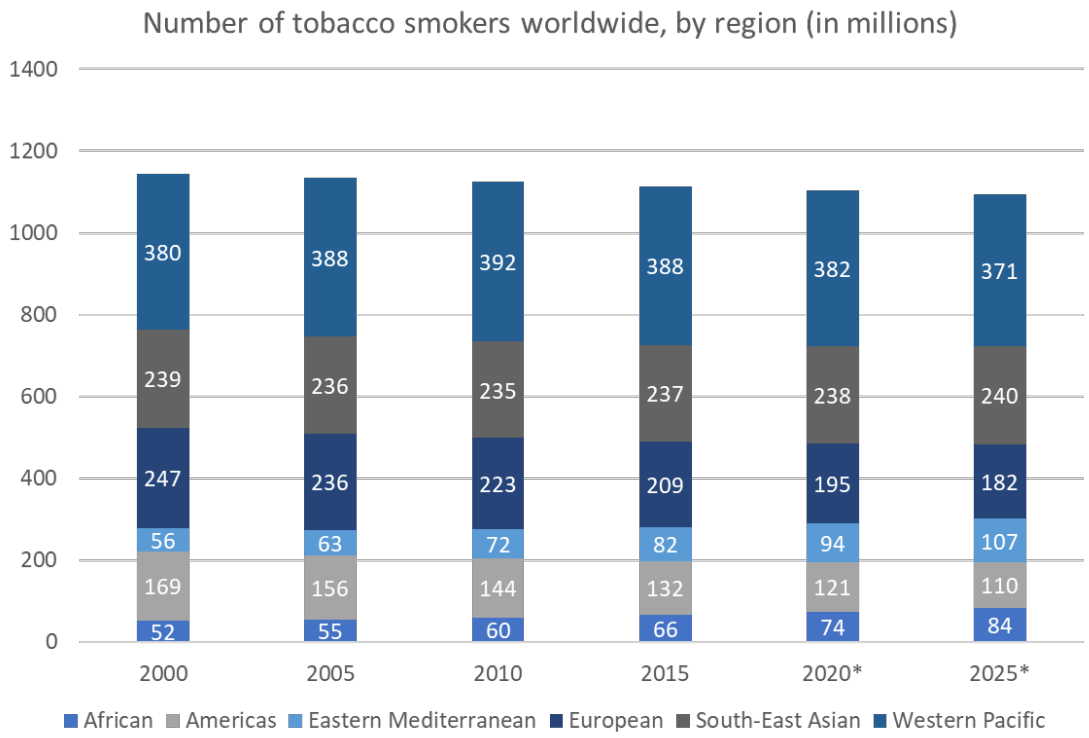
Which actions are needed in order to achieve this goal?

Building trust is a rather long-term process which requires companies to fully commit to societal best practices, e.g., by fully aligning with UN SGD framework, the main driver for positive change in the world, and acknowledging and taking responsibility for all impacts the organization has. Building trust requires making a harsh trade-off between profit-making and delivering a better future for next generations, and hopefully companies will choose the latter. Even through building trust might imply sacrificing exponential profits, it comes with a great reward in the future. By following these practices, what should PMI do and what is in the game for them? Building trust starts from inside the company. The company's own workforce will notice the transformational journey firstand thus, will feel more purpose and impact-driven. This will result in positive externalities to attract new and better talent for the company. By putting society first, the company will be more and more perceived as a best practice from the outside, ranging from public opinion to regulators. As a result, PMI will ultimately obtain a seat at the table, resulting in playing an active role in delivering a smoke-free future at an international level . Therefore, the company will be granted with more opportunities to create awareness for IQOS and encourage cigarette smokers to switch and live a healthier life.

It is time that PMI's journey to take responsibility for its impacts and regain trust, and it is important that the company lives up to all promises that have been made.

