UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2021

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) ACT OF 1934**

For the transition period from _____ to _____

Commission File Number: 001-33708

PHILIP MORRIS INTERNATIONAL INC.

(Exact name of registrant as specified in its charter)

Virginia	**13-3435103**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
120 Park Avenue **New York** **New York**	**10017**
(Address of principal executive offices)	**(Zip Code)**

917-663-2000

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, no par value	PM	New York Stock Exchange
2.375% Notes due 2022	PM22B	New York Stock Exchange
2.500% Notes due 2022	PM22	New York Stock Exchange
2.500% Notes due 2022	PM22C	New York Stock Exchange
2.625% Notes due 2023	PM23	New York Stock Exchange
2.125% Notes due 2023	PM23B	New York Stock Exchange
3.600% Notes due 2023	PM23A	New York Stock Exchange
2.875% Notes due 2024	PM24	New York Stock Exchange
2.875% Notes due 2024	PM24C	New York Stock Exchange
0.625% Notes due 2024	PM24B	New York Stock Exchange
3.250% Notes due 2024	PM24A	New York Stock Exchange
2.750% Notes due 2025	PM25	New York Stock Exchange
3.375% Notes due 2025	PM25A	New York Stock Exchange

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
2.750% Notes due 2026	PM26A	New York Stock Exchange
2.875% Notes due 2026	PM26	New York Stock Exchange
0.125% Notes due 2026	PM26B	New York Stock Exchange
3.125% Notes due 2027	PM27	New York Stock Exchange
3.125% Notes due 2028	PM28	New York Stock Exchange
2.875% Notes due 2029	PM29	New York Stock Exchange
3.375% Notes due 2029	PM29A	New York Stock Exchange
0.800% Notes due 2031	PM31	New York Stock Exchange
3.125% Notes due 2033	PM33	New York Stock Exchange
2.000% Notes due 2036	PM36	New York Stock Exchange
1.875% Notes due 2037	PM37A	New York Stock Exchange
6.375% Notes due 2038	PM38	New York Stock Exchange
1.450% Notes due 2039	PM39	New York Stock Exchange
4.375% Notes due 2041	PM41	New York Stock Exchange
4.500% Notes due 2042	PM42	New York Stock Exchange
3.875% Notes due 2042	PM42A	New York Stock Exchange
4.125% Notes due 2043	PM43	New York Stock Exchange
4.875% Notes due 2043	PM43A	New York Stock Exchange
4.250% Notes due 2044	PM44	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☑ No ☐

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☑

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☑ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☑ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☑ Accelerated filer ☐

Non-accelerated filer ☐ Smaller reporting company ☐

Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report. ☑

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ☐ No ☑

As of June 30, 2021, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was approximately $154 billion based on the closing sale price of the common stock as reported on the New York Stock Exchange.

Class	Outstanding at January 31, 2022
Common Stock, no par value	1,549,827,817 shares

DOCUMENTS INCORPORATED BY REFERENCE

Document	Parts Into Which Incorporated
Portions of the registrant's definitive proxy statement for use in connection with its annual meeting of shareholders to be held on May 4, 2022, to be filed with the Securities and Exchange Commission on or about March 24, 2022.	Part III

TABLE OF CONTENTS

		Page
PART I		
Item 1.	Business	1
Item 1A.	Risk Factors	6
Item 1B.	Unresolved Staff Comments	15
Item 2.	Properties	15
Item 3.	Legal Proceedings	15
Item 4.	Mine Safety Disclosures	15
PART II		
Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	16
Item 6.	[Reserved]	19
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	19
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	64
Item 8.	Financial Statements and Supplementary Data	65
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	127
Item 9A.	Controls and Procedures	127
Item 9B.	Other Information	127
Item 9C.	Disclosure Regarding Foreign Jurisdictions that Prevent Inspections	127
PART III		
Item 10.	Directors, Executive Officers and Corporate Governance	127
Item 11.	Executive Compensation	130
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	130
Item 13.	Certain Relationships and Related Transactions, and Director Independence	130
Item 14.	Principal Accounting Fees and Services	130
PART IV		
Item 15.	Exhibits and Financial Statement Schedules	131
Signatures		136

In this report, "PMI," "we," "us" and "our" refers to Philip Morris International Inc. and its subsidiaries.

Trademarks and service marks in this report are the registered property of, or licensed by, the subsidiaries of Philip Morris International Inc. and are italicized.

PART I

Item 1. *Business.*

General Development of Business

General

Philip Morris International Inc. is a Virginia holding company incorporated in 1987. We are a leading international tobacco company working to deliver a smoke-free future and evolving our portfolio for the long-term to include products outside of the tobacco and nicotine sector. Our current product portfolio primarily consists of cigarettes and reduced-risk products, including heat-not-burn, vapor and oral nicotine products, which are sold in markets outside the United States. Since 2008, we have invested more than $9 billion to develop, scientifically substantiate and commercialize innovative smoke-free products for adults who would otherwise continue to smoke, with the goal of completely ending the sale of cigarettes. This includes the building of world-class scientific assessment capabilities, notably in the areas of pre-clinical systems toxicology, clinical and behavioral research, as well as post-market studies. The U.S. Food and Drug Administration ("FDA") has authorized the marketing of a version of PMI's *IQOS* Platform 1 device and consumables as a Modified Risk Tobacco Product ("MRTP"), finding that an exposure modification order for these products is appropriate to promote the public health. We describe the MRTP order in more detail in the "Business Environment" section of Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations*. With a strong foundation and significant expertise in life-sciences, in February 2021, we announced our ambition to expand into wellness and healthcare areas and deliver innovative products and solutions that aim to address unmet patient and consumer needs.

In March 2008, we became a U.S. public company listed on the New York Stock Exchange and subject to the rules of the Securities and Exchange Commission (the "SEC").

Reduced-risk products ("RRPs") is the term we use to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continuing to smoke. We have a range of RRPs in various stages of development, scientific assessment and commercialization. Our RRPs are smoke-free products that contain and/or generate far lower quantities of harmful and potentially harmful constituents than found in cigarette smoke.

Our *IQOS* smoke-free product brand portfolio includes heated tobacco and nicotine-containing vapor products. Our leading smoke-free platform ("Platform 1") is a precisely controlled heating device into which a specially designed and proprietary tobacco unit is inserted and heated to generate an aerosol. Heated tobacco units ("HTU") is the term we use to refer to heated tobacco consumables, which include our *HEETS*, *HEETS Creations, HEETS Dimensions, HEETS Marlboro* and *HEETS FROM MARLBORO (*defined collectively as "*HEETS")*, *Marlboro Dimensions*, *Marlboro HeatSticks, Parliament HeatSticks* and *TEREA,* as well as the KT&G-licensed brands, *Fiit* and *Miix* (outside of South Korea). Platform 1 was first introduced in Nagoya, Japan, in 2014. As of December 31, 2021, our smoke-free products are available for sale in 71 markets in key cities or nationwide.

Our cigarettes are sold in approximately 180 markets, and in many of these markets they hold the number one or number two market share position. We have a wide range of premium, mid-price and low-price brands. Our portfolio comprises both international and local brands and is led by *Marlboro*, the world's best-selling international cigarette, which accounted for approximately 38% of our total 2021 cigarette shipment volume. *Marlboro* is complemented in the premium-price category by *Parliament*. Our other leading international cigarette brands are *Bond Street, Chesterfield, L&M*, *Lark* and *Philip Morris.* These seven international cigarette brands contributed approximately 79% of our cigarette shipment volume in 2021. We also own a number of important local cigarette brands, such as *Dji Sam Soe* and *Sampoerna A* in Indonesia, and *Fortune* and *Jackpot* in the Philippines.

During 2021, we laid the foundation for our long-term growth ambitions beyond nicotine in wellness and healthcare, including the milestone acquisitions of Vectura Group PLC and Fertin Pharma A/S, which provide essential capabilities for future product development.

Source of Funds — Dividends

We are a legal entity separate and distinct from our direct and indirect subsidiaries. Accordingly, our right, and thus the right of our creditors and stockholders, to participate in any distribution of the assets or earnings of any subsidiary is subject to the prior rights of creditors of such subsidiary, except to the extent that claims of our company itself as a creditor may be recognized. As a holding company, our principal sources of funds, including funds to make payment on our debt securities, are from the receipt of dividends and repayment of debt from our subsidiaries. Our principal wholly owned and majority-owned subsidiaries currently are not limited by

long-term debt or other agreements in their ability to pay cash dividends or to make other distributions that are otherwise compliant with law.

Description of Business

We currently manage our business in six geographical segments and an Other category:

- The European Union Region ("EU") is headquartered in Lausanne, Switzerland, and covers all the European Union countries and also Switzerland, Norway, Iceland and the United Kingdom;
- The Eastern Europe Region ("EE") is also headquartered in Lausanne and includes Southeast Europe, Central Asia, Ukraine, Israel and Russia;
- The Middle East & Africa Region ("ME&A") is also headquartered in Lausanne and covers the African continent, the Middle East, Turkey and our international duty free business;
- The South & Southeast Asia Region ("S&SA") is headquartered in Hong Kong and includes Indonesia, the Philippines and other markets in this region;
- The East Asia & Australia Region ("EA&A") is also headquartered in Hong Kong and includes Australia, Japan, South Korea, the People's Republic of China and other markets in this region, as well as Malaysia and Singapore;
- The Americas Region ("AMCS") is headquartered in New York and covers the South American continent, Central America, Mexico, the Caribbean and Canada. AMCS also includes transactions under license with Altria Group, Inc., for the distribution of our Platform 1 product in the United States; and
- Other, which includes our third quarter 2021 acquisitions of Fertin Pharma A/S, Vectura Group plc. and OtiTopic, Inc. For further details, see Item 8, Note 6. *Acquisitions* and Item 8, Note 12. *Segment Reporting*.

In the third quarter of 2021, our former Latin America & Canada segment was renamed as the Americas segment.

In the fourth quarter of 2021, we announced that we will be relocating our PMI corporate headquarters, including our AMCS headquarters, from New York, New York, to Stamford, Connecticut. This move is expected to be completed by the third quarter of 2022.

As of March 22, 2019, we deconsolidated the financial results of our Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH"), from our financial statements. For further details, see Item 8, *Financial Statements and Supplementary Data* of this Annual Report on Form 10-K ("Item 8") Note 20. *Deconsolidation of RBH*.

Since the deconsolidation of our Canadian subsidiary, we have continued to report the volume of brands sold by RBH for which other PMI subsidiaries are the trademark owners. These include *HEETS*, *Next*, *Philip Morris* and *Rooftop*.

References to total international market, defined as worldwide cigarette and heated tobacco unit volume excluding the United States, total industry, total market and market shares in this Form 10-K, are our estimates for tax-paid products based on the latest available data from a number of internal and external sources and may, in defined instances, exclude the People's Republic of China and/or our duty free business. Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units.

2020 and 2021 estimates for total industry volume and market share in certain geographies reflect limitations on the availability and accuracy of industry data during pandemic-related restrictions.

Our total shipments, including cigarettes and heated tobacco units, increased by 2.2% in 2021 to 719.9 billion units. We estimate that international industry volumes, including cigarettes and heated tobacco units, were approximately 5.0 trillion units in 2021, a 1.3% increase from 2020. Excluding the People's Republic of China ("PRC"), we estimate that international cigarette and heated tobacco unit volume was 2.6 trillion units in 2021, a 2.4% increase from 2020. We estimate that our reported share of the international market (which is defined as worldwide cigarette

and heated tobacco unit volume, excluding the United States of America) was approximately 14.3% in 2021, 14.3% in 2020 and 15.1% in 2019. Excluding the PRC, we estimate that our reported share of the international market was approximately 27.3%, 27.7%, and 28.4% in 2021, 2020 and 2019, respectively.

Shipments of our principal cigarette brand, *Marlboro*, increased by 2.9% in 2021, and represented approximately 9.5% of the international cigarette market, excluding the PRC, in 2021, 9.5% in 2020, and 10.0% in 2019.

Total shipment volume of heated tobacco units reached 95.0 billion units in 2021, up from 76.1 billion units in 2020.

We have a market share of at least 15% in approximately 100 markets, including Algeria, Argentina, Australia, Austria, Belgium, Brazil, the Czech Republic, Egypt, France, Germany, Hong Kong, Hungary, Indonesia, Israel, Italy, Japan, Kuwait, Mexico, the Netherlands, Norway, the Philippines, Poland, Portugal, Russia, Saudi Arabia, South Korea, Spain, Switzerland, Turkey and Ukraine.

Distribution & Sales

Our main types of distribution and sales are tailored to the characteristics of each market and are often used simultaneously:

- Direct sales and distribution, where we have set up our own distribution selling directly to the retailers;
- Distribution through independent distributors that often distribute other fast-moving consumer goods and are responsible for distribution in a particular market;
- Exclusive zonified distribution, where the distributors are dedicated to us in multicategory products distribution and assigned to exclusive territories within a market;
- Distribution through national or regional wholesalers that then supply the retail trade;
- Our own e-commerce infrastructure for product sales to trade partners and to consumers; and
- Our own brand retail infrastructure for our RRP products and accessories for sales to consumers.

Competition

We are subject to highly competitive conditions in all aspects of our business. We compete primarily on the basis of product quality, brand recognition, brand loyalty, taste, R&D, innovation, packaging, customer service, marketing, advertising and retail price and, increasingly, adult smoker willingness to convert to our RRPs. In the combustible product category, we predominantly sell American blend cigarette brands, such as *Marlboro*, *L&M*, *Parliament, Philip Morris* and *Chesterfield*, which are the most popular across many of our markets. In the RRP product category, we predominantly sell Platform 1 devices and heated tobacco units under the *IQOS* brand umbrella. We seek to compete in all profitable retail price categories, although our brand portfolio is weighted towards the premium-price category.

The competitive environment and our competitive position can be significantly influenced by weak economic conditions, erosion of consumer confidence, competitors' introduction of lower-price products or innovative products, higher tobacco product taxes, higher absolute prices and larger gaps between retail price categories, and product regulation that diminishes the ability to differentiate tobacco products and restricts adult consumer access to truthful and non-misleading information about our RRPs. Competitors in our industry include three large international tobacco companies, new market entrants, particularly with respect to innovative products, several regional and local tobacco companies and, in some instances, state-owned tobacco enterprises, principally in Algeria, Egypt, the PRC, Taiwan, Thailand and Vietnam. Certain new market entrants in the non-combustible product category may alienate consumers from innovative products through inappropriate marketing campaigns, messaging and inferior product satisfaction, while not relying on scientific substantiation based on appropriate R&D protocols and standards. The growing use of digital media could increase the speed and extent of the dissemination of inaccurate and misleading information about our RRPs, all of which could have a mutual adverse effect on our profitability and results of operations.

Procurement and Raw Materials

We purchase tobacco leaf of various types, grades and styles throughout the world, mostly through independent tobacco suppliers. In 2021, we also contracted directly with farmers in several countries, including Argentina, Brazil,

Colombia, Italy, Pakistan and Poland. In 2021, direct sourcing from farmers represented approximately 25% of PMI's global leaf requirements. The largest supplies of tobacco leaf are sourced from Argentina, Brazil, China, Italy, Indonesia (mostly for domestic use in kretek products), Malawi, Mozambique, the Philippines, Turkey and the United States.

We believe that there is an adequate supply of tobacco leaf in the world markets to satisfy our current and anticipated production requirements.

In addition to tobacco leaf, we purchase a wide variety of direct materials from a total of approximately 360 suppliers. In 2021, our top ten suppliers of direct materials combined represented approximately 60% of our total direct materials purchases. The three most significant direct materials that we purchase are printed paper board used in packaging, acetate tow used in filter making and fine paper used in the manufacturing of cigarettes and heated tobacco units. In addition, the adequate supply and procurement of cloves are of particular importance to our Indonesian business.

We discuss the details of our supply chain for our RRPs in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations of this Annual Report on Form 10-K ("Item 7") in *Business Environment—Reduced-Risk Products*.

Business Environment

Information called for by this Item is hereby incorporated by reference to the paragraphs in Item 7, *Business Environment* to this Annual Report on Form 10-K.

Other Matters

Customers

As described in more detail in "*Distribution & Sales*" above, in many of our markets we sell our products to distributors. In 2021, sales to a distributor in the European Union Region and a distributor in the East Asia & Australia Region each amounted to 10 percent or more of our consolidated net revenues. See Item 8, Note 12. *Segment Reporting* for more information. We believe that none of our business segments is dependent upon a single customer or a few customers, the loss of which would have a material adverse effect on our consolidated results of operations. In some of our markets, particularly in the European Union, Eastern Europe and in the East Asia & Australia Regions, a loss of a distributor may result in a temporary market disruption.

Employees

Our Workforce. At December 31, 2021, we employed approximately 69,600 people worldwide of 133 different nationalities, including full-time, temporary and part-time staff. Our businesses are subject to a number of laws and regulations relating to our relationship with our employees. Generally, these laws and regulations are specific to the location of each business. We engage with legally recognized employee representative bodies and we have collective bargaining agreements in many of the countries in which we operate. In addition, in accordance with European Union requirements, we have established a European Works Council composed of management and elected members of our workforce. We believe we maintain good relations with our employees and their representative organizations.

Our Internal Transformation. To be successful in our transformation to a smoke-free future, we must continue transforming our culture and ways of working, align our talent with our business needs and innovate to become a truly consumer-centric business. To achieve our strategic goals, we need to attract, retain and motivate the best global talent with the right degree of diversity, experience, competencies and skills. Therefore, we strive to ensure the development of our existing talent while increasingly recruiting those with the expertise in areas that are new to us such as digital and technical solutions. We set the levels of our compensation and benefit programs that we believe are necessary to achieve these goals and remain competitive with other consumer product companies.

Oversight and Management. Our Board of Directors (the "Board") provides oversight of various matters pertaining to our workforce, and the Compensation and Leadership Development Committee of the Board is responsible for executive compensation matters and oversight of the risks and programs related to talent management. Our Code of Conduct, also known at PMI as the Guidebook for Success, highlights our commitment to ethical business conduct and honesty, respect, fairness in our ways of working.

Inclusion & Diversity. At PMI, we believe that a diverse workforce and an inclusive culture are strategic priorities which help fuel innovation and business success. As part of our commitment to workplace diversity in 2020, our Board appointed a Chief Diversity Officer. Improving gender balance especially in management positions continues to be one of our priorities:

- We set a target of 40% female representation in management positions by the end of 2022;
- We launched a Women in Leadership program to support our female talents; and
- We were the first multinational company to receive a global EQUAL-SALARY certification from the EQUAL-SALARY Foundation. This achievement is an important building block on the road to creating a more inclusive gender-balanced workplace and continuing our reputation as a top employer.

In recognition of our efforts, we were added to the 2021 Bloomberg Gender-Equality Index for transparency in gender reporting and advancing women's equity (among the 380 companies and 11 sectors who scored at or above the global threshold established by Bloomberg).

Creation of employee resource groups ("ERGs") was another important milestone to further inclusion at PMI. We believe these groups are an important platform for building an enhanced sense of belonging, visibility, and greater understanding of different experiences and dimensions of diversity in our company. Currently, we have established ERGs on race and ethnicity, LGBTQ+ inclusions, gender and disability. Each ERG is sponsored by a member of the PMI Senior Leadership Team, to illustrate our strong commitment to Inclusion & Diversity comes from the top.

Our Initiatives in Response to COVID-19. Since the outbreak of the global COVID-19 pandemic, we have focused on business continuity, health and safety of our employees, and have rapidly adapted our ways of working to a new environment. We have implemented additional safety measures for essential employees in our facilities and offices, and continue to pay salaries to those employees who are unable to work due to government restrictions. We have enhanced remote work arrangements and digital collaboration, and related risk management, and to date, a large majority of our employees continues to work remotely.

Government Regulation

As a company with global operations in a heavily regulated industry, we are subject to multiple laws and regulations of jurisdictions in which we operate. We discuss our regulatory environment in Item 7, *Business Environment*.

We are subject to international, national and local environmental laws and regulations in the countries in which we do business. We have specific programs across our business units designed to meet applicable environmental compliance requirements and reduce our carbon footprint, wastage, as well as water and energy consumption. We report externally about our climate change mitigation strategy, together with associated targets and results in reducing our carbon footprint, through CDP (formerly known as the Carbon Disclosure Project), the leading international non-governmental organization assessing the work of thousands of companies worldwide in the area of environmental impact, including climate change. Our environmental and occupational health and safety management program includes policies, standard practices and procedures at all our manufacturing centers. Furthermore, we have engaged an external certification body to validate the effectiveness of this management program at our manufacturing centers around the world, in accordance with internationally recognized standards for safety and environmental management. Our subsidiaries expect to continue to make investments in order to drive improved performance and maintain compliance with environmental laws and regulations. We assess and report to our management the compliance status of all our legal entities on a regular basis. Based on current regulations, the management and controls we have in place and our review of climate change risks (both physical and regulatory), environmental expenditures have not had, and are not expected to have, a material adverse effect on our consolidated results of operations, capital expenditures, financial position, earnings or competitive position.

Based on current regulations, compliance with government regulations, including environmental regulations, has not had, and is not expected to have a material adverse effect on our results of operations, capital expenditures, financial position, earnings, or competitive position.

As discussed in more detail in Item 1A. *Risk Factors*, our financial results could be significantly affected by regulatory initiatives that could result in a significant decrease in demand for our brands. More specifically, any regulatory requirements that lead to a commoditization of tobacco products or impede adult consumers' ability to convert to our RRPs, as well as any significant increase in the cost of complying with new regulatory requirements could have a material adverse effect on our financial results.

Information About Our Executive Officers

The disclosure regarding executive officers is hereby incorporated by reference to the discussion under the heading "Information about our Executive Officers as of February 10, 2022" in Part III, Item 10. *Directors, Executive Officers and Corporate Governance* of this Annual Report on Form 10-K ("Item 10").

Intellectual Property

Our trademarks are valuable assets, and their protection and reputation are essential to us. We own the trademark rights to all of our principal brands, including *Marlboro*, *HEETS* and *IQOS*, or have the right to use them in all countries in which these brands are advertised or sold.

In addition, we have a large number of granted patents and pending patent applications worldwide. Our patent portfolio, as a whole, is material to our business. However, no one patent, or group of related patents, is material to us. We also have registered industrial

designs, as well as unregistered proprietary trade secrets, technology, know-how, processes and other unregistered intellectual property rights.

Effective January 1, 2008, PMI entered into an Intellectual Property Agreement with Philip Morris USA Inc., a wholly owned subsidiary of Altria Group, Inc. ("PM USA"). The Intellectual Property Agreement allocates ownership of jointly funded intellectual property as follows:

- PMI owns all rights to jointly funded intellectual property outside the United States, its territories and possessions; and
- PM USA owns all rights to jointly funded intellectual property in the United States, its territories and possessions.

The parties agreed to submit disputes under the Intellectual Property Agreement first to negotiation between senior executives and then to binding arbitration.

Seasonality

Our business segments are not significantly affected by seasonality, although in certain markets cigarette consumption may be lower during the winter months due to the cold weather and may rise during the summer months due to outdoor use, longer daylight, and tourism.

Available Information

We are required to file with the SEC annual, quarterly and current reports, proxy statements and other information required by the Securities Exchange Act of 1934, as amended (the "Exchange Act"). The SEC maintains an Internet website at http://www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, from which investors can electronically access our SEC filings.

We make available free of charge on, or through, our website at www.pmi.com our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. Investors can access our filings with the SEC by visiting www.pmi.com.

The information on our website is not, and shall not be deemed to be, a part of this report or incorporated into any other filings we make with the SEC.

Item 1A. *Risk Factors.*

The following risk factors should be read carefully in connection with evaluating our business and the forward-looking statements contained in this Annual Report on Form 10-K. Any of the following risks could materially adversely affect our business, our operating results, our financial condition and the actual outcome of matters as to which forward-looking statements are made in this Annual Report on Form 10-K.

Forward-Looking and Cautionary Statements

We may from time to time make written or oral forward-looking statements, including statements contained in this Annual Report on Form 10-K and other filings with the SEC, in reports to stockholders and in press releases and investor webcasts. You can identify these forward-looking statements by use of words such as "strategy," "expects," "continues," "plans," "anticipates," "believes," "will," "aspires," "estimates," "intends," "projects," "aims," "goals," "targets," "forecasts" and other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts.

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Our RRPs constitute a new product category in its early stages that is less predictable than our mature cigarette business. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from those anticipated, estimated or projected. Investors should bear this in mind as they consider forward-looking statements and whether to invest in or remain invested in our securities. In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, we are identifying important factors that, individually or in the aggregate, could cause actual results and

outcomes to differ materially from those contained in any forward-looking statements made by us; any such statement is qualified by reference to the following cautionary statements. We elaborate on these and other risks we face throughout this document, particularly in Item 7, *Business Environment*. You should understand that it is not possible to predict or identify all risk factors. Consequently, you should not consider the following to be a complete discussion of all potential risks or uncertainties. We do not undertake to update any forward-looking statement that we may make from time to time, except in the normal course of our public disclosure obligations.

Overall Business Risks

We may be unsuccessful in our attempts to introduce reduced-risk products, and regulators may not permit the commercialization of these products or the communication of scientifically substantiated information and claims.

Our key strategic priorities are to: (i) develop and commercialize products that present less risk of harm to adult smokers who switch to those products versus continued smoking; and (ii) convince and educate current adult smokers who would otherwise continue to smoke to switch to those RRPs. For our efforts to be successful, we must:

- develop RRPs that adult smokers find acceptable alternatives to smoking;
- conduct rigorous scientific studies to substantiate that they reduce exposure to harmful and potentially harmful constituents in smoke and, ultimately, that these products present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to them versus continued smoking; and
- effectively advocate for a timely development of science-based regulatory frameworks for the development and commercialization of RRPs, including communication of scientifically substantiated information to enable adult smokers to make better consumer choices.

We might not succeed in our efforts. If we do not succeed, but others do, or if heat-not-burn products are inequitably regulated compared to other RRP categories without regard to the totality of the scientific evidence available for such products, we may be at a competitive disadvantage. In addition, actions of some market entrants, such as the inappropriate marketing of e-vapor products to youth, as well as alleged health consequences associated with the use of certain e-vapor products, may unfavorably impact public opinion and/or mischaracterize all e-vapor products or other RRPs to consumers, regulators and policy makers without regard to the totality of scientific evidence for specific products. This may impede our efforts to advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs. We cannot predict whether regulators will permit the sale and/or marketing of RRPs with scientifically substantiated information and claims. Such restrictions could limit the success of our RRPs.

The WHO study group on tobacco product regulation ("TobReg") published their eighth report on the scientific basis of tobacco product regulation in May 2021. The report is based on a review of scientific evidence related to novel and emerging nicotine and tobacco products, such as electronic nicotine delivery systems ("ENDS"), electronic non-nicotine delivery systems ("ENNDS") and heated tobacco products ("HTPs") on a number of scientific topics. The report concludes by making a number of policy recommendations on HTPs and ENDS that, if implemented, could restrict both the availability of these products, and the access to accurate information about them. In August 2021, the WHO FCTC Secretariat published two reports to the ninth session of the Conference of the Parties ("CoP") of the FCTC, which are not materially different from the WHO study group report.

Prior to CoP 9 that took place in November 2021, the WHO and the WHO FCTC Secretariat published two reports on novel and emerging tobacco products. The reports were noted by CoP 9 and related substantive discussions and decisions were deferred to CoP 10, currently scheduled for 2023. It is not possible to predict whether or to what extent measures recommended by the WHO's reports will be implemented as the reports are not binding to the WHO Member States.

Additionally, any claims, regardless of merit, challenging our research and clinical data available to date, may impact the development of science-based regulatory frameworks for the commercialization of the RRP category and the commercialization of the RRP category in general.

Our RRPs and commercial activities for these products are designed for, and directed toward, current adult smokers and users of nicotine-containing products, and not for non-smokers or youth. We put significant effort in place to restrict access of our products to non-smokers or youth. Nevertheless, technological, regulatory and/or commercial setbacks might prevent us from delivering necessary infrastructure required to fulfill our commitment of having 100% of our RRP device portfolio equipped with “Age Verification”-technology and device activation features by 2023.

If nonetheless there is a significant usage of our products or competitive products among youth or non-smokers, even in situations over which we have no control, our credibility may suffer, and our efforts to advocate for the development of science-based regulatory frameworks for the commercialization of RRPs may be significantly impacted.

Moreover, the FDA's premarket tobacco product and modified risk tobacco product authorizations of a version of our Platform 1 product are subject to strict marketing, reporting and other requirements. Although we have received these product authorizations from the FDA, there is no guarantee that the product will remain authorized for sale in the U.S., particularly if there is a significant uptake in youth or non-smoker initiation.

The financial and business performance of our reduced-risk products is less predictable than our cigarette business.
Our RRPs are novel products in a new category, and the pace at which adult smokers adopt them may vary, depending on the competitive, regulatory, fiscal and cultural environment, and other factors in a specific market. There may be periods of accelerated growth and periods of slower growth for these products, the timing and drivers of which may be more difficult for us to predict versus our mature cigarette business. The impact of this lower predictability on our projected results for a specific period may be significant, particularly during the early stages of this new product category, during the COVID-19 pandemic and as a result of unpredictability due to shortage of key components in our supply chain.

We may be unsuccessful in our efforts to differentiate reduced-risk products and cigarettes with respect to taxation.
To date, we have been largely successful in demonstrating to regulators that our RRPs are not cigarettes due to the absence of combustion, and as such they are generally taxed either as a separate category or as other tobacco products, which typically yields more favorable tax rates than cigarettes. Nevertheless, we are unable to predict whether regulators will be issuing new regulations where RRP will be equally taxed in line with other tobacco products such as ordinary cigarettes. However, if we cease to be successful in these efforts, RRP unit margins may be materially adversely affected.

Consumption of tax-paid cigarettes continues to decline in many of our markets.
This decline is due to multiple factors, including increased taxes and pricing, governmental actions, the diminishing social acceptance of smoking and health concerns, competition, continuing economic and geopolitical uncertainty, and the continuing prevalence of illicit products. These factors and their potential consequences are discussed more fully below and in Item 7, *Business Environment*. A continuous decline in the consumption of cigarettes could have a material adverse effect on our revenue and profitability.

Cigarettes are subject to substantial taxes. Significant increases in cigarette-related taxes have been proposed or enacted and are likely to continue to be proposed or enacted in numerous jurisdictions. These tax increases may disproportionately affect our profitability and make us less competitive versus certain of our competitors.
Tax regimes, including excise taxes, sales taxes and import duties, can disproportionately affect the retail price of cigarettes versus other combustible tobacco products, or disproportionately affect the relative retail price of our cigarette brands versus cigarette brands manufactured by certain of our competitors. Because our portfolio is weighted toward the premium-price cigarette category, tax regimes based on sales price can place us at a competitive disadvantage in certain markets. Furthermore, our volume and profitability may be adversely affected in these markets.

In addition, increases in cigarette taxes are expected to continue to have an adverse impact on our sales of cigarettes, due to resulting lower consumption levels, a shift in sales from manufactured cigarettes to other combustible tobacco products and from the premium-price to the mid-price or low-price cigarette categories, where we may be under-represented, from local sales to legal cross-border purchases of lower price products, or to illicit products such as contraband, counterfeit and "illicit whites."

Our business faces significant governmental action aimed at increasing regulatory requirements with the goal of reducing or preventing the use of tobacco products.
Governmental actions, combined with the diminishing social acceptance of smoking and private actions to restrict smoking, have resulted in reduced industry volumes for our products in many of our markets, and we expect that such factors will continue to reduce consumption levels and will increase down-trading and the risk of counterfeiting,

contraband, "illicit whites" and legal cross-border purchases. Significant regulatory developments will continue to take place over the next few years in most of our markets, driven principally by the World Health Organization's Framework Convention on Tobacco Control (the "FCTC"). Since it came into force in 2005, the FCTC has led to increased efforts by tobacco control advocates and public health organizations to promote increasingly restrictive regulatory measures on the marketing and sale of tobacco products to adult smokers. Regulatory initiatives that have been proposed, introduced or enacted by governmental authorities in various jurisdictions include:

- restrictions on or licensing of outlets permitted to sell cigarettes;
- the levying of substantial and increasing tax and duty charges;

- restrictions or bans on advertising, marketing and sponsorship;
- the display of larger health warnings, graphic health warnings and other labeling requirements;
- restrictions on packaging design, including the use of colors, and mandating plain packaging;
- restrictions on packaging and cigarette formats and dimensions;
- restrictions or bans on the display of tobacco product packaging at the point of sale and restrictions or bans on vending machines;
- requirements regarding testing, disclosure and performance standards for tar, nicotine, carbon monoxide and other smoke constituents;
- disclosure, restrictions, or bans of tobacco product ingredients, including bans on the flavors of certain tobacco products;
- increased restrictions on smoking and use of tobacco and nicotine-containing products in public and work places and, in some instances, in private places and outdoors;
- restrictions or prohibitions of novel tobacco or nicotine-containing products;
- elimination of duty free sales and duty free allowances for travelers;
- encouraging litigation against tobacco companies; and
- excluding tobacco companies from transparent public dialogue regarding public health and other policy matters.

Our financial results could be materially affected by regulatory initiatives resulting in a significant decrease in demand for our brands. More specifically, requirements that lead to a commoditization of tobacco products or impede adult consumers' ability to convert to our RRPs, as well as any significant increase in the cost of complying with new regulatory requirements could have a material adverse effect on our financial results.

Changes in the earnings mix and changes in tax laws may result in significant variability in our effective tax rates. Our ability to receive payments from foreign subsidiaries or to repatriate royalties and dividends could be restricted by local country currency exchange controls and other regulations.
We are subject to income tax laws in the United States and numerous foreign jurisdictions. The new administration resulting from the 2020 U.S. presidential and congressional elections could lead to changes in the U.S. tax system, including significant increases in the U.S. corporate income tax rate and the minimum tax rate on certain earnings of foreign subsidiaries. If ultimately enacted into law, such changes could have a material adverse impact on our effective tax rate thereby reducing our net earnings. Further changes in the tax laws of foreign jurisdictions could arise as a result of the base erosion and profit shifting project undertaken by the Organisation for Economic Co-operation and Development, which recommended changes to numerous long-standing tax principles. If implemented, such changes, as well as changes in taxing jurisdictions' administrative interpretations, decisions, policies, or positions, could also have a material adverse impact on our effective tax rate thereby reducing our net earnings. In future periods, our ability to recover deferred tax assets could be subject to additional uncertainty as a result of such developments. Furthermore, changes in the earnings mix or applicable foreign tax laws may result in significant variability in our effective tax rates.

Because we are a U.S. holding company, our most significant source of funds is distributions from our non-U.S. subsidiaries. Certain countries in which we operate have adopted or could institute currency exchange controls and other regulations that limit or prohibit our local subsidiaries' ability to convert local currency into U.S. dollars or to make payments outside the country. This could subject us to the risks of local currency devaluation and business disruption.

Risks Related to Sourcing of Materials, Products and Services

Use of third-party resources may negatively impact quality and availability of our products and services, and we may be required to replace third-party contract manufacturers or service providers with our own resources.
We increasingly rely on third-party resources and their subcontractors/suppliers to manufacture some of our products and product parts (particularly, the electronic devices and accessories), and to provide services, including to support

our finance, commercialization and information technology processes. While many of these arrangements improve efficiencies and decrease our operating costs, they also diminish our direct control. Such diminished control may have a material adverse effect on the quality and availability of products or services, our supply chain, and the speed and flexibility in our response to changing market conditions and adult consumer preferences, all of which may place us at a competitive disadvantage. In addition, we may be unable to renew these agreements on satisfactory terms for numerous reasons, including government regulations, and our costs may increase significantly if we must replace such third parties with our own resources.

Government mandated prices, production control programs, shifts in crops driven by economic conditions and the impact of climate change may increase the cost or reduce the quality of the tobacco and other agricultural products used to manufacture our products.
As with other agricultural commodities, the price of tobacco leaf and cloves can be influenced by imbalances in supply and demand and the impacts of natural disasters and pandemics such as COVID-19. Furthermore, crop quality may be influenced by variations in weather patterns, including those caused by climate change. Tobacco production in certain countries is subject to a variety of controls, including government mandated prices and production control programs. Changes in the patterns of demand for agricultural products could cause farmers to produce less tobacco or cloves. Any significant change in tobacco leaf and clove prices, quality and quantity could affect our profitability and our business.

Risks Related to our International Operations

Because we have operations in numerous countries, our results may be adversely impacted by economic, regulatory and political developments, natural disasters, pandemics or conflicts.
Some of the countries in which we operate face the threat of civil unrest and can be subject to regime changes. In others, nationalization, terrorism, conflict and the threats of war or acts of war may have a significant impact on the business environment. Natural disasters, pandemics, economic, political, regulatory, acts of war or threats of war, or other developments could disrupt our supply chain, manufacturing capabilities or distribution capabilities, and our business continuity plans and other safeguards might not always be effective to fully mitigate their impact. In addition, such developments could increase costs of our materials and operations and lead to loss of property or equipment that are critical to our business in certain markets and difficulty in staffing and managing our operations, all of which could have a material adverse effect on our operations, volumes, revenue, net earnings and profitability. We discuss risks associated with the COVID-19 pandemic below.

In certain markets, we are dependent on governmental approvals of various actions such as price changes, and failure to obtain such approvals could impair growth of our profitability.

In addition, despite our high ethical standards and rigorous controls and compliance procedures aimed at preventing and detecting unlawful conduct, given the breadth and scope of our international operations, we may not be able to detect all potential improper or unlawful conduct by our employees and partners. Such improper or unlawful conduct (actual or alleged) could lead to litigation and regulatory action, cause damage to our reputation and that of our brands, and result in substantial costs.

Our reported results could be adversely affected by unfavorable currency exchange rates, and currency fluctuations could impair our competitiveness.
We conduct our business primarily in local currency and, for purposes of financial reporting, the local currency results are translated into U.S. dollars based on average exchange rates prevailing during a reporting period. Foreign currencies may fluctuate significantly against the U.S. dollar reducing our net revenues, operating income and EPS. Our primary local currency cost bases may be different from our primary currency revenue markets, and U.S. dollar fluctuations against various currencies may have disproportionate negative impact on net revenues as compared to our gross profit and operating income margins.

Risks Related to Legal Challenges and Investigations

Litigation related to tobacco use and exposure to environmental tobacco smoke could substantially reduce our profitability and could severely impair our liquidity.
There is litigation related to tobacco products pending in certain jurisdictions in which we operate. Damages claimed in some tobacco-related litigation are significant and, in certain cases in Brazil, Canada, and Nigeria, range into the billions of U.S. dollars. We anticipate that new cases will continue to be filed. The FCTC encourages litigation against tobacco product manufacturers. It is possible that our consolidated results of operations, cash flows or financial position could be materially adversely affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. We face various administrative and legal challenges related to certain RRP activities, including allegations concerning product classification, advertising restrictions, corporate communications, product coach activities, scientific substantiation, product liability, and unfair competition. While we design our programs to comply with relevant regulations, we expect these or similar challenges to continue as we expand our efforts to commercialize RRPs and to communicate publicly. The outcomes of these matters may affect

our RRP commercialization and public communication activities and performance in one or more markets. Also see Item 8, Note 17. *Contingencies* to our condensed consolidated financial statements for a discussion of pending litigation.

From time to time, we are subject to governmental investigations on a range of matters.
Investigations include allegations of contraband shipments of cigarettes, allegations of unlawful pricing activities within certain markets, allegations of underpayment of income taxes, customs duties and/or excise taxes, allegations of false and misleading usage of

descriptors, allegations of unlawful advertising, and allegations of unlawful labor practices. We cannot predict the outcome of those investigations or whether additional investigations may be commenced, and it is possible that our business could be materially adversely affected by an unfavorable outcome of pending or future investigations. See Item 8, Note 17. *Contingencies—Other Litigation* and "Management's Discussion and Analysis of Financial Condition and Results of Operations—Operating Results by Business Segment—Business Environment—Governmental Investigations" for a description of certain governmental investigations to which we are subject.

We may be unable to adequately protect our intellectual property rights, and disputes relating to intellectual property rights could harm our business.

Our intellectual property rights are valuable assets, and their protection is important to our business. If the steps we take to protect our intellectual property rights globally, including through a combination of trademark, design, patent, trade secrets and other intellectual property rights, are inadequate, or if others infringe or misappropriate our intellectual property rights, notwithstanding legal protection, our business could be adversely impacted. Moreover, failing to manage our existing and/or future intellectual property may place us at a competitive disadvantage. Intellectual property rights of third parties may limit our ability to commercialize our products or improve product quality in one or more markets. Competitors or other third parties may claim that we infringe their intellectual property rights. Any such claims, regardless of merit, could divert management's attention, be costly, disruptive, time-consuming and unpredictable and expose us to significant litigation costs and damages, and impede our ability to manufacture, commercialize and improve our products, and thus have a material adverse effect on our revenue and our profitability. In addition, if, as a result, we are unable to manufacture or sell our RRPs or improve their quality in one or more markets, our ability to convert adult smokers to our RRPs in such markets would be adversely affected. See Item 8, Note 17. *Contingencies—Other Litigation* to our condensed consolidated financial statements for a description of certain intellectual property proceedings.

Risks Related to our Competitive Environment

We face intense competition, and our failure to compete effectively could have a material adverse effect on our profitability and results of operations.

We are subject to highly competitive conditions in all aspects of our business. We compete primarily on the basis of product quality, brand recognition, brand loyalty, taste, R&D, innovation, packaging, customer service, marketing, advertising and retail price and, increasingly, adult smoker willingness to convert to our RRPs. The competitive environment and our competitive position can be significantly influenced by weak economic conditions, erosion of consumer confidence, competitors' introduction of lower-price products or innovative products, higher tobacco product taxes, higher absolute prices and larger gaps between retail price categories, and product regulation that diminishes the ability to differentiate tobacco products and restricts adult consumer access to truthful and non-misleading information about our RRPs. Competitors in our industry include three large international tobacco companies, new market entrants, particularly with respect to innovative products, several regional and local tobacco companies and, in some instances, state-owned tobacco enterprises, principally in Algeria, Egypt, the PRC, Taiwan, Thailand and Vietnam. Some competitors have different profit, volume and regulatory objectives, and some international competitors are susceptible to changes in different currency exchange rates. Certain new market entrants in the non-combustible product category may alienate consumers from innovative products through inappropriate marketing campaigns, messaging and inferior product satisfaction, while not relying on scientific substantiation based on appropriate R&D protocols and standards. The growing use of digital media could increase the speed and extent of the dissemination of inaccurate and misleading information about our RRPs, all of which could have a mutual adverse effect on our profitability and results of operations.

We may be unable to anticipate changes in adult consumer preferences.

Our business is subject to changes in adult consumer preferences, which may be influenced by local economic conditions, accessibility to our products and availability of accurate information related to our products.

To be successful, we must:

- promote brand equity successfully;
- anticipate and respond to new adult consumer trends;
- ensure that our products meet our quality standards;
- develop new products and markets and broaden brand portfolios;
- improve productivity;
- educate and convince adult smokers to convert to our RRPs;
- ensure effective adult consumer engagement, including communication about product characteristics and usage of RRPs;
- provide excellent customer care;
- ensure adequate production capacity to meet demand for our products; and
- be able to protect or enhance margins through price increases.

In periods of economic uncertainty, adult consumers may tend to purchase lower-price brands, and the volume of our premium-price and mid-price brands and our profitability could be materially adversely impacted as a result. Such down-trading trends may be reinforced by regulation that limits branding, communication and product differentiation.

Our ability to grow profitability may be limited by our inability to introduce new products, enter new markets or improve our margins through higher pricing and improvements in our brand and geographic mix.
Our profit growth may be materially adversely impacted if we are unable to introduce new products or enter new markets successfully, to raise prices or to improve the proportion of our sales of higher margin products and in higher margin geographies.

We may be unable to expand our brand portfolio through successful acquisitions or the development of strategic business relationships, and the intended benefits from our investments may not materialize.
One element of our growth strategy is to expand our brand portfolio and market positions through selective acquisitions and the development of strategic business relationships. Acquisition and strategic business development opportunities are limited and present risks of failing to achieve efficient and effective integration, strategic objectives and/or anticipated revenue improvements and cost savings. There is no assurance that we will be able to acquire attractive businesses or enter into strategic business relationships on favorable terms ahead of our competitors, or that such acquisitions or strategic business development relationships will be accretive to earnings or improve our competitive position. In addition, we may not have a controlling position in certain strategic investments or relationships, which could impact the extent to which the intended financial growth and other benefits from these investments or relationships may ultimately materialize.

Our ability to achieve our strategic goals may be impaired if we fail to attract, motivate and retain the best global talent and effectively align our organizational design with the goals of our transformation.
To be successful, we must continue transforming our culture and ways of working, align our talent and organizational design with our increasingly complex business needs, and innovate and transform to a consumer-centric business. We compete for talent, including in areas that are new to us, such as digital, information technology, life sciences, with companies in the consumer products, technology, pharmaceutical and other sectors that enjoy greater societal acceptance. As a result, we may be unable to attract, motivate and retain the best global talent with the right degree of diversity, experience and skills to achieve our strategic goals.

Risks Related to the Impact of COVID-19 on our Business

Our business, results of operations, cash flows and financial position may be adversely impacted during the continuation of the COVID-19 pandemic.

The ongoing COVID-19 pandemic has created significant societal and economic disruption, and resulted in closures of stores, factories and offices, and restrictions on manufacturing, distribution and travel, all of which have and will continue to adversely impact our business, results of operations, cash flows and financial position. Our business continuity plans and other safeguards may not be effective to mitigate the impact of the pandemic.

An adequate supply chain for our RRP portfolio, including the supply of electronic devices, is important to our business. We work with four electronics manufacturing service providers for the supply of our Platform 1 and Platform 4 devices, and a small number of other providers for other products in our RRP portfolio and related accessories. Due to the COVID-19 pandemic, the operations of our two main electronic manufacturing service providers were temporarily suspended at different times. Even though these suspensions did not materially affect our operations, if one or more of these service providers were significantly constrained at the same time, the supply of the devices could be disrupted. Although we work closely with these service providers on monitoring their production capability and financial health, we cannot guarantee that they will remain capable of meeting their commitments, particularly during the COVID-19 pandemic; if they will not, the commercialization of our RRPs could be adversely affected. The production of our RRP portfolio requires various metals, and we believe that there is an adequate supply of such metals in the world markets to satisfy our current and anticipated production requirements. However, some components and materials necessary for the production of our RRPs, including those for the electronic devices, are obtained from single or limited sources, and can be subject to industry-wide shortages and price fluctuations. While we were successful in maintaining adequate supply of such components and materials so far, we may not be able to secure such supply going forward, particularly during the COVID-19 pandemic; this could negatively impact the commercialization of our RRPs.

Significant risks to our business during the ongoing COVID-19 pandemic also include our diminished ability to convert adult smokers to our RRPs, significant volume declines in our duty-free business and certain other key markets, disruptions or delays in our manufacturing and supply chain, including delays and increased costs in the shipment of parts to manufacture our products or for the products themselves, increased currency volatility, and delays in certain cost saving, transformation and restructuring initiatives. Our business could also be adversely impacted if key personnel or a significant number of employees or business partners become unavailable due to the COVID-19 outbreak. The significant adverse impact of COVID-19 on the economic or political conditions in markets in which we operate could result in changes to the preferences of our adult consumers and lower demand for our products, particularly for our mid-price or premium-price brands.

Continuation of the pandemic could disrupt our access to the credit markets or increase our borrowing costs. Governments may temporarily be unable to focus on the development of science-based regulatory frameworks for the development and commercialization of RRPs or on the enforcement or implementation of regulations that are significant to our business. In addition, messaging about the potential negative impacts of the use of our products on COVID-19 risks may lead to increasingly restrictive regulatory measures on the sale and use of our products, negatively impact demand for our products and the willingness of adult consumers to switch to our RRPs, and adversely impact our efforts to advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs. All of the aforementioned impacts of the ongoing COVID-19 pandemic could have a material adverse effect on our business, operations, results of operations, revenues, cash flow and profitability.

The impact of these risks also depends on factors beyond our knowledge or control, including the duration and severity of the COVID-19 pandemic in general and specifically in the jurisdictions in which we operate, its recurrence in our key markets, actions taken to contain its spread and to mitigate its public health effects, and the ultimate economic consequences thereof.

Risks Related to Illicit Trade

We lose revenues as a result of counterfeiting, contraband, cross-border purchases, "illicit whites," non-tax-paid volume produced by local manufacturers, and counterfeiting of our Platform 1 device and heated tobacco units.

Large quantities of counterfeit cigarettes are sold in the international market. We believe that *Marlboro* is the most heavily counterfeited international cigarette brand, although we cannot quantify the revenues we lose as a result of this activity. In addition, our revenues are reduced by contraband, legal cross-border purchases, "illicit whites" and non-tax-paid volume produced by local manufacturers. Our revenues and consumer satisfaction with our Platform 1 device and heated tobacco units may be adversely affected by counterfeit products that do not meet our product quality standards and scientific validation procedures.

Risks Related to Cybersecurity and Data Governance

The failure of our information systems and systems owned and operated by our business partners to function as intended, or their penetration with the intent to corrupt them, or our and our business partners failure to adhere to strict data governance and cybersecurity protocols, and to comply with privacy laws and regulations, could result in business disruption, loss of reputation, litigation and regulatory action, and loss of revenue, assets or personal or other confidential data.

We as well as our business partners use information systems to help manage business processes, collect and interpret data and communicate internally and externally with employees, suppliers, consumers, customers and others. Some of these information systems are managed by third-party service providers. We are continuously evolving our approach to business continuity planning and backups to provide appropriate business resilience, particularly in light of the increasing cyber threat landscape. Nevertheless, failure of these systems to function as intended, or penetration of these systems and systems owned and operated by our business partners by parties intent on extracting or corrupting information or otherwise disrupting business processes, could place us at a competitive disadvantage, result in a loss of revenue, assets, including our intellectual property, personal or other sensitive data, result in litigation and regulatory action, cause damage to our reputation and that of our brands and result in significant remediation and other costs. Failure to protect personal data, respect the rights of data subjects, and adhere to strict data governance and cybersecurity protocols could subject us to substantial fines and other legal challenges under regulations such as the EU General Data Protection Regulation. As we are increasingly relying on digital platforms in our business, and as privacy laws in the jurisdictions in which we do business are introduced or become more stringent, the magnitude of these risks is likely to increase.

Risks Related to the Acquisitions of OtiTopic, Inc. ("OtiTopic"), Fertin Pharma and Vectura Group Plc (now known as Vectura Group Ltd.)

As previously disclosed in this Form 10-K, we have acquired Fertin Pharma A/G ("Fertin Pharma") and Vectura Group Ltd. ("Vectura") (with the Fertin Pharma acquisition and the Vectura acquisition being collectively referred to in these Risk Factors as the “Acquisitions”).

We may be unable to successfully integrate and realize the expected benefits from the Acquisitions.

The successful integration of the acquired businesses and their operations into those of our own and our ability to realize the benefits of the Acquisitions, are subject to a number of risks and uncertainties, many of which are not in our control. The risks and uncertainties relating to integrating the businesses acquired include, among other things: (i) the challenge of integrating complex organizations, systems, operating procedures, industry specific compliance programs, technology, networks and other assets of the businesses that we acquire, and the costs related to such integration efforts; (ii) the possibility that we are unable to gain access to differentiated proprietary technology and pharmaceutical development expertise as anticipated by these Acquisitions, and thus fail to realize our desired entry into additional smoke-free and wellness and healthcare platforms; (iii) the challenge of integrating the cultures and business practices of each of Fertin Pharma and Vectura to our culture and business practices, which if not managed correctly, could lead to difficulties in retaining key management and other key employees; and (iv) the challenge of achieving a successful integration as a result of our affiliation to our combustible product portfolio. In addition, even if we are able to successfully integrate, the anticipated benefits of the Acquisitions may not be realized fully, or at all, or may take longer to realize than expected. Furthermore, the success of the Acquisition also depends on the success of the research and development efforts of Fertin Pharma and Vectura, including the ability to obtain regulatory approval for new products, and the ability to commercialize or license these new products developed by them. Moreover, our affiliation to its combustible product portfolio may stand in the way of introducing and growing new product categories, and may prevent us in being successful in developing a long-term sustainable ecosystem of products in the wellness and healthcare categories.

The businesses that we acquire in the Acquisitions may have liabilities that are not known to us.

The businesses that we have acquired in the Acquisitions may have liabilities that we were unable to identify, or were unable to discover, in the course of performing our due diligence investigations during the Acquisitions thereof. We cannot assure you that the indemnification available to us under the respective acquisition agreements that we have negotiated, will be sufficient in amount, scope or duration to fully offset the possible liabilities associated with the respective business or property that we will assume upon consummation of each acquisition. Any such liabilities, individually or in the aggregate, could have a material adverse effect on our business, financial condition and results of operations.

Accounting adjustments related to the Acquisitions could adversely affect our financial results.
We have accounted for the completion of the Acquisitions using the acquisition method of accounting. Differences between preliminary estimates and the final acquisition accounting may occur, and these differences could have a material impact on the consolidated financial statements and our future results of operations and financial position in combination with the businesses acquired. Furthermore, given the nature of the assets being acquired in the Acquisitions, we may not be able to avoid future impairments of those assets, which may also have a material impact on our future results of operation and financial position.

PMI, Fertin Pharma and Vectura may be subject to uncertainties that could adversely affect our respective businesses, and adversely affect the financial results of our combined businesses.
Our success following these Acquisitions will depend in part upon our ability, and the ability of Fertin Pharma and Vectura, respectively, to maintain respective business relationships. Uncertainty about the effect of the Fertin Pharma Acquisition and the Vectura acquisition on customers, suppliers, employees and other constituencies of each of Fertin Pharma and Vectura, may have a material adverse effect on us and/or the businesses that we have acquired with the proposed Acquisitions. Customers, suppliers and others who do business with Fertin Pharma or Vectura may delay or defer business decisions, decide to terminate, modify or renegotiate their relationships, or take other actions as a result of our acquisitions of Fertin Pharma and Vectura, respectively, which could negatively affect the revenues, earnings and cash flows of our company or the businesses that we have acquired with these Acquisitions. If we are unable to maintain the business and operational relationships of Fertin Pharma and/or Vectura, our financial position, results of operations or cash flows upon combining with these companies could be adversely affected.

Item 1B. *Unresolved Staff Comments.*

None.

Item 2. *Properties.*

We own or lease various manufacturing, office and research and development facilities in locations primarily outside the United States. We own properties in Switzerland where our operations center and state-of-the-art research and development facility are located.

At December 31, 2021, we operated and owned a total of 39 manufacturing facilities across our six geographical segments and other category. Among them, 7 factories produced heated tobacco units.

In 2021, certain facilities each manufactured over 30 billion units (cigarettes and heated tobacco units combined). The largest manufacturing facilities, in terms of volume, are located in Russia (EE), Indonesia (S&SA), Turkey (ME&A), Poland (EU), the Philippines (S&SA), Italy (EU), Lithuania (EU) and Portugal (EU). As part of our global operating model, products manufactured in a particular manufacturing facility are not necessarily distributed in the operating segment where the facility is located.

We have integrated the production of our heated tobacco units into a number of our existing manufacturing facilities, and we are progressing with our plans to build manufacturing capacity for our other RRP platforms. We will continue to optimize our manufacturing infrastructure.

We believe the properties owned or leased by our subsidiaries are maintained in good condition and are believed to be suitable and adequate for our present needs.

Item 3. *Legal Proceedings.*

The information called for by this Item is incorporated herein by reference to Item 8, Note 17. *Contingencies*.

Item 4. *Mine Safety Disclosures.*

Not applicable.

PART II

Item 5. *Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.*

The principal stock exchange on which our common stock (no par value) is listed is the New York Stock Exchange (ticker symbol "PM"). At January 31, 2022, there were approximately 45,700 holders of record of our common stock.

Performance Graph

The graph below compares the cumulative total shareholder return on PMI's common stock with the cumulative total return for the same period of PMI's Peer Group and the S&P 500 Index. The graph assumes the investment of $100 as of December 31, 2016, in PMI common stock (at prices quoted on the New York Stock Exchange), and each of the indices as of the market close and reinvestment of dividends on a quarterly basis.

pm-20211231_g1.jpg

Date	PMI	PMI Peer Group [1]	S&P 500 Index
December 31, 2016	$100.00	$100.00	$100.00
December 31, 2017	$119.90	$117.40	$119.40
December 31, 2018	$80.00	$105.50	$112.00
December 31, 2019	$108.00	$130.70	$144.30
December 31, 2020	$112.20	$140.00	$167.80
December 31, 2021	$135.50	$162.00	$212.90

[1] The PMI Peer Group presented in this graph is the same as that used in the prior year. The PMI Peer Group was established based on a review of four characteristics: global presence; a focus on consumer products; and net revenues and a market capitalization of a similar size to those of PMI. The review also considered the primary international tobacco companies. As a result of this review, the following companies constitute the PMI Peer Group: Altria Group, Inc., Anheuser-Busch InBev SA/NV, British American Tobacco p.l.c., The Coca-Cola Company, Colgate-Palmolive Co., Diageo plc, Heineken N.V., Imperial Brands PLC, Japan Tobacco Inc., Johnson & Johnson, Kimberly-Clark Corporation, The Kraft-Heinz Company, McDonald's Corp., Mondelēz International, Inc., Nestlé S.A., PepsiCo, Inc., The Procter & Gamble Company, Roche Holding AG, and Unilever NV and PLC.

Note: Figures are rounded to the nearest $0.10.

Issuer Purchases of Equity Securities During the Quarter Ended December 31, 2021

Our share repurchase activity for each of the three months in the quarter ended December 31, 2021, was as follows:

Period	Total Number of Shares Repurchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Programs
October 1, 2021 – October 31, 2021 (1)	892,728	$ 96.13	1,842,587	$ 6,820,151,548
November 1, 2021 – November 30, 2021 (1)	—	$ —	1,842,587	$ 6,820,151,548
December 1, 2021 – December 31, 2021 (1)	6,672,042	$ 90.64	8,514,629	$ 6,215,395,934
Pursuant to Publicly Announced Plans or Programs	7,564,770	$ 91.29		
October 1, 2021 – October 31, 2021 (2)	5,368	$ 96.66		
November 1, 2021 – November 30, 2021 (2)	4,521	$ 95.19		
December 1, 2021 – December 31, 2021 (2)	1,497	$ 86.98		
For the Quarter Ended December 31, 2021	7,576,156	$ 91.29		

(1) On June 11, 2021, our Board of Directors authorized a new share repurchase program of up to $7 billion, with target spending of $5 billion to $7 billion over a three-year period that commenced in July 2021. These share repurchases have been made pursuant to the $7 billion program.

(2) Shares repurchased represent shares tendered to us by employees who vested in restricted and performance share unit awards and used shares to pay all, or a portion of, the related taxes.

Item 6. *[Reserved].*

Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations.*

The following discussion should be read in conjunction with the other sections of this Annual Report on Form 10-K, including the consolidated financial statements and related notes contained in Item 8, and the discussion of risks and cautionary factors that may affect future results in Item 1A. *Risk Factors*.

Description of Our Company

We are a leading international tobacco company working to deliver a smoke-free future and evolving our portfolio for the long-term to include products outside of the tobacco and nicotine sector. Our current product portfolio primarily consists of cigarettes and reduced-risk products, including heat-not-burn, vapor and oral nicotine products, which are sold in markets outside the United States. Since 2008, we have invested more than $9 billion to develop, scientifically substantiate and commercialize innovative smoke-free products for adults who would otherwise continue to smoke, with the goal of completely ending the sale of cigarettes. This includes the building of world-class scientific assessment capabilities, notably in the areas of pre-clinical systems toxicology, clinical and behavioral research, as well as post-market studies. The U.S. Food and Drug Administration ("FDA") has authorized the marketing of a version of PMI's *IQOS* Platform 1 device and consumables as a Modified Risk Tobacco Product (MRTP), finding that an exposure modification order for these products is appropriate to promote the public health. We describe the MRTP order in more detail in the "Business Environment" section of this Item 7. With a strong foundation and significant expertise in life sciences, in February 2021, we announced our ambition to expand into wellness and healthcare areas and deliver innovative products and solutions that aim to address unmet patient and consumer needs.

In the third quarter of 2021, our former Latin America & Canada segment was renamed as the Americas segment.

We currently manage our business in six geographical segments and an Other category:

- European Union ("EU");
- Eastern Europe ("EE");
- Middle East & Africa ("ME&A"), which includes our international duty free business;
- South & Southeast Asia ("S&SA");
- East Asia & Australia ("EA&A");
- Americas ("AMCS"); and
- Other, which includes our third quarter 2021 acquisitions of Fertin Pharma A/S, Vectura Group plc. (also known as Vectura Group Ltd.) and OtiTopic, Inc. For further details, see Item 8, Note 6. *Acquisitions,* and Item 8, Note 12. *Segment Reporting.*

Our cigarettes are sold in approximately 180 markets, and in many of these markets they hold the number one or number two market share position. We have a wide range of premium, mid-price and low-price brands. Our portfolio comprises both international and local brands.

In addition to the manufacture and sale of cigarettes, we are engaged in the development and commercialization of reduced-risk products ("RRPs"). RRPs is the term we use to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continuing smoking. *IQOS* is the leading brand in our smoke-free product portfolio. As of December 31, 2021, our smoke-free products are available for sale in 71 markets in key cities or nationwide.

During 2021, we laid the foundation for our long-term growth ambitions beyond nicotine in wellness and healthcare, including the milestone acquisitions of Vectura Group plc and Fertin Pharma A/S which provide essential capabilities for future product development.

We use the term net revenues to refer to our operating revenues from the sale of our products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. Our net revenues and operating income are

affected by various factors, including the volume of products we sell, the price of our products, changes in currency exchange rates and the mix of products we sell. Mix is a term used to refer to the proportionate value of premium-price brands to mid-price or low-price brands in any given market (product mix). Mix can also refer to the proportion of shipment volume in more profitable markets versus shipment volume in less profitable markets (geographic mix).

Our cost of sales consists principally of: tobacco leaf, non-tobacco raw materials, labor and manufacturing costs; shipping and handling costs; and the cost of devices produced by third-party electronics manufacturing service providers. Estimated costs associated with device warranty programs are generally provided for in cost of sales in the period the related revenues are recognized.

Our marketing, administration and research costs include the costs of marketing and selling our products, other costs generally not related to the manufacture of our products (including general corporate expenses), and costs incurred to develop new products. The most significant components of our marketing, administration and research costs are marketing and sales expenses and general and administrative expenses.

Philip Morris International Inc. is a legal entity separate and distinct from its direct and indirect subsidiaries. Accordingly, our right, and thus the right of our creditors and stockholders, to participate in any distribution of the assets or earnings of any subsidiary is subject to the prior rights of creditors of such subsidiary, except to the extent that claims of our company itself as a creditor may be recognized. As a holding company, our principal sources of funds, including funds to make payment on our debt securities, are from the receipt of dividends and repayment of debt from our subsidiaries. Our principal wholly owned and majority-owned subsidiaries currently are not limited by long-term debt or other agreements in their ability to pay cash dividends or to make other distributions that are otherwise compliant with law.

Executive Summary

The following executive summary provides the business update and significant highlights from the *Discussion and Analysis* that follows.

Consolidated Operating Results

- **Net Revenues –** Net revenues of $31.4 billion for the year ended December 31, 2021, increased by $2.7 billion, or 9.4%, from the comparable 2020 amount, and were impacted by the effects of the COVID-19 pandemic, particular in 2020. The change in our net revenues from the comparable 2020 amount was driven by the following (variances not to scale):
  pm-20211231_g2.jpg

  Net revenues, excluding currency and acquisitions, increased by 6.7%, mainly reflecting: favorable volume/mix, primarily driven by higher heated tobacco unit volume (notably in the EU, particularly Germany, Hungary, Italy and Poland, as well as Japan, Russia and Ukraine), and higher device volume (notably in the EU, primarily Italy, and Japan, partly offset by South Korea), partially offset by lower cigarette volume (mainly in the EU Region, notably the Czech Republic, France and Germany, as well as the GCC, North Africa, the Philippines, Russia and Ukraine, partly offset by India, Indonesia, PMI Duty Free and Turkey) and unfavorable cigarette mix (primarily in Germany, Japan and Russia, partially offset by Indonesia and PMI Duty Free); and a favorable pricing variance (notably driven by the Czech Republic, Germany, Japan, Kazakhstan, the Philippines, Russia and Turkey, partly offset by Australia, Indonesia, Poland and Ukraine); partially offset by the unfavorable impact of the Saudi Arabia customs assessments of $246 million, included in "Other" and further described in the following "*Diluted Earnings Per Share*" discussion.

  This net revenue growth reflects the continued strength of *IQOS*, and the recovery of the combustible business in many markets from the low base in 2020 due to the impact of COVID-19.

Net revenues by product category for the years ended December 31, 2021 and 2020, are shown below:

pm-20211231_g3.jpg pm-20211231_g4.jpg

Net revenues in the Other category primarily consist of operating revenues generated from the sale of inhaled therapeutics, and oral and intra-oral delivery systems resulting from the third quarter 2021 acquisitions of Fertin Pharma A/S, Vectura Group plc. and OtiTopic, Inc.

- **Diluted Earnings Per Share –** The changes in our reported diluted earnings per share ("diluted EPS") for the year ended December 31, 2021, from the comparable 2020 amounts, were as follows:

		Diluted EPS
For the year ended December 31, 2020	**$**	**5.16**
2020 Asset impairment and exit costs		**0.08**
2020 Brazil indirect tax credit		**(0.05)**
2020 Fair value adjustment for equity security investments		**0.04**
2020 Tax items		**(0.06)**
Subtotal of 2020 items		**0.01**
2021 Asset impairment and exit costs		**(0.12)**
2021 Saudi Arabia customs assessments		**(0.14)**
2021 Asset acquisition cost		**(0.03)**
2021 Equity investee ownership dilution		**0.04**
2021 Tax items		**—**
Subtotal of 2021 items		**(0.25)**
Currency		**0.12**
Interest		**—**
Change in tax rate		**0.08**
Operations		**0.71**
For the year ended December 31, 2021	**$**	**5.83**

Asset impairment and exit costs – During 2020, we recorded pre-tax asset impairment and exit costs of $149 million, representing $124 million net of income tax and a diluted EPS charge of $0.08 per share, related to the organizational design optimization plan,

primarily in Switzerland. During 2021, we recorded pre-tax asset impairment and exit costs of $216 million, representing $181 million net of income tax and a diluted EPS charge of $0.12 per share, related to the organizational design optimization plan, primarily in Switzerland, and the product distribution restructuring in South Korea. The total pre-tax charges in 2020 and 2021 were included in marketing, administration and research costs on the consolidated statements of earnings. For further details, see Item 8, Note 19. *Asset Impairment and Exit Costs*.

Brazil indirect tax credit - Following a final and enforceable decision by the highest court in Brazil in October 2020, we recorded a gain of $119 million for tax credits in 2020 ($79 million net of income tax and $0.05 per share increase in diluted EPS) representing overpayments of indirect taxes for the period from March 2012 through December 2019; these tax credits were applied to tax liabilities in Brazil during 2021. This amount was included as a reduction in marketing, administration and research costs in the consolidated statements of earnings for the year ended December 31, 2020, and was included in the operating income of the Americas segment. An additional amount of overpaid indirect taxes of approximately $90 million is dependent on a potential tax authority challenge.

Fair Value adjustment for equity security investments – During 2020, we recorded an unfavorable fair value adjustment for our equity security investments of $60 million after tax (or $0.04 per share decrease in diluted EPS). The fair value adjustment for our equity security investments was included in equity investments and securities (income)/loss, net ($76 million loss) and provision for income taxes ($16 million benefit) on the consolidated statements of earnings in 2020. For further details, see Item 8, Note 4. *Related Parties - Equity Investments and Other.*

Income taxes – The 2020 Tax items that increased our 2020 diluted EPS by $0.06 per share in the table above were due to final U.S. tax regulations under the Global Intangible Low-Taxed Income ("GILTI") provisions of the Internal Revenue Code for years 2018 and 2019 ($93 million).

The change in the tax rate that increased our diluted EPS by $0.08 per share in the table above was primarily due to the corporate income tax rate reduction in the Philippines (enacted in the first quarter of 2021), as well as changes in earnings mix by taxing jurisdiction. For further details, see Item 8, Note 11. *Income Taxes*.

*Saudi Arabia customs assessment*s – In June 2021, the Customs Appeal Committee in Riyadh notified our distributors in Saudi Arabia of its decisions to largely reject their challenges of the Saudi Arabia Customs General Authority assessments as described in Item 8, Note 17. *Contingencies*. On the basis of these decisions and in line with arrangements with the distributors, we recorded a pre-tax charge of $246 million in the second quarter of 2021 (representing $215 million net of income tax and a diluted EPS charge of $0.14 per share). The pre-tax charge was recorded as a reduction of net revenues on the consolidated statement of earnings for the year ended December 31, 2021, and was included in the Middle East & Africa segment results.

Asset acquisition cost – In August 2021, we acquired 100% of OtiTopic, Inc., a U.S. respiratory drug development company with a late-stage dry powder inhalation aspirin treatment for acute myocardial infarction. We accounted for this transaction as an asset acquisition since the acquired in-process research and development ("IPR&D") of the dry powder inhalation aspirin treatment represented substantially all of the fair value of the gross assets acquired. At the date of acquisition, we determined that the acquired IPR&D had no alternative future use. As a result, we recorded a pre-tax charge of $51 million (representing a $0.03 per share charge to diluted EPS) to research and development costs within marketing, administration and research costs in the consolidated statements of earnings for the year ended December 31, 2021. For further details, see Item 8, Note 6. *Acquisitions*.

Equity investee ownership dilution – In 2021, our equity method investee, Medicago Inc, initiated additional rounds of equity funding in which we did not participate. As a result, our share of holdings in Medicago Inc. was reduced from approximately 32% to approximately 23% as of December 31, 2021. The ownership dilution resulted in a $0.04 per share favorable impact to diluted EPS and income of $55 million to Equity investments and securities (income)/loss, net in the consolidated statements of earnings for the year ended December 31, 2021. For further details, see Item 8, Note 17. *Contingencies - Third Party Guarantees*.

Currency – The favorable impact of $0.12 per share during the reporting period primarily results from the fluctuations of the U.S. dollar, especially against the Euro. This favorable currency movement has impacted our profitability across our primary revenue markets and local currency cost bases.

Operations – The increase in diluted EPS of $0.71 per share from our operations in the table above was due primarily to the following segments:

- European Union: Favorable volume/mix, lower manufacturing costs and favorable pricing, partially offset by higher marketing, administration and research costs;
- Middle East & Africa: Favorable pricing, favorable volume/mix and lower manufacturing costs, partially offset by lower

fees for certain distribution rights and higher marketing, administration and research costs;

- Eastern Europe: Favorable volume/mix, lower manufacturing costs, favorable pricing and lower marketing, administration and research costs;
- East Asia & Australia: Favorable pricing and lower manufacturing costs, partially offset by higher marketing, administration and research costs; and
- Americas: Favorable pricing and lower marketing, administration and research costs, partially offset by higher manufacturing costs;

partially offset by

- South & Southeast Asia: Unfavorable pricing, unfavorable volume/mix and higher marketing, administration and research costs.

For further details, see the *Consolidated Operating Results* and *Operating Results by Business Segment* sections of the following *Discussion and Analysis*.

***IQOS* Device Supply**

The current global semiconductor shortage has resulted in a tightness in *IQOS* device supply in the second half of 2021. In the fourth quarter of 2021, the *IQOS* device supply situation eased, resulting in an improved *IQOS* user growth versus the third quarter. We expect an improving *IQOS* device supply situation, with a gradual return to an unconstrained *IQOS* user quarterly growth progression. However, we still do not have full visibility over the full year 2022.

***IQOS* in the United States**

On November 29, 2021, an importation ban and cease-and-desist orders imposed by the U.S. International Trade Commission ("ITC") relating to *IQOS* Platform 1 products (including consumables and infringing components) went into effect. As a result, *IQOS* is not currently available for sale in the U.S. We have appealed the patent and statutory issues related to the ITC's Final Determination, and also have contingency plans underway, including domestic production. We hope to be able to resume U.S. supply in the first half of 2023. For more details on the ITC case and related legal matters, please refer to Item 8, Note 17. *Contingencies*.

The ITC decision has no bearing outside the U.S.; competitor lawsuits based on the same patent families have repeatedly and universally failed in European courts and the European Patent Office.

Acquisitions

During 2021, PMI acquired the following companies:

- Vectura Group plc, an inhaled therapeutics company based in the United Kingdom;
- Fertin Pharma A/S, a Danish company that is a leading developer and manufacturer of innovative pharmaceutical and well-being products based on oral and intra-oral delivery systems;
- OtiTopic, Inc., a U.S. respiratory drug development company with a late-stage dry powder inhalation aspirin treatment for acute myocardial infarction; and
- AG Snus Aktieselskab, a Danish company, and its Swedish subsidiary, Tobacco House of Sweden AB, fully owned by AG Snus, which operates in the oral tobacco and modern oral product categories.

For further details on these acquisitions, see Item 8, Note 6. *Acquisitions*.

Discussion and Analysis

Critical Accounting Estimates

Item 8, Note 2. *Summary of Significant Accounting Policies* to our consolidated financial statements includes a summary of the significant accounting policies and methods used in the preparation of our consolidated financial statements. In most instances, we must use a particular accounting policy or method because it is the only one that is permitted under U.S. GAAP.

The preparation of financial statements requires that we use estimates and assumptions that affect the reported amounts of our assets, liabilities, net revenues and expenses, as well as our disclosure of contingencies. If actual amounts differ from previous estimates, we include the revisions in our consolidated results of operations in the period during which we know the actual amounts. Historically, aggregate differences, if any, between our estimates and actual amounts in any year have not had a significant impact on our consolidated financial statements.

The selection and disclosure of our critical accounting estimates have been discussed with our Audit Committee. The following is a discussion of the more significant assumptions, estimates, accounting policies and methods used in the preparation of our consolidated financial statements:

Revenue Recognition - We recognize revenue as performance obligations are satisfied. Our primary performance obligation is the distribution and sales of cigarettes and reduced-risk products, including heat-not-burn, vapor and oral nicotine products. Our performance obligations are typically satisfied upon shipment or delivery to our customers. The company estimates the cost of sales returns based on historical experience, and these estimates are immaterial. Estimated costs associated with warranty programs for *IQOS* devices are generally provided for in cost of sales in the period the related revenues are recognized, based on a number of factors, including historical experience, product failure rates and warranty policies. The transaction price is typically based on the amount billed to the customer and includes estimated variable consideration where applicable. Such variable consideration is typically not constrained and is estimated based on the most likely amount that PMI expects to be entitled to under the terms of the contracts with customers, historical experience of discount or rebate redemption, where relevant, and the terms of any underlying discount or rebate programs, which may change from time to time as the business and product categories evolve.

Inventories - Our inventories are valued at the lower of cost or market based upon assumptions about future demand and market conditions. The valuation of inventory also requires us to estimate obsolete and excess inventory. We perform regular reviews of our inventory on hand, as well as our future purchase commitments with our suppliers, considering multiple factors, including demand forecasts, product life cycle, current sales levels, pricing strategy and cost trends. If our review indicates that inventories of raw materials, components or finished products have become obsolete or are in excess of anticipated demand or that inventory cost exceeds net realizable value, we may be required to make adjustments that will impact the results of operations.

Goodwill and Non-Amortizable Intangible Assets Valuation - We test goodwill and non-amortizable intangible assets for impairment annually or more frequently if events occur that would warrant such review. While the company has the option to perform a qualitative assessment for both goodwill and non-amortizable intangible assets to determine if it is more likely than not that an impairment exists, the company elects to perform the quantitative assessment for our annual impairment analysis. The impairment analysis involves comparing the fair value of each reporting unit or non-amortizable intangible asset to the carrying value. If the carrying value exceeds the fair value, goodwill or a non-amortizable intangible asset is considered impaired. To determine the fair value of goodwill, we primarily use the market approach using earnings multiples of comparable global companies within the tobacco industry, supported by a discounted cash flow model. At December 31, 2021, the carrying value of our goodwill was $6.7 billion, which is related to ten geographical reporting units, each of which consists of a group of markets with similar operating and economic characteristics and our 2021 acquisitions. The Fertin Pharma A/S, Vectura Group plc. and OtiTopic, Inc. acquisitions in 2021 are considered separate operating segments and are accounted for within the Other category. For additional information see Item 8, Note 6. *Acquisitions*. The estimated fair value of each of our ten reporting units and additional businesses acquired in 2021 exceeded the carrying value as of December 31, 2021. To determine the fair value of non-amortizable intangible assets, we primarily use a discounted cash flow model applying the relief-from-royalty method. We concluded that the fair value of our non-amortizable intangible assets exceeded the carrying value. These discounted cash flow models include management assumptions relevant

for forecasting operating cash flows, which are subject to changes in business conditions, such as volumes and prices, costs to produce, discount rates and estimated capital needs. Management considers historical experience and all available information at the time the fair values are estimated, and we believe these assumptions are consistent with the assumptions a hypothetical marketplace participant would use. Since the March 28, 2008, spin-off from Altria Group, Inc., we have not recorded a charge to earnings for an impairment of goodwill or non-amortizable intangible assets.

Marketing Costs - We incur certain costs to support our products through programs that include advertising, marketing, consumer engagement and trade promotions. The costs of our advertising and marketing programs are expensed in accordance with U.S. GAAP. Recognition of the cost related to our consumer engagement and trade promotion programs contain uncertainties due to the judgment required in estimating the potential performance and compliance for each program. For volume-based incentives provided to customers, management continually assesses and estimates, by customer, the likelihood of the customer's achieving the specified targets, and records the reduction of revenue as the sales are made. For other trade promotions, management relies on estimated utilization rates that have been developed from historical experience. Changes in the assumptions used in estimating the cost of any individual marketing program would not result in a material change in our financial position, results of operations or operating cash flows.

Employee Benefit Plans - As discussed in Item 8, Note 13. *Benefit Plans* to our consolidated financial statements, we provide a range of benefits to our employees and retired employees, including pensions, postretirement health care and postemployment benefits (primarily severance). We record annual amounts relating to these plans based on calculations specified by U.S. GAAP. These calculations include various actuarial assumptions, such as discount rates, assumed rates of return on plan assets, compensation increases, mortality, turnover rates and health care cost trend rates. We review actuarial assumptions on an annual basis and make modifications to the assumptions based on current rates and trends when it is deemed appropriate to do so. As permitted by U.S. GAAP, any effect of the modifications is generally amortized over future periods. We believe that the assumptions utilized in calculating our obligations under these plans are reasonable based upon our historical experience and advice from our actuaries.

Weighted-average discount rate assumptions for pension and postretirement plan obligations at December 31, 2021 and 2020 are as follows:

	2021	2020
Pension plans	**0.86%**	0.56%
Postretirement plans	**3.08%**	2.84%

We anticipate that assumption changes will decrease 2022 pre-tax pension and postretirement expense to approximately $152 million as compared with approximately $300 million in 2021, excluding amounts related to employee severance and early retirement programs. The anticipated decrease is primarily due to lower amortization of unrecognized actuarial gains/losses of $123 million, coupled with lower service cost of $45 million and other movements of $9 million, partially offset by higher interest cost of $29 million.

Weighted-average expected rate of return and discount rate assumptions have a significant effect on the amount of expense reported for the employee benefit plans. A fifty-basis-point decrease in our discount rate would increase our 2022 pension and postretirement expense by approximately $70 million, and a fifty-basis-point increase in our discount rate would decrease our 2022 pension and postretirement expense by approximately $58 million. Similarly, a fifty-basis-point decrease (increase) in the expected return on plan assets would increase (decrease) our 2022 pension expense by approximately $43 million.

Income Taxes - Income tax provisions for jurisdictions outside the United States, as well as state and local income tax provisions, are determined on a separate company basis, and the related assets and liabilities are recorded in our consolidated balance sheets.

The extent of our operations involves dealing with uncertainties and judgments in the application of complex tax regulations in a multitude of jurisdictions. The final taxes paid are dependent upon many factors, including negotiations with taxing authorities in various jurisdictions and resolution of disputes arising from federal, state, and international tax audits. In accordance with the authoritative guidance for income taxes, we evaluate potential tax exposures and record tax liabilities for anticipated tax audit issues based on our estimate of whether, and the extent to which, additional taxes will be due. We adjust these reserves in light of changing facts and circumstances; however, due to the complexity of some of these uncertainties, the ultimate resolution may result in a payment that is materially different from our current estimate of the tax liabilities. If our estimate of tax liabilities proves to be less than the ultimate assessment, an additional charge to expense would result. If payment of these amounts ultimately proves to be less than the recorded amounts, the reversal of the liabilities would result in tax benefits being recognized in the period when we determine the liabilities are no longer necessary.

We are required to assess the likelihood of recovering deferred tax assets against future sources of taxable income. If we determine, using all available evidence, that we do not reach the more likely than not threshold for recovery, a valuation allowance is recorded. Significant judgment is required in determining the need for and amount of valuation allowances for deferred tax assets including estimates of future taxable income in the applicable jurisdictions and the feasibility of on-going tax planning strategies, as applicable.

The effective tax rates used for interim reporting are based on our full-year geographic earnings mix projections. Changes in currency exchange rates, earnings mix by taxing jurisdiction or future regulatory developments may have an impact on the effective tax rates. Significant judgment is required in determining income tax provisions and in evaluating tax positions.

For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements.

Hedging - As discussed below in "Market Risk," we use derivative financial instruments principally to reduce exposures to market risks resulting from fluctuations in foreign currency exchange and interest rates by creating offsetting exposures. For derivative contracts that are designated and qualify as fair value hedges the gain or loss on the derivative, as well as the offsetting gain or loss on the hedged items attributable to the hedged risk, is recognized in the consolidated statement of earnings. For our other derivatives to which we have elected to apply hedge accounting, gains and losses on these derivatives are initially deferred in accumulated other comprehensive losses on the consolidated balance sheet and recognized in the consolidated statement of earnings into the same line item as the impact of the underlying transaction and in the periods when the related hedged transactions are also recognized in operating results. If we had elected not to use the hedge accounting provisions, gains (losses) deferred in stockholders' (deficit) equity would have been recorded in our net earnings for these derivatives.

Fair value of non-marketable equity securities - For further details, see Item 8, Note 20. *Deconsolidation of RBH.*

Contingencies - As discussed in Item 8, Note 17. *Contingencies* to our consolidated financial statements, legal proceedings covering a wide range of matters are pending or threatened against us, and/or our subsidiaries, and/or our indemnitees in various jurisdictions. We and our subsidiaries record provisions in the consolidated financial statements for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. The variability in pleadings in multiple jurisdictions, together with the actual experience of management in litigating claims, demonstrate that the monetary relief that may be specified in a lawsuit bears little relevance to the ultimate outcome. Much of the tobacco-related litigation is in its early stages, and litigation is subject to uncertainty. At the present time, except as stated otherwise in Item 8, Note 17. *Contingencies,* while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available to it: (i) management has not concluded that it is probable that a loss has been incurred in any of the pending tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any. Legal defense costs are expensed as incurred.

Consolidated Operating Results

Our net revenues and operating income by segment were as follows:

(in millions)	2021	2020	2019
Net Revenues			
European Union	**$ 12,275**	$ 10,702	$ 9,817
Eastern Europe	**3,544**	3,378	3,282
Middle East & Africa	**3,293**	3,088	4,042
South & Southeast Asia	**4,396**	4,396	5,094
East Asia & Australia	**5,953**	5,429	5,364
Americas [1]	**1,843**	1,701	2,206
Other	**101**	—	—
Net revenues	**$ 31,405**	$ 28,694	$ 29,805
Operating Income (Loss)			
European Union	**$ 6,119**	$ 5,098	$ 3,970
Eastern Europe	**1,213**	871	547
Middle East & Africa	**1,146**	1,026	1,684
South & Southeast Asia	**1,506**	1,709	2,163
East Asia & Australia	**2,556**	2,400	1,932
Americas [1]	**487**	564	235
Other	**(52)**	—	—
Operating income	**$ 12,975**	$ 11,668	$ 10,531

[1] As of March 22, 2019, PMI deconsolidated the financial results of its Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH"), from PMI's financial statements. For further details, see Item 8, Note 20. *Deconsolidation of RBH*.

Items affecting the comparability of results from operations were as follows:

- **Asset impairment and exit costs** - See Item 8, Note 19. *Asset Impairment and Exit Costs* for details of the $216 million, $149 million and $422 million pre-tax charges for the years ended December 31, 2021, 2020 and 2019, respectively, as well as a breakdown of these costs by segment.
- **Saudi Arabia customs assessments** – See Item 8, Note 17. *Contingencies* for the details of the $246 million reduction in net revenues of combustible products included in the Middle East & Africa segment for the year ended December 31, 2021.
- **Asset acquisition cost** - See Item 8, Note 6. *Acquisitions* for the details of the $51 million pre-tax charge associated with the asset acquisition of OtiTopic, Inc. included in Other within the operating income table above for the year ended December 31, 2021.
- **Russia excise and VAT audit charge** - See Item 8, Note 17. *Contingencies* for details of the $374 million pre-tax charge included in the Eastern Europe segment for the year ended December 31, 2019.
- **Canadian tobacco litigation-related expense** - See Item 8, Note 17. *Contingencies* and Note 20. *Deconsolidation of RBH* for details of the $194 million pre-tax charge included in the Americas segment for the year ended December 31, 2019.
- **Loss on deconsolidation of RBH** - See Item 8, Note 20. *Deconsolidation of RBH* for details of the $239 million loss included in the Americas segment for the year ended December 31, 2019.
- **Brazil indirect tax credit** - Following a final and enforceable decision by the highest court in Brazil in October 2020, PMI recorded a gain of $119 million for tax credits representing overpayments of indirect taxes for the period from March 2012 through December 2019; these tax credits were applied to tax liabilities in Brazil during 2021. This amount was included as a reduction in marketing, administration and research costs in the consolidated statements of earnings for the year ended December 31, 2020, and was included in the operating

income of the Americas segment. An additional amount of overpaid indirect taxes of approximately $90 million is dependent on a potential tax authority challenge.

Our net revenues by product category were as follows:

PMI Net Revenues by Product Category

(in millions)	2021	2020	2019
Combustible Products			
European Union	**$ 8,211**	$ 8,053	$ 8,093
Eastern Europe	**2,240**	2,250	2,438
Middle East & Africa	**3,148**	3,031	3,721
South & Southeast Asia	**4,385**	4,395	5,094
East Asia & Australia	**2,414**	2,468	2,693
Americas	**1,790**	1,670	2,179
Total Combustible Products	**$ 22,190**	$ 21,867	$ 24,218
Reduced-Risk Products			
European Union	**$ 4,064**	$ 2,649	$ 1,724
Eastern Europe	**1,304**	1,128	844
Middle East & Africa	**145**	57	321
South & Southeast Asia	**11**	1	—
East Asia & Australia	**3,539**	2,961	2,671
Americas	**53**	31	27
Total Reduced-Risk Products	**$ 9,115**	$ 6,827	$ 5,587
Other			
Other	**$ 101**	**$ —**	**$ —**
Total PMI Net Revenues	**$ 31,405**	$ 28,694	$ 29,805

Note: Sum of product categories or Regions might not foot to total PMI due to rounding.

Net revenues related to combustible products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of our cigarettes and other tobacco products combined. Other tobacco products primarily include roll-your-own and make-your-own cigarettes, pipe tobacco, cigars and cigarillos and do not include reduced-risk products.

Net revenues related to reduced-risk products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of our heated tobacco units, heat-not-burn devices and related accessories, and other nicotine-containing products, which primarily include our e-vapor and oral nicotine products.

Net revenues in the Other category primarily consist of operating revenues generated from the sale of inhaled therapeutics, and oral and intra-oral delivery systems resulting from the third quarter 2021 acquisitions of Fertin Pharma A/S, Vectura Group plc. and OtiTopic, Inc.

PMI's heat-not-burn products include licensed KT&G heat-not-burn products.

Revenues from shipments of Platform 1 devices, heated tobacco units and accessories to Altria Group, Inc., commencing in the third quarter of 2019, for sale under license in the United States, are included in Net Revenues of the Americas segment.

References to "Cost/Other" in the Consolidated Financial Summary table of total PMI and the six geographical segments throughout this *"Discussion and Analysis"* reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs (including asset impairment and exit costs); and amortization of intangibles. “Cost/Other” also includes the currency-neutral net revenue variance, unrelated to volume/mix and price components, attributable to: fees for certain distribution rights

billed to customers in certain markets in the ME&A Region, and the Saudi Arabia customs assessment net revenue adjustment.