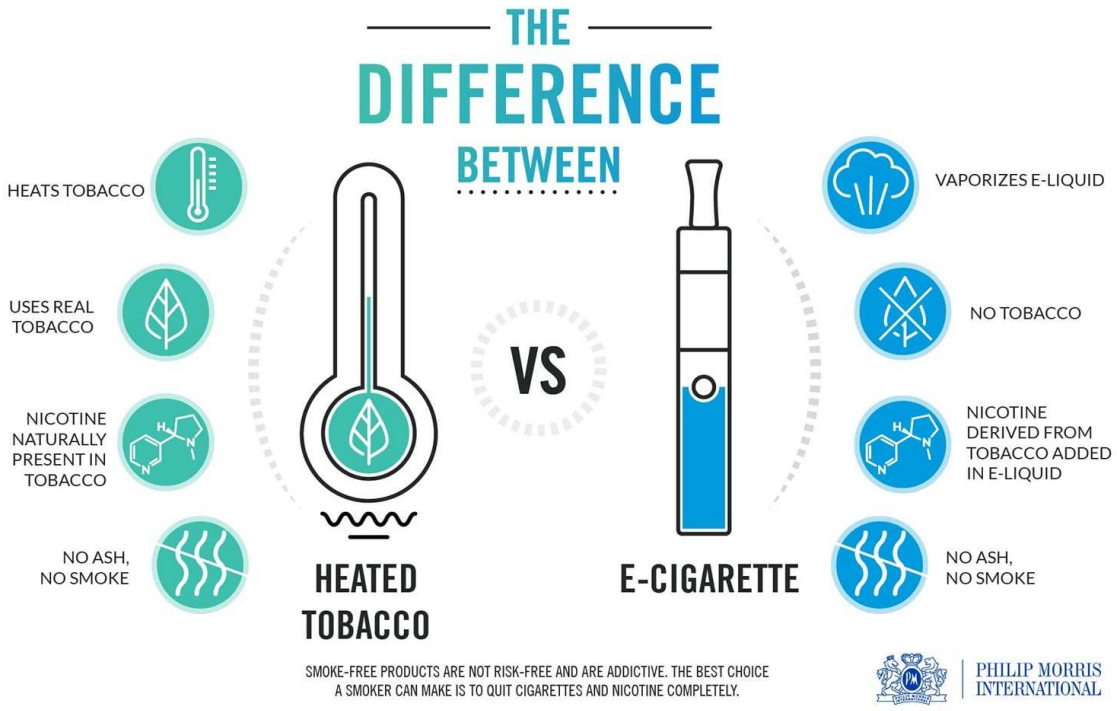
Appendix

Exhibit 1: The Evolution of the Number of Smokers by Region



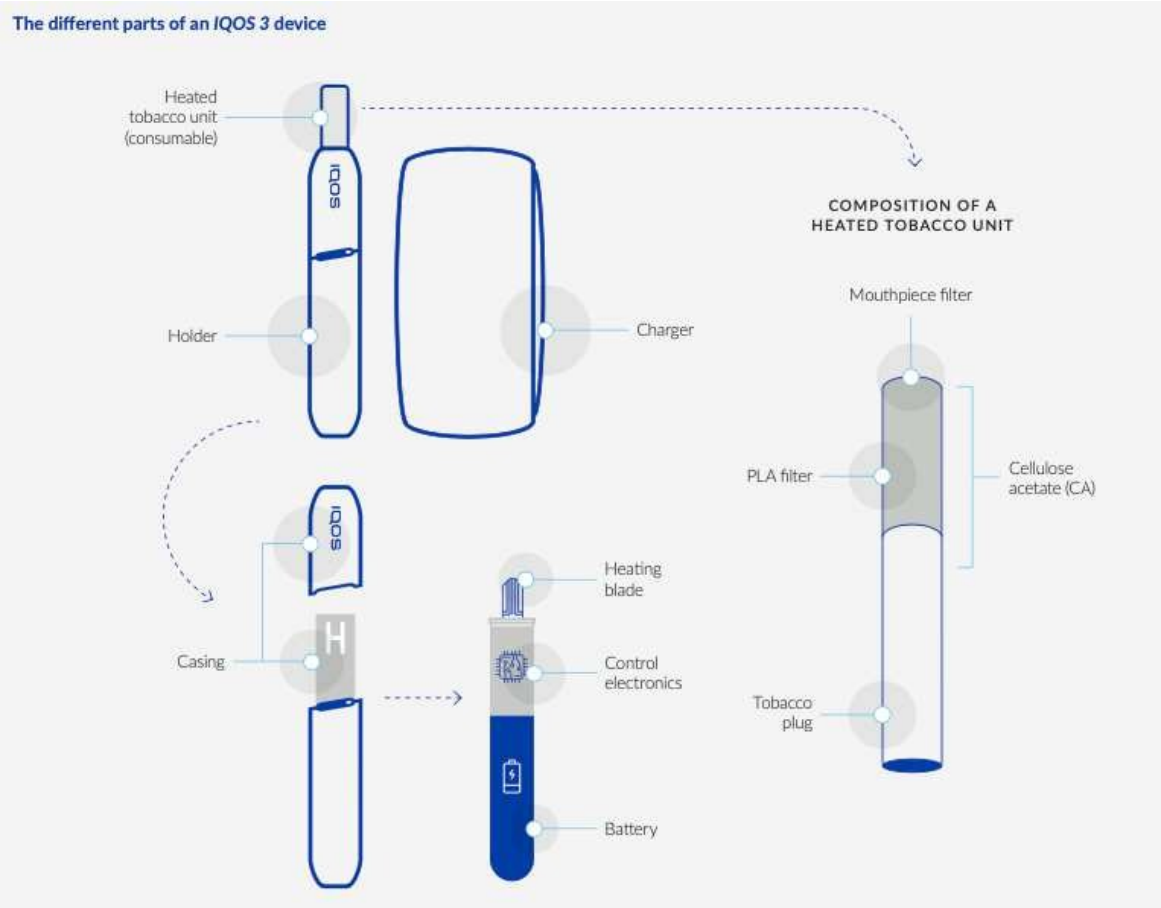
Source: https://www.who.int/publications/i/item/9789240039322 (Accessed December 16, 2021)

Exhibit 2: The difference between Heated Tobacco and E-Cigarettes



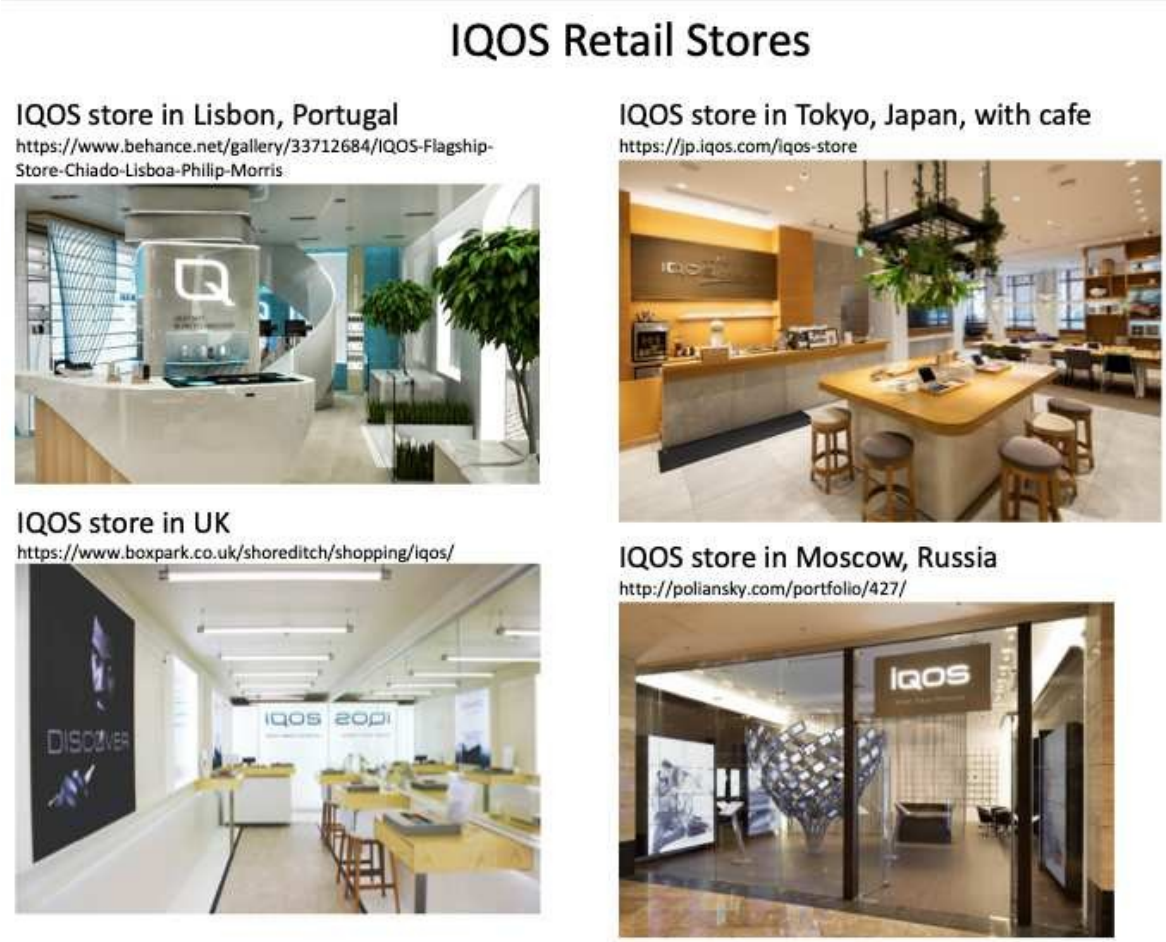
Source: https://www.pmi.com/our-science/difference-between-heated-tobacco-products-and-ecigarettes (Accessed 17 Nov, 2021)

Exhibit 3: The different parts of an IQOS 3 device



Source: https://www.pmi.com/sustainability/integrated-report-2020-digital (Accessed 17 Nov, 2021)