Our shipment volume by segment for cigarettes and heated tobacco units was as follows:

	PMI Shipment Volume (Million Units)	
	2021	**2020**
Cigarettes		
European Union	**157,843**	163,4
Eastern Europe	**88,698**	93,4
Middle East & Africa	**127,911**	117,9
South & Southeast Asia	**141,923**	144,7
East Asia & Australia	**43,913**	45,1
Americas	**64,587**	63,7
Total Cigarettes	**624,875**	628,5
Heated Tobacco Units		
European Union	**28,208**	19,
Eastern Europe	**25,650**	20,
Middle East & Africa	**2,140**	1,
South & Southeast Asia	**240**	
East Asia & Australia	**38,162**	33,
Americas	**576**	
Total Heated Tobacco Units	**94,976**	76,
Cigarettes and Heated Tobacco Units		
European Union	**186,051**	183,
Eastern Europe	**114,348**	114,
Middle East & Africa	**130,051**	119,
South & Southeast Asia	**142,163**	144,
East Asia & Australia	**82,075**	78,
Americas	**65,163**	64,
Total Cigarettes and Heated Tobacco Units	**719,851**	704,

Following the deconsolidation of our Canadian subsidiary, we continue to report the volume of brands sold by RBH for which other PMI subsidiaries are the trademark owners. These include *HEETS*, *Next*, *Philip Morris* and *Rooftop.*

Heated tobacco units ("HTU") is the term we use to refer to heated tobacco consumables, which include our *HEETS*, *HEETS Creations, HEETS Dimensions, HEETS Marlboro* and *HEETS FROM MARLBORO (*defined collectively as *HEETS)*, *Marlboro Dimensions*, *Marlboro HeatSticks, Parliament HeatSticks* and *TEREA*, as well as the KT&G-licensed brands, *Fiit* and *Miix* (outside of South Korea).

Market share for HTUs is defined as the total sales volume for HTUs as a percentage of the total estimated sales volume for cigarettes and HTUs.

Shipment volume of heated tobacco units to the United States is included in the heated tobacco unit shipment volume of the Americas segment.

References to total international market, defined as worldwide cigarette and heated tobacco unit volume excluding the United States, total industry, total market and market shares throughout this *"Discussion and Analysis"* are our estimates for tax-paid products based on the latest available data from a number of internal and external sources and may, in defined instances, exclude the People's Republic of China and/or our duty free business.

2020 and 2021 estimates for total industry volume and market share in certain geographies reflect limitations on the availability and accuracy of industry data during pandemic-related restrictions.

In-market sales ("IMS") is defined as sales to the retail channel, depending on the market and distribution model.

North Africa is defined as Algeria, Egypt, Libya, Morocco and Tunisia.

The Gulf Cooperation Council ("GCC") is defined as Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates (UAE).

Southeast Europe is defined as Albania, Bosnia & Herzegovina, Kosovo, Montenegro, North Macedonia and Serbia.

References to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units, unless otherwise stated.

From time to time, PMI's shipment volumes are subject to the impact of distributor inventory movements, and estimated total industry/market volumes are subject to the impact of inventory movements in various trade channels that include estimated trade inventory movements of PMI's competitors arising from market-specific factors that significantly distort reported volume disclosures. Such factors may include changes to the manufacturing supply chain, shipment methods, consumer demand, timing of excise tax increases or other influences that may affect the timing of sales to customers. In such instances, in addition to reviewing PMI shipment volumes and certain estimated total industry/market volumes on a reported basis, management reviews these measures on an adjusted basis that excludes the impact of distributor and/or estimated trade inventory movements. Management also believes that disclosing PMI shipment volumes and estimated total industry/market volumes in such circumstances on a basis that excludes the impact of distributor and/or estimated trade inventory movements improves the comparability of performance and trends for these measures over different reporting periods.

2021 compared with 2020

The following discussion compares our consolidated operating results for the year ended December 31, 2021, with the year ended December 31, 2020.

Estimated international industry cigarette and heated tobacco unit volume, excluding China and the U.S., of 2.6 trillion, increased by 2.4%, driven by the EU, Middle East & Africa, South & Southeast Asia and Americas Regions, partly offset by the Eastern Europe and East Asia & Australia Regions, as described in the Regional sections.

Our total shipment volume increased by 2.2%, driven by:

- the EU, reflecting higher heated tobacco unit shipment volume across the Region, particularly in Germany, Hungary, Italy and Poland, partly offset by lower cigarette shipment volume, notably in the Czech Republic, France and Germany;
- Middle East & Africa, reflecting higher cigarette shipment volume (primarily in PMI Duty Free and Turkey, partly offset by the GCC and North Africa), as well as higher heated tobacco unit shipment volume across the Region;
- East Asia & Australia, reflecting higher heated tobacco unit shipment volume driven by Japan, partly offset by lower cigarette shipment volume, predominantly in South Korea; and
- Americas, mainly reflecting higher cigarette shipment volume, primarily in Brazil and Mexico, partially offset by Argentina;

partly offset by

- South & Southeast Asia, primarily reflecting lower cigarette shipment volume, mainly in the Philippines, partially offset by Indonesia and Pakistan.

Total shipment volume in Eastern Europe was essentially flat, reflecting lower cigarette shipment volume, mainly in Russia and Ukraine, almost fully offset by higher heated tobacco unit shipment volume, primarily in Russia and Ukraine.

Impact of Inventory Movements

Excluding the net favorable impact of estimated distributor inventory movements of approximately 8.4 billion units, our total in-market sales increased by 1.0%, driven by a 21.1% increase in heated tobacco units, partly offset by a 1.5% decrease in cigarettes.

The net favorable impact of approximately 8.4 billion units reflected:

- A net favorable impact of 5.6 billion cigarettes, mainly driven by 2020 movements in Japan, PMI Duty Free and Russia; and
- A net favorable impact of 2.7 billion heated tobacco units, primarily reflecting the growing category and driven by Japan, Italy, PMI Duty Free and Russia.

Our total heated tobacco unit in-market sales volume in the year was 92.5 billion units.

Our cigarette shipment volume by brand and heated tobacco unit shipment volume was as follows:

PMI Shipment Volume by Brand (Million Units)

	2021	2020	Change
Cigarettes			
Marlboro	**239,905**	233,158	2.9 %
L&M	**84,342**	91,098	(7.4)%
Chesterfield	**58,800**	52,139	12.8 %
Philip Morris	**42,395**	45,645	(7.1)%
Parliament	**41,621**	34,737	19.8 %
Sampoerna A	**37,815**	32,862	15.1 %
Dji Sam Soe	**22,627**	24,754	(8.6)%
Lark	**15,487**	15,489	— %
Bond Street	**14,175**	24,113	(41.2)%
Next	**8,849**	8,980	(1.5)%
Others	**58,859**	65,543	(10.2)%
Total Cigarettes	**624,875**	628,518	(0.6)%
Heated Tobacco Units	**94,976**	76,111	24.8 %
Total Cigarettes and Heated Tobacco Units	**719,851**	704,629	2.2 %

Note: *Lark* includes *Lark Harmony*; *Next* includes *Next Dubliss*; *Philip Morris* includes *Philip Morris/Dubliss*; and *Sampoerna A* includes *Sampoerna*.

The increase in our heated tobacco unit shipment volume was mainly driven by the EU (notably Italy), Eastern Europe (notably Russia and Ukraine) and Japan.

Our cigarette shipment volume of the following brands increased:

- *Marlboro,* mainly driven by Mexico, PMI Duty Free, Russia and Turkey, partly offset by France, Japan and the Philippines;
- *Chesterfield*, primarily driven by Brazil, the Philippines and Russia, partly offset by Saudi Arabia;
- *Parliament*, mainly driven by Russia, Saudi Arabia and Turkey, partly offset by South Korea; and
- *Sampoerna A* in Indonesia, primarily driven by premium *A Mild*.

Our cigarette shipment volume of the following brands decreased:

- *L&M*, mainly due to Egypt, Germany, Poland, Russia and Turkey;

- *Philip Morris*, primarily due to Indonesia, Italy and Russia, partly offset by Japan;
- *Dji Sam Soe* in Indonesia, mainly due to *Dji Sam Soe Magnum Mild*;

- *Bond Street*, primarily due to Kazakhstan, Russia and Ukraine;
- *Next*, primarily due to Canada and Ukraine, partly offset by Russia; and
- "Others," notably due to: mid-price *Fortune* (Philippines) and *Sampoerna U* (Indonesia); and low-price *Jackpot* (Philippines) and *More* (Philippines); partly offset by mid-price *Sampoerna Hijau* (Indonesia) and low-price *Morven* (Pakistan).

PMI's cigarette shipment volume for *Lark* was flat.

2021 International Share of Market (excluding China and the United States)

Our total international market share (excluding China and the United States), defined as our cigarette and heated tobacco unit sales volume as a percentage of total industry cigarette and heated tobacco unit sales volume, decreased by 0.4 points to 27.3%, reflecting:

- Total international market share for cigarettes of 23.8%, down by 0.9 points; and
- Total international market share for heated tobacco units of 3.5%, up by 0.5 points.

Our total international cigarette sales volume as a percentage of total industry cigarette sales volume was down by 0.8 points to 24.9%, mainly reflecting lower cigarette market share and/or an unfavorable geographic mix impact, notably in Japan, the Philippines and Russia, partly offset by Indonesia and Turkey.

In 2021, we owned five of the world's top 15 international cigarette brands, with international cigarette market shares as follows: *Marlboro*, 9.5%; *L&M*, 3.4%; *Chesterfield*, 2.3%; *Philip Morris*, 1.7%; and *Parliament*, 1.7%.

Key Market Data

Key market data regarding total market size, our shipments and market share were as follows:

Market	Total Market (billion units)		PMI Shipments (billion units)						PMI Market Share (%)[1]			
			Total		Cigarette		Heated Tobacco Unit		Total		Heated Tobacco Unit	
	2021	2020	2021	2020	2021	2020	2021	2020	2021	2020	2021	2020
Total	2,613.2	2,551.1	719.9	704.6	624.9	628.5	95.0	76.1	27.3	27.7	3.5	3.0
European Union												
France	34.3	36.6	15.2	16.3	15.0	16.1	0.2	0.2	43.9	44.9	0.7	0.5
Germany	74.1	74.6	28.6	29.1	26.3	27.4	2.3	1.6	38.6	39.0	3.1	2.2
Italy	70.4	67.4	38.6	34.6	29.7	29.0	8.9	5.6	53.0	52.2	11.5	8.1
Poland	49.3	45.6	18.4	17.8	15.3	15.4	3.1	2.4	37.3	39.0	6.3	5.2
Spain	42.7	41.8	13.2	13.2	12.6	12.8	0.5	0.4	31.1	31.4	1.2	1.0
Eastern Europe												
Russia	216.8	219.1	68.8	69.2	52.5	55.6	16.3	13.6	31.7	32.3	7.4	6.3
Middle East & Africa												
Saudi Arabia	21.1	21.7	8.9	9.1	8.7	9.0	0.2	0.1	41.6	39.0	1.0	0.3
Turkey	124.2	114.8	55.7	47.5	55.7	47.5	—	—	44.8	41.3	—	—
South & Southeast Asia												
Indonesia	296.2	276.2	82.8	79.5	82.8	79.5	—	—	28.0	28.8	—	—
Philippines	55.4	62.1	34.4	41.7	34.2	41.7	0.2	—	62.0	67.2	0.3	0.1
East Asia & Australia												
Australia	9.7	11.0	3.1	3.3	3.1	3.3	—	—	32.3	29.9	—	—
Japan	139.5	142.9	55.2	51.1	22.1	22.2	33.1	28.9	38.5	37.1	22.9	20.4
South Korea	71.7	71.6	14.1	14.8	9.4	10.2	4.7	4.6	19.7	20.7	6.5	6.5
Americas												
Argentina	36.1	33.6	19.9	20.5	19.9	20.5	—	—	55.1	61.0	—	—
Mexico	32.0	30.7	20.5	19.5	20.4	19.5	0.1	0.1	64.0	63.7	0.3	0.2

(1) Market share estimates are calculated using IMS data

Note: % change for Total Market and PMI shipments is computed based on millions of units. "-" indicates volume below 50 million units and market share below 0.1%

Financial Summary

Financial Summary - Years Ended December 31, (in millions)	2021	2020	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr. & Acquis.	Variance Fav./(Unfav.) Total	Cur-rency	Acqui-sitions	Price	Vol/ Mix	Cost/ Other
Net Revenues [1]	**$ 31,405**	$ 28,694	9.4 %	6.7 %	$ 2,711	$ 678	$ 109	$ 667	$ 1,538	$ (281)
Cost of Sales	**(10,030)**	(9,569)	(4.8)%	(1.2)%	(461)	(266)	(82)	—	(530)	417
Marketing, Administration and Research Costs [2]	**(8,304)**	(7,384)	(12.5)%	(10.4)%	(920)	(143)	(8)	—	—	(769)
Amortization of Intangibles	**(96)**	(73)	(31.5)%	(5.5)%	(23)	(1)	(18)	—	—	(4)
Operating Income	**$ 12,975**	$ 11,668	11.2 %	8.9 %	$ 1,307	$ 268	$ 1	$ 667	$ 1,008	$ (637)

[1] Cost/Other variance includes a $246 million reduction in net revenues in 2021 related to the Saudi Arabia customs assessments. For more details, see Item 8, Note 17. *Contingencies*.

[2] Cost/Other variance includes charges in 2021 and 2020 of $216 million and $149 million, respectively, for asset impairment and exit costs. Cost/Other variance also includes in 2021 the pre-tax charge of $51 million associated with the asset acquisition cost of OtiTopic, Inc., and in 2020 the Brazil indirect tax credit of $119 million. For more details, see Item 8, Note 6. *Acquisitions, Item 8,* Note 12. *Segment Reporting* and *Item 8,* Note 19. *Asset Impairment and Exit Costs*.

Net revenues, excluding currency and acquisitions, increased by 6.7%, mainly reflecting: favorable volume/mix, primarily driven by higher heated tobacco unit volume (notably in the EU, particularly Germany, Hungary, Italy and Poland, as well as Japan, Russia and Ukraine) and higher device volume (notably in the EU, primarily Italy, and Japan, partly offset by South Korea), partially offset by lower cigarette volume (mainly in the EU Region, notably the Czech Republic, France and Germany, as well as the GCC, North Africa, the Philippines, Russia and Ukraine, partly offset by India, Indonesia, PMI Duty Free and Turkey) and unfavorable cigarette mix (primarily in Germany, Japan and Russia, partially offset by Indonesia and PMI Duty Free); and a favorable pricing variance (notably driven by the Czech Republic, Germany, Japan, Kazakhstan, the Philippines, Russia and Turkey, partly offset by Australia, Indonesia, Poland and Ukraine); partially offset by the unfavorable impact of the Saudi Arabia customs assessments of $246 million, shown in "Cost/Other". Excluding the unfavorable impact of the Saudi Arabia customs assessments of $246 million, net revenues increased by 10.3%, or 7.6% excluding favorable currency of $678 million and acquisitions of $109 million.

The favorable currency in net revenues was due primarily to the Australian dollar, Czech krona, Euro, Indonesian rupiah, Mexican peso and Philippine peso, partially offset by the Russian ruble and Turkish lira.

Net revenues include $9.1 billion in 2021 and $6.8 billion in 2020 related to the sale of RRPs. For the year ended December 31, 2021, *IQOS* devices accounted for over 6% of RRP net revenues, with a step-up in the second half of 2021 reflecting the *IQOS ILUMA* launch; outweighing the effect of supply constraints on other *IQOS* versions.

Operating income, excluding currency and acquisitions, increased by 8.9%, primarily reflecting: favorable volume/mix, mainly driven by higher heated tobacco unit volume, partly offset by lower cigarette volume and unfavorable cigarette mix (each mainly reflecting the same geographies as for net revenues noted above); a favorable pricing variance; and lower manufacturing costs (driven by significant productivity gains related to reduced-risk and combustible products); partly offset by higher marketing, administration and research costs, including an unfavorable comparison related to the Brazil indirect tax credit in 2020, higher asset impairment and exit costs (mainly related to organizational design optimization, as well as product distribution restructuring in South Korea) and asset acquisition costs related to OtiTopic; and the unfavorable impact of the Saudi Arabia customs assessments (as noted above for net revenues).

Interest expense, net, of $628 million increased by $10 million (1.6%).

Our effective tax rate increased by 0.1 percentage point to 21.8%. We estimate that our 2022 effective tax rate will be around 22%, excluding discrete tax events. For further details, see Item 8, Note 11. *Income Taxes*.

Net earnings attributable to PMI of $9.1 billion increased by $1.1 billion or 13.1%. This increase was due primarily to higher operating income as discussed above, partially offset by a higher effective tax rate. Basic and diluted EPS of $5.83 increased by 13.0%. Excluding a favorable currency impact of $0.12, diluted EPS increased by 10.7%.

2020 compared with 2019

For a discussion comparing our consolidated operating results for the year ended December 31, 2020, with the year ended December 31, 2019, refer to Part II, Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operation - Discussion and Analysis - Consolidated Operating Results* in our Annual Report on Form 10-K for the year ended December 31, 2020, which was filed with the U.S. Securities and Exchange Commission on February 9, 2021.

Operating Results by Business Segment

Business Environment

Taxes, Legislation, Regulation and Other Matters Regarding the Manufacture, Marketing, Sale and Use of Tobacco Products

The tobacco industry and our company face a number of challenges that may adversely affect our business, volume, results of operations, cash flows and financial position. These challenges, which are discussed below and in "*Cautionary Factors That May Affect Future Results*," include:

- regulatory restrictions on our products, including restrictions on the packaging, marketing, and sale of tobacco or other nicotine-containing products that could reduce our competitiveness, eliminate our ability to communicate with adult consumers, or even ban certain of our products;
- fiscal challenges, such as excessive excise tax increases and discriminatory tax structures;
- illicit trade in cigarettes and other tobacco and nicotine-containing products, including counterfeit, contraband and so-called "illicit whites";
- intense competition, including from non-tax paid volume by certain local manufacturers;
- pending and threatened litigation as discussed in Item 8, Note 17. *Contingencies*; and
- governmental investigations.

Regulatory Restrictions: The tobacco industry operates in a highly regulated environment. The well-known risks of smoking have led regulators to impose significant restrictions and high excise taxes on cigarettes.

Much of the regulation that shapes the business environment in which we operate is driven by the Framework Convention on Tobacco Control (the "FCTC") of the World Health Organization (the "WHO"), which entered into force in 2005. The FCTC has as its main objective to establish a global agenda for tobacco regulation, with the purpose of reducing tobacco use. To date, 182 countries and the European Union are Parties to the FCTC. The treaty requires Parties to have in place various tobacco control measures and recommends others. The FCTC governing body, the Conference of the Parties ("CoP"), has also adopted non-binding guidelines and policy recommendations related to certain articles of the FCTC that go beyond the text of the treaty. In October 2018, the CoP recognized the need for more scientific assessment and improved reporting to define policy on heated tobacco products. Similar to its previous policy recommendations on e-cigarettes, the CoP invited countries to regulate, restrict or prohibit heated tobacco products, as appropriate under their national laws.

Prior to CoP 9 that took place in November 2021, the WHO and the WHO FCTC Secretariat published two reports on novel and emerging tobacco products. The reports were noted by CoP 9 and related substantive discussions and decisions were deferred to CoP 10, currently scheduled for 2023. It is not possible to predict whether or to what extent measures recommended by the WHO's reports will be implemented as the reports are not binding to the WHO Member States.

We believe that when better alternatives to cigarettes exist, the discussion should not be whether these alternatives should be made available to the more than one billion people who smoke today, but how fast, and within what regulatory framework to maximize their adoption while minimizing unintended use. Therefore, we advocate for regulatory frameworks that recognize a significant difference on a risk continuum between combustible tobacco on the one hand and non-combustible tobacco and other nicotine-containing products on the other. Regulation should include measures that will accelerate switching to non-combustible products, for example, by allowing adult consumers who would not otherwise quit to receive truthful and non-misleading information about such products to

enable them to make informed decisions and by applying uniform product standards to enable manufacturers to demonstrate the safety of these products as well as the absence of combustion. Regulation should also include specific rules for ingredients, labeling and consumer communication, and should ensure that the public is informed about the health risks of all combustible and non-combustible tobacco and nicotine-containing products. Importantly, regulation must include measures designed to prevent initiation by youth and non-smokers. We support mandated health warnings, minimum age laws, restrictions on advertising, and public place smoking restrictions. We also support regulatory measures that help reduce illicit trade.

Certain measures are discussed in more detail below and in the *Reduced-Risk Products (RRPs)* section.

Fiscal Challenges: Excessive and disruptive excise, sales and other tax increases and discriminatory tax structures are expected to continue to have an adverse impact on our profitability, due to lower consumption and consumer down-trading to non-premium, discount, other low-price or low-taxed combustible tobacco products such as fine cut tobacco and illicit cigarettes. In addition, in certain jurisdictions, some of our combustible products are subject to tax structures that discriminate against premium-price products and manufactured cigarettes. We believe that such tax policies undermine public health by encouraging consumers to turn to illicit trade, and ultimately undercut government revenue objectives, disrupt the competitive environment, and encourage criminal activity. Other jurisdictions have imposed, or are seeking to impose, levies or other taxes specifically on tobacco companies, such as taxes on revenues and/or profits.

World Customs Organization Developments: In 2020, the World Customs Organization (the "WCO") amended the harmonized system nomenclature to introduce dedicated custom codes for novel tobacco and nicotine products, including heated tobacco products, e-cigarettes and other nicotine-containing products. The amendments became effective as of January 1, 2022. These amendments require WCO member states to transfer products from customs codes in the current nomenclature to the new one. These amendments are not expected to significantly impact current customs duty rates.

EU Tobacco Products Directive: In April 2014, the EU adopted a significantly revised EU Tobacco Products Directive (the "TPD"), which entered into force in May 2016. All member states have adopted laws transposing the TPD. The TPD sets forth a comprehensive set of regulatory requirements for tobacco products, including:

- health warnings covering 65% of the front and back panels of cigarette packs, with an option for member states to further standardize tobacco packaging, including the introduction of plain packaging;
- a ban on characterizing flavors in some tobacco products, with a transition period for menthol that expired in May 2020;
- security features and tracking and tracing measures that became effective in May 2019; and
- a framework for the regulation of novel tobacco products and e-cigarettes, including requirements for health warnings and information leaflets, a prohibition on product packaging text related to reduced risk, and the introduction of notification requirements or authorization procedures in advance of commercialization.

In May 2021, the European Commission published its first report on the application of the TPD. The report identifies significant progress made due to the implementation of the TPD and where there is still room for improvement. Most notably, it finds that the EU legislation has enhanced tobacco control, contributed to protecting the health of EU citizens by providing Member States with strong rules to address the use of tobacco products in the EU. The TPD reportedly achieved the 2% reduction target of the impact assessment with decreased smoking prevalence among youth. The report also concludes that there is scope for improvement in certain areas, such as enforcement at national level, assessment of ingredients, and a better consideration for novel and emerging products.

In November 2021, the European Commission published the implementation roadmap to Europe's Beating Cancer Plan (the "Plan"). According to the Plan, a revision of the TPD is planned for 2024.

EU Tobacco Excise Directive: The EU Commission is preparing a legislative proposal for the revision of the 2011 EU Tobacco Excise Directive that may include definitions and tax treatment for novel tobacco and nicotine-containing products, including heated tobacco products and e-cigarettes. The proposal is expected to be finalized and adopted by the EU Council in 2023. The adoption of the final proposal by the EU Council will require unanimous agreement by all EU member states.

Plain Packaging and Other Packaging Restrictions: Plain packaging legislation bans the use of branding, logos and colors on packaging other than the brand name and variant that may be printed only in specified locations and in a uniform font. To date, plain packaging laws have been adopted in certain markets in all of our operating segments, including the key markets of Australia, France, Saudi Arabia and Turkey. Some countries, such as Canada, Denmark, Israel and New Zealand adopted plain packaging regulations that apply to all tobacco products, including RRPs. Other countries are also considering plain packaging legislation.

Some countries have adopted, or are considering adopting, packaging restrictions that could have an impact similar to plain packaging. Examples of such restrictions include standardizing the shape and size of packages, prohibiting certain colors or the use of certain descriptive phrases on packaging, and requiring very large graphic health warnings that leave little space for branding.

Restrictions and Bans on the Use of Ingredients: The WHO and others in the public health community have recommended restrictions or total bans on the use of some or all ingredients in tobacco products, including menthol. Broad restrictions and ingredient bans would require us to reformulate our American blend tobacco products and could reduce our ability to differentiate these products in the market in the long term. In many countries, menthol bans would eliminate the entire category of mentholated tobacco products. The European Union banned cigarettes and roll-your-own tobacco products with characterizing flavors. Other tobacco products, including heated tobacco products, are exempted from this flavor ban. The EU Commission is required to withdraw this exemption for a particular product category if it determines that there is a substantial change of circumstances, such as a significant increase of EU-wide sales volumes in such product category. Other countries may follow the EU's approach. Turkey banned menthol as of May 2020. Broader ingredient bans have been adopted by Brazil and Canada.
Bans on Display of Tobacco Products at Retail: In a number of our markets, including, but not limited to, Australia and Russia, governments have banned the display of tobacco products at the point of sale. Other countries are considering similar bans.

Bans and Restrictions on Advertising, Marketing, Promotions and Sponsorships: For many years, the FCTC has called for, and countries have imposed, partial or total bans on tobacco advertising, marketing, promotions and sponsorships, including bans and restrictions on advertising on radio and television, in print and on the Internet. The FCTC's non-binding guidelines recommend that governments prohibit all forms of communication with adult smokers.

Restrictions on Product Design: Some members of the public health community are calling for the further standardization of tobacco products by requiring, for example, that cigarettes have a certain minimum diameter, which would amount to a ban on slim cigarettes, or requiring the use of standardized filter and cigarette paper designs. In addition, at its meeting in November 2016, the CoP adopted non-binding guidelines recommending that countries regulate product design features that increase the attractiveness of tobacco products, such as the diameter of cigarettes and the use of flavor capsules.

Restrictions on Public Smoking and Use of Nicotine-Containing Products in Public: The pace and scope of restrictions on the use of our products have increased significantly in most of our markets. Many countries around the world have adopted, or are likely to adopt, regulations that restrict or ban smoking and use of nicotine-containing products in public and/or work places, restaurants, bars and nightclubs. Some public health groups have called for, and some countries, regional governments and municipalities have adopted or proposed, bans on smoking in outdoor places, as well as bans on smoking in cars (typically, when minors are present) and private homes.

Other Regulatory Issues: Some regulators are considering, or in some cases have adopted, regulatory measures designed to reduce the supply of tobacco products. These include regulations intended to reduce the number of retailers selling tobacco products by, for example, reducing the overall number of tobacco retail licenses available or banning the sale of tobacco products within specified distances of certain public facilities. In addition, South Africa banned the sale of tobacco products, e-cigarettes, and electronic devices that heat tobacco for several months during the COVID-19 pandemic. The ban, which was lifted on August 17, 2020, resulted in a significant increase of illicit trade of tobacco products.

In a limited number of markets, most notably Japan, we are dependent on governmental approvals that may limit our pricing flexibility.

The EU Single-Use Plastics Directive, which will require tobacco manufacturers and importers to cover the costs of public collection systems for tobacco product filters, under Extended Producer Responsibility ("EPR") schemes, entered into force on July 2, 2019. To date, some member states transposed the Directive into national legislation. We expect remaining member states to transpose the EU Single-Use Plastics Directive into national legislation including EPR schemes by January 2023. While we cannot predict the impact of this initiative on our business at this time, we are monitoring developments in this area.

Illicit Trade: Illicit tobacco trade creates a cheap and unregulated supply of tobacco products, undermines efforts to reduce smoking prevalence, especially among youth, damages legitimate businesses and intellectual property rights, stimulates organized crime, increases corruption and reduces government tax revenue. We generally estimate that, excluding China and the U.S., illicit trade may account for as much as 12% of global cigarette consumption; this includes counterfeit, contraband and the persistent problem of "illicit whites," which are cigarettes legally produced in one jurisdiction for the sole purpose of being exported and illegally sold in another jurisdiction where they have no legitimate market. Currently, we estimate that illicit trade in the European Union accounted for approximately 8% of total cigarette consumption in 2021.

A number of jurisdictions are considering actions to prevent illicit trade. In November 2012, the FCTC adopted the Protocol to Eliminate Illicit Trade in Tobacco Products (the "Protocol"), which includes supply chain control measures, such as licensing of manufacturers and distributors, enforcement of these control measures in free trade zones, controls on duty free and Internet channels and the implementation of tracking and tracing technologies. To date, 63 Parties, including the European Union, have ratified it. The Protocol came into force in September 2018. Parties must start implementing its provisions in their national legislation. In November 2021, the second Meeting of the Parties to the Protocol decided, among others, to focus on the implementation of a framework for global information sharing to combat illicit tobacco trade and enable the parties to exchange products' tracking and tracing information in a secure manner. We welcome this decision and expect that other Parties will ratify the Protocol.

We devote substantial resources to help prevent illicit trade in combustible tobacco products and RRPs. For example, we engage with governments, our business partners and other stakeholders to implement effective measures to combat illicit trade and, in some instances, pursue legal remedies to protect our intellectual property rights.

The tracking and tracing regulations for cigarettes and roll-your-own products manufactured or destined for the EU became effective on May 20, 2019. The effective date for other tobacco-containing products, including some of our RRPs such as heated tobacco units, is May 20, 2024. While we expect that this regulation will increase our operating expenses, we do not expect this increase to be significant.

In 2009, our Colombian subsidiaries entered into an Investment and Cooperation Agreement with the national and regional governments of Colombia to promote investment in, and cooperation on, anti-contraband and anti-counterfeit efforts. The agreement provides $200 million in funding over a 20-year period to address issues such as combating illegal cigarette trade and increasing the quality and quantity of locally-grown tobacco.

In May 2016, PMI launched PMI IMPACT, a global initiative that supports third-party projects dedicated to fighting illegal trade and related crimes such as corruption, organized criminal networks and money laundering. The centerpiece of PMI IMPACT is a council of external independent experts in the fields of law, anti-corruption and law enforcement. The experts are responsible for evaluating and approving funding proposals for PMI IMPACT grants. PMI has pledged $100 million to fund projects within PMI IMPACT over three funding rounds.

Reduced-Risk Products (RRPs)

Our Approach to RRPs: We recognize that smoking cigarettes causes serious diseases and that the best way to avoid the harms of smoking is never to start or to quit. Nevertheless, it is predicted that by 2025, the number of smokers will remain largely unchanged from the current estimate of 1.1 billion, despite the considerable efforts to discourage smoking.

Cigarettes burn tobacco, which produces smoke. As a result of the combustion process, the smoker inhales various toxic substances. In contrast, RRPs do not burn tobacco and therefore contain significantly lower levels of harmful and potentially harmful constituents ("HPHCs") than found in cigarette smoke.

For adult smokers who would otherwise continue to smoke, we believe that RRPs, while not risk-free, offer a much better consumer choice. Accordingly, our key strategic priorities are to: (i) to develop and commercialize products that present less risk of harm to adult smokers who switch to those products versus continued smoking; and (ii) educate and convince convince current adult smokers who would otherwise continue to smoke to switch to those products.

We recognize that this transformation from cigarettes to RRPs will take time and that the speed of transformation will depend in part upon factors beyond our control, such as the willingness of governments, regulators and other policy groups to embrace RRPs as a desired alternative to continued cigarette smoking. For as long as a significant number of adult smokers continues to smoke, responsible leadership of the category is critical. We aim to maintain our competitive position in the cigarette market through selective investment. As a leading international cigarette manufacturer, we will continue to accelerate this transformation by using our regulatory and commercial expertise and extensive commercial and distribution infrastructure as an effective platform for the commercialization of our RRPs and communication with adult smokers and trade partners about the benefits of switching to our RRPs.

While seeking to remain competitive in the cigarette market, we are judiciously reallocating resources from cigarettes to RRPs and are streamlining our cigarette portfolio.

We have a range of RRPs in various stages of development, scientific assessment and commercialization. We conduct rigorous scientific assessments of our RRP platforms to substantiate that they reduce exposure to HPHCs and, ultimately, that these products

present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to them versus continued smoking. We draw upon a team of expert scientists and engineers from a broad spectrum of scientific disciplines and our extensive learnings of adult consumer preferences to develop and assess our RRPs. Our efforts are guided by the following key objectives:

- to develop RRPs that adult smokers who would otherwise continue to smoke find to be satisfying alternatives to smoking;
- for those adult smokers, our goal is to offer RRPs with a scientifically substantiated risk-reduction profile that approaches as closely as possible that associated with smoking cessation;
- to substantiate the reduction of risk for the individual adult smoker and the reduction of harm to the population as a whole, based on scientific evidence of the highest standard that is made available for scrutiny and review by external independent scientists and relevant regulatory bodies; and
- to advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs, including the communication of scientifically substantiated information to enable adult smokers to make better consumer choices.

Our RRP Platforms: Our product development is based on the elimination of combustion via tobacco heating and other innovative systems, which we believe are the most promising path to providing a better consumer choice for those who would otherwise continue to smoke. We recognize that no single product will appeal to all adult smokers. Therefore, we are developing a portfolio of products intended to appeal to a variety of distinct adult consumer preferences.

Five PMI-developed or improved RRP platforms are in various stages of development and commercialization readiness:

Platform 1 uses a precisely controlled heating device incorporating our *IQOS HeatControl* technology, into which a specially designed and proprietary tobacco unit is inserted and heated to generate an aerosol. We have conducted a series of clinical studies for this platform, the results of which were included in our submission to the U.S. Food and Drug Administration ("FDA") described below. We completed a 6+6-month exposure response study and shared the results with the FDA in April 2020. The study showed that for the group that switched to our Platform 1 product, the eight clinical risk endpoints that were tested as co-primary endpoints in the first six-month term moved in the same direction as observed for smoking cessation after 12 months of use of this product. In addition, we completed an 18-month combined chronic toxicity and carcinogenicity study in mice, which was on-going at the time of our FDA submission. We shared the results with the FDA in August 2018. In addition to the original version of Platform 1 which relies on a heating technology using a blade, a new version of Platform 1 is now available using induction. All studies referenced above were conducted with the blade version of Platform 1. We believe that there is full comparability between the versions, therefore the data from these studies remain valid.

Platform 2 uses a pressed carbon heat source which, when ignited, generates a nicotine-containing aerosol by heating tobacco. The results of our pharmacokinetic study (that measured the nicotine pharmacokinetic profile as well as subjective effects) and of our five-day reduced exposure study indicate that this platform could be an acceptable substitute for adult smokers who seek an alternative to cigarettes. The reduced exposure study results showed a substantial reduction in relevant biomarkers of exposure to the measured HPHCs in those who switched to Platform 2 compared to those who continued to smoke cigarettes over a five-day period. The sustainability of this reduction as well as changes in clinical risk markers were assessed in a three-month reduced exposure study, which was completed in 2018. We conducted a consumer test of our Platform 2 design in the last quarter of 2021. As a result of the feedback from this consumer test, the design of our current Platform 2 technology has been discontinued. We are assessing alternative designs for this consumer segment.

Platform 3 provides an aerosol of nicotine salt. We have explored two routes for this platform, one with electronics and one without, and conducted nicotine pharmacokinetic studies with both versions. The results of our pharmacokinetic study related to the version without electronics indicate this product's potential as an acceptable alternative to continued cigarette smoking in terms of product satisfaction. In February 2020, we completed a one-month product use and adaptation study in adult smokers for the product variant without electronics. The results of the study indicated that while during the study period, the adult smokers did not fully switch from smoking cigarettes to this Platform 3 product, on average, they used this product on a daily basis and significantly reduced their daily

consumption of cigarettes. We are working on product modifications to enable switching by those adult smokers who are looking for better alternatives to cigarettes.

Platform 4 covers e-vapor products, which are battery-powered devices that produce an aerosol by vaporizing a nicotine-containing liquid solution. In 2020, our e-vapor products comprised devices with the "coil and wick" technology as well as our e-vapor mesh technology designed to ensure the consistency and quality of the generated aerosol compared to the products with the "coil and wick" technology. Recently, we discontinued the commercialization of devices with the "coil and wick" technology. We conducted a nicotine pharmacokinetic study with respect to products with our e-vapor mesh technology in 2017. The results of this

study indicate that these products are an effective means of nicotine delivery while being a satisfying alternative for e-cigarette users. In March 2019, a six-month pre-clinical study in mice evaluating the impact of e-cigarette vapor on the risks of pulmonary and cardiovascular disease compared to cigarette smoke was completed; this study did not pertain to a specific product. The study demonstrated that e-cigarette vapors induce significantly lower biological responses associated with cardiovascular and pulmonary diseases compared with cigarette smoke. Recently, we designed a new consumable for our e-vapor mesh technology to deliver real tobacco taste satisfaction in an E-Vapor product liquid-using patented technology, where flavors and nicotine are extracted directly from the tobacco leaves and captured in a liquid solution, without having to add flavoring ingredients. This consumable has been commercialized in one market in December 2021.

Platform 5 covers Modern Oral Nicotine Pouches, which consist of white pre-portioned pouches containing nicotine derived from tobacco. Users place a pouch between the upper lip and gum and leave it there while the nicotine and taste are being released. At the end of the use, the user can dispose of the pouch. Nicotine pouches are inherently smoke-free as they are consumed orally, and no combustion process occurs during use. Our nicotine pouches do not contain tobacco. Instead, they contain primarily nicotine, flavors, and a cellulose substrate. The nicotine used in the pouches is of pharmaceutical-grade like the nicotine used in medicinal products, such as gums and inhalers, while the flavors are approved for use in food in accordance with the product quality standards for nicotine pouches developed by the Swedish Institute for Standards. In 2021, PMI acquired AG Snus as well as Fertin Pharma, two companies manufacturing and/or marketing nicotine pouches.

We aim to expand our brand portfolio and market positions with additional RRPs. In addition, we are continuing to use our expertise, technology and capabilities to explore new growth opportunities beyond our current business, including products that do not contain nicotine or tobacco.

After we receive the results of our scientific studies, including those mentioned above, in accordance with standard scientific practices, we share the conclusions in scientific forums and submit them for inclusion in peer-reviewed publications.

The research and development expense for our smoke-free portfolio accounted for 99%, 99% and 98% of our total research and development expense for the years ended December 31, 2021, 2020 and 2019, respectively. The research and development expense for the years ended December 31, 2021, 2020 and 2019, is set forth in Item 8, Note 14. *Additional Information* to the consolidated financial statements.

Commercialization of RRPs: We are building a new product category and tailor our commercialization strategy to the characteristics of each specific market. We focus our commercialization efforts on consumer retail experience, guided consumer trials and customer care, and increasingly, digital communication programs and e-commerce. In order to accelerate switching to our Platform 1 products, our initial market introductions typically entail one-to-one consumer engagement (in person or by digital means) and device discounts. These initial commercialization efforts require substantial investment, which we believe will moderate over time and further benefit from the increased use of digital engagement capabilities. During the COVID-19 pandemic, we accelerated our investments in, and pivot to, digital consumer engagement.

As of December 31, 2021, PMI's smoke-free products are available for sale in 71 markets in key cities or nationwide.

In 2014, we introduced our Platform 1 product in pilot city launches in Nagoya, Japan, and in Milan, Italy. Since then, we have continuously expanded our commercialization activities.

We believe that only a very small percentage of adult smokers who convert to our Platform 1 product switch back to cigarettes.

We have integrated the production of our heated tobacco units into a number of our existing manufacturing facilities, are progressing with our plans to build manufacturing capacity for our other RRP platforms, and continue to optimize our manufacturing infrastructure.

An adequate supply chain for our RRP portfolio, including the supply of electronic devices, is important to our business. We work with four electronics manufacturing service providers for the supply of our Platform 1 and Platform 4 devices, and a small number of other providers for other products in our RRP portfolio and related

accessories. Due to the COVID-19 pandemic, the operations of our two main electronic manufacturing service providers were temporarily suspended at different times. Even though these suspensions did not materially affect our operations, if one or more of these service providers were significantly constrained at the same time, the supply of the devices could be disrupted. Although we work closely with these service providers on monitoring their production capability and financial health, we cannot guarantee that they will remain capable of meeting their commitments, particularly during the COVID-19 pandemic; if they will not, the commercialization of our RRPs could be adversely affected. The production of our RRP portfolio requires various metals, and we believe that there is an adequate supply of such metals in the world markets to satisfy our

current and anticipated production requirements. However, some components and materials necessary for the production of our RRPs, including those for the electronic devices, are obtained from single or limited sources, and can be subject to industry-wide shortages and price fluctuations. While we were successful in maintaining adequate supply of such components and materials so far, we may not be able to secure such supply going forward, particularly during the COVID-19 pandemic; this could negatively impact the commercialization of our RRPs.

In addition, we are also exposed to a world-wide shortage of semiconductors, which continues to put constraints on our device supplies for RRPs. We believe, however, that the overall impact of this shortage remains manageable, and we have adjusted our device assortments to limit the effect on consumer availability of our RRPs.

We discuss product warranties in more detail in Item 8, Note 5. *Product Warranty*. The significance of warranty claims is dependent on a number of factors, including device version mix, product failure rates, logistics and service delivery costs, and warranty policies, and may increase with the number of devices sold.

Product quality may affect consumer acceptance of our RRPs.

Our near-term planned commercialization efforts for the other PMI-developed RRP platforms are as follows:

- We started commercializing an improved version of our *IQOS MESH* product in Canada, Corsica, Croatia, the Czech Republic, Finland, Italy, Ukraine and New Zealand under the *IQOS VEEV* or *VEEV* brand names. We currently plan to launch this product in additional markets.

- With respect to *TEEPS*, our Platform 2 product, we finalized our improvements to this product and conducted a consumer test in the last quarter of 2021. As a result of the feedback from this consumer test, the design of our current Platform 2 technology has been discontinued. We are assessing alternative designs for this consumer segment.

- Following the consumer test conducted in 2020, and the results of the product use and adaptation study described above, we are incorporating our learnings into our plans to improve our Platform 3 product.

- We launched a Platform 5 product in Sweden in January 2022, that is a reformulated version of the already commercialized nicotine pouches bearing the *Shiro* brand by our newly acquired affiliate AG Snus.

Due to the COVID-19 pandemic, certain of these commercialization efforts could be delayed.

RRP Regulation and Taxation: RRPs contain nicotine and are not risk-free. As we describe in more detail above, we support science-based regulation and taxation of RRPs, and believe that regulation and taxation should differentiate between cigarettes and products that present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to these products versus continued smoking and should recognize a continuum of risk for tobacco and other nicotine-containing products. Regulation, as well as industry practices, should reflect the fact that youth should not consume nicotine in any form.

Some governments have banned or are seeking to ban or severely restrict emerging tobacco and nicotine-containing products such as our RRPs and communication of truthful and non-misleading information about such products.

These regulations might foreclose or unreasonably restrict adult consumer access even to products that might be shown to be a better consumer choice than continuing to smoke. During the COVID-19 pandemic, some governments have been and may continue to be temporarily unable to focus on the development of science-based regulatory frameworks for the development and commercialization of RRPs or on the enforcement or implementation of regulations that are significant to our business.

We oppose blanket bans and unreasonable restrictions of products that have the potential to present less risk of harm compared to continued smoking. By contrast, we support regulation that sets clear standards for all RRP categories and propels innovation to benefit adult smokers who would otherwise continue to smoke.

In the United States, an established regulatory framework for assessing “Modified Risk Tobacco Products” and “New Tobacco Products” exists under the jurisdiction of the FDA. We submitted to the FDA a Modified Risk Tobacco

Product Application (“MRTPA”) for our Platform 1 product in December 2016, and a Premarket Tobacco Product Application (“PMTA”) for our Platform 1 product in March 2017.

On April 30, 2019, the FDA determined that a version of our Platform 1 product, namely, *IQOS* 2.4 and three related consumables, is appropriate for the protection of public health and authorized it for sale in the United States. The FDA's decision followed its comprehensive assessment of our PMTA. On December 7, 2020, the FDA reached the same determination for the *IQOS 3* device and authorized that version of our Platform 1 product for sale in the United States.

On July 7, 2020, the FDA determined that the available scientific evidence demonstrates that the issuance of an exposure modification order would be appropriate for the promotion of public health and authorized the marketing of a version of our Platform 1 product, namely *IQOS* 2.4 and three related consumables, as a "modified risk tobacco product." The FDA authorized the marketing of this product in the U.S. with the following information:

"AVAILABLE EVIDENCE TO DATE:

- the *IQOS* system heats tobacco but does not burn it.
- this significantly reduces the production of harmful and potentially harmful chemicals.
- scientific studies have shown that switching completely from conventional cigarettes to the *IQOS* system significantly reduces your body's exposure to harmful or potentially harmful chemicals."

We must request and receive authorization from the FDA in order to continue marketing this product with the same modified exposure information after the present order expires in four years from the date of the orders.

On March 18, 2021, we submitted to the FDA a supplemental MRTPA ("sMRTPA") for *IQOS* 3 requesting authorization to market this version of the device as a Modified Risk Tobacco Product with reduced exposure information like *IQOS* 2.4. In June 2021, the FDA formally accepted and filed our sMRTPA for substantive scientific review and, already in May 2021, the FDA opened the period for the public to provide comments on our application. The public comment period, which was initially scheduled to be closed on August 2, 2021, was extended on July 20, 2021 to provide time for the public to review application materials that were not previously posted by FDA. The FDA closed the comment period for *IQOS 3*'s sMRTPA on December 10, 2021.

There are two types of MRTP orders the FDA may issue: a "risk modification" order or an "exposure modification" order. We had requested both types of orders for *IQOS* 2.4 and an initial selection of 3 consumables' variants. After review, the FDA determined that the evidence did not support issuing a "risk modification" order at this time but that it did support issuing an "exposure modification" order for the product. This determination included a finding that issuance of the exposure modification order is expected to benefit the health of the population as a whole.

We look forward to working with the FDA to provide any additional information they may require in order to market this product with reduced risk claims.

The FDA's PMTA and MRTP orders do not mean that the agency "approved" our Platform 1 product. These authorizations are subject to strict marketing, reporting and other requirements, and are not a guarantee that the product will remain authorized, particularly if there is a significant uptake in youth or non-smoker initiation. The FDA will monitor the marketing of the product.

Some states and municipalities in the U.S. have introduced severe restrictions for the sale of certain e-cigarettes and tobacco products, including those authorized by the FDA. We believe that such restrictions on FDA-authorized products will not advance public health and will unreasonably limit adult consumer access to products that are shown to be a better alternative to continued smoking.

In March 2020, we requested a clarification from the FDA regarding the applicability of its new health warning requirements to our heated tobacco units sold in the United States. In June 2021, the FDA responded to our letter and requested additional information regarding the applicability of the cigarette health warnings rule to the *IQOS* System and *HeatSticks*. Philip Morris Products S.A. is committed to providing adult consumers of tobacco products with complete, accurate and non-misleading information regarding the health risks associated with the use of the *IQOS* System and *HeatSticks*. We shared our views with the FDA on the applicability of new health warnings to our products in our submission on December 2, 2021.

In the U.S., tobacco and nicotine-containing products that were not commercially marketed as of February 15, 2007, are subject to review and authorization by the FDA. Manufacturers of all non-authorized products currently on the market were required to file a PMTA with the FDA by September 9, 2020. The FDA announced on September 9, 2020 that it will prioritize enforcement against any tobacco and nicotine-containing product sold without a PMTA. On October 5, 2021, FDA published its final PMTA rule in the Federal Register, which is effective November 4, 2021. All future applications will have to comply with the requirements in the PMTA rule, which is substantially similar to the version of the final PMTA rule which was posted on Advanced Federal Register on January 19, 2021.

FDA actions may influence the regulatory approach of other governments.

On September 29, 2021, the International Trade Commission ("ITC") issued its Final Determination ("FD"), Limited Exclusion Order ("LEO") and Cease and Desist Order ("CDO"). The ITC upheld the finding of infringement in the ID and found a subsequent violation. The ITC issued a LEO prohibiting the importation of infringing tobacco heating articles and components thereof and cease and desist orders against Philip Morris USA, Inc. and Altria Client Services, LLC, which went into effect at the end of the 60-day Presidential review period on November 28, 2021. We have appealed the patent issues. Furthermore, lawsuits based on the same patent families have been repeatedly and universally rejected in European courts and the European Patent Office. The decision has no bearing outside the United States.

Until recently, there were no countries with specific product standards for heat-not-burn products. Currently, national standards setting minimum quality and safety requirements for such products have been adopted in several countries with technical heat-not-burn specifications and/or methods for demonstrating the absence of combustion. They are mandatory in Egypt, Jordan, Saudi Arabia, Tunisia, the UAE, Uzbekistan and Bahrain, and voluntary in Armenia, Costa Rica, Indonesia, Kazakhstan, Kyrgyzstan, Russia, Tajikistan, Vietnam, the U.K. and Ukraine. In Japan, a voluntary standard sets minimum safety requirements for tobacco heating devices. We expect other governments to consider similar product standards and encourage making them mandatory.

All EU member states have transposed the EU Tobacco Products Directive, including the provisions on novel tobacco products, such as heated tobacco units, and e-cigarettes. Most of the EU member states require a notification submitted six months before the intended placing on the market of such products, while some require pre-market authorizations for the introduction of such products. To date, we have filed a comprehensive dossier summarizing our scientific assessment of our Platform 1 product in over 20 member states.

In addition, in Italy, in April 2018, we submitted an application for *HEETS*, used with the *IQOS* device, requesting regulatory recognition of the reduction of toxic substances and potential risk reduction resulting from switching to this product compared to continued cigarette smoking. In January 2019, our application was not granted primarily on the grounds of insufficient data and questions of methodology. Due to the constraints of the review process, we had been unable to supplement the application with all the data we subsequently filed with the FDA and to address methodological questions during the review. We plan to submit a new application where we will clarify the concerns raised by the decision and further strengthen our application by submitting additional evidence that became available since we submitted our first application, consistent with our FDA filings. We are confident that our evidence supports our application.

On October 31, 2019, our Australian subsidiary, Philip Morris Limited (“PML”), submitted an application to the Scheduling Committee of the Therapeutic Goods Administration of Australia (“TGA”) seeking to exempt heated tobacco products from being prohibited in Australia. In August 2020, the TGA issued its decision denying the application and stating that it did not present compelling evidence to establish a public health benefit from greater access to nicotine in heated tobacco products.

To date, several governmental agencies have published their scientific findings that analyze the harm-reduction potential of certain RRPs versus continuing smoking, including:

In December 2017, at the request of the U.K. Department of Health and Public Health England, the U.K. Committee on Toxicity published its assessment of the risk of heat-not-burn products relative to cigarette smoking. This assessment included analysis of scientific data for two heat-not-burn products, one of which was our Platform 1 product. The assessment concluded that, while still harmful to health, compared with the known risks from cigarettes, heat-not-burn products are probably less harmful. Subsequently, in February 2018, Public Health England published a report stating that the available evidence suggests that heat-not-burn products may be considerably less harmful than cigarettes and more harmful than e-cigarettes.

In May 2018, the German Federal Institute for Risk Assessment (“BfR”) published a study on the Platform 1 aerosol relative to cigarette smoke using the Health Canada Intense Smoking Regimen. BfR found reductions in selected HPHCs in a range of 80-99%. This publication indicates that significant reductions in the levels of selected toxicants

are likely to reduce toxicant exposure, which BfR stated might be regarded as a discrete benefit compared to combustible cigarettes.

In May 2018, the Dutch National Institute for Public Health and Environment ("RIVM") published a factsheet on novel tobacco products that heat rather than burn tobacco, focusing on our Platform 1 product. RIVM analyzed the aerosol generated by our Platform 1 product and concluded that the use of this product, while still harmful to health, is probably less harmful than continued smoking.

In June 2018, the Korean Food and Drug Administration ("KFDA") issued a statement on products that heat rather than burn tobacco. The KFDA tested three heat-not-burn products, one of which was our Platform 1 product. The KFDA confirmed that the levels of the nine HPHCs tested in the aerosol of these products were on average approximately 90% lower compared to those measured in the cigarette smoke of the top five cigarette brands in South Korea. However, the KFDA stated that it could not establish that the tested heat-not-burn products are less harmful than cigarettes. In October 2018, our Korean subsidiary filed a request with a local court seeking information underlying KFDA's analysis, conclusions and public statements. In May 2020, the court ordered KFDA to produce certain records.

In August 2018, the Science & Technology Committee of the U.K. House of Commons published a report of its inquiry into e-cigarettes and heat-not-burn products. The report concluded that e-cigarettes are significantly less harmful to health than smoking tobacco. The report also observed that for those smokers who do not accept e-cigarettes, heat-not-burn products may offer a public health benefit despite their relative risk. The report called for a risk-proportionate regulatory environment for both e-cigarettes and heat-not-burn products and noted that e-cigarettes should remain the least taxed, cigarettes the most taxed, with heat-not-burn products falling between the two. The U.K. Committee on Advertising Practice announced the removal of a prohibition of health claims in the advertising of e-cigarettes in the U.K. effective November 2018.

In November 2018, the Eurasian Economic Commission (regulatory body of the Eurasian Union consisting of Armenia, Belarus, Kazakhstan, Kyrgyzstan and Russia) published the results of its commissioned study on novel nicotine-containing products, including our Platform 1 product. The study confirms significantly lower levels of HPHCs in the aerosol generated by this product compared to cigarette smoke.

In January 2019, scientific media published the results of the study of the China National Tobacco Quality Supervision and Test Centre ("CNTQST") comparing the aerosol generated by our Platform 1 product with cigarette smoke. The CNTQST found that the former contained fewer, and lower levels of, harmful constituents than the latter and concluded that the lower temperature of heating tobacco in our Platform 1 product contributed to the difference. The CNTQST stated that the reduction in emissions of harmful constituents cannot be interpreted as a harm/risk reduction for smokers in the same proportion.

In 2020, the Superior Health Council of Belgium ("SHC") published results of its inquiry into heat-not-burn products. The SHC concluded that heat-not-burn products, while not safe, have a more favorable toxicity profile than cigarettes. However, in light of the uncertainty of such products' short and long-term impacts, the toxic effects of the dual use with cigarettes, and the existence of approved smoking cessation tools, the SHC recommended that current regulations for cigarettes should apply to heat-not-burn products.

The foregoing scientific findings of government agencies may not be indicative of the measures that the relevant government authorities could take in regulating our products.

We make our scientific findings publicly available for scrutiny and peer review through several channels, including our websites. From time to time, adult consumers, competitors, members of the scientific community, and others inquire into our scientific methodologies, challenge our scientific conclusions or request further study of certain aspects of our RRPs and their health effects. We are committed to a robust and open scientific debate and believe that such debate should be based on accurate and reliable scientific information. We seek to provide accurate and reliable scientific information about our RRPs; nonetheless, we may not be able to prevent third-party dissemination of false, misleading or unsubstantiated information about these products. The dissemination of scientifically unsubstantiated information or studies with a strong confirmation bias by third parties may cause confusion among adult smokers and affect their decision to switch to better alternatives to continued smoking, such as our RRPs.

To date, we have been largely successful in demonstrating to regulators that our heated tobacco units are not cigarettes due to the absence of combustion, and as such they are generally taxed either as a separate category or as other tobacco products, which typically yields more favorable tax rates than cigarettes. Although we believe that this is sensible from the public health perspective, we cannot guarantee that regulators will continue this approach.

There can be no assurance that we will succeed in our efforts to replace cigarettes with RRPs or that regulation will allow us to commercialize RRPs in all markets, to communicate about our RRPs, including making scientifically substantiated risk-reduction claims, or to treat RRPs differently from cigarettes.

Legal Challenges to RRPs: We face various administrative and legal challenges related to certain RRP activities, including allegations concerning product classification, advertising restrictions, corporate communications, product coach activities, scientific substantiation, product liability, and unfair competition. While we design our programs to comply with relevant regulations, we expect these or similar challenges to continue as we expand our efforts to commercialize RRPs and to communicate publicly. The

outcomes of these matters may affect our RRP commercialization and public communication activities and performance in one or more markets.

Our RRP Business Development Initiatives: In December 2013, we established a strategic framework with Altria Group, Inc. ("Altria") setting out terms on how the parties would collaborate to develop and commercialize e-vapor products and commercialize two of our RRPs in the U.S. In late 2018, Altria announced that it will participate in the e-vapor category only through another e-vapor company in which Altria acquired a minority interest. In September 2019, Altria's subsidiary, Philip Morris USA Inc. ("PM USA"), began commercialization of a version of our Platform 1 product in the U.S. Under the agreement, PM USA must achieve certain milestones to maintain its exclusive distribution right and additional milestones to extend the agreement after the initial 5-year term. PMI and Altria are currently discussing these milestones, the contractual obligations, and the impact of the United States International Trade Commission ("ITC") Orders (For more details please refer to Item 8, Note 17. *Contingencies*).

In January 2020, we announced an agreement with KT&G, a leading tobacco and nicotine company in South Korea, for the commercialization of KT&G's smoke-free products outside of South Korea on an exclusive basis. For more information, see *Acquisitions and Other Business Arrangements* below.

Other Developments: In September 2017, we announced our support of the Foundation for a Smoke-Free World. In September 2020, our pledge agreement with the Foundation was amended. We contributed $45 million in 2020, $40 million in 2021, and expect to contribute $35 million annually from 2022 through 2029, as specified in the amended pledge agreement. To date, we contributed a total of $249.5 million. The Foundation is an independent body and is governed by its independent Board of Directors. The Foundation's role, as set out in its corporate charter, includes funding research in the field of tobacco harm reduction, encouraging measures that reduce the harm caused by smoking, and assessing the effect of reduced cigarette consumption on the industry value chain.

Governmental Investigations

From time to time, we are subject to governmental investigations on a range of matters, including tax, customs, antitrust, advertising, and labor practices. We describe certain matters pending in Russia, South Korea and Thailand in Item 8, Note 17. *Contingencies*.

In November 2010, a World Trade Organization ("WTO") panel issued its decision in a dispute relating to facts that arose from August 2006, between the Philippines and Thailand, concerning a series of Thai customs and tax measures affecting cigarettes imported by PM Thailand into Thailand (see Item 8, Note 17. *Contingencies* for additional information). The WTO panel decision, which was upheld by the WTO Appellate Body, concluded that Thailand had no basis to find that PM Thailand's declared customs values and taxes paid were too low, as alleged by the Department of Special Investigations of the government of Thailand ("DSI") in 2009. The decision also created obligations for Thailand to revise its laws, regulations, or practices affecting the customs valuation and tax treatment of future cigarette imports. Thailand agreed in September 2011 to fully comply with the decision by October 2012. The Philippines asserts that to date Thailand has not fully complied with the WTO panel decision and commenced challenges at the WTO Appellate Body. The WTO Appellate Body is not operational, and the appeals by Thailand are suspended indefinitely. In December 2020, the Philippines and Thailand agreed to pursue facilitator-assisted discussions aimed at progressing and resolving outstanding issues. It is not possible to predict any future developments in these proceedings or the outcome of these discussions.

The Public Prosecutor's office of Rome, Italy, notified our Italian subsidiary, Philip Morris Italia S.r.l. ("PM Italia"), as well as three former or current employees and a former external consultant of PM Italia in July 2020 and March 2020, respectively, that it concluded a preliminary investigation against them for alleged contravention of anti-corruption laws and related disruption of trade freedom. The Public Prosecutor alleges that the individuals involved promised certain personal favors to government officials from January to July of 2018 in exchange for favorable treatment for PM Italia, and that PM Italia lacked appropriate organizational controls to prevent the alleged actions by the individuals. At the first trial hearing held on September 22, 2021, BAT filed a civil claim against PM Italia claiming vicarious liability for any wrongdoing of its former or current employees. BAT claims EUR 50 million in damages. The court admitted the claim as a matter of course and issued summons for PM Italia to appear as civil party in the case. The next trial hearing is scheduled for April 8, 2022. PM Italia believes the charges brought against it by the Public Prosecutor are without merit and will defend them vigorously.

Asset Impairment and Exit Costs

We discuss asset impairment and exit costs in Item 8, Note 19. *Asset Impairment and Exit Costs* to our consolidated financial statements.

Acquisitions and Other Business Arrangements

We discuss our 2021 acquisitions in Item 8, Note 6. *Acquisitions* to our consolidated financial statements.

Turkey

On January 5, 2022, we acquired the remaining 25% stake of our holding in Philsa Philip Morris Sabancı Sigara ve Tütüncülük Sanayi ve Ticaret A.Ş. ("PHILSA") and 24.75% stake in Philip Morris SA, Philip Morris Sabancı Pazarlama ve Satış A.Ş. ("PMSA") from our Turkish partners, Sabanci Holding for an acquisition price of $205 million (TRY 2,747 million). This amount was paid on January 5th 2022, but the final acquisition price remains subject to certain predetermined adjustments based on the audited financial results of PHILSA and PMSA for fiscal years 2021 and 2022. As a result of this acquisition, PMI now owns 100% of these Turkish subsidiaries.

Global Collaboration Agreement with KT&G

In January 2020, PMI announced a global collaboration agreement with the leading tobacco and nicotine company in South Korea, KT&G, to commercialize KT&G's smoke-free products outside of the country. The agreement will run for an initial period of three years. The two companies plan for global collaboration with the intention to actively expand to cover many markets, based on commercial success. The agreement allows PMI to distribute current KT&G smoke-free products, and their evolutions, on an exclusive basis, and does not restrict PMI from distributing its own or third-party products. KT&G's smoke-free product brand portfolio includes heat-not-burn tobacco products (e.g., *LIL Mini* and *LIL Plus*), hybrid technologies that combine heat-not-burn tobacco and e-vapor technologies (e.g., *LIL HYBRID*), and e-vapor products (e.g., *LIL Vapor*). PMI will be responsible for the commercialization of smoke-free products supplied under the agreement.

Products sold under the agreement are subject to careful assessment to ensure they meet the regulatory requirements in the markets where they are launched, as well as our standards of quality and scientific substantiation to confirm the absence of combustion and significant reductions of emissions of harmful chemicals compared to cigarettes. PMI and KT&G will seek any necessary regulatory approvals that may be required on a market-by-market basis. There are no current plans to commercialize KT&G products in the United States.

Since the third quarter of 2020, we have launched commercial initiatives for licensed KT&G products in select markets.

Equity Investments

We discuss our equity investments in Item 8, Note 4. *Related Parties - Equity Investments and Other* to our consolidated financial statements.

Trade Policy

We are subject to various trade restrictions imposed by the U.S. and countries in which we do business ("Trade Sanctions"), including the trade and economic sanctions administered by the U.S. Department of the Treasury's Office of Foreign Assets Control and the U.S. Department of State. It is our policy to comply fully with these Trade Sanctions.

Tobacco products are agricultural products under U.S. law and are not technological or strategic in nature. From time to time, we make sales in countries subject to Trade Sanctions, either where such sanctions do not apply to our business or pursuant to exemptions or licenses.

From time to time, a subsidiary sells products to distributors that, in turn, sell those products to duty free customers that supply U.N. peacekeeping forces around the world, including those in the U.N. peacekeeping mission located in Abyei, a special administrative territory in Sudan. We do not believe that these sales, which are not subject to Trade Sanctions, and are *de minimis* in volume and value, present a material risk to our shareholders, our reputation or the value of our shares. We have no employees, operations or assets in Sudan.

We do not sell products in Iran, North Korea and Syria. From time to time, we explore opportunities to sell our products in one or more of these countries, as permitted by law.

We sell cigarettes in Cuba under a distribution agreement. These sales are permitted by U.S. law under a License Exception for Agricultural Commodities, issued by the United States Department of Commerce (Bureau of Industry and Security), granted to our

distributor.

Certain states within the U.S. have enacted legislation permitting or requiring state pension funds to divest or abstain from future investment in stocks of companies that do business with certain countries that are sanctioned by the U.S. Because we do business in certain of these countries, these state pension funds may have divested of our stock or may not invest in our stock. We do not believe such legislation has had a material effect on the price of our shares.

PMI is also subject to various Trade Sanctions imposed by the EU and other jurisdictions ("Trade Sanctions"). We comply fully with these Trade Sanctions.

The EU imposed new sanctions regarding the Republic of Belarus ("Belarus") on June 21, 2021, including the designation of additional EU sanctions targets (individuals and legal entities) in Belarus. On June 24, 2021, the EU council introduced additional sectoral economic sanctions aimed at specific sectors of the Belarus economy, including restrictions on the trade of goods used for the production or manufacture of tobacco products. Subsequently, six non-EU countries (Norway, Iceland, Liechtenstein, North Macedonia, Montenegro, and Albania) announced that they “aligned themselves” with the EU sanctions of June 21. On July 6, 2021, Switzerland imposed sanctions on Belarusian individuals and legal entities effective July 7, 2021. The Swiss sanctions are similar in scope to the EU sanctions of June 21, 2021.

Further, on August 9, 2021, the U.K. introduced sectoral economic sanctions similar in scope to the EU sectoral sanctions of June 24, 2021. Also on August 9, 2021, the U.S. imposed blocking sanctions on certain individuals and entities pursuant to an Executive Order adding them to the list of Specially Designated Nationals and Blocked Persons (the "SDN List") issued by the U.S. Department of Treasury's Office of Foreign Asset Control ("OFAC"). The Executive Order expanded the bases for the imposition of sanctions, including, among others, by authorizing the imposition by OFAC of blocking sanctions on persons operating in the tobacco sector of the Belarus economy, as well as for providing material support or assistance to any SDN. In December 2021, the U.S., the EU, the U.K. and Canada amended their respective sanctions lists by including additional Belarusian individuals, entities, and aircraft.

PMI complies with all applicable laws and regulations, including sanctions, in the markets where it operates. We have taken appropriate actions in response to the latest sanctions to ensure full compliance with the relevant restrictions.

2021 compared with 2020

The following discussion compares operating results within each of our geographical segments and Other category for 2021 with 2020.

Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units. Estimates for total industry volume and market share in certain geographies reflect limitations on the availability and accuracy of industry data.

European Union:

Financial Summary - Years Ended December 31,			**Change Fav./(Unfav.)**		**Variance Fav./(Unfav.)**					
(in millions)	**2021**	**2020**	**Total**	**Excl. Curr. & Acquis.**	**Total**	**Cur-rency**	**Acqui-sitions**	**Price**	**Vol/ Mix**	**Cost/ Other**
Net Revenues	**$ 12,275**	$ 10,702	14.7 %	8.8 %	$ 1,573	$ 618	$ 8	$ 69	$ 878	$ —
Operating Income	**$ 6,119**	$ 5,098	20.0 %	12.5 %	$ 1,021	$ 384	$ 2	$ 69	$ 728	$ (162)

Net revenues, excluding currency and acquisitions, increased by 8.8%, reflecting: favorable volume/mix, mainly driven by higher heated tobacco unit volume (notably in Germany, Hungary, Italy and Poland), as well as higher device volume and favorable device mix (notably in Italy), partly offset by lower cigarette volume (notably in the Czech Republic, France and Germany) and unfavorable cigarette mix (primarily in Germany); and a favorable pricing variance, driven by higher combustible pricing (mainly in Germany and Portugal, partly offset by France and Poland) and higher heated tobacco unit pricing (notably in the Czech Republic and Germany, partially offset by Poland), partly offset by lower device pricing (notably in Germany and Italy).

Operating income, excluding currency and acquisitions, increased by 12.5%, primarily reflecting: favorable volume/mix, mainly driven by higher heated tobacco unit volume and favorable device mix, partly offset by lower cigarette volume and unfavorable cigarette mix (each primarily reflecting the same geographies as for net revenues noted above); lower manufacturing costs (driven by combustible and reduced-risk products); and a favorable pricing variance; partly offset by higher marketing, administration and research costs (due to combustible and reduced-risk products).

European Union - Total Market, PMI Shipment Volume and Market Share Commentaries

Total market and market share performance are shown in the table below:

European Union Key Data	**Full-Year**		
	2021	**2020**	**Change % / pp**
Total Market (billion units)	**478.2**	473.4	1.0 %
PMI Market Share			
Marlboro	**16.6 %**	17.5 %	(0.9)
L&M	**5.6 %**	6.2 %	(0.6)
Chesterfield	**5.4 %**	5.5 %	(0.1)
Philip Morris	**2.2 %**	2.4 %	(0.2)
Heated Tobacco Units	**5.7 %**	4.2 %	1.5
Others	**3.1 %**	3.0 %	0.1
Total European Union	**38.6 %**	38.8 %	(0.2)

The estimated total market in the EU increased by 1.0% to 478.2 billion units, primarily driven by:

- Italy, up by 4.4%, mainly reflecting the impact on adult smoker average daily consumption of the easing of pandemic-related measures; and
- Poland, up by 8.1%, primarily reflecting the impact on adult smoker average daily consumption and border sales of the easing of pandemic-related measures, as well as a lower prevalence of illicit trade;

partly offset by

- Czech Republic, down by 7.3%, mainly reflecting the impact of excise tax-driven price increases; and
- France, down by 6.2%, primarily reflecting the impact of excise tax-driven price increases and higher cross-border (non-domestic) purchases due to the easing of pandemic-related measures.

Our Regional market share decreased by 0.2 points to 38.6%, with declines in the Czech Republic, France and Germany, partly offset by gains in Greece and Italy.

pm-20211231_g5.jpg

Our total shipment volume increased by 1.5% to 186.1 billion units, primarily driven by:

- Italy, up by 11.5%, or by 6.1% excluding the net favorable impact of estimated distributor inventory movements, mainly reflecting the higher total market and a higher market share driven by heated tobacco units; and
- Poland, up by 3.7%, primarily reflecting the higher total market, partially offset by a lower market share due to cigarettes;

partly offset by

- Czech Republic, down by 9.7%, mainly reflecting the lower total market and a lower market share due to cigarettes; and
- France, down by 6.6%, primarily reflecting the lower total market and a lower market share due to cigarettes.

Eastern Europe:

Financial Summary - Years Ended December 31,			**Change Fav./(Unfav.)**		**Variance Fav./(Unfav.)**					
(in millions)	**2021**	**2020**	**Total**	**Excl. Curr. & Acquis.**	**Total**	**Cur-rency**	**Acqui-sitions**	**Price**	**Vol/ Mix**	**Cost/ Other**
Net Revenues	**$ 3,544**	$ 3,378	4.9 %	5.9 %	$ 166	$ (32)	$ —	$ 68	$ 130	$ —
Operating Income	**$ 1,213**	$ 871	39.3 %	38.5 %	$ 342	$ 7	$ —	$ 68	$ 139	$ 128

Net revenues, excluding currency and acquisitions, increased by 5.9%, reflecting: favorable volume/mix, driven by higher heated tobacco unit volume (mainly in Russia and Ukraine), partly offset by lower cigarette volume (primarily in Russia and Ukraine), as well as unfavorable cigarette mix (mainly in Russia); and a favorable pricing variance, primarily driven by higher combustible pricing (mainly in Kazakhstan, Russia and Ukraine), partially offset by lower device pricing (primarily in Russia and Ukraine) and lower heated tobacco unit pricing (mainly in Ukraine, partly offset by Russia).

Operating income, excluding currency and acquisitions, increased by 38.5%, primarily reflecting: favorable volume/mix, mainly driven by higher heated tobacco unit volume, partly offset by lower cigarette volume and unfavorable cigarette mix (all primarily reflecting the same geographies as for net revenues noted above); lower manufacturing costs (mainly related to reduced-risk products, primarily in Russia); a favorable pricing variance; and lower marketing, administration and research costs.

Eastern Europe - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in Eastern Europe decreased by 1.8% to 373.3 billion units, mainly due to:

- Russia, down by 1.0%, or by 2.7% excluding the net favorable impact of estimated trade inventory movements, primarily reflecting the impact of excise tax-driven price increases and a higher prevalence of illicit trade, partly offset by the impact on adult smoker average daily consumption of the easing of pandemic-related measures; and
- Ukraine, down by 9.8%, mainly reflecting the impact of excise tax-driven price increases and a higher prevalence of illicit trade.

Our Regional market share increased by 0.1 point to 30.6%.

pm-20211231_g6.jpg

Our total shipment volume was flat at 114.3 billion units, notably reflecting:

- Southeast Europe, up by 6.9%, primarily reflecting a higher total market and a higher market share (driven by heated tobacco units);

partly offset by

- Belarus, down by 43.9%, mainly reflecting the halt of shipments as of the third quarter due to international sanctions;
- Russia, down by 0.5%, or by 3.0% excluding the net favorable impact of estimated distributor inventory movements, mainly reflecting a lower market share (due to cigarettes, partly offset by heated tobacco units) and the lower total market; and
- Ukraine, down by 3.3%, mainly reflecting the lower total market, partly offset by a higher market share driven by heated tobacco units.

Excluding the net favorable impact of estimated distributor inventory movements, our total in-market sales volume decreased by 1.3%.

Middle East & Africa:

Financial Summary - Years Ended December 31, (in millions)	2021	2020	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr. & Acquis.	Variance Fav./(Unfav.) Total	Cur-rency	Acqui-sitions	Price	Vol/ Mix	Cost/ Other
Net Revenues	**$ 3,293**	$ 3,088	6.6 %	10.4 %	$ 205	$ (115)	$ —	$ 287	$ 320	$ (287)
Operating Income	**$ 1,146**	$ 1,026	11.7 %	23.8 %	$ 120	$ (124)	$ —	$ 287	$ 237	$ (280)

Net revenues, excluding currency and acquisitions, increased by 10.4%, despite the unfavorable impact of the Saudi Arabia customs assessments of $246 million, shown in "Cost/Other". Excluding the unfavorable impact of the Saudi Arabia customs assessments, unfavorable currency and acquisitions, net revenues increased by 18.3%, reflecting: favorable volume/mix, primarily driven by higher cigarette volume (predominantly in PMI Duty Free and Turkey, partly offset by the GCC and North Africa), higher heated tobacco unit volume (mainly in Egypt, Jordan and PMI Duty Free) and favorable cigarette mix (mainly in the GCC, PMI Duty Free and Turkey); and a favorable pricing variance, mainly driven by combustible pricing (primarily in Egypt and Turkey); partially offset by lower fees for certain distribution rights billed to customers in certain markets, shown in "Cost/Other".

Operating income, excluding currency and acquisitions, increased by 23.8%, mainly reflecting: a favorable pricing variance; favorable volume/mix, driven by the same factors and geographies as for net revenues noted above; and lower manufacturing costs (primarily related to combustible products); partly offset by the unfavorable impact of the Saudi Arabia customs assessments, as noted above for net revenues; higher marketing, administration and research costs; and lower fees for certain distribution rights, as noted above for net revenues.

Middle East & Africa - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in the Middle East & Africa increased by 2.9% to 560.5 billion units, mainly driven by:

- Algeria, up by 6.2%, primarily reflecting the impact on adult smoker average daily consumption of the easing of pandemic-related measures, partly offset by the impact of price increases;
- Egypt, up by 8.8%, mainly reflecting a favorable comparison due to pandemic-related supply chain shortages for competitors' products in 2020, as well as the favorable impact of adult smoker in-switching to cigarettes (mainly in the low-tax tier) from other combustible tobacco products;
- South Africa, up by 13.2%, primarily reflecting a favorable comparison versus the second and third quarters of 2020, in which the total market was impacted by the pandemic-related ban on all tobacco sales from March 27th through August 17th, partly offset by a higher estimated prevalence of illicit trade stemming from the ban; and
- Turkey, up by 8.2%, mainly reflecting the impact on adult smoker average daily consumption of the easing of pandemic-related measures, coupled with increased in-bound tourism (particularly by Turkish expatriates), partially offset by a higher estimated prevalence of illicit trade;

partly offset by

- International Duty Free, down by 10.6%, primarily reflecting the impact of government travel restrictions and reduced passenger traffic since the start of the pandemic in March 2020; and
- Tunisia, down by 15.6%, mainly reflecting higher estimated prevalence of illicit trade (primarily due to market disruptions impacting product availability and the impact of price increases in July 2021).

Our Regional market share increased by 1.1 points to 23.1%.

pm-20211231_g7.jpg

Our total shipment volume increased by 9.3% to 130.1 billion units, notably driven by:

- PMI Duty Free, up by 56.9%. Excluding the net favorable impact of estimated distributor inventory movements (principally due to cigarettes), PMI in-market sales volume was up by 4.1%, primarily reflecting a higher market share driven by *Marlboro*, partly offset by the lower total market; and
- Turkey, up by 17.2%, mainly reflecting a higher market share driven by adult smoker up-trading (mainly benefiting *Marlboro* and *Parliament*) and the higher total market;

partly offset by

- Egypt, down by 5.2%, mainly reflecting a lower market share (due primarily to adult smoker down-trading to products in the low-tax tier), partly offset by the higher total market; and
- Kuwait, down by 23.4%, or by 12.3% excluding the net unfavorable impact of estimated distributor inventory movements, primarily reflecting a lower total market.

South & Southeast Asia:

Financial Summary - Years Ended December 31,			**Change Fav./(Unfav.)**		**Variance Fav./(Unfav.)**					
(in millions)	**2021**	**2020**	**Total**	**Excl. Curr. & Acquis.**	**Total**	**Cur-rency**	**Acqui-sitions**	**Price**	**Vol/ Mix**	**Cost/ Other**
Net Revenues	**$ 4,396**	$ 4,396	— %	(2.3)%	$ —	$ 99	$ —	$ (93)	$ (6)	$ —
Operating Income	**$ 1,506**	$ 1,709	(11.9)%	(14.0)%	$ (203)	$ 36	$ —	$ (93)	$ (90)	$ (56)

Net revenues, excluding currency and acquisitions, decreased by 2.3%, primarily reflecting: an unfavorable pricing variance, mainly due to lower pricing for combustible products (primarily in Indonesia, partly offset by the Philippines). Volume/mix was slightly unfavorable, mainly due to lower cigarette volume (primarily in the Philippines, partly offset by India and Indonesia), largely offset by favorable cigarette mix (mainly in Indonesia and the Philippines).

Operating income, excluding currency and acquisitions, decreased by 14.0%, primarily reflecting: an unfavorable pricing variance; unfavorable volume/mix, mainly due to lower cigarette volume (primarily in the Philippines, partly offset by India and Indonesia), partially offset by favorable cigarette mix (mainly in Indonesia and the Philippines); and higher marketing, administration and research costs (mainly in Indonesia and the Philippines).

South & Southeast Asia - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in South & Southeast Asia increased by 7.2% to 722.6 billion units, notably driven by:

- Bangladesh, up by 12.9%, primarily reflecting a favorable comparison versus the prior year, during which pandemic-related restrictions impacted tobacco product availability;
- India, up by 13.6%, mainly reflecting a favorable comparison versus the prior year, during which pandemic-related restrictions impacted the movement of certain products, including tobacco;
- Indonesia, up by 7.2%, primarily reflecting the growth of the tax-advantaged 'below tier one' segment and the impact on adult smoker consumption of the easing of pandemic-related measures;
- Pakistan, up by 17.3%, notably reflecting a lower prevalence of illicit trade (partly due to pandemic-related supply disruptions for illicit products); and
- Vietnam, up by 10.0%, mainly reflecting a lower prevalence of illicit trade due to pandemic-related supply disruptions for illicit products;

partly offset by:

- the Philippines, down by 10.7%, primarily reflecting the impact of industry-wide price increases in the fourth quarter of 2020.

Our Regional market share decreased by 1.7 points to 19.7%.

pm-20211231_g8.jpg

Our total shipment volume decreased by 1.8% to 142.2 billion units, primarily due to:

- the Philippines, down by 17.6%, mainly reflecting the lower total market and a lower market share (predominantly due to mid-price *Fortune*, reflecting the impact of price increases in the fourth quarter of 2020, partly offset by *Marlboro*); and
- Thailand, down by 4.7%, primarily reflecting a lower total market, partly offset by a higher market share driven by *L&M 7.1*;

partly offset by

- India, up by 43.2%, mainly reflecting a higher market share (driven by *Marlboro*) and the higher total market;
- Indonesia, up by 4.3%, primarily reflecting the higher total market, partly offset by a lower market share (mainly due to adult smoker down-trading to the 'below tier one' segment as a result of significantly lower retail prices, partly offset by share growth for PMI's premium and hand-rolled portfolio); and
- Pakistan, up by 10.1%, mainly reflecting the higher total market, partly offset by a lower market share.

East Asia & Australia:

Financial Summary - Years Ended December 31, (in millions)	2021	2020	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr. & Acquis.	Variance Fav./(Unfav.) Total	Currency	Acquisitions	Price	Vol/ Mix	Cost/ Other
Net Revenues	**$ 5,953**	$ 5,429	9.7 %	8.5 %	$ 524	$ 62	$ —	$ 291	$ 171	$ —
Operating Income	**$ 2,556**	$ 2,400	6.5 %	8.7 %	$ 156	$ (53)	$ —	$ 291	$ (2)	$ (80)

Net revenues, excluding currency and acquisitions, increased by 8.5%, reflecting: a favorable pricing variance, primarily driven by higher heated tobacco, combustible and device net pricing in Japan, partly offset by lower combustible pricing in Australia; and favorable volume/mix, mainly driven by higher heated tobacco unit volume and favorable device volume/mix in Japan (driven by the launch of *IQOS ILUMA*), partly offset by unfavorable cigarette mix (mainly in Australia and Japan), lower cigarette volume (primarily in Australia, Japan and South Korea) and unfavorable heated tobacco unit mix in Japan

Operating income, excluding currency acquisitions, increased by 8.7%, mainly reflecting: a favorable pricing variance; and lower manufacturing costs (primarily related to reduced-risk products in Japan and South Korea); partly offset by higher marketing, administration and research costs (notably due to the launch of *IQOS ILUMA* in Japan and higher asset impairment and exit costs, mainly related to product distribution restructuring in South Korea). Volume/mix was slightly unfavorable, primarily reflecting unfavorable cigarette mix (mainly in Australia and Japan), lower cigarette volume (primarily in Australia, Japan and South Korea), as well as unfavorable heated tobacco unit mix and device mix in Japan, largely offset by higher heated tobacco unit volume in Japan.

East Asia & Australia - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in East Asia & Australia, excluding China, decreased by 1.4% to 284.7 billion units, mainly due to:

- Australia, down by 11.3%, primarily reflecting the impact of the ending of the pandemic-related wage subsidy by the government, coupled with the impact of pandemic-related restrictions; and
- Japan, down by 2.4%, mainly reflecting the impact of the October 2020 and 2021 excise tax-driven price increases.

Our Regional market share, excluding China, increased by 0.3 points to 27.5%.

pm-20211231_g9.jpg

Our total shipment volume increased by 3.9% to 82.1 billion units, mainly driven by:

- Japan, up by 8.0%, or by 1.3% excluding the net favorable impact of estimated distributor inventory movements, primarily reflecting a higher market share (driven by heated tobacco units), partly offset by the lower total market;

partly offset by

- South Korea, down by 4.7%, mainly reflecting a lower market share due mainly to *Parliament*.

Excluding the net favorable impact of estimated distributor inventory movements, our total in-market sales volume declined by 0.4%.

Americas:

Financial Summary - Years Ended December 31,			**Change Fav./(Unfav.)**		**Variance Fav./(Unfav.)**					
(in millions)	**2021**	**2020**	**Total**	**Excl. Curr. & Acquis.**	**Total**	**Cur-rency**	**Acqui-sitions**	**Price**	**Vol/ Mix**	**Cost/ Other**
Net Revenues	**$ 1,843**	$ 1,701	8.3 %	5.6 %	$ 142	$ 46	$ —	$ 45	$ 45	$ 6
Operating Income	**$ 487**	$ 564	(13.7)%	(16.8)%	$ (77)	$ 18	$ —	$ 45	$ (4)	$ (136)

Net revenues, excluding currency and acquisitions, increased by 5.6%, mainly reflecting: a favorable pricing variance, driven by higher combustible pricing (mainly in Argentina and Colombia); and favorable volume/mix, primarily driven by higher cigarette volume (mainly in Brazil and Mexico, partly offset by Argentina) and higher device volume, partially offset by unfavorable cigarette mix (primarily in Brazil).

Operating income, excluding currency and acquisitions, decreased by 16.8%, mainly reflecting an unfavorable comparison related to the Brazil indirect tax credit of $119 million in 2020 and higher manufacturing costs (due to reduced-risk and combustible products), partly offset by a favorable pricing variance and lower marketing, administration and research costs. Volume/mix was slightly unfavorable, mainly reflecting unfavorable cigarette mix (notably in Brazil), largely offset by higher cigarette volume (primarily in Brazil and Mexico, partly offset by Argentina).

Americas - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in Americas, excluding the U.S., increased by 2.2% to 193.9 billion units, mainly driven by:

- Argentina, up by 7.4%, primarily reflecting a lower estimated prevalence of illicit trade and a favorable comparison related to retail out-of-stock in the second quarter of 2020 (due to temporary factory shutdowns related to the pandemic), partly offset by the impact of price increases;
- Brazil, up by 3.1%, mainly reflecting a lower estimated prevalence of illicit trade due to reduced price gaps with legal products and the impact of social incentives provided by the government to mitigate the effects of the pandemic; and
- Mexico, up by 4.2%, primarily reflecting the impact on adult smoker average daily consumption of the easing of pandemic-related measures coupled with the impact of increased in-bound tourism;

partly offset by

- Canada, down by 9.3%, notably reflecting the impact of price increases and out-switching from cigarettes to e-vapor products.

Our Regional market share, excluding the U.S., decreased by 0.4 points to 33.4%.

pm-20211231_g10.jpg

Our total shipment volume increased by 1.5% to 65.2 billion units, primarily driven by:

- Brazil, up by 5.2%, mainly reflecting the higher total market and a higher market share driven by *Chesterfield*; and
- Mexico, up by 4.7%, primarily reflecting the higher total market, as well as a higher market share driven by *Marlboro*;

partly offset by

- Argentina, down by 2.9%, mainly reflecting a lower market share (primarily due to adult smoker down-trading to ultra-low-price brands produced by local manufacturers).

Other:

Following the acquisitions of Fertin Pharma A/S, Vectura Group plc. and OtiTopic, Inc., we added the "Other" category in the third quarter of 2021. Business operations for the Other category are managed and evaluated separately from the geographical segments.

Financial Summary - Years Ended December 31, (in millions)	2021	2020	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr. & Acquis.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Currency	Variance Fav./(Unfav.) Acquisitions	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/Mix	Variance Fav./(Unfav.) Cost/Other
Net Revenues	**$ 101**	$ —	— %	— %	$ 101	$ —	$ 101	$ —	$ —	$ —
Operating Income / (Loss)	**$ (52)**	$ —	— %	— %	$ (52)	$ —	$ (1)	$ —	$ —	$ (51)

We recorded net revenues of $101 million in the Other category, with approximately 39% of the total coming from Fertin Pharma's nicotine replacement therapy and nicotine-containing oral products businesses.

The operating loss of $52 million primarily reflected a pre-tax charge of $51 million in the third quarter of 2021 related to the OtiTopic, Inc. transaction. The charge was recorded to research and development costs (within marketing, administration and research costs) and reflected PMI's accounting for the OtiTopic transaction as an asset acquisition, since the in-process research and development of the dry powder inhalation aspirin treatment represented substantially all of the fair value of the gross assets acquired and had no alternative future use. For further details, see Item 8, Note 6. *Acquisitions* and Item 8, Note 12. *Segment Reporting*.

2020 compared with 2019

For a discussion comparing our consolidated operating results within each of our geographical segments for the year ended December 31, 2020, with the year ended December 31, 2019, refer to Part II, Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operation - Operating Results by Business Segment* in our Annual Report on Form 10-K for the year ended December 31, 2020, which was filed with the U.S. Securities and Exchange Commission on February 9, 2021.

Financial Review

pm-20211231_g11.jpgpm-20211231_g12.jpgpm-20211231_g13.jpg

	For the Years Ended Decembe	
(in millions)	**2021**	**2020**
Net cash provided by operating activities	$ 11,967	$ 9,812 $
Net cash used in investing activities	(2,358)	(1,154)
Net cash used in financing activities	(11,977)	(8,496)

2021 compared with 2020

- *Net Cash Provided by Operating Activities*

Net cash provided by operating activities for the year ended December 31, 2021 increased by $2.2 billion compared with 2020. Excluding favorable currency movements of $0.8 billion, net cash provided by operating activities increased by $1.4 billion, due primarily to higher net earnings and lower working capital requirements of $0.5 billion, partially offset by higher pension plan contributions.

The lower working capital requirements in 2021 as compared with 2020 were primarily due to more cash provided by the net impact of both inventories and accrued liabilities and other current assets mainly reflecting COVID-19 pandemic related build-up of inventory levels in our supply chain in 2020, and the timing of excise tax-paid inventory movements and excise tax payments, as well as higher cash provided by accounts payable primarily reflecting higher *IQOS* device purchases in 2021. More cash used in accounts receivable was mainly due to the lower usage of our factoring arrangements to sell trade receivable, partially offset by the Brazil indirect tax credit recovered in 2021. For further details on our factoring arrangements to sell trade receivables and our Brazil indirect tax credit recovered in 2021, see Item 8, Note 18. *Sale of Accounts Receivable* and Item 8, Note 12. *Segment Reporting,* respectively.

- *Net Cash Used in Investing Activities*

Net cash used in investing activities of $2.4 billion for the year ended December 31, 2021, increased by $1.2 billion from the comparable 2020 period. This increase was primarily due to $2.1 billion of cash used in 2021 for our acquisitions, net of acquired cash, partially offset by favorable movements of $1.0 billion in cash collateral exchanged with financial institutions to secure derivatives designated as net investment hedges of Euro assets principally related to changes in exchange rates between the Euro and

the U.S. dollar. For further detail on our 2021 acquisitions and derivatives designated as net investment hedges, see Item 8, Note 6. *Acquisitions* and Item 8, Note 15. *Financial Instruments.*

Our capital expenditures were $0.7 billion in 2021 and $0.6 billion in 2020. The 2021 expenditures were primarily related to our ongoing investments in RRPs. We expect total capital expenditures in 2022 of approximately $1.0 billion (including capital expenditures related to our ongoing investment in RRPs), to be funded by operating cash flows.

- *Net Cash Used in Financing Activities*

Net cash used in financing activities of $12.0 billion for the year ended December 31, 2021, increased by $3.5 billion from the comparable 2020 period. The change was primarily due to the proceeds we received in 2020 from long-term U.S. dollar debt issuances ($3.7 billion), share purchases in 2021 under the new share repurchase program and higher dividend payments, partially offset by lower repayments of long-term debt and lower payments to noncontrolling interests.