Exhibit y: IQOS Retail stores around the world



Source: https://www.tobaccofreekids.org/assets/content/press_office/2019/IQOS-mktg.pdf

(Accessed 04 Dec, 2021)

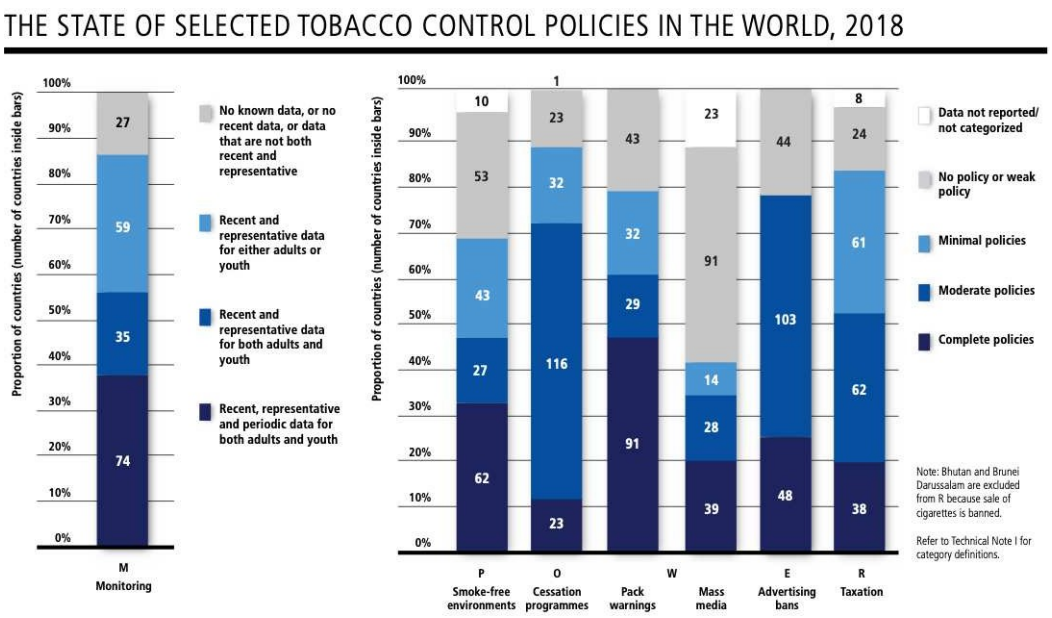
Exhibit 5: Business transformation metrics

Business transformation metrics	**2016**	**2017**	**2018**	**2019**	**2020**
R&D expenditure (in millions USD)*	429	453	383	465	495
R&D expenditure (smoke-free/total)* [1]	72%	74%	92%	98%	99%
Cumulative investments behind smoke-free products (since 2008, in billions USD)[6]	3.2	4.6	6.2	7.2	8.1
Year-on-year change in number of SKUs—combustible products[8]	-1.7%	-6.5%	-6.1%	-5.5%	-4.1%

Year-on-year change in number of SKUs—smoke-free products	78.2%	9.9%	37.1%	24.9%	38.2%
SKUs (smoke-free/total)	4.7%	5.5%	7.8%	10.1%	13.9%
Number of markets where IQOS is available for sale*	20	38	44	52	64
Proportion of markets where IQOS is available for sale that are outside the OECD	32%	41%	44%	45%	52%
Number of IQOS stores	26	63	81	199	259
Commercial expenditure (marketing) (smoke-free/total)	15%	39%	60%	71%	76%
Smoke-free product shipment volume (billion units)	8	36	42	60	76
Combustible product shipment volume (billion units)	845	791	767	732	654
Smoke-free product shipment ratio (smoke-free/total)	0.9%	4.4%	5.1%	7.6%	10.4%
Total IQOS users (in millions)	2.1	6.9	9.6	13.5	17.5
Estimated users who have switched to IQOS and stopped smoking (in millions)	1.5	4.7	6.6	9.6	12.7
Estimated users outside the OECD countries who have switched to IQOS and stopped smoking (in millions)	0.0	0.2	1.1	2.9	4.3
Net revenues (smoke-free/total)	2.7%	12.7%	13.8%	18.7%	23.8%
Number of markets where net revenues from smoke-free products exceed 10% of total net revenues	1	5	19	31	38
Number of markets where net revenues from smoke-free products exceed 50% of total net revenues	0	1	3	4	6

Source: https://www.pmi.com/sustainability/business-transformation-metrics (Accessed 17 Nov, 2021)

Exhibit 6: The state of selected tobacco control policies in the world, 2018



Source: https://apps.who.int/iris/bitstream/handle/10665/325968/WHO-NMH-PND-2019.5-eng.pdf?ua=1 (Accessed 17 Nov, 2021)

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