Dividends paid in 2021 and 2020 were $7.6 billion and $7.4 billion, respectively.

2020 compared with 2019

For a discussion comparing our net cash activities (operating, investing and financing) for the year ended December 31, 2020, with the year ended December 31, 2019, refer to Part II, Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation - Financial Review in our Annual Report on Form 10-K for the year ended December 31, 2020, which was filed with the U.S. Securities and Exchange Commission on February 9, 2021.

Debt and Liquidity

We define cash and cash equivalents as short-term, highly liquid investments, readily convertible to known amounts of cash that mature within a maximum of three months and have an insignificant risk of change in value due to interest rate or credit risk changes. As a policy, we do not hold any investments in structured or equity-linked products. Our cash and cash equivalents are predominantly held with institutions that have investment-grade long-term credit rating. As part of our cash management strategy and in order to manage counterparty exposure, we also enter into reverse repurchase agreements. Such agreements are collateralized with government or corporate securities held by a custodial bank and, at maturity, cash is paid back to PMI, and the collateral is returned to the bank. For 2021 and 2020, the activities for such reverse repurchase agreements were not material.

In August 2021, we published a business transformation-linked financing framework ("Framework"), which integrates the company's smoke-free transformation into its financing strategy. The Framework outlines the guidelines that we will follow in issuing business transformation-linked financing instruments in the debt capital and loan markets, which may include public notes offerings, private placements, loans, and other relevant financing instruments.

Credit Ratings – The cost and terms of our financing arrangements as well as our access to commercial paper markets may be affected by applicable credit ratings. At February 10, 2022, our credit ratings and outlook by major credit rating agencies were as follows:

	Short-term	Long-ter
Moody's	P-1	A2
Standard & Poor's	A-1	A
Fitch	F1	A

Credit Facilities – On January 28, 2022, we entered into an agreement to amend and extend the term of our $1.8 billion 364-day revolving credit facility from February 1, 2022, to January 31, 2023.

At February 10, 2022, our committed credit facilities were as follows:

(in billions)

Type		Committed Credit Facilities
364-day revolving credit, expiring January 31, 2023	**$**	**1.8**
Multi-year revolving credit, expiring February 10, 2026[(1)]		**2.0**
Multi-year revolving credit, expiring September 29, 2026[(2)]		**2.5**
Total facilities	**$**	**6.3**

[(1)] On January 28, 2022, we entered into an agreement, effective February 10, 2022, to amend and extend the term of our $2.0 billion multi-year revolving credit facility, for an additional year covering the period February 11, 2026 to February 10, 2027, in the amount of $1.9 billion.
[(2)] Includes business transformation-linked pricing adjustments that may result in the reduction or increase in both the interest rate and commitment fee under the credit agreement if PMI achieves, or fails to achieve, certain specified targets based on its business transformation goals.

At February 10, 2022, there were no borrowings under the committed credit facilities, and the entire committed amounts were available for borrowing. Subject to market conditions, PMI currently expects to request a further extension of the terms of its $2.5 billion multi-year revolving credit facility for an additional one-year period, in accordance with and subject to the terms and conditions of the relevant revolving credit facility agreement.

All banks participating in our committed credit facilities have an investment-grade long-term credit rating from the credit rating agencies. We continuously monitor the credit quality of our banking group, and at this time we are not aware of any potential non-performing credit provider.

These facilities do not include any credit rating triggers, material adverse change clauses or any provisions that could require us to post collateral. We expect to continue to meet our covenants.

In addition to the committed credit facilities discussed above, certain of our subsidiaries maintain short-term credit arrangements to meet their respective working capital needs. These credit arrangements, which amounted to approximately $2.3 billion at December 31, 2021 and approximately $2.7 billion at December 31, 2020, are for the sole use of our subsidiaries. Borrowings under these arrangements and other bank loans amounted to $225 million at December 31, 2021, and $244 million at December 31, 2020.

Commercial Paper Program – We continue to have access to liquidity in the commercial paper market through programs in place in the U.S. and in Europe having an aggregate issuance capacity of $8.0 billion. At December 31, 2021, and December 31, 2020, we had no commercial paper outstanding. The average commercial paper balance outstanding during 2021 and 2020 was $1.1 billion and $1.2 billion, respectively.

Sale of Accounts Receivable – To mitigate credit risk and enhance cash and liquidity management, we sell trade receivables to unaffiliated financial institutions. These arrangements allow us to sell, on an ongoing basis, certain trade receivables without recourse. The trade receivables sold are generally short-term in nature and are removed from the consolidated balance sheets. We sell trade receivables under two types of arrangements, servicing and nonservicing.

Our operating cash flows were positively impacted by the amount of the trade receivables sold and derecognized from the consolidated balance sheets, which remained outstanding with the unaffiliated financial institutions. The trade receivables sold that remained outstanding under these arrangements as of December 31, 2021, 2020 and 2019, were $0.9 billion, $1.2 billion and $0.9 billion, respectively. The net proceeds received are included in cash provided by operating activities in the consolidated statements of cash flows.

For further details, see Item 8, Note 18. *Sale of Accounts Receivable* to our consolidated financial statements.

Debt – Our total debt was $27.8 billion at December 31, 2021, and $31.5 billion at December 31, 2020. Our total debt is primarily fixed rate in nature. The weighted-average all-in financing cost of our total debt was 2.4% in 2021 and 2020. For further details,

including the fair value of our debt, see Item 8, Note 7. *Indebtedness*. The amount of debt that we can issue is subject to approval by our Board of Directors.

On February 11, 2020, we filed a shelf registration statement with the U.S. Securities and Exchange Commission, under which we may from time to time sell debt securities and/or warrants to purchase debt securities over a three-year period.

During 2021, we had no public debt issuances.

The weighted-average time to maturity of our long-term debt was approximately 10 years at the end of 2021 and 2020.

Cash Requirements – At December 31, 2021, our material short-term and long-term cash requirements for various contractual obligations and commitments primarily consisted of the following:

- principal payments related to long-term debt and the associated interest payments. For further details, see Item 8, Note 7. *Indebtedness* to our consolidated financial statements;
- accounts payable and accrued liabilities on our consolidated balance sheet (primarily short-term in nature);
- purchase obligations for inventory and production costs to be utilized in the normal course of business such as raw materials, electronic devices, indirect materials and supplies, packaging, co-manufacturing arrangements, storage and distribution, as well as capital expenditures. These purchase obligations are expected to be approximately $2.7 billion in 2022 and approximately $1.6 billion for years beyond;
- operating lease liabilities, on an undiscounted basis, which were included in our consolidated balance sheets. For further details, see Item 8, Note 21. *Leases* to our consolidated financial statements; and
- other long-term liabilities mainly related to transition tax. For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements.

We utilize long-term and short-term debt financing, including a commercial paper program that is regularly used to finance ongoing liquidity requirements, as part of our overall cash management strategy. Our ability to access the capital and credit markets as well as overall dynamics of these markets may impact borrowing costs. We expect that the combination of our long-term and short-term debt financing, the commercial paper program and the committed credit facilities, coupled with our operating cash flows, will enable us to meet our liquidity requirements.

- **Off-Balance Sheet Arrangements**

We have no off-balance sheet arrangements, including special purpose entities, other than guarantees, and cash requirements discussed above.

Guarantees – At December 31, 2021, we have guarantees of our own performance, which are primarily related to excise taxes on the shipment of our products. There is no liability in the consolidated financial statements associated with these guarantees. These guarantees have not had, and are not expected to have, a significant impact on PMI's liquidity. In October 2020, we guaranteed an obligation for an equity method investee. For further details, see Item 8, Note 17. *Contingencies* to our consolidated financial statements.

Equity and Dividends

We discuss our stock awards as of December 31, 2021, in Item 8, Note 9. *Stock Plans* to our consolidated financial statements.

During 2020 and the first six months of 2021, we did not repurchase any shares under a share repurchase program. On June 11, 2021, our Board of Directors authorized a new share repurchase program of up to $7 billion, with target spending of $5 billion to $7 billion over a three-year period. On July 22, 2021, we began repurchasing shares under this new share repurchase program. From July 22, 2021 through December 31, 2021, we repurchased 8.5 million shares of our common stock at a cost of $785 million.

Dividends paid in 2021 were $7.6 billion. During the third quarter of 2021, our Board of Directors approved a 4.2% increase in the quarterly dividend to $1.25 per common share. As a result, the present annualized dividend rate is $5.00 per common share.

Market Risk

Counterparty Risk - We predominantly work with financial institutions with strong short- and long-term credit ratings as assigned by Standard & Poor's and Moody's. These banks are also part of a defined group of relationship banks. Non-investment grade institutions are only used in certain emerging markets to the extent required by local business needs. We have a conservative approach when it comes to choosing financial counterparties and financial instruments. As such we do not invest or hold investments in any structured or equity-linked products. The majority of our cash and cash equivalents is currently invested with maturities of less than 30 days.

We continuously monitor and assess the credit worthiness of all our counterparties.

Derivative Financial Instruments - We operate in markets outside of the United States of America, with manufacturing and sales facilities in various locations throughout the world. Consequently, we use certain financial instruments to manage our foreign currency and interest rate exposure. We use derivative financial instruments principally to reduce our exposure to market risks resulting from fluctuations in foreign exchange and interest rates by creating offsetting exposures. We are not a party to leveraged derivatives and, by policy, do not use derivative financial instruments for speculative purposes.

See Item 8, Note 15. *Financial Instruments* to our consolidated financial statements for further details on our derivative financial instruments and the related collateral arrangements.

Value at Risk - We use a value at risk computation to estimate the potential one-day loss in the fair value of our interest-rate-sensitive and foreign currency price-sensitive derivative financial instruments. This computation includes our debt and foreign currency forwards, swaps and options. Anticipated transactions, foreign currency trade payables and receivables, and net investments in foreign subsidiaries, which the foregoing instruments are intended to hedge, were excluded from the computation.

The computation estimates were made assuming normal market conditions, using a 95% confidence interval and a one-day holding period using a "parametric delta-gamma" approximation technique to determine the observed interrelationships between movements in interest rates and various currencies and in calculating the risk of the underlying positions in the portfolio. These interrelationships were determined by observing interest rate and forward currency rate movements primarily over the preceding quarter for determining value at risk at December 31, 2021 and 2020, and primarily over each of the four preceding quarters for the calculation of average, high and low value at risk amounts during each year.

(in millions)	At December 31, 2021	Fair Value Impact Average	Hig
Instruments sensitive to:			
Foreign currency rates	**$24**	**$36**	**$4**
Interest rates	**$217**	**$200**	**$2**

(in millions)	At December 31, 2020	Fair Value Impact Average	Hig
Instruments sensitive to:			
Foreign currency rates	$59	$78	$1
Interest rates	$180	$445	$1,1

The significant year-over-year decrease in "average" and "high" impact on the value at risk computation above was primarily due to an increase in interest rate and foreign currency volatility during the first quarter of 2020 resulting from the impact of the COVID-19 pandemic.

The value at risk computation is a risk analysis tool designed to statistically estimate the maximum probable daily loss from adverse movements in interest and foreign currency rates under normal market conditions. The computation does not purport to represent actual losses in fair value or earnings to be incurred by us, nor does it consider the effect of favorable changes in market rates. We

cannot predict actual future movements in such market rates and do not present these results to be indicative of future movements in market rates or to be representative of any actual impact that future changes in market rates may have on our future results of operations or financial position.

Contingencies

See Item 3 and Item 8, Note 17. *Contingencies* to our consolidated financial statements for a discussion of contingencies.

Cautionary Factors That May Affect Future Results

Forward-Looking and Cautionary Statements

We may from time to time make written or oral forward-looking statements, including statements contained in filings with the SEC, in reports to stockholders and in press releases and investor webcasts. You can identify these forward-looking statements by use of words such as "strategy," "expects," "continues," "plans," "anticipates," "believes," "will," "aspires," "estimates," "intends," "projects," "aims," "goals," "targets," "forecasts" and other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts.

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Our RRPs constitute a new product category in its early stages that is less predictable than our mature cigarette business. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from those anticipated, estimated or projected. Investors should bear this in mind as they consider forward-looking statements and whether to invest in or remain invested in our securities. In connection with the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995, we are identifying important factors that, individually or in the aggregate, could cause actual results and outcomes to differ materially from those contained in any forward-looking statements made by us; any such statement is qualified by reference to the following cautionary statements. We elaborate on these and other risks we face throughout this document, particularly in Item 1A. *Risk Factors* and *Business Environment* of this section. You should understand that it is not possible to predict or identify all risk factors. Consequently, you should not consider this discussion of potential risks or uncertainties to be complete. We do not undertake to update any forward-looking statement that we may make from time to time, except in the normal course of our public disclosure obligations.

Item 7A. *Quantitative and Qualitative Disclosures About Market Risk.*

The information called for by this Item is included in Item 7, *Market Risk*.

Item 8. *Financial Statements and Supplementary Data.*

Consolidated Statements of Earnings

(in millions of dollars, except per share data)

for the years ended December 31,	2021	2020	2019
Revenues including excise taxes	**$ 82,223**	$ 76,047	$ 77,921
Excise taxes on products	**50,818**	47,353	48,116
Net revenues	**31,405**	28,694	29,805
Cost of sales	**10,030**	9,569	10,513
Gross profit	**21,375**	19,125	19,292
Marketing, administration and research costs (Notes 6, 12, 17, 19 & 20)	**8,304**	7,384	8,695
Amortization of intangibles	**96**	73	66
Operating income	**12,975**	11,668	10,531
Interest expense, net (Note 14)	**628**	618	570
Pension and other employee benefit costs (Note 13)	**115**	97	89
Earnings before income taxes	**12,232**	10,953	9,872
Provision for income taxes (Note 11)	**2,671**	2,377	2,293
Equity investments and securities (income)/loss, net	**(149)**	(16)	(149)
Net earnings	**9,710**	8,592	7,728
Net earnings attributable to noncontrolling interests	**601**	536	543
Net earnings attributable to PMI	**$ 9,109**	$ 8,056	$ 7,185
Per share data (Note 10):			
Basic earnings per share	**$ 5.83**	$ 5.16	$ 4.61
Diluted earnings per share	**$ 5.83**	$ 5.16	$ 4.61

See notes to consolidated financial statements.

Consolidated Statements of Comprehensive Earnings

(in millions of dollars)

for the years ended December 31,	2021	2020	2019
Net earnings	**$ 9,710**	$ 8,592	$ 7,728
Other comprehensive earnings (losses), net of income taxes:			
Change in currency translation adjustments:			
Unrealized gains (losses), net of income taxes of $(58) in 2021, $94 in 2020 and $(161) in 2019	**58**	(1,265)	505
(Gains)/losses transferred to earnings - deconsolidation of RBH, net of income taxes of $0 in 2021, 2020 and 2019 (Note 20)	**—**	—	502
Change in net loss and prior service cost:			
Net gains (losses) and prior service costs, net of income taxes of $(210) in 2021, $139 in 2020 and $247 in 2019	**1,055**	(726)	(454)
Amortization of net losses, prior service costs and net transition costs, net of income taxes of $(72) in 2021, $(67) in 2020 and $(69) in 2019	**323**	299	243
(Gains)/losses transferred to earnings - deconsolidation of RBH, net of income taxes of $0 in 2021, $0 in 2020 and $(15) in 2019 (Note 20)	**—**	—	27
Change in fair value of derivatives accounted for as hedges:			
Gains (losses) recognized, net of income taxes of $(20) in 2021, $13 in 2020 and $2 in 2019	**124**	(68)	(18)
(Gains) losses transferred to earnings, net of income taxes of $7 in 2021, $0 in 2020 and $3 in 2019	**(35)**	(20)	(14)
Total other comprehensive earnings (losses)	**1,525**	(1,780)	791
Total comprehensive earnings	**11,235**	6,812	8,519
Less comprehensive earnings attributable to:			
Noncontrolling interests	**522**	574	586
Comprehensive earnings attributable to PMI	**$ 10,713**	$ 6,238	$ 7,933

See notes to consolidated financial statements.

Consolidated Balance Sheets

(in millions of dollars, except share data)

at December 31,	2021	2020
Assets		
Cash and cash equivalents	**$ 4,496**	$ 7,280
Trade receivables (less allowances of $70 in 2021 and $23 in 2020)	**3,123**	2,905
Other receivables (less allowances of $36 in 2021 and $38 in 2020)	**817**	856
Inventories:		
Leaf tobacco	**1,642**	2,063
Other raw materials	**1,652**	1,712
Finished product	**5,426**	5,816
	8,720	9,591
Other current assets	**561**	860
Total current assets	**17,717**	21,492
Property, plant and equipment, at cost:		
Land and land improvements	**565**	590
Buildings and building equipment	**4,293**	4,410
Machinery and equipment	**9,275**	9,460
Construction in progress	**599**	449
	14,732	14,909
Less: accumulated depreciation	**8,564**	8,544
	6,168	6,365
Goodwill (Note 3)	**6,680**	5,964
Other intangible assets, net (Note 3)	**2,818**	2,019
Equity investments (Note 4)	**4,463**	4,798
Deferred income taxes	**895**	1,410
Other assets (less allowances of $21 in 2021 and $22 in 2020)	**2,549**	2,767
Total Assets	**$ 41,290**	$ 44,815

See notes to consolidated financial statements.

at December 31,	2021	2020
Liabilities		
Short-term borrowings (Note 7)	**$ 225**	$ 244
Current portion of long-term debt (Note 7)	**2,798**	3,124
Accounts payable	**3,331**	2,780
Accrued liabilities:		
Marketing and selling	**811**	782
Taxes, except income taxes	**6,324**	6,403
Employment costs	**1,146**	1,189
Dividends payable	**1,958**	1,880
Other	**1,637**	2,122
Income taxes (Note 11)	**1,025**	1,091
Total current liabilities	**19,255**	19,615
Long-term debt (Note 7)	**24,783**	28,168
Deferred income taxes	**726**	684
Employment costs	**2,968**	4,470
Income taxes and other liabilities (Note 11)	**1,766**	2,509
Total liabilities	**49,498**	55,446
Contingencies (Note 17)		
Stockholders' (Deficit) Equity		
Common stock, no par value (2,109,316,331 shares issued in 2021 and 2020)	**—**	—
Additional paid-in capital	**2,225**	2,105
Earnings reinvested in the business	**33,082**	31,638
Accumulated other comprehensive losses	**(9,577)**	(11,181)
	25,730	22,562
Less: cost of repurchased stock (559,146,338 and 551,942,600 shares in 2021 and 2020, respectively)	**35,836**	35,129
Total PMI stockholders' deficit	**(10,106)**	(12,567)
Noncontrolling interests	**1,898**	1,936
Total stockholders' deficit	**(8,208)**	(10,631)
Total Liabilities and Stockholders' (Deficit) Equity	**$ 41,290**	$ 44,815

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(in millions of dollars)

for the years ended December 31,	2021	2020	2019
CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES			
Net earnings	**$ 9,710**	$ 8,592	$ 7,728
Adjustments to reconcile net earnings to operating cash flows:			
Depreciation and amortization	**998**	981	964
Deferred income tax (benefit) provision	**(17)**	(143)	(141)
Asset impairment and exit costs, net of cash paid (Note 19)	**(22)**	(14)	371
Cash effects of changes, net of the effects from acquired companies:			
Receivables, net	**(198)**	26	(331)
Inventories	**549**	(165)	(548)
Accounts payable	**653**	406	451
Accrued liabilities and other current assets	**623**	121	1,108
Income taxes	**(260)**	(260)	75
Pension plan contributions	**(269)**	(102)	(200)
Other	**200**	370	613 [(1)]
Net cash provided by operating activities	**11,967**	9,812	10,090
CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES			
Capital expenditures	**(748)**	(602)	(852)
Acquisitions, net of acquired cash (Note 6)	**(2,111)**	—	—
Equity investments	**(34)**	(47)	(31)
Deconsolidation of RBH (Note 20)	**—**	—	(1,346) [(2)]
Net investment hedges	**466**	(551)	386
Other	**69**	46	32
Net cash used in investing activities	**(2,358)**	(1,154)	(1,811)

See notes to consolidated financial statements.

for the years ended December 31,	2021	2020	2019
CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES			
Short-term borrowing activity by original maturity:			
Net issuances (repayments) - maturities of 90 days or less	**$ —**	$ (70)	$ (364)
Issuances - maturities longer than 90 days	**—**	45	989
Repayments - maturities longer than 90 days	**—**	(45)	(989)
Long-term debt proceeds	**—**	3,713	3,819
Long-term debt repaid	**(3,042)**	(3,999)	(3,998)
Repurchases of common stock	**(775)**	—	—
Dividends paid	**(7,580)**	(7,364)	(7,161)
Payments to noncontrolling interests and Other	**(580)**	(776)	(357)
Net cash used in financing activities	**(11,977)**	(8,496)	(8,061)
Effect of exchange rate changes on cash, cash equivalents and restricted cash	**(417)**	258	27
Cash, cash equivalents and restricted cash[3]:			
Increase (Decrease)	**(2,785)**	420	245
Balance at beginning of year	**7,285**	6,865	6,620
Balance at end of year	**$ 4,500**	$ 7,285	$ 6,865
Cash Paid:			
Interest	**$ 716**	$ 728	$ 800
Income taxes	**$ 2,936**	$ 2,785	$ 2,430

[1] Includes the Loss on Deconsolidation of RBH ($239 million) and the Canadian tobacco litigation-related charge ($194 million) that were included in marketing, administration and research costs in the consolidated statements of earnings for the year ended December 31, 2019. For further details on these charges, see Note 20. *Deconsolidation of RBH*.

[2] Includes deconsolidation of RBH cash and cash equivalents of $1,323 million and restricted cash of $23 million.

[3] The amounts for cash, cash equivalents and restricted cash shown above include restricted cash of $4 million, $5 million and $4 million as of December 31, 2021, 2020 and 2019, respectively, which were included in other current assets in the consolidated balance sheets.

See notes to consolidated financial statements.

Consolidated Statements of Stockholders' (Deficit) Equity

(in millions of dollars, except per share data)

	PMI Stockholders' (Deficit) Equity						
	Common Stock	Additional Paid-in Capital	Earnings Reinvested in the Business	Accumulated Other Comprehensive Losses	Cost of Repurchased Stock	Noncontrolling Interests	Total
Balances, January 1, 2019	$ —	$ 1,939	$ 31,014	$ (10,111)	$ (35,301)	$ 1,720	$ (10,739)
Net earnings			7,185			543	7,728
Other comprehensive earnings (losses), net of income taxes				219		43	262
Issuance of stock awards		79			81		160
Dividends declared ($4.62 per share)			(7,212)				(7,212)
Payments to noncontrolling interests						(378)	(378)
Deconsolidation of RBH (Note 20)				529			529
Other		1				50	51
Balances, December 31, 2019	—	2,019	30,987	(9,363)	(35,220)	1,978	(9,599)
Net earnings			8,056			536	8,592
Other comprehensive earnings (losses), net of income taxes				(1,818)		38	(1,780)
Issuance of stock awards		69			91		160
Dividends declared ($4.74 per share)			(7,405)				(7,405)
Payments to noncontrolling interests						(602)	(602)
Other		17				(14)	3
Balances, December 31, 2020	—	2,105	31,638	(11,181)	(35,129)	1,936	(10,631)
Net earnings			**9,109**			**601**	**9,710**
Other comprehensive earnings (losses), net of income taxes				**1,604**		**(79)**	**1,525**
Issuance of stock awards		**119**			**78**		**197**
Dividends declared ($4.90 per share)			**(7,665)**				**(7,665)**
Payments to noncontrolling interests						**(560)**	**(560)**
Common stock repurchased					**(785)**		**(785)**
Other		**1**					**1**
Balances, December 31, 2021	**$ —**	**$ 2,225**	**$ 33,082**	**$ (9,577)**	**$ (35,836)**	**$ 1,898**	**$ (8,208)**

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements
Note 1.

Background and Basis of Presentation:

Background

Philip Morris International Inc. is a holding company incorporated in Virginia, U.S.A. (also referred to herein as the U.S., the United States or the United States of America), whose subsidiaries and affiliates and their licensees are primarily engaged in the manufacture and sale of cigarettes and reduced-risk products including heat-not-burn, vapor and oral nicotine products, in markets outside of the United States of America. In addition, during 2021, 2020 and 2019, PMI shipped versions of its Platform 1 device and its consumables authorized by the U.S. Food and Drug Administration ("FDA") to Altria Group, Inc., for sale in the United States under license. For further developments related to the sale of these products in the U.S., see Note 17. *Contingencies*. Throughout these financial statements, the term "PMI" refers to Philip Morris International Inc. and its subsidiaries.

Reduced-risk products ("RRPs") is the term PMI uses to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continuing smoking. PMI has a range of RRPs in various stages of development, scientific assessment and commercialization.

"Platform 1" is the term PMI uses to refer to PMI's reduced-risk product that uses a precisely controlled heating device into which a specially designed and proprietary tobacco unit is inserted and heated to generate an aerosol.

Basis of presentation

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities at the dates of the financial statements and the reported amounts of net revenues and expenses during the reporting periods. Significant estimates and assumptions include, among other things: pension and benefit plan assumptions; useful lives and valuation assumptions of goodwill and other intangible assets; valuation assumptions for non-marketable equity securities; marketing programs, and income taxes. Actual results could differ from those estimates.

The consolidated financial statements include PMI, as well as its wholly owned and majority-owned subsidiaries. Investments in which PMI exercises significant influence (generally 20%-50% ownership interest) are accounted for under the equity method of accounting. Investments not accounted for under the equity method of accounting are measured at fair value, if it is readily determinable, with changes in fair value recognized in net income. Investments without readily determinable fair values, non-marketable equity securities, are measured and recorded using a measurement alternative that values the security at cost minus any impairment. All intercompany transactions and balances have been eliminated.

In the third quarter of 2021, the former Latin America & Canada segment was renamed as the Americas segment. Additionally, due to the acquisitions of Fertin Pharma A/S, Vectura Group plc. and OtiTopic, Inc. in the third quarter of 2021, PMI added an Other category. For further details, see Note 6. *Acquisitions* and Note 12. *Segment Reporting*.

As of March 22, 2019, PMI deconsolidated the financial results of its Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH") from PMI's financial statements. For further details, see Note 20. *Deconsolidation of RBH*.

Certain prior years' amounts have been reclassified to conform with the current year's presentation. The changes did not have a material impact on PMI's consolidated financial position, results of operations or cash flows in any of the periods presented.

Note 2.

Summary of Significant Accounting Policies:

Cash and cash equivalents

Cash equivalents include demand deposits with banks and all highly liquid investments with original maturities of three months or less.

Depreciation

Property, plant and equipment are stated at historical cost and depreciated primarily using the straight-line method over the estimated useful lives of the assets. Machinery and equipment are depreciated primarily over periods ranging from 3 to 15 years, and buildings and building improvements primarily over periods up to 40 years.

Employee benefit plans

PMI provides a range of benefits to its employees and retired employees, including pensions, postretirement health care and postemployment benefits (primarily severance). PMI records annual amounts relating to these plans based on calculations specified under U.S. GAAP. PMI recognizes the funded status of its defined pension and postretirement plans on the consolidated balance sheets. The funded status is measured as the difference between the fair value of the plans assets and the benefit obligation. PMI measures the plan assets and liabilities at the end of the fiscal year. For defined benefit pension plans, the benefit obligation is the projected benefit obligation. For the postretirement health care plans, the benefit obligation is the accumulated postretirement benefit obligation. Any plan with an overfunded status is recognized as an asset, and any plan with an underfunded status is recognized as a liability. Any gains or losses and prior service costs or credits that have not been recognized as a component of net periodic benefit costs are recorded as a component of other comprehensive earnings (losses), net of deferred taxes. PMI elects to recognize actuarial gains/(losses) using the corridor approach.

Fair value measurements

PMI follows ASC 820, *Fair Value Measurements and Disclosures* with respect to assets and liabilities that are measured at fair value. The guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The guidance also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of input that may be used to measure fair value. Level 1 inputs are quoted prices in active markets for identical assets or liabilities. Level 2 inputs include quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 3 are unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

Foreign currency translation

PMI translates the results of operations of its subsidiaries and affiliates using average exchange rates during each period, whereas balance sheet accounts are translated using exchange rates at the end of each period. Currency translation adjustments are recorded as a component of stockholders' (deficit) equity. In addition, some of PMI's subsidiaries have assets and liabilities denominated in currencies other than their functional currencies, and to the extent those are not designated as net investment hedges, these assets and liabilities generate transaction gains and losses when translated into their respective functional currencies.

Goodwill and non-amortizable intangible assets valuation

PMI tests goodwill and non-amortizable intangible assets for impairment annually or more frequently if events occur that would warrant such review. PMI performs its annual impairment analysis in the second quarter of each year. The

impairment analysis involves comparing the fair value of each reporting unit or non-amortizable intangible asset to the carrying value. If the carrying value exceeds the fair value, goodwill or a non-amortizable intangible asset is considered impaired.

Hedging instruments

Derivative financial instruments are recorded at fair value on the consolidated balance sheets as either assets or liabilities. Changes in the fair value of derivatives are recorded each period either in accumulated other comprehensive losses on the consolidated balance sheet or in earnings, depending on whether a derivative is designated and effective as part of a hedge transaction and, if it is, the type of hedge transaction. Gains and losses on derivative instruments reported in accumulated other comprehensive losses are reclassified to the consolidated statements of earnings, into the same line item as the impact of the underlying transaction, in the periods in which operating results are affected by the hedged item. Cash flows from hedging instruments are classified in the same manner as the affected hedged item in the consolidated statements of cash flows.

Impairment of long-lived assets

PMI reviews long-lived assets, including amortizable intangible assets, for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable. PMI performs undiscounted operating cash flow analyses to determine if an impairment exists. For purposes of recognition and measurement of an impairment for assets held for use, PMI groups assets and liabilities at the lowest level for which cash flows are separately identifiable. If an impairment is determined to exist, any related impairment loss is calculated based on fair value. Impairment losses on assets to be disposed of, if any, are based on the estimated proceeds to be received, less costs of disposal.

Impairment of investment in non-marketable equity securities

Non-marketable equity securities are subject to periodic impairment reviews during which PMI considers both qualitative and quantitative factors that may have a significant impact on the investees' fair value. Upon determining that an impairment may exist, the security's fair value is calculated and compared to its carrying value, and an impairment is recognized immediately if the carrying value exceeds the fair value. For further details see Note 20. *Deconsolidation of RBH*.

Impairment of equity method investments

Equity method investments are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of the investments may not be recoverable. An impairment loss would be recorded whenever a decline in value of an equity investment below its carrying amount is determined to be other than temporary. PMI determines whether a loss is other than temporary by considering the length of time and extent to which the fair value of the equity investment has been less than the carrying amount, the financial condition of the equity investment, and the intent to retain the investment for a period of time is sufficient to allow for any anticipated recovery in market value.

Income taxes

Income taxes are provided on all earnings for jurisdictions outside the United States. These provisions, as well as state and local income tax provisions, are determined on a separate company basis, and the related assets and liabilities are recorded in PMI's consolidated balance sheets. Significant judgment is required in determining income tax provisions and in evaluating tax positions. PMI recognizes accrued interest and penalties associated with uncertain tax positions as part of the provision for income taxes on the consolidated statements of earnings. PMI recognizes income taxes associated with Global Intangible Low-Taxed Income ("GILTI") taxes as current period expense rather than including these amounts in the measurement of deferred taxes.

Inventories

Inventories are stated at the lower of cost or market. The first-in, first-out and average cost methods are used to cost substantially all inventories. It is a generally recognized industry practice to classify leaf tobacco inventory as a current asset, although part of such inventory, because of the duration of the aging process, ordinarily would not be utilized within one year.

Leases

PMI determines that a contract contains a lease if the contract conveys a right to control the use of the identified asset for a period of time in exchange for consideration. Operating lease expense is recognized on a straight-line basis over the lease term. Finance lease expense is amortized based on production activity or the lease term. Lease expense is recorded in cost of sales or marketing, administration and research costs depending on the nature of the leased item. At lease commencement, PMI recognizes lease liabilities and the corresponding right-of-use assets (at the present value of future payments) for predominately all of its leases. The recognition of the right-of-use asset and lease liability includes renewal options when it is reasonably certain that they will be exercised. Certain of PMI's leases include payments that are based on changes to an index or on actual usage. These lease payments are adjusted periodically and are included within variable lease costs. PMI accounts for lease and nonlease components as a single-lease component with the exception of its vehicle leases, of which PMI accounts for the lease components separately from the nonlease components. Additionally, leases with an initial term of 12 months or less are not included in the right-of-use asset or lease liability on the consolidated statement of financial position.

Marketing costs

PMI supports its products with advertising, adult consumer engagement and trade promotions. Such programs include, but are not limited to, discounts, rebates, in-store display incentives, e-commerce, mobile and other digital platforms, adult consumer activation and promotion activities, as well as costs associated with adult consumer experience outlets and other adult consumer touchpoints and volume-based incentives. Advertising, as well as certain consumer engagement and trade activities costs, are expensed as incurred. Trade promotions are recorded as a reduction of revenues based on amounts estimated as being due to customers at the end of a period, based principally on historical utilization. For interim reporting purposes, advertising and certain consumer engagement expenses are charged to earnings based on estimated sales and related expenses for the full year.

Revenue recognition

PMI recognizes revenue primarily through the manufacture and sale of cigarettes and reduced-risk products, including heat-not-burn, vapor and oral nicotine products. The majority of PMI revenues are generated by sales through direct and indirect distribution networks with short-term payment conditions and where control is typically transferred to the customer either upon shipment or delivery of goods. PMI evaluates the transfer of control through evidence of the customer's receipt and acceptance, transfer of title, PMI's right to payment for those products and the customer's ability to direct the use of those products upon receipt. Typically, PMI's performance obligations are satisfied and revenue is recognized either upon shipment or delivery of goods.

In certain instances, PMI facilitates shipping and handling activities after control has transferred to the customer. PMI has elected to record all shipping and handling activities as costs to fulfill a contract. The shipping and handling costs that have not been incurred at the time revenue is recognized are accrued. The transaction price is typically based on the amount billed to the customer and includes estimated variable consideration, where applicable. Such variable consideration is typically not constrained and is estimated based on the most likely amount that PMI expects to be entitled to under the terms of the contracts with customers, historical experience of discount or rebate redemption, where relevant, and the terms of any underlying discount or rebate programs, which may change from time to time as the business and product categories evolve. PMI has elected to exclude excise taxes collected from customers from the measurement of the transaction price, thereby presenting revenues net of excise taxes. Estimated costs associated with warranty programs are generally provided for in cost of sales in the period the related revenues are recognized.

Research and Development and Acquired In-Process Research and Development ("IPR&D")

Research and development costs are expensed as incurred.

In a business combination, the fair value of IPR&D acquired is initially capitalized and accounted for as indefinite-lived intangible assets until completion or abandonment of the projects. Upon completion, a determination as to the useful life is performed and the intangible asset is accounted for as a definite-lived intangible asset. Both the indefinite and definite-lived intangible assets are subject to impairment testing annually or more frequently if indicators exist. In an asset acquisition, the initial cost to acquire the IPR&D is expensed in the consolidated statements of earnings when the project has no alternative future use. PMI records these costs within marketing, administration and research costs in its consolidated statements of earnings.

Stock-based compensation

PMI measures compensation cost for all stock-based awards at fair value on date of grant and recognizes the compensation costs over the service periods for awards expected to vest. PMI's accounting policy is to estimate the number of awards expected to be forfeited and adjust the expense when it is no longer probable that the employee will fulfill the service condition. For further details, see Note 9. *Stock Plans*.

Note 3.

Goodwill and Other Intangible Assets, net:

The movements in goodwill were as follows:

(in millions)	European Union	Eastern Europe	Middle East & Africa	South & Southeast Asia	East Asia & Australia	Americas	Other	Total
Balances at January 1, 2020	$ 1,338	$ 300	$ 89	$ 2,898	$ 551	$ 682	$ —	$ 5,858
Changes due to:								
Currency	96	17	(3)	17	8	(29)	—	106
Balances, December 31, 2020	1,434	317	86	2,915	559	653	—	5,964
Changes due to:								
Acquisitions	**30**	**—**	**—**	**—**	**—**	**—**	**968**	**998**
Currency	**(91)**	**(22)**	**(7)**	**(87)**	**(20)**	**(42)**	**(13)**	**(282)**
Balances, December 31, 2021	**$ 1,373**	**$ 295**	**$ 79**	**$ 2,828**	**$ 539**	**$ 611**	**$ 955**	**$ 6,680**

The increase in goodwill in 2021 was due primarily to the preliminary purchase price allocation of PMI's business combinations. For further details on these business combinations, see Note 6. *Acquisitions*.

At December 31, 2021, goodwill primarily reflects PMI's business combinations in Colombia, Greece, Indonesia, Mexico, Pakistan, the Philippines and Serbia, as well as the preliminary purchase price allocation of Fertin Pharma A/S and Vectura Group plc., which were acquired in September 2021.

Details of other intangible assets were as follows:

		December 31, 2021			December 31, 2020		
(in millions)	Weighted-Average Remaining Useful Life	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Non-amortizable intangible assets		**$ 1,312**		**$ 1,312**	$ 1,289		$ 1,289
Amortizable intangible assets:							
Trademarks	**12 years**	**1,201**	**$ 639**	**562**	1,233	$ 594	639
Developed technology, including patents	**12 years**	**859**	**63**	**796**	93	41	52
Other[1]	**12 years**	**238**	**90**	**148**	126	87	39
Total other intangible assets		**$ 3,610**	**$ 792**	**$ 2,818**	$ 2,741	$ 722	$ 2,019

[1] Primarily includes distribution networks and customer relationships.

Non-amortizable intangible assets substantially consist of trademarks from PMI’s acquisitions in Indonesia and Mexico. The increase since December 31, 2020, was due to the preliminary purchase price allocation associated with PMI's business combinations in 2021

(primarily in-process research and development ("IPR&D")) in the amount of $53 million, partially offset by currency movements of ($30 million). For further details, see Note 6. *Acquisitions*.

The increase in the gross carrying amount of amortizable intangible assets from December 31, 2020, was due to the preliminary purchase price allocation associated with PMI's business combinations in 2021 (primarily developed technology and customer relationships) in the amount of $917 million, partially offset by currency movements of ($71 million).

The change in the accumulated amortization from December 31, 2020 was mainly due to the 2021 amortization of $96 million, partially offset by currency movements of ($26 million).

Amortization expense for each of the next five years (including PMI's 2021 acquisitions of Fertin Pharma A/S and Vectura Group plc.) is estimated to be $152 million or less, assuming no additional transactions occur that require the amortization of intangible assets.

During the second quarter of 2021, PMI completed its annual review of goodwill and non-amortizable intangible assets for potential impairment, and no impairment charges were required as a result of this review.

Note 4.

Related Parties - Equity Investments and Other:

Equity Method Investments:

At December 31, 2021 and 2020, PMI had total equity method investments of $879 million and $966 million, respectively. Equity method investments are initially recorded at cost. Under the equity method of accounting, the investment is adjusted for PMI's proportionate share of earnings or losses, dividends, capital contributions, changes in ownership interests and movements in currency translation adjustments. The carrying value of our equity method investments at December 31, 2021 and 2020, exceeded our share of the investees' book value by $764 million and $773 million, respectively. The difference between the investment carrying value and the amount of underlying equity in net assets, excluding $728 million and $745 million attributable to goodwill as of December 31, 2021 and 2020, respectively, which consists primarily of definite-lived intangible assets is being amortized on a straight-line basis. At December 31, 2021 and 2020, PMI received year-to-date dividends from equity method investees of $176 million and $79 million, respectively.

PMI holds a 23% equity interest in Megapolis Distribution BV, the holding company of CJSC TK Megapolis, PMI's distributor in Russia (Eastern Europe segment).

PMI holds a 49% equity interest in United Arab Emirates-based Emirati Investors-TA (FZC) (“EITA”). PMI holds an approximate 25% economic interest in Société des Tabacs Algéro-Emiratie (“STAEM”), an Algerian joint venture that is 51% owned by EITA and 49% by the Algerian state-owned enterprise Management et Développement des Actifs et des Ressources Holding ("MADAR Holding"), which manufactures and distributes under license some of PMI’s brands (Middle East & Africa segment).

The initial investments in Megapolis Distribution BV and EITA were recorded at cost and are included in equity investments on the consolidated balance sheets.

Equity securities:

Following the deconsolidation of RBH on March 22, 2019, PMI recorded the continuing investment in RBH, PMI's wholly owned subsidiary in Canada, at fair value of $3,280 million at the date of deconsolidation, within equity investments. For further details, see Note 20. *Deconsolidation of RBH*. Transactions between PMI and RBH are considered to be related-party transactions from the date of deconsolidation and are included in the tables below.

The fair value of PMI’s other equity securities, which have been classified within Level 1, was $283 million and $256 million for the years ending December 31, 2021 and 2020, respectively. Unrealized pre-tax gains (losses) of $19 million and $(76) million ($15 million and $(60) million net of tax) on these equity securities were recorded in

the consolidated statements of earnings for the years ended December 31, 2021 and 2020, respectively. For a description of the fair value hierarchy and the three levels of inputs used to measure fair values, see Note 2. *Summary of Significant Accounting Policies*.

Other related parties:

United Arab Emirates-based Trans-Emirates Trading and Investments (FZC) ("TTI") holds a 33% non-controlling interest in Philip Morris Misr LLC ("PMM"), an entity incorporated in Egypt which is consolidated in PMI's financial statements in the Middle East & Africa segment. PMM sells, under license, PMI brands in Egypt through an exclusive distribution agreement with a local entity that is also controlled by TTI.

Godfrey Phillips India Ltd ("GPI") is one of the non-controlling interest holders in IPM India, which is a 56.3% owned PMI consolidated subsidiary in the South & Southeast Asia segment. GPI also acts as contract manufacturer and distributor for IPM India. Amounts in the tables below include transactions between these related parties.

Financial activity with the above related parties:

PMI's net revenues and expenses with the above related parties were as follows:

	For the Years Ended December 31,		
(in millions)	**2021**	**2020**	**2019**
Net revenues			
Megapolis Group	**$ 2,207**	$ 2,174	$ 2,236
Other	**1,123**	1,059	1,015
Net revenues [(a)]	**$ 3,330**	$ 3,233	$ 3,251
Expenses:			
Other	**$ 69**	$ 51	$ 63
Expenses	**$ 69**	$ 51	$ 63

[(a)] Net revenues exclude excise taxes and VAT billed to customers.

PMI's balance sheet activity with the above related parties was as follows:

	At December 31,	
(in millions)	**2021**	**2020**
Receivables:		
Megapolis Group	**$ 319**	$ 209
Other	**199**	156
Receivables	**$ 518**	$ 365
Payables:		
Other	**$ 25**	$ 13
Payables	**$ 25**	$ 13

The activities with the above related parties are in the ordinary course of business, and are primarily for distribution, service fees, contract manufacturing and license agreements. PMI eliminated its respective share of all significant intercompany transactions with the equity method investees.

Note 5.

Product Warranty:

PMI's heat-not-burn devices and e-vapor products are subject to standard product warranties generally for a period of 12 months from the date of purchase or such other periods as required by law. PMI generally provides in cost of sales for the estimated cost of warranty in the period the related revenue is recognized. PMI assesses the adequacy of its accrued product warranties and adjusts the amounts as necessary based on actual experience and changes in future estimates. Factors that affect product warranties may vary across markets but typically include device version mix, product failure rates, logistics and service delivery costs, and warranty policies. PMI accounts for its product warranties within other accrued liabilities. At December 31, 2021 and December 31, 2020, these amounts were as follows:

	At Decemb
(in millions)	**2021**
Balance at beginning of period	**$ 137** $
Changes due to:	
Warranties issued	**154**
Settlements	**(177)**
Currency/Other	**(1)**
Balance at end of period	**$ 113** $

Note 6.

Acquisitions:

Business Combinations

AG Snus - On May 6, 2021, PMI acquired 100% of AG Snus Aktieselskab ("AG Snus"), a company based in Denmark, and its Swedish subsidiary Tobacco House of Sweden AB fully owned by AG Snus, which operates in the oral tobacco (i.e. snus) and modern oral (i.e. nicotine pouches) product categories. The purchase price was $28 million in cash, net of cash acquired, with additional contingent payments of up to $10 million, primarily relating to product development and performance targets over a less than two-year period. The operating results of AG Snus are included in the European Union segment, and were not material.

Fertin Pharma – On September 15, 2021, PMI acquired 100% of Fertin Pharma A/S (“Fertin Pharma”), a company based in Denmark. Fertin Pharma is a developer and manufacturer of pharmaceutical and well-being products based on oral and intra-oral delivery systems. The acquisition was funded with existing cash. The total consideration of $821 million (DKK 5.2 billion) included cash of $580 million and the payment of $241 million related to the settlement of Fertin Pharma’s indebtedness. The purchase price of $821 million was preliminarily allocated to cash ($24 million), current assets including receivables and inventories ($69 million), non-current assets including property, plant and equipment ($228 million), goodwill ($378 million), and other intangible assets ($245 million, which primarily consisted of customer relationships, developed technology, and in-process research and development ("IPR&D")), partially offset by current liabilities ($44 million, which primarily consisted of accrued liabilities and accounts payable) and non-current liabilities ($79 million, primarily deferred income tax). Goodwill is primarily attributable to future growth opportunities provided by acquired R&D capabilities and any intangibles that did not qualify for separate recognition. The amortizable intangible assets are being amortized over their estimated useful lives of 8 to 19 years. Subsequent to the acquisition date, PMI made certain measurement period adjustments to the preliminary purchase price allocation, which resulted in an increase to goodwill of $41 million. The increase was primarily due to a decrease in other intangible assets ($82 million), partially offset by a decrease in deferred income tax liabilities ($21 million), and an increase in property, plant and equipment ($19 million). The purchase price allocation is preliminary and continues to be subject to refinement. PMI is evaluating the deductibility of goodwill for income tax purposes. Fertin Pharma's results of operations from the acquisition date through December 31, 2021 were included in PMI's consolidated statements of earnings, and were not material.

Vectura – During the third quarter and up to September 15, 2021, PMI acquired a controlling interest of 74.77% of the total issued shares in Vectura Group plc ("Vectura"), an inhaled therapeutics company based in the United Kingdom. The shares were acquired through a series of open market purchases and acceptances of the tender offer at a price of 165 pence per share. As a result of additional acceptances of the offer and the exercise of the right to acquire compulsorily the Vectura shares, in accordance with the applicable English law, PMI completed the acquisition of 100% of Vectura in the fourth quarter of 2021. The acquisition was funded with existing cash from a designated account operated solely for the purpose of funding this acquisition.

The total purchase price of $1,384 million (GBP 1.0 billion) for 100% of the Vectura shares was preliminarily allocated to cash ($136 million), current assets including receivables and inventories ($89 million), non-current assets including property, plant and equipment ($67 million), goodwill ($590 million), and other intangible assets ($719 million, which primarily consisted of developed technology, and IPR&D), partially offset by current liabilities ($100 million, primarily accrued liabilities), and non-current liabilities ($117 million, primarily deferred income tax). Goodwill is primarily attributable to future growth opportunities provided by acquired R&D capabilities and any intangibles that did not qualify for separate recognition. The amortizable intangible assets are being amortized over their estimated useful lives of 3 to 15 years. Subsequent to the acquisition date, PMI made certain measurement period adjustments to the preliminary purchase price allocation, which resulted in a decrease to goodwill of $115 million. The decrease was primarily due to increase in other intangible assets ($73 million), and a decrease in deferred income tax liabilities ($22 million). The purchase price allocation is preliminary and continues to be subject to refinement. PMI is evaluating the deductibility of goodwill for income tax purposes. Vectura's results of operations from September 15, 2021 through December 31, 2021 were included in PMI's consolidated statements of earnings, and were not material.

Pro forma results of operations for the above business combinations have not been presented as the aggregate impact is not material to PMI's consolidated statements of earnings.

PMI elected to early adopt ASU No. 2021-08 “Business Combinations (Topic 805) Accounting for Contract Assets and Contract Liabilities from Contracts with Customers,” which did not have a material impact on PMI’s consolidated operating results, statement of financial position or cash flows.

Asset Acquisition

On August 9, 2021, PMI acquired 100% of OtiTopic, Inc., a U.S. respiratory drug development company with a late-stage dry powder inhalation aspirin treatment for acute myocardial infarction. The transaction price was $38 million in cash, plus transaction costs, with additional contingent payment of $13 million, primarily related to certain key milestones that PMI deemed probable. Additionally, PMI may owe up to $25 million in future additional contingent payments dependent upon the achievement of certain milestones. PMI accounted for this transaction as an asset acquisition since the IPR&D of the dry powder inhalation aspirin treatment represented substantially all of the fair value of the gross assets acquired. At the date of acquisition, PMI determined that the acquired IPR&D had no alternative future use. As a result, PMI recorded a charge of $51 million to research and development costs within marketing, administration and research costs in the consolidated statements of earnings for the year ended December 31, 2021.

While PMI builds and organizes its future capabilities in wellness and healthcare, Fertin Pharma, Vectura and OtiTopic are considered separate operating segments with their operating results included in the Other category. For additional information see Note 12. *Segment Reporting*.

Note 7.

Indebtedness:

Short-Term Borrowings

At December 31, 2021 and 2020, PMI’s short-term borrowings and related average interest rates consisted of the following:

	December 31, 2021		December 31, 2020	
(in millions)	**Amount Outstanding**	**Average Year-End Rate**	**Amount Outstanding**	**Average Year-End Rate**
Commercial paper	**$ —**	**— %**	$ —	— %
Bank loans	**225**	**12.0**	244	5.3
	$ 225		$ 244	

Given the mix of subsidiaries and their respective local economic environments, the average interest rate for bank loans above can vary significantly from day to day and country to country.

The fair values of PMI's short-term borrowings at December 31, 2021 and 2020, based upon current market interest rates, approximate the amounts disclosed above.

Long-Term Debt

At December 31, 2021 and 2020, PMI's long-term debt consisted of the following:

(in millions)	December 31, 2021	December 31, 2020
U.S. dollar notes, 0.875% to 6.375% (average interest rate 3.245%), due through 2044	**$ 19,397**	$ 21,221
Foreign currency obligations:		
Euro notes, 0.125% to 3.125% (average interest rate 1.995%), due through 2039	**7,687**	9,253
Swiss franc notes, 1.625%, due 2024	**273**	622
Other (average interest rate 3.329%), due through 2029 [(a)]	**224**	196
Carrying value of long-term debt	**27,581**	31,292
Less current portion of long-term debt	**2,798**	3,124
	$ 24,783	$ 28,168

[(a)] Includes mortgage debt in Switzerland as well as $71 million and $37 million in finance leases at December 31, 2021 and 2020, respectively.

The fair value of PMI's outstanding long-term debt, which is utilized solely for disclosure purposes, is determined using quotes and market interest rates currently available to PMI for issuances of debt with similar terms and remaining maturities. At December 31, 2021 and 2020 the fair value of PMI's outstanding long-term debt, excluding the aforementioned finance leases, was as follows:

(in millions)	December 31, 2021	December 31, 2020
Level 1	**$ 29,597**	$ 35,227
Level 2	**165**	177

For a description of the fair value hierarchy and the three levels of inputs used to measure fair values, see Note 2. *Summary of Significant Accounting Policies*.

Debt Issuances Outstanding:

PMI's debt issuances outstanding at December 31, 2021, were as follows:

(in millions)

Type		Face Value	Interest Rate	Issuance	Maturity
U.S. dollar notes		**$500**	**2.625%**	February 2017	February 2022
U.S. dollar notes		**$750**	**2.375%**	August 2017	August 2022
U.S. dollar notes		**$750**	**2.500%**	August 2012	August 2022
U.S. dollar notes		**$750**	**2.500%**	November 2017	November 2022
U.S. dollar notes		**$600**	**2.625%**	March 2013	March 2023
U.S. dollar notes		**$500**	**2.125%**	May 2016	May 2023
U.S. dollar notes		**$750**	**1.125%**	May 2020	May 2023
U.S. dollar notes		**$500**	**3.600%**	November 2013	November 2023
U.S. dollar notes		**$900**	**2.875%**	May 2019	May 2024
U.S. dollar notes		**$750**	**3.250%**	November 2014	November 2024
U.S. dollar notes		**$750**	**1.500%**	May 2020	May 2025
U.S. dollar notes		**$750**	**3.375%**	August 2015	August 2025
U.S. dollar notes		**$750**	**2.750%**	February 2016	February 2026
U.S. dollar notes		**$750**	**0.875%**	November 2020	May 2026
U.S. dollar notes		**$500**	**3.125%**	August 2017	August 2027
U.S. dollar notes		**$500**	**3.125%**	November 2017	March 2028
U.S. dollar notes		**$750**	**3.375%**	May 2019	August 2029
U.S. dollar notes		**$750**	**2.100%**	May 2020	May 2030
U.S. dollar notes		**$750**	**1.750%**	November 2020	November 2030
U.S. dollar notes		**$1,500**	**6.375%**	May 2008	May 2038
U.S. dollar notes		**$750**	**4.375%**	November 2011	November 2041
U.S. dollar notes		**$700**	**4.500%**	March 2012	March 2042
U.S. dollar notes		**$750**	**3.875%**	August 2012	August 2042
U.S. dollar notes		**$850**	**4.125%**	March 2013	March 2043
U.S. dollar notes		**$750**	**4.875%**	November 2013	November 2043
U.S. dollar notes		**$750**	**4.250%**	November 2014	November 2044
U.S. dollar notes	(a)	**$500**	**4.250%**	May 2016	November 2044
EURO notes	(b)	**€600 (approximately $761)**	**2.875%**	May 2012	May 2024
EURO notes	(b)	**€500 (approximately $582)**	**0.625%**	November 2017	November 2024
EURO notes	(b)	**€750 (approximately $972)**	**2.750%**	March 2013	March 2025
EURO notes	(b)	**€1,000 (approximately $1,372)**	**2.875%**	March 2014	March 2026
EURO notes	(b)	**€500 (approximately $557)**	**0.125%**	August 2019	August 2026
EURO notes	(b)	**€500 (approximately $697)**	**2.875%**	May 2014	May 2029
EURO notes	(b)	**€750 (approximately $835)**	**0.800%**	August 2019	August 2031
EURO notes	(b)	**€500 (approximately $648)**	**3.125%**	June 2013	June 2033
EURO notes	(b)	[illegible]	[illegible]	[illegible]	[illegible]

[a] These notes are a further issuance of the 4.250% notes issued by PMI in November 2014.
[b] USD equivalents for foreign currency notes were calculated based on exchange rates on the date of issuance.

The net proceeds from the sale of the securities listed in the table above were used for general corporate purposes, including working capital requirements and repurchase of PMI's common stock.

On January 18, 2022, PMI redeemed all of its outstanding 2.625% U.S. dollar notes due February 18, 2022. As of December 31, 2021, $500 million aggregate principal amount of the U.S. dollar notes were outstanding. The pre-tax loss related to this debt extinguishment, which was not material, will be included in Interest expense, net on PMI's condensed consolidated statements of earnings for the three months ended March 31, 2022.

Aggregate maturities:

Aggregate maturities of long-term debt are as follows:

(in millions)

2022	$	2,798
2023		2,371
2024		3,318
2025		2,351
2026		3,199
2027-2031		4,666
2032-2036		1,132
Thereafter		7,965
		27,800
Debt discounts		(219)
Total long-term debt	$	27,581

Credit Facilities

At December 31, 2021, PMI's total committed credit facilities were as follows:

Type (in billions)		**Committed Credit Facilities**
364-day revolving credit, expiring February 1, 2022	**$**	**1.8**
Multi-year revolving credit, expiring February 10, 2026		**2.0**
Multi-year revolving credit, expiring September 29, 2026[1]		**2.5**
Total facilities	**$**	**6.3**

[1] Includes pricing adjustments that may result in the reduction or increase in both the interest rate and commitment fee under the credit agreement if PMI achieves, or fails to achieve, certain specified targets.

At December 31, 2021, there were no borrowings under these committed credit facilities, and the entire committed amounts were available for borrowing.

These facilities do not include any credit rating triggers, material adverse change clauses or any provisions that could require PMI to post collateral.

On January 28, 2022, PMI entered into an agreement to amend and extend the term of its $1.8 billion 364-day revolving credit facility from February 1, 2022, to January 31, 2023. On January 28, 2022, PMI also entered into an agreement, effective February 10, 2022, to amend and extend the term of its $2.0 billion multi-year revolving credit facility, for an additional year covering the period February 11, 2026 to February 10, 2027, in the amount of $1.9 billion.

In addition to the committed credit facilities discussed above, certain subsidiaries maintain short-term credit arrangements to meet their respective working capital needs. These credit arrangements, which amounted to approximately $2.3 billion at December 31,

2021, and approximately $2.7 billion at December 31, 2020, are for the sole use of the subsidiaries. Borrowings under these arrangements and other bank loans amounted to $225 million at December 31, 2021, and $244 million at December 31, 2020.

Note 8.

Capital Stock:

Shares of authorized common stock are 6.0 billion; issued, repurchased and outstanding shares were as follows:

	Shares Issued	Shares Repurchased	Shares Outstanding
Balances, January 1, 2019	2,109,316,331	(554,736,610)	1,554,579,721
Issuance of stock awards		1,314,942	1,314,942
Balances, December 31, 2019	2,109,316,331	(553,421,668)	1,555,894,663
Issuance of stock awards		1,479,068	1,479,068
Balances, December 31, 2020	2,109,316,331	(551,942,600)	1,557,373,731
Repurchase of shares		**(8,514,629)**	**(8,514,629)**
Issuance of stock awards		**1,310,891**	**1,310,891**
Balances, December 31, 2021	**2,109,316,331**	**(559,146,338)**	**1,550,169,993**

On June 11, 2021, PMI's Board of Directors authorized a new share repurchase program of up to $7 billion, with target spending of $5 billion to $7 billion over a three-year period. On July 22, 2021, PMI began repurchasing shares under this new share repurchase program. From July 22, 2021 through December 31, 2021, PMI repurchased 8.5 million shares of its common stock at a cost of $785 million.

At December 31, 2021, 23,461,358 shares of common stock were reserved for stock awards under PMI's stock plans, and 250 million shares of preferred stock, without par value, were authorized but unissued. PMI currently has no plans to issue any shares of preferred stock.

Note 9.

Stock Plans:

In May 2017, PMI's shareholders approved the Philip Morris International Inc. 2017 Performance Incentive Plan (the "2017 Plan"). Under the 2017 Plan, PMI may grant to eligible employees restricted shares and restricted share units, performance-based cash incentive awards and performance-based equity awards. Up to 25 million shares of PMI's common stock may be issued under the 2017 Plan. At December 31, 2021, shares available for grant under the 2017 Plan were 14,832,141.

In May 2017, PMI's shareholders also approved the Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors (the "2017 Non-Employee Directors Plan"). A non-employee director is defined as a member of the PMI Board of Directors who is not a full-time employee of PMI or of any corporation in which PMI owns, directly or indirectly, stock possessing at least 50% of the total combined voting power of all classes of stock entitled to vote in the election of directors in such corporation. Up to 1 million shares of PMI common stock may be awarded under the 2017 Non-Employee Directors Plan. At December 31, 2021, shares available for grant under the plan were 914,413.

Restricted share unit (RSU) awards

PMI may grant RSU awards to eligible employees; recipients may not sell, assign, pledge or otherwise encumber such awards. Such awards are subject to forfeiture if certain employment conditions are not met. RSU awards

generally vest on the third anniversary of the grant date. RSU awards do not carry voting rights, although they do earn dividend equivalents.

During 2021, the activity for RSU awards was as follows:

	Number of Shares	A Da
Balance at January 1, 2021	**4,098,240**	**$**
Granted	**2,020,860**	
Vested	**(1,256,441)**	
Forfeited	**(221,895)**	
Balance at December 31, 2021	**4,640,764**	**$**

During the years ended December 31, 2021, 2020 and 2019, the grant date fair value of the RSU awards granted to PMI employees and the recorded compensation expense related to RSU awards were as follows:

(in millions, except per RSU award granted)	Total Grant Date Fair Value of RSU Awards Granted	Weighted-Average Grant Date Fair Value Per RSU Award Granted	Compensation Expense related to RSU Awards
2021	**$ 166**	**$ 82.17**	**$ 139**
2020	$ 148	$ 85.79	$ 129
2019	$ 133	$ 77.28	$ 118

The fair value of the RSU awards at the date of grant is amortized to expense over the restriction period, typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2021, PMI had $144 million of total unrecognized compensation costs related to non-vested RSU awards. These costs are expected to be recognized over a weighted-average period of approximately seventeen months, or upon death, disability or reaching the age of 58.

During the years ended December 31, 2021, 2020 and 2019, share and fair value information for PMI RSU awards that vested were as follows:

(dollars in millions)	Shares of RSU Awards that Vested	Grant Date Fair Value of Vested Shares of RSU Awards	Total Fair Value of RSU Awards that Vested
2021	**1,256,441**	**$ 121**	**$ 111**
2020	1,206,871	$ 117	$ 102
2019	1,126,057	$ 101	$ 95

Performance share unit (PSU) awards

PMI may grant PSU awards to certain executives; recipients may not sell, assign, pledge or otherwise encumber such awards. The PSU awards require the achievement of certain performance factors, which are predetermined at the time of grant, typically over a three-year performance cycle. The performance metrics for such PSU's granted during 2021 and 2020 consisted of PMI's Total Shareholder Return ("TSR") relative to a predetermined peer group and on an absolute basis (40% weight), PMI's currency-neutral compound annual adjusted diluted earnings per share growth rate (30% weight), and PMI's performance against specific measures of PMI's transformation, defined as net revenues from PMI's RRPs and any other non-combustible products as a percentage of PMI's total net revenues in the last year of the performance cycle (30% weight). The performance metrics for such PSUs granted during 2019 consisted of PMI's TSR relative to a predetermined peer group and on an absolute basis (50% weight), PMI's currency-neutral compound annual adjusted operating income growth rate, excluding acquisitions (30% weight), and PMI's performance against specific measures of PMI's transformation (20% weight).

The aggregate of the weighted performance factors for the three metrics in each such PSU award determines the percentage of PSUs that will vest at the end of the three-year performance cycle. The minimum percentage of such PSUs that can vest is zero, with a target percentage of 100 and a maximum percentage of 200. Each such vested PSU entitles the participant to one share of common stock. An aggregate weighted PSU performance factor of 100 will result in the targeted number of PSUs being vested. At the end of the performance cycle, participants are entitled to an amount equivalent to the accumulated dividends paid on common stock during the performance cycle for the number of shares earned. PSU awards do not carry voting rights.

During 2021, the activity for PSU awards was as follows:

	Number of Shares	Grant Date Fair Value Subject to Other Performance Factors (Per Share)	Grant Date Fair Value Subject to TSR Performance Factor (Per Share)
Balance at January 1, 2021	**1,472,800**	**$ 86.76**	**$ 90.48**
Granted	**574,410**	**81.86**	**106.93**
Vested	**(189,839)**	**100.69**	**118.98**
Forfeited	**(320,351)**	**97.76**	**72.55**
Balance at December 31, 2021	**1,537,020**	**$ 82.14**	**$ 96.25**

During the years ended December 31, 2021, 2020 and 2019, the grant date fair value of the PSU awards granted to PMI employees and the recorded compensation expense related to PSU awards were as follows:

(in millions, except per PSU award granted)	PSU Grant Date Fair Value Subject to Other Performance Factors		PSU Grant Date Fair Value Subject to TSR Performance Factor		Compensation Expense related to PSU Awards
	Total	Per PSU Award	Total	Per PSU Award	Total
2021	**$ 28**	**$ 81.86**	**$ 25**	**$ 106.93**	**$ 71**
2020	$ 28	$ 86.04	$ 28	$ 80.36	$ 38
2019	$ 30	$ 77.23	$ 21	$ 83.59	$ 54

The grant date fair value of the PSU awards subject to the other performance factors was determined by using the average of the high and low market price of PMI's stock at the date of the grant. The grant date fair value of the PSU market-based awards subject to the TSR performance factor was determined by using the Monte Carlo simulation model. The following assumptions were used to determine the grant date fair value of the PSU awards subject to the TSR performance factor for the years ended December 31, 2021, 2020 and 2019:

	For the Years
	2021
Risk-free interest rate [a]	0.2 %
Expected volatility [b]	31.7 %

[a] Based on the U.S. Treasury yield curve.
[b] Determined using the observed historical volatility.

The fair value of the PSU award at the date of grant is amortized to expense over the performance period, which is typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2021, PMI had $48 million of total unrecognized compensation cost related to non-vested PSU awards. This cost is recognized over a weighted-average performance cycle period of approximately seventeen months, or upon death, disability or reaching the age of 58.

During the years ended December 31, 2021, 2020 and 2019, share and fair value information for PMI PSU awards that vested were as follows:

(dollars in millions)	Shares of PSU Awards that Vested	Grant Date Fair Value of Vested Shares of PSU Awards	Total Fair Value of PSU Awards that Vested
2021	**189,839**	**$ 21**	**$ 16**
2020	343,806	$ 35	$ 30
2019	330,616	$ 32	$ 28

Note 10.

Earnings per Share:

Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are participating securities and therefore are included in PMI's earnings per share calculation pursuant to the two-class method.

Basic and diluted earnings per share ("EPS") were calculated using the following:

(in millions)	For the Years Ended December 31		
	2021	2020	2019
Net earnings attributable to PMI	**$ 9,109**	$ 8,056	$ 7,185
Less distributed and undistributed earnings attributable to share-based payment awards	**26**	20	17
Net earnings for basic and diluted EPS	**$ 9,083**	$ 8,036	$ 7,168
Weighted-average shares for basic EPS	**1,558**	1,557	1,555
Plus contingently issuable performance stock units (PSUs)	**1**	1	1
Weighted-average shares for diluted EPS	**1,559**	1,558	1,556

For the 2021, 2020 and 2019 computations, there were no antidilutive stock awards.

Note 11.

Income Taxes:

Earnings before income taxes and provision for income taxes consisted of the following for the years ended December 31, 2021, 2020 and 2019:

(in millions)	2021	2020	2019
Earnings before income taxes	**$ 12,232**	$ 10,953	$ 9,872
Provision for income taxes:			
United States federal and state:			
Current	**$ 73**	$ (80)	$ 17
Deferred	**27**	53	24
Total United States	**100**	(27)	41
Outside United States:			
Current	**2,616**	2,600	2,417
Deferred	**(45)**	(196)	(165)
Total outside United States	**2,571**	2,404	2,252
Total provision for income taxes	**$ 2,671**	$ 2,377	$ 2,293

On March 11, 2021, the American Rescue Plan Act of 2021 ("the Act") was signed into law in the U.S. to provide certain relief as a result of the COVID-19 pandemic. As of December 31, 2021, PMI has determined that the Act had no significant impact on PMI's effective tax rate.

On July 20, 2020, the U.S. Department of the Treasury and the Internal Revenue Service released final and proposed regulations under the Global Intangible Low-Taxed Income ("GILTI") and other provisions of the Internal Revenue Code. PMI has analyzed these elective regulations and recorded the impact in its consolidated financial statements, as described below.

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act and, on December 27, 2020, the Consolidated Appropriations Act, 2021 ("U.S. COVID-19 Acts") were signed into law in the U.S. to provide certain relief as a result of the COVID-19 pandemic. In addition, governments around the world have enacted or implemented various forms of tax relief measures in response to the economic conditions in the wake of COVID-19. PMI has determined that neither the U.S. COVID-19 Acts nor changes to income tax laws or regulations in other jurisdictions had a significant impact on PMI's effective tax rate, with the exception of the 2020 corporate income tax rate reduction in Indonesia.

At December 31, 2017, PMI recorded a one-time transition tax liability on its accumulated foreign earnings, which is payable over an eight-year period beginning in 2018. At December 31, 2021 and December 31, 2020, $0.9 billion and $1.1 billion of PMI's remaining long-term portion of transition tax liability, respectively, was recorded in "income taxes and other liabilities" on PMI's consolidated balance sheets.

At December 31, 2021 and 2020, U.S. federal and foreign deferred income taxes have been provided on all accumulated earnings of PMI's foreign subsidiaries.

PMI is regularly examined by tax authorities around the world and is currently under examination in a number of jurisdictions. The U.S. federal statute of limitations remains open for the years 2017 and onward. Foreign and U.S. state jurisdictions have statutes of limitations generally ranging from three to five years. Years still open to

examination by foreign tax authorities in major jurisdictions include Germany (2015 onward), Indonesia (2014 onward), Russia (2019 onward) and Switzerland (2017 onward).

In October 2021, a subsidiary of PMI in Indonesia, PT Hanjaya Mandala Sampoerna Tbk ("HMS"), received a tax assessment in the amount of 3.8 trillion Indonesian rupiah (approximately $260 million) primarily relating to corporate income taxes on domestic and other intercompany transactions for the years 2017 to 2019. HMS paid the assessment in the fourth quarter of 2021 in order to avoid potential penalties and filed an objection letter with the tax office in January 2022. The amount paid was included in other assets in PMI's consolidated balance sheets at December 31, 2021 and negatively impacted net cash provided by operating activities in the consolidated statements of cash flows in the period of payment.

It is reasonably possible that within the next 12 months certain tax examinations will close, which could result in a change in unrecognized tax benefits, along with related interest and penalties. An estimate of any possible change cannot be made at this time.

A reconciliation of the beginning and ending amount of unrecognized tax benefits was as follows:

(in millions)	2021	2020	2019
Balance at January 1,	**$ 72**	$ 63	$ 56
Additions based on tax positions related to the current year	**12**	11	10
Additions for tax positions of previous years	**15**	1	1
Reductions for tax positions of prior years	**(1)**	(4)	(2)
Reductions due to lapse of statute of limitations	**(3)**	(1)	(1)
Settlements	**—**	—	—
Other	**(6)**	2	(1)
Balance at December 31,	**$ 89**	$ 72	$ 63

Unrecognized tax benefits and PMI's liability for contingent income taxes, interest and penalties were as follows:

(in millions)	December 31, 2021	December 31, 2020	December 31, 2019
Unrecognized tax benefits	**$ 89**	$ 72	$ 63
Accrued interest and penalties	**18**	17	16
Tax credits and other indirect benefits	**(7)**	(9)	(12)
Liability for tax contingencies	**$ 100**	$ 80	$ 67

The amount of unrecognized tax benefits that, if recognized, would impact the effective tax rate was $82 million at December 31, 2021. The remainder, if recognized, would principally affect deferred taxes.

For the years ended December 31, 2021, 2020 and 2019, PMI recognized income (expense) in its consolidated statements of earnings of $(3) million, $(1) million and $(4) million, respectively, related to interest and penalties associated with uncertain tax positions.

The effective income tax rate on pre-tax earnings differed from the U.S. federal statutory rate for the following reasons for the years ended December 31, 2021, 2020 and 2019:

	2021	2020	2019
U.S. federal statutory rate	**21.0 %**	21.0 %	21.0 %
Increase (decrease) resulting from:			
Foreign rate differences	**(0.3)**	0.6	1.8
Dividend repatriation cost	**0.6**	0.4	(0.5)
Global intangible low-taxed income	**0.8**	0.1	1.4
U.S. state taxes	**0.2**	0.2	0.7
Foreign derived intangible income	**(0.7)**	(0.6)	(1.2)
Other	**0.2**	—	—
Effective tax rate	**21.8 %**	21.7 %	23.2 %

The 2021 effective tax rate increased 0.1 percentage point to 21.8%. The change in the effective tax rate for 2021, as compared to 2020, was unfavorably impacted by repatriation cost differences and foreign tax credit limitations

related to GILTI, partially offset by the corporate income tax rate reduction in the Philippines (enacted in the first quarter of 2021) and changes in earnings mix by taxing jurisdiction.

The 2020 effective tax rate decreased 1.5 percentage points to 21.7%. The change in the effective tax rate for 2020, as compared to 2019, was favorably impacted by changes in earnings mix by taxing jurisdiction, a reduction of U.S. state tax expense, a reduction of estimated U.S. income tax liabilities for years 2018 and 2019 due to the GILTI regulations mentioned above ($93 million) and the

corporate income tax rate reduction in Indonesia, partially offset by a decrease in deductions related to foreign-derived intangible income for the years 2018 and 2019 and repatriation cost differences.

The tax effects of temporary differences that gave rise to deferred income tax assets and liabilities consisted of the following:

(in millions)	At Decem 2021
Deferred income tax assets:	
Accrued postretirement and postemployment benefits	$ 234
Accrued pension costs	392
Inventory[1]	177
Accrued liabilities	168
Net operating loss carryforwards and tax credits	408
Foreign exchange	—
Other	112
Total deferred income tax assets	1,491
Less: valuation allowance	(239)
Deferred income tax assets, net of valuation allowance	1,252
Deferred income tax liabilities:	
Trade names	(591)
Property, plant and equipment	(140)
Unremitted earnings	(206)
Foreign exchange	(146)
Total deferred income tax liabilities	(1,083)
Net deferred income tax assets	$ 169

[1]Includes deferred tax charges of $153 million and $209 million in 2021 and 2020, respectively, related to intercompany transactions.

At December 31, 2021, PMI recorded deferred tax assets for net operating loss carryforwards and tax credits of $408 million, with varying dates of expiration, primarily after 2026, including $183 million with an unlimited carryforward period. At December 31, 2021, PMI has recorded a valuation allowance of $239 million against deferred tax assets that do not meet the more-likely-than not recognition threshold.

At December 31, 2020, PMI recorded deferred tax assets for net operating loss carryforwards of $351 million, with varying dates of expiration, primarily after 2025, including $79 million with an unlimited carryforward period. At December 31, 2020, PMI has recorded a valuation allowance of $250 million against deferred tax assets that do not meet the more-likely-than-not recognition threshold.

Note 12.

Segment Reporting:

PMI’s subsidiaries and affiliates are primarily engaged in the manufacture and sale of cigarettes and RRPs, including heat-not-burn, vapor and oral nicotine products, in markets outside of the United States of America. PMI's segments are generally organized by geographic region and managed by segment managers who are responsible for the operating and financial results of the regions inclusive of combustible and reduced-risk product categories sold in the region. PMI currently has six geographical segments: the European Union; Eastern Europe; Middle East & Africa; South & Southeast Asia; East Asia & Australia; and Americas; as well as an Other category. Other consists of the 2021 acquisitions of Fertin Pharma A/S, Vectura Group plc. and OtiTopic, Inc. For further details on these acquisitions, see Note 6. *Acquisitions*. PMI records net revenues and operating income to its geographical segments

based upon the geographic area in which the customer resides. Revenues from shipments of Platform 1 devices, heated tobacco units and accessories to Altria Group, Inc. for sale under license in the United States are included in net revenues of the Americas segment.

PMI's chief operating decision maker evaluates geographical segment performance and allocates resources based on regional operating income, which includes results from all product categories sold in each region. Business operations in the Other category are managed and evaluated separately. Interest expense, net, and provision for income taxes are centrally managed and, accordingly,

such items are not presented by segment since they are excluded from the measure of segment profitability reviewed by management. Information about total assets by segment is not disclosed because such information is not reported to or used by PMI's chief operating decision maker. Segment goodwill and other intangible assets, net, are disclosed in Note 3. *Goodwill and Other Intangible Assets, net.* The accounting policies of the segments are the same as those described in Note 2. *Summary of Significant Accounting Policies.*

PMI disaggregates its net revenue from contracts with customers by both geographic location and product category for each of PMI's six geographical segments. For the 2021 acquisitions discussed above, net revenues from contracts with customers are included in the Other category. PMI believes this best depicts how the nature, amount, timing and uncertainty of its revenue and cash flows are affected by economic factors.

Net revenues by geographic segment and Other category were as follows:

	For the Years Ended December 31,		
(in millions)	**2021**	**2020**	**2019**
Net revenues:			
European Union	**$ 12,275**	$ 10,702	$ 9,817
Eastern Europe	**3,544**	3,378	3,282
Middle East & Africa	**3,293**	3,088	4,042
South & Southeast Asia	**4,396**	4,396	5,094
East Asia & Australia	**5,953**	5,429	5,364
Americas	**1,843**	1,701	2,206
Other	**101**	—	—
Net revenues	**$ 31,405**	$ 28,694	$ 29,805

Total net revenues attributable to customers located in Japan, PMI's largest market in terms of net revenues, were $4.6 billion, $4.1 billion and $3.9 billion in 2021, 2020 and 2019, respectively. PMI had one customer in the East Asia & Australia segment that accounted for 15%, 14% and 13% of PMI's consolidated net revenues, and one customer in the European Union segment that accounted for 13%, 11% and 10% of PMI's consolidated net revenues in 2021, 2020 and 2019, respectively.

PMI's net revenues by product category were as follows:

(in millions)	For the Years Ended December 31, 2021	2020	2019
Combustible products:			
European Union	**$ 8,211**	$ 8,053	$ 8,093
Eastern Europe	**2,240**	2,250	2,438
Middle East & Africa	**3,148**	3,031	3,721
South & Southeast Asia	**4,385**	4,395	5,094
East Asia & Australia	**2,414**	2,468	2,693
Americas	**1,790**	1,670	2,179
Total combustible products	**$ 22,190**	$ 21,867	$ 24,218
Reduced-risk products:			
European Union	**$ 4,064**	$ 2,649	$ 1,724
Eastern Europe	**1,304**	1,128	844
Middle East & Africa	**145**	57	321
South & Southeast Asia	**11**	1	—
East Asia & Australia	**3,539**	2,961	2,671
Americas	**53**	31	27
Total reduced-risk products	**$ 9,115**	$ 6,827	$ 5,587
Other:			
Other	**$ 101**	$ —	$ —
Total PMI net revenues	**$ 31,405**	$ 28,694	$ 29,805

Note: Sum of product categories or Regions might not foot to total PMI due to roundings.

Net revenues related to combustible products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of PMI's cigarettes and other tobacco products combined. Other tobacco products primarily include roll-your-own and make-your-own cigarettes, pipe tobacco, cigars and cigarillos and do not include reduced-risk products.

Net revenues related to reduced-risk products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of PMI's heated tobacco units, heat-not-burn devices and related accessories, and other nicotine-containing products, which primarily include PMI's e-vapor and oral nicotine products.

Net revenues in the Other category primarily consist of operating revenues generated from the sale of inhaled therapeutics, and oral and intra-oral delivery systems resulting from the third quarter 2021 acquisitions of Fertin Pharma A/S, Vectura Group plc. and OtiTopic, Inc.

Operating income (loss) by geographic segment and Other category were as follows:

(in millions)	For the Years Ended December 31,		
	2021	**2020**	**2019**
Operating income (loss):			
European Union	**$ 6,119**	$ 5,098	$ 3,970
Eastern Europe	**1,213**	871	547
Middle East & Africa	**1,146**	1,026	1,684
South & Southeast Asia	**1,506**	1,709	2,163
East Asia & Australia	**2,556**	2,400	1,932
Americas	**487**	564	235
Other	**(52)**	—	—
Operating income	**$ 12,975**	$ 11,668	$ 10,531

Items affecting the comparability of results from operations were as follows:

- **Asset impairment and exit costs** - See Note 19. *Asset Impairment and Exit Costs* for details of the $216 million, $149 million and $422 million pre-tax charges for the year ended December 31, 2021, 2020 and 2019, respectively, as well as a breakdown of these costs by segment.
- **Saudi Arabia customs assessments** - See Note 17. *Contingencies* for the details of the $246 million reduction in net revenues of combustible products included in the Middle East & Africa segment for the year ended December 31, 2021.
- **Asset acquisition cost** - See Note 6. *Acquisitions* for the details of the $51 million pre-tax charge associated with the asset acquisition of OtiTopic, Inc. included in Other within the operating income table above for the year ended December 31, 2021.
- **Russia excise and VAT audit charge** - See Note 17. *Contingencies* for details of the $374 million pre-tax charge included in the Eastern Europe segment for the year ended December 31, 2019.
- **Canadian tobacco litigation-related expense** - See Note 17. *Contingencies* and Note 20. *Deconsolidation of RBH* for details of the $194 million pre-tax charge included in the Americas segment for the year ended December 31, 2019.
- **Loss on deconsolidation of RBH** - See Note 20. *Deconsolidation of RBH* for details of the $239 million loss included in the Americas segment for the year ended December 31, 2019.
- **Brazil indirect tax credit** - Following a final and enforceable decision by the highest court in Brazil in October 2020, PMI recorded a gain of $119 million for tax credits representing overpayments of indirect taxes for the period from March 2012 through December 2019; these tax credits were applied to tax liabilities in Brazil during 2021. This amount was included as a reduction in marketing, administration and research costs in the consolidated statements of earnings for the year ended December 31, 2020 and was included in the operating income of the Americas segment. An additional amount of overpaid indirect taxes of approximately $90 million is dependent on a potential tax authority challenge.

Other segment data were as follows:

(in millions)	For the Years Ended December 31, 2021	2020	2019
Depreciation expense:			
European Union	**$ 307**	$ 266	$ 254
Eastern Europe	**131**	173	147
Middle East & Africa	**89**	75	90
South & Southeast Asia	**143**	137	142
East Asia & Australia	**154**	188	185
Americas	**62**	69	80
Other	**16**	—	—
Total depreciation expense	**$ 902**	$ 908	$ 898

(in millions)	For the Years Ended December 31, 2021	2020	2019
Capital expenditures:			
European Union	**$ 470**	$ 384	$ 466
Eastern Europe	**71**	88	132
Middle East & Africa	**37**	22	35
South & Southeast Asia	**52**	57	100
East Asia & Australia	**36**	13	67
Americas	**54**	38	52
Other	**28**	—	—
Total capital expenditures	**$ 748**	$ 602	$ 852

(in millions)	At December 31, 2021	2020	2019
Long-lived assets:			
European Union	**$ 4,504**	$ 4,500	$ 4,275
Eastern Europe	**635**	668	774
Middle East & Africa	**289**	375	369
South & Southeast Asia	**1,386**	1,348	1,361
East Asia & Australia	**740**	807	829
Americas	**661**	784	680
Other	**292**	—	—
Total long-lived assets	**8,507**	8,482	8,288
Financial instruments	**210**	650	314
Total property, plant and equipment, net and Other assets	**$ 8,717**	$ 9,132	$ 8,602

Long-lived assets consist of non-current assets other than goodwill; other intangible assets, net; deferred tax assets, equity investments, and financial instruments. PMI's largest markets in terms of long-lived assets are Switzerland, Italy and Indonesia. Total long-lived assets located in Switzerland, which is reflected in the European Union segment above, were $1.3 billion, $1.3 billion and $1.1 billion at December 31, 2021, 2020 and 2019, respectively. Total long-lived assets located in Italy, which is reflected in the European Union segment above, were $0.9 billion, $1.1 billion and $1.1 billion at December 31, 2021, 2020 and 2019, respectively. Total long-lived assets located in Indonesia, which is reflected in the South & Southeast Asia segment above, were $0.9 billion, $0.7 billion and $0.8 billion at December 31, 2021, 2020 and 2019, respectively.

Note 13.

Benefit Plans:

Pension coverage for employees of PMI's subsidiaries is provided, to the extent deemed appropriate, through separate plans, many of which are governed by local statutory requirements. In addition, PMI provides health care and other benefits to substantially all U.S. retired employees and certain non-U.S. retired employees. In general, health care benefits for non-U.S. retired employees are covered through local government plans.

Pension and other employee benefit costs per the consolidated statements of earnings consisted of the following for December 31, 2021, 2020 and 2019:

(in millions)	2021	2020	2019
Net pension costs (income)	**$ (1)**	$ (14)	$ (18)
Net postemployment costs	**108**	103	100
Net postretirement costs	**8**	8	7
Total pension and other employee benefit costs	**$ 115**	$ 97	$ 89

Pension and Postretirement Benefit Plans

Obligations and Funded Status

The postretirement health care plans are not funded. The projected benefit obligations, plan assets and funded status of PMI's pension plans, and the accumulated benefit obligation and net amount accrued for PMI's postretirement health care plans, at December 31, 2021 and 2020, were as follows:

(in millions)	Pension[1]		Postretirement	
	2021	2020	2021	2020
Benefit obligation at January 1	**$ 12,243**	$ 10,612	**$ 198**	$ 190
Service cost	**291**	268	**2**	2
Interest cost	**50**	68	**5**	6
Benefits paid	**(417)**	(356)	**(8)**	(7)
Employee contributions	**145**	130	**—**	—
Settlement, curtailment and plan amendment	**(194)**	(117)		
Actuarial losses (gains)	**(559)**	653	**5**	5
Currency	**(587)**	992	**(4)**	3
Other	**26**	(7)	**—**	(1)
Benefit obligation at December 31,	**10,998**	12,243	**198**	198
Fair value of plan assets at January 1,	**8,746**	7,928		
Actual return on plan assets	**1,054**	206		
Employer contributions	**269**	102		
Employee contributions	**145**	130		
Benefits paid	**(417)**	(356)		
Settlement	**(37)**	(16)		
Currency	**(444)**	752		
Other	**21**	—		
Fair value of plan assets at December 31,	**9,337**	8,746		
Net pension and postretirement liability recognized at December 31,	**$ (1,661)**	$ (3,497)	**$ (198)**	$ (198)

(1) Primarily non-U.S. based defined benefit retirement plans.

At December 31, 2021, actuarial losses (gains) consisted primarily of gains for assumption changes related to higher discount rates year-over-year for Swiss, German and Dutch plans. At December 31, 2020, actuarial losses (gains) consisted primarily of losses for assumption changes related to lower discount rates year-over-year for Swiss, German and Dutch plans.

At December 31, 2021 and 2020, the Swiss pension plan represented 65% and 63% of the benefit obligation, respectively, and approximately 60% and 59% of the fair value of plan assets at December 31, 2021 and 2020, respectively. At December 31, 2021 and 2020, the U.S. pension plan represented 4% and 4% of the benefit obligation, respectively, and approximately 3% and 4% of the fair value of plan assets at December 31, 2021 and 2020, respectively.

At December 31, 2021 and 2020, the amounts recognized on PMI's consolidated balance sheets for the pension and postretirement plans were as follows:

	Pension		Postretirement	
(in millions)	**2021**	**2020**	**2021**	**2020**
Other assets	**$ 323**	$ 43		
Accrued liabilities — employment costs	**(24)**	(26)	**$ (9)**	$ (8)
Long-term employment costs	**(1,960)**	(3,514)	**(189)**	(190)
	$ (1,661)	$ (3,497)	**$ (198)**	$ (198)

The accumulated benefit obligation, which represents benefits earned to date, for the pension plans was $10.4 billion and $11.5 billion at December 31, 2021 and 2020, respectively.

For pension plans with accumulated benefit obligations in excess of plan assets, the accumulated benefit obligation and fair value of plan assets were $7.5 billion and $5.9 billion, respectively, as of December 31, 2021. The accumulated benefit obligation and fair value of plan assets were $10.5 billion and $7.7 billion, respectively, as of December 31, 2020.

For pension plans with projected benefit obligations in excess of plan assets, the projected benefit obligation and fair value of plan assets were $8.6 billion and $6.7 billion, respectively, as of December 31, 2021. The projected benefit obligation and fair value of plan assets were $12.1 billion and $8.6 billion, respectively, as of December 31, 2020.

The following weighted-average assumptions were used to determine PMI’s pension and postretirement benefit obligations at December 31:

	Pension		Postretirement	
	2021	**2020**	**2021**	**2020**
Discount rate	**0.86 %**	0.56 %	**3.08 %**	2.84 %
Rate of compensation increase	**1.77**	1.79		
Interest crediting rate	**3.15**	3.20		
Health care cost trend rate assumed for next year			**6.27**	6.21
Ultimate trend rate			**4.80**	4.73
Year that rate reaches the ultimate trend rate			**2029**	2029

The discount rate for the largest pension plans is based on a yield curve constructed from a portfolio of high quality corporate bonds that produces a cash flow pattern equivalent to each plan’s expected benefit payments. The discount rate for the remaining plans is developed from local bond indices that match local benefit obligations as closely as possible.

Components of Net Periodic Benefit Cost

Net periodic pension and postretirement health care costs consisted of the following for the years ended December 31, 2021, 2020 and 2019:

(in millions)	Pension			Postretirement		
	2021	**2020**	**2019**	**2021**	**2020**	**2019**
Service cost	**$ 291**	$ 268	$ 214	**$ 2**	$ 2	$ 2
Interest cost	**50**	68	118	**5**	6	7
Expected return on plan assets	**(371)**	(353)	(328)	**—**	—	—
Amortization:						
Net losses	**314**	265	189	**3**	2	—
Prior service cost	**1**	1	(1)	**—**	—	—
Net transition obligation	**—**	1	—	**—**	—	—
Settlement and curtailment	**5**	4	4	**—**	—	—
Net periodic pension and postretirement costs	**$ 290**	$ 254	$ 196	**$ 10**	$ 10	$ 9

Settlement and curtailment charges were due primarily to employee severance and early retirement programs.

The following weighted-average assumptions were used to determine PMI's net pension and postretirement health care costs:

	Pension			Postretirement		
	2021	**2020**	**2019**	**2021**	**2020**	**2019**
Discount rate - service cost	**0.72 %**	1.25 %	2.14 %	**2.84 %**	3.28 %	3.97 %
Discount rate - interest cost	**0.44**	0.67	1.35	**2.84**	3.28	3.97
Expected rate of return on plan assets	**4.43**	4.59	4.70			
Rate of compensation increase	**1.79**	1.82	1.86			
Interest crediting rate	**3.20**	3.20	3.40			
Health care cost trend rate				**6.21**	6.21	6.17

PMI's expected rate of return on pension plan assets is determined by the plan assets' historical long-term investment performance, current asset allocation and estimates of future long-term returns by asset class.

PMI and certain of its subsidiaries sponsor defined contribution plans. Amounts charged to expense for defined contribution plans totaled $71 million, $66 million and $63 million for the years ended December 31, 2021, 2020 and 2019, respectively.

Plan Assets

PMI's investment strategy for pension plans is based on an expectation that equity securities will outperform debt securities over the long term. Accordingly, the target allocation of PMI's plan assets is broadly characterized as approximately 55% in equity securities and approximately 45% in debt securities and other assets. The strategy primarily utilizes indexed U.S. equity securities, international equity securities and investment-grade debt securities. PMI's plans have no investments in hedge funds, private equity or derivatives. PMI attempts to mitigate investment risk by rebalancing between equity and debt asset classes once a year or as PMI's contributions and benefit payments are made.

The fair value of PMI's pension plan assets at December 31, 2021 and 2020, by asset category was as follows:

Asset Category (in millions)	At December 31, 2021	Quoted Prices In Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$ 355	$ 355		
Equity securities:				
U.S. securities	193	193		
International securities	658	658		
Investment funds[(a)]	7,317	5,592	$ 1,725	
International government bonds	210	139	71	
Corporate bonds	278	278		
Other	4	3	1	
Total assets in the fair value hierarchy	$ 9,015	$ 7,218	$ 1,797	$ —
Investment funds measured at net asset value[(b)]	322			
Total assets	$ 9,337			

[(a)] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and JP Morgan EMBI for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 59% are invested in U.S. and international equities; 15% are invested in U.S. and international government bonds; 14% are invested in corporate bonds and 12% are invested in real estate.

[(b)] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Asset Category (in millions)	At December 31, 2020	Quoted Prices In Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$ 324	$ 324		
Equity securities:				
U.S. securities	175	175		
International securities	605	605		
Investment funds[(a)]	6,811	5,206	$ 1,605	
International government bonds	225	149	76	
Corporate bonds	292	292		
Other	7	7		
Total assets in the fair value hierarchy	$ 8,439	$ 6,758	$ 1,681	$ —
Investment funds measured at net asset value[(b)]	307			
Total assets	$ 8,746			

[(a)] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and JP Morgan EMBI for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 63% were invested in U.S. and international equities; 16% were invested in U.S. and international government bonds; 12% were invested in real estate, and 9% were invested in corporate bonds.

[(b)] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

For a description of the fair value hierarchy and the three levels of inputs used to measure fair values, see Note 2. *Summary of Significant Accounting Policies*.

PMI makes, and plans to make, contributions to the extent that they are tax deductible and to meet specific funding requirements of its funded pension plans. Currently, PMI anticipates making contributions of approximately $108 million in 2022 to its pension plans, based on current tax and benefit laws. However, this estimate is subject to change as a result of changes in tax and other benefit laws, as well as asset performance significantly above or below the assumed long-term rate of return on pension assets, or changes in interest and currency rates.

The estimated future benefit payments from PMI pension plans at December 31, 2021, are as follows:

(in millions)		
2022	$	407
2023		421
2024		386
2025		382
2026		400
2027 - 2031		2,193

PMI's expected future annual benefit payments for its postretirement health care plans are estimated to be not material through 2031.

Postemployment Benefit Plans

PMI and certain of its subsidiaries sponsor postemployment benefit plans covering substantially all salaried and certain hourly employees. The cost of these plans is charged to expense over the working life of the covered employees. Net postemployment costs were $228 million, $208 million and $171 million for the years ended December 31, 2021, 2020 and 2019, respectively.

The amounts recognized in accrued postemployment costs net of plan assets on PMI's consolidated balance sheets at December 31, 2021 and 2020, were $925 million and $923 million, respectively.

The accrued postemployment costs were determined using a weighted-average discount rate of 3.1% and 3.0% in 2021 and 2020, respectively; an assumed ultimate annual weighted-average turnover rate of 2.9% and 3.0% in 2021 and 2020, respectively; assumed compensation cost increases of 2.1% in 2021 and 2.1% in 2020, and assumed benefits as defined in the respective plans. In accordance with local regulations, certain postemployment plans are funded. As a result, the accrued postemployment costs disclosed above are presented net of the related assets of $46 million and $46 million at December 31, 2021 and 2020, respectively. Postemployment costs arising from actions that offer employees benefits in excess of those specified in the respective plans are charged to expense when incurred.

Comprehensive Earnings (Losses)

The amounts recorded in accumulated other comprehensive losses at December 31, 2021, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (2,495)	$ (64)	$ (884)	$ (3,443)
Prior service cost	71	1	(22)	50
Net transition obligation	(3)	—	—	(3)
Deferred income taxes	278	24	214	516
Losses to be amortized	$ (2,149)	$ (39)	$ (692)	$ (2,880)

The amounts recorded in accumulated other comprehensive losses at December 31, 2020, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (4,147)	$ (64)	$ (839)	$ (5,050)
Prior service cost	22	2	(22)	2
Net transition obligation	(3)	—	—	(3)
Deferred income taxes	570	24	204	798
Losses to be amortized	$ (3,558)	$ (38)	$ (657)	$ (4,253)

The amounts recorded in accumulated other comprehensive losses at December 31, 2019, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (3,718)	$ (63)	$ (775)	$ (4,556)
Prior service cost	3	2	—	5
Net transition obligation	(4)	—	—	(4)
Deferred income taxes	520	24	182	726
Losses to be amortized	$ (3,199)	$ (37)	$ (593)	$ (3,829)

The movements in other comprehensive earnings (losses) during the year ended December 31, 2021, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings:				
Amortization:				
Net losses	**$ 294**	**$ 4**	**$ 85**	**$ 383**
Prior service cost	**7**	**(1)**	**—**	**6**
Net transition obligation	**—**	**—**	**—**	**—**
Other income/expense:				
Net losses	**5**	**1**	**—**	**6**
Prior service cost	**—**	**—**	**—**	**—**
Deferred income taxes	**(51)**	**(1)**	**(20)**	**(72)**
	255	**3**	**65**	**323**
Other movements during the year:				
Net losses	**1,353**	**(5)**	**(130)**	**1,218**
Prior service cost	**42**	**—**	**—**	**42**
Deferred income taxes	**(241)**	**1**	**30**	**(210)**
	1,154	**(4)**	**(100)**	**1,050**
Total movements in other comprehensive earnings (losses)	**$ 1,409**	**$ (1)**	**$ (35)**	**$ 1,373**

The movements in other comprehensive earnings (losses) during the year ended December 31, 2020, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings:				
Amortization:				
Net losses	$ 250	$ 3	$ 78	$ 331
Prior service cost	29	—	—	29
Net transition obligation	1	—	—	1
Other income/expense:				
Net losses	3	—	—	3
Prior service cost	2	—	—	2
Deferred income taxes	(49)	(1)	(17)	(67)
	236	2	61	299
Other movements during the year:				
Net losses	(682)	(4)	(142)	(828)
Prior service cost	(12)	—	(22)	(34)
Deferred income taxes	99	1	39	139
	(595)	(3)	(125)	(723)
Total movements in other comprehensive earnings (losses)	$ (359)	$ (1)	$ (64)	$ (424)

The movements in other comprehensive earnings (losses) during the year ended December 31, 2019, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings:				
Amortization:				
Net losses	$ 198	$ 3	$ 77	$ 278
Prior service cost	32	(1)	—	31
Other income/expense:				
Net losses	3	—	—	3
Deferred income taxes	(51)	(1)	(17)	(69)
	182	1	60	243
Other movements during the year:				
Net losses	(521)	(27)	(150)	(698)
Prior service cost	(2)	—	—	(2)
Deconsolidation of RBH (net of deferred income taxes)	26	1	—	27
Deferred income taxes	206	6	35	247
	(291)	(20)	(115)	(426)
Total movements in other comprehensive earnings (losses)	$ (109)	$ (19)	$ (55)	$ (183)

Note 14.

Additional Information:

(in millions)	For the Years Ended Dece	
	2021	2020
Research and development expense	**$ 617**	$ 495
Advertising expense	**$ 807**	$ 637
Foreign currency net transaction (gains)/losses	**$ 45**	$ 90
Interest expense	**$ 737**	$ 728
Interest income	**(109)**	(110)
Interest expense, net	**$ 628**	$ 618

Note 15.

Financial Instruments:

Overview

PMI operates in markets outside of the United States of America, with manufacturing and sales facilities in various locations around the world. PMI utilizes certain financial instruments to manage foreign currency and interest rate exposures. Derivative financial instruments are used by PMI principally to reduce exposures to market risks resulting from fluctuations in foreign currency exchange and interest rates by creating offsetting exposures. PMI is not a party to leveraged derivatives and, by policy, does not use derivative financial instruments for speculative purposes. Substantially all of PMI's derivative financial instruments are subject to master netting arrangements, whereby the right to offset occurs in the event of default by a participating party. While these contracts contain the enforceable right to offset through close-out netting rights, PMI elects to present them on a gross basis in the consolidated balance sheets. Collateral associated with these arrangements is in the form of cash and is unrestricted. Financial instruments qualifying for hedge accounting must maintain a specified level of effectiveness between the hedging instrument and the item being hedged, both at inception and throughout the hedged period. PMI formally documents the nature and relationships between the hedging instruments and hedged items, as well as its risk-management objectives, strategies for undertaking the various hedge transactions and method of assessing hedge effectiveness. Additionally, for hedges of forecasted transactions, the significant characteristics and expected terms of the forecasted transaction must be specifically identified, and it must be probable that each forecasted transaction will occur. If it were deemed probable that the forecasted transaction would not occur, the gain or loss would be recognized in earnings.

PMI uses deliverable and non-deliverable forward foreign exchange contracts, foreign currency swaps and foreign currency options, collectively referred to as foreign exchange contracts ("foreign exchange contracts"), and interest rate contracts to mitigate its exposure to changes in exchange and interest rates from third-party and intercompany actual and forecasted transactions. Both foreign exchange contracts and interest rate contracts are collectively referred to as derivative contracts ("derivative contracts"). The primary currencies to which PMI is exposed include the Euro, Indonesian rupiah, Japanese yen, Mexican peso, Philippine peso, Russian ruble and Swiss franc. At December 31, 2021 and 2020, PMI had contracts with aggregate notional amounts of $20.7 billion and $26.5 billion, respectively. Of the $20.7 billion aggregate notional amount at December 31, 2021, $3.8 billion related to cash flow hedges, $6.2 billion related to hedges of net investments in foreign operations, $0.4 billion related to fair value hedges and $10.3 billion related to other derivatives that primarily offset currency exposures on intercompany financing. Of the $26.5 billion aggregate notional amount at December 31, 2020, $5.0 billion related to cash flow

hedges, $8.9 billion related to hedges of net investments in foreign operations and $12.6 billion related to other derivatives that primarily offset currency exposures on intercompany financing.

The fair value of PMI's derivative contracts included in the consolidated balance sheets as of December 31, 2021 and 2020, were as follows:

	Derivative Assets			Derivative Liabilities		
		Fair Value			Fair Value	
(in millions)	Balance Sheet Classification	2021	2020	Balance Sheet Classification	2021	2020
Derivative contracts designated as hedging instruments	Other current assets	**$ 173**	$ 130	Other accrued liabilities	**$ 34**	$ 241
	Other assets	**22**	6	Income taxes and other liabilities	**190**	605
Derivative contracts not designated as hedging instruments	Other current assets	**37**	46	Other accrued liabilities	**75**	207
	Other assets	**—**	—	Income taxes and other liabilities	**—**	57
Total gross amount derivatives contracts presented in the consolidated balance sheets		**$ 232**	$ 182		**$ 299**	$ 1,110
Gross amounts not offset in the consolidated balance sheets						
Financial instruments		**(126)**	(156)		**(126)**	(156)
Cash collateral received/ pledged		**(93)**	(23)		**(151)**	(892)
Net amount		**$ 13**	$ 3		**$ 22**	$ 62

PMI assesses the fair value of its foreign exchange contracts and interest rate contracts using standard valuation models that use, as their basis, readily observable market inputs. The fair value of PMI's foreign exchange forward contracts, foreign currency swaps and interest rate contracts is determined by using the prevailing foreign exchange spot rates and interest rate differentials, and the respective maturity dates of the instruments. The fair value of PMI's currency options is determined by using a Black-Scholes methodology based on foreign exchange spot rates and interest rate differentials, currency volatilities and maturity dates. PMI's derivative contracts have been classified within Level 2 at December 31, 2021 and 2020.

For the years ended December 31, 2021, 2020 and 2019, PMI's derivative contracts impacted the consolidated statements of earnings and comprehensive earnings as follows:

(pre-tax, in millions)	For the Years Ended December 31,											
	Amount of Gain/ (Loss) Recognized in Other Comprehensive Earnings/(Losses) on Derivatives			Statement of Earnings Classification of Gain/(Loss) on Derivatives	Amount of Gain/ (Loss) Reclassified from Other Comprehensive Earnings/(Losses) into Earnings			Amount of Gain/ (Loss) Recognized in Earnings		
	2021	**2020**	**2019**		**2021**	**2020**	**2019**	**2021**	**2020**	**2019**
Derivative contracts designated as hedging instruments:										
Cash flow hedges	**$ 144**	$ (81)	$ (20)							
				Net revenues	**$ 59**	$ (3)	$ 22			
				Cost of sales	**—**	7	1			
				Marketing, administration and research costs	**(10)**	27	2			
				Interest expense, net	**(7)**	(11)	(8)			
Fair value hedges				Interest expense, net				**$ 1**	$ —	$ —
Net investment hedges [(a)]	**484**	(514)	369	Interest expense, net [(b)]				**150**	194	230
Derivative contracts not designated as hedging instruments				Interest expense, net				**55**	71	94
				Marketing, administration and research costs [(c)]				**215**	(368)	(115)
Total	**$ 628**	$ (595)	$ 349		**$ 42**	$ 20	$ 17	**$ 421**	$ (103)	$ 209

[(a)] Amount of gains (losses) on hedges of net investments principally related to changes in exchange and interest rates between the Euro and U.S. dollar

[(b)] Represent the gains for amounts excluded from the effectiveness testing

[(c)] The gains (losses) from these contracts attributable to changes in foreign currency exchange rates substantially offset the (losses) and gains generated by the underlying intercompany and third-party loans being hedged

Cash Flow Hedges

PMI has entered into derivative contracts to hedge the foreign currency exchange and interest rate risks related to certain forecasted transactions. Gains and losses associated with qualifying cash flow hedge contracts are deferred as components of accumulated other comprehensive losses until the underlying hedged transactions are reported in PMI's consolidated statements of earnings. As of December 31, 2021, PMI has hedged forecasted transactions for periods not exceeding the next twelve months, with the exception of one derivative contract that expires in May 2024. The impact of these hedges is primarily included in operating cash flows on PMI's consolidated statements of cash flows.

Fair Value Hedges

PMI has entered into fixed-to-floating interest rate contracts, designated as fair value hedges to minimize exposure to changes in the fair value of fixed rate U.S. dollar-denominated debt that results from fluctuations in benchmark interest rates. For derivative contracts that are designated and qualify as fair value hedges the gain or loss on the derivative, as well as the offsetting gain or loss on the hedged items attributable to the hedged risk, is recognized in current earnings. The carrying amount of the debt hedged, which includes the cumulative adjustment for fair value gains/losses, as of December 31, 2021 was $398 million, and is recorded in long-term debt in the consolidated balance sheets.

Hedges of Net Investments in Foreign Operations

PMI designates derivative contracts and certain foreign currency denominated debt instruments as net investment hedges, primarily of its Euro net assets. The amount of pre-tax gain/(loss) related to these debt instruments, that was reported as a component of accumulated other comprehensive losses within currency translation adjustment, was $278 million, $(465) million and $234 million, for the years ended December 31, 2021, 2020 and 2019, respectively. The premiums paid for, and settlements of, net investment hedges are included in investing cash flows on PMI's consolidated statements of cash flows.

Other Derivatives

PMI has entered into derivative contracts to hedge the foreign currency exchange and interest rate risks related to intercompany loans between certain subsidiaries, and third-party loans. While effective as economic hedges, no hedge accounting is applied for these contracts; therefore, the gains (losses) relating to these contracts are reported in PMI's consolidated statements of earnings.

Qualifying Hedging Activities Reported in Accumulated Other Comprehensive Losses

Derivative gains or losses reported in accumulated other comprehensive losses are a result of qualifying hedging activity. Transfers of these gains or losses to earnings are offset by the corresponding gains or losses on the underlying hedged item. Hedging activity affected accumulated other comprehensive losses, net of income taxes, as follows:

(in millions)	For the Years Ended December 31, 2021	2020
Gain/(loss) as of January 1,	**$ (85)**	$ 3
Derivative (gains)/ losses transferred to earnings	**(35)**	(20)
Change in fair value	**124**	(68)
Gain/(loss) as of December 31,	**$ 4**	$ (85)

At December 31, 2021, PMI expects $27 million of derivative gains that are included in accumulated other comprehensive losses to be reclassified to the consolidated statement of earnings within the next 12 months. These gains are expected to be substantially offset by the statement of earnings impact of the respective hedged transactions.

Contingent Features

PMI's derivative instruments do not contain contingent features.

Credit Exposure and Credit Risk

PMI is exposed to credit loss in the event of non-performance by counterparties. While PMI does not anticipate non-performance, its risk is limited to the fair value of the financial instruments less any cash collateral received or pledged. PMI actively monitors its exposure to credit risk through the use of credit approvals and credit limits and by selecting and continuously monitoring a diverse group of major international banks and financial institutions as counterparties.

Note 16.

Accumulated Other Comprehensive Losses:

PMI's accumulated other comprehensive losses, net of taxes, consisted of the following:

(Losses) Earnings	**At December 31,**		
(in millions)	**2021**	**2020**	**2019**
Currency translation adjustments	**$ (6,701)**	$ (6,843)	$ (5,537)
Pension and other benefits	**(2,880)**	(4,253)	(3,829)
Derivatives accounted for as hedges	**4**	(85)	3
Total accumulated other comprehensive losses	**$ (9,577)**	$ (11,181)	$ (9,363)

Reclassifications from Other Comprehensive Earnings

The movements in accumulated other comprehensive losses and the related tax impact, for each of the components above, that are due to current period activity and reclassifications to the income statement, including those related to the deconsolidation of RBH, are shown on the consolidated statements of comprehensive earnings for the years ended December 31, 2021, 2020, and 2019. For additional information, see Note 13. *Benefit Plans* for disclosures related to PMI's pension and other benefits, Note 15. *Financial Instruments* for disclosures related to derivative financial instruments and Note 20. *Deconsolidation of RBH* for disclosures related to the deconsolidation of RBH.

Note 17.

Contingencies:

Tobacco-Related Litigation

Legal proceedings covering a wide range of matters are pending or threatened against us, and/or our subsidiaries, and/or our indemnitees in various jurisdictions. Our indemnitees include distributors, licensees, and others that have been named as parties in certain cases and that we have agreed to defend, as well as to pay costs and some or all of judgments, if any, that may be entered against them. Pursuant to the terms of the Distribution Agreement between Altria Group, Inc. ("Altria") and PMI, PMI will indemnify Altria and Philip Morris USA Inc. ("PM USA"), a U.S. tobacco subsidiary of Altria, for tobacco product claims based in substantial part on products manufactured by PMI or contract manufactured for PMI by PM USA, and PM USA will indemnify PMI for tobacco product claims based in substantial part on products manufactured by PM USA, excluding tobacco products contract manufactured for PMI.

It is possible that there could be adverse developments in pending cases against us and our subsidiaries. An unfavorable outcome or settlement of pending tobacco-related litigation could encourage the commencement of additional litigation.

Damages claimed in some of the tobacco-related litigation are significant and, in certain cases in Brazil, Canada and Nigeria, range into the billions of U.S. dollars. The variability in pleadings in multiple jurisdictions, together with the

actual experience of management in litigating claims, demonstrate that the monetary relief that may be specified in a lawsuit bears little relevance to the ultimate outcome. Much of the tobacco-related litigation is in its early stages, and litigation is subject to uncertainty. However, as discussed below, we have to date been largely successful in defending tobacco-related litigation.

We and our subsidiaries record provisions in the consolidated financial statements for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. At the present time, except as stated otherwise in this Note 17. *Contingencies,* while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available to it (i) management has not concluded that it is probable that a loss has been incurred in any of the pending tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any. Legal defense costs are expensed as incurred.

It is possible that our consolidated results of operations, cash flows or financial position could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. Nevertheless, although litigation is subject to uncertainty, we and each of our subsidiaries named as a defendant believe, and each has been so advised by counsel handling the respective cases, that we have valid defenses to the litigation pending against us, as well as valid bases for appeal of adverse verdicts. All such cases are, and will continue to be, vigorously defended. However, we and our subsidiaries may enter into settlement discussions in particular cases if we believe it is in our best interests to do so.

CCAA Proceedings and Stay of Tobacco-Related Cases Pending in Canada

As a result of the Court of Appeal of Quebec's decision in both the *Létourneau* and *Blais* cases described below, our subsidiary, Rothmans, Benson & Hedges Inc. ("RBH"), and the other defendants, JTI Macdonald Corp., and Imperial Tobacco Canada Limited, sought protection in the Ontario Superior Court of Justice under the Companies' Creditors Arrangement Act ("CCAA") on March 22, March 8, and March 12, 2019 respectively. CCAA is a Canadian federal law that permits a Canadian business to restructure its affairs while carrying on its business in the ordinary course. The initial CCAA order made by the Ontario Superior Court on March 22, 2019 authorizes RBH to pay all expenses incurred in carrying on its business in the ordinary course after the CCAA filing, including obligations to employees, vendors, and suppliers. As further described in Note 20. *Deconsolidation of RBH*, RBH's financial results have been deconsolidated from our consolidated financial statements since March 22, 2019. As part of the CCAA proceedings, there is currently a comprehensive stay up to and including March 31, 2022 of all tobacco-related litigation pending in Canada against RBH and the other defendants, including PMI and our indemnitees (PM USA and Altria), namely, the smoking and health class actions filed in various Canadian provinces and health care cost recovery actions. These proceedings are presented below under the caption "*Stayed Litigation — Canada*." Ernst & Young Inc. has been appointed as monitor of RBH in the CCAA proceedings. In accordance with the CCAA process, as the parties work towards a plan of arrangement or compromise in a confidential mediation, it is anticipated that the court will set additional hearings and further extend the stay of proceedings. On April 17, 2019, the Ontario Superior Court ruled that RBH and the other defendants will not be allowed to file an application to the Supreme Court of Canada for leave to appeal the Court of Appeal's decision in the *Létourneau* and the *Blais* cases so long as the comprehensive stay of all tobacco-related litigation in Canada remains in effect and that the time period to file the application would be extended by the stay period. While RBH believes that the findings of liability and damages in both *Létourneau* and the *Blais* cases were incorrect, the CCAA proceedings will provide a forum for RBH to seek resolution through a plan of arrangement or compromise of all tobacco-related litigation pending in Canada. It is not possible to predict the resolution of the underlying legal proceedings or the length of the CCAA process.

Stayed Litigation — Canada

Smoking and Health Litigation — Canada

In the first class action pending in Canada, *Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI-Macdonald Corp., Quebec Superior Court, Canada*, filed in November 1998, RBH and other Canadian cigarette manufacturers (Imperial Tobacco Canada Ltd. and JTI-Macdonald Corp.) are defendants. The plaintiffs, an anti-smoking organization and an individual smoker, sought compensatory and punitive damages for each member of the class who suffers allegedly from certain smoking-related diseases. The class was certified in 2005. The trial court issued its judgment on May 27, 2015. The trial court found RBH and two other Canadian manufacturers liable and found that the class members' compensatory damages totaled approximately CAD 15.5 billion, including pre-judgment interest (approximately $12.1 billion). The trial court awarded compensatory damages on a joint and several liability basis, allocating 20% to our subsidiary (approximately CAD 3.1 billion, including pre-judgment interest (approximately $2.4 billion)). In addition, the trial

court awarded CAD 90,000 (approximately $70,500) in punitive damages, allocating CAD 30,000 (approximately $23,500) to RBH. The trial court estimated the disease class at 99,957 members. RBH appealed to the Court of Appeal of Quebec. In October 2015, the Court of Appeal ordered RBH to furnish security totaling CAD 226 million (approximately $177 million) to cover both the *Létourneau* and *Blais* cases, which RBH has paid in installments through March 2017. The Court of Appeal ordered Imperial Tobacco Canada Ltd. to furnish security totaling CAD 758 million (approximately $594 million) in installments through June 2017. JTI Macdonald Corp. was not required to furnish security in accordance with plaintiffs' motion. The Court of Appeal ordered that the security is payable upon a final judgment of the Court of Appeal affirming the trial court's judgment or upon further order of the Court of Appeal.

On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's findings of liability and the compensatory and punitive damages award while reducing the total amount of compensatory damages to approximately CAD 13.5 billion including interest (approximately $10.6 billion) due to the trial court's error in the calculation of interest. The compensatory damages award is on a joint and several basis with an allocation of 20% to RBH (approximately CAD 2.7 billion, including pre-judgment interest (approximately $2.1 billion)). The Court of Appeal upheld the trial court's findings that defendants violated the Civil Code of Quebec, the Quebec Charter of Human Rights and Freedoms, and the Quebec Consumer Protection Act by failing to warn adequately of the dangers of smoking and by conspiring to prevent consumers from learning of the dangers of smoking. The Court of Appeal further held that the plaintiffs either need not prove, or had adequately proven, that these faults were a cause of the class members' injuries. In accordance with the judgment, defendants were required to deposit their respective portions of the damages awarded in both the *Létourneau* case described below and the *Blais* case, approximately CAD 1.1 billion (approximately $862 million), into trust accounts within 60 days. RBH's share of the deposit was approximately CAD 257 million (approximately $194 million). PMI recorded a pre-tax charge of $194 million in its consolidated results, representing $142 million net of tax, as tobacco litigation-related expense, in the first quarter of 2019. The charge reflects PMI's assessment of the portion of the judgment that represents probable and estimable loss prior to the deconsolidation of RBH and corresponds to the trust account deposit required by the judgment.

In the second class action pending in Canada, *Cecilia Létourneau v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI-Macdonald Corp., Quebec Superior Court, Canada,* filed in September 1998, RBH and other Canadian cigarette manufacturers (Imperial Tobacco Canada Ltd. and JTI-Macdonald Corp.) are defendants. The plaintiff, an individual smoker, sought compensatory and punitive damages for each member of the class who is deemed addicted to smoking. The class was certified in 2005. The trial court issued its judgment on May 27, 2015. The trial court found RBH and two other Canadian manufacturers liable and awarded a total of CAD 131 million (approximately $103 million) in punitive damages, allocating CAD 46 million (approximately $36 million) to RBH. The trial court estimated the size of the addiction class at 918,000 members but declined to award compensatory damages to the addiction class because the evidence did not establish the claims with sufficient accuracy. The trial court found that a claims process to allocate the awarded punitive damages to individual class members would be too expensive and difficult to administer. On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's findings of liability and the total amount of punitive damages awarded allocating CAD 57 million including interest (approximately $45 million) to RBH. See the *Blais* description above and Note 20. *Deconsolidation of RBH* below for further detail concerning the security order pertaining to both *Létourneau* and *Blais* cases and the impact of the decision on PMI's financial statements.

RBH and PMI believe the findings of liability and damages in both *Létourneau* and the *Blais* cases were incorrect and in contravention of applicable law on several grounds including the following: (i) defendants had no obligation to warn class members who knew, or should have known, of the risks of smoking; (ii) defendants cannot be liable to class members who would have smoked regardless of what warnings were given; and (iii) defendants cannot be liable to all class members given the individual differences between class members.

In the third class action pending in Canada, *Kunta v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Winnipeg, Canada*, filed June 12, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic obstructive pulmonary disease ("COPD"), severe asthma, and mild reversible lung disease resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products.

In the fourth class action pending in Canada, *Adams v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Saskatchewan, Canada*, filed July 10, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, emphysema, heart disease, or cancer, as well as restitution of profits.

In the fifth class action pending in Canada, *Semple v. Canadian Tobacco Manufacturers' Council, et al., The Supreme Court (trial court), Nova Scotia, Canada*, filed June 18, 2009, we, RBH, and our indemnitees (PM USA and Altria),

and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and COPD resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products.

In the sixth class action pending in Canada, *Dorion v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Alberta, Canada,* filed June 15, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic bronchitis and severe sinus infections resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class

comprised of all smokers, their estates, dependents and family members, restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products. To date, we, our subsidiaries, and our indemnitees have not been properly served with the complaint.

In the seventh class action pending in Canada, *McDermid v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and heart disease resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from heart disease allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed.

In the eighth class action pending in Canada, *Bourassa v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, the heir to a deceased smoker, alleges that the decedent was addicted to tobacco products and suffered from emphysema resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from chronic respiratory diseases allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed. In December 2014, plaintiff filed an amended statement of claim.

In the ninth class action pending in Canada, *Suzanne Jacklin v. Canadian Tobacco Manufacturers' Council, et al., Ontario Superior Court of Justice,* filed June 20, 2012, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, heart disease, or cancer, as well as restitution of profits.

Health Care Cost Recovery Litigation — Canada

In the first health care cost recovery case pending in Canada, *Her Majesty the Queen in Right of British Columbia v. Imperial Tobacco Limited, et al., Supreme Court, British Columbia, Vancouver Registry, Canada,* filed January 24, 2001, we, RBH, our indemnitee (PM USA), and other members of the industry are defendants. The plaintiff, the government of the province of British Columbia, brought a claim based upon legislation enacted by the province authorizing the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, resulting from a "tobacco related wrong."

In the second health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of New Brunswick v. Rothmans Inc., et al., Court of Queen's Bench of New Brunswick, Trial Court, New Brunswick, Fredericton, Canada,* filed March 13, 2008, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of New Brunswick based on legislation enacted in the province. This legislation is similar to the law introduced in British Columbia that authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the third health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of Ontario v. Rothmans Inc., et al., Ontario Superior Court of Justice, Toronto, Canada*, filed September 29, 2009, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Ontario based on legislation enacted in the province. This legislation is similar to the laws introduced in British Columbia and New Brunswick that authorize the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the fourth health care cost recovery case filed in Canada, *Attorney General of Newfoundland and Labrador v. Rothmans Inc., et al., Supreme Court of Newfoundland and Labrador, St. Johns, Canada*, filed February 8, 2011, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Newfoundland and Labrador based on legislation enacted in the province that

is similar to the laws introduced in British Columbia, New Brunswick and Ontario. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the fifth health care cost recovery case filed in Canada, *Attorney General of Quebec v. Imperial Tobacco Limited, et al., Superior Court of Quebec, Canada*, filed June 8, 2012, we, RBH, our indemnitee (PM USA), and other members of the industry are defendants. The claim was filed by the government of the province of Quebec based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the sixth health care cost recovery case filed in Canada, *Her Majesty in Right of Alberta v. Altria Group, Inc., et al., Supreme Court of Queen's Bench Alberta, Canada*, filed June 8, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Alberta based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the seventh health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Manitoba v. Rothmans, Benson & Hedges, Inc., et al., The Queen's Bench, Winnipeg Judicial Centre, Canada*, filed May 31, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Manitoba based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the eighth health care cost recovery case filed in Canada, *The Government of Saskatchewan v. Rothmans, Benson & Hedges Inc., et al., Queen's Bench, Judicial Centre of Saskatchewan, Canada*, filed June 8, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Saskatchewan based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the ninth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Prince Edward Island v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Prince Edward Island (General Section), Canada*, filed September 10, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Prince Edward Island based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the tenth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Nova Scotia v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Nova Scotia, Canada*, filed January 2, 2015, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Nova Scotia based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

The table below lists the number of tobacco-related cases pertaining to combustible products pending against us and/or our subsidiaries or indemnitees as of December 31, 2021, December 31, 2020 and December 31, 2019:[1]

Type of Case	Number of Cases Pending as of December 31, 2021	Number of Cases Pending as of December 31, 2020	Number of Cases Pending as of December 31, 2019
Individual Smoking and Health Cases	40	43	50
Smoking and Health Class Actions	9	9	10
Health Care Cost Recovery Actions	17	17	17
Label-Related Class Actions	—	—	—
Individual Label-Related Cases	3	5	5
Public Civil Actions	1	2	2

Since 1995, when the first tobacco-related litigation was filed against a PMI entity, 523 Smoking and Health, Label-Related, Health Care Cost Recovery, and Public Civil Actions in which we and/or one of our subsidiaries and/or

indemnitees were a defendant have been terminated in our favor. Fourteen cases have had decisions in favor of plaintiffs. Ten of these cases have subsequently reached final resolution in our favor and four remain on appeal.

[1] Includes cases pending in Canada.

The table below lists the verdict and significant post-trial developments in the four pending cases where a verdict was returned in favor of the plaintiff:

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict
May 27, 2015	Canada/Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec rule in favor of the *Blais* clas on liability and found th class members' compensatory damages totaled approximately C 15.5 billion (approximat $12.1 billion), including pre-judgment interest. T trial court awarded compensatory damages a joint and several liabili basis, allocating 20% to subsidiary (approximate CAD 3.1 billion includi pre-judgment interest (approximately $2.4 billion)). The trial court awarded CAD 90,000 (approximately $70,500 punitive damages, allocating CAD 30,000 (approximately $23,500 our subsidiary. The trial court ordered defendants pay CAD 1 billion (approximately $783 million) of the compensatory damage award, CAD 200 million (approximately $157 million) of which is our subsidiary's portion, into trust within 60 days.

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict
May 27, 2015	Canada/Cecilia Létourneau	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec rule in favor of the *Létournea* class on liability and awarded a total of CAD 131 million (approximat $103 million) in punitive damages, allocating CA 46 million (approximate $36 million) to RBH. Th trial court ordered defendants to pay the ful punitive damage award i a trust within 60 days. T court did not order the payment of compensator damages.

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict
August 5, 2016	Argentina/Hugo Lespada	Individual Action	On August 5, 2016, the Civil Court No. 14 - Mar del Plata, issued a verdic favor of plaintiff, an individual smoker, and awarded him ARS 110,0 (approximately $1,044), plus interest, in compensatory and moral damages. The trial court found that our subsidiary failed to warn plaintiff o the risk of becoming addicted to cigarettes.

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
June 17, 2021	Argentina/Claudia Milano	Individual Action	On June 17, 2021, the Civil Court No. 9 - Mar del Plata, issued a verdict in favor of plaintiff, an individual smoker, and awarded her smoking cessation treatments, ARS 150,000 (approximately $1,423), in compensatory and moral damages, and ARS 4,000,000 (approximately $37,958) in punitive damages, plus interest and costs. The trial court found that our subsidiary failed to warn plaintiff of the risk of becoming addicted to cigarettes.	On July 2, 2021, our subsidiary filed its notice of appeal. In addition, plaintiff filed an appeal challenging the dismissal of the claim for psychological damages. As required by local law, our subsidiary deposited the damages awarded, plus interest and costs, in total ARS 6,114,428 (approximately $58,024), into a court escrow account. Our subsidiary challenged the amount determined by the court. The Mar del Plata Court of Appeals granted our subsidiary's challenge to the escrow amount determined by the trial court. As a result, on December 16, 2021, ARS 893,428 (approximately $8,478) was returned to our subsidiary. If our subsidiary ultimately prevails on appeal, the remaining deposited amounts will be returned to our subsidiary.

Pending claims related to tobacco products generally fall within the following categories:

Smoking and Health Litigation: These cases primarily allege personal injury and are brought by individual plaintiffs or on behalf of a class or purported class of individual plaintiffs. Plaintiffs' allegations of liability in these cases are based on various theories of recovery, including negligence, gross negligence, strict liability, fraud, misrepresentation, design defect, failure to warn, breach of express and implied warranties, violations of deceptive trade practice laws and consumer protection statutes. Plaintiffs in these cases seek various forms of relief, including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include licit activity, failure to state a claim, lack of defect, lack of proximate cause, assumption of the risk, contributory negligence, and statute of limitations.

As of December 31, 2021, there were a number of smoking and health cases pending against us, our subsidiaries or indemnitees, as follows:

- 40 cases brought by individual plaintiffs in Argentina (31), Brazil (2), Canada (2), Chile (1), the Philippines (1), Turkey (1) and Scotland (1), as well as 1 case brought by an individual plaintiff in the United States District Court for the District of Oregon in May 2021. The provisions of the 2008 Share Distribution Agreement between PMI and Altria provide for indemnities to PMI for certain liabilities concerning tobacco products as described above under the caption "*Tobacco-Related Litigation,*"compared with 43 such cases on December 31, 2020, and 50 cases on December 31, 2019; and
- 9 cases brought on behalf of classes of individual plaintiffs, compared with 9 such cases on December 31, 2020 and 10 such cases on December 31, 2019.

The class actions pending in Canada are described above under the caption "*Smoking and Health Litigation — Canada.*"

Health Care Cost Recovery Litigation: These cases, brought by governmental and non-governmental plaintiffs, seek reimbursement of health care cost expenditures allegedly caused by tobacco products. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including unjust enrichment, negligence, negligent design, strict liability, breach of express and implied warranties, violation of a voluntary undertaking or special duty, fraud, negligent misrepresentation, conspiracy, public nuisance, defective product, failure to warn, sale of cigarettes to minors, and claims under statutes governing competition and deceptive trade practices. Plaintiffs in these cases seek various forms of relief including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include lack of proximate cause, remoteness of injury, failure to state a claim, adequate remedy at law, “unclean hands” (namely, that plaintiffs cannot obtain equitable relief because they participated in, and benefited from, the sale of cigarettes), and statute of limitations.

As of December 31, 2021, there were 17 health care cost recovery cases pending against us, our subsidiaries or indemnitees in Brazil (1), Canada (10), Korea (1) and Nigeria (5), compared with 17 such cases on December 31, 2020 and 17 such cases on December 31, 2019.

The health care cost recovery actions pending in Canada are described above under the caption "*Health Care Cost Recovery Litigation — Canada.*"

In the health care cost recovery case in Brazil, *The Attorney General of Brazil v. Souza Cruz Ltda., et al., Federal Trial Court, Porto Alegre, Rio Grande do Sul, Brazil*, filed May 21, 2019, we, our subsidiaries, and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases in certain prior years, payment of anticipated costs of treating future alleged smoking-related diseases, and moral damages. Defendants filed answers to the complaint in May 2020.

In the first health care cost recovery case in Nigeria, *The Attorney General of Lagos State v. British American Tobacco (Nigeria) Limited, et al., High Court of Lagos State, Lagos, Nigeria,* filed March 13, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of making challenges to service and the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the second health care cost recovery case in Nigeria, *The Attorney General of Kano State v. British American Tobacco (Nigeria) Limited, et al., High Court of Kano State, Kano, Nigeria,* filed May 9, 2007, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of challenging the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the third health care cost recovery case in Nigeria, *The Attorney General of Gombe State v. British American Tobacco (Nigeria) Limited, et al., High Court of Gombe State, Gombe, Nigeria,* filed October 17, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In February 2011, the court ruled that the plaintiff had not complied with the procedural steps necessary to serve us. As a result of this ruling, plaintiff must re-serve its claim. We have not yet been re-served.

In the fourth health care cost recovery case in Nigeria, *The Attorney General of Oyo State, et al., v. British American Tobacco (Nigeria) Limited, et al., High Court of Oyo State, Ibadan, Nigeria,* filed May 25, 2007, we and other members of the industry are defendants. Plaintiffs seek reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We challenged service as improper. In June 2010, the court ruled that plaintiffs did not have leave to serve the writ of summons on the defendants and that they must re-serve the writ. We have not yet been re-served.

In the fifth health care cost recovery case in Nigeria, *The Attorney General of Ogun State v. British American Tobacco (Nigeria) Limited, et al., High Court of Ogun State, Abeokuta, Nigeria*, filed February 26, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In May 2010, the trial court rejected our objections to the court's jurisdiction. We have appealed. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the health care cost recovery case in Korea, the *National Health Insurance Service v. KT&G, et. al.,* filed April 14, 2014, our subsidiary and other Korean manufacturers are defendants. Plaintiff alleges that defendants concealed the health hazards of smoking, marketed to youth, added ingredients to make their products more harmful and addictive, and misled consumers into believing that *Lights* cigarettes are safer than regular cigarettes. The National Health Insurance Service seeks to recover damages allegedly incurred in treating 3,484 patients with small cell lung cancer,

squamous cell lung cancer, and squamous cell laryngeal cancer from 2003 to 2012. The trial court dismissed the case in its entirety on November 20, 2020. Plaintiff appealed.

Label-Related Cases: These cases, now brought only by individual plaintiffs, allege that the use of the descriptor “Lights” or other alleged misrepresentations or omissions of labeling information constitute fraudulent and misleading conduct. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including misrepresentation, deception, and breach of consumer protection laws. Plaintiffs seek various forms of relief including restitution, injunctive relief, and compensatory and other damages. Defenses raised include lack of causation, lack of reliance, assumption of the risk, and statute of limitations.

As of December 31, 2021, there were 3 label-related cases brought by individual plaintiffs in Italy (1) and Chile (2) pending against our subsidiaries, compared with 5 such cases on December 31, 2020, and 5 such cases on December 31, 2019.

Public Civil Actions: Claims have been filed either by an individual, or a public or private entity, seeking to protect collective or individual rights, such as the right to health, the right to information or the right to safety. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including product defect, concealment, and misrepresentation. Plaintiffs in these cases seek various forms of relief including injunctive relief such as banning cigarettes, descriptors, smoking in certain places and advertising, as well as implementing communication campaigns and reimbursement of medical expenses incurred by public or private institutions.

As of December 31, 2021, there was 1 public civil action pending against our subsidiary in Venezuela (1), compared with 2 such cases on December 31, 2020, and 2 such cases on December 31, 2019.

In a public civil action in Venezuela, *Federation of Consumers and Users Associations ("FEVACU"), et al. v. National Assembly of Venezuela and the Venezuelan Ministry of Health, Constitutional Chamber of the Venezuelan Supreme Court*, filed April 29, 2008, we were not named as a defendant, but the plaintiffs published a notice pursuant to court order, notifying all interested parties to appear in the case. In January 2009, our subsidiary appeared in the case in response to this notice. The plaintiffs purport to represent the right to health of the citizens of Venezuela and claim that the government failed to protect adequately its citizens' right to health. The claim asks the court to order the government to enact stricter regulations on the manufacture and sale of tobacco products. In addition, the plaintiffs ask the court to order companies involved in the tobacco industry to allocate a percentage of their "sales or benefits" to establish a fund to pay for the health care costs of treating smoking-related diseases. In October 2008, the court ruled that plaintiffs have standing to file the claim and that the claim meets the threshold admissibility requirements. In December 2012, the court admitted our subsidiary and BAT's subsidiary as interested third parties. In February 2013, our subsidiary answered the complaint.

Reduced-Risk Products

In Colombia, an individual filed a purported class action, *Ana Ferrero Rebolledo v. Philip Morris Colombia S.A., et al.*, in April 2019 against our subsidiaries with the Civil Court of Bogota related to the marketing of our Platform 1 product. Plaintiff alleged that our subsidiaries advertise the product in contravention of law and in a manner that misleads consumers by portraying the product in a positive light, and further asserts that the Platform 1 vapor contains many toxic compounds, creates a high level of dependence, and has damaging second-hand effects. Plaintiff sought injunctive relief and damages on her behalf and on a behalf of two classes (class 1 - all Platform 1 consumers in Colombia who seek damages for the purchase price of the product and personal injuries related to the alleged addiction, and class 2 - all residents of the neighborhood where the advertising allegedly took place who seek damages for exposure to the alleged illegal advertising). Our subsidiaries answered the complaint in January 2020, and in February 2020, plaintiff filed an amended complaint. The amended complaint modifies the relief sought on behalf of the named plaintiff and on behalf of a single class (all consumers of Platform 1 products in Colombia who seek damages for the product purchase price and personal injuries related to the use of an allegedly harmful product). In June 2021, our subsidiaries answered the amended complaint.

Other Litigation

The Department of Special Investigations of the government of Thailand ("DSI") conducted an investigation into alleged underpayment by our subsidiary, Philip Morris (Thailand) Limited ("PM Thailand"), of customs duties and excise taxes relating to imports from the Philippines covering the period 2003-2007. On January 18, 2016, the Public Prosecutor filed charges against our subsidiary and seven former and current employees in the Bangkok Criminal Court alleging that PM Thailand and the individual defendants jointly and with the intention to defraud the Thai government, under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries of cigarettes from the Philippines during the period of July 2003 to June 2006. The government is seeking a fine of approximately THB 80.8 billion (approximately $2.4 billion). In May 2017, Thailand enacted a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and other Thai governmental agencies. Trial in the case began in November 2017 and concluded in September 2019. In November 2019, the trial

court found our subsidiary guilty of under-declaration of the prices and imposed a fine of approximately THB 1.2 billion (approximately $36 million). The trial court dismissed all charges against the individual defendants. In December 2019, as required by the Thai law, our subsidiary paid the fine. This payment is included in other assets on the consolidated balance sheets and negatively impacted net cash provided by operating activities in the consolidated statements of cash flows in the period of payment. Our subsidiary filed an appeal of the trial court's decision. In addition, the Public Prosecutor filed an appeal of the trial court's decision challenging the dismissal of charges against the individual defendants and the amount of the fine imposed. If our subsidiary ultimately prevails on appeal, then Thailand will be required to return this payment to our subsidiary. The appellate court is scheduled to issue its decision on the appeals on June 1, 2022.

The DSI also conducted an investigation into alleged underpayment by PM Thailand of customs duties and excise taxes relating to imports from Indonesia covering the period 2000-2003. On January 26, 2017, the Public Prosecutor filed charges against PM Thailand and its former Thai employee in the Bangkok Criminal Court alleging that PM Thailand and its former employee jointly and with the intention to defraud the Thai government under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries during the period from January 2002 to July 2003. The government is seeking a fine of approximately THB 19.8 billion (approximately $599 million). In May 2017, Thailand enacted a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law, and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and a Thai court. Trial in the case began in November 2018 and concluded in December 2019. In March 2020, the trial court found our subsidiary guilty of under-declaration of the prices and imposed a fine of approximately THB 130 million (approximately $4 million). The trial court dismissed all charges against the individual defendant. In April 2020, as required by Thai law, our subsidiary paid the fine. This payment is included in other assets on the condensed consolidated balance sheets and negatively impacted net cash provided by operating activities in the condensed consolidated statements of cash flows in the period of payment. Our subsidiary filed an appeal of the trial court's decision. In addition, the Public Prosecutor filed an appeal of the trial court's decision challenging the dismissal of charges against the individual defendant and the amount of the fine imposed. If our subsidiary ultimately prevails on appeal, then Thailand will be required to return this payment to our subsidiary.

The South Korean Board of Audit and Inspection ("BAI") conducted an audit of certain Korean government agencies and the tobacco industry into whether inventory movements ahead of the January 1, 2015 increase of cigarette-related taxes by tobacco companies, including Philip Morris Korea Inc. ("PM Korea"), our South Korean subsidiary, were in compliance with South Korean tax laws. In November 2016, the tax authorities completed their audit and assessed allegedly underpaid taxes and penalties. In order to avoid nonpayment financial costs, PM Korea paid approximately KRW 272 billion (approximately $227 million), of which KRW 100 billion (approximately $83 million) was paid in 2016 and KRW 172 billion (approximately $143 million) was paid in the first quarter of 2017. These paid amounts are included in other assets in the consolidated balance sheets and negatively impacted net cash provided by operating activities in the consolidated statements of cash flows in the period of payment. PM Korea appealed the assessments. In January 2020, a trial court ruled that PM Korea did not underpay taxes in the amount of approximately KRW 218 billion (approximately $182 million). The tax authorities appealed this decision to the appellate court. In September 2020, the appellate court upheld the trial court's decision. The tax authorities have appealed to the Supreme Court of South Korea. In June 2020, another trial court ruled that PM Korea did not underpay approximately KRW 54 billion (approximately $45 million) of alleged underpayments. The government agencies appealed this decision. In January 2021, the appellate court upheld the trial court's decision. The government agencies appealed to the Supreme Court of South Korea. If the tax authorities and government agencies ultimately lose, then they would be required to return the paid amounts to PM Korea.

The Moscow Tax Inspectorate for Major Taxpayers ("MTI") conducted an audit of AO Philip Morris Izhora ("PM Izhora"), our Russian subsidiary, for the 2015-2017 financial years. On July 26, 2019, MTI issued its initial assessment, claiming that intercompany sales of cigarettes between PM Izhora and another Russian subsidiary prior to excise tax increases and submission by PM Izhora of the maximum retail sales price notifications for cigarettes to the tax authorities were improper under Russian tax laws and resulted in underpayment of excise taxes and VAT. In August 2019, PM Izhora submitted its objections disagreeing with MTI's allegations set forth in the initial assessment and MTI's methodology for calculating the alleged underpayments. MTI accepted some of PM Izhora's arguments, and in September 2019, issued the final tax assessment claiming an underpayment of RUB $24.3 billion (approximately $374 million), including penalties and interest. In accordance with Russian tax laws, PM Izhora paid the entire amount of MTI's final assessment. This amount was neither imposed on, nor concurrent with, the specific revenue-producing transaction, nor was it collected from customers of our Russian subsidiaries. In the third quarter of 2019, PMI recorded a pre-tax charge of $374 million, in marketing, administration and research costs in the condensed consolidated statements of earnings, representing $315 million net of an associated income tax benefit of $59 million.

The Saudi Arabia Customs General Authority issued its assessments requiring our distributors to pay additional customs duties in the amount of approximately 1.5 billion Saudi Riyal, or approximately $396 million, in relation to the fees paid by these distributors under their agreements with our subsidiary for exclusive rights to distribute our products in Saudi Arabia. In order to challenge these assessments, the distributors posted bank guarantees. To enable

the distributors' challenge, our subsidiary agreed with the banks to bear a portion of the amount the authority may draw on the bank guarantees. In September and October 2020, respectively, the distributors lost their challenges of the assessments. Both distributors appealed, and in June 2021, the Customs Appeal Committee in Riyadh notified the distributors of its decisions to largely reject their appeals. On the basis of the above-mentioned decisions, in June 2021, PMI recorded a pre-tax charge of $246 million in relation to the period of 2014 through 2020 in line with existing and contemplated arrangements with the distributors. The estimated amounts for 2021 are immaterial. In accordance with U.S. GAAP, the charge was recorded as a reduction in net revenues on the consolidated statements of earnings for the three months and six months ended June 30, 2021. Despite the unfavorable decisions, our subsidiary believes that customs duties paid in Saudi Arabia were in compliance with the applicable law and the WTO Customs Valuation Agreement.

A putative shareholder class action lawsuit, *In re Philip Morris International Inc. Securities Litigation*, is pending in the United States District Court for the Southern District of New York, purportedly on behalf of purchasers of Philip Morris International Inc. stock between July 26, 2016 and April 18, 2018. The lawsuit names Philip Morris International Inc. and certain officers and employees as defendants and includes allegations that the defendants made false and/or misleading statements and/or failed to disclose information about PMI's business, operations, financial condition, and prospects, related to product sales of, and alleged irregularities in clinical studies of, PMI's Platform 1 product. The lawsuit seeks various forms of relief, including damages. In November 2018, the court consolidated three putative shareholder class action lawsuits with similar allegations previously filed in the Southern District of New York (namely, *City of Westland Police and Fire Retirement System v. Philip Morris International Inc., et al., Greater Pennsylvania Carpenters' Pension Fund v. Philip Morris International Inc., et al., and Gilchrist v. Philip Morris International Inc., et al.*) into these proceedings. A putative shareholder class action lawsuit, *Rubenstahl v. Philip Morris International Inc., et al.*, that had been previously filed in December 2017 in the United States District Court for the District of New Jersey, was voluntarily dismissed by the plaintiff due to similar allegations in these proceedings. On February 4, 2020, the court granted defendants' motion in its entirety, dismissing all but one of the plaintiffs' claims with prejudice. The court noted that one of plaintiffs' claims (allegations relating to four non-clinical studies of PMI's Platform 1 product) did not state a viable claim but allowed plaintiffs to replead that claim by March 3, 2020. On February 18, 2020, the plaintiffs filed a motion for reconsideration of the court's February 4th decision; this motion was denied on September 21, 2020. On September 28, 2020, plaintiffs filed an amended complaint seeking to replead allegations relating to four non-clinical studies of PMI's Platform 1 product. On September 10, 2021, the court granted defendant's motion to dismiss plaintiffs' amended complaint in its entirety. On October 8, 2021, the plaintiffs filed a Notice of Appeal to the U.S. Court of Appeal for the Second Circuit. We believe that this lawsuit is without merit and will continue to defend it vigorously.

In April 2020, affiliates of British American Tobacco plc ("BAT") commenced patent infringement proceedings, *RAI Strategic Holdings, Inc., et al. v. Altria Client Services LLC, et al.*, in the federal court in the Eastern District of Virginia, where PMI's subsidiary, Philip Morris Products S.A., as well as Altria Group, Inc.'s subsidiaries, are defendants. Plaintiffs seek damages and injunctive relief against the commercialization of the Platform 1 products in the United States. In April 2020, BAT affiliates filed a complaint against PMI, Philip Morris Products S.A., Altria Group, Inc., and its subsidiaries before the International Trade Commission ("ITC"). Plaintiffs seek an order to prevent the importation of Platform 1 products into the United States. The ITC evidentiary hearing closed on February 1, 2021. On May 14, 2021, the administrative law judge issued an Initial and Recommended Determination ("ID/RD") finding that the Platform 1 product infringes two of the three patents asserted by Plaintiffs, recommending that the ITC issue a Limited Exclusion order against infringing products, and recommending against a cease-and-desist, as well as recommending against a bond pending Presidential review of the ITC's Final Determination ("FD"). Defendants and Plaintiffs filed separate Petitions for Review with the ITC of the ID on May 28, 2021; on July 27, 2021, the ITC granted each of the petitions in part, deciding to review certain issues in the ID. Plaintiffs and Defendants also submitted brief statements of the public interest factors in issue to the ITC on June 15, 2021. On September 29, 2021, the ITC issued its FD finding a violation of section 337 of the U.S. Tariff Act and issued (a) a limited exclusion order against Philip Morris Products S.A., prohibiting, inter alia, the importation of Platform 1 product and infringing components; and (b) a cease-and-desist order against Altria Client Services, LLC and its affiliate prohibiting, inter alia, sales of imported Platform 1 products. The ITC predicated the orders on its finding that Platform 1 products infringe two patents owned by a BAT affiliate. The ITC also found that Platform 1 products do not infringe a third patent owned by a BAT affiliate. The ITC further held that there were insufficient concerns over public interest to prevent the issuance of remedial orders. Following the Presidential Review period, the orders became effective and Defendants filed a petition for review of the FD with the U.S. Court of Appeals for the Federal Circuit. Defendants also filed motions in the ITC and Federal Circuit for a stay of the orders pending disposition of the appeal; the ITC denied the motion on January 20, 2022 and the Federal Circuit denied the motion on January 25, 2022. We estimate that an adverse ruling is probable due to our inability to import the products and components impacted by the ITC's FD with immaterial financial impact. In the Eastern District of Virginia case, the defendants also counterclaimed that BAT infringed their patents relating to certain e-vapor products, seeking damages for, and injunctive relief against, the commercialization of these products by BAT; defendants' claims against BAT are set for trial beginning the week of June 6, 2022. Upon petition of Philip Morris Products S.A., the Patent Trial and Appeal Board ("PTAB") of the United States Patent and Trademark Office has instituted review of certain claims pertaining to four of the six patents asserted by BAT affiliates in both proceedings. On January 11, 2022, PTAB issued its final decision on one of the two patents underlying the ITC's FD, invalidating all challenged claims of BAT's patent. We expect PTAB's final decision on the second of the two BAT patents underlying the ITC's FD to arrive on or before April 2, 2022; the parties may appeal PTAB results to the U.S. Court of Appeals for the Federal Circuit.

In April 2020, BAT's affiliate commenced patent infringement proceedings, *Nicoventures Trading Limited v. PM GmbH, et al.,* against PMI's German subsidiary, Philip Morris GmbH, and Philip Morris Products S.A., in the Regional Court in Munich, Germany. Plaintiffs seek damages and injunctive relief against the commercialization of the Platform 1 products in Germany. In June 2021, the court stayed the proceeding in respect of one of the two patents asserted by BAT's Affiliate.

In September 2020, BAT's affiliates commenced patent infringement and unfair competition proceedings, *RAI Strategic Holdings, Inc., et al. v. Philip Morris Products S.A., et al.*, against Philip Morris Products S.A. and PMI's Italian subsidiaries, Philip Morris Manufacturing & Technology Bologna S.p.A. and Philip Morris Italia S.r.l., in the Court of Milan, Italy. Plaintiffs seek damages, as well as injunctive relief against the manufacture in Italy of the Platform 1 heated tobacco units allegedly infringing the asserted patents and the commercialization of the Platform 1 products in Italy. As part of this proceeding, in October 2020, BAT's affiliates filed a

request based on one of the two asserted patents seeking preliminary injunctive relief against the manufacture and commercialization of the Platform 1 products in Italy.

In October 2020, BAT's affiliates commenced patent infringement proceedings, *RAI Strategic Holdings, Inc., et al. v. Philip Morris Japan, Limited*, *et al*., against PMI's Japanese subsidiary, Philip Morris Japan Limited, and a third-party distributor in the Tokyo District Court. Plaintiffs seek damages and injunctive relief against the commercialization of the Platform 1 products in Japan.

In November 2020, BAT's affiliates commenced patent infringement proceedings, *RAI Strategic Holdings, Inc., et al. v. Philip Morris Romania SRL, et al.*, against PMI's Romanian subsidiaries, Philip Morris Romania S.R.L. and Philip Morris Trading S.R.L., and a third-party distributor in the Court of Law of Bucharest, Civil Registry. Plaintiffs seek damages and preliminary and permanent injunctive relief against the manufacture and commercialization of the Platform 1 products in Romania. In February 2021, the court dismissed plaintiffs' request for a preliminary injunction. In April 2021, the appellate court denied plaintiffs' appeal, confirming the dismissal of plaintiffs' request for preliminary injunction. Plaintiffs' proceeding requesting damages and a permanent injunction remains pending before the Court of Law of Bucharest, Civil Registry. In an October 14, 2021 hearing, the court stayed the proceeding.

In March 2021, BAT's affiliates commenced patent infringement proceedings, *RAI Strategic Holdings, Inc., et al. v. Philip Morris Korea, Co., Ltd.,* against PM Korea in the Seoul Central District Court. Plaintiffs seek damages and injunctive relief against the commercialization of the Platform 1 heated tobacco units in South Korea.

Other patent challenges by both parties are pending in various jurisdictions.

We believe that the foregoing proceedings by the affiliates of BAT are without merit and will defend them vigorously.

We are also involved in additional litigation arising in the ordinary course of our business. While the outcomes of these proceedings are uncertain, management does not expect that the ultimate outcomes of other litigation, including any reasonably possible losses in excess of current accruals, will have a material adverse effect on our consolidated results of operations, cash flows or financial position.

Third-Party Guarantees

On October 17, 2020, Medicago Inc., an equity method investee of Philip Morris Investments B.V. ("PMIBV"), a PMI subsidiary, entered into a contribution agreement with the Canadian government (the "Contribution Agreement") whereby the Canadian government agreed to contribute up to CAD 173 million (approximately $131 million on the date of signing) to Medicago Inc., to support its on-going COVID-19 vaccine development and clinical trials, and for the construction of its Quebec City manufacturing facility (the "Project"). PMIBV and the majority shareholder of Medicago Inc. are also parties to the Contribution Agreement as guarantors of Medicago Inc.'s obligations thereunder on a joint and several basis ("Co-Guarantors"). The Co-Guarantors agreed to repay amounts contributed by the Canadian government plus interest, if Medicago Inc. fails to do so, and could be responsible for the costs of other Medicago's obligations (such as the achievement of specific milestones of the Project). The maximum amount of these obligations is currently non-estimable. As of December 31, 2021, PMI has determined that these guarantees did not have a material impact on its consolidated financial statements.

In connection with the Contribution Agreement, PMIBV and the majority shareholder of Medicago Inc. entered into a guarantors' agreement that apportions Co-Guarantors' obligations and limits those of PMIBV to its share of holdings in Medicago Inc. During 2021, Medicago Inc. initiated additional rounds of equity funding in which PMIBV did not participate. As a result, PMIBV's share of holdings in Medicago Inc. was reduced from approximately 32% to approximately 23% as of December 31, 2021. The guarantees are in effect through March 31, 2026.

Note 18.

Sale of Accounts Receivable:

To mitigate risk and enhance cash and liquidity management PMI sells trade receivables to unaffiliated financial institutions. These arrangements allow PMI to sell, on an ongoing basis, certain trade receivables without recourse. The trade receivables sold are generally short-term in nature and are removed from the consolidated balance sheets. PMI sells trade receivables under two types of arrangements, servicing and non-servicing. For servicing arrangements, PMI continues to service the sold trade receivables on an administrative basis and does not act on behalf of the unaffiliated financial institutions. When applicable, a servicing liability is recorded for the estimated fair value of the servicing. The amounts associated with the servicing liability were not material for the

years ended December 31, 2021 and 2020. Under the non-servicing arrangements, PMI does not provide any administrative support or servicing after the trade receivables have been sold to the unaffiliated financial institutions.

Cumulative trade receivables sold, including excise taxes, for the years ended December 31, 2021 and 2020, were $11.8 billion and $11.5 billion, respectively. PMI's operating cash flows were positively impacted by the amount of the trade receivables sold and derecognized from the consolidated balance sheets, which remained outstanding with the unaffiliated financial institutions. The trade receivables sold that remained outstanding under these arrangements as of December 31, 2021, 2020 and 2019, were $0.9 billion, $1.2 billion and $0.9 billion, respectively. The net proceeds received are included in cash provided by operating activities in the consolidated statements of cash flows. The difference between the carrying amount of the trade receivables sold and the sum of the cash received is recorded as a loss on sale of trade receivables within marketing, administration and research costs in the consolidated statements of earnings. For the years ended December 31, 2021, 2020 and 2019 the loss on sale of trade receivables was immaterial.

Note 19.

Asset Impairment and Exit Costs:

For the years ended December 31, 2021, 2020 and 2019, PMI recorded total pre-tax asset impairment and exit costs of $216 million, $149 million and $422 million, respectively. The total pre-tax asset impairment and exit costs were included in marketing, administration and research costs on the consolidated statements of earnings.

South Korea

In the first quarter of 2021, PM Korea commenced the implementation of a new business operating model, which requires the restructuring of its current distribution agreements. As a result, PMI recorded exit costs of $57 million in the year ended December 31, 2021, related to contract terminations and restructuring with certain distributors.

Organizational Design Optimization

As part of PMI's transformation to a smoke-free future, PMI seeks to optimize its organizational design, which includes the elimination, relocation and outsourcing of certain operations center and centralized activities. In January 2020, PMI commenced a multi-phase restructuring project in Switzerland. PMI initiated the employee consultation procedures, as required under Swiss law, for the impacted employees. The consultation procedures for the first two phases were completed in 2020 with the final phases initiated and completed in 2021. Additionally, since the commencement of this multi-phase restructuring project in 2020, PMI launched a voluntary separation program in Switzerland for certain eligible employees and announced the outsourcing of certain activities in Argentina, Indonesia, Poland and the United States. This multi-phase restructuring project was completed in the fourth quarter of 2021.

For the years ended December 31, 2021 and 2020, PMI recorded pre-tax charges of $159 million and $149 million, respectively, related to the organizational design optimization. Since inception of this multi-phase restructuring project in January 2020 through December 31, 2021, approximately 1,020 positions in total were impacted, resulting in cumulative pre-tax charges of $308 million related to the organizational design optimization program. Of this cumulative pre-tax amount, $300 million related to separation program charges and $8 million related to asset impairment charges.

Global Manufacturing Infrastructure Optimization

In light of declining PMI cigarette volumes resulting from lower total industry volumes and the shift to smoke-free alternatives, PMI continues to optimize its global manufacturing infrastructure. During 2019, PMI recorded asset impairment and exit costs related to plant closures in Argentina, Colombia, Germany and Pakistan as part of its global manufacturing infrastructure optimization.

Germany

On November 4, 2019, PMI announced that, as part of its global manufacturing infrastructure optimization, its German affiliate, Philip Morris Manufacturing GmbH ("PMMG"), reached an agreement with employee representatives to end cigarette production in its factory in Berlin, Germany, by January 1, 2020. As a result of this agreement, during 2019, PMI recorded pre-tax asset impairment and exit costs of $342 million in the European Union segment. This amount included pension and employee separation costs of $251 million, which are paid in cash, and asset impairment costs of $91 million, primarily related to machinery and equipment, which were non-cash charges.

Other

During 2019, PMI also recorded pre-tax asset impairment and exit costs of $80 million as part of its global manufacturing infrastructure optimization. These costs were related to cigarette plant closures in Argentina ($15 million), Colombia ($45 million) and Pakistan ($20 million). The charges were reflected in the Americas segment (Argentina and Colombia) and the South & Southeast Asia segment (Pakistan).

Asset Impairment and Exit Costs by Segment

During 2021, 2020 and 2019, PMI recorded the following pre-tax asset impairment and exit costs by segment:

(in millions)	**2021**	**2020**	**2019**
Separation programs: [1]			
European Union	**$ 68**	$ 53	$ 251
Eastern Europe	**14**	14	—
Middle East & Africa	**17**	18	—
South & Southeast Asia	**21**	22	3
East Asia & Australia	**31**	25	—
Americas	**8**	9	49
Total separation programs	**159**	141	303
Contract termination charges:			
East Asia & Australia	**57**	—	—
Total contract termination charges	**57**	—	—
Asset impairment charges [1]			
European Union	**—**	4	91
Eastern Europe	**—**	1	—
Middle East & Africa	**—**	1	—
South & Southeast Asia	**—**	1	17
East Asia & Australia	**—**	1	—
Americas	**—**	—	11
Total asset impairment charges	**—**	8	119
Asset impairment and exit costs	**$ 216**	149	422

[1] Organizational design optimization pre-tax charges in 2021 and 2020 were allocated across all geographical segments.

Movement in Exit Cost Liabilities

The movement in exit cost liabilities for the year ended December 31, 2021 was as follows:

(in millions)	
Liability balance, January 1, 2021	$ 180
Charges, net	216
Cash spent	(238)
Currency/other	(16)
Liability balance, December 31, 2021	$ 142

Future cash payments for exit costs incurred to date are anticipated to be substantially paid by the end of 2023.

Note 20.

Deconsolidation of RBH:

As discussed in Note 17. *Contingencies,* following the March 1, 2019, judgment of the Court of Appeal of Québec in two class action lawsuits against PMI's Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH"), PMI recorded in its consolidated results a pre-tax charge of $194 million, representing $142 million net of tax, in the first quarter of 2019. This pre-tax Canadian tobacco litigation-related expense was included in marketing, administration and research costs on PMI's consolidated statement of earnings for the year ended December 31, 2019. The charge reflects PMI's assessment of the portion of the judgment that represents probable and estimable loss prior to the deconsolidation of RBH and corresponds to the trust account deposit required by the judgment. RBH's share of the deposit is approximately CAD 257 million.

On March 22, 2019, RBH obtained an initial order from the Ontario Superior Court of Justice granting it protection under the Companies' Creditors Arrangement Act ("CCAA"), which is a Canadian federal law that permits a Canadian business to restructure its affairs while carrying on its business in the ordinary course with minimal disruption to its customers, suppliers and employees.

The administration of the CCAA process, principally relating to the powers provided to the court and the court appointed monitor, removes certain elements of control of the business from both PMI and RBH. As a result, PMI has determined that it no longer has a controlling financial interest over RBH as defined in ASC 810 (Consolidation), and PMI deconsolidated RBH as of the date of the CCAA filing. PMI has also determined that it does not exert "significant influence" over RBH as that term is defined in ASC 323 (Investments-Equity Method and Joint Ventures). Therefore, as of March 22, 2019, PMI accounted for its continuing investment in RBH in accordance with ASC 321 (Investments-Equity Securities) as an equity security, without readily determinable fair value.

Following the deconsolidation, the carrying value of assets and liabilities of RBH was removed from the consolidated balance sheet of PMI, and the continuing investment in RBH was recorded at fair value at the date of deconsolidation. The total amount deconsolidated from PMI's balance sheet was $3,519 million, including $1,323 million of cash, $1,463 million of goodwill, $529 million of accumulated other comprehensive earnings, primarily related to historical currency translation and $204 million of other assets and liabilities, net. While PMI is accounting for its investment in RBH as an equity security, PMI would recognize dividends as income upon receipt. However, while it remains under creditor protection, RBH does not anticipate paying dividends.

The fair value of PMI's continuing investment in RBH of $3,280 million was determined at the date of deconsolidation, recorded within equity investments and is assessed for impairment on an ongoing basis. The estimated fair value of the underlying business was determined based on an income approach using a discounted cash flow analysis, as well as a market approach for certain contingent liabilities. The information used in the estimate includes observable inputs, primarily a discount rate of 8%, a terminal growth rate of 2.5% and information about total tobacco market size in Canada and RBH's share of the market, as well as unobservable inputs such as operating budgets and strategic plans, various inflation scenarios, estimated shipment volumes, and expected product pricing and projected margins.

The difference between the carrying value of the assets and liabilities of RBH that were deconsolidated and the fair value of the continuing investment, as determined at the date of deconsolidation, was $239 million, before tax, and this loss on deconsolidation is reflected within marketing, administration and research costs on PMI's consolidated statement of earnings for the year ended December 31, 2019. PMI also recorded a tax benefit of $49 million within the provision for income taxes for the year ended December 31, 2019, related to the reversal of a deferred tax liability on unremitted earnings of RBH.

RBH is party to transactions with PMI and its consolidated subsidiaries entered into in the normal course of business; these transactions include royalty payments and recharge of various corporate expenses for services benefiting RBH. Up to the date of the CCAA filing, these transactions were eliminated on consolidation and had no impact on PMI's consolidated statement of earnings. After deconsolidating RBH, these transactions are treated as third-party transactions in PMI's financial statements. The amount of these related-party transactions is included within Note 4. *Related Parties - Equity investments and Other.*

Developments in the CCAA process, including resolution through a plan of arrangement or compromise of all pending tobacco-related litigation currently stayed in Canada, as discussed in Note 17. *Contingencies*, could result in a material change in the fair value of PMI's continuing investment in RBH.

Note 21.

Leases:

PMI has operating and finance leases that are principally for real estate (office space, warehouses and retail store space), machinery and equipment, and vehicles. Lease terms range from 1 year to 72 years, some of which include options to renew, which are reasonably certain to be renewed. Lease terms may also include options to terminate the lease. The exercise of a lease renewal or termination option is at PMI's discretion.

PMI's operating and finance leases at December 31, 2021 and 2020, were as follows:

	At December 31,		
(in millions)	**2021**		
	Operating Leases	Finance Leases	Operati Lease
Assets:			
Machinery and equipment	**$ — $**	**108**	$
Other assets	**526**	**—**	
Total lease assets	**$ 526 $**	**108**	$
Liabilities:			
Current			
Current portion of long-term debt	**$ — $**	**48**	$
Accrued liabilities - Other	**192**	**—**	
Noncurrent			
Long-term debt	**—**	**23**	
Income taxes and other liabilities	**344**	**—**	
Total lease liabilities	**$ 536 $**	**71**	$

The components of PMI's lease cost were as follows for the years ended December 31, 2021, 2020 and 2019:

	For the Years Ended I		
(in millions)	**2021**		**2020**
Operating lease cost	**$ 259**	$	
Finance lease cost:			
Amortization of right-of-use assets	**54**		
Interest on lease liabilities	**1**		
Short-term lease cost	**55**		
Variable lease cost	**25**		
Total lease cost	**$ 394**	$	

Maturity of PMI's lease liabilities, on an undiscounted basis, as of December 31, 2021, were as follows:

(in millions)	Operating Leases	Finance Leases
2022	$ 215	$ 49
2023	131	18
2024	84	2
2025	54	1
2026	24	1
Thereafter	140	1
Total lease payments	648	72
Less: Interest	112	1
Present value of lease liabilities	$ 536	$ 71

Other information related to PMI's leases was as follows for the year ended December 31, 2021, 2020 and 2019:

	December 31,					
(in millions)	2021		2020		2019	
	Operating Leases	Finance Leases	Operating Leases	Finance Leases	Operating Leases	Finance Leases
Cash paid for amounts included in the measurement of lease liabilities in operating cash flows [1]	$ 259	$ —	$ 238	$ —	$ 240	$ —
Cash paid for amounts included in the measurement of lease liabilities in financing cash flows	$ —	$ 26	$ —	$ 19	$ —	$ 1
Leased assets obtained in exchange for new lease liabilities	$ 64	$ 89	$ 149	$ 32	$ 221	$ 3
Weighted-average remaining lease term (years)	8.3	1.7	10.1	1.6	9.6	2.
Weighted-average discount rate[2] [3]	3.6 %	5.3 %	4.3 %	6.7 %	4.4 %	7.

[1] Cash paid included in the operating cash flows of finance leases is not material.
[2] PMI's weighted-average discount rate for operating leases is based on its estimated pre-tax cost of debt adjusted for country-specific risk.
[3] PMI's weighted-average discount rate for finance leases, excluding embedded leases, is based on its estimated pre-tax cost of debt adjusted for country-specific risk and where applicable the interest rate explicit to lease contracts.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of
Philip Morris International Inc.:

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Philip Morris International Inc. and its subsidiaries (the "Company") as of December 31, 2021 and 2020, and the related consolidated statements of earnings, comprehensive earnings, stockholders' (deficit) equity and cash flows for each of the three years in the period ended December 31, 2021, including the related notes (collectively referred to as the "consolidated financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2021, based on criteria established in *Internal Control - Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2021 and 2020, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2021 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2021, based on criteria established in *Internal Control - Integrated Framework* (2013) issued by the COSO.

Basis for Opinions

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Report of Management on Internal Control over Financial Reporting. Our responsibility is to express opinions on the Company's consolidated financial statements and on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly

reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Critical Audit Matters

The critical audit matter communicated below is a matter arising from the current period audit of the consolidated financial statements that was communicated or required to be communicated to the audit committee and that (i) relates to accounts or disclosures that are material to the consolidated financial statements and (ii) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the consolidated financial statements, taken as a whole, and we are not, by communicating the critical audit matter below, providing a separate opinion on the critical audit matter or on the accounts or disclosures to which it relates.

Tobacco-Related Litigation for Smoking and Health Class Actions and Health Care Cost Recovery Actions

As described in Note 17 to the consolidated financial statements, the Company has 9 smoking and health class actions and 17 health care cost recovery actions pending. The Company records provisions in the consolidated financial statements for pending litigation when management determines that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. Except as stated otherwise in Note 17, while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available, (i) management has not concluded that it is probable that a loss has been incurred in any of the pending smoking and health class actions and health care cost recovery cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending smoking and health class actions and health care cost recovery cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any.

The principal considerations for our determination that performing procedures relating to tobacco-related litigation for smoking and health class actions and health care cost recovery actions is a critical audit matter are that there was significant judgment by management when determining the probability of a loss being incurred and an estimate of the amount or range of the potential loss for each case, which in turn led to a high degree of auditor subjectivity, judgment and effort in evaluating management's assessment related to the loss contingencies associated with smoking and health class actions and health care cost recovery actions related claims.

Addressing the matter involved performing procedures and evaluating audit evidence in connection with forming our overall opinion on the consolidated financial statements. These procedures included testing the effectiveness of controls relating to management's evaluation of smoking and health class actions and health care cost recovery actions, including controls over determining the probability and range of loss as well as controls over financial statement disclosures. These procedures also included, among others, obtaining and evaluating the letters of audit inquiry with external and internal legal counsel, evaluating the reasonableness of management's assessment regarding whether an unfavorable outcome is reasonably possible or probable and reasonably estimable, and evaluating the sufficiency of the Company's smoking and health class actions and health care cost recovery actions contingencies disclosures.

/S/ PRICEWATERHOUSECOOPERS SA

PricewaterhouseCoopers SA

Lausanne, Switzerland
February 11, 2022

We have served as the Company's auditor since 2008.

Report of Management on Internal Control Over Financial Reporting

Management of Philip Morris International Inc. ("PMI") is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended. PMI's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes those written policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of PMI;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America;
- provide reasonable assurance that receipts and expenditures of PMI are being made only in accordance with the authorization of management and directors of PMI; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets that could have a material effect on the consolidated financial statements.

Internal control over financial reporting includes the controls themselves, monitoring and internal auditing practices and actions taken to correct deficiencies as identified.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of PMI's internal control over financial reporting as of December 31, 2021. Management based this assessment on criteria for effective internal control over financial reporting described in *Internal Control — Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management's assessment included an evaluation of the design of PMI's internal control over financial reporting and testing of the operational effectiveness of its internal control over financial reporting. Management reviewed the results of its assessment with the Audit Committee of our Board of Directors.

Based on this assessment, management determined that, as of December 31, 2021, PMI maintained effective internal control over financial reporting.

PricewaterhouseCoopers SA, an independent registered public accounting firm, who audited and reported on the consolidated financial statements of PMI included in this report, has audited the effectiveness of PMI's internal control over financial reporting as of December 31, 2021, as stated in their report herein.

February 11, 2022

Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.*

None.

Item 9A. *Controls and Procedures.*

PMI carried out an evaluation, with the participation of PMI's management, including PMI's Chief Executive Officer and Chief Financial Officer, of the effectiveness of PMI's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based upon that evaluation, PMI's Chief Executive Officer and Chief Financial Officer concluded that PMI's disclosure controls and procedures are effective. There have been no changes in PMI's internal control over financial reporting during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, PMI's internal control over financial reporting.

The Report of Management on Internal Control over Financial Reporting and the Report of Independent Registered Public Accounting Firm are included in Item 8.

Item 9B. Other Information.

None.

Item 9C. Disclosure Regarding Foreign Jurisdictions that Prevent Inspections.

Not applicable.

PART III

Except for the information relating to the executive officers set forth in Item 10 and the information relating to equity compensation plans set forth in Item 12, the information called for by Items 10-14 is hereby incorporated by reference to PMI's definitive proxy statement for use in connection with its annual meeting of stockholders to be held on May 4, 2022, that will be filed with the SEC on or about March 24, 2022 (the "proxy statement"), and, except as indicated therein, made a part hereof.

Item 10. *Directors, Executive Officers and Corporate Governance.*

Information About Our Executive Officers as of February 10, 2022:

Name	Office	Age
Jacek Olczak	Chief Executive Officer	57
Drago Azinovic	President, Middle East & Africa Region and PMI Duty Free	59
Emmanuel Babeau	Chief Financial Officer	54
Werner Barth	President Combustibles Category & Global Combustibles Marketing	57
Frederic de Wilde	President, European Union Region	54
Reginaldo Dobrowolski	Vice President and Controller	47
Suzanne Rich Folsom	Senior Vice President and General Counsel	60
Stacey Kennedy	President, South and Southeast Asia Region	49
Marco Mariotti	President, Eastern Europe Region	57
Deepak Mishra	President. Americas Region	50
Paul Riley	President, East Asia and Australia Region	56
Stefano Volpetti	President Smoke-Free Products Category & Chief Consumer Officer	50

Jacek Olczak – Age 57

Mr. Olczak was appointed as our Chief Executive Officer in May 2021. From January 2018 until May 2021, Mr. Olczak has served as our Chief Operating Officer, and from August 2012 until January 2018, he served as our Chief Financial Officer. He joined the

Company's Polish affiliate in 1993 and progressed through various roles in finance and general management positions across Europe, including as Managing Director of PMI's markets in Poland and Germany and as President of the European Union Region, before being appointed Chief Financial Officer. Prior to joining PMI, Mr. Olczak worked for BDO, an international network of public accounting, tax, consulting and business advisory firms.

Drago Azinovic – Age 59

Mr. Azinovic was appointed as our President, Middle East & Africa Region and PMI Duty Free in January 2018. From July 2015 until January 2018, Mr. Azinovic was our President Eastern Europe, Middle East and Africa and Global Duty Free. Mr. Azinovic also served as our President of the European Union Region, a position he held from August 2012 to July 2015, as well as the President of Philip Morris Japan, from July 2011 to August 2012. Prior to joining Philip Morris Asia Limited in March 2009 as Vice President of Marketing and Sales for Philip Morris International's Asia Region, Mr. Azinovic held a variety of positions at The Procter & Gamble Company ("Procter & Gamble"), a multinational consumer goods company, and Altadis, a tobacco company, and, after the acquisition of Altadis in 2008, at Imperial Tobacco, a tobacco company.

Emmanuel Babeau – Age 54

Mr. Babeau was appointed as our Chief Financial Officer in May 2020. Prior to joining PMI in May 2020, Mr Babeau served as the Deputy Chief Executive Officer of Schneider Electric, an energy and automation digital solutions company. In this position he was in charge of Finance and Legal Affairs. Mr. Babeau joined Schneider Electric in 2009 as Executive Vice President Finance and a member of the Management Board. Mr. Babeau also served on the board of Sanofi S.A., a French multinational healthcare company, from 2018 to 2020. Mr. Babeau started his career in 1990 at Arthur Andersen and from 1993 to 2009 he progressed through various positions at Pernod Ricard, a beverage company, the latest being Chief Financial Officer and Group Deputy Managing Director. Mr. Babeau also served as a non-executive director at Sodexo, a French food services and facilities management company, from January 2016 until December 2021.

Werner Barth – Age 57

Mr. Barth was appointed as our President Combustibles Category & Global Combustibles Marketing in November 2021. Mr. Barth joined PMI in 1990 as Marketing Trainee at Philip Morris Germany and throughout his career he progressed through various roles at PMI in marketing, product management, brand supervision and general management. Prior to his current position, from 2015 Mr. Barth held the role of Senior Vice President, Marketing & Sales, and from 2018, he held the role of Senior Vice President, Commercial.

Frederic de Wilde – Age 54

Mr. de Wilde was appointed as our President, European Union Region in July 2015. Mr. de Wilde joined PMI in 1992 as Brand Manager L&M at Philip Morris Belgium and throughout his career he progressed through various roles at PMI in marketing, sales and general management. Prior to his current position, from July 2011 until July 2015, Mr. de Wilde held the role of Senior Vice President, Marketing & Sales.

Reginaldo Dobrowolski – Age 47

Mr. Dobrowolski was appointed as our Vice President & Controller in August 2021. From May 2019 until August 2021, Mr. Dobrowolski was our Vice President Corporate Financial Planning, Data & Reporting. Prior to that, Mr. Dobrowolski held various roles in our Finance department, including Director Corporate Financial Planning & Reporting from October 2014 until May 2019.

Suzanne Rich Folsom - Age 60

Ms. Folsom was appointed as our Senior Vice President and General Counsel in July 2020. She is responsible for all legal, compliance and governance matters at PMI. From March 2019 until July 2020, Ms. Folsom was a Partner and Co-Chair of the Investigations, Compliance and Strategic Response Group at Manatt, Phelps & Phillips, LLP, a law firm. From 2014 to 2018, Ms. Folsom served as the General Counsel, Chief Compliance Officer and Senior Vice President, Government Affairs and Global Public Policy at United States Steel Corporation, an American integrated

steel producer. Ms. Folsom is an accomplished C-suite executive and attorney with deep experience advising management and boards of directors.

Stacey Kennedy – Age 49

Ms. Kennedy was appointed as our President, South and Southeast Asia Region in January 2018. From 2015 until her current appointment, Ms. Kennedy served as Managing Director for Germany, Austria, Croatia, and Slovenia. Ms. Kennedy began her career with Philip Morris USA in 1995 as a Territory Sales Manager. Throughout her career she held a number of positions of increasing responsibility in sales and general management.

Marco Mariotti – Age 57

Mr. Mariotti was appointed as our President, Eastern Europe Region in January 2018. From 2015 until his current appointment, Mr. Mariotti served as Senior Vice President, Corporate Affairs. Since joining PMI in 1997, Mr. Mariotti has held numerous leadership roles in Argentina and across Europe, such as President, Russia & Belarus, Managing Director Italy and Managing Director Argentina.

Deepak Mishra - Age 50

Mr. Mishra was appointed as our President, Americas Region in July 2021. Mr. Mishra joined PMI in September 2018, as Senior Vice President and Chief Strategy Officer. From 2014 until September 2018, he was Managing Director, Portfolio Operations at Centerbridge Partners, a private equity firm, where he led commercial, operational, and digital transformation in various business sectors. Prior to Centerbridge Partners, Mr. Mishra was a Partner at McKinsey & Co., a management consulting firm in London, and part of their Consumer Goods, Retail and Operations leadership teams from 2001 to 2014, supporting clients in the FMCG, retail and private equity industries on commercial and operational transformations.

Paul Riley – Age 56

Mr. Riley was appointed as our President, East Asia and Australia Region in January 2018. From 2015 until his current appointment, Mr. Riley served as President of Philip Morris Japan. Mr. Riley joined Philip Morris Australia in 1988. Over the following two decades, he held a number of positions in Australia, Hong Kong, and Japan, before being named Managing Director, Serbia & Montenegro in 2010. Mr. Riley returned to the Asian Region in 2013, when he became President of Philip Morris Fortune Tobacco Corporation in the Philippines.

Stefano Volpetti – Age 50

Mr. Volpetti was appointed as our President Smoke-Free Products Category & Chief Consumer Officer in November 2021. Mr. Volpetti joined PMI in June 2019 as Chief Consumer Officer. From February 2016 until May 2019, Mr. Volpetti served as the Vice President & Brand Franchise Leader of a multi-functional, global business unit at Procter & Gamble, a multinational consumer goods company. Mr. Volpetti spent 22 years at Procter & Gamble, progressing through various roles with increasing responsibility locally in Italy and Mexico, and on a regional level for the European market. Mr. Volpetti also served as Chief Marketing Officer at Luxottica Group S.p.A, an Italian eyewear conglomerate, in 2015.

Codes of Conduct and Corporate Governance

We have adopted a code of conduct, which we call the Guidebook for Success. The Guidebook for Success complies with requirements set forth in Item 406 of Regulation S-K, applies to all of our employees, including our principal executive officer, principal financial officer, principal accounting officer or controller, and persons performing similar functions. We have also adopted a code of business conduct and ethics that applies to the members of our Board of Directors. These documents are available free of charge on our website at www.pmi.com.

In addition, we have adopted corporate governance guidelines and charters for our Audit, Finance, Compensation and Leadership Development, Product Innovation and Regulatory Affairs, Consumer Relationships and Regulation, and Nominating and Corporate Governance committees of the Board of Directors. All of these documents are available free of charge on our website at www.pmi.com. Any waiver granted by Philip Morris International Inc. to its principal executive officer, principal financial officer or controller, or any person performing similar functions under

the Guidebook for Success, or certain amendments to the Guidebook for Success, will be disclosed on our website at www.pmi.com.

The information on our website is not, and shall not be deemed to be, a part of this Report or incorporated into any other filings made with the SEC.

Also refer to *Board Operations and Governance—Committees of the Board*, *Election of Directors—Process for Nominating Directors* and *Election of Directors—Director Nominees* and *Stock Ownership Information—Delinquent Section 16(a) Reports* sections of the proxy statement.

Item 11. *Executive Compensation.*

Refer to *Compensation Discussion and Analysis, Compensation of Directors,* and *Pay Ratio* sections of the proxy statement.

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.*

The number of shares to be issued upon exercise or vesting and the number of shares remaining available for future issuance under PMI's equity compensation plans at December 31, 2021, were as follows:

	Number of Securities to be Issued upon Exercise of Outstanding Options and Vesting of RSUs and PSUs (a)	Weighted Average Exercise Price of Outstanding Options (b)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (excluding Securities reflected in column (a)) (c)
Equity compensation plans approved by stockholders	7,714,804 [1]	$ —	15,746,554

[1] Represents 4,640,764 shares of common stock that may be issued upon vesting of the restricted share units and 3,074,040 shares that may be issued upon vesting of the performance share units if maximum performance targets are achieved for each performance cycle. PMI has not granted options since the spin-off from Altria on March 28, 2008.

Also refer to *Stock Ownership Information—Ownership of Equity Securities* section of the proxy statement.

Item 13. *Certain Relationships and Related Transactions, and Director Independence.*

Refer to *Related Person Transactions and Code of Conduct* and *Election of Directors—Independence of Nominees* sections of the proxy statement.

Item 14. *Principal Accounting Fees and Services.*

Refer to *Audit Committee Matters* section of the proxy statement.

PART IV

Item 15. *Exhibits and Financial Statement Schedules.*

(a) Index to Consolidated Financial Statements and Schedules

	Page
Consolidated Statements of Earnings for the years ended December 31, 2021, 2020 and 2019	65
Consolidated Statements of Comprehensive Earnings for the years ended December 31, 2021, 2020 and 2019	66
Consolidated Balance Sheets at December 31, 2021 and 2020	67 - 68
Consolidated Statements of Cash Flows for the years ended December 31, 2021, 2020 and 2019	69 - 70
Consolidated Statements of Stockholders' (Deficit) Equity for the years ended December 31, 2021, 2020 and 2019	71
Notes to Consolidated Financial Statements	72 - 123
Report of Independent Registered Public Accounting Firm (PCAOB ID 1358)	124 - 125
Report of Management on Internal Control Over Financial Reporting	126

Schedules have been omitted either because such schedules are not required or are not applicable.

(b) The following exhibits are filed as part of this Report:

2.1	—	Distribution Agreement between Altria Group, Inc. and Philip Morris International Inc. dated January 30, 2008 (incorporated by reference to Exhibit 2.1 to the Registration Statement on Form 10 filed February 7, 2008).
2.2	—	Share Sale and Purchase Agreement by and among Claudio Topco B.V., Bagger-Sorenson & Co. A/S and PMI Global Services, Inc., dated June 30, 2021 (portions of this Exhibit 2.1 have been omitted) (incorporated by reference to Exhibit 2.1 to the Current Report on Form 8-K filed July 7, 2021).
3.1	—	Amended and Restated Articles of Incorporation of Philip Morris International Inc. (incorporated by reference to Exhibit 3.1 to the Registration Statement on Form 10 filed February 7, 2008).
3.2	—	Amended and Restated By-Laws of Philip Morris International Inc., effective as of February 4, 2021 (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed February 9, 2021).
4.1	—	Specimen Stock Certificate of Philip Morris International Inc. (incorporated by reference to Exhibit 4.1 to the Registration Statement on Form 10 filed February 7, 2008).
4.2	—	Indenture dated as of April 25, 2008, between Philip Morris International Inc. and HSBC Bank USA, National Association, as Trustee (incorporated by reference to Exhibit 4.3 to the Registration Statement on Form S-3, dated April 25, 2008).
4.3	—	Description of Common Stock.
4.4	—	Description of Debt Securities.

4.6	—	The Registrant agrees to furnish copies of any instruments defining the rights of holders of long-term debt of the Registrant and its consolidated subsidiaries that does not exceed 10 percent of the total assets of the Registrant and its consolidated subsidiaries to the Commission upon request.
10.1	—	Employee Matters Agreement between Altria Group, Inc. and Philip Morris International Inc., dated as of March 28, 2008 (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed March 31, 2008).
10.2	—	Intellectual Property Agreement between Philip Morris International Inc. and Philip Morris USA Inc., dated as of January 1, 2008 (incorporated by reference to Exhibit 10.4 to the Registration Statement on Form 10 filed March 5, 2008).

10.3	—	Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 15, 2013).
10.4	—	Extension Agreement, effective February 7, 2017, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders party thereto, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 30, 2017).
10.5	—	Extension Agreement, effective January 31, 2014, to Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders party thereto and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.3 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2014).
10.6	—	Extension Agreement, effective as of February 10, 2015, to Credit Agreement dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2015).
10.7	—	Amendment No. 1, dated as of July 20, 2015, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, The Royal Bank of Scotland plc, as resigning administrative agent, and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as successor administrative agent (incorporated by reference to Exhibit 10.52 to the Annual Report on Form 10-K for the year ended December 31, 2015).
10.8	—	Credit Agreement, dated as of October 1, 2015, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as Facility Agent, and Citibank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed October 5, 2015).
10.9	—	Amendment No. 2, effective as of February 9, 2016, to the Credit Agreement dated as of February 12, 2013, with the lenders named therein and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 28, 2016).
10.10	—	Extension Agreement, effective as of October 1, 2016, to the Credit Agreement dated as of October 1, 2015, among Philip Morris International Inc., lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as Facility Agent, and Citibank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 31, 2016).
10.11	—	Extension Agreement, effective as of October 1, 2017, to the Credit Agreement, dated as of October 1, 2015, among Philip Morris International Inc., the lenders party thereto and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as Facility Agent, and Citibank N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 29, 2017).
10.12	—	Extension Agreement, effective as of February 6, 2018, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2018).
10.13	—	Extension Agreement, effective as of February 5, 2019, to the Credit Agreement dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2019).
10.14	—	Amendment and Extension Agreement, effective February 4, 2020, among Philip Morris International Inc., each lender named therein and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 3, 2020).

10.15	—	Credit Agreement, dated as of February 10, 2020, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch, as Facility Agent, and Citibank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 11, 2020).
10.16	—	Amendment and Extension Agreement, effective February 2, 2021, among PMI, the lenders named therein and Citibank Europe PLC, UK Branch (legal successor to Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 2, 2021).
10.17	—	Amendment and Extension Agreement, effective February 10, 2021, among PMI, the lenders named therein, Citibank Europe PLC, UK Branch, as facility agent, and Citibank, N.A., as swingline agent (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 2, 2021).
10.18	—	Credit Agreement, dated as of September 29, 2021, among PMI, the lenders named therein, Citibank Europe PLC, UK Branch, as facility agent, and Citibank, N.A., as swingline agent (incorporated by reference to Exhibit 10.1to the Current Report on Form 8-K filed September 30, 2021).

10.19	—	Philip Morris International Inc. 2017 Performance Incentive Plan, effective May 3, 2017 (incorporated by reference to Exhibit B to the Definitive Proxy Statement filed on March 23, 2017).*
10.20	—	Pension Fund of Philip Morris in Switzerland (IC) (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2015).*
10.21	—	Summary of Supplemental Pension Plan of Philip Morris in Switzerland (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).*
10.22	—	Philip Morris International Inc. Amended and Restated Automobile Policy, dated as of October 1, 2019 (incorporated by reference to Exhibit 10.16 to the Annual Report on Form 10-K for the year ended December 31, 2020).*
10.23	—	Philip Morris International Benefit Equalization Plan, amended and restated (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2019).*
10.24	—	Form of Restated Employee Grantor Trust Enrollment Agreement (Executive Trust Arrangement) (incorporated by reference to Exhibit 10.18 to the Registration Statement on Form 10 filed February 7, 2008).*
10.25	—	Form of Restated Employee Grantor Trust Enrollment Agreement (Secular Trust Arrangement) (incorporated by reference to Exhibit 10.19 to the Registration Statement on Form 10 filed February 7, 2008).*
10.26	—	Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors (as amended and restated as of January 1, 2018) (incorporated by reference to Exhibit 10.26 to the Annual Report on Form 10-K for the year ended December 31, 2017).*
10.27	—	Philip Morris International Inc. 2008 Deferred Fee Plan for Non-Employee Directors (incorporated by reference to Exhibit 10.24 the the Annual Report on Form 10-K for the year ended December 31, 2020).*
10.28	—	Supplemental Letter to the Employment Agreement (as amended) with André Calantzopoulos (incorporated by reference to Exhibit 10.25 to the Annual Report on Form 10-K for the year ended December 31, 2020). The Employment Agreement was previously filed as Exhibit 10.22 to the Registration Statement on Form 10 filed February 7, 2008 and is incorporated by reference to this Exhibit 10.28.*
10.29	—	Supplemental Letter to Employment Agreement with Marc S. Firestone (incorporated by reference to Exhibit 10.5 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017). The Employment Agreement was previously filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 and is incorporated by reference to this Exhibit 10.29.*
10.30	—	Employment Agreement with Martin G. King, effective June 1, 2020 (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2020).*
10.31	—	Restricted Stock Unit Agreement (2021 Grant) (Martin G. King) (incorporated by reference to Exhibit 10.4 to the Current Report on Form 8-K filed February 9, 2021).*
10.32	—	Performance Stock Unit Agreement (2021 Grant) (Martin G. King) (incorporated by reference to Exhibit 10.6 to the Current Report on Form 8-K filed February 9, 2021).*
10.33	—	Separation Agreement and Release with Martin G. King, dated August 16, 2021 (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 20, 2021).*

10.34	—	Early Retirement Agreement and Release with Marc S. Firestone, effective November 3, 2020 (incorporated by reference to Exhibit 10.28 to the Annual Report on Form 10-K for the year ended December 31, 2020).*
10.35	—	Supplemental Letter to the Employment Agreement (as amended) with Jacek Olczak (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2019. The Employment Agreement was previously filed as Exhibit 10.4 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, and is incorporated by reference to this Exhibit 10.35.*
10.36	—	Supplemental Letter to the Employment Agreement (as amended) with Miroslaw Zielinski (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2019). The Employment Agreement was previously filed as Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 and is incorporated by reference to this Exhibit 10.36.*
10.37	—	Early Retirement and Release Agreement with Miroslaw Zielinski, effective April 30, 2020 (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed May 1, 2020).*
10.38	—	Employment Agreement with Emmanuel Babeau, effective as of May 1, 2020 (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed March 2, 2020).*
10.39	—	Restricted Stock Unit Agreement (2021 Grant) (Emmanuel Babeau) (incorporated by reference to Exhibit 10.3 to the Current Report on Form 8-K filed February 9, 2021).*
10.40	—	Performance Stock Unit Agreement (2021 Grant) (Emmanuel Babeau) (incorporated by reference to Exhibit 10.5 to the Current Report on Form 8-K filed February 9, 2021).*
10.41	—	Employment Agreement with Frederic de Wilde, effective July 1, 2011 (incorporated by reference to Exhibit 10.12 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2021).*
10.42	—	Supplemental Letter to the Employment Agreement with Frederic de Wilde, effective July 1, 2015 (incorporated by reference to Exhibit 10.13 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2021).*
10.43	—	Off-Cycle Restricted Stock Unit Agreement (2021 Grant) (Frederic de Wilde) (incorporated by reference to Exhibit 10.14 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2021).*
10.44	—	Employment Agreement with Stefano Volpetti, effective June 1, 2019 (incorporated by reference to Exhibit 10.10 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2021).*
10.45	—	Supplemental Letter to the Employment Agreement with Stefano Volpetti, effective June 1, 2019 (incorporated by reference to Exhibit 10.11 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2021).*
10.46	—	Supplemental Letter to the Employment Agreement with Stefano Volpetti, effective November 1, 2021.*
10.47	—	Restricted Stock Unit Agreement (Vesting in Installments), between Philip Morris International Inc. and Emmanuel Babeau, effective as of May 1, 2020 (incorporated by reference to Exhibit 10.33 to the Annual Report on Form 10-K for the year ended December 31, 2020.*
10.48	—	Supplemental Letter to the Employment Agreement with André Calantzopoulos, effective May 5, 2021 (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2021). *
10.49	—	Supplemental Letter to the Employment Agreement with Jacek Olczak, effective May 5, 2021 (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2021).*
10.50	—	Restricted Stock Unit Agreement, between Philip Morris International Inc. and Emmanuel Babeau, effective as of May 1, 2020 (incorporated by reference to Exhibit 10.34 to the Annual Report on Form 10-K for the year ended December 31, 2020).*
10.51	—	Performance Stock Unit Agreement, between Philip Morris International Inc. and Emmanuel Babeau, effective as of May 1, 2020 (incorporated by reference to Exhibit 10.35 to the Annual Report on Form 10-K for the year ended December 31, 2020).*
10.52	—	Agreement with Louis C. Camilleri (incorporated by reference to Exhibit 10.25 to the Registration Statement on Form 10 filed February 7, 2008).*
10.53	—	Form of Supplemental Equalization Plan Employee Grantor Trust Enrollment Agreement (Secular Trust) (incorporated by reference to Exhibit 10.31 to the Annual Report on Form 10-K for the year ended December 31, 2008).*

10.54	—	Form of Supplemental Equalization Plan Employee Grantor Trust Enrollment Agreement (Executive Trust) (incorporated by reference to Exhibit 10.32 to the Annual Report on Form 10-K for the year ended December 31, 2008).*
10.55	—	Philip Morris International Inc. Form of Indemnification Agreement with Directors and Executive Officers (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed September 18, 2009).*
10.56	—	Philip Morris International Inc. Tax Return Preparation Services Policy (incorporated by reference to Exhibit 10.51 to the Annual Report on Form 10-K for the year ended December 31, 2014).*
10.57	—	Form of Restricted Stock Unit Agreement (2019 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 12, 2019).*
10.58	—	Form of Performance Share Unit Agreement (2019 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 12, 2019).*
10.59	—	Form of Restricted Stock Unit Agreement (2020 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 11, 2020).*
10.60	—	Form of Performance Share Unit Agreement (2020 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 11, 2020).*
10.61		Form of Restricted Stock Unit Agreement (2021 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 9, 2021).*
10.62	—	Form of Performance Share Unit Agreement (2021 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 9, 2021).*
21	—	Subsidiaries of Philip Morris International Inc.
23	—	Consent of independent registered public accounting firm.
31.1	—	Certification of the Registrant's Chief Executive Officer pursuant to Rule 13a-14(a)/ 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	—	Certification of the Registrant's Chief Financial Officer pursuant to Rule 13a-14(a)/ 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	—	Certification of the Registrant's Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	—	Certification of the Registrant's Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	—	XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.
101.SCH	—	XBRL Taxonomy Extension Schema.
101.CAL	—	XBRL Taxonomy Extension Calculation Linkbase.
101.DEF	—	XBRL Taxonomy Extension Definition Linkbase.
101.LAB	—	XBRL Taxonomy Extension Label Linkbase.
101.PRE	—	XBRL Taxonomy Extension Presentation Linkbase.
104	—	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

* Denotes management contract or compensatory plan or arrangement in which directors or executive officers are eligible to participate.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PHILIP MORRIS INTERNATIONAL INC.

By: /s/ JACEK OLCZAK

(Jacek Olczak
Chief Executive Officer)

Date: February 11, 2022

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Jacek Olczak, Emmanuel Babeau, and Darlene Quashie Henry and each of them, acting individually, as his or her true and lawful attorney-in-fact, each with full power of substitution and resubstitution, for him or her and in his or her name, place and stead, in any and all capacities, to sign any and all amendments to this Annual Report on Form 10-K for the year ended December 31, 2021, and other documents in connection herewith and therewith, and to file the same, with all exhibits thereto, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection herewith and therewith and about the premises, as fully to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated:

Signature	Title	Date
/s/ JACEK OLCZAK (Jacek Olczak)	Chief Executive Officer and Director	February 11, 2022
/s/ EMMANUEL BABEAU (Emmanuel Babeau)	Chief Financial Officer	February 11, 2022
/s/ REGINALDO DOBROWOLSKI (Reginaldo Dobrowolski)	Vice President and Controller	February 11, 2022
/s/ ANDRÉ CALANTZOPOULOS (André Calantzopoulos)	Executive Chairman	February 11, 2022
/s/ BONIN BOUGH (Bonin Bough)	Director	February 11, 2022
/s/ MICHEL COMBES (Michel Combes)	Director	February 11, 2022
/s/ DR. JUAN JOSÉ DABOUB (Juan José Daboub)	Director	February 11, 2022

/s/ WERNER GEISSLER (Werner Geissler)	Director	February 11, 2022
/s/ LISA A. HOOK (Lisa A. Hook)	Director	February 11, 2022
/s/ JUN MAKIHARA (Jun Makihara)	Director	February 11, 2022
/s/ KALPANA MORPARIA (Kalpana Morparia)	Director	February 11, 2022
/s/ LUCIO A. NOTO (Lucio A. Noto)	Director	February 11, 2022
/s/ FREDERIK PAULSEN (Frederik Paulsen)	Director	February 11, 2022
/s/ ROBERT B. POLET (Robert B. Polet)	Director	February 11, 2022
/s/ DESSISLAVA TEMPERLEY (Dessislava Temperley)	Director	February 11, 2022
/s/ SHLOMO YANAI (Shlomo Yanai)	Director	February 11, 2022

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2020

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) ACT OF 1934**

For the transition period from _____ to _____

Commission File Number: 001-33708

PHILIP MORRIS INTERNATIONAL INC.

(Exact name of registrant as specified in its charter)

Virginia	**13-3435103**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
120 Park Avenue **New York** **New York**	**10017**
(Address of principal executive offices)	**(Zip Code)**

917-663-2000

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, no par value	PM	New York Stock Exchange
1.875% Notes due 2021	PM21B	New York Stock Exchange
4.125% Notes due 2021	PM21	New York Stock Exchange
2.900% Notes due 2021	PM21A	New York Stock Exchange
2.625% Notes due 2022	PM22A	New York Stock Exchange
2.375% Notes due 2022	PM22B	New York Stock Exchange
2.500% Notes due 2022	PM22	New York Stock Exchange
2.500% Notes due 2022	PM22C	New York Stock Exchange
2.625% Notes due 2023	PM23	New York Stock Exchange
2.125% Notes due 2023	PM23B	New York Stock Exchange
3.600% Notes due 2023	PM23A	New York Stock Exchange
2.875% Notes due 2024	PM24	New York Stock Exchange
2.875% Notes due 2024	PM24C	New York Stock Exchange
0.625% Notes due 2024	PM24B	New York Stock Exchange
3.250% Notes due 2024	PM24A	New York Stock Exchange
2.750% Notes due 2025	PM25	New York Stock Exchange
3.375% Notes due 2025	PM25A	New York Stock Exchange

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
2.750% Notes due 2026	PM26A	New York Stock Exchange
2.875% Notes due 2026	PM26	New York Stock Exchange
0.125% Notes due 2026	PM26B	New York Stock Exchange
3.125% Notes due 2027	PM27	New York Stock Exchange
3.125% Notes due 2028	PM28	New York Stock Exchange
2.875% Notes due 2029	PM29	New York Stock Exchange
3.375% Notes due 2029	PM29A	New York Stock Exchange
0.800% Notes due 2031	PM31	New York Stock Exchange
3.125% Notes due 2033	PM33	New York Stock Exchange
2.000% Notes due 2036	PM36	New York Stock Exchange
1.875% Notes due 2037	PM37A	New York Stock Exchange
6.375% Notes due 2038	PM38	New York Stock Exchange
1.450% Notes due 2039	PM39	New York Stock Exchange
4.375% Notes due 2041	PM41	New York Stock Exchange
4.500% Notes due 2042	PM42	New York Stock Exchange
3.875% Notes due 2042	PM42A	New York Stock Exchange
4.125% Notes due 2043	PM43	New York Stock Exchange
4.875% Notes due 2043	PM43A	New York Stock Exchange
4.250% Notes due 2044	PM44	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☑ No ☐

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☑

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☑ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☑ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☑ Accelerated filer ☐

Non-accelerated filer ☐ Smaller reporting company ☐

Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report. ☑

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ☐ No ☑

As of June 30, 2020, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was approximately $109 billion based on the closing sale price of the common stock as reported on the New York Stock Exchange.

Class	Outstanding at January 29, 2021
Common Stock, no par value	1,557,451,856 shares

DOCUMENTS INCORPORATED BY REFERENCE

Document	Parts Into Which Incorporated
Portions of the registrant's definitive proxy statement for use in connection with its annual meeting of shareholders to be held on May 5, 2021, to be filed with the Securities and Exchange Commission ("SEC") on or about March 25, 2021.	Part III

TABLE OF CONTENTS

		Page
PART I		
Item 1.	Business	1
Item 1A.	Risk Factors	6
Item 1B.	Unresolved Staff Comments	12
Item 2.	Properties	12
Item 3.	Legal Proceedings	12
Item 4.	Mine Safety Disclosures	13
PART II		
Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	13
Item 6.	Selected Financial Data	16
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	16
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	58
Item 8.	Financial Statements and Supplementary Data	59
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	119
Item 9A.	Controls and Procedures	119
Item 9B.	Other Information	119
PART III		
Item 10.	Directors, Executive Officers and Corporate Governance	120
Item 11.	Executive Compensation	122
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	122
Item 13.	Certain Relationships and Related Transactions, and Director Independence	122
Item 14.	Principal Accounting Fees and Services	122
PART IV		
Item 15.	Exhibits and Financial Statement Schedules	123
Signatures		127

In this report, "PMI," "we," "us" and "our" refers to Philip Morris International Inc. and its subsidiaries.

Trademarks and service marks in this report are the registered property of, or licensed by, the subsidiaries of Philip Morris International Inc. and are italicized.

PART I

Item 1. *Business.*

General Development of Business

General

Philip Morris International Inc. is a Virginia holding company incorporated in 1987. We are a leading international tobacco company engaged in the manufacture and sale of cigarettes, as well as smoke-free products, associated electronic devices and accessories, and other nicotine-containing products in markets outside the United States of America. In addition, we ship versions of our Platform 1 device and consumables to Altria Group, Inc. for sale under license in the United States, where these products have received marketing authorizations from the U.S. Food and Drug Administration ("FDA") under the premarket tobacco product application ("PMTA") pathway; the FDA has also authorized the marketing of a version of our Platform 1 device and its consumables as a Modified Risk Tobacco Product ("MRTP"), finding that an exposure modification order for these products is appropriate to promote the public health.

We are leading a transformation in the tobacco industry to create a smoke-free future, based on a new category of reduced-risk products that, while not risk free, are a much better choice than continuing to smoke. Our goal is to ultimately replace cigarettes with smoke-free products to the benefit of adults who would otherwise continue to smoke, society, the company and its shareholders.

Reduced-risk products ("RRPs") is the term we use to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continuing smoking. We have a range of RRPs in various stages of development, scientific assessment and commercialization. Because our RRPs do not burn tobacco, they produce an aerosol that contains far lower quantities of harmful and potentially harmful constituents than found in cigarette smoke. Through multidisciplinary capabilities in product development, state-of-the-art facilities and scientific substantiation, we aim to ensure that our RRPs meet adult consumer preferences and rigorous regulatory requirements.

Our *IQOS* smoke-free product brand portfolio includes heated tobacco and nicotine-containing vapor products. Our leading smoke-free platform ("Platform 1") is a precisely controlled device into which a specially designed heated tobacco unit is inserted and heated to generate an aerosol. Heated tobacco units ("HTU") is the term we use to refer to heated tobacco consumables, which for us include our *HEETS*, *HEETS Creations, HEETS Dimensions, HEETS Marlboro* and *HEETS FROM MARLBORO (*defined collectively as *HEETS)*, *Marlboro Dimensions*, *Marlboro HeatSticks* and *Parliament HeatSticks,* as well as the KT&G-licensed brands, *Fiit* and *Miix* (outside of Korea). Platform 1 was first introduced in Nagoya, Japan, in 2014. As of December 31, 2020, Platform 1 is available for sale in 64 markets in key cities or nationwide.

Our cigarettes are sold in more than 175 markets, and in many of these markets they hold the number one or number two market share position. We have a wide range of premium, mid-price and low-price brands. Our portfolio comprises both international and local brands and is led by *Marlboro*, the world's best-selling international cigarette, which accounted for approximately 37% of our total 2020 cigarette shipment volume. *Marlboro* is complemented in the premium-price category by *Parliament*. Our other leading international cigarette brands are *Bond Street, Chesterfield, L&M*, *Lark* and *Philip Morris.* These seven international cigarette brands contributed approximately 79% of our cigarette shipment volume in 2020. We also own a number of important local cigarette brands, such as *Dji Sam Soe*, *Sampoerna A* and *Sampoerna U* in Indonesia, and *Fortune* and *Jackpot* in the Philippines.

Source of Funds — Dividends

We are a legal entity separate and distinct from our direct and indirect subsidiaries. Accordingly, our right, and thus the right of our creditors and stockholders, to participate in any distribution of the assets or earnings of any subsidiary is subject to the prior rights of creditors of such subsidiary, except to the extent that claims of our company itself as a creditor may be recognized. As a holding company, our principal sources of funds, including funds to make payment on our debt securities, are from the receipt of dividends and repayment of debt from our subsidiaries. Our principal wholly owned and majority-owned subsidiaries currently are not limited by long-term

debt or other agreements in their ability to pay cash dividends or to make other distributions that are otherwise compliant with law.

Description of Business

We manage our business in six operating segments as follows:

- The European Union Region ("EU") is headquartered in Lausanne, Switzerland, and covers all the European Union countries and also Switzerland, Norway, Iceland and the United Kingdom;
- The Eastern Europe Region ("EE") is also headquartered in Lausanne and includes Southeast Europe, Central Asia, Ukraine, Israel and Russia;
- The Middle East & Africa Region ("ME&A") is also headquartered in Lausanne and covers the African continent, the Middle East, Turkey and our international duty free business;
- The South & Southeast Asia Region ("S&SA") is headquartered in Hong Kong and includes Indonesia, the Philippines and other markets in this region;
- The East Asia & Australia Region ("EA&A") is also headquartered in Hong Kong and includes Australia, Japan, South Korea, the People's Republic of China and other markets in this region, as well as Malaysia and Singapore; and
- The Latin America & Canada Region ("LA&C") is headquartered in New York and covers the South American continent, Central America, Mexico, the Caribbean and Canada. LA&C also includes transactions under license with Altria Group, Inc., for the distribution of our Platform 1 product in the United States.

As of March 22, 2019, we deconsolidated the financial results of our Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH") from our financial statements. For further details, see Item 8, *Financial Statements and Supplementary Data* of this Annual Report on Form 10-K ("Item 8") Note 20. *Deconsolidation of RBH*.

Following the deconsolidation of our Canadian subsidiary, we will continue to report the volume of brands sold by RBH for which other PMI subsidiaries are the trademark owners. These include *HEETS*, *Next*, *Philip Morris* and *Rooftop*.

References to total international market, defined as worldwide cigarette and heated tobacco unit volume excluding the United States, total industry, total market and market shares in this Form 10-K are our estimates for tax-paid products based on the latest available data from a number of internal and external sources and may, in defined instances, exclude the People's Republic of China and/or our duty free business. Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units. In addition, to reflect the deconsolidation of RBH, effective March 22, 2019, PMI's total market share has been restated for previous periods.

2020 estimates for total industry volume and market share in certain geographies reflect limitations on the availability and accuracy of industry data during pandemic-related restrictions.

Our total shipments, including cigarettes and heated tobacco units, decreased by 8.1% in 2020 to 704.6 billion units. We estimate that international industry volumes, including cigarettes and heated tobacco units, were approximately 4.9 trillion units in 2020, a 3.0% decrease from 2019. Excluding the People's Republic of China ("PRC"), we estimate that international cigarette and heated tobacco unit volume was 2.5 trillion units in 2020, a 5.8% decrease from 2019. We estimate that our reported share of the international market (which is defined as worldwide cigarette and heated tobacco unit volume, excluding the United States of America) was approximately 14.4% in 2020, 15.1% in 2019 and 15.2% in 2018. Excluding the PRC, we estimate that our reported share of the international market was approximately 27.7%, 28.4%, and 28.3% in 2020, 2019 and 2018, respectively.

Shipments of our principal cigarette brand, *Marlboro*, decreased by 11.3% in 2020 and represented approximately 9.5% of the international cigarette market, excluding the PRC, in 2020, 10.0% in 2019 and 9.7% in 2018.

Total shipment volume of heated tobacco units reached 76.1 billion units in 2020, up from 59.7 billion units in 2019.

We have a market share of at least 15% in approximately 95 markets, including Algeria, Argentina, Australia, Austria, Belgium, Brazil, the Czech Republic, Egypt, France, Germany, Hong Kong, Hungary, Indonesia, Israel, Italy, Japan, Korea, Kuwait, Mexico, the Netherlands, Norway, the Philippines, Poland, Portugal, Russia, Saudi Arabia, Spain, Switzerland, Turkey and Ukraine.

Distribution & Sales

Our main types of distribution are tailored to the characteristics of each market and are often used simultaneously:

- Direct sales and distribution, where we have set up our own distribution selling directly to the retailers;
- Distribution through independent distributors that often distribute other fast-moving consumer goods and are responsible for distribution in a particular market;
- Exclusive zonified distribution, where the distributors are dedicated to us in tobacco products distribution and assigned to exclusive territories within a market;
- Distribution through national or regional wholesalers that then supply the retail trade; and
- Our own brand retail and e-commerce infrastructures for our RRP products and accessories.

Competition

We are subject to highly competitive conditions in all aspects of our business. We compete primarily on the basis of product quality, brand recognition, brand loyalty, taste, R&D, innovation, packaging, customer service, marketing, advertising and retail price and, increasingly, adult smoker willingness to convert to our RRPs. In the combustible product category, we predominantly sell American blend cigarette brands, such as *Marlboro*, *L&M*, *Parliament, Philip Morris* and *Chesterfield*, which are the most popular across many of our markets. In the RRP product category, we predominantly sell Platform 1 devices and heated tobacco units under the *IQOS* brand umbrella. We seek to compete in all profitable retail price categories, although our brand portfolio is weighted towards the premium-price category.

The competitive environment and our competitive position can be significantly influenced by weak economic conditions, erosion of consumer confidence, competitors' introduction of lower-price products or innovative products, higher tobacco product taxes, higher absolute prices and larger gaps between retail price categories, and product regulation that diminishes the ability to differentiate tobacco products and restricts adult consumer access to truthful and non-misleading information about our RRPs. Competitors include three large international tobacco companies, new market entrants, particularly with respect to innovative products, several regional and local tobacco companies and, in some instances, state-owned tobacco enterprises, principally in Algeria, Egypt, the PRC, Taiwan, Thailand and Vietnam. Industry consolidation and privatizations of state-owned enterprises have led to an overall increase in competitive pressures. Some competitors have different profit and volume objectives, and some international competitors are susceptible to changes in different currency exchange rates. Certain new market entrants may alienate consumers from innovative products through inappropriate marketing campaigns, messaging and inferior product satisfaction, while not relying on scientific substantiation based on appropriate R&D protocols and standards. The growing use of digital media could increase the speed and extent of the dissemination of inaccurate and misleading information about our RRPs.

Procurement and Raw Materials

We purchase tobacco leaf of various types, grades and styles throughout the world, mostly through independent tobacco suppliers. In 2020, we also contracted directly with farmers in several countries, including Argentina, Brazil, Colombia, Italy, Pakistan and Poland. In 2020, direct sourcing from farmers represented approximately 25% of PMI's global leaf requirements. The largest supplies of tobacco leaf are sourced from Argentina, Brazil, China, Italy, Indonesia (mostly for domestic use in kretek products), Malawi, Mozambique, the Philippines, Turkey and the United States.

We believe that there is an adequate supply of tobacco leaf in the world markets to satisfy our current and anticipated production requirements.

In addition to tobacco leaf, we purchase a wide variety of direct materials from a total of approximately 400 suppliers. In 2020, our top ten suppliers of direct materials combined represented approximately 55% of our total direct materials purchases. The three most significant direct materials that we purchase are printed paper board used in packaging, acetate tow used in filter making and fine paper used in the manufacturing of cigarettes and heated

tobacco units. In addition, the adequate supply and procurement of cloves are of particular importance to our Indonesian business.

We discuss the details of our supply chain for our RRPs in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations of this Annual Report on Form 10-K ("Item 7") in *Business Environment—Reduced-Risk Products*.

Business Environment

Information called for by this Item is hereby incorporated by reference to the paragraphs in Item 7, *Business Environment*.

Other Matters

Customers

As described in more detail in "*Distribution & Sales*" above, in many of our markets we sell our products to distributors. In 2020, sales to a distributor in the European Union Region and a distributor in the East Asia & Australia Region each amounted to 10 percent or more of our consolidated net revenues. See Item 8, Note 12. *Segment Reporting* for more information. We believe that none of our business segments is dependent upon a single customer or a few customers, the loss of which would have a material adverse effect on our consolidated results of operations. In some of our markets, particularly in the European Union and in the East Asia & Australia Regions, a loss of a distributor may result in a temporary market disruption.

Employees

Our Workforce. At December 31, 2020, we employed approximately 71,000 people worldwide, including full-time, temporary and part-time staff. Our businesses are subject to a number of laws and regulations relating to our relationship with our employees. Generally, these laws and regulations are specific to the location of each business. We engage with legally recognized employee representative bodies and we have collective bargaining agreements in many of the countries in which we operate. In addition, in accordance with European Union requirements, we have established a European Works Council composed of management and elected members of our workforce. We believe we maintain good relations with our employees and their representative organizations.

Our Internal Transformation. To be successful in our transformation to a smoke-free future, we must continue transforming our culture and ways of working, align our talent with our business needs and innovate to become a truly consumer-centric business. To achieve our strategic goals, we need to attract, retain and motivate the best global talent with the right degree of diversity, experience and skills. Therefore, we strive to ensure the development of our existing talent while increasingly recruiting those with the expertise in areas that are new to us such as digital and technical solutions. We set the levels of our compensation and benefit programs that we believe are necessary to achieve these goals and remain competitive with other consumer product companies.

Oversight and Management. Our Board of Directors provides oversight of various matters pertaining to our workforce, and the Compensation and Leadership Development Committee of the Board is responsible for executive compensation matters and oversight of the risks and programs related to talent management. As part of our commitment to workplace diversity in 2020, our Board appointed a Chief Diversity Officer who reports directly to our CEO. Our Code of Conduct highlights our commitment to diversity, inclusion, fairness, safety and equal opportunity in all aspects of employment. We were the first multinational company to receive a global EQUAL-SALARY certification from the EQUAL-SALARY Foundation. This achievement is an important building block on the road to creating a more inclusive gender-balanced workplace and continuing our reputation as a top employer.

Our Initiatives in Response to COVID-19. We focused on business continuity, health and safety of our employees, and rapidly adapting our ways of working to a new environment. We implemented additional safety measures for essential employees in our facilities and offices and continue to pay salaries to those employees who are unable to work due to government restrictions. We enhanced remote work arrangements and digital collaboration and related risk management, and to date, a large majority of our employees continues to work remotely.

Government Regulation

As a company with global operations in a heavily regulated industry, we are subject to multiple laws and regulations of jurisdictions in which we operate. We discuss our regulatory environment in Item 7, *Business Environment*.

We are subject to international, national and local environmental laws and regulations in the countries in which we do business. We have specific programs across our business units designed to meet applicable environmental compliance requirements and reduce our carbon footprint, wastage, as well as water and energy consumption. We

report externally about our climate change mitigation strategy, together with associated targets and results in reducing our carbon footprint, through CDP (formerly known as the Carbon Disclosure Project), the leading international non-governmental organization assessing the work of thousands of companies worldwide in the area of environmental impact, including climate change. Our environmental and occupational health and safety management program includes policies, standard practices and procedures at all our manufacturing centers. Furthermore, we have engaged an external certification body to validate the effectiveness of this management program at our manufacturing centers around the world, in accordance with internationally recognized standards for safety and environmental management. Our subsidiaries expect to continue to

make investments in order to drive improved performance and maintain compliance with environmental laws and regulations. We assess and report to our management the compliance status of all our legal entities on a regular basis. Based on current regulations, the management and controls we have in place and our review of climate change risks (both physical and regulatory), environmental expenditures have not had, and are not expected to have, a material adverse effect on our consolidated results of operations, capital expenditures, financial position, earnings or competitive position.

Based on current regulations, compliance with government regulations, including environmental regulations, has not had, and is not expected to have a material adverse effect on our results of operations, capital expenditures, financial position, earnings, or competitive position.

As discussed in more detail in Item 1A. *Risk Factors*, our financial results could be significantly affected by regulatory initiatives that could result in a significant decrease in demand for our brands. More specifically, any regulatory requirements that lead to a commoditization of tobacco products or impede adult consumers' ability to convert to our RRPs, as well as any significant increase in the cost of complying with new regulatory requirements could have a material adverse effect on our financial results.

Information About Our Executive Officers

The disclosure regarding executive officers is hereby incorporated by reference to the discussion under the heading "Information about our Executive Officers as of February 8, 2021" in Part III, Item 10. *Directors, Executive Officers and Corporate Governance* of this Annual Report on Form 10-K ("Item 10").

Intellectual Property

Our trademarks are valuable assets, and their protection and reputation are essential to us. We own the trademark rights to all of our principal brands, including *Marlboro*, *HEETS* and *IQOS*, or have the right to use them in all countries where we use them.

In addition, we have a large number of granted patents and pending patent applications worldwide. Our patent portfolio, as a whole, is material to our business. However, no one patent, or group of related patents, is material to us. We also have registered industrial designs, as well as unregistered proprietary trade secrets, technology, know-how, processes and other unregistered intellectual property rights.

Effective January 1, 2008, PMI entered into an Intellectual Property Agreement with Philip Morris USA Inc., a wholly owned subsidiary of Altria Group, Inc. ("PM USA"). The Intellectual Property Agreement allocates ownership of jointly funded intellectual property as follows:

- PMI owns all rights to jointly funded intellectual property outside the United States, its territories and possessions; and
- PM USA owns all rights to jointly funded intellectual property in the United States, its territories and possessions.

The parties agreed to submit disputes under the Intellectual Property Agreement first to negotiation between senior executives and then to binding arbitration.

Seasonality

Our business segments are not significantly affected by seasonality, although in certain markets cigarette consumption may be lower during the winter months due to the cold weather and may rise during the summer months due to outdoor use, longer daylight, and tourism.

Available Information

We are required to file with the SEC annual, quarterly and current reports, proxy statements and other information required by the Securities Exchange Act of 1934, as amended (the "Exchange Act"). The SEC maintains an Internet website at http://www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, from which investors can electronically access our SEC filings.

We make available free of charge on, or through, our website at www.pmi.com our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of

the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. Investors can access our filings with the SEC by visiting www.pmi.com.

The information on our website is not, and shall not be deemed to be, a part of this report or incorporated into any other filings we make with the SEC.

Item 1A. *Risk Factors.*

The following risk factors should be read carefully in connection with evaluating our business and the forward-looking statements contained in this Annual Report on Form 10-K. Any of the following risks could materially adversely affect our business, our operating results, our financial condition and the actual outcome of matters as to which forward-looking statements are made in this Annual Report on Form 10-K.

Forward-Looking and Cautionary Statements

We may from time to time make written or oral forward-looking statements, including statements contained in this Annual Report on Form 10-K and other filings with the SEC, in reports to stockholders and in press releases and investor webcasts. You can identify these forward-looking statements by use of words such as "strategy," "expects," "continues," "plans," "anticipates," "believes," "will," "estimates," "intends," "projects," "aims," "goals," "targets," "forecasts" and other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts.

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Our RRPs constitute a new product category in its early stages that is less predictable than our mature cigarette business. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from those anticipated, estimated or projected. Investors should bear this in mind as they consider forward-looking statements and whether to invest in or remain invested in our securities. In connection with the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995, we are identifying important factors that, individually or in the aggregate, could cause actual results and outcomes to differ materially from those contained in any forward-looking statements made by us; any such statement is qualified by reference to the following cautionary statements. We elaborate on these and other risks we face throughout this document, particularly in Item 7, *Business Environment*. You should understand that it is not possible to predict or identify all risk factors. Consequently, you should not consider the following to be a complete discussion of all potential risks or uncertainties. We do not undertake to update any forward-looking statement that we may make from time to time, except in the normal course of our public disclosure obligations.

Overall Business Risks

Consumption of tax-paid cigarettes continues to decline in many of our markets.
This decline is due to multiple factors, including increased taxes and pricing, governmental actions, the diminishing social acceptance of smoking and health concerns, continuing economic and geopolitical uncertainty, and the continuing prevalence of illicit products. These factors and their potential consequences are discussed more fully below and in Item 7, *Business Environment*.

Cigarettes are subject to substantial taxes. Significant increases in cigarette-related taxes have been proposed or enacted and are likely to continue to be proposed or enacted in numerous jurisdictions. These tax increases may disproportionately affect our profitability and make us less competitive versus certain of our competitors.
Tax regimes, including excise taxes, sales taxes and import duties, can disproportionately affect the retail price of cigarettes versus other combustible tobacco products, or disproportionately affect the relative retail price of our cigarette brands versus cigarette brands manufactured by certain of our competitors. Because our portfolio is weighted toward the premium-price cigarette category, tax regimes based on sales price can place us at a competitive disadvantage in certain markets. As a result, our volume and profitability may be adversely affected in these markets.

Increases in cigarette taxes are expected to continue to have an adverse impact on our sales of cigarettes, due to resulting lower consumption levels, a shift in sales from manufactured cigarettes to other combustible tobacco products and from the premium-price to the mid-price or low-price cigarette categories, where we may be under-

represented, from local sales to legal cross-border purchases of lower price products, or to illicit products such as contraband, counterfeit and "illicit whites."

Our business faces significant governmental action aimed at increasing regulatory requirements with the goal of reducing or preventing the use of tobacco products.

Governmental actions, combined with the diminishing social acceptance of smoking and private actions to restrict smoking, have resulted in reduced industry volume in many of our markets, and we expect that such factors will continue to reduce consumption levels and will increase down-trading and the risk of counterfeiting, contraband, "illicit whites" and legal cross-border purchases. Significant regulatory developments will continue to take place over the next few years in most of our markets, driven principally by the World Health Organization's Framework Convention on Tobacco Control ("FCTC"). Since it came into force in 2005, the FCTC has led to increased efforts by tobacco control advocates and public health organizations to promote increasingly restrictive regulatory measures on the marketing and sale of tobacco products to adult smokers. Regulatory initiatives that have been proposed, introduced or enacted include:

- restrictions on or licensing of outlets permitted to sell cigarettes;
- the levying of substantial and increasing tax and duty charges;
- restrictions or bans on advertising, marketing and sponsorship;
- the display of larger health warnings, graphic health warnings and other labeling requirements;
- restrictions on packaging design, including the use of colors, and mandating plain packaging;
- restrictions on packaging and cigarette formats and dimensions;
- restrictions or bans on the display of tobacco product packaging at the point of sale and restrictions or bans on vending machines;
- requirements regarding testing, disclosure and performance standards for tar, nicotine, carbon monoxide and other smoke constituents;
- disclosure, restrictions, or bans of tobacco product ingredients;
- increased restrictions on smoking and use of tobacco and nicotine-containing products in public and work places and, in some instances, in private places and outdoors;
- restrictions or prohibitions of novel tobacco or nicotine-containing products;
- elimination of duty free sales and duty free allowances for travelers;
- encouraging litigation against tobacco companies; and
- excluding tobacco companies from transparent public dialogue regarding public health and other policy matters.

Our financial results could be significantly affected by regulatory initiatives resulting in a significant decrease in demand for our brands. More specifically, requirements that lead to a commoditization of tobacco products or impede adult consumers' ability to convert to our RRPs, as well as any significant increase in the cost of complying with new regulatory requirements could have a material adverse effect on our financial results.

Changes in the earnings mix and changes in tax laws may result in significant variability in our effective tax rates. Our ability to receive payments from foreign subsidiaries or to repatriate royalties and dividends could be restricted by local country currency exchange controls and other regulations.

We are subject to income tax laws in the United States and numerous foreign jurisdictions. The results of the 2020 U.S. presidential and congressional elections could lead to changes in the U.S. tax system, including significant increases in the U.S. corporate income tax rate and the minimum tax rate on certain earnings of foreign subsidiaries. If ultimately enacted into law, such changes could have a material adverse impact on our effective tax rate thereby reducing our net earnings. Further changes in the tax laws of foreign jurisdictions could arise as a result of the base erosion and profit shifting project undertaken by the Organisation for Economic Co-operation and Development, which recommended changes to numerous long-standing tax principles. If implemented, such changes, as well as changes in taxing jurisdictions' administrative interpretations, decisions, policies, or positions, could also have a material adverse impact on our effective tax rate thereby reducing our net earnings. In future periods, our ability to recover deferred tax assets could be subject to additional uncertainty as a result of such developments. Furthermore, changes in the earnings mix or applicable foreign tax laws may result in significant variability in our effective tax rates.

Because we are a U.S. holding company, our most significant source of funds is distributions from our non-U.S. subsidiaries. Certain countries in which we operate have adopted or could institute currency exchange controls and other regulations that limit or prohibit our local subsidiaries' ability to convert local currency into U.S. dollars or to make payments outside the country. This could subject us to the risks of local currency devaluation and business disruption.

Risks Related to our International Operations

Because we have operations in numerous countries, our results may be adversely impacted by economic, regulatory and political developments, natural disasters, pandemics or conflicts.
Some of the countries in which we operate face the threat of civil unrest and can be subject to regime changes. In others, nationalization, terrorism, conflict and the threat of war may have a significant impact on the business environment. Natural disasters, pandemics, economic, political, regulatory or other developments could disrupt our supply chain, manufacturing capabilities or distribution capabilities. In addition, such developments could increase costs of our materials and operations and lead to loss of property or equipment that are critical to our business in certain markets and difficulty in staffing and managing our operations, all of which could reduce our volumes, revenues and net earnings. We discuss risks associated with the COVID-19 pandemic below.

In certain markets, we are dependent on governmental approvals of various actions such as price changes, and failure to obtain such approvals could impair growth of our profitability.

In addition, despite our high ethical standards and rigorous control and compliance procedures aimed at preventing and detecting unlawful conduct, given the breadth and scope of our international operations, we may not be able to detect all potential improper or unlawful conduct by our employees and partners.

Our reported results could be adversely affected by unfavorable currency exchange rates, and currency devaluations could impair our competitiveness.
We conduct our business primarily in local currency and, for purposes of financial reporting, the local currency results are translated into U.S. dollars based on average exchange rates prevailing during a reporting period. During times of a strengthening U.S. dollar, our reported net revenues, operating income and EPS will be reduced because the local currency translates into fewer U.S. dollars. During periods of economic crises, such as during the ongoing COVID-19 pandemic, foreign currencies may be devalued significantly against the U.S. dollar, reducing our margins. Actions to recover margins may result in lower volume and a weaker competitive position.

Risks Related to Legal Challenges and Investigations

Litigation related to tobacco use and exposure to environmental tobacco smoke could substantially reduce our profitability and could severely impair our liquidity.
There is litigation related to tobacco products pending in certain jurisdictions in which we operate. Damages claimed in some tobacco-related litigation are significant and, in certain cases in Brazil, Canada, and Nigeria, range into the billions of U.S. dollars. We anticipate that new cases will continue to be filed. The FCTC encourages litigation against tobacco product manufacturers. It is possible that our consolidated results of operations, cash flows or financial position could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. See Item 8, Note 17. *Contingencies* to our condensed consolidated financial statements for a discussion of pending litigation and "Business Environment—Reduced-Risk Products (RRPs)—Legal Challenges to RRPs."

From time to time, we are subject to governmental investigations on a range of matters.
Investigations include allegations of contraband shipments of cigarettes, allegations of unlawful pricing activities within certain markets, allegations of underpayment of income taxes, customs duties and/or excise taxes, allegations of false and misleading usage of descriptors, allegations of unlawful advertising, and allegations of unlawful labor practices. We cannot predict the outcome of those investigations or whether additional investigations may be commenced, and it is possible that our business could be materially affected by an unfavorable outcome of pending or future investigations. See Item 8, Note 17. *Contingencies—Other Litigation* and “Management's Discussion and Analysis of Financial Condition and Results of Operations—Operating Results by Business Segment—Business Environment—Governmental Investigations” for a description of certain governmental investigations to which we are subject.

We may be unable to adequately protect our intellectual property rights, and disputes relating to intellectual property rights could harm our business.
Our intellectual property rights are valuable assets, and their protection is important to our business. If the steps we take to protect our intellectual property rights globally, including through a combination of trademark, design, patent and other intellectual property rights, are inadequate, or if others infringe or misappropriate our intellectual property

rights, notwithstanding legal protection, our business could be adversely impacted. Intellectual property rights of third parties may limit our ability to commercialize our products or improve product quality in one or more markets. Competitors or other third parties may claim that we infringe their intellectual property rights. Any such claims, regardless of merit, could divert management's attention, be costly, disruptive, time-consuming and unpredictable and expose us to litigation costs and damages, and impede our ability to manufacture, commercialize and improve our products. If, as a result, we are unable to manufacture or sell our RRPs or improve their quality in one or more markets, our ability to

convert adult smokers to our RRPs in such markets would be adversely affected. See Item 8, Note 17. *Contingencies—Other Litigation* to our condensed consolidated financial statements for a description of certain intellectual property proceedings.

Risks Related to our Competitive Environment

We face intense competition, and our failure to compete effectively could have a material adverse effect on our profitability and results of operations.

We are subject to highly competitive conditions in all aspects of our business. We compete primarily on the basis of product quality, brand recognition, brand loyalty, taste, R&D, innovation, packaging, customer service, marketing, advertising and retail price and, increasingly, adult smoker willingness to convert to our RRPs. The competitive environment and our competitive position can be significantly influenced by weak economic conditions, erosion of consumer confidence, competitors' introduction of lower-price products or innovative products, higher tobacco product taxes, higher absolute prices and larger gaps between retail price categories, and product regulation that diminishes the ability to differentiate tobacco products and restricts adult consumer access to truthful and non-misleading information about our RRPs. Competitors include three large international tobacco companies, new market entrants, particularly with respect to innovative products, several regional and local tobacco companies and, in some instances, state-owned tobacco enterprises, principally in Algeria, Egypt, the PRC, Taiwan, Thailand and Vietnam. Industry consolidation and privatizations of state-owned enterprises have led to an overall increase in competitive pressures. Some competitors have different profit and volume objectives, and some international competitors are susceptible to changes in different currency exchange rates. Certain new market entrants may alienate consumers from innovative products through inappropriate marketing campaigns, messaging and inferior product satisfaction, while not relying on scientific substantiation based on appropriate R&D protocols and standards. The growing use of digital media could increase the speed and extent of the dissemination of inaccurate and misleading information about our RRPs.

We may be unable to anticipate changes in adult consumer preferences.

Our business is subject to changes in adult consumer preferences, which may be influenced by local economic conditions.

To be successful, we must:

- promote brand equity successfully;
- anticipate and respond to new adult consumer trends;
- develop new products and markets and broaden brand portfolios;
- improve productivity;
- convince adult smokers to convert to our RRPs;
- ensure effective adult consumer engagement, including communication about product characteristics and usage of RRPs;
- provide excellent customer care;
- ensure adequate production capacity to meet demand for our products; and
- be able to protect or enhance margins through price increases.

In periods of economic uncertainty, adult consumers may tend to purchase lower-price brands, and the volume of our premium-price and mid-price brands and our profitability could be materially adversely impacted as a result. Such down-trading trends may be reinforced by regulation that limits branding, communication and product differentiation.

Our ability to grow profitability may be limited by our inability to introduce new products, enter new markets or improve our margins through higher pricing and improvements in our brand and geographic mix.

Our profit growth may be adversely impacted if we are unable to introduce new products or enter new markets successfully, to raise prices or to improve the proportion of our sales of higher margin products and in higher margin geographies.

We may be unable to expand our brand portfolio through successful acquisitions or the development of strategic business relationships.

One element of our growth strategy is to strengthen our brand portfolio and market positions through selective acquisitions and the development of strategic business relationships. Acquisition and strategic business development opportunities are limited and present risks of failing to achieve efficient and effective integration, strategic objectives and anticipated revenue improvements and cost savings. There is no assurance that we will be able to acquire attractive businesses on favorable terms, or that future acquisitions or strategic business developments will be accretive to earnings.

Our ability to achieve our strategic goals may be impaired if we fail to attract, motivate and retain the best global talent and effectively align our organizational design with the goals of our transformation.
To be successful, we must continue transforming our culture and ways of working, align our talent and organizational design with our increasingly complex business needs, and innovate and transform to a consumer-centric business. We compete for talent, including in areas that are new to us, such as digital and technical solutions, with companies in the consumer products, technology and other sectors that enjoy greater societal acceptance. As a result, we may be unable to attract, motivate and retain the best global talent with the right degree of diversity, experience and skills to achieve our strategic goals.

Risks Related to the Impact of COVID-19 on our Business

Our business, results of operations, cash flows and financial position will be adversely impacted during the continuation of the COVID-19 pandemic.
The COVID-19 pandemic has created significant societal and economic disruption, and resulted in closures of stores, factories and offices, and restrictions on manufacturing, distribution and travel, all of which have and will continue to adversely impact our business, results of operations, cash flows and financial position while the pandemic continues. Our business continuity plans and other safeguards may not be effective to mitigate the impact of the pandemic.

Currently, significant risks include our diminished ability to convert adult smokers to our RRPs, significant volume declines in our duty-free business and certain other key markets, disruptions or delays in our manufacturing and supply chain, increased currency volatility, and delays in certain cost saving, transformation and restructuring initiatives. Our business could also be adversely impacted if key personnel or a significant number of employees or business partners become unavailable due to the COVID-19 outbreak. The significant adverse impact of COVID-19 on the economic or political conditions in markets in which we operate could result in changes to the preferences of our adult consumers and lower demand for our products, particularly for our mid-price or premium-price brands. Continuation of the pandemic could disrupt our access to the credit markets or increase our borrowing costs. Governments may temporarily be unable to focus on the development of science-based regulatory frameworks for the development and commercialization of RRPs or on the enforcement or implementation of regulations that are significant to our business. In addition, messaging about the potential negative impacts of the use of our products on COVID-19 risks may lead to increasingly restrictive regulatory measures on the sale and use of our products, negatively impact demand for our products and the willingness of adult consumers to switch to our RRPs, and adversely impact our efforts to advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs.

The impact of these risks also depends on factors beyond our knowledge or control, including the duration and severity of the COVID-19 pandemic in general and specifically in the jurisdictions in which we operate, its recurrence in our key markets, actions taken to contain its spread and to mitigate its public health effects, and the ultimate economic consequences thereof.

Risks Related to Sourcing of Materials, Products and Services

Use of third-party resources may negatively impact quality of our products and services, and we may be required to replace third-party contract manufacturers or service providers with our own resources.
We increasingly rely on third-party resources to manufacture some of our products and product parts (particularly, the electronic devices and accessories) and to provide services, including to support our finance and information technology processes. While many of these arrangements improve efficiencies and decrease our operating costs, they also diminish our direct control. Such diminished control may have an adverse effect on the quality of products or services, our supply chain, and the speed and flexibility in our response to changing market conditions and adult consumer preferences, all of which may place us at a competitive disadvantage. In addition, we may be unable to renew these agreements on satisfactory terms for numerous reasons, including government regulations, and our costs may increase significantly if we must replace such third parties with our own resources.

Government mandated prices, production control programs, shifts in crops driven by economic conditions and the impact of climate change may increase the cost or reduce the quality of the tobacco and other agricultural products used to manufacture our products.
As with other agricultural commodities, the price of tobacco leaf and cloves can be influenced by imbalances in supply and demand and the impacts of natural disasters and pandemics such as COVID-19. Furthermore, crop quality

may be influenced by variations in weather patterns, including those caused by climate change. Tobacco production in certain countries is subject to a variety of controls, including government mandated prices and production control programs. Changes in the patterns of demand for agricultural products could cause farmers to produce less tobacco or cloves. Any significant change in tobacco leaf and clove prices, quality and quantity could affect our profitability and our business.

Risks Related to the Success of our Reduced-Risk Products

The financial and business performance of our reduced-risk products is less predictable than our cigarette business.

Our RRPs are novel products in a new category, and the pace at which adult smokers adopt them may vary, depending on the competitive, regulatory, fiscal and cultural environment, and other factors in a specific market. There may be periods of accelerated growth and periods of slower growth for these products, the timing and drivers of which may be more difficult for us to predict versus our mature cigarette business. The impact of this lower predictability on our projected results for a specific period may be significant, particularly during the early stages of this new product category and during the COVID-19 pandemic.

We may be unsuccessful in our attempts to introduce reduced-risk products, and regulators may not permit the commercialization of these products or the communication of scientifically substantiated information and claims.

Our key strategic priorities are: to develop and commercialize products that present less risk of harm to adult smokers who switch to those products versus continued smoking; and to convince current adult smokers who would otherwise continue to smoke to switch to those RRPs. For our efforts to be successful, we must:

- develop RRPs that such adult smokers find acceptable alternatives to smoking;
- conduct rigorous scientific studies to substantiate that they reduce exposure to harmful and potentially harmful constituents in smoke and, ultimately, that these products present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to them versus continued smoking; and
- effectively advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs, including communication of scientifically substantiated information to enable adult smokers to make better consumer choices.

We might not succeed in our efforts. If we do not succeed, but others do, or if heat-not-burn products are inequitably regulated compared to other RRP categories without regard to the totality of the scientific evidence available for such products, we may be at a competitive disadvantage. In addition, actions of some market entrants, such as the inappropriate marketing of e-vapor products to youth, as well as alleged health consequences associated with the use of certain e-vapor products, may unfavorably impact public opinion and/or mischaracterize all e-vapor products or other RRPs to consumers, regulators and policy makers without regard to the totality of scientific evidence for specific products. This may impede our efforts to advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs. We cannot predict whether regulators will permit the sale and/or marketing of RRPs with scientifically substantiated information and claims. Such restrictions could limit the success of our RRPs.

Our RRPs and commercial activities for these products are designed for, and directed toward, current adult smokers and users of nicotine-containing products, and not for non-smokers or youth. If nonetheless there is a significant usage of our products or competitive products among youth or non-smokers, even in situations over which we have no control, our credibility may suffer, and our efforts to advocate for the development of science-based regulatory frameworks for the commercialization of RRPs may be significantly impacted.

Moreover, the FDA's premarket tobacco product and modified risk tobacco product authorizations of a version of our Platform 1 product are subject to strict marketing, reporting and other requirements. Although we have received these product authorizations from the FDA, there is no guarantee that the product will remain authorized, particularly if there is a significant uptake in youth or non-smoker initiation.

We may be unsuccessful in our efforts to differentiate reduced-risk products and cigarettes with respect to taxation.

To date, we have been largely successful in demonstrating to regulators that our RRPs are not cigarettes due to the absence of combustion, and as such they are generally taxed either as a separate category or as other tobacco products, which typically yields more favorable tax rates than cigarettes. If we cease to be successful in these efforts, RRP unit margins may be adversely affected.

Risks Related to Illicit Trade

We lose revenues as a result of counterfeiting, contraband, cross-border purchases, "illicit whites," non-tax-paid volume produced by local manufacturers, and counterfeiting of our Platform 1 device and heated tobacco units.

Large quantities of counterfeit cigarettes are sold in the international market. We believe that *Marlboro* is the most heavily counterfeited international cigarette brand, although we cannot quantify the revenues we lose as a result of this activity. In addition, our revenues are reduced by contraband, legal cross-border purchases, "illicit whites" and non-tax-paid volume produced by local

manufacturers. Our revenues and consumer satisfaction with our Platform 1 device and heated tobacco units may be adversely affected by counterfeit products that do not meet our product quality standards and scientific validation procedures.

Risks Related to Cybersecurity and Data Governance

The failure of our information systems to function as intended or their penetration with the intent to corrupt them or our failure to adhere to strict data governance and cybersecurity protocols and to comply with privacy laws and regulations could result in business disruption, loss of reputation, litigation and regulatory action, and loss of revenue, assets or personal or other confidential data.
We use information systems to help manage business processes, collect and interpret data and communicate internally and externally with employees, suppliers, consumers, customers and others. Some of these information systems are managed by third-party service providers. We have backup systems and business continuity plans in place, and we work with our internal specialists and these third-party service providers to protect these systems and data from unauthorized access. Nevertheless, failure of these systems to function as intended, or penetration of these systems by parties intent on extracting or corrupting information or otherwise disrupting business processes, could place us at a competitive disadvantage, result in a loss of revenue, assets or personal or other sensitive data, litigation and regulatory action, cause damage to our reputation and that of our brands and result in significant remediation and other costs. Failure to protect personal data, respect the rights of data subjects, and adhere to strict data governance and cybersecurity protocols could subject us to substantial fines and other legal challenges under regulations such as the EU General Data Protection Regulation. As we are increasingly relying on digital platforms in our business, and as privacy laws in the jurisdictions in which we do business become more stringent, the magnitude of these risks is likely to increase.

Item 1B. *Unresolved Staff Comments.*

None.

Item 2. *Properties.*

We own or lease various manufacturing, office and research and development facilities in locations primarily outside the United States. We own properties in Switzerland where our operations center and state-of-the-art research and development facility are located.

At December 31, 2020, we operated and owned a total of 39 manufacturing facilities across our six operating segments. Among them, 7 factories produced heated tobacco units.

In 2020, certain facilities each manufactured over 30 billion units (cigarettes and heated tobacco units combined). The largest manufacturing facilities, in terms of volume, are located in Indonesia (S&SA), Poland (EU), Turkey (ME&A), Russia (EE), the Philippines (S&SA), Lithuania (EU), Italy (EU), the Czech Republic (EU) and Portugal (EU). As part of our global operating model, products manufactured in a particular manufacturing facility are not necessarily distributed in the operating segment where the facility is located.

We have integrated the production of our heated tobacco units into a number of our existing manufacturing facilities, and we are progressing with our plans to build manufacturing capacity for our other RRP platforms. We will continue to optimize our manufacturing infrastructure.

We believe the properties owned or leased by our subsidiaries are maintained in good condition and are believed to be suitable and adequate for our present needs.

Item 3. *Legal Proceedings.*

The information called for by this Item is incorporated herein by reference to Item 8, Note 17. *Contingencies*.

Item 4. *Mine Safety Disclosures.*

Not applicable.

PART II

Item 5. *Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.*

The principal stock exchange on which our common stock (no par value) is listed is the New York Stock Exchange (ticker symbol "PM"). At January 29, 2021, there were approximately 48,300 holders of record of our common stock.

Performance Graph

The graph below compares the cumulative total shareholder return on PMI's common stock with the cumulative total return for the same period of PMI's Peer Group and the S&P 500 Index. The graph assumes the investment of $100 as of December 31, 2015, in PMI common stock (at prices quoted on the New York Stock Exchange) and each of the indices as of the market close and reinvestment of dividends on a quarterly basis.

pm-20201231_g1.jpg

Date	PMI	PMI Peer Group [1]	S&P 500 Index
December 31, 2015	$100.00	$100.00	$100.00
December 31, 2016	$108.60	$101.70	$112.00
December 31, 2017	$130.20	$119.60	$136.40
December 31, 2018	$86.90	$107.80	$130.40
December 31, 2019	$117.30	$133.50	$171.50
December 31, 2020	$121.80	$143.10	$203.00

[1] The PMI Peer Group presented in this graph is the same as that used in the prior year. The PMI Peer Group was established based on a review of four characteristics: global presence; a focus on consumer products; and net revenues and a market capitalization of a similar size to those of PMI. The review also considered the primary international tobacco companies. As a result of this review, the following companies constitute the PMI Peer Group: Altria Group, Inc., Anheuser-Busch InBev SA/NV, British American Tobacco p.l.c., The Coca-Cola Company, Colgate-Palmolive Co., Diageo plc, Heineken N.V., Imperial Brands PLC, Japan Tobacco Inc., Johnson & Johnson, Kimberly-Clark Corporation, The Kraft-Heinz Company, McDonald's Corp., Mondelēz International, Inc., Nestlé S.A., PepsiCo, Inc., The Procter & Gamble Company, Roche Holding AG, and Unilever NV and PLC.

Note: Figures are rounded to the nearest $0.10.

Issuer Purchases of Equity Securities During the Quarter Ended December 31, 2020

Our share repurchase activity for each of the three months in the quarter ended December 31, 2020, was as follows:

Period	Total Number of Shares Repurchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Programs
October 1, 2020 – October 31, 2020 (1)	—	$ —	—	$ —
November 1, 2020 – November 30, 2020 (1)	—	$ —	—	$ —
December 1, 2020 – December 31, 2020 (1)	—	$ —	—	$ —
Pursuant to Publicly Announced Plans or Programs	—	$ —		
October 1, 2020 – October 31, 2020 (2)	1,126	$ 75.97		
November 1, 2020 – November 30, 2020 (2)	3,139	$ 70.54		
December 1, 2020 – December 31, 2020 (2)	1,155	$ 75.82		
For the Quarter Ended December 31, 2020	5,420	$ 72.79		

(1) During this reporting period, we did not have an authorized share repurchase program.

(2) Shares repurchased represent shares tendered to us by employees who vested in restricted and performance share unit awards and used shares to pay all, or a portion of, the related taxes.

Item 6. *Selected Financial Data.*

(in millions of dollars, except per share data)

	2020	2019	2018	2017	2016
Summary of Operations:					
Revenues including excise taxes	**$ 76,047**	$ 77,921	$ 79,823	$ 78,098	$ 74,953
Excise taxes on products	**47,353**	48,116	50,198	49,350	48,268
Net revenues	**28,694**	29,805	29,625	28,748	26,685
Operating income	**11,668**	10,531	11,377	11,581	10,903
Net earnings attributable to PMI	**8,056**	7,185	7,911	6,035	6,967
Basic earnings per share	**5.16**	4.61	5.08	3.88	4.48
Diluted earnings per share	**5.16**	4.61	5.08	3.88	4.48
Dividends declared per share	**4.74**	4.62	4.49	4.22	4.12
Total assets	**44,815**	42,875	39,801	42,968	36,851
Long-term debt [(1)]	**28,168**	26,656	26,975	31,334	25,851
Total debt	**31,536**	31,045	31,759	34,339	29,067

[(1)] Excluding current portion of long-term debt.

This Selected Financial Data should be read in conjunction with Item 7 and Item 8.

Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations.*

The following discussion should be read in conjunction with the other sections of this Annual Report on Form 10-K, including the consolidated financial statements and related notes contained in Item 8, and the discussion of risks and cautionary factors that may affect future results in Item 1A. *Risk Factors*.

Description of Our Company

We are leading a transformation in the tobacco industry to create a smoke-free future and ultimately replace cigarettes with smoke-free products to the benefit of adults who would otherwise continue to smoke, society, the company and its shareholders. We are a leading international tobacco company engaged in the manufacture and sale of cigarettes, as well as smoke-free products, associated electronic devices and accessories, and other nicotine-containing products in markets outside the United States. In addition, we ship versions of our Platform 1 device and consumables to Altria Group, Inc. for sale under license in the United States, where these products have received marketing authorizations from the U.S. Food and Drug Administration ("FDA") under the premarket tobacco product application ("PMTA") pathway; the FDA has also authorized the marketing of a version of our Platform 1 device and its consumables as a Modified Risk Tobacco Product ("MRTP"), finding that an exposure modification order for these products is appropriate to promote the public health. We are building a future on a new category of smoke-free products that, while not risk-free, are a much better choice than continuing to smoke. Through multidisciplinary capabilities in product development, state-of-the-art facilities and scientific substantiation, we aim

to ensure that our smoke-free products meet adult consumer preferences and rigorous regulatory requirements. Our smoke-free product portfolio includes heat-not-burn and nicotine-containing vapor products.

We manage our business in six operating segments:

- European Union ("EU");
- Eastern Europe ("EE");
- Middle East & Africa ("ME&A"), which includes our international duty free business;
- South & Southeast Asia ("S&SA");

- East Asia & Australia ("EA&A"); and
- Latin America & Canada ("LA&C"), which includes transactions under license with Altria Group, Inc. for the distribution of our Platform 1 product in the United States.

Our cigarettes are sold in more than 175 markets, and in many of these markets they hold the number one or number two market share position. We have a wide range of premium, mid-price and low-price brands. Our portfolio comprises both international and local brands. In addition to the manufacture and sale of cigarettes, we are engaged in the development and commercialization of reduced-risk products ("RRPs"). RRPs is the term we use to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continuing smoking.

We use the term net revenues to refer to our operating revenues from the sale of our products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. Our net revenues and operating income are affected by various factors, including the volume of products we sell, the price of our products, changes in currency exchange rates and the mix of products we sell. Mix is a term used to refer to the proportionate value of premium-price brands to mid-price or low-price brands in any given market (product mix). Mix can also refer to the proportion of shipment volume in more profitable markets versus shipment volume in less profitable markets (geographic mix).

Our cost of sales consists principally of: tobacco leaf, non-tobacco raw materials, labor and manufacturing costs; shipping and handling costs; and the cost of devices produced by third-party electronics manufacturing service providers. Estimated costs associated with device warranty programs are generally provided for in cost of sales in the period the related revenues are recognized.

Our marketing, administration and research costs include the costs of marketing and selling our products, other costs generally not related to the manufacture of our products (including general corporate expenses), and costs incurred to develop new products. The most significant components of our marketing, administration and research costs are marketing and sales expenses and general and administrative expenses.

Philip Morris International Inc. is a legal entity separate and distinct from its direct and indirect subsidiaries. Accordingly, our right, and thus the right of our creditors and stockholders, to participate in any distribution of the assets or earnings of any subsidiary is subject to the prior rights of creditors of such subsidiary, except to the extent that claims of our company itself as a creditor may be recognized. As a holding company, our principal sources of funds, including funds to make payment on our debt securities, are from the receipt of dividends and repayment of debt from our subsidiaries. Our principal wholly owned and majority-owned subsidiaries currently are not limited by long-term debt or other agreements in their ability to pay cash dividends or to make other distributions that are otherwise compliant with law.

Executive Summary

The following executive summary provides the business update and significant highlights from the *Discussion and Analysis* that follows.

Consolidated Operating Results

- **Net Revenues –** Net revenues of $28.7 billion for the year ended December 31, 2020, decreased by $1.1 billion, or 3.7%, from the comparable 2019 amount, and were impacted by the effects of the COVID-19 pandemic, particularly in the second quarter of 2020 and continuing throughout the second half of the year. The change in our net revenues from the comparable 2019 amount was driven by the following (variances not to scale):
  pm-20201231_g2.jpg

  Net revenues, excluding unfavorable currency, decreased by 2.2%, reflecting: unfavorable volume/mix, primarily due to lower cigarette volume (mainly in Argentina, Indonesia, Italy, Japan, Mexico, the Philippines, PMI Duty Free, Poland, Russia and Ukraine, partly offset by Germany), partially offset by higher heated tobacco unit volume (notably in the EU, Japan, Russia and Ukraine, partly offset by PMI Duty Free); and the unfavorable impact of $253 million, shown in "Cost/Other," mainly resulting from the deconsolidation of our Canadian subsidiary, Rothman, Benson & Hedges, Inc. ("RBH"), effective March 22, 2019, and lower fees for certain distribution rights billed to customers in certain markets; partly offset by a favorable pricing variance (notably driven by the Gulf Cooperation Council, Germany, Japan, Mexico, North Africa, the Philippines, PMI Duty Free, Russia and Ukraine, partially offset by Indonesia, Poland and Turkey). For further details on the deconsolidation of RBH, see Item 8, Note 17. *Contingencies* and Note 20. *Deconsolidation of RBH.* The Gulf Cooperation Council ("GCC") is defined as Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates (UAE).

Net revenues by product category for the years ended December 31, 2020 and 2019, are shown below:

pm-20201231_g3.jpg pm-20201231_g4.jpg

- **Diluted Earnings Per Share –** The changes in our reported diluted earnings per share ("diluted EPS") for the year ended December 31, 2020, from the comparable 2019 amounts, were as follows:

		Diluted EPS
For the year ended December 31, 2019	$	4.61
2019 Asset impairment and exit costs		0.23
2019 Canadian tobacco litigation-related expense		0.09
2019 Loss on deconsolidation of RBH		0.12
2019 Russia excise and VAT audit charge		0.20
2019 Fair value adjustment for equity security investments		(0.02)
2019 Tax items		(0.04)
Subtotal of 2019 items		0.58
2020 Asset impairment and exit costs		(0.08)
2020 Brazil indirect tax credit		0.05
2020 Fair value adjustment for equity security investments		(0.04)
2020 Tax items		0.06
Subtotal of 2020 items		(0.01)
Currency		(0.32)
Interest		(0.02)
Change in tax rate		0.05
Operations		0.27
For the year ended December 31, 2020	$	5.16

Asset impairment and exit costs – During 2019, as part of the optimization of our global manufacturing infrastructure, we recorded pre-tax asset impairment and exit costs of $422 million, representing $362 million net of income tax and a diluted EPS charge of $0.23 per share. This 2019 charge primarily related to a cigarette plant closure in Berlin, Germany (approximately $0.19 per share), as well as the closure of cigarette plants in Argentina, Colombia and Pakistan. During 2020, we recorded pre-tax asset impairment and exit costs of $149 million, representing $124 million net of income tax and a diluted EPS charge of

$0.08 per share, related to the organizational design optimization plan, primarily in Switzerland. The total pre-tax charges in 2019 and 2020 were included in marketing, administration and research costs on the consolidated statements of earnings. For further details, see Item 8, Note 19. *Asset Impairment and Exit Costs*.

Canadian tobacco litigation-related expense – In the first quarter of 2019, we recorded a pre-tax charge of $194 million, representing $142 million net of tax, relating to the judgment against RBH in two Québec smoking and health class actions. The charge of $0.09 per share reflects our assessment of the portion of the judgment that represents a probable and estimable loss prior to the deconsolidation of RBH and corresponds to the trust account deposit required by the judgment. The total pre-tax charge was included in marketing, administration and research costs on the consolidated statements of earnings and was included in the operating income of the Latin America & Canada segment. For further details, see Item 8, Note 17. *Contingencies* and Item 8, Note 20. *Deconsolidation of RBH*.

Loss on deconsolidation of RBH – Following the judgment in the two Québec smoking and health class actions, RBH obtained an initial order from the Ontario Superior Court of Justice granting it protection under the Companies' Creditors Arrangement Act ("CCAA"), which is a Canadian federal law that permits a Canadian business to restructure its affairs while carrying on its business in the ordinary course with minimal disruption to its customers, suppliers and employees. The administration of the CCAA process, principally relating to the powers provided to the court and the court appointed monitor, removes certain elements of control of the business from both PMI and RBH. As a result, we have determined that we no longer have a controlling financial interest over RBH and that we do not exert "significant influence" over RBH under U.S. GAAP. Therefore, we deconsolidated RBH as of the date of the CCAA filing on March 22, 2019, and have accounted for our continuing investment in RBH as an equity security, without readily determinable fair value.

A loss on the deconsolidation of RBH of $239 million was included in marketing, administration and research costs on the consolidated statements of earnings for the year ended December 31, 2019, and was included in the operating income of the Latin America & Canada segment. The $0.12 per share impact also included a tax benefit of $49 million within the provision for income taxes, as discussed below, related to the reversal of a deferred tax liability on the unremitted earnings of RBH. For further details, see Item 8, Note 17. *Contingencies* and Item 8, Note 20. *Deconsolidation of RBH*.

Russia excise and VAT audit charge – As a result of the final tax assessment for the 2015-2017 financial years received by our Russian affiliate, in the third quarter of 2019, PMI recorded a pre-tax charge of $374 million in marketing, administration and research costs in the consolidated statements of earnings, representing $315 million net of income tax and a diluted EPS charge of $0.20. The pre-tax charge of $374 million was included in the operating income of the Eastern Europe segment. For further details, see Item 8, Note 17. *Contingencies.*

Brazil indirect tax credit - Following a final and enforceable decision by the highest court in Brazil in October 2020, PMI recorded a gain of $119 million for tax credits ($79 million net of income tax and $0.05 per share increase in diluted EPS) representing overpayments of indirect taxes for the period from March 2012 through December 2019; these tax credits will be applied to future tax liabilities in Brazil. This amount was included as a reduction in marketing, administration and research costs in the consolidated statements of earnings for the year ended December 31, 2020 and was included in the operating income of the Latin America & Canada segment. A decision regarding an additional amount of overpaid indirect taxes of approximately $90 million is still pending before this court.

Fair Value adjustment for equity security investments – In the fourth quarter of 2019, PMI recorded a favorable fair value adjustment for its equity security investments of $35 million after tax (or $0.02 per share increase in diluted EPS). The fair value adjustment for its equity security investments was included in equity investments and securities (income)/loss, net ($44 million income) and provision for income taxes ($9 million expense) on the consolidated statements of earnings in 2019. During 2020, we recorded an unfavorable fair value adjustment for our equity security investments of $60 million after tax (or $0.04 per share decrease in diluted EPS). The fair value adjustment for our equity security investments was included in equity investments and securities (income)/loss, net ($76 million loss) and provision for income taxes ($16 million benefit) on the consolidated statements of earnings. For further details, see Item 8, Note 4. *Related Parties - Equity Investments and Other.*

Income taxes – The 2019 Tax items that increased our 2019 diluted EPS by $0.04 per share in the table above were primarily due to a reduction in estimated U.S. federal income tax on dividend repatriation for the years 2015 - 2018 ($67 million). The 2020 Tax items that increased our 2020 diluted EPS by $0.06 per share in the table above were due to final U.S. tax regulations under the Global Intangible Low-Taxed Income ("GILTI") provisions of the Internal Revenue Code for years 2018 and 2019 ($93 million). For further details, see Item 8, Note 11. *Income Taxes*.

The change in the tax rate that increased our diluted EPS by $0.05 per share in the table above was primarily due to changes in earnings mix by taxing jurisdiction, a reduction of U.S. state tax expense and the corporate income tax rate reduction in Indonesia,

partially offset by a decrease in deductions related to foreign-derived intangible income for the years 2018 and 2019 and repatriation cost differences. For further details, see Item 8, Note 11. *Income Taxes*.

Currency – The unfavorable currency impact during 2020 results from the fluctuations of the U.S. dollar, especially against the Argentine peso, Brazilian real, Indonesian rupiah, Mexican peso, Russian ruble, Swiss franc and Turkish lira, partially offset by the Egyptian pound, Japanese yen and Philippine peso. This unfavorable currency movement has impacted our profitability across our primary revenue markets and local currency cost bases.

Interest – The unfavorable impact of interest was due primarily to lower interest earned on cash balances.

Operations – The increase in diluted EPS of $0.27 from our operations in the table above was due primarily to the following segments:

- European Union: Favorable volume/mix, favorable pricing and lower manufacturing costs, partially offset by higher marketing, administration and research costs;
- East Asia & Australia: Lower marketing, administration and research costs, lower manufacturing costs and favorable pricing, partially offset by unfavorable volume/mix; and
- Eastern Europe: Favorable pricing, favorable volume/mix and lower manufacturing costs, partially offset by higher marketing, administration and research costs ;

partially offset by

- Middle East & Africa: Unfavorable volume/mix and lower fees for certain distribution rights billed to customers in certain markets, partially offset by favorable pricing, and lower marketing, administration and research costs;
- South & Southeast Asia: Unfavorable volume/mix and unfavorable pricing, partially offset by lower marketing, administration and research costs; and
- Latin America & Canada: Unfavorable volume/mix, as well as the unfavorable impact resulting from the deconsolidation of RBH, partially offset by favorable pricing and lower marketing, administration and research costs.

For further details, see the *Consolidated Operating Results* and *Operating Results by Business Segment* sections of the following *Discussion and Analysis*.

COVID-19 Impact on Our Business

<u>COVID-19: Business Continuity Update</u>

Since the onset of the COVID-19 pandemic, PMI has undertaken a number of business continuity measures to mitigate potential disruption to its operations and route-to-market in order to preserve the availability of products to its customers and adult consumers.

Currently:

- PMI has sufficient access to the inputs for its products and is not facing any significant business continuity issues with respect to key suppliers;
- All of of PMI's cigarette and heated tobacco unit manufacturing facilities globally are operational;
- COVID-related restrictions do not have a significant impact on the availability of PMI's products to its customers and adult consumers; and
- PMI has sufficient liquidity resources through cash on hand, the ongoing cash generation of its business, and its access to the commercial paper and debt markets.

Nonetheless, significant uncertainty remains as the spread of the disease is increasing in a number of markets, resulting in additional restrictions and increasing risk of disruptions.

Discussion and Analysis

Critical Accounting Estimates

Item 8, Note 2. *Summary of Significant Accounting Policies* to our consolidated financial statements includes a summary of the significant accounting policies and methods used in the preparation of our consolidated financial statements. In most instances, we must use a particular accounting policy or method because it is the only one that is permitted under U.S. GAAP.

The preparation of financial statements requires that we use estimates and assumptions that affect the reported amounts of our assets, liabilities, net revenues and expenses, as well as our disclosure of contingencies. If actual amounts differ from previous estimates, we include the revisions in our consolidated results of operations in the period during which we know the actual amounts. Historically, aggregate differences, if any, between our estimates and actual amounts in any year have not had a significant impact on our consolidated financial statements.

The selection and disclosure of our critical accounting estimates have been discussed with our Audit Committee. The following is a discussion of the more significant assumptions, estimates, accounting policies and methods used in the preparation of our consolidated financial statements:

Revenue Recognition - We recognize revenue as performance obligations are satisfied. Our primary performance obligation is the distribution and sales of cigarettes and other nicotine-containing products, including reduced-risk products. Our performance obligations are typically satisfied upon shipment or delivery to our customers. The company estimates the cost of sales returns based on historical experience, and these estimates are immaterial. Estimated costs associated with warranty programs for *IQOS* devices are generally provided for in cost of sales in the period the related revenues are recognized, based on a number of factors, including historical experience, product failure rates and warranty policies. The transaction price is typically based on the amount billed to the customer and includes estimated variable consideration where applicable. Such variable consideration is typically not constrained and is estimated based on the most likely amount that PMI expects to be entitled to under the terms of the contracts with customers, historical experience of discount or rebate redemption, where relevant, and the terms of any underlying discount or rebate programs, which may change from time to time as the business and product categories evolve.

Inventories - Our inventories are valued at the lower of cost or market based upon assumptions about future demand and market conditions. The valuation of inventory also requires us to estimate obsolete and excess inventory. We perform regular reviews of our inventory on hand, as well as our future purchase commitments with our suppliers, considering multiple factors, including demand forecasts, product life cycle, current sales levels, pricing strategy and cost trends. If our review indicates that inventories of raw materials, components or finished products have become obsolete or are in excess of anticipated demand or that inventory cost exceeds net realizable value, we may be required to make adjustments that will impact the results of operations.

Goodwill and Non-Amortizable Intangible Assets Valuation - We test goodwill and non-amortizable intangible assets for impairment annually or more frequently if events occur that would warrant such review. While the company has the option to perform a qualitative assessment for both goodwill and non-amortizable intangible assets to determine if it is more likely than not that an impairment exists, the company elects to perform the quantitative assessment for our annual impairment analysis. The impairment analysis involves comparing the fair value of each reporting unit or non-amortizable intangible asset to the carrying value. If the carrying value exceeds the fair value, goodwill or a non-amortizable intangible asset is considered impaired. To determine the fair value of goodwill, we primarily use the market approach using earnings multiples of comparable global companies within the tobacco industry, supported by a discounted cash flow model. At December 31, 2020, the carrying value of our goodwill was $6.0 billion, which is related to ten reporting units, each of which consists of a group of markets with similar operating and economic characteristics. The estimated fair value of each of our ten reporting units exceeded the carrying value as of December 31, 2020. To determine the fair value of non-amortizable intangible assets, we primarily use a discounted cash flow model applying the relief-from-royalty method. We concluded that the fair value of our non-amortizable intangible assets exceeded the carrying value. These discounted cash flow models include management assumptions relevant for forecasting operating cash flows, which are subject to changes in business conditions, such as volumes and prices, costs to produce, discount rates and estimated capital needs. Management considers historical experience and all available information at the time the fair values are

estimated, and we believe these assumptions are consistent with the assumptions a hypothetical marketplace participant would use. Since the March 28, 2008, spin-off from Altria Group, Inc., we have not recorded a charge to earnings for an impairment of goodwill or non-amortizable intangible assets.

Marketing Costs - We incur certain costs to support our products through programs that include advertising, marketing, consumer engagement and trade promotions. The costs of our advertising and marketing programs are expensed in accordance with U.S. GAAP. Recognition of the cost related to our consumer engagement and trade promotion programs contain uncertainties due to the

judgment required in estimating the potential performance and compliance for each program. For volume-based incentives provided to customers, management continually assesses and estimates, by customer, the likelihood of the customer's achieving the specified targets, and records the reduction of revenue as the sales are made. For other trade promotions, management relies on estimated utilization rates that have been developed from historical experience. Changes in the assumptions used in estimating the cost of any individual marketing program would not result in a material change in our financial position, results of operations or operating cash flows.

Employee Benefit Plans - As discussed in Item 8, Note 13. *Benefit Plans* to our consolidated financial statements, we provide a range of benefits to our employees and retired employees, including pensions, postretirement health care and postemployment benefits (primarily severance). We record annual amounts relating to these plans based on calculations specified by U.S. GAAP. These calculations include various actuarial assumptions, such as discount rates, assumed rates of return on plan assets, compensation increases, mortality, turnover rates and health care cost trend rates. We review actuarial assumptions on an annual basis and make modifications to the assumptions based on current rates and trends when it is deemed appropriate to do so. As permitted by U.S. GAAP, any effect of the modifications is generally amortized over future periods. We believe that the assumptions utilized in calculating our obligations under these plans are reasonable based upon our historical experience and advice from our actuaries.

Weighted-average discount rate assumptions for pension and postretirement plan obligations at December 31, 2020 and 2019 are as follows:

	2020	2019
Pension plans	**0.56%**	0.83%
Postretirement plans	**2.84%**	3.28%

We anticipate that assumption changes will increase 2021 pre-tax pension and postretirement expense to approximately $300 million as compared with approximately $264 million in 2020, excluding amounts related to employee severance and early retirement programs. The anticipated increase is primarily due to higher amortization of unrecognized actuarial gains/losses of $50 million, coupled with higher service cost of $24 million, partially offset by lower interest cost of $18 million and higher expected return on plan assets of $17 million and other movements of $3 million.

Weighted-average expected rate of return and discount rate assumptions have a significant effect on the amount of expense reported for the employee benefit plans. A fifty-basis-point decrease in our discount rate would increase our 2021 pension and postretirement expense by approximately $80 million, and a fifty-basis-point increase in our discount rate would decrease our 2021 pension and postretirement expense by approximately $70 million. Similarly, a fifty-basis-point decrease (increase) in the expected return on plan assets would increase (decrease) our 2021 pension expense by approximately $40 million.

Income Taxes - Income tax provisions for jurisdictions outside the United States, as well as state and local income tax provisions, are determined on a separate company basis, and the related assets and liabilities are recorded in our consolidated balance sheets.

The extent of our operations involves dealing with uncertainties and judgments in the application of complex tax regulations in a multitude of jurisdictions. The final taxes paid are dependent upon many factors, including negotiations with taxing authorities in various jurisdictions and resolution of disputes arising from federal, state, and international tax audits. In accordance with the authoritative guidance for income taxes, we evaluate potential tax exposures and record tax liabilities for anticipated tax audit issues based on our estimate of whether, and the extent to which, additional taxes will be due. We adjust these reserves in light of changing facts and circumstances; however, due to the complexity of some of these uncertainties, the ultimate resolution may result in a payment that is materially different from our current estimate of the tax liabilities. If our estimate of tax liabilities proves to be less than the ultimate assessment, an additional charge to expense would result. If payment of these amounts ultimately proves to be less than the recorded amounts, the reversal of the liabilities would result in tax benefits being recognized in the period when we determine the liabilities are no longer necessary.

We are required to assess the likelihood of recovering deferred tax assets against future sources of taxable income. If we determine, using all available evidence, that we do not reach the more likely than not threshold for recovery, a valuation allowance is recorded. Significant judgment is required in determining the need for and amount of

valuation allowances for deferred tax assets including estimates of future taxable income in the applicable jurisdictions and the feasibility of on-going tax planning strategies, as applicable.

The effective tax rates used for interim reporting are based on our full-year geographic earnings mix projections. Changes in currency exchange rates, earnings mix by taxing jurisdiction or future regulatory developments may have an impact on the effective tax rates. Significant judgment is required in determining income tax provisions and in evaluating tax positions.

For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements.

Hedging - As discussed below in "Market Risk," we use derivative financial instruments principally to reduce exposures to market risks resulting from fluctuations in foreign currency exchange and interest rates by creating offsetting exposures. For derivatives to which we have elected to apply hedge accounting, gains and losses on these derivatives are initially deferred in accumulated other comprehensive losses on the consolidated balance sheet and recognized in the consolidated statement of earnings into the same line item as the impact of the underlying transaction and in the periods when the related hedged transactions are also recognized in operating results. If we had elected not to use the hedge accounting provisions, gains (losses) deferred in stockholders' (deficit) equity would have been recorded in our net earnings for these derivatives.

Fair value of non-marketable equity securities - For further details, see Item 8, Note 20. *Deconsolidation of RBH.*

Contingencies - As discussed in Item 8, Note 17. *Contingencies* to our consolidated financial statements, legal proceedings covering a wide range of matters are pending or threatened against us, and/or our subsidiaries, and/or our indemnitees in various jurisdictions. We and our subsidiaries record provisions in the consolidated financial statements for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. The variability in pleadings in multiple jurisdictions, together with the actual experience of management in litigating claims, demonstrate that the monetary relief that may be specified in a lawsuit bears little relevance to the ultimate outcome. Much of the tobacco-related litigation is in its early stages, and litigation is subject to uncertainty. At the present time, except as stated otherwise in Item 8, Note 17. *Contingencies,* while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available to it: (i) management has not concluded that it is probable that a loss has been incurred in any of the pending tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any. Legal defense costs are expensed as incurred.

Consolidated Operating Results

Our net revenues and operating income by segment were as follows:

(in millions)	2020	2019	2018
Net Revenues			
European Union	**$ 10,702**	$ 9,817	$ 9,298
Eastern Europe	**3,378**	3,282	2,921
Middle East & Africa	**3,088**	4,042	4,114
South & Southeast Asia	**4,396**	5,094	4,656
East Asia & Australia	**5,429**	5,364	5,580
Latin America & Canada [1]	**1,701**	2,206	3,056
Net revenues	**$ 28,694**	$ 29,805	$ 29,625
Operating Income			
European Union	**$ 5,098**	$ 3,970	$ 4,105
Eastern Europe	**871**	547	902
Middle East & Africa	**1,026**	1,684	1,627
South & Southeast Asia	**1,709**	2,163	1,747
East Asia & Australia	**2,400**	1,932	1,851
Latin America & Canada [1]	**564**	235	1,145
Operating income	**$ 11,668**	$ 10,531	$ 11,377

[1] As of March 22, 2019, PMI deconsolidated the financial results of its Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH") from PMI's financial statements. For further details, see Item 8, Note 20. *Deconsolidation of RBH*.

Items affecting the comparability of results from operations were as follows:

- **Asset impairment and exit costs** - See Item 8, Note 19. *Asset Impairment and Exit Costs* for details of the $149 million and $422 million pre-tax charges for the years ended December 31, 2020 and 2019, respectively, as well as a breakdown of these costs by segment.
- **Russia excise and VAT audit charge** - See Item 8, Note 17. *Contingencies* for details of the $374 million pre-tax charge included in the Eastern Europe segment for the year ended December 31, 2019.
- **Canadian tobacco litigation-related expense** - See Item 8, Note 17. *Contingencies* and Note 20. *Deconsolidation of RBH* for details of the $194 million pre-tax charge included in the Latin America & Canada segment for the year ended December 31, 2019.
- **Loss on deconsolidation of RBH** - See Item 8, Note 20. *Deconsolidation of RBH* for details of the $239 million loss included in the Latin America & Canada segment for the year ended December 31, 2019.
- **Brazil indirect tax credit** - Following a final and enforceable decision by the highest court in Brazil in October 2020, PMI recorded a gain of $119 million for tax credits representing overpayments of indirect taxes for the period from March 2012 through December 2019; these tax credits will be applied to future tax liabilities in Brazil. This amount was included as a reduction in marketing, administration and research costs in the consolidated statements of earnings for the year ended December 31, 2020 and was included in the operating income of the Latin America & Canada segment. A decision regarding an additional amount of overpaid indirect taxes of approximately $90 million is still pending before this court.

Our net revenues by product category were as follows:

PMI Net Revenues by Product Category

(in millions)	2020	2019	2018
Combustible Products			
European Union	**$ 8,053**	$ 8,093	$ 8,433
Eastern Europe	**2,250**	2,438	2,597
Middle East & Africa	**3,031**	3,721	3,732
South & Southeast Asia	**4,395**	5,094	4,656
East Asia & Australia	**2,468**	2,693	3,074
Latin America & Canada	**1,670**	2,179	3,037
Total Combustible Products	**$ 21,867**	$ 24,218	$ 25,529
Reduced-Risk Products			
European Union	**$ 2,649**	$ 1,724	$ 865
Eastern Europe	**1,128**	844	324
Middle East & Africa	**57**	321	382
South & Southeast Asia	**1**	—	—
East Asia & Australia	**2,961**	2,671	2,506
Latin America & Canada	**31**	27	19
Total Reduced-Risk Products	**$ 6,827**	$ 5,587	$ 4,096
Total PMI Net Revenues	**$ 28,694**	$ 29,805	$ 29,625

Note: Sum of product categories or Regions might not foot to total PMI due to rounding.

Net revenues related to combustible products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of our cigarettes and other tobacco products combined. Other tobacco products primarily include roll-your-own and make-your-own cigarettes, pipe tobacco, cigars and cigarillos and do not include reduced-risk products.

Net revenues related to reduced-risk products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue

amounts consist of the sale of our heated tobacco units, heat-not-burn devices and related accessories, and other nicotine-containing products, which primarily include our e-vapor products.

PMI's heat-not-burn products include licensed KT&G heat-not-burn products.

Revenues from shipments of Platform 1 devices, heated tobacco units and accessories to Altria Group, Inc., commencing in the third quarter of 2019, for sale under license in the United States, are included in Net Revenues of the Latin America & Canada segment.

References to "Cost/Other" in the Consolidated Financial Summary table of total PMI and the six operating segments throughout this *"Discussion and Analysis"* reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs (including asset impairment and exit costs, the Canadian tobacco litigation-related expense, the charge related to the deconsolidation of RBH in Canada, and the Russia excise and VAT audit charge); and amortization of intangibles. “Cost/Other” also includes the currency-neutral net revenue variance, unrelated to volume/mix and price components, attributable to fees for certain distribution rights billed to customers in certain markets in the ME&A Region, as well as the impact of the deconsolidation in RBH.

Our shipment volume by segment for cigarettes and heated tobacco units was as follows:

	PMI Shipment Volume (Million Units)	
	2020	**2019**
Cigarettes		
European Union	**163,420**	174,3
Eastern Europe	**93,462**	100,6
Middle East & Africa	**117,999**	134,5
South & Southeast Asia	**144,788**	174,9
East Asia & Australia	**45,100**	49,9
Latin America & Canada	**63,749**	72,2
Total Cigarettes	**628,518**	706,7
Heated Tobacco Units		
European Union	**19,842**	12,
Eastern Europe	**20,898**	13,
Middle East & Africa	**1,022**	2,
South & Southeast Asia	**36**	
East Asia & Australia	**33,862**	30,
Latin America & Canada [1]	**451**	
Total Heated Tobacco Units	**76,111**	59,
Cigarettes and Heated Tobacco Units		
European Union	**183,262**	186,
Eastern Europe	**114,360**	114,
Middle East & Africa	**119,021**	137,
South & Southeast Asia	**144,824**	174,
East Asia & Australia	**78,962**	80,
Latin America & Canada	**64,200**	72,
Total Cigarettes and Heated Tobacco Units	**704,629**	766,

[1] *Includes shipments to Altria Group, Inc., commencing in the third quarter of 2019, for sale in the United States under license.*

Following the deconsolidation of our Canadian subsidiary, we will continue to report the volume of brands sold by RBH for which other PMI subsidiaries are the trademark owners. These include *HEETS*, *Next*, *Philip Morris* and *Rooftop*.

Heated tobacco units ("HTU") is the term we use to refer to heated tobacco consumables, which for us include our *HEETS*, *HEETS Creations, HEETS Dimensions, HEETS Marlboro* and *HEETS FROM MARLBORO (*defined collectively as *HEETS)*, *Marlboro Dimensions*, *Marlboro HeatSticks* and *Parliament HeatSticks,* as well as the KT&G-licensed brands, *Fiit* and *Miix* (outside of Korea).

Market share for HTUs is defined as the total sales volume for HTUs as a percentage of the total estimated sales volume for cigarettes and HTUs.

Shipment volume of heated tobacco units to the United States is included in the heated tobacco unit shipment volume of the Latin America & Canada segment.

References to total international market, defined as worldwide cigarette and heated tobacco unit volume excluding the United States, total industry, total market and market shares throughout this *"Discussion and Analysis"* are our estimates for tax-paid products based on the latest available data from a number of internal and external sources and may, in defined instances, exclude the People's Republic of China and/or our duty free business. In addition, to reflect the deconsolidation of RBH, effective March 22, 2019, PMI's total market share has been restated for previous periods.

2020 estimates for total industry volume and market share in certain geographies reflect limitations on the availability and accuracy of industry data during pandemic-related restrictions.

In-market sales ("IMS") is defined as sales to the retail channel, depending on the market and distribution model.

North Africa is defined as Algeria, Egypt, Libya, Morocco and Tunisia.

The Gulf Cooperation Council ("GCC") is defined as Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates (UAE).

Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units.

From time to time, PMI’s shipment volumes are subject to the impact of distributor inventory movements, and estimated total industry/market volumes are subject to the impact of inventory movements in various trade channels that include estimated trade inventory movements of PMI’s competitors arising from market-specific factors that significantly distort reported volume disclosures. Such factors may include changes to the manufacturing supply chain, shipment methods, consumer demand, timing of excise tax increases or other influences that may affect the timing of sales to customers. In such instances, in addition to reviewing PMI shipment volumes and certain estimated total industry/market volumes on a reported basis, management reviews these measures on an adjusted basis that excludes the impact of distributor and/or estimated trade inventory movements. Management also believes that disclosing PMI shipment volumes and estimated total industry/market volumes in such circumstances on a basis that excludes the impact of distributor and/or estimated trade inventory movements improves the comparability of performance and trends for these measures over different reporting periods.

2020 compared with 2019

The following discussion compares our consolidated operating results for the year ended December 31, 2020, with the year ended December 31, 2019.

Estimated international industry cigarette and heated tobacco unit volume, excluding China and the United States, of 2.5 trillion, decreased by 5.8%, due to all PMI Regions, as described in the Regional sections below.

Our total shipment volume decreased by 8.1%, due to:

- the EU, reflecting lower cigarette shipment volume, notably in Italy, Poland and Spain, partly offset by higher heated tobacco unit shipment volume across the Region, particularly in Italy and Poland;

- Middle East & Africa, reflecting lower cigarette shipment volume, primarily in PMI Duty Free and Turkey, as well as lower heated tobacco unit shipment volume due to PMI Duty Free;
- South & Southeast Asia, reflecting lower cigarette shipment volume, primarily in Indonesia, Pakistan and the Philippines;

- East Asia & Australia, reflecting lower cigarette shipment volume, predominantly in Japan, partly offset by higher heated tobacco unit shipment volume driven by Japan; and
- Latin America & Canada, reflecting lower cigarette shipment volume, primarily in Argentina and Mexico, partially offset by Brazil. Excluding the volume impact from the RBH deconsolidation, our total shipment volume in the Region decreased by 10.3%;

partly offset by

- Eastern Europe, reflecting higher heated tobacco unit shipment volume across the Region, notably in Russia and Ukraine, partly offset by lower cigarette shipment volume, mainly in Russia and Ukraine.

Excluding the volume impact from the RBH deconsolidation of approximately 1.0 billion units (reflecting first quarter 2019 volume of RBH-owned brands and including Duty-Free sales of these brands in Canada), PMI's total shipment volume decreased by 7.9%.

Impact of Inventory Movements

The net impact of estimated distributor inventory movements for the full year was immaterial. Excluding the volume impact from the deconsolidation of RBH, our total in-market sales declined by 7.8%.

Our cigarette shipment volume by brand and heated tobacco unit shipment volume was as follows:

PMI Shipment Volume by Brand (Million Units)

	Full-Year		
	2020	**2019**	**Change**
Cigarettes			
Marlboro	**233,158**	262,908	(11.3)%
L&M	**91,098**	92,873	(1.9)%
Chesterfield	**52,139**	57,185	(8.8)%
Philip Morris	**45,645**	49,164	(7.2)%
Parliament	**34,737**	38,723	(10.3)%
Sampoerna A	**32,862**	35,133	(6.5)%
Dji Sam Soe	**24,754**	32,435	(23.7)%
Bond Street	**24,113**	28,025	(14.0)%
Lark	**15,489**	19,602	(21.0)%
Next	**8,980**	8,602	4.4 %
Others	**65,543**	82,059	(20.1)%
Total Cigarettes	**628,518**	706,709	(11.1)%
Heated Tobacco Units [1]	**76,111**	59,652	27.6 %
Total Cigarettes and Heated Tobacco Units	**704,629**	766,361	(8.1)%

[1] *Includes shipments to Altria Group, Inc., commencing in the third quarter of 2019, for sale in the United States under license.*

Note: *Sampoerna A* includes *Sampoerna*; *Philip Morris* includes *Philip Morris/Dubliss*; *Lark* includes *Lark Harmony; and Next includes Next/Dubliss*

Our cigarette shipment volume of the following brands decreased:

- *Marlboro,* mainly due to Indonesia, Italy, Japan, Mexico, the Philippines, PMI Duty Free, Saudi Arabia and Turkey, partly offset by Russia;
- *L&M*, notably due to PMI Duty Free and Poland, partly offset by Mexico and Turkey;
- *Chesterfield*, mainly due to Poland, Russia and Turkey, partly offset by Brazil and Saudi Arabia;
- *Philip Morris*, primarily due to Argentina and Italy, partly offset by Russia;

- *Parliament*, mainly due to PMI Duty Free, Russia and Turkey;
- *Sampoerna A* in Indonesia, mainly due to premium *A Mild*;

- *Dji Sam Soe* in Indonesia, mainly due to *Dji Sam Soe Magnum Mild*;
- *Bond Street*, largely due to Russia and Ukraine;
- *Lark*, primarily due to Japan and Turkey; and
- "Others," notably due to: the impact of the deconsolidation of RBH in Canada; mid-price *Fortune* and *Hope* in the Philippines, *Muratti* in Turkey and *Sampoerna U* in Indonesia; and low-price *Baronet* (morphed to *L&M*) in Mexico, *Jackpot* in the Philippines and *Morven* in Pakistan; partly offset by mid-price *Sampoerna Hijau* in Indonesia.

Our cigarette shipment volume of the following brand increased:

- *Next*, notably driven by Israel and Russia.

The increase in our heated tobacco unit shipment volume was mainly driven by the EU (notably Italy and Poland), Eastern Europe (notably Russia and Ukraine) and Japan, partly offset by PMI Duty Free.

2020 International Share of Market (excluding China and the United States)

Our total international market share (excluding China and the U.S.), defined as our cigarette and heated tobacco unit sales volume as a percentage of total industry cigarette and heated tobacco unit sales volume, decreased by 0.7 points to 27.7%, reflecting:

- Total international market share for cigarettes of 24.7%, down by 1.5 points; and
- Total international market share for heated tobacco units of 3.0%, up by 0.8 points.

Our total international cigarette sales volume as a percentage of total industry cigarette sales volume was down by 1.2 points to 25.7%, mainly reflecting: out-switching to heated tobacco units, as well as lower cigarette market share and/or an unfavorable geographic mix impact, notably in Indonesia, Mexico, the Philippines and PMI Duty Free, partly offset by Brazil and Germany.

In 2020, we owned five of the world's top 15 international cigarette brands, with international cigarette market shares as follows: *Marlboro*, 9.5%; *L&M*, 3.7%; *Chesterfield*, 2.2%; *Philip Morris*, 1.9%; and *Parliament*, 1.4%.

Key Market Data

Key market data regarding total market size, our shipments and market share were as follows:

Market	Total Market (billion units)		PMI Shipments (billion units)						PMI Market Share (%)[1]			
			Total		Cigarette		Heated Tobacco Unit		Total		Heated Tobacco Unit	
	2020	2019	2020	2019	2020	2019	2020	2019	2020	2019	2020	2019
Total	2,548.4	2,705.0	704.6	766.4	628.5	706.7	76.1	59.7	27.7	28.4	3.0	2.2
European Union												
France	36.6	37.9	16.3	17.0	16.1	16.9	0.2	0.1	44.9	45.0	0.5	0.2
Germany	74.6	73.3	29.1	27.9	27.4	27.0	1.6	0.9	39.0	38.0	2.2	1.2
Italy	67.4	67.9	34.6	34.9	29.0	31.4	5.6	3.5	52.2	51.8	8.1	4.8
Poland	45.6	46.2	17.8	19.0	15.4	17.9	2.4	1.1	39.0	41.2	5.2	2.5
Spain	41.8	45.4	13.2	14.5	12.8	14.1	0.4	0.3	31.4	31.3	1.0	0.7
Eastern Europe												
Russia	219.1	226.5	69.2	68.0	55.6	58.8	13.6	9.2	32.3	30.1	6.3	3.8
Middle East & Africa												
Saudi Arabia	21.7	20.8	9.1	9.2	9.0	9.2	0.1	—	39.0	43.0	0.3	—
Turkey	114.8	119.7	47.5	51.9	47.5	51.9	—	—	41.3	43.4	—	—
South & Southeast Asia												
Indonesia	276.3	305.7	79.5	98.5	79.5	98.5	—	—	28.8	32.2	—	—
Philippines	62.1	70.5	41.7	49.7	41.7	49.7	—	—	67.2	70.5	0.1	—
East Asia & Australia												
Australia	11.0	12.0	3.3	3.3	3.3	3.3	—	—	29.9	27.5	—	—
Japan	142.9	157.8	51.1	52.4	22.2	26.6	28.9	25.8	37.1	34.5	20.4	17.1
Korea	71.6	68.6	14.8	15.5	10.2	10.8	4.6	4.6	20.7	22.6	6.5	6.8
Latin America & Canada												
Argentina	33.6	33.4	20.5	23.3	20.5	23.3	—	—	61.0	70.0	—	—
Mexico	30.7	35.5	19.5	23.8	19.5	23.8	0.1	—	63.7	67.1	0.2	—

(1) Market share estimates are calculated using IMS data

Note: % change for Total Market and PMI shipments is computed based on millions of units; PMI Market Share estimates for previous periods are restated to reflect RBH deconsolidation and exclude RBH-owned brands.

Financial Summary

Financial Summary - Years Ended December 31, (in millions)	2020	2019	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Cur-rency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/ Mix	Variance Fav./(Unfav.) Cost/ Other[1]
Net Revenues	**$ 28,694**	$ 29,805	(3.7)%	(2.2)%	$(1,111)	$ (469)	$ 794	$(1,183)	$ (253)
Cost of Sales	**(9,569)**	(10,513)	9.0 %	7.5 %	944	158	—	464	322
Marketing, Administration and Research Costs [2]	**(7,384)**	(8,695)	15.1 %	17.0 %	1,311	(166)	—	—	1,477
Amortization of Intangibles	**(73)**	(66)	(10.6)%	(13.6)%	(7)	2	—	—	(9)
Operating Income	**$ 11,668**	$ 10,531	10.8 %	15.3 %	$ 1,137	$ (475)	$ 794	$ (719)	$ 1,537

[1] *Cost/Other variance includes the impact of the RBH deconsolidation.*

[2] *Favorable Cost/Other variance includes the 2019 Russia excise and VAT audit charge of $374 million, the 2019 Canadian tobacco litigation-related expense of $194 million, the 2019 loss on deconsolidation of RBH of $239 million, the 2019 asset impairment and exit costs of $422 million, the 2020 asset impairment and exit costs of ($149 million) and the 2020 Brazil indirect tax credit of $119 million, as well as the impact of the RBH deconsolidation.*

Note: Net Revenues include revenues from shipments of Platform 1 devices, heated tobacco units and accessories to Altria Group, Inc., commencing in the third quarter of 2019, for sale under license in the United States.

Net revenues, excluding unfavorable currency, decreased by 2.2%, reflecting: unfavorable volume/mix, primarily due to lower cigarette volume (mainly in Argentina, Indonesia, Italy, Japan, Mexico, the Philippines, PMI Duty Free, Poland, Russia and Ukraine, partly offset by Germany), partially offset by higher heated tobacco unit volume (notably in the EU, Japan, Russia and Ukraine, partly offset by PMI Duty Free); and the unfavorable impact of $253 million, shown in "Cost/Other," mainly resulting from the deconsolidation of RBH and lower fees for certain distribution rights billed to customers in certain markets; partly offset by a favorable pricing variance (notably driven by the GCC, Germany, Japan, Mexico, North Africa, the Philippines, PMI Duty Free, Russia and Ukraine, partially offset by Indonesia, Poland and Turkey).

The unfavorable currency in net revenues was due primarily to the Brazilian real, Indonesian rupiah, Mexican pesos, Russian ruble and Turkish lira, partially offset by the Euro, Japanese yen and Philippine peso.

Net revenues include $6.8 billion in 2020 and $5.6 billion in 2019 related to the sale of RRPs. *IQOS* devices accounted for approximately 7% of RRP net revenues for the year ended December 31, 2020, mainly due to a naturally lower ratio of new users to existing users, longer replacement cycles and geographic mix.

Operating income, excluding unfavorable currency, increased by 15.3%, notably reflecting a favorable comparison, shown in "Cost/Other," of a net charge of $30 million recorded in 2020 related to asset impairment and exit costs of $149 million (associated with organizational design optimization) and the Brazil indirect tax credit of $119 million, to charges recorded in 2019 of $1.2 billion, related to: asset impairment and exit costs ($422 million), associated with plant closures in Argentina, Colombia, Germany and Pakistan), the loss on the deconsolidation of RBH ($239 million), the Canadian tobacco litigation-related expense ($194 million), and the Russia excise and VAT audit charge ($374 million).

Excluding these 2020 and 2019 items noted above, and unfavorable currency of $475 million, operating income increased by 3.5%, primarily reflecting: a favorable pricing variance; lower manufacturing costs (driven by productivity gains related to reduced-risk and combustible products) and lower marketing, administration and research costs (partly driven by cost efficiencies); partially offset by unfavorable volume/mix, mainly due to lower cigarette volume (primarily in Indonesia, Italy, Japan, Mexico, the Philippines, PMI Duty Free, Poland and Russia), partly offset by higher heated tobacco unit volume (notably in the EU, Japan, Russia and Ukraine, partially offset by PMI Duty Free); and the unfavorable impact of the deconsolidation of RBH, included in "Cost/Other."

Interest expense, net, of $618 million increased by $48 million (8.4%) due primarily to lower interest earned on cash balances.

Our effective tax rate decreased by 1.5 percentage points to 21.7%. The effective tax rate for the year ended December 31, 2020 was favorably impacted by changes in earnings mix by taxing jurisdiction, a reduction of U.S. state tax expense, a reduction of estimated U.S. federal income tax liabilities for years 2018 and 2019 due to final regulations under the GILTI provisions of the Internal Revenue Code ($93 million) and the corporate income tax rate reduction in Indonesia, partially offset by a decrease in deductions related to

foreign-derived intangible income for the years 2018 and 2019 and repatriation cost differences. We estimate that our 2021 effective tax rate will be around 22%, excluding discrete tax events. Changes in currency exchange rates, earnings mix by taxing jurisdiction or future regulatory developments may have an impact on the effective tax rates, which we monitor each quarter. Significant judgment is required in determining income tax provisions and in evaluating tax positions. For further details, see Item 8, Note 11. *Income Taxes*.

We are regularly examined by tax authorities around the world, and we are currently under examination in a number of jurisdictions. It is reasonably possible that within the next 12 months certain tax examinations will close, which could result in a change in unrecognized tax benefits along with related interest and penalties. An estimate of any possible change cannot be made at this time.

Net earnings attributable to PMI of $8.1 billion increased by $871 million or 12.1%. This increase was due primarily to higher operating income as discussed above and a lower effective tax rate. Diluted and basic EPS of $5.16 increased by 11.9%. Excluding an unfavorable currency impact of $0.32, diluted EPS increased by 18.9%.

2019 compared with 2018

For a discussion comparing our consolidated operating results for the year ended December 31, 2019, with the year ended December 31, 2018, refer to Part II, Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operation - Discussion and Analysis - Consolidated Operating Results* in our Annual Report on Form 10-K for the year ended December 31, 2019, which was filed with the U.S. Securities and Exchange Commission on February 7, 2020.

Operating Results by Business Segment

Business Environment

Taxes, Legislation, Regulation and Other Matters Regarding the Manufacture, Marketing, Sale and Use of Tobacco Products

The tobacco industry and our company face a number of challenges that may adversely affect our business, volume, results of operations, cash flows and financial position. These challenges, which are discussed below and in "*Cautionary Factors That May Affect Future Results*," include:

- regulatory restrictions on our products, including restrictions on the packaging, marketing, and sale of tobacco or other nicotine-containing products that could reduce our competitiveness, eliminate our ability to communicate with adult consumers, or even ban certain of our products;
- fiscal challenges, such as excessive excise tax increases and discriminatory tax structures;
- illicit trade in cigarettes and other tobacco and nicotine-containing products, including counterfeit, contraband and so-called "illicit whites";
- intense competition, including from non-tax paid volume by certain local manufacturers;
- pending and threatened litigation as discussed in Item 8, Note 17. *Contingencies*; and
- governmental investigations.

<u>*Regulatory Restrictions:*</u> The tobacco industry operates in a highly regulated environment. The well-known risks of smoking have led regulators to impose significant restrictions and high excise taxes on cigarettes.

Much of the regulation that shapes the business environment in which we operate is driven by the World Health Organization's ("WHO") Framework Convention on Tobacco Control ("FCTC"), which entered into force in 2005. The FCTC has as its main objective to establish a global agenda for tobacco regulation, with the purpose of reducing tobacco use. To date, 181 countries and the European Union are Parties to the FCTC. The treaty requires Parties to have in place various tobacco control measures and recommends others. The FCTC governing body, the Conference of the Parties ("CoP"), has also adopted non-binding guidelines and policy recommendations related to certain

articles of the FCTC that go beyond the text of the treaty. In October 2018, the CoP recognized the need for more scientific assessment and improved reporting to define policy on heated tobacco products. Similar to its previous policy recommendations on e-cigarettes, the CoP invited countries to regulate, restrict or prohibit heated tobacco products, as appropriate under their national laws.

In July 2019, the WHO issued the Report on the Global Tobacco Epidemic 2019. While citing insufficient independent studies regarding the benefits and the unknown long-term health impacts of electronic nicotine delivery systems and heated tobacco products, the WHO has taken the position that such products are not risk-free and should be regulated in the same manner as cigarettes and in line with the FCTC provisions. It is not possible to predict whether or to what extent measures recommended by the WHO, including the FCTC guidelines, will be implemented.

We believe that when better alternatives to cigarettes exist, the discussion should not be whether these alternatives should be made available to the more than one billion men and women who smoke today, but how fast, and within what regulatory framework to maximize their adoption while minimizing unintended use. Therefore, we advocate for regulatory frameworks that recognize a significant difference on a risk continuum between combustible tobacco on the one hand and non-combustible tobacco and other nicotine-containing products on the other. Regulation should include measures that will accelerate switching to non-combustible products, for example, by allowing adult consumers who would not otherwise quit to receive truthful and non-misleading information about such products to enable them to make informed decisions and by applying uniform product standards to enable manufacturers to demonstrate the safety of these products as well as the absence of combustion. Regulation should also include specific rules for ingredients, labeling and consumer communication, and should ensure that the public is informed about the health risks of all combustible and non-combustible tobacco and nicotine-containing products. Importantly, regulation must include measures designed to prevent initiation by youth and non-smokers. We support mandated health warnings, minimum age laws, restrictions on advertising, and public place smoking restrictions. We also support regulatory measures that help reduce illicit trade.

Certain measures are discussed in more detail below and in the *Reduced-Risk Products (RRPs)* section.

Fiscal Challenges: Excessive and disruptive excise, sales and other tax increases and discriminatory tax structures are expected to continue to have an adverse impact on our profitability, due to lower consumption and consumer down-trading to non-premium, discount, other low-price or low-taxed combustible tobacco products such as fine cut tobacco and illicit cigarettes. In addition, in certain jurisdictions, some of our combustible products are subject to tax structures that discriminate against premium-price products and manufactured cigarettes. We believe that such tax policies undermine public health by encouraging consumers to turn to illicit trade, and ultimately undercut government revenue objectives, disrupt the competitive environment, and encourage criminal activity. Other jurisdictions have imposed, or are seeking to impose, levies or other taxes specifically on tobacco companies, such as taxes on revenues and/or profits.

World Customs Organization Developments: In 2020, the World Customs Organization ("WCO") amended the harmonized system nomenclature to introduce dedicated custom codes for novel tobacco and nicotine products, including heated tobacco products, e-cigarettes and other nicotine-containing products. The amendments will be effective as of January 1, 2022. These amendments require WCO member states to transfer products from customs codes in the current nomenclature to the new one. These amendments are not expected to significantly impact current customs duty rates.

EU Tobacco Products Directive: In April 2014, the EU adopted a significantly revised EU Tobacco Products Directive (TPD), which entered into force in May 2016. All member states have adopted laws transposing the TPD. The TPD sets forth a comprehensive set of regulatory requirements for tobacco products, including:

- health warnings covering 65% of the front and back panels of cigarette packs, with an option for member states to further standardize tobacco packaging, including the introduction of plain packaging;
- a ban on characterizing flavors in some tobacco products, with a transition period for menthol that expired in May 2020;
- security features and tracking and tracing measures that became effective on May 20, 2019; and
- a framework for the regulation of novel tobacco products and e-cigarettes, including requirements for health warnings and information leaflets, a prohibition on product packaging text related to reduced risk, and the introduction of notification requirements or authorization procedures in advance of commercialization.

The EU Commission's Directorate General for Health and Food Safety is preparing a report on the implementation of the TPD, including the evaluation of whether the TPD has achieved its objectives and is still relevant considering

scientific, international and technical developments, including in novel tobacco products and e-cigarettes. The report is expected to include recommendations on potential revisions of the TPD to account for such developments. The report is due by May 2021.

EU Tobacco Excise Directive: The EU Commission is preparing a legislative proposal for the revision of the 2011 EU Tobacco Excise Directive that may include definitions and tax treatment for novel tobacco and nicotine-containing products, including heated tobacco products and e-cigarettes. The proposal is expected to be finalized by the end of 2021. The adoption of the proposal will require unanimous agreement by all EU member states.

Plain Packaging and Other Packaging Restrictions: Plain packaging legislation bans the use of branding, logos and colors on packaging other than the brand name and variant that may be printed only in specified locations and in a uniform font. To date, plain packaging laws have been adopted in certain markets in all of our operating segments, including the key markets of Australia, France, Saudi Arabia and Turkey. Some countries, such as Canada, New Zealand, Israel and Denmark adopted plain packaging regulations that apply to all tobacco products, including RRPs. Other countries are also considering plain packaging legislation.

Some countries have adopted, or are considering adopting, packaging restrictions that could have an impact similar to plain packaging. Examples of such restrictions include standardizing the shape and size of packages, prohibiting certain colors or the use of certain descriptive phrases on packaging, and requiring very large graphic health warnings that leave little space for branding.

Restrictions and Bans on the Use of Ingredients: The WHO and others in the public health community have recommended restrictions or total bans on the use of some or all ingredients in tobacco products, including menthol. Broad restrictions and ingredient bans would require us to reformulate our American blend tobacco products and could reduce our ability to differentiate these products in the market in the long term. In many countries, menthol bans would eliminate the entire category of mentholated tobacco products. The European Union banned cigarettes and roll-your-own tobacco products with characterizing flavors. Other tobacco products, including heated tobacco products, are exempted from this flavor ban. The EU Commission is required to withdraw this exemption for a particular product category if it determines that there is a substantial change of circumstances, such as a significant increase of EU-wide sales volumes in such product category. Other countries may follow the EU's approach. Turkey banned menthol as of May 2020. Broader ingredient bans have been adopted by Canada and Brazil.
Bans on Display of Tobacco Products at Retail: In a number of our markets, including, but not limited to, Australia and Russia, governments have banned the display of tobacco products at the point of sale. Other countries are considering similar bans.

Bans and Restrictions on Advertising, Marketing, Promotions and Sponsorships: For many years, the FCTC has called for, and countries have imposed, partial or total bans on tobacco advertising, marketing, promotions and sponsorships, including bans and restrictions on advertising on radio and television, in print and on the Internet. The FCTC's non-binding guidelines recommend that governments prohibit all forms of communication with adult smokers.

Restrictions on Product Design: Some members of the public health community are calling for the further standardization of tobacco products by requiring, for example, that cigarettes have a certain minimum diameter, which would amount to a ban on slim cigarettes, or requiring the use of standardized filter and cigarette paper designs. In addition, at its meeting in November 2016, the CoP adopted non-binding guidelines recommending that countries regulate product design features that increase the attractiveness of tobacco products, such as the diameter of cigarettes and the use of flavor capsules.

Restrictions on Public Smoking and Use of Nicotine-Containing Products in Public: The pace and scope of restrictions on the use of our products have increased significantly in most of our markets. Many countries around the world have adopted, or are likely to adopt, regulations that restrict or ban smoking and use of nicotine-containing products in public and/or work places, restaurants, bars and nightclubs. Some public health groups have called for, and some countries, regional governments and municipalities have adopted or proposed, bans on smoking in outdoor places, as well as bans on smoking in cars (typically, when minors are present) and private homes.

Other Regulatory Issues: Some regulators are considering, or in some cases have adopted, regulatory measures designed to reduce the supply of tobacco products. These include regulations intended to reduce the number of retailers selling tobacco products by, for example, reducing the overall number of tobacco retail licenses available or banning the sale of tobacco products within specified distances of certain public facilities. In addition, South Africa banned the sale of tobacco products, e-cigarettes, and electronic devices that heat tobacco for several months during the COVID-19 pandemic. The ban, which was lifted on August 17, 2020, resulted in a significant increase of illicit trade of tobacco products.

In a limited number of markets, most notably Japan, we are dependent on governmental approvals that may limit our pricing flexibility.

The EU Single-Use Plastics Directive, which will require tobacco manufacturers and importers to cover the costs of public collection systems for tobacco product filters, entered into force on July 2, 2019, after which member states will have two years to transpose it into national law. While we cannot predict the impact of this initiative on our business at this time, we are monitoring developments in this area.

Illicit Trade: Illicit tobacco trade creates a cheap and unregulated supply of tobacco products, undermines efforts to reduce smoking prevalence, especially among youth, damages legitimate businesses and intellectual property rights, stimulates organized crime,

increases corruption and reduces government tax revenue. Without accounting for any potential COVID-19-related impact, we generally estimate that, excluding China and the U.S., illicit trade may account for as much as 10 to 12% of global cigarette consumption; this includes counterfeit, contraband and the persistent problem of "illicit whites," which are cigarettes legally produced in one jurisdiction for the sole purpose of being exported and illegally sold in another jurisdiction where they have no legitimate market. Currently, we estimate that illicit trade in the European Union accounted for approximately 8% of total cigarette consumption in 2019.

A number of jurisdictions are considering actions to prevent illicit trade. In November 2012, the FCTC adopted the Protocol to Eliminate Illicit Trade in Tobacco Products (the "Protocol"), which includes supply chain control measures, such as licensing of manufacturers and distributors, enforcement of these control measures in free trade zones, controls on duty free and Internet channels and the implementation of tracking and tracing technologies. To date, 62 Parties, including the European Union, have ratified it. The Protocol came into force in September 2018. Parties must start implementing its provisions in their national legislation. In October 2018, the first Meeting of the Parties to the Protocol decided to produce a comprehensive report on good practices for the implementation of tracking and tracing systems and to prepare a conceptual framework for global information sharing to combat illicit tobacco trade. We welcome this decision and expect that other Parties will ratify the Protocol.

We devote substantial resources to help prevent illicit trade in combustible tobacco products and RRPs. For example, we engage with governments, our business partners and other stakeholders to implement effective measures to combat illicit trade and, in some instances, pursue legal remedies to protect our intellectual property rights.

The tracking and tracing regulations for cigarettes and roll-your-own products manufactured or destined for the EU became effective on May 20, 2019. The effective date for other tobacco-containing products, including some of our RRPs such as heated tobacco units, is May 20, 2024. While we expect that this regulation will increase our operating expenses, we do not expect this increase to be significant.

In 2009, our Colombian subsidiaries entered into an Investment and Cooperation Agreement with the national and regional governments of Colombia to promote investment in, and cooperation on, anti-contraband and anti-counterfeit efforts. The agreement provides $200 million in funding over a 20-year period to address issues such as combating illegal cigarette trade and increasing the quality and quantity of locally-grown tobacco.

In May 2016, PMI launched PMI IMPACT, a global initiative that supports third-party projects dedicated to fighting illegal trade and related crimes such as corruption, organized criminal networks and money laundering. The centerpiece of PMI IMPACT is a council of external independent experts in the fields of law, anti-corruption and law enforcement. The experts are responsible for evaluating and approving funding proposals for PMI IMPACT grants. PMI has pledged $100 million to fund projects within PMI IMPACT over three funding rounds.

Reduced-Risk Products (RRPs)

Our Approach to RRPs: We recognize that smoking cigarettes causes serious diseases and that the best way to avoid the harms of smoking is never to start or to quit. Nevertheless, it is predicted that over the next decade the number of smokers will remain largely unchanged from the current estimate of 1.1 billion, despite the considerable efforts to discourage smoking.

Cigarettes burn tobacco, which produces smoke. As a result of the combustion process, the smoker inhales various toxic substances. In contrast, RRPs do not burn tobacco and produce an aerosol that contains significantly lower levels of harmful and potentially harmful constituents ("HPHCs") than found in cigarette smoke.

For adult smokers who would otherwise continue to smoke, we believe that RRPs, while not risk-free, offer a much better consumer choice. Accordingly, our key strategic priorities are: to develop and commercialize products that present less risk of harm to adult smokers who switch to those products versus continued smoking; and to convince current adult smokers who would otherwise continue to smoke to switch to those products.

We recognize that this transformation from cigarettes to RRPs will take time and that the speed of transformation will depend in part upon factors beyond our control, such as the willingness of governments, regulators and other policy groups to embrace RRPs as a desired alternative to continued cigarette smoking. We also recognize that our part in this transformation must be funded from our existing cigarette business. For as long as a significant number of adult

smokers continues to smoke, it is critical that the industry be led by responsible and ethical manufacturers. Therefore, during the transformation, we intend to remain a leading international cigarette manufacturer.

We have a range of RRPs in various stages of development, scientific assessment and commercialization. We conduct rigorous scientific assessments of our RRP platforms to substantiate that they reduce exposure to HPHCs and, ultimately, that these products present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to them versus continued smoking. We draw upon a team of expert scientists and engineers from a broad spectrum of scientific disciplines and our extensive learnings of adult consumer preferences to develop and assess our RRPs. Our efforts are guided by the following key objectives:

- to develop RRPs that adult smokers who would otherwise continue to smoke find to be satisfying alternatives to smoking;
- for those adult smokers, our goal is to offer RRPs with a scientifically substantiated risk-reduction profile that approaches as closely as possible that associated with smoking cessation;
- to substantiate the reduction of risk for the individual adult smoker and the reduction of harm to the population as a whole, based on scientific evidence of the highest standard that is made available for scrutiny and review by external independent scientists and relevant regulatory bodies; and
- to advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs, including the communication of scientifically substantiated information to enable adult smokers to make better consumer choices.

Our RRP Platforms: Our product development is based on the elimination of combustion via tobacco heating and other innovative systems for aerosol generation, which we believe is the most promising path to providing a better consumer choice for those who would otherwise continue to smoke. We recognize that no single product will appeal to all adult smokers. Therefore, we are developing a portfolio of products intended to appeal to a variety of distinct adult consumer preferences.

Four PMI-developed RRP platforms are in various stages of development and commercialization readiness:

Platform 1 uses a precisely controlled heating device incorporating our *IQOS HeatControl* technology, into which a specially designed and proprietary tobacco unit is inserted and heated to generate an aerosol. We have conducted a series of clinical studies for this platform, the results of which were included in our submission to the U.S. Food and Drug Administration ("FDA") described below. We completed a 6+6-month exposure response study and shared the results with the FDA in April 2020. The study showed that for the group that switched to our Platform 1 product, the eight clinical risk endpoints that were tested as co-primary endpoints in the first six-month term moved in the same direction as observed for smoking cessation after 12 months of use of this product. In addition, we completed an 18-month combined chronic toxicity and carcinogenicity study in mice, which was on-going at the time of our FDA submission. We shared the results with the FDA in August 2018.

Platform 2 uses a pressed carbon heat source which, when ignited, generates a nicotine-containing aerosol by heating tobacco. The results of our pharmacokinetic study (that measured the nicotine pharmacokinetic profile as well as subjective effects) and of our five-day reduced exposure study indicate that this platform could be an acceptable substitute for adult smokers who seek an alternative to cigarettes. The reduced exposure study results showed a substantial reduction in relevant biomarkers of exposure to the measured HPHCs in those who switched to Platform 2 compared to those who continued to smoke cigarettes over a five-day period. The sustainability of this reduction as well as changes in clinical risk markers were assessed in a three-month reduced exposure study, which was completed in 2018.

Platform 3 provides an aerosol of nicotine salt. We have explored two routes for this platform, one with electronics and one without, and conducted nicotine pharmacokinetic studies with both versions. The results of our pharmacokinetic study related to the version without electronics indicate this product's potential as an acceptable alternative to continued cigarette smoking in terms of product satisfaction. In February 2020, we completed a product use and adaptation study in adult smokers for the product variant without electronics.

Platform 4 covers e-vapor products, which are battery-powered devices that produce an aerosol by vaporizing a nicotine-containing liquid solution. In 2020, our e-vapor products comprised devices with the "coil and wick" technology as well as our e-vapor mesh technology designed to ensure the consistency and quality of the generated aerosol compared to the products with the "coil and wick" technology. Recently, we discontinued the

commercialization of devices with the “coil and wick” technology. We conducted a nicotine pharmacokinetic study with respect to products with our e-vapor mesh technology in 2017. The results of this study indicate that these products are an effective means of nicotine delivery while being a satisfying alternative for e-cigarette users. In March 2019, a six-month pre-clinical study in mice evaluating the impact of e-cigarette vapor on the risks of pulmonary and cardiovascular disease compared to cigarette smoke was completed; this study did not pertain to a specific product. The study demonstrated that e-cigarette vapors induce significantly lower biological responses associated with cardiovascular and pulmonary diseases compared with cigarette smoke.

After we receive the results of our scientific studies mentioned above, in accordance with standard scientific practices, we intend to share the conclusions in scientific forums and to submit them for inclusion in peer-reviewed publications.

The research and development expense for our RRP portfolio accounted for 99%, 98% and 92% of our total research and development expense for the years ended December 31, 2020, 2019 and 2018, respectively. The research and development expense for the years ended December 31, 2020, 2019 and 2018, is set forth in Item 8, Note 14. *Additional Information* to the consolidated financial statements.

Commercialization of RRPs: We are building a new product category and tailor our commercialization strategy to the characteristics of each specific market. We focus our commercialization efforts on consumer retail experience, guided consumer trials and customer care, and increasingly, digital communication programs and e-commerce. In order to accelerate switching to our Platform 1 products, our initial market introductions typically entail one-to-one consumer engagement (in person or by digital means) and device discounts. These initial commercialization efforts require substantial investment, which we believe will moderate over time and further benefit from the increased use of digital engagement capabilities. During the COVID-19 pandemic, we accelerated our investments in, and pivot to, digital consumer engagement.

In 2014, we introduced our Platform 1 product in pilot city launches in Nagoya, Japan, and in Milan, Italy. Since then, we have continuously expanded our commercialization activities, and as of December 31, 2020 the product has been commercialized in 64 markets in key cities or nationwide. While our Platform 1 products are currently available for sale in Mexico, that country banned the importation of e-cigarettes and devices that heat tobacco.
We believe that only a very small percentage of adult smokers who convert to our Platform 1 product switch back to cigarettes.

We have integrated the production of our heated tobacco units into a number of our existing manufacturing facilities, are progressing with our plans to build manufacturing capacity for our other RRP platforms, and continue to optimize our manufacturing infrastructure.

An adequate supply chain for our RRP portfolio, including the supply of electronic devices, is important to our business. We work with two electronics manufacturing service providers for the supply of our Platform 1 and *IQOS VEEV* devices and a small number of other providers for other products in our RRP portfolio and related accessories. Due to the COVID-19 pandemic, the operations of our two electronic manufacturing service providers were temporarily suspended at different times. Even though these suspensions did not materially affect our operations, if both of these service providers were significantly constrained at the same time, the supply of the devices could be disrupted. Although we work closely with these service providers on monitoring their production capability and financial health, we cannot guarantee that they will remain capable of meeting their commitments, particularly during the COVID-19 pandemic; if they will not, the commercialization of our RRPs could be adversely affected. The production of our RRP portfolio requires various metals, and we believe that there is an adequate supply of such metals in the world markets to satisfy our current and anticipated production requirements. However, some components and materials necessary for the production of our RRPs, including those for the electronic devices, are obtained from single or limited sources, and can be subject to industry-wide shortages and price fluctuations. While we were successful in maintaining adequate supply of such components and materials so far, we may not be able to secure such supply going forward, particularly during the COVID-19 pandemic; this could negatively impact the commercialization of our RRPs. For details on the impact of COVID-19 on our production and supply chain, see the "*Executive Summary*" section within this Item 7 of this Form 10-K.

Our Platform 1 and *IQOS VEEV* devices are subject to standard product warranties generally for a period of 12 months from the date of purchase or such other periods as required by law. We discuss product warranties in more detail in Item 8, Note 5. *Product Warranty*. The significance of warranty claims is dependent on a number of factors, including device version mix, product failure rates, logistics and service delivery costs, and warranty policies, and may increase with the number of devices sold.

Product quality may affect consumer acceptance of our RRPs.

Our commercialization efforts for the other RRP platforms are as follows:

- In 2020, we started commercializing an improved version of our *IQOS MESH* product in New Zealand and the Czech Republic under the *IQOS VEEV* brand name. We currently plan to launch this product in additional markets under the *IQOS VEEV* or *VEEV* brand names.

- With respect to *TEEPS*, our Platform 2 product, we are finalizing our improvements to this product and plan to conduct a consumer test in 2021.

- Following the consumer test conducted in 2020 and the results of the product use and adaptation study described above, we are incorporating our learnings into our plans to improve our Platform 3 product.

Due to the COVID-19 pandemic, these plans may be delayed.

RRP Regulation and Taxation: RRPs contain nicotine and are not risk-free. As we describe in more detail above, we support science-based regulation and taxation of RRPs and believe that regulation and taxation should differentiate between cigarettes and products that present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to these products versus continued smoking and should recognize a continuum of risk for tobacco and other nicotine-containing products. Regulation, as well as industry practices, should reflect the fact that youth should not consume nicotine in any form.

Some governments have banned or are seeking to ban or severely restrict emerging tobacco and nicotine-containing products such as our RRPs and communication of truthful and non-misleading information about such products. For example, the commercialization of e-cigarettes and heat-not-burn products is prohibited in Australia, the commercialization of e-cigarettes is prohibited in Argentina, the importation of e-cigarettes and heat-not-burn products is prohibited in Turkey, and the importation of e-cigarettes and devices that heat tobacco is prohibited in Mexico.

These regulations might foreclose or unreasonably restrict adult consumer access even to products that might be shown to be a better consumer choice than continuing to smoke. During the COVID-19 pandemic, governments may temporarily be unable to focus on the development of science-based regulatory frameworks for the development and commercialization of RRPs or on the enforcement or implementation of regulations that are significant to our business.

We oppose blanket bans and unreasonable restrictions of products that have the potential to present less risk of harm compared to continued smoking. By contrast, we support regulation that sets clear standards for all RRP categories and propels innovation to benefit adult smokers who would otherwise continue to smoke.

In the United States, an established regulatory framework for assessing “Modified Risk Tobacco Products” and “New Tobacco Products” exists under the jurisdiction of the FDA. We submitted to the FDA a Modified Risk Tobacco Product Application (“MRTPA”) for our Platform 1 product in December 2016, and a Premarket Tobacco Product Application (“PMTA”) for our Platform 1 product in March 2017.

On April 30, 2019, the FDA determined that a version of our Platform 1 product, namely, *IQOS* 2.4 and three related consumables, is appropriate for the protection of public health and authorized it for sale in the United States. The FDA’s decision followed its comprehensive assessment of our PMTA. On December 7, 2020, the FDA reached the same determination for the *IQOS 3* device and authorized that version of our Platform 1 product for sale in the United States.

On July 7, 2020, the FDA determined that the available scientific evidence demonstrates that the issuance of an exposure modification order would be appropriate for the promotion of public health and authorized the marketing of a version of our Platform 1 product, namely *IQOS* 2.4 and three related consumables, as a "modified risk tobacco product." The FDA authorized the marketing of this product in the U.S. with the following information:

"AVAILABLE EVIDENCE TO DATE:

- the *IQOS* system heats tobacco but does not burn it.
- this significantly reduces the production of harmful and potentially harmful chemicals.
- scientific studies have shown that switching completely from conventional cigarettes to the *IQOS* system significantly reduces your body’s exposure to harmful or potentially harmful chemicals."

We must request and receive authorization from the FDA in order to continue marketing this product with the same modified exposure information after the present order expires in four years.

There are two types of MRTP orders the FDA may issue: a “risk modification” order or an “exposure modification” order. We had requested both types of orders. After review, the FDA determined that the evidence did not support issuing a "risk modification" order at this time but that it did support issuing an "exposure modification" order for the product. This determination included a finding that issuance of the exposure modification order is expected to benefit the health of the population as a whole.

We look forward to working with the FDA to provide any additional information they may require in order to market this product with reduced risk claims.

The FDA's PMTA and MRTP orders do not mean that the agency "approved" our Platform 1 product. These authorizations are subject to strict marketing, reporting and other requirements and are not a guarantee that the product will remain authorized, particularly if there is a significant uptake in youth or non-smoker initiation. The FDA will monitor the marketing of the product.

Some states and municipalities in the U.S. have introduced severe restrictions for the sale of certain e-cigarettes and tobacco products, including those authorized by the FDA. We believe that such restrictions on FDA-authorized products will not advance public health and will unreasonably limit adult consumer access to products that are shown to be a better alternative to continued smoking.

In March 2020, we requested a clarification from the FDA regarding the applicability of its new health warning requirements to our heated tobacco units sold in the United States.

In the U.S., tobacco and nicotine-containing products that were not commercially marketed as of February 15, 2007 are subject to review and authorization by the FDA. Manufacturers of all non-authorized products currently on the market were required to file a PMTA with the FDA by September 9, 2020. The FDA announced on September 9, 2020 that it will prioritize enforcement against any tobacco and nicotine-containing product sold without a PMTA.

FDA actions may influence the regulatory approach of other governments.

Until recently, there were no countries with specific product standards for heat-not-burn products. Currently, national standards setting minimum quality and safety requirements for such products have been adopted in several countries with technical heat-not-burn specifications and/or methods for demonstrating the absence of combustion. They are mandatory in Egypt, Jordan, Saudi Arabia, Tunisia and the UAE, and voluntary in the U.K., Russia, Ukraine, Kazakhstan, Kyrgyzstan, Vietnam, and Indonesia. In Japan, a voluntary standard sets minimum safety requirements for tobacco heating devices. We expect other governments to consider similar product standards and encourage making them mandatory.

All EU member states have transposed the EU Tobacco Products Directive, including the provisions on novel tobacco products, such as heated tobacco units, and e-cigarettes. Most of the EU member states require a notification submitted six months before the intended placing on the market of a novel tobacco product, while some require pre-market authorizations for the introduction of such products. To date, we have filed a comprehensive dossier summarizing our scientific assessment of our Platform 1 product in over 20 member states.

In addition, in Italy, in April 2018, we submitted an application for *HEETS*, used with the *IQOS* device, requesting regulatory recognition of the reduction of toxic substances and potential risk reduction resulting from switching to this product compared to continued cigarette smoking. In January 2019, our application was not granted primarily on the grounds of insufficient data and questions of methodology. Due to the constraints of the review process, we had been unable to supplement the application with all the data we subsequently filed with the FDA and to address methodological questions during the review. We plan to submit a new application where we will clarify the concerns raised by the decision and further strengthen our application by submitting additional evidence that became available since we submitted our first application, consistent with our FDA filings. We are confident that our evidence supports our application.

On October 31, 2019, our Australian subsidiary, Philip Morris Limited ("PML"), submitted an application to the Scheduling Committee of the Therapeutic Goods Administration of Australia ("TGA") seeking to exempt heated tobacco products from being prohibited in Australia. In August 2020, the TGA issued its decision denying the application and stating that it did not present compelling evidence to establish a public health benefit from greater access to nicotine in heated tobacco products.

To date, several governmental agencies have published their scientific findings that analyze the harm-reduction potential of certain RRPs versus continuing smoking, including:

In December 2017, at the request of the U.K. Department of Health and Public Health England, the U.K. Committee on Toxicity published its assessment of the risk of heat-not-burn products relative to cigarette smoking. This assessment included analysis of scientific data for two heat-not-burn products, one of which was our Platform 1 product. The assessment concluded that, while still harmful to health, compared with the known risks from cigarettes, heat-not-burn products are probably less harmful. Subsequently, in February 2018, Public Health England published a report stating that the available evidence suggests that heat-not-burn products may be considerably less harmful than cigarettes and more harmful than e-cigarettes.

In May 2018, the German Federal Institute for Risk Assessment ("BfR") published a study on the Platform 1 aerosol relative to cigarette smoke using the Health Canada Intense Smoking Regimen. BfR found reductions in selected HPHCs in a range of 80-99%. This publication indicates that significant reductions in the levels of selected toxicants are likely to reduce toxicant exposure, which BfR stated might be regarded as a discrete benefit compared to combustible cigarettes.

In May 2018, the Dutch National Institute for Public Health and Environment ("RIVM") published a factsheet on novel tobacco products that heat rather than burn tobacco, focusing on our Platform 1 product. RIVM analyzed the aerosol generated by our Platform 1 product and concluded that the use of this product, while still harmful to health, is probably less harmful than continued smoking.

In June 2018, the Korean Food and Drug Administration ("KFDA") issued a statement on products that heat rather than burn tobacco. The KFDA tested three heat-not-burn products, one of which was our Platform 1 product. The KFDA confirmed that the levels of the nine HPHCs tested in the aerosol of these products were on average approximately 90% lower compared to those measured in the cigarette smoke of the top five cigarette brands in South Korea. However, the KFDA stated that it could not establish that the tested heat-not-burn products are less harmful than cigarettes. In October 2018, our Korean subsidiary filed a request with a local court seeking information underlying KFDA's analysis, conclusions and public statements. In May 2020, the court ordered KFDA to produce certain records.

In August 2018, the Science & Technology Committee of the U.K. House of Commons published a report of its inquiry into e-cigarettes and heat-not-burn products. The report concluded that e-cigarettes are significantly less harmful to health than smoking tobacco. The report also observed that for those smokers who do not accept e-cigarettes, heat-not-burn products may offer a public health benefit despite their relative risk. The report called for a risk-proportionate regulatory environment for both e-cigarettes and heat-not-burn products and noted that e-cigarettes should remain the least taxed, cigarettes the most taxed, with heat-not-burn products falling between the two. The U.K. Committee on Advertising Practice announced the removal of a prohibition of health claims in the advertising of e-cigarettes in the U.K. effective November 2018.

In November 2018, the Eurasian Economic Commission (regulatory body of the Eurasian Union consisting of Armenia, Belarus, Kazakhstan, Kyrgyzstan and Russia) published the results of its commissioned study on novel nicotine-containing products, including our Platform 1 product. The study confirms significantly lower levels of HPHCs in the aerosol generated by this product compared to cigarette smoke.

In January 2019, scientific media published the results of the study of the China National Tobacco Quality Supervision and Test Centre ("CNTQST") comparing the aerosol generated by our Platform 1 product with cigarette smoke. The CNTQST found that the former contained fewer, and lower levels of, harmful constituents than the latter and concluded that the lower temperature of heating tobacco in our Platform 1 product contributed to the difference. The CNTQST stated that the reduction in emissions of harmful constituents cannot be interpreted as equivalent to a proportionate harm/risk reduction for smokers.

The foregoing scientific findings of government agencies may not be indicative of the measures that the relevant government authorities could take in regulating our products.

We make our scientific findings publicly available for scrutiny and peer review through several channels, including our websites. From time to time, adult consumers, competitors, members of the scientific community, and others inquire into our scientific methodologies, challenge our scientific conclusions or request further study of certain aspects of our RRPs and their health effects. We are committed to a robust and open scientific debate and believe that such debate should be based on accurate and reliable scientific information. We seek to provide accurate and reliable scientific information about our RRPs; nonetheless, we may not be able to prevent third-party dissemination of false, misleading or unsubstantiated information about these products. The dissemination of scientifically unsubstantiated information or studies with a strong confirmation bias by third parties may cause confusion among adult smokers and affect their decision to switch to better alternatives to continued smoking, such as our RRPs.

To date, we have been largely successful in demonstrating to regulators that our heated tobacco units are not cigarettes due to the absence of combustion, and as such they are generally taxed either as a separate category or as

other tobacco products, which typically yields more favorable tax rates than cigarettes. Although we believe that this is sensible from the public health perspective, we cannot guarantee that regulators will continue this approach.

There can be no assurance that we will succeed in our efforts to replace cigarettes with RRPs or that regulation will allow us to commercialize RRPs in all markets, to communicate about our RRPs, including making scientifically substantiated risk-reduction claims, or to treat RRPs differently from cigarettes.

Legal Challenges to RRPs: We face various administrative and legal challenges related to certain RRP activities, including allegations concerning product classification, advertising restrictions, corporate communications, product coach activities, scientific substantiation, product liability, and unfair competition. While we design our programs to comply with relevant regulations, we expect these or similar challenges to continue as we expand our efforts to commercialize RRPs and to communicate publicly. The outcomes of these matters may affect our RRP commercialization and public communication activities and performance in one or more markets.

Our RRP Business Development Initiatives: In December 2013, we established a strategic framework with Altria Group, Inc. ("Altria") setting out terms on how the parties would collaborate to develop and commercialize e-vapor products and commercialize two of our RRPs in the U.S. In late 2018, Altria announced that it will participate in the e-vapor category only through another e-vapor company in which Altria acquired a minority interest. In September 2019, Altria's subsidiary, Philip Morris USA Inc. ("PM USA"), began commercialization of a version of our Platform 1 product in the U.S. PM USA is responsible for the marketing of this product in the U.S. and communication of the reduced exposure information authorized by the FDA in its MRTP marketing order described above.

In January 2020, we announced an agreement with KT&G, a leading tobacco and nicotine company in South Korea, for the commercialization of KT&G's smoke-free products outside of South Korea on an exclusive basis. For more information, see *Acquisitions and Other Business Arrangements* below.

Other Developments: In September 2017, we announced our support of the Foundation for a Smoke-Free World. In September 2020, our pledge agreement with the Foundation was amended. We contributed $45 million in 2020 and expect to contribute $40 million in 2021 and $35 million annually from 2022 through 2029, as specified in the amended pledge agreement. To date, we contributed a total of $209.5 million. The Foundation is an independent body and is governed by its independent Board of Directors. The Foundation's role, as set out in its corporate charter, includes funding research in the field of tobacco harm reduction, encouraging measures that reduce the harm caused by smoking, and assessing the effect of reduced cigarette consumption on the industry value chain.

Governmental Investigations

From time to time, we are subject to governmental investigations on a range of matters, including tax, customs, antitrust, advertising, and labor practices. We describe certain matters pending in Thailand, Russia and South Korea in Item 8, Note 17. *Contingencies*.

In November 2010, a WTO panel issued its decision in a dispute relating to facts that arose from August 2006 between the Philippines and Thailand concerning a series of Thai customs and tax measures affecting cigarettes imported by PM Thailand into Thailand (see Item 8, Note 17. *Contingencies* for additional information). The WTO panel decision, which was upheld by the WTO Appellate Body, concluded that Thailand had no basis to find that PM Thailand's declared customs values and taxes paid were too low, as alleged by the Department of Special Investigations of the government of Thailand ("DSI") in 2009. The decision also created obligations for Thailand to revise its laws, regulations, or practices affecting the customs valuation and tax treatment of future cigarette imports. Thailand agreed in September 2011 to fully comply with the decision by October 2012. The Philippines asserts that to date Thailand has not fully complied with the WTO panel decision and commenced challenges at the WTO Appellate Body. The WTO Appellate Body is not operational, and the appeals by Thailand are suspended indefinitely. In December 2020, the Philippines and Thailand agreed to pursue facilitator-assisted discussions aimed at progressing and resolving outstanding issues. It is not possible to predict any future developments in these proceedings or the outcome of these discussions.

The Public Prosecutor's office of Rome, Italy, notified our Italian subsidiary, Philip Morris Italia S.r.l. ("PM Italia"), as well as three former or current employees and a former external consultant of PM Italia in July 2020 and March 2020, respectively, that it concluded a preliminary investigation against them for alleged contravention of anti-corruption laws and related disruption of trade freedom. The Public Prosecutor alleges that the individuals involved promised certain personal favors to government officials from January to July of 2018 in exchange for favorable treatment for PM Italia, and that PM Italia lacked appropriate organizational controls to prevent the alleged actions by the individuals. In September 2020, the Public Prosecutor referred the matter to trial. PM Italia believes the charges brought against it by the Public Prosecutor are without merit and will defend them vigorously.

Asset Impairment and Exit Costs

We discuss asset impairment and exit costs in Item 8, Note 19. *Asset Impairment and Exit Costs* to our consolidated financial statements.

Acquisitions and Other Business Arrangements

We discuss our acquisitions in Item 8, Note 6. *Acquisitions* to our consolidated financial statements.

Global Collaboration Agreement with KT&G

In January 2020, PMI announced a global collaboration agreement with the leading tobacco and nicotine company in South Korea, KT&G, to commercialize KT&G's smoke-free products outside of the country. The agreement will run for an initial period of three years. The two companies plan for global collaboration with the intention to actively expand to cover many markets, based on commercial success. The agreement allows PMI to distribute current KT&G smoke-free products, and their evolutions, on an exclusive basis, and does not restrict PMI from distributing its own or third-party products. KT&G's smoke-free product brand portfolio includes heat-not-burn tobacco products (e.g., *LIL Mini* and *LIL Plus*), hybrid technologies that combine heat-not-burn tobacco and e-vapor technologies (e.g., *LIL HYBRID*), and e-vapor products (e.g., *LIL Vapor*). PMI will be responsible for the commercialization of smoke-free products supplied under the agreement.

Products sold under the agreement are subject to careful assessment to ensure they meet the regulatory requirements in the markets where they are launched, as well as our standards of quality and scientific substantiation to confirm the absence of combustion and significant reductions of emissions of harmful chemicals compared to cigarettes. PMI and KT&G will seek any necessary regulatory approvals that may be required on a market-by-market basis. There are no current plans to commercialize KT&G products in the United States.

In the third quarter of 2020, we launched commercial initiatives for licensed KT&G products in select markets.

Equity Investments

We discuss our equity investments in Item 8, Note 4. *Related Parties - Equity Investments and Other* to our consolidated financial statements.

Trade Policy

We are subject to various trade restrictions imposed by the United States of America and countries in which we do business ("Trade Sanctions"), including the trade and economic sanctions administered by the U.S. Department of the Treasury's Office of Foreign Assets Control and the U.S. Department of State. It is our policy to comply fully with these Trade Sanctions.

Tobacco products are agricultural products under U.S. law and are not technological or strategic in nature. From time to time we make sales in countries subject to Trade Sanctions, either where such sanctions do not apply to our business or pursuant to exemptions or licenses.

A subsidiary sells products to distributors that, in turn, sell those products to duty free customers that supply U.N. peacekeeping forces around the world, including those in the U.N. peacekeeping mission located in Abyei, a special administrative territory in Sudan. We do not believe that these sales, which are not subject to Trade Sanctions, and are *de minimis* in volume and value, present a material risk to our shareholders, our reputation or the value of our shares. We have no employees, operations or assets in Sudan.

We do not sell products in Iran, North Korea and Syria. From time to time, we explore opportunities to sell our products in one or more of these countries, as permitted by law.

We sell cigarettes in Cuba under a distribution agreement. These sales are permitted by U.S. law under a License Exception for Agricultural Commodities, issued by the United States Department of Commerce (Bureau of Industry and Security), granted to our distributor.

Certain states within the U.S. have enacted legislation permitting or requiring state pension funds to divest or abstain from future investment in stocks of companies that do business with certain countries that are sanctioned by the U.S. Because we do business in certain of these countries, these state pension funds may have divested of our stock or may not invest in our stock. We do not believe such legislation has had a material effect on the price of our shares.

2020 compared with 2019

The following discussion compares operating results within each of our operating segments for 2020 with 2019.

Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units. Estimates for total industry volume and market share in certain geographies reflect limitations on the availability and accuracy of industry data.

European Union:

Financial Summary - Years Ended December 31, (in millions)	2020	2019	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Cur-rency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/ Mix	Variance Fav./(Unfav.) Cost/ Other
Net Revenues	**$ 10,702**	$ 9,817	9.0 %	8.8 %	$ 885	$ 21	$ 187	$ 677	$ —
Operating Income	**$ 5,098**	$ 3,970	28.4 %	29.0 %	$ 1,128	$ (24)	$ 187	$ 663	$ 302

Net revenues, excluding favorable currency, increased by 8.8%, reflecting: favorable volume/mix, mainly driven by higher heated tobacco unit volume across the Region (notably in the Czech Republic, Germany, Hungary, Italy and Poland), partly offset by lower cigarette volume (notably in the Czech Republic, Italy, Poland and Spain, partly offset by Germany) and lower cigarette mix (mainly in Germany); and a favorable pricing variance (driven by higher combustible pricing, notably in Germany, partly offset by lower heated tobacco unit and *IQOS* device pricing).

Operating income, excluding unfavorable currency, increased by 29.0%, notably reflecting a favorable comparison, shown in "Cost/Other," of asset impairment and exit costs recorded in 2020 associated with organizational design optimization ($57 million), to those recorded in 2019 associated with a plant closure in Germany ($342 million).

Excluding these asset impairment and exit costs, as well as unfavorable currency of $24 million, operating income increased by 20.1%, primarily reflecting: favorable volume/mix, mainly driven by the same factors as for net revenues noted above; a favorable pricing variance; and lower manufacturing costs (notably in Germany); partly offset by higher marketing, administration and research costs (mainly related to increased investments behind reduced-risk products, notably in Germany and Poland).

European Union - Total Market, PMI Shipment and Market Share Commentaries

Total market, PMI shipment volume and market share performance are shown in the table below:

European Union Key Data	**Full-Year**		
	2020	**2019**	**Change % / pp**
Total Market (billion units)	**472.7**	482.8	(2.1)%
PMI Shipment Volume (million units)			
Cigarettes	**163,420**	174,319	(6.3)%
Heated Tobacco Units	**19,842**	12,569	57.9 %
Total European Union	**183,262**	186,888	(1.9)%
PMI Market Share			
Marlboro	**17.5 %**	18.0 %	(0.5)
L&M	**6.2 %**	6.7 %	(0.5)
Chesterfield	**5.5 %**	5.8 %	(0.3)
Philip Morris	**2.4 %**	2.7 %	(0.3)
HEETS	**4.2 %**	2.5 %	1.7
Others	**3.1 %**	3.1 %	—
Total European Union	**38.9 %**	38.8 %	0.1

Note: HEETS includes HEETS Dimensions.

The estimated total market in the EU decreased by 2.1% to 472.7 billion units, notably due to:

- Czech Republic, down by 10.9%, primarily reflecting lower border sales due to lockdown measures;
- France, down by 3.6%, mainly reflecting the impact of significant excise tax-driven price increases, partly offset by the pandemic-related impact of lower cross-border (non-domestic) purchases and a lower estimated prevalence of illicit trade due to border restrictions; and
- Spain, down by 7.8%, primarily reflecting lower in-bound tourism and border sales due to the pandemic;

partly offset by

- Germany, up by 1.9%, notably reflecting the pandemic-related impact of lower cross-border (non-domestic) purchases and reduced out-bound tourism, partly offset by the impact of retail price increases in the first quarter of 2020 and adult smoker out-switching to other combustible tobacco products.

Our total shipment volume decreased by 1.9% to 183.3 billion units, reflecting:

- lower cigarette shipment volume, mainly due to the lower total market and lower cigarette market share (notably in Italy and Poland, partly reflecting out-switching to heated tobacco units);

partly offset by

- higher heated tobacco unit shipment volume across the Region (notably in Germany, Italy and Poland), driven by higher market share.

Our Regional market share increased by 0.1 point to 38.9%, with gains in Germany and Italy, partly offset by a decline in Poland.

Eastern Europe:

Financial Summary - Years Ended December 31, (in millions)	2020	2019	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Cur-rency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/ Mix	Variance Fav./(Unfav.) Cost/ Other
Net Revenues	**$ 3,378**	$ 3,282	2.9 %	10.9 %	$ 96	$ (263)	$ 162	$ 197	$ —
Operating Income	**$ 871**	$ 547	59.2 %	100%	$ 324	$ (299)	$ 162	$ 146	$ 315

Net revenues, excluding unfavorable currency, increased by 10.9%, reflecting: favorable volume/mix, predominantly driven by higher heated tobacco unit volume across the Region (notably in Russia and Ukraine) and higher heated tobacco unit mix (mainly in Russia), partly offset by unfavorable cigarette volume (primarily in Russia and Ukraine, partially offset by Israel) and unfavorable cigarette mix (mainly in Russia); and a favorable pricing variance, driven by higher combustible pricing (primarily in Russia and Ukraine), partly offset by lower *IQOS* device pricing (mainly in Russia).

Operating income, excluding unfavorable currency, increased by over 100%, primarily reflecting a favorable comparison, shown in "Cost/Other," mainly due to a charge recorded in 2019 of $374 million, related to the Russia excise and VAT audit.

Excluding the 2019 Russia excise and VAT audit charge of $374 million, the 2020 charge for asset impairment and exit costs of $15 million and unfavorable currency of $299 million, operating income increased by 28.7%, reflecting: a favorable pricing variance; favorable volume/mix, driven by the same factors as for net revenues noted above; and lower manufacturing costs; partly offset by higher marketing, administration and research costs (partly related to increased investments behind reduced-risk products, notably in Russia and Ukraine).

Eastern Europe - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in Eastern Europe decreased by 4.6% to 379.4 billion units, notably due to:

- Russia, down by 3.3%, primarily reflecting the impact of price increases, partly offset by a lower estimated prevalence of illicit trade due to pandemic-related border restrictions; and
- Ukraine, down by 10.2%, mainly reflecting the impact of excise tax-driven price increases.

Our Regional market share increased by 1.8 points to 30.5%.

PMI Shipment Volume (million units)	202
Cigarettes	**93,46**
Heated Tobacco Units	**20,89**
Total Eastern Europe	**114,36**

Our total shipment volume increased by 0.2% to 114.4 billion units, mainly due to:

- Russia, up by 1.8%, or by 3.9% excluding the net unfavorable impact of estimated distributor inventory movements, primarily reflecting a higher market share, driven by heated tobacco units, partly offset by the lower total market;

partly offset by

- Ukraine, down by 4.3%, mainly due to the lower total market, partly offset by a higher market share driven by heated tobacco units.

Middle East & Africa:

Financial Summary - Years Ended December 31, (in millions)	2020	2019	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Currency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/Mix	Variance Fav./(Unfav.) Cost/Other
Net Revenues	**$ 3,088**	$ 4,042	(23.6)%	(21.7)%	$ (954)	$ (77)	$ 186	$(1,001)	$ (62)
Operating Income	**$ 1,026**	$ 1,684	(39.1)%	(35.2)%	$ (658)	$ (65)	$ 186	$ (784)	$ 5

Net revenues, excluding unfavorable currency, decreased by 21.7%, reflecting: unfavorable volume/mix, mainly due to lower cigarette volume, heated tobacco unit volume and *IQOS* device volume in PMI Duty Free, as well as lower cigarette volume in South Africa and Turkey; and lower fees for certain distribution rights billed to customers in certain markets, shown in "Cost/Other"; partially offset by a favorable pricing variance, driven by combustible pricing (mainly in the GCC, particularly Saudi Arabia, as well as North Africa and PMI Duty Free, partly offset by Turkey).

Operating income, excluding unfavorable currency, decreased by 35.2%, mainly reflecting: unfavorable volume/mix, predominantly due to lower cigarette and heated tobacco unit volume in PMI Duty Free; and lower fees for certain distribution rights as noted above for net revenues; partially offset by a favorable pricing variance; and lower marketing, administration and research costs.

Excluding asset impairment and exit costs of $19 million in 2020 and unfavorable currency of $65 million, operating income decreased by 34.1%.

Middle East & Africa - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in the Middle East & Africa decreased by 8.0% to 546.4 billion units, mainly due to:

- International Duty Free, down by 62.0%, reflecting the impact of government travel restrictions and reduced passenger traffic due to the pandemic;
- South Africa, down by 35.5%, primarily reflecting the impact of the pandemic-related ban on all tobacco sales from March 27, 2020, through August 17, 2020;
- Turkey, down by 4.2%, mainly reflecting the impact of lockdown measures on adult smoker average daily consumption, as well as a higher prevalence of illicit trade related to cut tobacco, particularly during the first-half of 2020, following significant industry-wide cigarette price increases in 2019; and
- The UAE, down by 38.1%, primarily reflecting the adverse impact on low-price brands from the implementation of a minimum excise tax and digital tax stamps in the second half of 2019.

Our Regional market share decreased by 1.4 points to 22.0%.

PMI Shipment Volume (million units)	202
Cigarettes	**117,99**
Heated Tobacco Units	**1,02**
Total Middle East & Africa	**119,02**

Our total shipment volume decreased by 13.3% to 119.0 billion units, notably due to:

- PMI Duty Free, down by 70.8%, or by 58.8% excluding the net unfavorable impact of estimated distributor inventory movements (principally due to cigarettes), mainly reflecting the lower total market; and

- Turkey, down by 8.5%, mainly reflecting the lower total market and a lower market share, notably due to adult smoker down-trading following the 2019 price increases.

South & Southeast Asia:

Financial Summary - Years Ended December 31,			**Change Fav./(Unfav.)**		**Variance Fav./(Unfav.)**				
(in millions)	**2020**	**2019**	**Total**	**Excl. Curr.**	**Total**	**Cur-rency**	**Price**	**Vol/ Mix**	**Cost/ Other**
Net Revenues	**$ 4,396**	$ 5,094	(13.7)%	(13.3)%	$ (698)	$ (19)	$ (44)	$ (635)	$ —
Operating Income	**$ 1,709**	$ 2,163	(21.0)%	(21.1)%	$ (454)	$ 2	$ (44)	$ (457)	$ 45

Net revenues, excluding unfavorable currency, decreased by 13.3%, reflecting: unfavorable volume/mix, primarily due to lower cigarette volume in Indonesia and the Philippines, partly offset by favorable cigarette mix in Indonesia; and an unfavorable pricing variance, due to combustible pricing in Indonesia, partly offset by the Philippines.

Operating income, excluding favorable currency, decreased by 21.1%, mainly reflecting: unfavorable volume/mix, due to the same factors as for net revenues noted above; and an unfavorable pricing variance; partly offset by lower marketing, administration and research costs (primarily in Indonesia).

Excluding asset impairment and exit costs of $23 million in 2020 and $20 million in 2019, as well as favorable currency of $2 million, operating income decreased by 20.8%.

South & Southeast Asia - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in South & Southeast Asia decreased by 8.7% to 672.3 billion units, notably due to:

- India, down by 17.9%, mainly reflecting the impact of lockdown restrictions on the movement of certain products, including tobacco;
- Indonesia, down by 9.6%, mainly reflecting the impact of excise tax-driven price increases and pandemic-related measures on adult smoker average daily consumption;
- Pakistan, down by 10.3%, mainly reflecting the impact of excise tax-driven price increases in June 2019 and price increases on PMI value brands in February 2020; and
- the Philippines, down by 12.0%, mainly reflecting the impact of pandemic-related quarantines, as well as industry-wide price increases in the third quarter of 2019 and the fourth quarter of 2020.

Our Regional market share decreased by 2.2 points to 21.5%.

PMI Shipment Volume (million units)	
	202
Cigarettes	**144,78**
Heated Tobacco Units	**3**
Total South & Southeast Asia	**144,82**

Our total shipment volume decreased by 17.2% to 144.8 billion units, notably due to:

- Indonesia, down by 19.3%, reflecting the lower total market, as well as a lower market share, mainly due to: adult smoker down-trading to the tax-advantaged 'below tier one' segment, the impact of elevated price gaps in the tier one segment (partly due to the

delay in minimum price enforcement), and the disproportionate impact of stricter public mobility restrictions in urban areas, where PMI's share is higher;

- Pakistan, down by 20.0%, mainly reflecting the lower total market and a lower market share, mainly due to low-price *Morven*; and
- the Philippines, down by 16.1%, mainly reflecting the lower total market and a lower market share, primarily for mid-price *Fortune* due to the impact of price increases in the third quarter of 2019 and the fourth quarter of 2020.

East Asia & Australia:

Financial Summary - Years Ended December 31,			**Change Fav./(Unfav.)**		**Variance Fav./(Unfav.)**				
(in millions)	**2020**	**2019**	**Total**	**Excl. Curr.**	**Total**	**Cur-rency**	**Price**	**Vol/ Mix**	**Cost/ Other**
Net Revenues	**$ 5,429**	$ 5,364	1.2 %	0.6 %	$ 65	$ 33	$ 168	$ (136)	$ —
Operating Income	**$ 2,400**	$ 1,932	24.2 %	23.1 %	$ 468	$ 21	$ 168	$ (68)	$ 347

Net revenues, excluding favorable currency, increased by 0.6%, reflecting: a favorable pricing variance, mainly driven by higher heated tobacco and combustible pricing in Japan, partly offset by lower *IQOS* device pricing in Japan; and unfavorable volume/mix, mainly due to lower cigarette volume (primarily in Japan), unfavorable cigarette mix in Australia, lower device volume/mix in Japan and lower heated tobacco unit mix in Japan, partly offset by higher heated tobacco unit volume in Japan.

Operating income, excluding favorable currency, increased by 23.1%, mainly reflecting: lower marketing, administration and research costs (notably in Japan); lower manufacturing costs (mainly related to Japan and Korea); and a favorable pricing variance; partly offset by unfavorable volume/mix, mainly due to lower cigarette volume (primarily in Japan), unfavorable cigarette mix in Australia and lower heated tobacco unit mix in Japan, partly offset by higher heated tobacco unit volume in Japan.

Excluding asset impairment and exit costs of $26 million in 2020 and favorable currency of $21 million, operating income increased by 24.5%.

East Asia & Australia - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in East Asia & Australia, excluding China, decreased by 3.6% to 288.6 billion units, notably due to:

- Australia, down by 8.8%, primarily reflecting the impact of excise tax-driven price increases; and
- Japan, down by 9.4%, mainly reflecting the impact of excise tax-driven price increases, reduced adult smoker consumption occasions due to pandemic-related measures, as well as adult smoker out-switching from cigarettes to the cigarillo category;

partly offset by

- Korea, up by 4.4%, mainly reflecting the shift of adult smokers from duty-free to domestic purchases due to the pandemic-related decline in international travel; and
- Taiwan, up by 5.4%, primarily driven by the same factor as for Korea.

Our Regional market share, excluding China, increased by 0.3 points to 27.2%.

PMI Shipment Volume (million units)	
	202
Cigarettes	**45,10**
Heated Tobacco Units	**33,86**
Total East Asia & Australia	**78,96**

Our total shipment volume decreased by 2.1% to 79.0 billion units, notably in:

- Japan, down by 2.4%, mainly due to the lower total market, partly offset by a higher market share driven by heated tobacco units; and
- Korea, down by 4.3%, primarily due to a lower market share, mainly reflecting the unfavorable impact of the growth of the cigarette new taste dimension segment, in which PMI has a relatively low share, partly offset by the higher total market.

Latin America & Canada:

Financial Summary - Years Ended December 31,			**Change Fav./(Unfav.)**		**Variance Fav./(Unfav.)**				
(in millions)	**2020**	**2019**	**Total**	**Excl. Curr.**	**Total**	**Cur-rency**	**Price**	**Vol/ Mix**	**Cost/ Other[1]**
Net Revenues	**$ 1,701**	$ 2,206	(22.9)%	(15.5)%	$ (505)	$ (164)	$ 135	$ (285)	$ (191)
Operating Income	**$ 564**	$ 235	+100%	+100%	$ 329	$ (110)	$ 135	$ (219)	$ 523

[1] Cost/Other variance includes the impact of the RBH deconsolidation.

Note: Net Revenues include revenues from shipments of Platform 1 devices, heated tobacco units and accessories to Altria Group, Inc., commencing in the third quarter of 2019, for sale under license in the United States.

Net revenues, excluding unfavorable currency, decreased by 15.5%, reflecting: unfavorable volume/mix, due to lower cigarette volume, mainly in Argentina and Mexico, partly offset by Brazil; and the unfavorable impact of the deconsolidation of RBH shown in "Cost/Other"; partially offset by a favorable pricing variance, driven by higher combustible pricing across the Region (notably in Brazil and Mexico).

Operating income, excluding unfavorable currency, increased by over 100%, notably reflecting a favorable comparison, shown in "Cost/Other," of net favorable items recorded in 2020 of $110 million related to the Brazil indirect tax credit of $119 million and asset impairment and exit costs of $9 million (associated with organizational design optimization), and charges recorded in 2019 of $493 million related to: asset impairment and exit costs ($60 million) associated with plant closures in Argentina and Colombia, the loss on the deconsolidation of RBH ($239 million), and the Canadian tobacco litigation-related expense ($194 million).

Excluding these 2020 and 2019 items noted above, and unfavorable currency of $110 million, operating income decreased by 22.5%, mainly reflecting: unfavorable volume/mix, due to the same factors as for net revenues noted above; and the unfavorable impact of the deconsolidation of RBH, included in "Cost/Other"; partly offset by a favorable pricing variance; and lower marketing, administration and research costs (notably in Argentina).

Latin America & Canada - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in Latin America & Canada decreased by 2.8% to 189.0 billion units, notably due to:

- Colombia, down by 14.2%, primarily reflecting reduced product availability (mainly in the second quarter of 2020) and lower adult smoker average daily consumption due to the impact of pandemic-related mobility restrictions; and
- Mexico, down by 13.6%, mainly due to the impact of excise tax-driven price increases in January 2020 and pandemic-related measures on adult smoker average daily consumption;

partly offset by

- Brazil, up by 13.4%, mainly reflecting a lower estimated prevalence of illicit trade due to: reduced price gaps with legal products and the impact of border restrictions imposed as a result of the pandemic.

Our Regional market share decreased by 3.0 points to 33.9%.

PMI Shipment Volume (million units)	
	202
Cigarettes	**63,74**
Heated Tobacco Units	**45**
Total Latin America & Canada	**64,20**

Our total shipment volume decreased by 11.6% to 64.2 billion units, or by 10.3% excluding the impact of the RBH deconsolidation, notably due to

- Argentina, down by 12.2%, primarily reflecting a lower market share, mainly due to adult smoker down-trading to ultra-low-price brands produced by local manufacturers, as well as the impact of retail out-of-stock of PMI brands during the second quarter;
- Canada, down by 18.6%, due to the unfavorable impact of the deconsolidation of RBH;
- Colombia, down by 14.2%, primarily reflecting the lower total market; and
- Mexico, down by 18.0%, mainly due to the lower total market and a lower market share, primarily reflecting: adult smoker down-trading following the January 2020 price increases and the impact of the pandemic on adult smoker consumption patterns;

partly offset by

- Brazil, up by 13.2%, mainly reflecting the higher total market.

2019 compared with 2018

For a discussion comparing our consolidated operating results within each of our operating segments for the year ended December 31, 2019, with the year ended December 31, 2018, refer to Part II, Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operation - Operating Results by Business Segment* in our Annual Report on Form 10-K for the year ended December 31, 2019, which was filed with the U.S. Securities and Exchange Commission on February 7, 2020.

Financial Review

pm-20201231_g5.jpgpm-20201231_g6.jpgpm-20201231_g7.jpg

	For the Years Ended Decemb	
(in millions)	**2020**	**2019**
Net cash provided by operating activities	$ 9,812	$ 10,090
Net cash used in investing activities	(1,154)	(1,811)
Net cash used in financing activities	(8,496)	(8,061)

2020 compared with 2019

- *Net Cash Provided by Operating Activities*

Net cash provided by operating activities for the year ended December 31, 2020 decreased by $0.3 billion compared with 2019. Excluding unfavorable currency movements of $0.5 billion, net cash provided by operating activities increased by $0.2 billion, due primarily to higher net earnings (excluding 2019 non-cash charges related to the Canadian tobacco litigation-related expense and the loss on deconsolidation of RBH), partially offset by higher working capital requirements of $0.5 billion and higher cash payments in 2020 for asset impairment and exit costs. For further details, see Item 8, Note 19. *Asset Impairment and Exit Costs* for additional information.

Higher net earnings in 2020, excluding the impact of the above 2019 non-cash charges, were partly attributable to the Russia excise and VAT audit charge of $374 million which was paid in the third quarter of 2019. For further details, Item 8, Note 17. *Contingencies* for additional information.

The higher working capital requirements were primarily due to net cash used in inventories and accrued liabilities and other current assets reflecting COVID-19 pandemic related build-up of inventory in our supply chain, and the timing of excise tax-paid inventory movements and excise tax payments. This change was partially offset by cash provided by accounts receivable due to the varying levels of usage of our factoring arrangements to sell trade receivables and timing of sales and cash collections.

- *Net Cash Used in Investing Activities*

Net cash used in investing activities of $1.2 billion for the year ended December 31, 2020, decreased by $0.7 billion from the comparable 2019 period. This decrease in net cash used in investing activities was primarily due to the reduction of cash in 2019 resulting from the deconsolidation of RBH and lower capital expenditures, partially offset by higher cash collateral posted to secure derivatives designated as net investment hedges of Euro assets principally related to changes in exchange rates between the Euro and the U.S. dollar. For further details on deconsolidation of RBH, see Item 8. Note 20. *Deconsolidation of RBH*. For further details on

our derivatives designated as net investment hedges, see Item 8. Note 15. *Financial Instruments*.

Our capital expenditures were $0.6 billion in 2020 and $0.9 billion in 2019. The 2020 expenditures were primarily related to our ongoing investments in RRPs. We expect total capital expenditures in 2021 of approximately $0.8 billion (including capital expenditures related to our ongoing investment in RRPs), to be funded by operating cash flows.

- *Net Cash Used in Financing Activities*

Net cash used in financing activities of $8.5 billion for the year ended December 31, 2020, increased by $0.4 billion from the comparable 2019 period. The change was due primarily to higher payments to noncontrolling interests and higher dividends paid, partially offset by debt activity.

Dividends paid in 2020 and 2019 were $7.4 billion and $7.2 billion, respectively.

2019 compared with 2018

For a discussion comparing our net cash activities (operating, investing and financing) for the year ended December 31, 2019, with the year ended December 31, 2018, refer to Part II, Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation - Financial Review in our Annual Report on Form 10-K for the year ended December 31, 2019, which was filed with the U.S. Securities and Exchange Commission on February 7, 2020.

Debt and Liquidity

We define cash and cash equivalents as short-term, highly liquid investments, readily convertible to known amounts of cash that mature within a maximum of three months and have an insignificant risk of change in value due to interest rate or credit risk changes. As a policy, we do not hold any investments in structured or equity-linked products. Our cash and cash equivalents are predominantly held in demand deposits with institutions that have investment-grade long-term credit rating. As part of our cash management strategy and in order to manage counterparty exposure, we also enter into reverse repurchase agreements. Such agreements are collateralized with government or corporate securities held by a custodial bank and, at maturity, cash is paid back to PMI, and the collateral is returned to the bank. For 2020 and 2019, the activities for such reverse repurchase agreements were not material.

We utilize long-term and short-term debt financing, including a commercial paper program that is regularly used to finance ongoing liquidity requirements, as part of our overall cash management strategy. Our ability to access the capital and credit markets as well as overall dynamics of these markets may impact borrowing costs. We expect that the combination of our long-term and short-term debt financing, the commercial paper program and the committed credit facilities, coupled with our operating cash flows, will enable us to meet our liquidity requirements.

Credit Ratings – The cost and terms of our financing arrangements as well as our access to commercial paper markets may be affected by applicable credit ratings. At February 8, 2021, our credit ratings and outlook by major credit rating agencies were as follows:

	Short-term	Long-term
Moody's	P-1	A2
Standard & Poor's	A-1	A
Fitch	F1	A

Credit Facilities – On January 29, 2021, we entered into an agreement to amend and extend the term of our 364-day revolving credit facility from February 2, 2021, to February 1, 2022 in the amount of $1.75 billion.

At February 8, 2021, our committed credit facilities were as follows:

(in billions)

Type		Committed Credit Facilities
364-day revolving credit, expiring February 1, 2022	**$**	**1.75**
Multi-year revolving credit, expiring October 1, 2022		**3.50**
Multi-year revolving credit, expiring February 10, 2025[(a)]		**2.00**
Total facilities	**$**	**7.25**

[(a)] On January 29, 2021, we entered into an agreement, effective February 10, 2021, to amend and extend the term of our $2.0 billion multi-year revolving credit facility, for an additional year covering the period February 11, 2025 to February 10, 2026, in the amount of $1.86 billion.

At February 8, 2021, there were no borrowings under the committed credit facilities, and the entire committed amounts were available for borrowing.

All banks participating in our committed credit facilities have an investment-grade long-term credit rating from the credit rating agencies. We continuously monitor the credit quality of our banking group, and at this time we are not aware of any potential non-performing credit provider.

These facilities do not include any credit rating triggers, material adverse change clauses or any provisions that could require us to post collateral. The $3.5 billion multi-year revolving credit facility in the table above requires us to maintain a ratio of consolidated earnings before interest, taxes, depreciation and amortization ("consolidated EBITDA") to consolidated interest expense of not less than 3.5 to 1.0 on a rolling four-quarter basis. At December 31, 2020, our ratio calculated in accordance with the agreement was 12.6 to 1.0. We expect to continue to meet our covenants. The terms "consolidated EBITDA" and "consolidated interest expense," both of which include certain adjustments, are defined in the facility agreements previously filed with the U.S. Securities and Exchange Commission.

In addition to the committed credit facilities discussed above, certain of our subsidiaries maintain short-term credit arrangements to meet their respective working capital needs. These credit arrangements, which amounted to approximately $2.7 billion at December 31, 2020 and December 31, 2019, respectively, are for the sole use of our subsidiaries. Borrowings under these arrangements and other bank loans amounted to $244 million at December 31, 2020, and $338 million at December 31, 2019.

Commercial Paper Program – We continue to have access to liquidity in the commercial paper market through programs in place in the U.S. and in Europe having an aggregate issuance capacity of $8.0 billion. At December 31, 2020, and December 31, 2019, we had no commercial paper outstanding. The average commercial paper balance outstanding during 2020 and 2019 was $1.2 billion and $2.3 billion, respectively.

Sale of Accounts Receivable – To mitigate credit risk and enhance cash and liquidity management, we sell trade receivables to unaffiliated financial institutions. These arrangements allow us to sell, on an ongoing basis, certain trade receivables without recourse. The trade receivables sold are generally short-term in nature and are removed from the consolidated balance sheets. We sell trade receivables under two types of arrangements, servicing and nonservicing.

Our operating cash flows were positively impacted by the amount of the trade receivables sold and derecognized from the consolidated balance sheets, which remained outstanding with the unaffiliated financial institutions. The trade receivables sold that remained outstanding under these arrangements as of December 31, 2020, 2019 and 2018, were $1.2 billion, $0.9 billion and $1.0 billion, respectively. The net proceeds received are included in cash provided by operating activities in the consolidated statements of cash flows.

For further details, see Item 8, Note 18. *Sale of Accounts Receivable* to our consolidated financial statements.

Debt – Our total debt was $31.5 billion at December 31, 2020, and $31.0 billion at December 31, 2019. Our total debt is primarily fixed rate in nature. The weighted-average all-in financing cost of our total debt was 2.4% in 2020 and 2.5% in 2019. For further

details, including the fair value of our debt, see Item 8, Note 7. *Indebtedness*. The amount of debt that we can issue is subject to approval by our Board of Directors.

On February 11, 2020, we filed a shelf registration statement with the U.S. Securities and Exchange Commission, under which we may from time to time sell debt securities and/or warrants to purchase debt securities over a three-year period.

Our debt issuances in 2020 were as follows:

(in millions)

Type		Face Value	Interest Rate	Issuance	Maturity
U.S. dollar notes	(a)	$750	1.125%	May 2020	May 2023
U.S. dollar notes	(a)	$750	1.500%	May 2020	May 2025
U.S. dollar notes	(a)	$750	2.100%	May 2020	May 2030
U.S. dollar notes	(b)	$750	0.875%	November 2020	May 2026
U.S. dollar notes	(b)	$750	1.750%	November 2020	November 2030

[(a)] Interest on these notes is payable semi-annually in arrears beginning in November 2020.

[(b)] Interest on these notes is payable semi-annually in arrears beginning in May 2021.

The net proceeds from the sale of the securities listed in the table above have been and will be used for general corporate purposes, including repayment of outstanding commercial paper and redemption on January 25, 2021, of our outstanding $750 million 1.875% U.S. dollar notes due February 25, 2021.

The weighted-average time to maturity of our long-term debt was 9.7 years at the end of 2020 and 10.2 years at the end of 2019.

- **Off-Balance Sheet Arrangements and Aggregate Contractual Obligations**

We have no off-balance sheet arrangements, including special purpose entities, other than guarantees and contractual obligations discussed below.

Guarantees – At December 31, 2020, we were contingently liable for guarantees of our own performance, of which $0.3 billion were related to our obligations under indemnity agreements to enable appeals of customs assessments against our distributors. In October 2020, we guaranteed an obligation for an equity method investee. For further details, see Item 8, Note 17. *Contingencies* to our consolidated financial statements. Additionally, we have other guarantees of our own performance, which are primarily related to excise taxes on the shipment of our products. There is no liability in the consolidated financial statements associated with these guarantees. These guarantees have not had, and are not expected to have, a significant impact on PMI's liquidity.

Aggregate Contractual Obligations – The following table summarizes our contractual obligations at December 31, 2020:

		Paymen	
(in millions)	**Total**	**2021**	**2022-2023**
Long-term debt [1]	$31,552	$3,124	$5,122
Interest on borrowings [2]	9,781	874	1,531
Operating leases [3]	896	215	271
Purchase obligations [4]:			
Inventory and production costs	2,902	2,048	584
Other	1,719	1,038	363
	4,621	3,086	947
Other long-term liabilities [5]	1,699	267	361
	$48,549	$7,566	$8,232

[1] Amounts represent the expected cash payments at the face value of our long-term debt and finance lease obligations. For further details, see Item 8, Note 7. *Indebtedness* to our consolidated financial statements.

[2] Amounts represent the expected cash payments of our interest expense on our long-term debt, including the current portion of long-term debt. Interest on our fixed-rate debt is presented using the stated interest rate. Interest on our variable debt is estimated using the rate in effect at December 31, 2020. Amounts exclude the amortization of debt discounts, the amortization of loan fees and fees for lines of credit that would be included in interest expense in the consolidated statements of earnings.

[3] Amounts represent the maturity of PMI's operating lease liabilities, on an undiscounted basis.

[4] Purchase obligations for inventory and production costs (such as raw materials, electonic devices, indirect materials and supplies, packaging, co-manufacturing arrangements, storage and distribution) are commitments for projected needs to be utilized in the normal course of business. Other purchase obligations include commitments for marketing, advertising, capital expenditures, information technology and professional services. Other purchase obligations also include the expected future contributions to the Foundation for a Smoke-Free World. For further details see *Business Environment—Other Developments*. Arrangements are considered purchase obligations if a contract specifies all significant terms, including fixed or minimum quantities to be purchased, a pricing structure and approximate timing of the transaction. Amounts represent the minimum commitments under non-cancelable contracts. Any amounts reflected on the consolidated balance sheet as accounts payable and accrued liabilities are excluded from the table above.

[5] Other long-term liabilities consist primarily of transition tax (as discussed in Item 8, Note 11. *Income Taxes* to our consolidated financial statements), postretirement health care costs, accruals established for employment costs and accruals established for Exit activities (for further details, see Note 19. *Asset impairment and Exit Costs*). The following long-term liabilities included on the consolidated balance sheet are excluded from the table above: accrued pension and postemployment costs, tax contingencies, insurance accruals and other accruals. We are unable to estimate the timing of payments (or contributions in the case of accrued pension costs) for these items. Currently, we anticipate making pension contributions of approximately $262 million in 2021, based on current tax and benefit laws (as discussed in Item 8, Note 13. *Benefit Plans* to our consolidated financial statements).

Equity and Dividends

We discuss our stock awards as of December 31, 2020, in Item 8, Note 9. *Stock Plans* to our consolidated financial statements.

During 2020, 2019 and 2018, we did not repurchase any shares under a share repurchase program.

Dividends paid in 2020 were $7.4 billion. During the third quarter of 2020, our Board of Directors approved a 2.6% increase in the quarterly dividend to $1.20 per common share. As a result, the present annualized dividend rate is $4.80 per common share.

Market Risk

Counterparty Risk - We predominantly work with financial institutions with strong short- and long-term credit ratings as assigned by Standard & Poor's and Moody's. These banks are also part of a defined group of relationship banks. Non-investment grade institutions are only used in certain emerging markets to the extent required by local business needs. We have a conservative approach when it comes to choosing financial counterparties and financial instruments. As such we do not invest or hold investments in any structured or equity-linked products. The majority of our cash and cash equivalents is currently invested with maturities of less than 30 days.

We continuously monitor and assess the credit worthiness of all our counterparties.

Derivative Financial Instruments - We operate in markets outside of the United States of America, with manufacturing and sales facilities in various locations throughout the world. Consequently, we use certain financial instruments to manage our foreign currency and interest rate exposure. We use derivative financial instruments principally to reduce our exposure to market risks resulting from fluctuations in foreign exchange and interest rates by creating offsetting exposures. We are not a party to leveraged derivatives and, by policy, do not use derivative financial instruments for speculative purposes.

See Item 8, Note 15. *Financial Instruments* to our consolidated financial statements for further details on our derivative financial instruments and the related collateral arrangements.

Value at Risk - We use a value at risk computation to estimate the potential one-day loss in the fair value of our interest-rate-sensitive and foreign currency price-sensitive derivative financial instruments. This computation includes our debt and foreign currency forwards, swaps and options. Anticipated transactions, foreign currency trade payables and receivables, and net investments in foreign subsidiaries, which the foregoing instruments are intended to hedge, were excluded from the computation.

The computation estimates were made assuming normal market conditions, using a 95% confidence interval and a one-day holding period using a "parametric delta-gamma" approximation technique to determine the observed interrelationships between movements in interest rates and various currencies and in calculating the risk of the underlying positions in the portfolio. These interrelationships were determined by observing interest rate and forward currency rate movements primarily over the preceding quarter for determining value at risk at December 31, 2020 and 2019, and primarily over each of the four preceding quarters for the calculation of average, high and low value at risk amounts during each year.

	Fair Value Impact		
(in millions)	**At December 31, 2020**	**Average**	**High**
Instruments sensitive to:			
Foreign currency rates	**$59**	**$78**	**$136**
Interest rates	**$180**	**$445**	**$1,146**

	Fair Value Impact		
(in millions)	**At December 31, 2019**	**Average**	**High**
Instruments sensitive to:			
Foreign currency rates	$18	$20	$24
Interest rates	$301	$247	$346

The significant year-over-year increase in "average" and "high" impact on the value at risk computation above was primarily due to an increase in interest rate and foreign currency volatility during the first quarter of 2020 resulting from the impact of the COVID-19 pandemic.

The value at risk computation is a risk analysis tool designed to statistically estimate the maximum probable daily loss from adverse movements in interest and foreign currency rates under normal market conditions. The computation does not purport to represent actual losses in fair value or earnings to be incurred by us, nor does it consider the effect of favorable changes in market rates. We cannot predict actual future movements in such market rates and do not present these results to be indicative of future movements in market rates or to be representative of any actual impact that future changes in market rates may have on our future results of operations or financial position.

Contingencies

See Item 3 and Item 8, Note 17. *Contingencies* to our consolidated financial statements for a discussion of contingencies.

Cautionary Factors That May Affect Future Results

Forward-Looking and Cautionary Statements

We may from time to time make written or oral forward-looking statements, including statements contained in filings with the SEC, in reports to stockholders and in press releases and investor webcasts. You can identify these forward-looking statements by use of words such as "strategy," "expects," "continues," "plans," "anticipates," "believes," "will," "estimates," "intends," "projects," "aims," "goals," "targets" and other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts.

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Our RRPs constitute a new product category in its early stages that is less predictable than our mature cigarette business. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from those anticipated, estimated or projected. Investors should bear this in mind as they consider forward-looking statements and whether to invest in or remain invested in our securities. In connection with the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995, we are identifying important factors that, individually or in the aggregate, could cause actual results and outcomes to differ materially from those contained in any forward-looking statements made by us; any such statement is qualified by reference to the following cautionary statements. We elaborate on these and other risks we face throughout this document, particularly in Item 1A. *Risk Factors* and *Business Environment* of this section. You should understand that it is not possible to predict or identify all risk factors. Consequently, you should not consider this discussion of potential risks or uncertainties to be complete. We do not undertake to update any forward-looking statement that we may make from time to time, except in the normal course of our public disclosure obligations.

Item 7A. *Quantitative and Qualitative Disclosures About Market Risk.*

The information called for by this Item is included in Item 7, *Market Risk*.

Item 8. *Financial Statements and Supplementary Data.*

Consolidated Statements of Earnings

(in millions of dollars, except per share data)

for the years ended December 31,	2020	2019	2018
Revenues including excise taxes	**$ 76,047**	$ 77,921	$ 79,823
Excise taxes on products	**47,353**	48,116	50,198
Net revenues	**28,694**	29,805	29,625
Cost of sales	**9,569**	10,513	10,758
Gross profit	**19,125**	19,292	18,867
Marketing, administration and research costs (Notes 12, 17, 19 & 20)	**7,384**	8,695	7,408
Amortization of intangibles	**73**	66	82
Operating income	**11,668**	10,531	11,377
Interest expense, net (Note 14)	**618**	570	665
Pension and other employee benefit costs (Note 13)	**97**	89	41
Earnings before income taxes	**10,953**	9,872	10,671
Provision for income taxes (Note 11)	**2,377**	2,293	2,445
Equity investments and securities (income)/loss, net	**(16)**	(149)	(60)
Net earnings	**8,592**	7,728	8,286
Net earnings attributable to noncontrolling interests	**536**	543	375
Net earnings attributable to PMI	**$ 8,056**	$ 7,185	$ 7,911
Per share data (Note 10):			
Basic earnings per share	**$ 5.16**	$ 4.61	$ 5.08
Diluted earnings per share	**$ 5.16**	$ 4.61	$ 5.08

See notes to consolidated financial statements.

Consolidated Statements of Comprehensive Earnings

(in millions of dollars)

for the years ended December 31,	2020	2019	2018
Net earnings	**$ 8,592**	$ 7,728	$ 8,286
Other comprehensive earnings (losses), net of income taxes:			
Change in currency translation adjustments:			
Unrealized gains (losses), net of income taxes of $94 in 2020, $(161) in 2019 and $(47) in 2018	**(1,265)**	505	(812)
(Gains)/losses transferred to earnings - deconsolidation of RBH, net of income taxes of $0 in 2020, 2019 and 2018 (Note 20)	**—**	502	—
Change in net loss and prior service cost:			
Net gains (losses) and prior service costs, net of income taxes of $139 in 2020, $247 in 2019 and $65 in 2018	**(726)**	(454)	(1,046)
Amortization of net losses, prior service costs and net transition costs, net of income taxes of $(67) in 2020, $(69) in 2019 and $(43) in 2018	**299**	243	218
(Gains)/losses transferred to earnings - deconsolidation of RBH, net of income taxes of $0 in 2020, $(15) in 2019 and $0 in 2018 (Note 20)	**—**	27	—
Change in fair value of derivatives accounted for as hedges:			
Gains (losses) recognized, net of income taxes of $13 in 2020, $2 in 2019 and $(4) in 2018	**(68)**	(18)	24
(Gains) losses transferred to earnings, net of income taxes of $0 in 2020, $3 in 2019 and $5 in 2018	**(20)**	(14)	(31)
Total other comprehensive earnings (losses)	**(1,780)**	791	(1,647)
Total comprehensive earnings	**6,812**	8,519	6,639
Less comprehensive earnings attributable to:			
Noncontrolling interests	**574**	586	304
Comprehensive earnings attributable to PMI	**$ 6,238**	$ 7,933	$ 6,335

See notes to consolidated financial statements.

Consolidated Balance Sheets

(in millions of dollars, except share data)

at December 31,	2020	2019
Assets		
Cash and cash equivalents	**$ 7,280**	$ 6,861
Trade receivables (less allowances of $23 in 2020 and $20 in 2019)	**2,905**	3,080
Other receivables (less allowances of $38 in 2020 and $35 in 2019)	**856**	637
Inventories:		
Leaf tobacco	**2,063**	2,052
Other raw materials	**1,712**	1,596
Finished product	**5,816**	5,587
	9,591	9,235
Other current assets	**860**	701
Total current assets	**21,492**	20,514
Property, plant and equipment, at cost:		
Land and land improvements	**590**	566
Buildings and building equipment	**4,410**	4,132
Machinery and equipment	**9,460**	9,354
Construction in progress	**449**	394
	14,909	14,446
Less: accumulated depreciation	**8,544**	7,815
	6,365	6,631
Goodwill (Note 3)	**5,964**	5,858
Other intangible assets, net (Note 3)	**2,019**	2,113
Equity investments (Note 4)	**4,798**	4,635
Deferred income taxes	**1,410**	1,153
Other assets (less allowances of $22 in 2020 and $15 in 2019)	**2,767**	1,971
Total Assets	**$ 44,815**	$ 42,875

See notes to consolidated financial statements.

at December 31,	2020	2019
Liabilities		
Short-term borrowings (Note 7)	**$ 244**	$ 338
Current portion of long-term debt (Note 7)	**3,124**	4,051
Accounts payable	**2,780**	2,299
Accrued liabilities:		
Marketing and selling	**782**	666
Taxes, except income taxes	**6,403**	5,837
Employment costs	**1,189**	1,042
Dividends payable	**1,880**	1,831
Other	**2,122**	1,973
Income taxes (Note 11)	**1,091**	796
Total current liabilities	**19,615**	18,833
Long-term debt (Note 7)	**28,168**	26,656
Deferred income taxes	**684**	908
Employment costs	**4,470**	3,634
Income taxes and other liabilities (Note 11)	**2,509**	2,443
Total liabilities	**55,446**	52,474
Contingencies (Note 17)		
Stockholders' (Deficit) Equity		
Common stock, no par value (2,109,316,331 shares issued in 2020 and 2019)	**—**	—
Additional paid-in capital	**2,105**	2,019
Earnings reinvested in the business	**31,638**	30,987
Accumulated other comprehensive losses	**(11,181)**	(9,363)
	22,562	23,643
Less: cost of repurchased stock (551,942,600 and 553,421,668 shares in 2020 and 2019, respectively)	**35,129**	35,220
Total PMI stockholders' deficit	**(12,567)**	(11,577)
Noncontrolling interests	**1,936**	1,978
Total stockholders' deficit	**(10,631)**	(9,599)
Total Liabilities and Stockholders' (Deficit) Equity	**$ 44,815**	$ 42,875

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(in millions of dollars)

for the years ended December 31,	2020	2019	2018
CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES			
Net earnings	**$ 8,592**	$ 7,728	$ 8,286
Adjustments to reconcile net earnings to operating cash flows:			
Depreciation and amortization	**981**	964	989
Deferred income tax (benefit) provision	**(143)**	(141)	(100)
Asset impairment and exit costs, net of cash paid (Note 19)	**(14)**	371	(3)
Cash effects of changes in:			
Receivables, net	**26**	(331)	53
Inventories	**(165)**	(548)	(613)
Accounts payable	**406**	451	(51)
Accrued liabilities and other current assets	**121**	1,108	910
Income taxes	**(260)**	75	(135)
Pension plan contributions	**(102)**	(200)	(110)
Other	**370**	613 [(1)]	252
Net cash provided by operating activities	**9,812**	10,090	9,478
CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES			
Capital expenditures	**(602)**	(852)	(1,436)
Equity investments	**(47)**	(31)	(63)
Deconsolidation of RBH (Note 20)	**—**	(1,346) [(2)]	—
Net investment hedges	**(551)**	386	416
Other	**46**	32	85
Net cash used in investing activities	**(1,154)**	(1,811)	(998)

See notes to consolidated financial statements.

for the years ended December 31,	2020	2019	2018
CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES			
Short-term borrowing activity by original maturity:			
Net issuances (repayments) - maturities of 90 days or less	**$ (70)**	$ (364)	$ 255
Issuances - maturities longer than 90 days	**45**	989	—
Repayments - maturities longer than 90 days	**(45)**	(989)	—
Long-term debt proceeds	**3,713**	3,819	—
Long-term debt repaid	**(3,999)**	(3,998)	(2,484)
Dividends paid	**(7,364)**	(7,161)	(6,885)
Payments to noncontrolling interests and Other	**(776)**	(357)	(537)
Net cash used in financing activities	**(8,496)**	(8,061)	(9,651)
Effect of exchange rate changes on cash, cash equivalents and restricted cash	**258**	27	(685)
Cash, cash equivalents and restricted cash[3]:			
Increase (Decrease)	**420**	245	(1,856)
Balance at beginning of year	**6,865**	6,620	8,476
Balance at end of year	**$ 7,285**	$ 6,865	$ 6,620
Cash Paid:			
Interest	**$ 728**	$ 800	$ 882
Income taxes	**$ 2,785**	$ 2,430	$ 2,749

[1] Includes the Loss on Deconsolidation of RBH ($239 million) and the Canadian tobacco litigation-related charge ($194 million) that were included in marketing, administration and research costs in the consolidated statements of earnings for the year ended December 31, 2019. For further details on these charges, see Note 20. *Deconsolidation of RBH*.

[2] Includes deconsolidation of RBH cash and cash equivalents of $1,323 million and restricted cash of $23 million.

[3] The amounts for cash and cash equivalents shown above include restricted cash of $5 million, $4 million and $27 million as of December 31, 2020, 2019 and 2018, respectively, which were included in other current assets in the consolidated balance sheets.

See notes to consolidated financial statements.

Consolidated Statements of Stockholders' (Deficit) Equity

(in millions of dollars, except per share data)

	PMI Stockholders' (Deficit) Equity						
	Common Stock	Additional Paid-in Capital	Earnings Reinvested in the Business	Accumulated Other Comprehensive Losses	Cost of Repurchased Stock	Noncontrolling Interests	Total
Balances, January 1, 2018	$ —	$ 1,972	$ 29,859	$ (8,535)	$ (35,382)	$ 1,856	$ (10,230)
Net earnings			7,911			375	8,286
Other comprehensive earnings (losses), net of income taxes				(1,572)		(75)	(1,647)
Issuance of stock awards		47			81		128
Dividends declared ($4.49 per share)			(6,994)				(6,994)
Payments to noncontrolling interests						(435)	(435)
Adoption of new accounting standards [1]			238				238
Other (Note 6)		(80)		(4)		(1)	(85)
Balances, December 31, 2018	—	1,939	31,014	(10,111)	(35,301)	1,720	(10,739)
Net earnings			7,185			543	7,728
Other comprehensive earnings (losses), net of income taxes				219		43	262
Issuance of stock awards		79			81		160
Dividends declared ($4.62 per share)			(7,212)				(7,212)
Payments to noncontrolling interests						(378)	(378)
Deconsolidation of RBH (Note 20)				529			529
Other		1		—		50	51
Balances, December 31, 2019	—	2,019	30,987	(9,363)	(35,220)	1,978	(9,599)
Net earnings			**8,056**			**536**	**8,592**
Other comprehensive earnings (losses), net of income taxes				**(1,818)**		**38**	**(1,780)**
Issuance of stock awards		**69**			**91**		**160**
Dividends declared ($4.74 per share)			**(7,405)**				**(7,405)**
Payments to noncontrolling interests						**(602)**	**(602)**
Other		**17**		**—**		**(14)**	**3**
Balances, December 31, 2020	**$ —**	**$ 2,105**	**$ 31,638**	**$ (11,181)**	**$ (35,129)**	**$ 1,936**	**$ (10,631)**

[1] Financial Accounting Standard Update ASU 2016-01, "Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities"

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Note 1.

Background and Basis of Presentation:

Background

Philip Morris International Inc. is a holding company incorporated in Virginia, U.S.A., whose subsidiaries and affiliates and their licensees are engaged in the manufacture and sale of cigarettes and other nicotine-containing products, including reduced-risk products, in markets outside of the United States of America. In addition, PMI ships versions of its Platform 1 device and its consumables authorized by the U.S. Food and Drug Administration ("FDA") to Altria Group, Inc., for sale in the United States under license. Throughout these financial statements, the term "PMI" refers to Philip Morris International Inc. and its subsidiaries.

Reduced-risk products ("RRPs") is the term PMI uses to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continuing smoking. PMI has a range of RRPs in various stages of development, scientific assessment and commercialization.

"Platform 1" is the term PMI uses to refer to PMI's reduced-risk product that uses a precisely controlled heating device incorporating our *IQOS HeatControl* technology, into which a specially designed and proprietary tobacco unit is inserted and heated to generate an aerosol.

Basis of presentation

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities at the dates of the financial statements and the reported amounts of net revenues and expenses during the reporting periods. Significant estimates and assumptions include, among other things: pension and benefit plan assumptions; useful lives and valuation assumptions of goodwill and other intangible assets; valuation assumptions for non-marketable equity securities; marketing programs, and income taxes. Actual results could differ from those estimates.

The consolidated financial statements include PMI, as well as its wholly owned and majority-owned subsidiaries. Investments in which PMI exercises significant influence (generally 20%-50% ownership interest) are accounted for under the equity method of accounting. Investments not accounted for under the equity method of accounting are measured at fair value, if it is readily determinable, with changes in fair value recognized in net income. Investments without readily determinable fair values, non-marketable equity securities, are measured and recorded using a measurement alternative that values the security at cost minus any impairment. All intercompany transactions and balances have been eliminated.

PMI has analyzed the impact of the Coronavirus pandemic ("COVID-19") on its financial statements as of December 31, 2020. PMI has determined that the changes to its significant judgments and estimates did not have a material impact with respect to goodwill, intangible assets, long-lived assets or its hedge accounting activities.

As of March 22, 2019, PMI deconsolidated the financial results of its Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH") from PMI's financial statements. For further details, see Note 20. *Deconsolidation of RBH*.

Certain prior years' amounts have been reclassified to conform with the current year's presentation. The changes did not have a material impact on PMI's consolidated financial position, results of operations or cash flows in any of the periods presented.

Note 2.

Summary of Significant Accounting Policies:

Cash and cash equivalents

Cash equivalents include demand deposits with banks and all highly liquid investments with original maturities of three months or less.

Depreciation

Property, plant and equipment are stated at historical cost and depreciated by the straight-line method over the estimated useful lives of the assets. Machinery and equipment are depreciated over periods ranging from 3 to 15 years, and buildings and building improvements over periods up to 40 years.

Employee benefit plans

PMI provides a range of benefits to its employees and retired employees, including pensions, postretirement health care and postemployment benefits (primarily severance). PMI records annual amounts relating to these plans based on calculations specified under U.S. GAAP. PMI recognizes the funded status of its defined pension and postretirement plans on the consolidated balance sheets. The funded status is measured as the difference between the fair value of the plans assets and the benefit obligation. PMI measures the plan assets and liabilities at the end of the fiscal year. For defined benefit pension plans, the benefit obligation is the projected benefit obligation. For the postretirement health care plans, the benefit obligation is the accumulated postretirement benefit obligation. Any plan with an overfunded status is recognized as an asset, and any plan with an underfunded status is recognized as a liability. Any gains or losses and prior service costs or credits that have not been recognized as a component of net periodic benefit costs are recorded as a component of other comprehensive earnings (losses), net of deferred taxes. PMI elects to recognize actuarial gains/(losses) using the corridor approach.

Fair value measurements

PMI follows ASC 820, *Fair Value Measurements and Disclosures* with respect to assets and liabilities that are measured at fair value. The guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The guidance also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of input that may be used to measure fair value. Level 1 inputs are quoted prices in active markets for identical assets or liabilities. Level 2 inputs include quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 3 are unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

Foreign currency translation

PMI translates the results of operations of its subsidiaries and affiliates using average exchange rates during each period, whereas balance sheet accounts are translated using exchange rates at the end of each period. Currency translation adjustments are recorded as a component of stockholders' (deficit) equity. In addition, some of PMI's subsidiaries have assets and liabilities denominated in currencies other than their functional currencies, and to the extent those are not designated as net investment hedges, these assets and liabilities generate transaction gains and losses when translated into their respective functional currencies.

Goodwill and non-amortizable intangible assets valuation

PMI tests goodwill and non-amortizable intangible assets for impairment annually or more frequently if events occur that would warrant such review. PMI performs its annual impairment analysis in the second quarter of each year. The impairment analysis involves comparing the fair value of each reporting unit or non-amortizable intangible asset to the carrying value. If the carrying value exceeds the fair value, goodwill or a non-amortizable intangible asset is considered impaired.

Hedging instruments

Derivative financial instruments are recorded at fair value on the consolidated balance sheets as either assets or liabilities. Changes in the fair value of derivatives are recorded each period either in accumulated other comprehensive losses on the consolidated balance sheet or in earnings, depending on whether a derivative is designated and effective as part of a hedge transaction and, if it is, the type of hedge transaction. Gains and losses on

derivative instruments reported in accumulated other comprehensive losses are reclassified to the consolidated statements of earnings, into the same line item as the impact of the underlying transaction, in the periods in which operating results are affected by the hedged item. Cash flows from hedging instruments are classified in the same manner as the affected hedged item in the consolidated statements of cash flows.

Impairment of long-lived assets

PMI reviews long-lived assets, including amortizable intangible assets, for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable. PMI performs undiscounted operating cash flow analyses to determine if an impairment exists. For purposes of recognition and measurement of an impairment for assets held for use, PMI groups assets and liabilities at the lowest level for which cash flows are separately identifiable. If an impairment is determined to exist, any related impairment loss is calculated based on fair value. Impairment losses on assets to be disposed of, if any, are based on the estimated proceeds to be received, less costs of disposal.

Impairment of investment in non-marketable equity securities

Non-marketable equity securities are subject to periodic impairment reviews during which PMI considers both qualitative and quantitative factors that may have a significant impact on the investees' fair value. Upon determining that an impairment may exist, the security's fair value is calculated and compared to its carrying value, and an impairment is recognized immediately if the carrying value exceeds the fair value. For further details see Note 20. *Deconsolidation of RBH*.

Impairment of equity method investments

Equity method investments are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of the investments may not be recoverable. An impairment loss would be recorded whenever a decline in value of an equity investment below its carrying amount is determined to be other than temporary. PMI determines whether a loss is other than temporary by considering the length of time and extent to which the fair value of the equity investment has been less than the carrying amount, the financial condition of the equity investment, and the intent to retain the investment for a period of time is sufficient to allow for any anticipated recovery in market value.

Income taxes

Income taxes are provided on all earnings for jurisdictions outside the United States. These provisions, as well as state and local income tax provisions, are determined on a separate company basis, and the related assets and liabilities are recorded in PMI's consolidated balance sheets. Significant judgment is required in determining income tax provisions and in evaluating tax positions. PMI recognizes accrued interest and penalties associated with uncertain tax positions as part of the provision for income taxes on the consolidated statements of earnings. PMI recognizes income taxes associated with Global Intangible Low-Taxed Income ("GILTI") taxes as current period expense rather than including these amounts in the measurement of deferred taxes.

Inventories

Inventories are stated at the lower of cost or market. The first-in, first-out and average cost methods are used to cost substantially all inventories. It is a generally recognized industry practice to classify leaf tobacco inventory as a current asset, although part of such inventory, because of the duration of the aging process, ordinarily would not be utilized within one year.

Leases

PMI determines that a contract contains a lease if the contract conveys a right to control the use of the identified asset for a period of time in exchange for consideration. Lease expense is recognized on a straight-line basis over the lease term with the expense recorded in cost of sales or marketing, administration and research costs depending on the nature of the leased item. At lease commencement, PMI recognizes lease liabilities and the corresponding right-of-use assets (at the present value of future payments) for predominately all of its operating leases. The recognition of the right-of-use asset and lease liability includes renewal options when it is reasonably certain that they will be exercised. Certain of PMI's leases include payments that are based on changes to an index or on actual usage. These lease payments are adjusted periodically and are included within variable lease costs. PMI accounts for lease and nonlease components as a single-lease component with the exception of its vehicle leases, of which PMI accounts for the lease components separately from the nonlease components. Additionally, leases with an initial term of 12 months or less are not included in the right-of-use asset or lease liability on the consolidated statement of financial position.

Marketing costs

PMI supports its products with advertising, adult consumer engagement and trade promotions. Such programs include, but are not limited to, discounts, rebates, in-store display incentives, e-commerce, mobile and other digital platforms, adult consumer activation and promotion activities, as well as costs associated with adult consumer experience outlets and other adult consumer touchpoints and volume-based incentives. Advertising, as well as certain consumer engagement and trade activities costs, are expensed as incurred. Trade promotions are recorded as a reduction of revenues based on amounts estimated as being due to customers at the end of a period, based principally on historical utilization. For interim reporting purposes, advertising and certain consumer engagement expenses are charged to earnings based on estimated sales and related expenses for the full year.

Revenue recognition

PMI recognizes revenue primarily through the manufacture and sale of cigarettes and other nicotine-containing products, including reduced-risk products. The majority of PMI revenues are generated by sales through direct and indirect distribution networks with short-term payment conditions and where control is typically transferred to the customer either upon shipment or delivery of goods. PMI evaluates the transfer of control through evidence of the customer's receipt and acceptance, transfer of title, PMI's right to payment for those products and the customer's ability to direct the use of those products upon receipt. Typically, PMI's performance obligations are satisfied and revenue is recognized either upon shipment or delivery of goods.

In certain instances, PMI facilitates shipping and handling activities after control has transferred to the customer. PMI has elected to record all shipping and handling activities as costs to fulfill a contract. The shipping and handling costs that have not been incurred at the time revenue is recognized are accrued. The transaction price is typically based on the amount billed to the customer and includes estimated variable consideration, where applicable. Such variable consideration is typically not constrained and is estimated based on the most likely amount that PMI expects to be entitled to under the terms of the contracts with customers, historical experience of discount or rebate redemption, where relevant, and the terms of any underlying discount or rebate programs, which may change from time to time as the business and product categories evolve. PMI has elected to exclude excise taxes collected from customers from the measurement of the transaction price, thereby presenting revenues net of excise taxes. Estimated costs associated with warranty programs are generally provided for in cost of sales in the period the related revenues are recognized.

Stock-based compensation

PMI measures compensation cost for all stock-based awards at fair value on date of grant and recognizes the compensation costs over the service periods for awards expected to vest. PMI's accounting policy is to estimate the number of awards expected to be forfeited and adjust the expense when it is no longer probable that the employee will fulfill the service condition. For further details, see Note 9. *Stock Plans*.

Note 3.

Goodwill and Other Intangible Assets, net:

The movements in goodwill were as follows:

(in millions)	European Union	Eastern Europe	Middle East & Africa	South & Southeast Asia	East Asia & Australia	Latin America & Canada	Total
Balance at January 1, 2019	$ 1,357	$ 303	$ 87	$ 2,795	$ 536	$ 2,111	$ 7,189
Changes due to:							
Currency	(19)	(3)	2	103	15	34	132
Deconsolidation of RBH						(1,463)	(1,463)
Balances, December 31, 2019	1,338	300	89	2,898	551	682	5,858
Changes due to:							
Currency	**96**	**17**	**(3)**	**17**	**8**	**(29)**	**106**
Balances, December 31, 2020	**$ 1,434**	**$ 317**	**$ 86**	**$ 2,915**	**$ 559**	**$ 653**	**$ 5,964**

At December 31, 2020, goodwill primarily reflects PMI's acquisitions in Colombia, Greece, Indonesia, Mexico, Pakistan and Serbia, as well as the business combination in the Philippines.

For details on the deconsolidation of RBH, see Note 20. *Deconsolidation of RBH.*

Details of other intangible assets were as follows:

		December 31, 2020			December 31, 2019		
(in millions)	Weighted-Average Remaining Useful Life	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Non-amortizable intangible assets		**$ 1,289**		**$ 1,289**	$ 1,319		$ 1,319
Amortizable intangible assets:							
Trademarks	**13 years**	**1,233**	**$ 594**	**639**	1,217	$ 526	691
Distribution networks	**7 years**	**115**	**78**	**37**	113	72	41
Other*	**8 years**	**104**	**50**	**54**	106	44	62
Total other intangible assets		**$ 2,741**	**$ 722**	**$ 2,019**	$ 2,755	$ 642	$ 2,113

* Primarily includes intellectual property rights

Non-amortizable intangible assets substantially consist of trademarks from PMI's acquisitions in Indonesia and Mexico. The decrease since December 31, 2019, was due to currency movements of $(30) million.

The increase in the gross carrying amount of amortizable intangible assets from December 31, 2019, was mainly due to currency movements of $15 million.

The change in the accumulated amortization from December 31, 2019 was mainly due to the 2020 amortization of $73 million, combined with currency movements of $7 million.

Amortization expense for each of the next five years is estimated to be $72 million or less, assuming no additional transactions occur that require the amortization of intangible assets.

During the second quarter of 2020, PMI completed its annual review of goodwill and non-amortizable intangible assets for potential impairment, and no impairment charges were required as a result of this review.

Note 4.

Related Parties - Equity Investments and Other:

Equity Method Investments:

At December 31, 2020 and 2019, PMI had total equity method investments of $966 million and $1,053 million, respectively. Equity method investments are initially recorded at cost. Under the equity method of accounting, the investment is adjusted for PMI's proportionate share of earnings or losses, dividends, capital contributions, changes in ownership interests and movements in currency translation adjustments. The carrying value of our equity method investments at December 31, 2020 and 2019, exceeded our share of the investees' book value by $773 million and $901 million, respectively. The difference between the investment carrying value and the amount of underlying equity in net assets, excluding $745 million and $863 million attributable to goodwill as of December 31, 2020 and 2019, respectively, is being amortized on a straight-line basis over the underlying assets' estimated useful lives of 10 to 20 years. At December 31, 2020 and 2019, PMI received year-to-date dividends from equity method investees of $79 million and $100 million, respectively.

PMI holds a 23% equity interest in Megapolis Distribution BV, the holding company of CJSC TK Megapolis, PMI's distributor in Russia (Eastern Europe segment).

PMI holds a 49% equity interest in United Arab Emirates-based Emirati Investors-TA (FZC) (“EITA”). PMI holds an approximate 25% economic interest in Société des Tabacs Algéro-Emiratie (“STAEM”), an Algerian joint venture that is 51% owned by EITA and 49% by the Algerian state-owned enterprise Management et Développement des Actifs et des Ressources Holding ("MADAR Holding"), which is part of the Middle East & Africa segment, manufactures and distributes under license some of PMI’s brands.

The initial investments in Megapolis Distribution BV and EITA were recorded at cost and are included in equity investments on the consolidated balance sheets.

Equity securities:

Following the deconsolidation of RBH on March 22, 2019, PMI recorded the continuing investment in RBH, PMI's wholly owned subsidiary in Canada, at fair value of $3,280 million at the date of deconsolidation, within equity investments. For further details, see Note 20. *Deconsolidation of RBH*. Transactions between PMI and RBH are considered to be related-party transactions from the date of deconsolidation and are included in the tables below.

The fair value of PMI’s other equity securities, which have been classified within Level 1, was $256 million and $332 million for the years ending December 31, 2020 and 2019, respectively. Unrealized pre-tax gain (loss) of $(76) million and $44 million ($(60) million and $35 million net of tax) on these equity securities was recorded in the consolidated statement of earnings for the years ended December 31, 2020 and 2019, respectively. For a description of the fair value hierarchy and the three levels of inputs used to measure fair values, see Note 2. *Summary of Significant Accounting Policies*.

Other related parties:

United Arab Emirates-based Trans-Emirates Trading and Investments (FZC) ("TTI") holds a 33% non-controlling interest in Philip Morris Misr LLC ("PMM"), an entity incorporated in Egypt which is consolidated in PMI’s financial statements in the Middle East & Africa segment. PMM sells, under license, PMI brands in Egypt through an exclusive distribution agreement with a local entity that is also controlled by TTI.

Godfrey Phillips India Ltd ("GPI") is one of the non-controlling interest holders in IPM India, which is a 56.3% owned PMI consolidated subsidiary in the South & Southeast Asia segment. GPI also acts as contract manufacturer and distributor for IPM India. Amounts in the tables below include transactions between these related parties.

Financial activity with the above related parties:

PMI's net revenues and expenses with the above related parties were as follows:

(in millions)	For the Years Ended December 31, 2020	2019	2018
Net revenues			
Megapolis Group	**$ 2,174**	$ 2,236	$ 1,994
Other	**1,059**	1,015	720
Net revenues [(a)]	**$ 3,233**	$ 3,251	$ 2,714
Expenses:			
Other	**$ 51**	$ 63	$ 21
Expenses	**$ 51**	$ 63	$ 21

[(a)] Net revenues exclude excise taxes and VAT billed to customers.

PMI's balance sheet activity with the above related parties was as follows:

(in millions)	At December 31, 2020	2019
Receivables:		
Megapolis Group	**$ 209**	$ 375
Other	**156**	148
Receivables	**$ 365**	$ 523
Payables:		
Other	**$ 13**	$ 20
Payables	**$ 13**	$ 20

The activities with the above related parties are in the ordinary course of business, and are primarily for distribution, service fees, contract manufacturing and license agreements. PMI eliminated its respective share of all significant intercompany transactions with the equity method investees.

Note 5.

Product Warranty:

PMI's *IQOS* devices are subject to standard product warranties generally for a period of 12 months from the date of purchase or such other periods as required by law. PMI generally provides in cost of sales for the estimated cost of warranty in the period the related revenue is recognized. PMI assesses the adequacy of its accrued product warranties and adjusts the amounts as necessary based on actual experience and changes in future estimates. Factors that affect product warranties may vary across markets but typically include device version mix, product failure rates, logistics and service delivery costs, and warranty policies. PMI accounts for its product warranties within other accrued liabilities. At December 31, 2020 and December 31, 2019, these amounts were as follows:

(in millions)	At Decemb 2020	
Balance at beginning of period	$ 140	$
Changes due to:		
Warranties issued	242	
Settlements	(254)	
Currency/Other	9	
Balance at end of period	$ 137	$

Note 6.

Acquisitions:

On March 21, 2018, PMI acquired the remaining 49% interest in Tabacalera Costarricense, S.A. and Mendiola y Compañía, S.A. for a net purchase price of $95 million, which included $2 million of contingent consideration. As a result, PMI now owns 100% of these Costa Rican affiliates. The purchase of the remaining 49% interest resulted in a decrease to PMI's additional paid-in capital of $86 million.

Note 7.

Indebtedness:

Short-Term Borrowings

At December 31, 2020 and 2019, PMI's short-term borrowings and related average interest rates consisted of the following:

	December 31, 2020		December 31, 2019	
(in millions)	Amount Outstanding	Average Year-End Rate	Amount Outstanding	Average Year-End Rate
Commercial paper	$ —	— %	$ —	— %
Bank loans	244	5.3	338	5.5
	$ 244		$ 338	

Given the mix of subsidiaries and their respective local economic environments, the average interest rate for bank loans above can vary significantly from day to day and country to country.

The fair values of PMI's short-term borrowings at December 31, 2020 and 2019, based upon current market interest rates, approximate the amounts disclosed above.

Long-Term Debt

At December 31, 2020 and 2019, PMI's long-term debt consisted of the following:

(in millions)	December 31, 2020	December 31, 2019
U.S. dollar notes, 0.875% to 6.375% (average interest rate 3.199%), due through 2044	**$ 21,221**	$ 19,783
Foreign currency obligations:		
Euro notes, 0.125% to 3.125% (average interest rate 1.983%), due through 2039	**9,253**	9,822
Swiss franc notes, 1.625% to 2.000% (average interest rate 1.830%), due through 2024	**622**	899
Other (average interest rate 3.187%), due through 2025 [(a)]	**196**	203
Carrying value of long-term debt	**31,292**	30,707
Less current portion of long-term debt	**3,124**	4,051
	$ 28,168	$ 26,656

[(a)] Includes mortgage debt in Switzerland as well as $37 million and $56 million in finance leases at December 31, 2020 and 2019, respectively.

The fair value of PMI's outstanding long-term debt, which is utilized solely for disclosure purposes, is determined using quotes and market interest rates currently available to PMI for issuances of debt with similar terms and remaining maturities. At December 31, 2020 and 2019 the fair value of PMI's outstanding long-term debt, excluding the aforementioned finance leases, was as follows:

(in millions)	December 31, 2020	December 31, 2019
Level 1	**$ 35,227**	$ 32,821
Level 2	**177**	167

For a description of the fair value hierarchy and the three levels of inputs used to measure fair values, see Note 2. *Summary of Significant Accounting Policies*.

Debt Issuances Outstanding:

PMI's debt issuances outstanding at December 31, 2020, were as follows:

(in millions)

Type	Face Value	Interest Rate	Issuance	Maturity
U.S. dollar notes	**$750**	**1.875%**	February 2016	February 2021
U.S. dollar notes	**$350**	**4.125%**	May 2011	May 2021
U.S. dollar notes	**$750**	**2.900%**	November 2011	November 2021
U.S. dollar notes	**$500**	**2.625%**	February 2017	February 2022
U.S. dollar notes	**$750**	**2.375%**	August 2017	August 2022
U.S. dollar notes	**$750**	**2.500%**	August 2012	August 2022
U.S. dollar notes	**$750**	**2.500%**	November 2017	November 2022
U.S. dollar notes	**$600**	**2.625%**	March 2013	March 2023
U.S. dollar notes	**$500**	**2.125%**	May 2016	May 2023
U.S. dollar notes	**$750**	**1.125%**	May 2020	May 2023
U.S. dollar notes	**$500**	**3.600%**	November 2013	November 2023
U.S. dollar notes	**$900**	**2.875%**	May 2019	May 2024
U.S. dollar notes	**$750**	**3.250%**	November 2014	November 2024
U.S. dollar notes	**$750**	**1.500%**	May 2020	May 2025
U.S. dollar notes	**$750**	**3.375%**	August 2015	August 2025
U.S. dollar notes	**$750**	**2.750%**	February 2016	February 2026
U.S. dollar notes	**$750**	**0.875%**	November 2020	May 2026
U.S. dollar notes	**$500**	**3.125%**	August 2017	August 2027
U.S. dollar notes	**$500**	**3.125%**	November 2017	March 2028
U.S. dollar notes	**$750**	**3.375%**	May 2019	August 2029
U.S. dollar notes	**$750**	**2.100%**	May 2020	May 2030
U.S. dollar notes	**$750**	**1.750%**	November 2020	November 2030
U.S. dollar notes	**$1,500**	**6.375%**	May 2008	May 2038
U.S. dollar notes	**$750**	**4.375%**	November 2011	November 2041
U.S. dollar notes	**$700**	**4.500%**	March 2012	March 2042
U.S. dollar notes	**$750**	**3.875%**	August 2012	August 2042
U.S. dollar notes	**$850**	**4.125%**	March 2013	March 2043
U.S. dollar notes	**$750**	**4.875%**	November 2013	November 2043
U.S. dollar notes	**$750**	**4.250%**	November 2014	November 2044
U.S. dollar notes [a]	**$500**	**4.250%**	May 2016	November 2044
EURO notes [b]	**€750 (approximately $1,029)**	**1.875%**	March 2014	March 2021
EURO notes [b]	**€600 (approximately $761)**	**2.875%**	May 2012	May 2024
EURO notes [b]	**€500 (approximately $582)**	**0.625%**	November 2017	November 2024
EURO notes [b]	**€750 (approximately $972)**	**2.750%**	March 2013	March 2025
EURO notes [b]	**€1,000 (approximately $1,372)**	**2.875%**	March 2014	March 2026

[a] These notes are a further issuance of the 4.250% notes issued by PMI in November 2014.
[b] USD equivalents for foreign currency notes were calculated based on exchange rates on the date of issuance.

The net proceeds from the sale of the securities listed in the table above were used for general corporate purposes, including working capital requirements and repurchase of PMI's common stock until 2015.

On January 25, 2021, PMI redeemed all of its outstanding 1.875% U.S. dollar notes due February 25, 2021. As of December 31, 2020, $750 million aggregate principal amount of the U.S. dollar notes were outstanding. The pre-tax loss related to this debt extinguishment, which was not material, will be included in Interest expense, net on PMI's condensed consolidated statements of earnings for the three months ended March 31, 2021.

Aggregate maturities:

Aggregate maturities of long-term debt are as follows:

(in millions)

2021	$	3,124
2022		2,760
2023		2,362
2024		3,442
2025		2,424
2026-2030		7,206
2031-2035		1,535
Thereafter		8,699
		31,552
Debt discounts		(260)
Total long-term debt	$	31,292

Credit Facilities

At December 31, 2020, PMI's total committed credit facilities were as follows:

Type (in billions of dollars)		**Committed Credit Facilities**
364-day revolving credit, expiring February 2, 2021	**$**	**2.0**
Multi-year revolving credit, expiring October 1, 2022		**3.5**
Multi-year revolving credit, expiring February 10, 2025		**2.0**
Total facilities	**$**	**7.5**

At December 31, 2020, there were no borrowings under these committed credit facilities, and the entire committed amounts were available for borrowing.

These facilities do not include any credit rating triggers, material adverse change clauses or any provisions that could require PMI to post collateral. The $3.5 billion multi-year revolving credit facility in the table above requires us to maintain a ratio of consolidated earnings before interest, taxes, depreciation and amortization ("consolidated EBITDA") to consolidated interest expense of not less than 3.5 to 1.0 on a rolling four-quarter basis. At December 31, 2020, PMI's ratio calculated in accordance with the agreement was 12.6 to 1.0. PMI expects to continue to meet PMI's covenants. The terms "consolidated EBITDA" and "consolidated interest expense," both of which include certain adjustments, are defined in the facility agreements previously filed with the U.S. Securities and Exchange Commission.

On January 29, 2021, PMI entered into an agreement to amend and extend the term of its 364-day revolving credit facility from February 2, 2021, to February 1, 2022 in the amount of $1.75 billion. On January 29, 2021, PMI also entered into an agreement, effective February 10, 2021, to amend and extend the term of its $2.0 billion multi-year revolving credit facility, for an additional year covering the period February 11, 2025 to February 10, 2026, in the amount of $1.86 billion.

In addition to the committed credit facilities discussed above, certain subsidiaries maintain short-term credit arrangements to meet their respective working capital needs. These credit arrangements, which amounted to approximately $2.7 billion at December 31, 2020 and December 31, 2019, respectively, are for the sole use of the subsidiaries. Borrowings under these arrangements and other bank loans amounted to $244 million at December 31, 2020, and $338 million at December 31, 2019.

Note 8.

Capital Stock:

Shares of authorized common stock are 6.0 billion; issued, repurchased and outstanding shares were as follows:

	Shares Issued	Shares Repurchased	Shares Outstanding
Balances, January 1, 2018	2,109,316,331	(556,098,569)	1,553,217,762
Issuance of stock awards		1,361,959	1,361,959
Balances, December 31, 2018	2,109,316,331	(554,736,610)	1,554,579,721
Issuance of stock awards		1,314,942	1,314,942
Balances, December 31, 2019	2,109,316,331	(553,421,668)	1,555,894,663
Issuance of stock awards		**1,479,068**	**1,479,068**
Balances, December 31, 2020	**2,109,316,331**	**(551,942,600)**	**1,557,373,731**

At December 31, 2020, 25,148,458 shares of common stock were reserved for stock awards under PMI's stock plans, and 250 million shares of preferred stock, without par value, were authorized but unissued. PMI currently has no plans to issue any shares of preferred stock.

Note 9.

Stock Plans:

In May 2017, PMI's shareholders approved the Philip Morris International Inc. 2017 Performance Incentive Plan (the "2017 Plan"). Under the 2017 Plan, PMI may grant to eligible employees restricted shares and restricted share units, performance-based cash incentive awards and performance-based equity awards. Up to 25 million shares of PMI's common stock may be issued under the 2017 Plan. At December 31, 2020, shares available for grant under the 2017 Plan were 17,293,960.

In May 2017, PMI's shareholders also approved the Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors (the "2017 Non-Employee Directors Plan"). A non-employee director is defined as a member of the PMI Board of Directors who is not a full-time employee of PMI or of any corporation in which PMI owns, directly or indirectly, stock possessing at least 50% of the total combined voting power of all classes of stock entitled to vote in the election of directors in such corporation. Up to 1 million shares of PMI common stock may be awarded under the 2017 Non-Employee Directors Plan. At December 31, 2020, shares available for grant under the plan were 933,338.

Restricted share unit (RSU) awards

PMI may grant RSU awards to eligible employees; recipients may not sell, assign, pledge or otherwise encumber such awards. Such awards are subject to forfeiture if certain employment conditions are not met. RSU awards generally vest on the third anniversary of the grant date. RSU awards do not carry voting rights, although they do earn dividend equivalents.

During 2020, the activity for RSU awards was as follows:

	Number of Shares	A Da
Balance at January 1, 2020	**3,725,870**	**$**
Granted	**1,728,680**	
Vested	**(1,206,871)**	
Forfeited	**(149,439)**	
Balance at December 31, 2020	**4,098,240**	**$**

During the years ended December 31, 2020, 2019 and 2018, the grant date fair value of the RSU awards granted to PMI employees and the recorded compensation expense related to RSU awards were as follows:

(in millions, except per RSU award granted)	Total Grant Date Fair Value of RSU Awards Granted	Weighted-Average Grant Date Fair Value Per RSU Award Granted	Compensation Expense related to RSU Awards
2020	**$ 148**	**$ 85.79**	**$ 129**
2019	$ 133	$ 77.28	$ 118
2018	$ 129	$ 100.19	$ 114

The fair value of the RSU awards at the date of grant is amortized to expense over the restriction period, typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2020, PMI had $133 million of total unrecognized compensation costs related to non-vested RSU awards. These costs are expected to be recognized over a weighted-average period of approximately two years, or upon death, disability or reaching the age of 58.

During the years ended December 31, 2020, 2019 and 2018, share and fair value information for PMI RSU awards that vested were as follows:

(dollars in millions)	Shares of RSU Awards that Vested	Grant Date Fair Value of Vested Shares of RSU Awards	Total Fair Value of RSU Awards that Vested
2020	**1,206,871**	**$ 117**	**$ 102**
2019	1,126,057	$ 101	$ 95
2018	1,451,876	$ 121	$ 149

Performance share unit (PSU) awards

PMI may grant PSU awards to certain executives; recipients may not sell, assign, pledge or otherwise encumber such awards. The PSU awards require the achievement of certain performance factors, which are predetermined at the time of grant, typically over a three-year performance cycle. The performance metrics for such PSU's granted during the 2020 consisted of PMI's Total Shareholder Return ("TSR") relative to a predetermined peer group and on an absolute basis (40% weight), PMI's currency-neutral compound annual adjusted diluted earnings per share growth rate (30% weight), and PMI's performance against specific measures of PMI's transformation, defined as net revenues from PMI's RRPs and any other non-combustible products as a percentage of PMI's total net revenues in the last year of the performance cycle (30% weight). The performance metrics for such PSUs granted during the years ended 2019 and 2018 consisted of PMI's TSR relative to a predetermined peer group and on an absolute basis (50% weight), PMI's currency-neutral compound annual adjusted operating income growth rate, excluding acquisitions (30% weight), and PMI's performance against specific measures of PMI's transformation (20% weight).

The aggregate of the weighted performance factors for the three metrics in each such PSU award determines the percentage of PSUs that will vest at the end of the three-year performance cycle. The minimum percentage of such PSUs that can vest is zero, with a target percentage of 100 and a maximum percentage of 200. Each such vested PSU entitles the participant to one share of common stock. An aggregate weighted PSU performance factor of 100 will result in the targeted number of PSUs being vested. At the end of the performance cycle, participants are entitled to an amount equivalent to the accumulated dividends paid on common stock during the performance cycle for the number of shares earned. PSU awards do not carry voting rights.

During 2020, the activity for PSU awards was as follows:

	Number of Shares	Grant Date Fair Value Subject to Other Performance Factors (Per Share)	Grant Date Fair Value Subject to TSR Performance Factor (Per Share)
Balance at January 1, 2020	**1,347,460**	**$ 88.19**	**$ 107.61**
Granted	**671,220**	**86.04**	**80.36**
Vested	**(343,806)**	**85.72**	**128.72**
Forfeited	**(202,074)**	**95.66**	**116.67**
Balance at December 31, 2020	**1,472,800**	**$ 86.76**	**$ 90.48**

During the years ended December 31, 2020, 2019 and 2018, the grant date fair value of the PSU awards granted to PMI employees and the recorded compensation expense related to PSU awards were as follows:

(in millions, except per PSU award granted)	PSU Grant Date Fair Value Subject to Other Performance Factors		PSU Grant Date Fair Value Subject to TSR Performance Factor		Compensation Expense related to PSU Awards
	Total	Per PSU Award	Total	Per PSU Award	Total
2020	**$ 28**	**$ 86.04**	**$ 28**	**$ 80.36**	**$ 38**
2019	$ 30	$ 77.23	$ 21	$ 83.59	$ 54
2018	$ 20	$ 100.69	$ 24	$ 118.98	$ 24

The grant date fair value of the PSU awards subject to the other performance factors was determined by using the average of the high and low market price of PMI's stock at the date of the grant. The grant date fair value of the PSU market-based awards subject to the TSR performance factor was determined by using the Monte Carlo simulation model. The following assumptions were used to determine the grant date fair value of the PSU awards subject to the TSR performance factor for the years ended December 31, 2020, 2019 and 2018:

	For the Years Ended December 31,	
	2020	**2019**
Risk-free interest rate [a]	**1.4 %**	2.4 %
Expected volatility	**23.5 %** [b]	21.4 % [b]

[a] Based on the U.S. Treasury yield curve.
[b] Determined using the observed historical volatility.
[c] Determined using a weighted-average of historical and implied volatility.

The fair value of the PSU award at the date of grant is amortized to expense over the performance period, which is typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2020, PMI had $39 million of total unrecognized compensation cost related to non-vested PSU awards. This cost is recognized over a weighted-average performance cycle period of approximately two years, or upon death, disability or reaching the age of 58.

During the years ended December 31, 2020, and 2019, share and fair value information for PMI PSU awards that vested were as follows:

(dollars in millions)	Shares of PSU Awards that Vested	Grant Date Fair Value of Vested Shares of PSU Awards	Total Fair Value of PSU Awards that Vested
2020	**343,806**	**$ 35**	**$ 30**
2019	330,616	$ 32	$ 28

During the year ended December 31, 2018, there were no PSU awards that vested.

Note 10.

Earnings per Share:

Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are participating securities and therefore are included in PMI's earnings per share calculation pursuant to the two-class method.

Basic and diluted earnings per share ("EPS") were calculated using the following:

(in millions)	For the Years Ended December 31		
	2020	**2019**	**2018**
Net earnings attributable to PMI	**$ 8,056**	$ 7,185	$ 7,911
Less distributed and undistributed earnings attributable to share-based payment awards	**20**	17	16
Net earnings for basic and diluted EPS	**$ 8,036**	$ 7,168	$ 7,895
Weighted-average shares for basic EPS	**1,557**	1,555	1,555
Plus contingently issuable performance stock units (PSUs)	**1**	1	—
Weighted-average shares for diluted EPS	**1,558**	1,556	1,555

For the 2020, 2019 and 2018 computations, there were no antidilutive stock options.

Note 11.

Income Taxes:

Earnings before income taxes and provision for income taxes consisted of the following for the years ended December 31, 2020, 2019 and 2018:

(in millions)	2020	2019	2018
Earnings before income taxes	**$ 10,953**	$ 9,872	$ 10,671
Provision for income taxes:			
United States federal and state:			
Current	**$ (80)**	$ 17	$ 120
Deferred	**53**	24	(113)
Total United States	**(27)**	41	7
Outside United States:			
Current	**2,600**	2,417	2,425
Deferred	**(196)**	(165)	13
Total outside United States	**2,404**	2,252	2,438
Total provision for income taxes	**$ 2,377**	$ 2,293	$ 2,445

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act and, on December 27, 2020, the Consolidated Appropriations Act, 2021 ("U.S. COVID-19 Acts") were signed into law in the U.S. to provide certain relief as a result of the COVID-19 pandemic. In addition, governments around the world have enacted or implemented various forms of tax relief measures in response to the economic conditions in the wake of COVID-19. As of December 31, 2020, PMI has determined that neither the U.S. COVID-19 Acts nor changes to income tax laws or regulations in other jurisdictions had a significant impact on PMI's effective tax rate, with the exception of the corporate income tax rate reduction in Indonesia.

On July 20, 2020, the U.S. Department of the Treasury and the Internal Revenue Service released final and proposed regulations under the Global Intangible Low-Taxed Income ("GILTI") and other provisions of the Internal Revenue Code. PMI has analyzed these elective regulations and recorded the impact in its consolidated financial statements, as described below.

At December 31, 2017, PMI recorded a one-time transition tax liability on its accumulated foreign earnings, which is payable over an eight-year period beginning in 2018. At December 31, 2020 and December 31, 2019, $1.1 billion and $1.2 billion of PMI's remaining transition tax liability, respectively, was recorded in "income taxes and other liabilities" on PMI's consolidated balance sheets.

At December 31, 2020 and December 31, 2019, U.S. federal and foreign deferred income taxes have been provided on all accumulated earnings of PMI's foreign subsidiaries.

PMI is regularly examined by tax authorities around the world and is currently under examination in a number of jurisdictions. The U.S. federal statute of limitations remains open for the years 2017 and onward. Foreign and U.S. state jurisdictions have statutes of limitations generally ranging from three to five years. Years still open to examination by foreign tax authorities in major jurisdictions include Germany (2015 onward), Indonesia (2014 onward), Russia (2018 onward), Switzerland (2017 onward), and Turkey (2015 onward).

It is reasonably possible that within the next 12 months certain tax examinations will close, which could result in a change in unrecognized tax benefits, along with related interest and penalties. An estimate of any possible change cannot be made at this time.

A reconciliation of the beginning and ending amount of unrecognized tax benefits was as follows:

(in millions)	2020	2019	2018
Balance at January 1,	**$ 63**	$ 56	$ 145
Additions based on tax positions related to the current year	**11**	10	10
Additions for tax positions of previous years	**1**	1	15
Reductions for tax positions of prior years	**(4)**	(2)	(94)
Reductions due to lapse of statute of limitations	**(1)**	(1)	(3)
Settlements	**—**	—	(19)
Other	**2**	(1)	2
Balance at December 31,	**$ 72**	$ 63	$ 56

Unrecognized tax benefits and PMI's liability for contingent income taxes, interest and penalties were as follows:

(in millions)	December 31, 2020	December 31, 2019	December 31, 2018
Unrecognized tax benefits	**$ 72**	$ 63	$ 56
Accrued interest and penalties	**17**	16	12
Tax credits and other indirect benefits	**(9)**	(12)	(14)
Liability for tax contingencies	**$ 80**	$ 67	$ 54

The amount of unrecognized tax benefits that, if recognized, would impact the effective tax rate was $62 million at December 31, 2020. The remainder, if recognized, would principally affect deferred taxes.

For the years ended December 31, 2020, 2019 and 2018, PMI recognized income (expense) in its consolidated statements of earnings of $(1) million, $(4) million and $4 million, respectively, related to interest and penalties associated with uncertain tax positions.

The effective income tax rate on pre-tax earnings differed from the U.S. federal statutory rate for the following reasons for the years ended December 31, 2020, 2019 and 2018:

	2020	2019	2018
U.S. federal statutory rate	**21.0 %**	21.0 %	21.0 %
Increase (decrease) resulting from:			
Foreign rate differences	**0.6**	1.8	1.3
Dividend repatriation cost	**0.4**	(0.5)	2.5
Global intangible low-taxed income	**0.1**	1.4	1.2
U.S. state taxes	**0.2**	0.7	(1.1)
Foreign derived intangible income	**(0.6)**	(1.2)	(1.1)
Other	**—**	—	(0.9)
Effective tax rate	**21.7 %**	23.2 %	22.9 %

The 2020 effective tax rate decreased 1.5 percentage points to 21.7%. The change in the effective tax rate for 2020, as compared to 2019, was favorably impacted by changes in earnings mix by taxing jurisdiction, a reduction of U.S. state tax expense, a reduction of estimated U.S. income tax liabilities for years 2018 and 2019 due to the GILTI regulations mentioned above ($93 million) and the corporate income tax rate reduction in Indonesia, partially offset

by a decrease in deductions related to foreign-derived intangible income for the years 2018 and 2019 and repatriation cost differences.

The 2019 effective tax rate increased 0.3 percentage points to 23.2%. The change in the effective tax rate for 2019, as compared to 2018, was unfavorably impacted by changes in earnings mix by taxing jurisdiction and U.S. state deferred income tax expense, partially offset by the reversal of a deferred tax liability on the unremitted earnings of PMI's Canadian subsidiary, RBH ($49 million), a reduction in estimated U.S. federal income tax on dividend repatriation for the years 2015-2018 ($67 million), and other repatriation cost differences.

The tax effects of temporary differences that gave rise to deferred income tax assets and liabilities consisted of the following:

(in millions)	At Decer 2020
Deferred income tax assets:	
Accrued postretirement and postemployment benefits	$ 225
Accrued pension costs	720
Inventory	232
Accrued liabilities	182
Net operating loss carryforwards and tax credits	351
Foreign exchange	27
Other	124
Total deferred income tax assets	1,861
Less: valuation allowance	(250)
Deferred income tax assets, net of valuation allowance	1,611
Deferred income tax liabilities:	
Trade names	(374)
Property, plant and equipment	(200)
Unremitted earnings	(311)
Foreign exchange	—
Total deferred income tax liabilities	(885)
Net deferred income tax assets	$ 726

At December 31, 2020, PMI recorded deferred tax assets for net operating loss carryforwards and tax credits of $351 million, with varying dates of expiration, primarily after 2025, including $79 million with an unlimited carryforward period. At December 31, 2020, PMI has recorded a valuation allowance of $250 million against deferred tax assets that do not meet the more-likely-than not recognition threshold.

At December 31, 2019, PMI recorded deferred tax assets for net operating loss carryforwards of $486 million, with varying dates of expiration, primarily after 2024, including $98 million with an unlimited carryforward period. At December 31, 2019, PMI has recorded a valuation allowance of $304 million against deferred tax assets that do not meet the more-likely-than-not recognition threshold.

Note 12.

Segment Reporting:

PMI's subsidiaries and affiliates are engaged in the manufacture and sale of cigarettes and other nicotine-containing products, including RRPs, in markets outside of the United States of America. In addition, PMI ships versions of its Platform 1 device and its consumables authorized by the FDA to Altria Group, Inc. for sale in the United States under license. Operating segments for PMI are organized by geographic region and managed by segment managers who are responsible for the operating and financial results of the regions inclusive of all product categories sold in the region. PMI's operating segments are the European Union; Eastern Europe; Middle East & Africa; South & Southeast Asia; East Asia & Australia; and Latin America & Canada. PMI records net revenues and operating income to its segments based upon the geographic area in which the customer resides. Revenues from shipments of Platform 1 devices, heated tobacco units and accessories to Altria Group, Inc. for sale under license in the United States are included in Net Revenues of the Latin America & Canada segment.

PMI's chief operating decision maker evaluates segment performance and allocates resources based on regional operating income, which includes results from all product categories sold in each region. Interest expense, net, and provision for income taxes are centrally managed and, accordingly, such items are not presented by segment since they are excluded from the measure of segment profitability reviewed by management. Information about total assets by segment is not disclosed because such information is not reported to or used by PMI's chief operating decision maker. Segment goodwill and other intangible assets, net, are disclosed in Note

3. *Goodwill and Other Intangible Assets, net.* The accounting policies of the segments are the same as those described in Note 2. *Summary of Significant Accounting Policies.*
PMI disaggregates its net revenue from contracts with customers by both geographic location and product category for each of PMI's six operating segments, as PMI believes this best depicts how the nature, amount, timing and uncertainty of its revenue and cash flows are affected by economic factors.

Net revenues by segment were as follows:

	For the Years Ended December 31,		
(in millions)	**2020**	**2019**	**2018**
Net revenues:			
European Union	**$ 10,702**	$ 9,817	$ 9,298
Eastern Europe	**3,378**	3,282	2,921
Middle East & Africa	**3,088**	4,042	4,114
South & Southeast Asia	**4,396**	5,094	4,656
East Asia & Australia	**5,429**	5,364	5,580
Latin America & Canada	**1,701**	2,206	3,056
Net revenues	**$ 28,694**	$ 29,805	$ 29,625

Total net revenues attributable to customers located in Japan, PMI's largest market in terms of net revenues, were $4.1 billion, $3.9 billion and $3.8 billion in 2020, 2019 and 2018, respectively. PMI had one customer in the East Asia & Australia segment that accounted for 14%, 13% and 13% of PMI's consolidated net revenues, and one customer in the European Union segment that accounted for 11%, 10% and 10% of PMI's consolidated net revenues in 2020, 2019 and 2018, respectively.

PMI's net revenues by product category were as follows:

	For the Years Ended December 31,		
(in millions)	**2020**	**2019**	**2018**
Combustible products:			
European Union	**$ 8,053**	$ 8,093	$ 8,433
Eastern Europe	**2,250**	2,438	2,597
Middle East & Africa	**3,031**	3,721	3,732
South & Southeast Asia	**4,395**	5,094	4,656
East Asia & Australia	**2,468**	2,693	3,074
Latin America & Canada	**1,670**	2,179	3,037
Total combustible products	**$ 21,867**	$ 24,218	$ 25,529
Reduced-risk products:			
European Union	**$ 2,649**	$ 1,724	$ 865
Eastern Europe	**1,128**	844	324
Middle East & Africa	**57**	321	382
South & Southeast Asia	**1**	—	—
East Asia & Australia	**2,961**	2,671	2,506
Latin America & Canada	**31**	27	19
Total reduced-risk products	**$ 6,827**	$ 5,587	$ 4,096
Total PMI net revenues	**$ 28,694**	$ 29,805	$ 29,625

Note: Sum of product categories or Regions might not foot to total PMI due to roundings.

Net revenues related to combustible products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of PMI's cigarettes and other tobacco products combined.

Other tobacco products primarily include roll-your-own and make-your-own cigarettes, pipe tobacco, cigars and cigarillos and do not include reduced-risk products.

Net revenues related to reduced-risk products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of PMI's heated tobacco units, heat-not-burn devices and related accessories, and other nicotine-containing products, which primarily include PMI's e-vapor products.

Operating income by segment were as follows:

(in millions)	For the Years Ended December 31,		
	2020	**2019**	**2018**
Operating income:			
European Union	**$ 5,098**	$ 3,970	$ 4,105
Eastern Europe	**871**	547	902
Middle East & Africa	**1,026**	1,684	1,627
South & Southeast Asia	**1,709**	2,163	1,747
East Asia & Australia	**2,400**	1,932	1,851
Latin America & Canada	**564**	235	1,145
Operating income	**$ 11,668**	$ 10,531	$ 11,377

Items affecting the comparability of results from operations were as follows:

- **Asset impairment and exit costs** - See Note 19. *Asset Impairment and Exit Costs* for details of the $149 million and $422 million pre-tax charges for the years ended December 31, 2020 and 2019, respectively, as well as a breakdown of these costs by segment.
- **Russia excise and VAT audit charge** - See Note 17. *Contingencies* for details of the $374 million pre-tax charge included in the Eastern Europe segment for the year ended December 31, 2019.
- **Canadian tobacco litigation-related expense** - See Note 17. *Contingencies* and Note 20. *Deconsolidation of RBH* for details of the $194 million pre-tax charge included in the Latin America & Canada segment for the year ended December 31, 2019.
- **Loss on deconsolidation of RBH** - See Note 20. *Deconsolidation of RBH* for details of the $239 million loss included in the Latin America & Canada segment for the year ended December 31, 2019.
- **Brazil indirect tax credit** - Following a final and enforceable decision by the highest court in Brazil in October 2020, PMI recorded a gain of $119 million for tax credits representing overpayments of indirect taxes for the period from March 2012 through December 2019; these tax credits will be applied to future tax liabilities in Brazil. This amount was included as a reduction in marketing, administration and research costs in the consolidated statements of earnings for the year ended December 31, 2020 and was included in the operating income of the Latin America & Canada segment. A decision regarding an additional amount of overpaid indirect taxes of approximately $90 million is still pending before this court.

Other segment data were as follows:

(in millions)	For the Years Ended December 31, 2020	2019	2018
Depreciation expense:			
European Union	**$ 266**	$ 254	$ 269
Eastern Europe	**173**	147	101
Middle East & Africa	**75**	90	105
South & Southeast Asia	**137**	142	154
East Asia & Australia	**188**	185	173
Latin America & Canada	**58**	69	94
	897	887	896
Other	**11**	11	11
Total depreciation expense	**$ 908**	$ 898	$ 907

(in millions)	For the Years Ended December 31, 2020	2019	2018
Capital expenditures:			
European Union	**$ 326**	$ 466	$ 813
Eastern Europe	**88**	132	136
Middle East & Africa	**22**	35	65
South & Southeast Asia	**115**	100	129
East Asia & Australia	**13**	67	215
Latin America & Canada	**36**	52	74
	600	852	1,432
Other	**2**	—	4
Total capital expenditures	**$ 602**	$ 852	$ 1,436

(in millions)	At December 31, 2020	2019	2018
Long-lived assets:			
European Union	**$ 4,500**	$ 4,275	$ 4,216
Eastern Europe	**668**	774	547
Middle East & Africa	**375**	369	362
South & Southeast Asia	**1,348**	1,361	1,297
East Asia & Australia	**807**	829	781
Latin America & Canada	**433**	478	779
Total long-lived assets	**8,131**	8,086	7,982
Other	**1,001**	516	664
Total property, plant and equipment, net and Other assets	**$ 9,132**	$ 8,602	$ 8,646

Long-lived assets consist of non-current assets other than goodwill; other intangible assets, net; deferred tax assets, equity investments, and financial instruments. PMI's largest markets in terms of long-lived assets are Switzerland, Italy and Indonesia. Total long-lived assets located in Switzerland, which is reflected in the European Union segment above, were $1.3 billion, $1.1 billion and $1.0 billion at December 31, 2020, 2019 and 2018, respectively. Total long-lived assets located in Italy, which is reflected in the European Union segment above, were $1.1 billion, $1.1 billion and $1.1 billion at December 31, 2020, 2019 and 2018, respectively. Total long-lived assets located in Indonesia, which is reflected in the South & Southeast Asia segment above, were $0.7 billion, $0.8 billion and $0.7 billion at December 31, 2020, 2019 and 2018, respectively.

Note 13.

Benefit Plans:

Pension coverage for employees of PMI's subsidiaries is provided, to the extent deemed appropriate, through separate plans, many of which are governed by local statutory requirements. In addition, PMI provides health care and other benefits to substantially all U.S. retired employees and certain non-U.S. retired employees. In general, health care benefits for non-U.S. retired employees are covered through local government plans.

Pension and other employee benefit costs per the consolidated statements of earnings consisted of the following for December 31, 2020, 2019 and 2018:

(in millions)	2020	2019	2018
Net pension costs (income)	**$ (14)**	$ (18)	$ (51)
Net postemployment costs	**103**	100	80
Net postretirement costs	**8**	7	12
Total pension and other employee benefit costs	**$ 97**	$ 89	$ 41

Pension and Postretirement Benefit Plans

Obligations and Funded Status

The postretirement health care plans are not funded. The projected benefit obligations, plan assets and funded status of PMI's pension plans, and the accumulated benefit obligation and net amount accrued for PMI's postretirement health care plans, at December 31, 2020 and 2019, were as follows:

(in millions)	Pension[1]		Postretirement	
	2020	2019	2020	2019
Benefit obligation at January 1	**$ 10,612**	$ 9,152	**$ 190**	$ 209
Service cost	**268**	214	**2**	2
Interest cost	**68**	118	**6**	7
Benefits paid[2]	**(356)**	(333)	**(7)**	(8)
Employee contributions[2]	**130**	127	**—**	—
Settlement, curtailment and plan amendment	**(117)**	50		
Actuarial losses (gains)	**653**	1,430	**5**	27
Currency	**992**	29	**3**	—
Deconsolidation of RBH	**—**	(166)	**—**	(42)
Other[2]	**(7)**	(9)	**(1)**	(5)
Benefit obligation at December 31,	**12,243**	10,612	**198**	190
Fair value of plan assets at January 1,	**7,928**	6,888		
Actual return on plan assets	**206**	1,211		
Employer contributions	**102**	200		
Employee contributions[2]	**130**	127		
Benefits paid[2]	**(356)**	(333)		
Settlement	**(16)**	—		
Currency	**752**	7		
Deconsolidation of RBH	**—**	(172)		
Fair value of plan assets at December 31,	**8,746**	7,928		
Net pension and postretirement liability recognized at December 31,	**$ (3,497)**	$ (2,684)	**$ (198)**	$ (190)

(1) Primarily non-U.S. based defined benefit retirement plans.
(2) Certain prior years' amounts pertaining to PMI's pension plans have been reclassified in the table above to conform with the current year's presentation.

For the years ended December 31, 2020 and 2019, actuarial losses (gains) consisted primarily of losses for assumption changes related to lower discount rates year-over-year for Swiss, German and Dutch plans.

At December 31, 2020 and 2019, the Swiss pension plan represented 63% and 62% of the benefit obligation, respectively, and approximately 59% and 59% of the fair value of plan assets at December 31, 2020 and 2019, respectively. At December 31, 2020 and 2019, the U.S. pension plan represented 4% and 4% of the benefit obligation, respectively, and approximately 4% and 4% of the fair value of plan assets at December 31, 2020 and 2019, respectively.

At December 31, 2020 and 2019, the amounts recognized on PMI's consolidated balance sheets for the pension and postretirement plans were as follows:

	Pension		Postretirement	
(in millions)	**2020**	**2019**	**2020**	**2019**
Other assets	**$ 43**	$ 43		
Accrued liabilities — employment costs	**(26)**	(23)	**$ (8)**	$ (8)
Long-term employment costs	**(3,514)**	(2,704)	**(190)**	(182)
	$ (3,497)	$ (2,684)	**$ (198)**	$ (190)

The accumulated benefit obligation, which represents benefits earned to date, for the pension plans was $11.5 billion and $10.0 billion at December 31, 2020 and 2019, respectively.

For pension plans with accumulated benefit obligations in excess of plan assets, the accumulated benefit obligation and fair value of plan assets were $10.5 billion and $7.7 billion, respectively, as of December 31, 2020. The accumulated benefit obligation and fair value of plan assets were $9.0 billion and $6.8 billion, respectively, as of December 31, 2019.

For pension plans with projected benefit obligations in excess of plan assets, the projected benefit obligation and fair value of plan assets were $12.1 billion and $8.6 billion, respectively, as of December 31, 2020. The projected benefit obligation and fair value of plan assets were $10.4 billion and $7.7 billion, respectively, as of December 31, 2019.

The following weighted-average assumptions were used to determine PMI’s pension and postretirement benefit obligations at December 31:

	Pension		Postretirement	
	2020	**2019**	**2020**	**2019**
Discount rate	**0.56 %**	0.83 %	**2.84 %**	3.28 %
Rate of compensation increase	**1.79**	1.82		
Interest crediting rate	**3.20**	3.20		
Health care cost trend rate assumed for next year			**6.21**	6.21
Ultimate trend rate			**4.73**	5.09
Year that rate reaches the ultimate trend rate			**2029**	2023

The discount rate for the largest pension plans is based on a yield curve constructed from a portfolio of high quality corporate bonds that produces a cash flow pattern equivalent to each plan’s expected benefit payments. The discount rate for the remaining plans is developed from local bond indices that match local benefit obligations as closely as possible.

Components of Net Periodic Benefit Cost

Net periodic pension and postretirement health care costs consisted of the following for the years ended December 31, 2020, 2019 and 2018:

(in millions)	Pension			Postretirement		
	2020	**2019**	**2018**	**2020**	**2019**	**2018**
Service cost	**$ 268**	$ 214	$ 210	**$ 2**	$ 2	$ 4
Interest cost	**68**	118	109	**6**	7	9
Expected return on plan assets	**(353)**	(328)	(349)	**—**	—	—
Amortization:						
Net losses	**265**	189	172	**2**	—	4
Prior service cost	**1**	(1)	2	**—**	—	(1)
Net transition obligation	**1**	—	—	**—**	—	—
Settlement and curtailment	**4**	4	15	**—**	—	—
Net periodic pension and postretirement costs	**$ 254**	$ 196	$ 159	**$ 10**	$ 9	$ 16

Settlement and curtailment charges were due primarily to employee severance and early retirement programs.

The following weighted-average assumptions were used to determine PMI's net pension and postretirement health care costs:

	Pension			Postretirement		
	2020	**2019**	**2018**	**2020**	**2019**	**2018**
Discount rate - service cost	**1.25 %**	2.14 %	1.92 %	**3.28 %**	3.97 %	3.79 %
Discount rate - interest cost	**0.67**	1.35	1.25	**3.28**	3.97	3.79
Expected rate of return on plan assets	**4.59**	4.70	4.76			
Rate of compensation increase	**1.82**	1.86	1.65			
Interest crediting rate	**3.20**	3.40	3.40			
Health care cost trend rate				**6.21**	6.17	6.17

PMI's expected rate of return on pension plan assets is determined by the plan assets' historical long-term investment performance, current asset allocation and estimates of future long-term returns by asset class.

PMI and certain of its subsidiaries sponsor defined contribution plans. Amounts charged to expense for defined contribution plans totaled $66 million, $63 million and $66 million for the years ended December 31, 2020, 2019 and 2018, respectively.

Plan Assets

PMI's investment strategy for pension plans is based on an expectation that equity securities will outperform debt securities over the long term. Accordingly, the target allocation of PMI's plan assets is broadly characterized as approximately 60% in equity securities and approximately 40% in debt securities and other assets. The strategy primarily utilizes indexed U.S. equity securities, international equity securities and investment-grade debt securities. PMI's plans have no investments in hedge funds, private equity or derivatives. PMI attempts to mitigate investment risk by rebalancing between equity and debt asset classes once a year or as PMI's contributions and benefit payments are made.

The fair value of PMI's pension plan assets at December 31, 2020 and 2019, by asset category was as follows:

Asset Category (in millions)	At December 31, 2020	Quoted Prices In Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$ 324	$ 324		
Equity securities:				
U.S. securities	175	175		
International securities	605	605		
Investment funds[(a)]	6,811	5,206	$ 1,605	
International government bonds	225	149	76	
Corporate bonds	292	292		
Other	7	7		
Total assets in the fair value hierarchy	$ 8,439	$ 6,758	$ 1,681	$ —
Investment funds measured at net asset value[(b)]	307			
Total assets	$ 8,746			

[(a)] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and JP Morgan EMBI for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 63% are invested in U.S. and international equities; 16% are invested in U.S. and international government bonds; 12% are invested in real estate, and 9% are invested in corporate bonds.

[(b)] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Asset Category (in millions)	At December 31, 2019	Quoted Prices In Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$ 276	$ 276		
Equity securities:				
U.S. securities	170	170		
International securities	563	563		
Investment funds[(a)]	6,125	4,625	$ 1,500	
International government bonds	197	137	60	
Corporate bonds	282	282		
Other	6	6		
Total assets in the fair value hierarchy	$ 7,619	$ 6,059	$ 1,560	$ —
Investment funds measured at net asset value[(b)]	309			
Total assets	$ 7,928			

[(a)] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and Barclays Capital U.S. for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 63% were invested in U.S. and international equities; 16% were invested in U.S. and international government bonds; 12% were invested in real estate and other money markets, and 9% were invested in corporate bonds.

[(b)] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

For a description of the fair value hierarchy and the three levels of inputs used to measure fair values, see Note 2. *Summary of Significant Accounting Policies*.

PMI makes, and plans to make, contributions to the extent that they are tax deductible and to meet specific funding requirements of its funded pension plans. Currently, PMI anticipates making contributions of approximately $262 million in 2021 to its pension plans, based on current tax and benefit laws. However, this estimate is subject to change as a result of changes in tax and other benefit laws, as well as asset performance significantly above or below the assumed long-term rate of return on pension assets, or changes in interest and currency rates.

The estimated future benefit payments from PMI pension plans at December 31, 2020, are as follows:

(in millions)	
2021	$ 401
2022	383
2023	387
2024	390
2025	399
2026 - 2030	2,226

PMI's expected future annual benefit payments for its postretirement health care plans are estimated to be not material through 2030.

Postemployment Benefit Plans

PMI and certain of its subsidiaries sponsor postemployment benefit plans covering substantially all salaried and certain hourly employees. The cost of these plans is charged to expense over the working life of the covered employees. Net postemployment costs were $208 million, $171 million and $158 million for the years ended December 31, 2020, 2019 and 2018, respectively.

The amounts recognized in accrued postemployment costs net of plan assets on PMI's consolidated balance sheets at December 31, 2020 and 2019, were $923 million and $751 million, respectively. The change in the liability is primarily due to actuarial losses of $142 million in 2020 resulting from increased employee severance payout primarily in countries in the European Union and Latin America & Canada segments, coupled with the periodic expense, partially offset by cash payments.

The accrued postemployment costs were determined using a weighted-average discount rate of 3.0% and 3.0% in 2020 and 2019, respectively; an assumed ultimate annual weighted-average turnover rate of 3.0% and 3.0% in 2020 and 2019, respectively; assumed compensation cost increases of 2.1% in 2020 and 2.6% in 2019, and assumed benefits as defined in the respective plans. In accordance with local regulations, certain postemployment plans are funded. As a result, the accrued postemployment costs disclosed above are presented net of the related assets of $46 million and $40 million at December 31, 2020 and 2019, respectively. Postemployment costs arising from actions that offer employees benefits in excess of those specified in the respective plans are charged to expense when incurred.

Comprehensive Earnings (Losses)

The amounts recorded in accumulated other comprehensive losses at December 31, 2020, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (4,147)	$ (64)	$ (839)	$ (5,050)
Prior service cost	22	2	(22)	2
Net transition obligation	(3)	—	—	(3)
Deferred income taxes	570	24	204	798
Losses to be amortized	$ (3,558)	$ (38)	$ (657)	$ (4,253)

The amounts recorded in accumulated other comprehensive losses at December 31, 2019, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (3,718)	$ (63)	$ (775)	$ (4,556)
Prior service cost	3	2	—	5
Net transition obligation	(4)	—	—	(4)
Deferred income taxes	520	24	182	726
Losses to be amortized	$ (3,199)	$ (37)	$ (593)	$ (3,829)

The amounts recorded in accumulated other comprehensive losses at December 31, 2018, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (3,438)	$ (41)	$ (702)	$ (4,181)
Prior service cost	(27)	3	—	(24)
Net transition obligation	(4)	—	—	(4)
Deferred income taxes	379	20	164	563
Losses to be amortized	$ (3,090)	$ (18)	$ (538)	$ (3,646)

The movements in other comprehensive earnings (losses) during the year ended December 31, 2020, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings:				
Amortization:				
Net losses	**$ 250**	**$ 3**	**$ 78**	**$ 331**
Prior service cost	**29**	**—**	**—**	**29**
Net transition obligation	**1**	**—**	**—**	**1**
Other income/expense:				
Net losses	**3**	**—**	**—**	**3**
Prior service cost	**2**	**—**	**—**	**2**
Deferred income taxes	**(49)**	**(1)**	**(17)**	**(67)**
	236	**2**	**61**	**299**
Other movements during the year:				
Net losses	**(682)**	**(4)**	**(142)**	**(828)**
Prior service cost	**(12)**	**—**	**(22)**	**(34)**
Deferred income taxes	**99**	**1**	**39**	**139**
	(595)	**(3)**	**(125)**	**(723)**
Total movements in other comprehensive earnings (losses)	**$ (359)**	**$ (1)**	**$ (64)**	**$ (424)**

The movements in other comprehensive earnings (losses) during the year ended December 31, 2019, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings:				
Amortization:				
Net losses	$ 198	$ 3	$ 77	$ 278
Prior service cost	32	(1)	—	31
Other income/expense:				
Net losses	3	—	—	3
Deferred income taxes	(51)	(1)	(17)	(69)
	182	1	60	243
Other movements during the year:				
Net losses	(521)	(27)	(150)	(698)
Prior service cost	(2)	—	—	(2)
Deconsolidation of RBH (net of deferred income taxes)	26	1	—	27
Deferred income taxes	206	6	35	247
	(291)	(20)	(115)	(426)
Total movements in other comprehensive earnings (losses)	$ (109)	$ (19)	$ (55)	$ (183)

The movements in other comprehensive earnings (losses) during the year ended December 31, 2018, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings:				
Amortization:				
Net losses	$ 180	$ 5	$ 62	$ 247
Prior service cost	—	(1)	—	(1)
Net transition obligation	1	—	—	1
Other income/expense:				
Net losses	14	—	—	14
Deferred income taxes	(28)	(1)	(14)	(43)
	167	3	48	218
Other movements during the year:				
Net losses	(1,008)	34	(147)	(1,121)
Prior service cost	8	—	—	8
Deferred income taxes	80	(7)	(8)	65
	(920)	27	(155)	(1,048)
Total movements in other comprehensive earnings (losses)	$ (753)	$ 30	$ (107)	$ (830)

Note 14.

Additional Information:

(in millions)	For the Years Ended Decemb		
	2020	2019	
Research and development expense	**$ 495**	$ 465	$
Advertising expense	**$ 637**	$ 730	$
Foreign currency net transaction (gains)/losses	**$ 90**	$ (95)	$
Interest expense	**$ 728**	$ 796	$
Interest income	**(110)**	(226)	
Interest expense, net	**$ 618**	$ 570	$
Total lease cost	**$ 317** [1]	$ 332 [1]	$

[1] For additional information on total lease costs, see Note 21. *Leases.*

Note 15.

Financial Instruments:

Overview

PMI operates in markets outside of the United States of America, with manufacturing and sales facilities in various locations around the world. PMI utilizes certain financial instruments to manage foreign currency and interest rate exposure. Derivative financial instruments are used by PMI principally to reduce exposures to market risks resulting from fluctuations in foreign currency exchange and interest rates by creating offsetting exposures. PMI is not a party to leveraged derivatives and, by policy, does not use derivative financial instruments for speculative purposes. Substantially all of PMI's derivative financial instruments are subject to master netting arrangements, whereby the right to offset occurs in the event of default by a participating party. While these contracts contain the enforceable right to offset through close-out netting rights, PMI elects to present them on a gross basis in the consolidated balance sheets. Collateral associated with these arrangements is in the form of cash and is unrestricted. Financial instruments qualifying for hedge accounting must maintain a specified level of effectiveness between the hedging instrument and the item being hedged, both at inception and throughout the hedged period. PMI formally documents the nature and relationships between the hedging instruments and hedged items, as well as its risk-management objectives, strategies for undertaking the various hedge transactions and method of assessing hedge effectiveness. Additionally, for hedges of forecasted transactions, the significant characteristics and expected terms of the forecasted transaction must be specifically identified, and it must be probable that each forecasted transaction will occur. If it were deemed probable that the forecasted transaction would not occur, the gain or loss would be recognized in earnings.

PMI uses deliverable and non-deliverable forward foreign exchange contracts, foreign currency swaps and foreign currency options, collectively referred to as foreign exchange contracts ("foreign exchange contracts"), and interest rate contracts to mitigate its exposure to changes in exchange and interest rates from third-party and intercompany actual and forecasted transactions. Both foreign exchange contracts and interest rate contracts are collectively referred to as derivative contracts ("derivative contracts"). The primary currencies to which PMI is exposed include the Euro, Indonesian rupiah, Japanese yen, Mexican peso, Philippine peso, Russian ruble and Swiss franc. At December 31, 2020 and 2019, PMI had contracts with aggregate notional amounts of $26.5 billion and $24.1 billion, respectively. Of the $26.5 billion aggregate notional amount at December 31, 2020, $5.0 billion related to cash flow

hedges, $8.9 billion related to hedges of net investments in foreign operations and $12.6 billion related to other derivatives that primarily offset currency exposures on intercompany financing. Of the $24.1 billion aggregate notional amount at December 31, 2019, $2.8 billion related to cash flow hedges, $9.9 billion related to hedges of net investments in foreign operations and $11.4 billion related to other derivatives that primarily offset currency exposures on intercompany financing.

The fair value of PMI's derivative contracts included in the consolidated balance sheets as of December 31, 2020 and 2019, were as follows:

	Derivative Assets			Derivative Liabilities		
		Fair Value			Fair Value	
(in millions)	Balance Sheet Classification	2020	2019	Balance Sheet Classification	2020	2019
Derivative contracts designated as hedging instruments	Other current assets	**$ 130**	$ 319	Other accrued liabilities	**$ 241**	$ 23
	Other assets	**6**	21	Income taxes and other liabilities	**605**	301
Derivative contracts not designated as hedging instruments	Other current assets	**46**	50	Other accrued liabilities	**207**	70
	Other assets	**—**	—	Income taxes and other liabilities	**57**	25
Total gross amount derivatives contracts presented in the consolidated balance sheets		**$ 182**	$ 390		**$ 1,110**	$ 419
Gross amounts not offset in the consolidated balance sheets						
Financial instruments		**(156)**	(297)		**(156)**	(297)
Cash collateral received/ pledged		**(23)**	(91)		**(892)**	(59)
Net amount		**$ 3**	$ 2		**$ 62**	$ 63

PMI assesses the fair value of its foreign exchange contracts and interest rate contracts using standard valuation models that use, as their basis, readily observable market inputs. The fair value of PMI's foreign exchange forward contracts, foreign currency swaps and interest rate contracts is determined by using the prevailing foreign exchange spot rates and interest rate differentials, and the respective maturity dates of the instruments. The fair value of PMI's currency options is determined by using a Black-Scholes methodology based on foreign exchange spot rates and interest rate differentials, currency volatilities and maturity dates. PMI's derivative contracts have been classified within Level 2 at December 31, 2020 and 2019.

For the years ended December 31, 2020, 2019 and 2018, PMI's derivative contracts impacted the consolidated statements of earnings and comprehensive earnings as follows:

(pre-tax, in millions)	For the Years Ended December 31,											
	Amount of Gain/ (Loss) Recognized in Other Comprehensive Earnings/(Losses) on Derivatives			Statement of Earnings Classification of Gain/(Loss) on Derivatives	Amount of Gain/ (Loss) Reclassified from Other Comprehensive Earnings/(Losses) into Earnings			Amount of Gain/ (Loss) Recognized in Earnings		
	2020	**2019**	**2018**		**2020**	**2019**	**2018**	**2020**	**2019**	**2018**
Derivative contracts designated as hedging instruments:										
Cash flow hedges	**$ (81)**	$ (20)	$ 28							
				Net revenues	**$ (3)**	$ 22	$ 18			
				Cost of sales	**7**	1	—			
				Marketing, administration and research costs	**27**	2	6			
				Interest expense, net	**(11)**	(8)	(1)			
Net investment hedges [a]	**(514)**	369	324	Interest expense, net [b]				**$ 194**	$ 230	$ 260
Derivative contracts not designated as hedging instruments				Interest expense, net				**71**	94	62
				Marketing, administration and research costs [c]				**(368)**	(115)	378
Total	**$ (595)**	$ 349	$ 352		**$ 20**	$ 17	$ 23	**$ (103)**	$ 209	$ 700

[a] Amount of gains (losses) on hedges of net investments principally related to changes in exchange and interest rates between the Euro and U.S. dollar

[b] Represent the gains for amounts excluded from the effectiveness testing

[c] The gains (losses) from these contracts attributable to changes in foreign currency exchange rates substantially offset the (losses) and gains generated by the underlying intercompany and third-party loans being hedged

Cash Flow Hedges

PMI has entered into derivative contracts to hedge the foreign currency exchange and interest rate risks related to certain forecasted transactions. Gains and losses associated with qualifying cash flow hedge contracts are deferred as components of accumulated other comprehensive losses until the underlying hedged transactions are reported in PMI's consolidated statements of earnings. As of December 31, 2020, PMI has hedged forecasted transactions for periods not exceeding the next eighteen months, with the exception of one derivative contract that expires in May 2024. The impact of these hedges is primarily included in operating cash flows on PMI's consolidated statements of cash flows.

Hedges of Net Investments in Foreign Operations

PMI designates derivative contracts and certain foreign currency denominated debt instruments as net investment hedges, primarily of its Euro net assets. The amount of pre-tax gain/(loss) related to these debt instruments, that was reported as a component of accumulated other comprehensive losses within currency translation adjustment, was $ (465) million, $234 million and $349 million, for the years ended December 31, 2020, 2019 and 2018, respectively. The premiums paid for, and settlements of, net investment hedges are included in investing cash flows on PMI's consolidated statements of cash flows.

Other Derivatives

PMI has entered into derivative contracts to hedge the foreign currency exchange and interest rate risks related to intercompany loans between certain subsidiaries, and third-party loans. While effective as economic hedges, no hedge accounting is applied for these contracts; therefore, the gains (losses) relating to these contracts are reported in PMI's consolidated statements of earnings.

Qualifying Hedging Activities Reported in Accumulated Other Comprehensive Losses

Derivative gains or losses reported in accumulated other comprehensive losses are a result of qualifying hedging activity. Transfers of these gains or losses to earnings are offset by the corresponding gains or losses on the underlying hedged item. Hedging activity affected accumulated other comprehensive losses, net of income taxes, as follows:

	For the Years Ended December 31,	
(in millions)	**2020**	**2019**
Gain as of January 1,	**$ 3**	$ 35
Derivative (gains)/ losses transferred to earnings	**(20)**	(14)
Change in fair value	**(68)**	(18)
Gain/(loss) as of December 31,	**$ (85)**	$ 3

At December 31, 2020, PMI expects $(49) million of derivative losses that are included in accumulated other comprehensive losses to be reclassified to the consolidated statement of earnings within the next 12 months. These losses are expected to be substantially offset by the statement of earnings impact of the respective hedged transactions.

Contingent Features

PMI's derivative instruments do not contain contingent features.

Credit Exposure and Credit Risk

PMI is exposed to credit loss in the event of non-performance by counterparties. While PMI does not anticipate non-performance, its risk is limited to the fair value of the financial instruments less any cash collateral received or pledged. PMI actively monitors its exposure to credit risk through the use of credit approvals and credit limits and by selecting and continuously monitoring a diverse group of major international banks and financial institutions as counterparties.

Note 16.

Accumulated Other Comprehensive Losses:

PMI's accumulated other comprehensive losses, net of taxes, consisted of the following:

(Losses) Earnings **(in millions)**	**At December 31,**		
	2020	**2019**	**2018**
Currency translation adjustments	**$ (6,843)**	$ (5,537)	$ (6,500)
Pension and other benefits	**(4,253)**	(3,829)	(3,646)
Derivatives accounted for as hedges	**(85)**	3	35
Total accumulated other comprehensive losses	**$ (11,181)**	$ (9,363)	$ (10,111)

Reclassifications from Other Comprehensive Earnings

The movements in accumulated other comprehensive losses and the related tax impact, for each of the components above, that are due to current period activity and reclassifications to the income statement, including those related to the deconsolidation of RBH, are shown on the consolidated statements of comprehensive earnings for the years ended December 31, 2020, 2019, and 2018. For additional information, see Note 13. *Benefit Plans* for disclosures related to PMI's pension and other benefits, Note 15. *Financial Instruments* for disclosures related to derivative financial instruments and Note 20. *Deconsolidation of RBH* for disclosures related to the deconsolidation of RBH.

Note 17.

Contingencies:

Tobacco-Related Litigation

Legal proceedings covering a wide range of matters are pending or threatened against us, and/or our subsidiaries, and/or our indemnitees in various jurisdictions. Our indemnitees include distributors, licensees, and others that have been named as parties in certain cases and that we have agreed to defend, as well as to pay costs and some or all of judgments, if any, that may be entered against them. Pursuant to the terms of the Distribution Agreement between Altria Group, Inc. ("Altria") and PMI, PMI will indemnify Altria and Philip Morris USA Inc. ("PM USA"), a U.S. tobacco subsidiary of Altria, for tobacco product claims based in substantial part on products manufactured by PMI or contract manufactured for PMI by PM USA, and PM USA will indemnify PMI for tobacco product claims based in substantial part on products manufactured by PM USA, excluding tobacco products contract manufactured for PMI.

It is possible that there could be adverse developments in pending cases against us and our subsidiaries. An unfavorable outcome or settlement of pending tobacco-related litigation could encourage the commencement of additional litigation.

Damages claimed in some of the tobacco-related litigation are significant and, in certain cases in Brazil, Canada and Nigeria, range into the billions of U.S. dollars. The variability in pleadings in multiple jurisdictions, together with the actual experience of management in litigating claims, demonstrate that the monetary relief that may be specified in a lawsuit bears little relevance to the ultimate outcome. Much of the tobacco-related litigation is in its early stages, and litigation is subject to uncertainty. However, as discussed below, we have to date been largely successful in defending tobacco-related litigation.

We and our subsidiaries record provisions in the consolidated financial statements for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. At the

present time, except as stated otherwise in this Note 17. *Contingencies,* while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available to it (i) management has not concluded that it is probable that a loss has been incurred in any of the pending tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any. Legal defense costs are expensed as incurred.

It is possible that our consolidated results of operations, cash flows or financial position could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. Nevertheless, although litigation is subject to uncertainty, we and each of our subsidiaries named as a defendant believe, and each has been so advised by counsel handling the respective cases, that we have valid defenses to the litigation pending against us, as well as valid bases for appeal of adverse verdicts. All such cases are, and will continue to be, vigorously defended. However, we and our subsidiaries may enter into settlement discussions in particular cases if we believe it is in our best interests to do so.

CCAA Proceedings and Stay of Tobacco-Related Cases Pending in Canada

As a result of the Court of Appeal of Quebec's decision in both the *Létourneau* and *Blais* cases described below, our subsidiary, Rothmans, Benson & Hedges Inc. ("RBH"), and the other defendants, JTI Macdonald Corp., and Imperial Tobacco Canada Limited, sought protection in the Ontario Superior Court of Justice under the Companies' Creditors Arrangement Act ("CCAA") on March 22, March 8, and March 12, 2019 respectively. CCAA is a Canadian federal law that permits a Canadian business to restructure its affairs while carrying on its business in the ordinary course. The initial CCAA order made by the Ontario Superior Court on March 22, 2019 authorizes RBH to pay all expenses incurred in carrying on its business in the ordinary course after the CCAA filing, including obligations to employees, vendors, and suppliers. As further described in Note 20. *Deconsolidation of RBH*, RBH is now deconsolidated from our consolidated financial statements. As part of the CCAA proceedings, there is currently a comprehensive stay up to and including March 31, 2021 of all tobacco-related litigation pending in Canada against RBH and the other defendants, including PMI and our indemnitees (PM USA and Altria), namely, the smoking and health class actions filed in various Canadian provinces and health care cost recovery actions. These proceedings are presented below under the caption "*Stayed Litigation — Canada*." Ernst & Young Inc. has been appointed as monitor of RBH in the CCAA proceedings. In accordance with the CCAA process, as the parties work towards a plan of arrangement or compromise in a confidential mediation, it is anticipated that the court will set additional hearings and further extend the stay of proceedings. On April 17, 2019, the Ontario Superior Court ruled that RBH and the other defendants will not be allowed to file an application to the Supreme Court of Canada for leave to appeal the Court of Appeal's decision in the *Létourneau* and the *Blais* cases so long as the comprehensive stay of all tobacco-related litigation in Canada remains in effect and that the time period to file the application would be extended by the stay period. While RBH believes that the findings of liability and damages in both *Létourneau* and the *Blais* cases were incorrect, the CCAA proceedings will provide a forum for RBH to seek resolution through a plan of arrangement or compromise of all tobacco-related litigation pending in Canada. It is not possible to predict the resolution of the underlying legal proceedings or the length of the CCAA process.

Stayed Litigation — Canada

Smoking and Health Litigation — Canada

In the first class action pending in Canada, *Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI-Macdonald Corp., Quebec Superior Court, Canada*, filed in November 1998, RBH and other Canadian manufacturers (Imperial Tobacco Canada Ltd. and JTI-Macdonald Corp.) are defendants. The plaintiffs, an anti-smoking organization and an individual smoker, sought compensatory and punitive damages for each member of the class who allegedly suffers from certain smoking-related diseases. The class was certified in 2005. The trial court issued its judgment on May 27, 2015. The trial court found RBH and two other Canadian manufacturers liable and found that the class members' compensatory damages totaled approximately CAD 15.5 billion, including pre-judgment interest (approximately $12.1 billion). The trial court awarded compensatory damages on a joint and several liability basis, allocating 20% to our subsidiary (approximately CAD 3.1 billion, including pre-judgment interest (approximately $2.4 billion)). In addition, the trial court awarded CAD 90,000 (approximately $70,250) in punitive damages, allocating CAD 30,000 (approximately $23,400) to RBH. The trial court estimated the disease class at 99,957 members. RBH appealed to the Court of Appeal of Quebec. In October 2015, the Court of Appeal ordered RBH to furnish security totaling CAD 226 million (approximately $176.4 million) to cover both the *Létourneau* and *Blais* cases, which RBH has paid in installments through March 2017. The Court of Appeal ordered Imperial Tobacco Canada Ltd. to furnish security totaling CAD 758 million (approximately $592 million) in installments through June 2017. JTI Macdonald Corp. was not required to furnish security in accordance with plaintiffs' motion. The Court of Appeal ordered that the security is payable upon a final judgment of the Court of Appeal affirming the trial court's judgment or upon further order of the Court of Appeal. On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's findings of liability and the compensatory and punitive damages award while reducing the total amount of compensatory damages to approximately CAD 13.5 billion including interest (approximately $10.5 billion) due to the trial court's error in the calculation of interest. The compensatory damages award is on a joint and several basis with an allocation of 20% to RBH (approximately CAD 2.7 billion, including pre-judgment interest (approximately $2.11 billion)). The Court of Appeal upheld the trial court's findings that defendants violated the Civil Code of Quebec, the Quebec Charter of Human Rights and Freedoms, and the Quebec Consumer Protection Act by failing to warn adequately of the dangers of smoking and by conspiring to prevent consumers from learning of the dangers of smoking. The Court of Appeal further held that the plaintiffs either need not prove, or had adequately proven, that these faults were a cause of the class members' injuries. In accordance with the judgment, defendants are required to deposit their respective portions of the damages awarded in both the *Létourneau* case described below and the *Blais* case, approximately CAD 1.1 billion (approximately $859 million), into trust accounts within 60 days. RBH's share of the deposit is approximately CAD 257 million (approximately $194 million). PMI recorded a pre-tax charge of $194 million in its consolidated results, representing $142 million net of tax, as tobacco litigation-related expense, in the first quarter of 2019. The charge reflects PMI's assessment of the portion of the judgment that represents probable and estimable loss prior to the deconsolidation of RBH and corresponds to the trust account deposit required by the judgment.

In the second class action pending in Canada, *Cecilia Létourneau v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI-Macdonald Corp., Quebec Superior Court, Canada,* filed in September 1998, RBH and other Canadian manufacturers (Imperial Tobacco Canada Ltd. and JTI-Macdonald Corp.) are defendants. The plaintiff, an individual smoker, sought compensatory and punitive damages for each member of the class who is deemed addicted to smoking. The class was certified in 2005. The trial court issued its judgment on May 27, 2015. The trial court found RBH and two other Canadian manufacturers liable and awarded a total of CAD 131 million (approximately $102.3 million) in punitive damages, allocating CAD 46 million (approximately $36 million) to RBH. The trial court estimated the size of the addiction class at 918,000 members but declined to award compensatory damages to the addiction class because the evidence did not establish the claims with sufficient accuracy. The trial court found that a claims process to allocate the awarded punitive damages to individual class members would be too expensive and difficult to administer. On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's findings of liability and the total amount of punitive damages awarded allocating CAD 57 million including interest (approximately $44.5 million) to RBH. See the *Blais* description above and Note 20. *Deconsolidation of RBH* below for further detail concerning the security order pertaining to both *Létourneau* and *Blais* cases and the impact of the decision on PMI's financial statements.

RBH and PMI believe the findings of liability and damages in both *Létourneau* and the *Blais* cases were incorrect and in contravention of applicable law on several grounds including the following: (i) defendants had no obligation to warn class members who knew, or should have known, of the risks of smoking; (ii) defendants cannot be liable to class members who would have smoked regardless of what warnings were given; and (iii) defendants cannot be liable to all class members given the individual differences between class members.

In the third class action pending in Canada, *Kunta v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Winnipeg, Canada*, filed June 12, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic obstructive pulmonary disease ("COPD"), severe asthma, and mild reversible lung disease resulting from the use of tobacco products. She is seeking compensatory

and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products.

In the fourth class action pending in Canada, *Adams v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Saskatchewan, Canada*, filed July 10, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, emphysema, heart disease, or cancer, as well as restitution of profits.

In the fifth class action pending in Canada, *Semple v. Canadian Tobacco Manufacturers' Council, et al., The Supreme Court (trial court), Nova Scotia, Canada*, filed June 18, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and COPD resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products.

In the sixth class action pending in Canada, *Dorion v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Alberta, Canada,* filed June 15, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic bronchitis and severe sinus infections resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products. To date, we, our subsidiaries, and our indemnitees have not been properly served with the complaint.

In the seventh class action pending in Canada, *McDermid v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and heart disease resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from heart disease allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed.

In the eighth class action pending in Canada, *Bourassa v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, the heir to a deceased smoker, alleges that the decedent was addicted to tobacco products and suffered from emphysema resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from chronic respiratory diseases allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed. In December 2014, plaintiff filed an amended statement of claim.

In the ninth class action pending in Canada, *Suzanne Jacklin v. Canadian Tobacco Manufacturers' Council, et al., Ontario Superior Court of Justice,* filed June 20, 2012, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, heart disease, or cancer, as well as restitution of profits.

Health Care Cost Recovery Litigation — Canada

In the first health care cost recovery case pending in Canada, *Her Majesty the Queen in Right of British Columbia v. Imperial Tobacco Limited, et al., Supreme Court, British Columbia, Vancouver Registry, Canada,* filed January 24, 2001, we, RBH, our indemnitee (PM USA), and other members of the industry are defendants. The plaintiff, the

government of the province of British Columbia, brought a claim based upon legislation enacted by the province authorizing the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, resulting from a "tobacco related wrong."

In the second health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of New Brunswick v. Rothmans Inc., et al., Court of Queen's Bench of New Brunswick, Trial Court, New Brunswick, Fredericton, Canada,* filed March 13, 2008, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of New Brunswick based on legislation enacted in the province. This legislation is similar to the law introduced in British Columbia that authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the third health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of Ontario v. Rothmans Inc., et al., Ontario Superior Court of Justice, Toronto, Canada*, filed September 29, 2009, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Ontario based on legislation enacted in the province. This legislation is similar to the laws introduced in British Columbia and New Brunswick that authorize the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the fourth health care cost recovery case filed in Canada, *Attorney General of Newfoundland and Labrador v. Rothmans Inc., et al., Supreme Court of Newfoundland and Labrador, St. Johns, Canada*, filed February 8, 2011, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Newfoundland and Labrador based on legislation enacted in the province that is similar to the laws introduced in British Columbia, New Brunswick and Ontario. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the fifth health care cost recovery case filed in Canada, *Attorney General of Quebec v. Imperial Tobacco Limited, et al., Superior Court of Quebec, Canada*, filed June 8, 2012, we, RBH, our indemnitee (PM USA), and other members of the industry are defendants. The claim was filed by the government of the province of Quebec based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the sixth health care cost recovery case filed in Canada, *Her Majesty in Right of Alberta v. Altria Group, Inc., et al., Supreme Court of Queen's Bench Alberta, Canada*, filed June 8, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Alberta based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the seventh health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Manitoba v. Rothmans, Benson & Hedges, Inc., et al., The Queen's Bench, Winnipeg Judicial Centre, Canada*, filed May 31, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Manitoba based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the eighth health care cost recovery case filed in Canada, *The Government of Saskatchewan v. Rothmans, Benson & Hedges Inc., et al., Queen's Bench, Judicial Centre of Saskatchewan, Canada*, filed June 8, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Saskatchewan based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the ninth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Prince Edward Island v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Prince Edward Island (General Section), Canada*, filed September 10, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Prince Edward Island based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the tenth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Nova Scotia v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Nova Scotia, Canada*, filed January 2, 2015, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed

by the government of the province of Nova Scotia based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

The table below lists the number of tobacco-related cases pertaining to combustible products pending against us and/or our subsidiaries or indemnitees as of February 5, 2021, February 3, 2020 and February 4, 2019:[1]

Type of Case	Number of Cases Pending as of February 5, 2021	Number of Cases Pending as of February 3, 2020	Number of Cases Pending as of February 4, 2019
Individual Smoking and Health Cases	43	50	55
Smoking and Health Class Actions	9	10	10
Health Care Cost Recovery Actions	17	17	16
Label-Related Class Actions	—	—	1
Individual Label-Related Cases	5	5	7
Public Civil Actions	2	2	2

Since 1995, when the first tobacco-related litigation was filed against a PMI entity, 510 Smoking and Health, Label-Related, Health Care Cost Recovery, and Public Civil Actions in which we and/or one of our subsidiaries and/or indemnitees were a defendant have been terminated in our favor. Thirteen cases have had decisions in favor of plaintiffs. Ten of these cases have subsequently reached final resolution in our favor and three remain on appeal.

The table below lists the verdict and significant post-trial developments in the three pending cases where a verdict was returned in favor of the plaintiff:

[1] Includes cases pending in Canada.

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict
May 27, 2015	Canada/Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec rule in favor of the *Blais* clas on liability and found th class members' compensatory damages totaled approximately C 15.5 billion (approximat $12.1 billion), including pre-judgment interest. T trial court awarded compensatory damages a joint and several liabili basis, allocating 20% to subsidiary (approximate CAD 3.1 billion includi pre-judgment interest (approximately $2.4 billion)). The trial court awarded CAD 90,000 (approximately $70,250 punitive damages, allocating CAD 30,000 (approximately $23,400 our subsidiary. The trial court ordered defendants pay CAD 1 billion (approximately $781 million) of the compensatory damage award, CAD 200 millio (approximately $156.1 million) of which is our subsidiary's portion, into trust within 60 days.

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict
May 27, 2015	Canada/Cecilia Létourneau	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec rule in favor of the *Létourneau* class on liability and awarded a total of CAD 131 million (approximat $102.3 million) in puniti damages, allocating CAI 46 million (approximate $36 million) to RBH. Th trial court ordered defendants to pay the ful punitive damage award i a trust within 60 days. T court did not order the payment of compensator damages.

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict
August 5, 2016	Argentina/Hugo Lespada	Individual Action	On August 5, 2016, the Civil Court No. 14 - Mar del Plata, issued a verdic favor of plaintiff, an individual smoker, and awarded him ARS 110,0 (approximately $1,252), plus interest, in compensatory and moral damages. The trial court found that our subsidiary failed to warn plaintiff o the risk of becoming addicted to cigarettes.

Pending claims related to tobacco products generally fall within the following categories:

Smoking and Health Litigation: These cases primarily allege personal injury and are brought by individual plaintiffs or on behalf of a class or purported class of individual plaintiffs. Plaintiffs' allegations of liability in these cases are based on various theories of recovery, including negligence, gross negligence, strict liability, fraud, misrepresentation, design defect, failure to warn, breach of express and implied warranties, violations of deceptive trade practice laws and consumer protection statutes. Plaintiffs in these cases seek various forms of relief, including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include licit activity, failure to state a claim, lack of defect, lack of proximate cause, assumption of the risk, contributory negligence, and statute of limitations.

As of February 5, 2021, there were a number of smoking and health cases pending against us, our subsidiaries or indemnitees, as follows:

- 43 cases brought by individual plaintiffs in Argentina (31), Brazil (3), Canada (2), Chile (2), China (1), Italy (1), the Philippines (1), Turkey (1) and Scotland (1), compared with 50 such cases on February 3, 2020, and 55 cases on February 4, 2019; and
- 9 cases brought on behalf of classes of individual plaintiffs in Canada, compared with 10 such cases on February 3, 2020 and 10 such cases on February 4, 2019.

The class actions pending in Canada are described above under the caption "*Smoking and Health Litigation — Canada.*"

In a class action in Brazil, *The Smoker Health Defense Association (ADESF) v. Souza Cruz, S.A. and Philip Morris Marketing, S.A., Nineteenth Lower Civil Court of the Central Courts of the Judiciary District of São Paulo, Brazil*, filed July 25, 1995, our subsidiary and another member of the industry are defendants. The plaintiff, a consumer organization, sought damages for all addicted smokers and former smokers, and injunctive relief. In 2004, the trial court found defendants liable without hearing evidence and awarded "moral damages" of R$1,000 (approximately $186) per smoker per full year of smoking plus interest at the rate of 1% per month, as of the date of the ruling. The court did not award actual damages, which were to be assessed in the second phase of the case. The size of the class was not estimated. Defendants appealed to the São Paulo Court of Appeals, which annulled the ruling in November 2008, finding that the trial court had inappropriately ruled without hearing evidence and returned the case to the trial court for further proceedings. In May 2011, the trial court dismissed the claim. In February 2015, the appellate court unanimously dismissed plaintiff's appeal. In September 2015, plaintiff appealed to the Superior Court of Justice. In February 2017, the Chief Justice of the Superior Court of Justice denied plaintiff's appeal. Plaintiff filed a further appeal. In August 2020, the Superior Court of Justice confirmed the denial of plaintiff's appeal finally dismissing the plaintiff's claim.

Health Care Cost Recovery Litigation: These cases, brought by governmental and non-governmental plaintiffs, seek reimbursement of health care cost expenditures allegedly caused by tobacco products. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including unjust enrichment, negligence, negligent design, strict liability, breach of express and implied warranties, violation of a voluntary undertaking or special duty, fraud, negligent misrepresentation, conspiracy, public nuisance, defective product, failure to warn, sale of cigarettes to minors, and claims under statutes governing competition and deceptive trade practices. Plaintiffs in these cases seek various forms of relief including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include lack of proximate cause, remoteness of injury, failure to state a claim, adequate

remedy at law, "unclean hands" (namely, that plaintiffs cannot obtain equitable relief because they participated in, and benefited from, the sale of cigarettes), and statute of limitations.

As of February 5, 2021, there were 17 health care cost recovery cases pending against us, our subsidiaries or indemnitees in Brazil (1), Canada (10), Korea (1) and Nigeria (5), compared with 17 such cases on February 3, 2020 and 16 such cases on February 4, 2019.

The health care cost recovery actions pending in Canada are described above under the caption "*Health Care Cost Recovery Litigation — Canada.*"

In the health care cost recovery case in Brazil, *The Attorney General of Brazil v. Souza Cruz Ltda., et al., Federal Trial Court, Porto Alegre, Rio Grande do Sul, Brazil*, filed May 21, 2019, we, our subsidiaries, and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past six years, payment of anticipated costs of treating future alleged smoking-related diseases, and moral damages. Defendants filed answers to the complaint in May 2020.

In the first health care cost recovery case in Nigeria, *The Attorney General of Lagos State v. British American Tobacco (Nigeria) Limited, et al., High Court of Lagos State, Lagos, Nigeria,* filed March 13, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of making challenges to service and the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the second health care cost recovery case in Nigeria, *The Attorney General of Kano State v. British American Tobacco (Nigeria) Limited, et al., High Court of Kano State, Kano, Nigeria,* filed May 9, 2007, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of making challenges to service and the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the third health care cost recovery case in Nigeria, *The Attorney General of Gombe State v. British American Tobacco (Nigeria) Limited, et al., High Court of Gombe State, Gombe, Nigeria,* filed October 17, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In February 2011, the court ruled that the plaintiff had not complied with the procedural steps necessary to serve us. As a result of this ruling, plaintiff must re-serve its claim. We have not yet been re-served.

In the fourth health care cost recovery case in Nigeria, *The Attorney General of Oyo State, et al., v. British American Tobacco (Nigeria) Limited, et al., High Court of Oyo State, Ibadan, Nigeria,* filed May 25, 2007, we and other members of the industry are defendants. Plaintiffs seek reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We challenged service as improper. In June 2010, the court ruled that plaintiffs did not have leave to serve the writ of summons on the defendants and that they must re-serve the writ. We have not yet been re-served.

In the fifth health care cost recovery case in Nigeria, *The Attorney General of Ogun State v. British American Tobacco (Nigeria) Limited, et al., High Court of Ogun State, Abeokuta, Nigeria*, filed February 26, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In May 2010, the trial court rejected our service objections. We have appealed.

In the health care cost recovery case in Korea, the *National Health Insurance Service v. KT&G, et. al.,* filed April 14, 2014, our subsidiary and other Korean manufacturers are defendants. Plaintiff alleges that defendants concealed the health hazards of smoking, marketed to youth, added ingredients to make their products more harmful and addictive,

and misled consumers into believing that *Lights* cigarettes are safer than regular cigarettes. The National Health Insurance Service seeks to recover damages allegedly incurred in treating 3,484 patients with small cell lung cancer, squamous cell lung cancer, and squamous cell laryngeal cancer from 2003 to 2012. The trial court dismissed the case in its entirety on November 20, 2020. Plaintiff appealed.

Label-Related Cases: These cases, now brought only by individual plaintiffs, allege that the use of the descriptor "Lights" or other alleged misrepresentations or omissions of labeling information constitute fraudulent and misleading conduct. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including misrepresentation, deception, and breach of consumer protection laws. Plaintiffs seek various forms of relief including restitution, injunctive relief, and compensatory and other damages. Defenses raised include lack of causation, lack of reliance, assumption of the risk, and statute of limitations.

As of February 5, 2021, there were 5 label-related cases brought by individual plaintiffs in Italy (1) and Chile (4) pending against our subsidiaries, compared with 5 such cases on February 3, 2020, and 7 such case on February 4, 2019.

Public Civil Actions: Claims have been filed either by an individual, or a public or private entity, seeking to protect collective or individual rights, such as the right to health, the right to information or the right to safety. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including product defect, concealment, and misrepresentation. Plaintiffs in these cases seek various forms of relief including injunctive relief such as banning cigarettes, descriptors, smoking in certain places and advertising, as well as implementing communication campaigns and reimbursement of medical expenses incurred by public or private institutions.

As of February 5, 2021, there were 2 public civil actions pending against our subsidiaries in Argentina (1) and Venezuela (1), compared with 2 such cases on February 3, 2020, and 2 such cases on February 4, 2019.

In the public civil action in Argentina, *Asociación Argentina de Derecho de Danos v. Massalin Particulares S.A., et al., Civil Court of Buenos Aires, Argentina,* filed February 26, 2007, our subsidiary and another member of the industry are defendants. The plaintiff, a consumer association, seeks the establishment of a relief fund for reimbursement of medical costs associated with diseases allegedly caused by smoking. Our subsidiary filed its answer in September 2007. In March 2010, the case file was transferred to the Federal Court on Administrative Matters after the Civil Court granted plaintiff's request to add the national government as a co-plaintiff in the case. The case is currently awaiting a court decision on the merits.

In the public civil action in Venezuela, *Federation of Consumers and Users Associations ("FEVACU"), et al. v. National Assembly of Venezuela and the Venezuelan Ministry of Health, Constitutional Chamber of the Venezuelan Supreme Court*, filed April 29, 2008, we were not named as a defendant, but the plaintiffs published a notice pursuant to court order, notifying all interested parties to appear in the case. In January 2009, our subsidiary appeared in the case in response to this notice. The plaintiffs purport to represent the right to health of the citizens of Venezuela and claim that the government failed to protect adequately its citizens' right to health. The claim asks the court to order the government to enact stricter regulations on the manufacture and sale of tobacco products. In addition, the plaintiffs ask the court to order companies involved in the tobacco industry to allocate a percentage of their "sales or benefits" to establish a fund to pay for the health care costs of treating smoking-related diseases. In October 2008, the court ruled that plaintiffs have standing to file the claim and that the claim meets the threshold admissibility requirements. In December 2012, the court admitted our subsidiary and BAT's subsidiary as interested third parties. In February 2013, our subsidiary answered the complaint.

Reduced-Risk Products

In Colombia, an individual filed a purported class action, *Ana Ferrero Rebolledo v. Philip Morris Colombia S.A., et al.*, in April 2019 against our subsidiaries with the Civil Court of Bogota related to the marketing of our Platform 1 product. Plaintiff alleged that our subsidiaries advertise the product in contravention of law and in a manner that misleads consumers by portraying the product in a positive light, and further asserts that the Platform 1 vapor contains many toxic compounds, creates a high level of dependence, and has damaging second-hand effects. Plaintiff sought injunctive relief and damages on her behalf and on a behalf of two classes (class 1 - all Platform 1 consumers in Colombia who seek damages for the purchase price of the product and personal injuries related to the alleged addiction, and class 2 - all residents of the neighborhood where the advertising allegedly took place who seek damages for exposure to the alleged illegal advertising). Our subsidiaries answered the complaint in January 2020, and in February 2020, plaintiff filed an amended complaint. The amended complaint modifies the relief sought on behalf of the named plaintiff and on behalf of a single class (all consumers of Platform 1 products in Colombia who seek damages for the product purchase price and personal injuries related to the use of an allegedly harmful product).

Other Litigation

The Department of Special Investigations of the government of Thailand ("DSI") conducted an investigation into alleged underpayment by our subsidiary, Philip Morris (Thailand) Limited ("PM Thailand"), of customs duties and excise taxes relating to imports from the Philippines covering the period 2003-2007. On January 18, 2016, the Public Prosecutor filed charges against our subsidiary and seven former and current employees in the Bangkok Criminal Court alleging that PM Thailand and the individual defendants jointly and with the intention to defraud the Thai

government, under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries of cigarettes from the Philippines during the period of July 2003 to June 2006. The government is seeking a fine of approximately THB 80.8 billion (approximately $2.7 billion). In May 2017, Thailand enacted a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and other Thai governmental agencies. Trial in the case began in November 2017 and concluded in September 2019. In November 2019, the trial court found our subsidiary guilty of under-declaration of the prices

and imposed a fine of approximately THB 1.2 billion (approximately $39.9 million). The trial court dismissed all charges against the individual defendants. In December 2019, as required by the Thai law, our subsidiary paid the fine. This payment is included in other assets on the consolidated balance sheets and negatively impacted net cash provided by operating activities in the consolidated statements of cash flows in the period of payment. Our subsidiary filed an appeal of the trial court's decision. In addition, the Public Prosecutor filed an appeal of the trial court's decision challenging the dismissal of charges against the individual defendants and the amount of the fine imposed. If our subsidiary ultimately prevails on appeal, then Thailand will be required to return this payment to our subsidiary.

The DSI also conducted an investigation into alleged underpayment by PM Thailand of customs duties and excise taxes relating to imports from Indonesia covering the period 2000-2003. On January 26, 2017, the Public Prosecutor filed charges against PM Thailand and its former Thai employee in the Bangkok Criminal Court alleging that PM Thailand and its former employee jointly and with the intention to defraud the Thai government under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries during the period from January 2002 to July 2003. The government is seeking a fine of approximately THB 19.8 billion (approximately $658 million). In May 2017, Thailand enacted a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law, and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and a Thai court. Trial in the case began in November 2018 and concluded in December 2019. In March 2020, the trial court found our subsidiary guilty of under-declaration of the prices and imposed a fine of approximately THB 130 million (approximately $4.3 million). The trial court dismissed all charges against the individual defendant. In April 2020, as required by Thai law, our subsidiary paid the fine. Our subsidiary will appeal the trial court's decision. In addition, the Public Prosecutor filed an appeal of the trial court's decision challenging the dismissal of charges against the individual defendant and the amount of the fine imposed. If our subsidiary ultimately prevails on appeal, then Thailand will be required to return this payment to our subsidiary.

The South Korean Board of Audit and Inspection ("BAI") conducted an audit of certain Korean government agencies and the tobacco industry into whether inventory movements ahead of the January 1, 2015 increase of cigarette-related taxes by tobacco companies, including Philip Morris Korea Inc. ("PM Korea"), our South Korean subsidiary, were in compliance with South Korean tax laws. In November 2016, the tax authorities completed their audit and assessed allegedly underpaid taxes and penalties. In order to avoid nonpayment financial costs, PM Korea paid approximately KRW 272 billion (approximately $243 million), of which KRW 100 billion (approximately $89.3 million) was paid in 2016 and KRW 172 billion (approximately $153.7 million) was paid in the first quarter of 2017. These paid amounts are included in other assets in the consolidated balance sheets and negatively impacted net cash provided by operating activities in the consolidated statements of cash flows in the period of payment. PM Korea appealed the assessments. In January 2020, a trial court ruled that PM Korea did not underpay taxes in the amount of approximately KRW 218 billion (approximately $195 million). The tax authorities appealed this decision to the appellate court. In September 2020, the appellate court upheld the trial court's decision. The tax authorities have appealed to the Supreme Court of South Korea. In June 2020, another trial court ruled that PM Korea did not underpay approximately KRW 54 billion (approximately $48 million) of alleged underpayments. The government agencies appealed this decision. In January 2021, the appellate court upheld the trial court's decision. The government agencies may appeal. If the tax authorities and government agencies ultimately lose, then they would be required to return the paid amounts to PM Korea.

The Moscow Tax Inspectorate for Major Taxpayers ("MTI") conducted an audit of AO Philip Morris Izhora ("PM Izhora"), our Russian subsidiary, for the 2015-2017 financial years. On July 26, 2019, MTI issued its initial assessment, claiming that intercompany sales of cigarettes between PM Izhora and another Russian subsidiary prior to excise tax increases and submission by PM Izhora of the maximum retail sales price notifications for cigarettes to the tax authorities were improper under Russian tax laws and resulted in underpayment of excise taxes and VAT. In August 2019, PM Izhora submitted its objections disagreeing with MTI's allegations set forth in the initial assessment and MTI's methodology for calculating the alleged underpayments. MTI accepted some of PM Izhora's arguments and in September 2019, issued the final tax assessment claiming an underpayment of RUB 24.3 billion (approximately $374 million), including penalties and interest. In accordance with Russian tax laws, PM Izhora paid the entire amount of MTI's final assessment. This amount was neither imposed on, nor concurrent with, the specific revenue-producing transaction, nor was it collected from customers of our Russian subsidiaries. In the third quarter of 2019, PMI recorded a pre-tax charge of $374 million, in marketing, administration and research costs in the

consolidated statements of earnings, representing $315 million net of an associated income tax benefit of $59 million.

The Saudi Arabia Customs General Authority issued its assessments requiring our distributors (one former and one current) to pay additional customs duties in an amount of approximately 1.5 billion Saudi Riyal, or approximately $396 million, in relation to the fees paid by these distributors under their agreements with our subsidiary for exclusive rights to distribute our products in Saudi Arabia during the period of 2014 through 2018. In order to challenge these assessments, the distributors posted bank guarantees equaling the amount of the above assessments. To enable the distributors' challenge, our subsidiary agreed with the banks to bear 80 percent of the amount the authority may draw on the bank guarantees. In September and October 2020, respectively, the distributors lost their

challenges of the assessments; both distributors appealed. Our subsidiary and our distributors believe that customs duties paid in Saudi Arabia were in compliance with the applicable law and the WTO Customs Valuation Agreement.

A putative shareholder class action lawsuit, *In re Philip Morris International Inc. Securities Litigation*, is pending in the United States District Court for the Southern District of New York, purportedly on behalf of purchasers of Philip Morris International Inc. stock between July 26, 2016 and April 18, 2018. The lawsuit names Philip Morris International Inc. and certain officers and employees as defendants and includes allegations that the defendants made false and/or misleading statements and/or failed to disclose information about PMI's business, operations, financial condition, and prospects, related to product sales of, and alleged irregularities in clinical studies of, PMI's Platform 1 product. The lawsuit seeks various forms of relief, including damages. In November 2018, the court consolidated three putative shareholder class action lawsuits with similar allegations previously filed in the Southern District of New York (namely, *City of Westland Police and Fire Retirement System v. Philip Morris International Inc., et al., Greater Pennsylvania Carpenters' Pension Fund v. Philip Morris International Inc., et al., and Gilchrist v. Philip Morris International Inc., et al.*) into these proceedings. A putative shareholder class action lawsuit, *Rubenstahl v. Philip Morris International Inc., et al.*, that had been previously filed in December 2017 in the United States District Court for the District of New Jersey, was voluntarily dismissed by the plaintiff due to similar allegations in these proceedings. On February 4, 2020, the court granted defendants' motion in its entirety, dismissing all but one of the plaintiffs' claims with prejudice. The court noted that one of plaintiffs' claims (allegations relating to four non-clinical studies of PMI's Platform 1 product) did not state a viable claim but allowed plaintiffs to replead that claim by March 3, 2020. On February 18, 2020, the plaintiffs filed a motion for reconsideration of the court's February 4th decision; this motion was denied on September 21, 2020. On September 28, 2020, plaintiffs filed an amended complaint seeking to replead allegations relating to four non-clinical studies of PMI's Platform 1 product. We believe that this lawsuit is without merit and will continue to defend it vigorously.

In April 2020, affiliates of British American Tobacco plc ("BAT") commenced patent infringement proceedings, *RAI Strategic Holdings, Inc., et al. v. Altria Client Services LLC, et al.*, in the federal court in the Eastern District of Virginia, where PMI's subsidiary, Philip Morris Products S.A., as well as Altria Group, Inc.'s subsidiaries, are defendants. Plaintiffs seek damages and injunctive relief against the commercialization of the Platform 1 products in the United States. In April 2020, BAT affiliates filed a complaint against PMI, Philip Morris Products S.A., Altria Group, Inc., and its subsidiaries before the International Trade Commission ("ITC"). Plaintiffs seek an order to prevent the importation of Platform 1 products into the United States. The ITC evidentiary hearing closed on February 1, 2021. The administrative law judge has scheduled an initial determination date of May 14, 2021 and the target date for the final determination of the ITC is September 15, 2021. In June 2020, defendants filed their responses in both proceedings. In the Eastern District of Virginia case, the defendants also counterclaimed that BAT infringed their patents relating to certain e-vapor products, seeking damages for the commercialization of these products by BAT.

In April 2020, BAT's affiliate commenced patent infringement proceedings, *Nicoventures Trading Limited v. PM GmbH, et al.,* against PMI's German subsidiary, Philip Morris GmbH, and Philip Morris Products S.A., in the Regional Court in Munich, Germany. Plaintiffs seek damages and injunctive relief against the commercialization of the Platform 1 products in Germany.

In July 2020, in response to a challenge in the United Kingdom by PMI's subsidiary to patents related to the BAT patents in the German proceedings, BAT affiliates brought a patent infringement action, *Nicoventures Trading Limited, et al. v. Philip Morris Products S.A., et al.,* against Philip Morris Products S.A. and PMI's U.K. subsidiary, Philip Morris Limited, in the English High Court, seeking damages and injunctive relief against the commercialization of the Platform 1 products in the United Kingdom.

In September 2020, BAT's affiliates commenced patent infringement and unfair competition proceedings, *RAI Strategic Holdings, Inc., et al. v. Philip Morris Products S.A., et al.*, against Philip Morris Products S.A. and PMI's Italian subsidiaries, Philip Morris Manufacturing & Technology Bologna S.p.A. and Philip Morris Italia S.r.l., in the Court of Milan, Italy. Plaintiffs seek damages, as well as injunctive relief against the manufacture in Italy of the Platform 1 heated tobacco units allegedly infringing the asserted patents and the commercialization of the Platform 1 products in Italy. As part of this proceeding, in October 2020, BAT's affiliates filed a request based on one of the two asserted patents seeking preliminary injunctive relief against the manufacture and commercialization of the Platform 1 products in Italy.

In October 2020, BAT's affiliate commenced patent infringement proceedings, *Nicoventures Trading Limited v. Philip Morris CR a.s., et al.*, against PMI's Czech subsidiary, Philip Morris CR a.s., and Philip Morris Products S.A.,

in the Town Court of Prague, Czech Republic, seeking preliminary injunctive relief against the commercialization of the Platform 1 products in the Czech Republic. In October 2020, the court dismissed plaintiff's request for preliminary injunction in its entirety. In October 2020, plaintiff appealed. In February 2021, the appellate court denied plaintiffs' appeal, confirming the dismissal of plaintiffs' request.

In October 2020, BAT's affiliate commenced patent infringement proceedings, *RAI Strategic Holdings, Inc. v. Philip Morris Polska Distribution sp. z o.o.*, against PMI's Polish subsidiary, Philip Morris Polska Distribution Sp. z o.o., in the Regional Court in Warsaw, IP Division. Plaintiff seeks preliminary injunctive relief against the commercialization of the Platform 1 products in Poland. In November 2020, the court dismissed plaintiff's request for preliminary injunction in its entirety. Plaintiff may appeal.

In October 2020, BAT's affiliates commenced patent infringement proceedings, *RAI Strategic Holdings, Inc., et al. v. Philip Morris Japan, Limited*, *et al*., against PMI's Japanese subsidiary, Philip Morris Japan Limited, and a third-party distributor in the Tokyo District Court. Plaintiffs seek damages and injunctive relief against the commercialization of the Platform 1 products in Japan.

In November 2020, BAT's affiliate commenced patent infringement proceedings, *RAI Strategic Holdings, Inc., et al. v. Philip Morris Bulgaria EOOD*, against PMI's Bulgarian subsidiary, Philip Morris Bulgaria EOOD, in the Sofia City Court, Bulgaria, seeking preliminary injunctive relief against the commercialization of the Platform 1 products in Bulgaria. In November 2020, the court dismissed plaintiffs' request for preliminary injunction in its entirety. Plaintiffs have appealed. In January 2021, the appellate court denied plaintiffs' appeal, confirming the dismissal of plaintiffs' request.

In November 2020, BAT's affiliates commenced patent infringement proceedings, *RAI Strategic Holdings, Inc., et al. v. Philip Morris Romania SRL*, et al., against PMI's Romanian subsidiaries, Philip Morris Romania S.R.L. and Philip Morris Trading S.R.L., and a third-party distributor in the Court of Law of Bucharest, Civil Registry. Plaintiffs seek damages and preliminary and permanent injunctive relief against the manufacture and commercialization of the Platform 1 products in Romania.

In December 2020, BAT's affiliate commenced proceedings, *Nicoventures Trading Limited v. Philip Morris Products S.A., et al.*, against PMI's German subsidiaries, Philip Morris GmbH and f6 Cigarettenfabrik GmbH & Co.KG, and Philip Morris Products S.A., in the Hamburg Regional Court, for the alleged infringement of a patent utility model, seeking preliminary injunctive relief against the manufacture and commercialization of the Platform 1 products in Germany.

Other patent challenges by both parties are pending in various jurisdictions.

We believe that the foregoing proceedings by the affiliates of BAT are without merit and will defend them vigorously.

We are also involved in additional litigation arising in the ordinary course of our business. While the outcomes of these proceedings are uncertain, management does not expect that the ultimate outcomes of other litigation, including any reasonably possible losses in excess of current accruals, will have a material adverse effect on our consolidated results of operations, cash flows or financial position.

Third-Party Guarantees

On October 17, 2020, Medicago Inc., an equity method investee of Philip Morris Investments B.V. ("PMIBV"), a PMI subsidiary, entered into a contribution agreement with the Canadian government (the "Contribution Agreement") whereby the Canadian government agreed to contribute up to CAD 173 million (approximately $131 million on the date of signing) to Medicago Inc., to support its on-going COVID-19 vaccine development and clinical trials, and for the construction of its Quebec City manufacturing facility (the "Project"). PMIBV and the majority shareholder of Medicago Inc. are also parties to the Contribution Agreement as guarantors of Medicago Inc.'s obligations thereunder on a joint and several basis ("Co-Guarantors"). The Co-Guarantors agreed to repay amounts contributed by the Canadian government plus interest, if Medicago Inc. fails to do so, and could be responsible for the costs of other Medicago's obligations (such as the achievement of specific milestones of the Project). The maximum amount of these obligations is currently non-estimable. As of December 31, 2020, PMI has determined that these guarantees did not have a material impact on its consolidated financial statements.

In connection with the Contribution Agreement, PMIBV and the majority shareholder of Medicago Inc. entered into a guarantors' agreement that apportions Co-Guarantors' obligations and limits those of PMIBV to its then share of holdings in Medicago Inc., which as of December 31, 2020 was approximately 32%. The guarantees are in effect through March 31, 2026.

Note 18.

Sale of Accounts Receivable:

To mitigate risk and enhance cash and liquidity management PMI sells trade receivables to unaffiliated financial institutions. These arrangements allow PMI to sell, on an ongoing basis, certain trade receivables without recourse. The trade receivables sold are generally short-term in nature and are removed from the consolidated balance sheets. PMI sells trade receivables under two types of arrangements, servicing and non-servicing. For servicing arrangements, PMI continues to service the sold trade receivables on an administrative basis and does not act on behalf of the unaffiliated financial institutions. When applicable, a servicing liability is recorded for the estimated fair value of the servicing. The amounts associated with the servicing liability were not material for the years ended December 31, 2020 and 2019. Under the non-servicing arrangements, PMI does not provide any administrative support or servicing after the trade receivables have been sold to the unaffiliated financial institutions.

Cumulative trade receivables sold, including excise taxes, for the years ended December 31, 2020 and 2019, were $11.5 billion and $10.7 billion, respectively. PMI's operating cash flows were positively impacted by the amount of the trade receivables sold and derecognized from the consolidated balance sheets, which remained outstanding with the unaffiliated financial institutions. The trade receivables sold that remained outstanding under these arrangements as of December 31, 2020, 2019 and 2018, were $1.2 billion, $0.9 billion and $1.0 billion, respectively. The net proceeds received are included in cash provided by operating activities in the consolidated statements of cash flows. The difference between the carrying amount of the trade receivables sold and the sum of the cash received is recorded as a loss on sale of trade receivables within marketing, administration and research costs in the consolidated statements of earnings. For the years ended December 31, 2020, 2019 and 2018 the loss on sale of trade receivables was immaterial.

Note 19.

Asset Impairment and Exit Costs:

Organizational Design Optimization

As part of PMI's transformation to a smoke-free future, PMI seeks to optimize its organizational design, which includes the elimination, relocation and outsourcing of certain operations center and centralized activities. In January 2020, PMI commenced a multi-phase restructuring project in Switzerland. PMI initiated the employee consultation procedures, as required under Swiss law, for the impacted employees. In 2020, the consultation procedures for two phases were completed. The third phase commenced in January 2021 and is expected to impact approximately 230 positions. Until the consultation process for the third phase is concluded, such phase is not considered probable (under U.S. GAAP), and the total potential costs cannot be determined. As a result, no related costs were recorded for the year ended December 31, 2020 related to the third phase of the restructuring project. Additionally, PMI launched a voluntary separation program in Switzerland for certain eligible employees and announced the outsourcing of certain activities in the United States and Poland.

These activities are expected to impact approximately 600 positions in total, excluding the third phase of the project in Switzerland, that will be either eliminated, relocated or outsourced. For the year ended December 31, 2020, PMI recorded pre-tax asset impairment and exit costs of $149 million related to the organizational design optimization.

The amounts related to the potential pension settlement accounting impact of the restructuring, which could be significant, have not been reflected in 2020 as the thresholds for accounting were not exceeded by December 31, 2020.

Global Manufacturing Infrastructure Optimization

In light of declining PMI cigarette volumes resulting from lower total industry volumes and the shift to smoke-free alternatives, PMI continues to optimize its global manufacturing infrastructure. During 2019, PMI recorded asset impairment and exit costs related to plant closures in Argentina, Colombia, Germany and Pakistan as part of its global manufacturing infrastructure optimization.

Germany

On November 4, 2019, PMI announced that, as part of its global manufacturing infrastructure optimization, its German affiliate, Philip Morris Manufacturing GmbH ("PMMG"), reached an agreement with employee representatives to end cigarette production in its factory in Berlin, Germany, by January 1, 2020. As a result of this agreement, during 2019, PMI recorded pre-tax asset impairment and exit costs of $342 million in the European Union segment. This amount included pension and employee separation costs of $251 million, which will be paid in cash, and asset impairment costs of $91 million, primarily related to machinery and equipment, which are non-cash charges.

Other

During 2019, PMI also recorded pre-tax asset impairment and exit costs of $80 million as part of its global manufacturing infrastructure optimization. These costs were related to cigarette plant closures in Argentina ($15 million), Colombia ($45 million) and Pakistan ($20 million). The charges were reflected in the Latin America & Canada segment (Argentina and Colombia) and the South & Southeast Asia segment (Pakistan).

Asset Impairment and Exit Costs by Segment

During 2020 and 2019, PMI recorded the following pre-tax asset impairment and exit costs by segment:

(in millions)	2020	2019
Separation programs: [1]		
European Union	$ 53	$ 251
Eastern Europe	14	—
Middle East & Africa	18	—
South & Southeast Asia	22	3
East Asia & Australia	25	—
Latin America & Canada	9	49
Total separation programs	141	303
Asset impairment charges [1]		
European Union	4	91
Eastern Europe	1	—
Middle East & Africa	1	—
South & Southeast Asia	1	17
East Asia & Australia	1	—
Latin America & Canada	—	11
Total asset impairment charges	8	119
Asset impairment and exit costs	$ 149	$ 422

[1] Organizational design optimization pre-tax charges in 2020 were allocated across all operating segments.

The total pre-tax asset impairment and exit costs above were included in marketing, administration and research costs on the consolidated statements of earnings. During 2018, PMI did not incur asset impairment and exit costs.

Movement in Exit Cost Liabilities

The movement in exit cost liabilities for the year ended December 31, 2020 was as follows:

(in millions)	
Liability balance, January 1, 2020	$ 191
Charges, net	141
Cash spent	(163)
Currency/other	11
Liability balance, December 31, 2020	$ 180

Future cash payments for exit costs incurred to date are anticipated to be substantially paid by the end of 2022, with approximately $150 million expected to be paid in 2021.

Note 20.

Deconsolidation of RBH:

As discussed in Note 17. *Contingencies,* following the March 1, 2019, judgment of the Court of Appeal of Québec in two class action lawsuits against PMI's Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH"), PMI recorded in its consolidated results a pre-tax charge of $194 million, representing $142 million net of tax, in the first quarter of 2019. This pre-tax Canadian tobacco litigation-related expense was included in marketing, administration

and research costs on PMI's consolidated statement of earnings for the year ended December 31, 2019. The charge reflects PMI's assessment of the portion of the judgment that represents probable and estimable loss prior to the deconsolidation of RBH and corresponds to the trust account deposit required by the judgment. RBH's share of the deposit is approximately CAD 257 million.

On March 22, 2019, RBH obtained an initial order from the Ontario Superior Court of Justice granting it protection under the Companies' Creditors Arrangement Act ("CCAA"), which is a Canadian federal law that permits a Canadian business to restructure its affairs while carrying on its business in the ordinary course with minimal disruption to its customers, suppliers and employees.

The administration of the CCAA process, principally relating to the powers provided to the court and the court appointed monitor, removes certain elements of control of the business from both PMI and RBH. As a result, PMI has determined that it no longer has a controlling financial interest over RBH as defined in ASC 810 (Consolidation), and PMI deconsolidated RBH as of the date of the CCAA filing. PMI has also determined that it does not exert "significant influence" over RBH as that term is defined in ASC 323 (Investments-Equity Method and Joint Ventures). Therefore, as of March 22, 2019, PMI accounted for its continuing investment in RBH in accordance with ASC 321 (Investments-Equity Securities) as an equity security, without readily determinable fair value.

Following the deconsolidation, the carrying value of assets and liabilities of RBH was removed from the consolidated balance sheet of PMI, and the continuing investment in RBH was recorded at fair value at the date of deconsolidation. The total amount deconsolidated from PMI's balance sheet was $3,519 million, including $1,323 million of cash, $1,463 million of goodwill, $529 million of accumulated other comprehensive earnings, primarily related to historical currency translation and $204 million of other assets and liabilities, net. While PMI is accounting for its investment in RBH as an equity security, PMI would recognize dividends as income upon receipt. However, while it remains under creditor protection, RBH does not anticipate paying dividends.

The fair value of PMI's continuing investment in RBH of $3,280 million was determined at the date of deconsolidation, recorded within equity investments and is assessed for impairment on an ongoing basis. The estimated fair value of the underlying business was determined based on an income approach using a discounted cash flow analysis, as well as a market approach for certain contingent liabilities. The information used in the estimate includes observable inputs, primarily a discount rate of 8%, a terminal growth rate of 2.5% and information about total tobacco market size in Canada and RBH's share of the market, as well as unobservable inputs such as operating budgets and strategic plans, various inflation scenarios, estimated shipment volumes, and expected product pricing and projected margins.

The difference between the carrying value of the assets and liabilities of RBH that were deconsolidated and the fair value of the continuing investment, as determined at the date of deconsolidation, was $239 million, before tax, and this loss on deconsolidation is reflected within marketing, administration and research costs on PMI's consolidated statement of earnings for the year ended December 31, 2019. PMI also recorded a tax benefit of $49 million within the provision for income taxes for the year ended December 31, 2019, related to the reversal of a deferred tax liability on unremitted earnings of RBH.

RBH is party to transactions with PMI and its consolidated subsidiaries entered into in the normal course of business; these transactions include royalty payments and recharge of various corporate expenses for services benefiting RBH. Up to the date of the CCAA filing, these transactions were eliminated on consolidation and had no impact on PMI's consolidated statement of earnings. After deconsolidating RBH, these transactions are treated as third-party transactions in PMI's financial statements. The amount of these related-party transactions is included within Note 4. *Related Parties - Equity investments and Other.*

Developments in the CCAA process, including resolution through a plan of arrangement or compromise of all pending tobacco-related litigation currently stayed in Canada, as discussed in Note 17. *Contingencies*, could result in a material change in the fair value of PMI's continuing investment in RBH.

Note 21.

Leases:

PMI's operating leases are principally for real estate (office space, warehouses and retail store space) and vehicles. Lease terms range from 1 year to 73 years, some of which include options to renew, which are reasonably certain to

be renewed. Lease terms may also include options to terminate the lease. The exercise of a lease renewal or termination option is at PMI's discretion.

PMI's operating leases at December 31, 2020 and 2019, were as follows:

(in millions)	At December 31, 2020	2019
Assets:		
Other assets	**$ 697**	$ 766
Liabilities:		
Current		
Accrued liabilities - Other	**$ 190**	$ 194
Noncurrent		
Income taxes and other liabilities	**517**	569
Total lease liabilities	**$ 707**	$ 763

For information regarding PMI's immaterial finance leases, see Note 7. *Indebtedness*.

The components of PMI's lease cost were as follows for the years ended December 31, 2020 and 2019:

(in millions)	For the Years Ended December 31, 2020	2019
Operating lease cost	**$ 237**	$ 242
Short-term lease cost	**49**	61
Variable lease cost	**31**	29
Total lease cost	**$ 317**	$ 332

Maturity of PMI's operating lease liabilities, on an undiscounted basis, as of December 31, 2020, was as follows:

(in millions)	Total
2021	**$ 215**
2022	**161**
2023	**110**
2024	**72**
2025	**47**
Thereafter	**291**
Total lease payments	**896**
Less: Interest	**189**
Present value of lease liabilities	**$ 707**

Other information related to PMI's operating leases was as follows for the year ended December 31, 2020 and 2019:

(in millions)	December 31, 2020	2019
Cash paid for amounts included in the measurement of lease liabilities in Operating cash flows	**$ 238**	$ 240
Leased assets obtained in exchange for new operating lease liabilities	**$ 149**	$ 221
Weighted-average remaining lease term (years)	**10.1**	9.6
Weighted-average discount rate[1]	**4.3 %**	4.4 %

[1] PMI's weighted-average discount rate is based on its estimated pre-tax cost of debt adjusted for country-specific risk.

Note 22.

Quarterly Financial Data (Unaudited):

(in millions, except per share data)	2020 Quarters			
	1st	2nd	3rd	4th
Net revenues	**$ 7,153**	**$ 6,651**	**$ 7,446**	**$ 7,444**
Gross profit	**$ 4,751**	**$ 4,472**	**$ 5,030**	**$ 4,872**
Net earnings attributable to PMI	**$ 1,826**	**$ 1,947**	**$ 2,307**	**$ 1,976**
Per share data:				
Basic EPS	**$ 1.17**	**$ 1.25**	**$ 1.48**	**$ 1.27**
Diluted EPS	**$ 1.17**	**$ 1.25**	**$ 1.48**	**$ 1.27**
Dividends declared	**$ 1.17**	**$ 1.17**	**$ 1.20**	**$ 1.20**

(in millions, except per share data)	2019 Quarters			
	1st	2nd	3rd	4th
Net revenues	$ 6,751	$ 7,699	$ 7,642	$ 7,713
Gross profit	$ 4,286	$ 5,034	$ 5,037	$ 4,935
Net earnings attributable to PMI	$ 1,354	$ 2,319	$ 1,896	$ 1,616
Per share data:				
Basic EPS	$ 0.87	$ 1.49	$ 1.22	$ 1.04
Diluted EPS	$ 0.87	$ 1.49	$ 1.22	$ 1.04
Dividends declared	$ 1.14	$ 1.14	$ 1.17	$ 1.17

Basic and diluted EPS are computed independently for each of the periods presented. Accordingly, the sum of the quarterly EPS amounts may not agree to the total for the year.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of
Philip Morris International Inc.:

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Philip Morris International Inc. and its subsidiaries (the "Company") as of December 31, 2020 and 2019, and the related consolidated statements of earnings, comprehensive earnings, stockholders' (deficit) equity and cash flows for each of the three years in the period ended December 31, 2020, including the related notes (collectively referred to as the "consolidated financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2020, based on criteria established in *Internal Control - Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2020 and 2019, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2020 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2020, based on criteria established in *Internal Control - Integrated Framework* (2013) issued by the COSO.

Basis for Opinions

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Report of Management on Internal Control over Financial Reporting. Our responsibility is to express opinions on the Company's consolidated financial statements and on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly

reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Critical Audit Matters

The critical audit matter communicated below is a matter arising from the current period audit of the consolidated financial statements that was communicated or required to be communicated to the audit committee and that (i) relates to accounts or disclosures that are material to the consolidated financial statements and (ii) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the consolidated financial statements, taken as a whole, and we are not, by communicating the critical audit matter below, providing a separate opinion on the critical audit matter or on the accounts or disclosures to which it relates.

Tobacco-Related Litigation for Smoking and Health Class Actions and Health Care Cost Recovery Actions

As described in Note 17 to the consolidated financial statements, the Company has 9 smoking and health class actions and 17 health care cost recovery actions pending. The Company records provisions in the consolidated financial statements for pending litigation when management determines that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. Except as stated otherwise in Note 17, while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available, (i) management has not concluded that it is probable that a loss has been incurred in any of the pending smoking and health class actions and health care cost recovery cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending smoking and health class actions and health care cost recovery cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any.

The principal considerations for our determination that performing procedures relating to tobacco-related litigation for smoking and health class actions and health care cost recovery actions is a critical audit matter are that there was significant judgment by management when determining the probability of a loss being incurred and an estimate of the amount or range of the potential loss for each case, which in turn led to a high degree of auditor subjectivity, judgment and effort in evaluating management's assessment related to the loss contingencies associated with smoking and health class actions and health care cost recovery actions related claims.

Addressing the matter involved performing procedures and evaluating audit evidence in connection with forming our overall opinion on the consolidated financial statements. These procedures included testing the effectiveness of controls relating to management's evaluation of smoking and health class actions and health care cost recovery actions, including controls over determining the probability and range of loss as well as controls over financial statement disclosures. These procedures also included, among others, obtaining and evaluating the letters of audit inquiry with external and internal legal counsel, evaluating the reasonableness of management's assessment regarding whether an unfavorable outcome is reasonably possible or probable and reasonably estimable, and evaluating the sufficiency of the Company's smoking and health class actions and health care cost recovery actions contingencies disclosures.

/S/ PRICEWATERHOUSECOOPERS SA

PricewaterhouseCoopers SA

/S/ CHAD MUELLER

Chad Mueller

/S/ TRAVIS RANDOLPH

Travis Randolph

Lausanne, Switzerland
February 9, 2021

We have served as the Company's auditor since 2008.

Report of Management on Internal Control Over Financial Reporting

Management of Philip Morris International Inc. ("PMI") is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended. PMI's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes those written policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of PMI;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America;
- provide reasonable assurance that receipts and expenditures of PMI are being made only in accordance with the authorization of management and directors of PMI; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets that could have a material effect on the consolidated financial statements.

Internal control over financial reporting includes the controls themselves, monitoring and internal auditing practices and actions taken to correct deficiencies as identified.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of PMI's internal control over financial reporting as of December 31, 2020. Management based this assessment on criteria for effective internal control over financial reporting described in *Internal Control — Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management's assessment included an evaluation of the design of PMI's internal control over financial reporting and testing of the operational effectiveness of its internal control over financial reporting. Management reviewed the results of its assessment with the Audit Committee of our Board of Directors.

Based on this assessment, management determined that, as of December 31, 2020, PMI maintained effective internal control over financial reporting.

PricewaterhouseCoopers SA, an independent registered public accounting firm, who audited and reported on the consolidated financial statements of PMI included in this report, has audited the effectiveness of PMI's internal control over financial reporting as of December 31, 2020, as stated in their report herein.

February 9, 2021

Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.*

None.

Item 9A. *Controls and Procedures.*

PMI carried out an evaluation, with the participation of PMI's management, including PMI's Chief Executive Officer and Chief Financial Officer, of the effectiveness of PMI's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based upon that evaluation, PMI's Chief Executive Officer and Chief Financial Officer concluded that PMI's disclosure controls and procedures are effective. There have been no changes in PMI's internal control over financial reporting during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, PMI's internal control over financial reporting.

The Report of Management on Internal Control over Financial Reporting and the Report of Independent Registered Public Accounting Firm are included in Item 8.

Item 9B. *Other Information.*

None.

PART III

Except for the information relating to the executive officers set forth in Item 10 and the information relating to equity compensation plans set forth in Item 12, the information called for by Items 10-14 is hereby incorporated by reference to PMI's definitive proxy statement for use in connection with its annual meeting of stockholders to be held on May 5, 2021, that will be filed with the SEC on or about March 25, 2021 (the "proxy statement"), and, except as indicated therein, made a part hereof.

Item 10. *Directors, Executive Officers and Corporate Governance.*

Information About Our Executive Officers as of February 8, 2021:

Name	Office	Age
André Calantzopoulos*	Chief Executive Officer	63
Massimo Andolina	Senior Vice President, Operations	52
Drago Azinovic	President, Middle East & Africa Region and PMI Duty Free	58
Emmanuel Babeau	Chief Financial Officer	53
Werner Barth	Senior Vice President, Commercial	56
Charles Bendotti	Global Head, People & Culture	48
Frank de Rooij	Vice President, Treasury and Corporate Finance	55
Frederic de Wilde	President, European Union Region	53
Suzanne Rich Folsom	Senior Vice President and General Counsel	59
Jorge Insuasty	Chief Life Sciences Officer	62
Stacey Kennedy	President, South and Southeast Asia Region	48
Martin G. King	CEO, PMI America	56
Michael Kunst	Senior Vice President, Commercial Transformation	52
Andreas Kurali	Vice President and Controller	55
Bin Li	Chief Product Officer	49
Marco Mariotti	President, Eastern Europe Region	56
Mario Masseroli	President, Latin America and Canada Region	50
Deepak Mishra	Chief Strategy Officer	49
Silke Muenster	Chief Diversity Officer	60
Jacek Olczak*	Chief Operating Officer	56
Paul Riley	President, East Asia and Australia Region	55
Marian Salzman	Senior Vice President, Global Communications	61
Gregoire Verdeaux	Senior Vice President, External Affairs	48
Michael Voegele	Chief Technology Officer	48
Stefano Volpetti	Chief Consumer Officer	49

*André Calantzopoulos will become Executive Chairman of the Board of Directors immediately before the 2021 Annual Meeting of Shareholders to be held on May 5, 2021 ("Annual Meeting"). Jacek Olczak will succeed Mr. Calantzopoulos as Chief Executive Officer effective immediately after the Annual Meeting.

All of the above-mentioned officers, except Mr. Babeau, Ms. Folsom, Dr. Insuasty, Mr. Kunst, Mr. Li, Mr. Mishra, Ms. Salzman, Mr. Voegele, Mr. Volpetti, and Mr. Verdeaux, have been employed by us in various capacities over the past five years. The business experience of Mr. Babeau, Ms. Folsom, Dr. Insuasty, Mr. Kunst, Mr. Li, Mr. Mishra, Ms. Salzman, Mr. Voegele, Mr. Volpetti, and Mr. Verdeaux for the past five years is summarized below.

Mr. Babeau joined Philip Morris International Inc. in May 2020. He was formerly Deputy Chief Executive Officer of Schneider Electric. During his tenure at Schneider Electric, Mr. Babeau helped grow the company from an €18 billion market cap to c. €60 billion while transforming the business model and winning industry accolades, including from the Harvard Business Review, which in 2019 cited Schneider Electric as one of the top 15 business transformations of the prior decade.

Ms. Folsom joined Philip Morris International Inc. in July 2020. She is a former Partner and Co-Chair of the Investigations, Compliance and Strategic Response Group at Manatt, Phelps & Phillips, LLP. A veteran general counsel of both public and private companies, and a transformation and restructuring leader, Ms. Folsom most recently served as the General Counsel, Chief Compliance Officer and Senior Vice President, Government Affairs and Global Public Policy at United States Steel Corporation.

Dr. Insuasty commenced his role at Philip Morris International Inc. in January 2021. He was formerly Global Franchise Head of Immunology, Oncology, and Neurology for Sanofi Genzyme, part of Sanofi S.A. His expertise includes orchestrating significant transformational change within R&D and commercial functions to substantially increase speed and efficiency. He is noted for

fostering external collaboration and innovation. Prior to Sanofi, Dr. Insuasty was Global Head of Development, Neuroscience, and Ophthalmology at Novartis International AG.

Mr. Kunst was appointed to Philip Morris International Inc. in January 2019. He was formerly a Partner at Bain & Company for a decade, leading Bain's Healthcare Practice in EMEA, and has worked with a broad set of clients on issues related to growth strategy, commercial capability building, change management, and organizational effectiveness.

Mr. Li joined Philip Morris International Inc. in August 2019, having served in senior executive capacities at Harman International, a subsidiary of Samsung Electronics Co. Ltd. He is an entrepreneurial leader with a strong technical, product development, and operations background and vast experience in product design and innovation developed within world-class consumer electronics companies. As a forward thinker with a passion for design and technology, he has a proven track record of success in translating the voice of the customer into product development cycles.

Mr. Mishra joined Philip Morris International Inc. in September 2018. Previously, he was Managing Director, Portfolio Operations at Centerbridge Partners, a private equity firm, where he led commercial, operational, and digital transformation in various business sectors. He is a former Partner of McKinsey & Co, where he supported clients in their transformation projects as part of the Consumer Goods, Retail and Operations leadership team.

Ms. Salzman joined Philip Morris International Inc. in April 2018. One of the most awarded female marketing executives in North America, she was formerly Chief Executive Officer of Havas PR North America. At Havas, Ms. Salzman also co-created and chaired the Global Collective, the Havas PR operation across several continents. Ms. Salzman has authored/co-authored 15 books on topics ranging from current affairs to the commercial workplace.

Mr. Voegele started at Philip Morris International Inc. in February 2019. Prior to that, he held senior roles at the Adidas Group, most recently as Global Chief Information Officer and part of the core leadership team. He is recognized globally for having initiated the digital transformation of Adidas and making its IT organization and strategy consumer-centric and supportive of innovation. Mr. Voegele is noted for implementing large enterprise delivery projects within multinational organizations.

Mr. Volpetti's appointment at Philip Morris International Inc. commenced in June 2019. He served as Chief Marketing Officer at Luxottica Group S.p.A before joining Philip Morris International Inc. and has also held executive roles at the Procter & Gamble Company, including as Vice President of a global business unit. Mr. Volpetti is a globally acclaimed marketer with broad experience in commercial roles, having obtained a winning track record with consumers in both developed and developing markets. Mr. Volpetti specializes in consumer-centric marketing programs, business model transformation, digital acceleration, and disruptive innovation.

Mr. Verdeaux joined Philip Morris International Inc. in September 2020. He was a former Partner at Hering Schuppner, a strategic communications consulting firm. Prior to this position, he was Group International Policy Director at Vodafone and European Policy Director at Electricité De France (EDF). A veteran of international and domestic politics, he served as Deputy Head of Cabinet of the French President from 2008 to 2011 and has also held senior positions at the United Nations and the European Commission.

Codes of Conduct and Corporate Governance

We have adopted the Philip Morris International Code of Conduct, which complies with requirements set forth in Item 406 of Regulation S-K. This Code of Conduct applies to all of our employees, including our principal executive officer, principal financial officer, principal accounting officer or controller, and persons performing similar functions. We have also adopted a code of business conduct and ethics that applies to the members of our Board of Directors. These documents are available free of charge on our website at www.pmi.com.

In addition, we have adopted corporate governance guidelines and charters for our Audit, Finance, Compensation and Leadership Development, Product Innovation and Regulatory Affairs, Consumer Relationships and Regulation, and Nominating and Corporate Governance committees of the Board of Directors. All of these documents are available free of charge on our website at www.pmi.com. Any waiver granted by Philip Morris International Inc. to its principal executive officer, principal financial officer or controller, or any person performing similar functions under

the Code of Conduct, or certain amendments to the Code of Conduct, will be disclosed on our website at www.pmi.com.

The information on our website is not, and shall not be deemed to be, a part of this Report or incorporated into any other filings made with the SEC.

Also refer to *Board Operations and Governance—Committees of the Board*, *Election of Directors—Process for Nominating Directors* and *Election of Directors—Director Nominees* and *Stock Ownership Information—Delinquent Section 16(a) Reports* sections of the proxy statement.

Item 11. *Executive Compensation.*

Refer to *Compensation Discussion and Analysis, Compensation of Directors,* and *Pay Ratio* sections of the proxy statement.

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.*

The number of shares to be issued upon exercise or vesting and the number of shares remaining available for future issuance under PMI's equity compensation plans at December 31, 2020, were as follows:

	Number of Securities to be Issued upon Exercise of Outstanding Options and Vesting of RSUs and PSUs (a)	Weighted Average Exercise Price of Outstanding Options (b)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (excluding Securities reflected in column (a)) (c)
Equity compensation plans approved by stockholders	6,921,160 [1]	$ —	18,227,298

[1] Represents 4,098,240 shares of common stock that may be issued upon vesting of the restricted share units and 2,822,920 shares that may be issued upon vesting of the performance share units if maximum performance targets are achieved for each performance cycle. PMI has not granted options since the spin-off from Altria on March 28, 2008.

Also refer to *Stock Ownership Information—Ownership of Equity Securities* section of the proxy statement.

Item 13. *Certain Relationships and Related Transactions, and Director Independence.*

Refer to *Related Person Transactions and Code of Conduct* and *Election of Directors—Independence of Nominees* sections of the proxy statement.

Item 14. *Principal Accounting Fees and Services.*

Refer to *Audit Committee Matters* section of the proxy statement.

PART IV

Item 15. *Exhibits and Financial Statement Schedules.*

(a) Index to Consolidated Financial Statements and Schedules

	Page
Consolidated Statements of Earnings for the years ended December 31, 2020, 2019 and 2018	59
Consolidated Statements of Comprehensive Earnings for the years ended December 31, 2020, 2019 and 2018	60
Consolidated Balance Sheets at December 31, 2020 and 2019	61 - 62
Consolidated Statements of Cash Flows for the years ended December 31, 2020, 2019 and 2018	63 - 64
Consolidated Statements of Stockholders' (Deficit) Equity for the years ended December 31, 2020, 2019 and 2018	65
Notes to Consolidated Financial Statements	66 - 115
Report of Independent Registered Public Accounting Firm	116 - 118
Report of Management on Internal Control Over Financial Reporting	118

Schedules have been omitted either because such schedules are not required or are not applicable.

(b) The following exhibits are filed as part of this Report:

2.1	—	Distribution Agreement between Altria Group, Inc. and Philip Morris International Inc. dated January 30, 2008 (incorporated by reference to Exhibit 2.1 to the Registration Statement on Form 10 filed February 7, 2008).
3.1	—	Amended and Restated Articles of Incorporation of Philip Morris International Inc. (incorporated by reference to Exhibit 3.1 to the Registration Statement on Form 10 filed February 7, 2008).
3.2	—	Amended and Restated By-Laws of Philip Morris International Inc., effective as of March 5, 2020 (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed March 6, 2020).
4.1	—	Specimen Stock Certificate of Philip Morris International Inc. (incorporated by reference to Exhibit 4.1 to the Registration Statement on Form 10 filed February 7, 2008).
4.2	—	Indenture dated as of April 25, 2008, between Philip Morris International Inc. and HSBC Bank USA, National Association, as Trustee (incorporated by reference to Exhibit 4.3 to the Registration Statement on Form S-3, dated April 25, 2008).
4.3	—	Description of Common Stock.
4.4	—	Description of Debt Securities.

4.6	—	The Registrant agrees to furnish copies of any instruments defining the rights of holders of long-term debt of the Registrant and its consolidated subsidiaries that does not exceed 10 percent of the total assets of the Registrant and its consolidated subsidiaries to the Commission upon request.
10.1	—	Employee Matters Agreement between Altria Group, Inc. and Philip Morris International Inc., dated as of March 28, 2008 (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed March 31, 2008).
10.2	—	Intellectual Property Agreement between Philip Morris International Inc. and Philip Morris USA Inc., dated as of January 1, 2008 (incorporated by reference to Exhibit 10.4 to the Registration Statement on Form 10 filed March 5, 2008).
10.3	—	Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 15, 2013).

10.4	—	Extension Agreement, effective February 7, 2017, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders party thereto, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 30, 2017).
10.5	—	Extension Agreement, effective January 31, 2014, to Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders party thereto and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.3 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2014).
10.6	—	Extension Agreement, effective as of February 10, 2015, to Credit Agreement dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2015).
10.7	—	Amendment No. 1, dated as of July 20, 2015, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, The Royal Bank of Scotland plc, as resigning administrative agent, and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as successor administrative agent (incorporated by reference to Exhibit 10.52 to the Annual Report on Form 10-K for the year ended December 31, 2015).
10.8	—	Credit Agreement, dated as of October 1, 2015, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as Facility Agent, and Citibank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed October 5, 2015).
10.9	—	Amendment No. 2, effective as of February 9, 2016, to the Credit Agreement dated as of February 12, 2013, with the lenders named therein and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 28, 2016).
10.10	—	Extension Agreement, effective as of October 1, 2016, to the Credit Agreement dated as of October 1, 2015, among Philip Morris International Inc., lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as Facility Agent, and Citibank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 31, 2016).
10.11	—	Extension Agreement, effective as of October 1, 2017, to the Credit Agreement, dated as of October 1, 2015, among Philip Morris International Inc., the lenders party thereto and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as Facility Agent, and Citibank N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 29, 2017).
10.12	—	Extension Agreement, effective as of February 6, 2018, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2018).
10.13	—	Extension Agreement, effective as of February 5, 2019, to the Credit Agreement dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2019).
10.14	—	Amendment and Extension Agreement, effective February 4, 2020, among Philip Morris International Inc., each lender named therein and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 3, 2020).
10.15	—	Credit Agreement, dated as of February 10, 2020, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch, as Facility Agent, and Citibank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 11, 2020).

10.16	—	Philip Morris International Inc. Amended and Restated Automobile Policy, dated as of October 1, 2019.*
10.17	—	Philip Morris International Benefit Equalization Plan, amended and restated (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2019).*

10.18	—	Philip Morris International Inc. 2017 Performance Incentive Plan, effective May 3, 2017 (incorporated by reference to Exhibit B to the Definitive Proxy Statement filed on March 23, 2017).*
10.19	—	Pension Fund of Philip Morris in Switzerland (IC) (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2015).*
10.20	—	Summary of Supplemental Pension Plan of Philip Morris in Switzerland (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).*
10.21	—	Form of Restated Employee Grantor Trust Enrollment Agreement (Executive Trust Arrangement) (incorporated by reference to Exhibit 10.18 to the Registration Statement on Form 10 filed February 7, 2008).*
10.22	—	Form of Restated Employee Grantor Trust Enrollment Agreement (Secular Trust Arrangement) (incorporated by reference to Exhibit 10.19 to the Registration Statement on Form 10 filed February 7, 2008).*
10.23	—	Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors (as amended and restated as of January 1, 2018) (incorporated by reference to Exhibit 10.26 to the Annual Report on Form 10-K for the year ended December 31, 2017).*
10.24	—	Philip Morris International Inc. 2008 Deferred Fee Plan for Non-Employee Directors.*
10.25	—	Supplemental Letter to the Employment Agreement (as amended) with André Calantzopoulos. The Employment Agreement was previously filed as Exhibit 10.22 to the Registration Statement on Form 10 filed February 7, 2008 and is incorporated by reference to this Exhibit 10.25.*
10.26	—	Supplemental Letter to Employment Agreement with Marc S. Firestone (incorporated by reference to Exhibit 10.5 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017). The Employment Agreement was previously filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 and is incorporated by reference to this Exhibit 10.26.*
10.27	—	Employment Agreement with Martin G. King, effective June 1, 2020 (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2020).*
10.28	—	Early Retirement Agreement and Release with Marc S. Firestone, effective November 3, 2020.*
10.29	—	Supplemental Letter to the Employment Agreement (as amended) with Jacek Olczak (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2019. The Employment Agreement was previously filed as Exhibit 10.4 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, and is incorporated by reference to this Exhibit 10.29.*
10.30	—	Supplemental Letter to the Employment Agreement (as amended) with Miroslaw Zielinski (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2019). The Employment Agreement was previously filed as Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 and is incorporated by reference to this Exhibit 10.30.*
10.31	—	Early Retirement and Release Agreement with Miroslaw Zielinski, effective April 30, 2020 (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed May 1, 2020).*
10.32	—	Employment Agreement with Emmanuel Babeau, effective as of May 1, 2020 (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed March 2, 2020).*
10.33	—	Restricted Stock Unit Agreement (Vesting in Installments), between Philip Morris International Inc. and Emmanuel Babeau, effective as of May 1, 2020.*
10.34	—	Restricted Stock Unit Agreement, between Philip Morris International Inc. and Emmanuel Babeau, effective as of May 1, 2020.*
10.35	—	Performance Stock Unit Agreement, between Philip Morris International Inc. and Emmanuel Babeau, effective as of May 1, 2020.*
10.36	—	Agreement with Louis C. Camilleri (incorporated by reference to Exhibit 10.25 to the Registration Statement on Form 10 filed February 7, 2008).*

10.37	—	Amended and Restated Supplemental Management Employees' Retirement Plan (incorporated by reference to Exhibit 10.27 to the Annual Report on Form 10-K for the year ended December 31, 2008).*
10.38	—	Supplemental Equalization Plan, amended and restated as of June 29, 2015 (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).*
10.39	—	Form of Supplemental Equalization Plan Employee Grantor Trust Enrollment Agreement (Secular Trust) (incorporated by reference to Exhibit 10.31 to the Annual Report on Form 10-K for the year ended December 31, 2008).*
10.40	—	Form of Supplemental Equalization Plan Employee Grantor Trust Enrollment Agreement (Executive Trust) (incorporated by reference to Exhibit 10.32 to the Annual Report on Form 10-K for the year ended December 31, 2008).*
10.41	—	Philip Morris International Inc. Form of Indemnification Agreement with Directors and Executive Officers (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed September 18, 2009).*
10.42	—	Philip Morris International Inc. Tax Return Preparation Services Policy (incorporated by reference to Exhibit 10.51 to the Annual Report on Form 10-K for the year ended December 31, 2014).*
10.43	—	Form of Restricted Stock Unit Agreement (2018 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 13, 2018).*
10.44	—	Form of Performance Share Unit Agreement (2018 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 13, 2018).*
10.45	—	Form of Restricted Stock Unit Agreement (2019 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 12, 2019).*
10.46	—	Form of Performance Share Unit Agreement (2019 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 12, 2019).*
10.47	—	Form of Restricted Stock Unit Agreement (2020 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 11, 2020).*
10.48	—	Form of Performance Share Unit Agreement (2020 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 11, 2020).*
21	—	Subsidiaries of Philip Morris International Inc.
23	—	Consent of independent registered public accounting firm.
24	—	Powers of attorney.
31.1	—	Certification of the Registrant's Chief Executive Officer pursuant to Rule 13a-14(a)/ 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	—	Certification of the Registrant's Chief Financial Officer pursuant to Rule 13a-14(a)/ 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	—	Certification of the Registrant's Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	—	Certification of the Registrant's Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	—	XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.
101.SCH	—	XBRL Taxonomy Extension Schema.
101.CAL	—	XBRL Taxonomy Extension Calculation Linkbase.
101.DEF	—	XBRL Taxonomy Extension Definition Linkbase.
101.LAB	—	XBRL Taxonomy Extension Label Linkbase.
101.PRE	—	XBRL Taxonomy Extension Presentation Linkbase.
104	—	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

* Denotes management contract or compensatory plan or arrangement in which directors or executive officers are eligible to participate.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PHILIP MORRIS INTERNATIONAL INC.

By: /s/ ANDRÉ CALANTZOPOULOS

(André Calantzopoulos
Chief Executive Officer)

Date: February 9, 2021

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated:

Signature	Title	Date
/s/ ANDRÉ CALANTZOPOULOS (André Calantzopoulos)	Chief Executive Officer	February 9, 2021
/s/ EMMANUEL BABEAU (Emmanuel Babeau)	Chief Financial Officer	February 9, 2021
/s/ ANDREAS KURALI (Andreas Kurali)	Vice President and Controller	February 9, 2021
*MICHEL COMBES, WERNER GEISSLER, LISA A. HOOK, JENNIFER LI, JUN MAKIHARA, KALPANA MORPARIA, LUCIO A. NOTO, FREDERIK PAULSEN, ROBERT B. POLET	Directors	
*By: /s/ ANDRÉ CALANTZOPOULOS (André Calantzopoulos Attorney-in-fact)		February 9, 2021

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2019

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

Commission File Number: 001-33708

PHILIP MORRIS INTERNATIONAL INC.

(Exact name of registrant as specified in its charter)

Virginia **(State or other jurisdiction of incorporation or organization)**	**13-3435103** **(I.R.S. Employer Identification No.)**
120 Park Avenue **New York** **New York** **(Address of principal executive offices)**	**10017** **(Zip Code)**

917-663-2000
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, no par value	PM	New York Stock Exchange
2.000% Notes due 2020	PM20B	New York Stock Exchange
Floating Notes due 2020	PM20C	New York Stock Exchange
1.750% Notes due 2020	PM20A	New York Stock Exchange
4.500% Notes due 2020	PM20	New York Stock Exchange
1.875% Notes due 2021	PM21B	New York Stock Exchange
1.875% Notes due 2021	PM21C	New York Stock Exchange
4.125% Notes due 2021	PM21	New York Stock Exchange
2.900% Notes due 2021	PM21A	New York Stock Exchange
2.625% Notes due 2022	PM22A	New York Stock Exchange
2.375% Notes due 2022	PM22B	New York Stock Exchange
2.500% Notes due 2022	PM22	New York Stock Exchange
2.500% Notes due 2022	PM22C	New York Stock Exchange
2.625% Notes due 2023	PM23	New York Stock Exchange
2.125% Notes due 2023	PM23B	New York Stock Exchange
3.600% Notes due 2023	PM23A	New York Stock Exchange
2.875% Notes due 2024	PM24	New York Stock Exchange
2.875% Notes due 2024	PM24C	New York Stock Exchange
0.625% Notes due 2024	PM24B	New York Stock Exchange

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
3.250% Notes due 2024	PM24A	New York Stock Exchange
2.750% Notes due 2025	PM25	New York Stock Exchange
3.375% Notes due 2025	PM25A	New York Stock Exchange
2.750% Notes due 2026	PM26A	New York Stock Exchange
2.875% Notes due 2026	PM26	New York Stock Exchange
0.125% Notes due 2026	PM26B	New York Stock Exchange
3.125% Notes due 2027	PM27	New York Stock Exchange
3.125% Notes due 2028	PM28	New York Stock Exchange
2.875% Notes due 2029	PM29	New York Stock Exchange
3.375% Notes due 2029	PM29A	New York Stock Exchange
0.800% Notes due 2031	PM31	New York Stock Exchange
3.125% Notes due 2033	PM33	New York Stock Exchange
2.000% Notes due 2036	PM36	New York Stock Exchange
1.875% Notes due 2037	PM37A	New York Stock Exchange
6.375% Notes due 2038	PM38	New York Stock Exchange
1.450% Notes due 2039	PM39	New York Stock Exchange
4.375% Notes due 2041	PM41	New York Stock Exchange
4.500% Notes due 2042	PM42	New York Stock Exchange
3.875% Notes due 2042	PM42A	New York Stock Exchange
4.125% Notes due 2043	PM43	New York Stock Exchange
4.875% Notes due 2043	PM43A	New York Stock Exchange
4.250% Notes due 2044	PM44	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☑ No ☐

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☑

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☑ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☑ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☑ Accelerated filer ☐

Non-accelerated filer ☐ Smaller reporting company ☐

Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ☐ No ☑

As of June 30, 2019, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was approximately $122 billion based on the closing sale price of the common stock as reported on the New York Stock Exchange.

Class	Outstanding at January 31, 2020
Common Stock, no par value	1,555,911,930 shares

DOCUMENTS INCORPORATED BY REFERENCE

Document	Parts Into Which Incorporated
Portions of the registrant's definitive proxy statement for use in connection with its annual meeting of shareholders to be held on May 6, 2020, to be filed with the Securities and Exchange Commission ("SEC") on or about March 26, 2020.	Part III

TABLE OF CONTENTS

		Page
PART I		
Item 1.	Business	1
Item 1A.	Risk Factors	5
Item 1B.	Unresolved Staff Comments	10
Item 2.	Properties	10
Item 3.	Legal Proceedings	11
Item 4.	Mine Safety Disclosures	11
PART II		
Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	11
Item 6.	Selected Financial Data	14
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	15
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	52
Item 8.	Financial Statements and Supplementary Data	53
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	114
Item 9A.	Controls and Procedures	114
Item 9B.	Other Information	114
PART III		
Item 10.	Directors, Executive Officers and Corporate Governance	115
Item 11.	Executive Compensation	116
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	116
Item 13.	Certain Relationships and Related Transactions, and Director Independence	117
Item 14.	Principal Accounting Fees and Services	117
PART IV		
Item 15.	Exhibits and Financial Statement Schedules	118
Signatures		123

In this report, "PMI," "we," "us" and "our" refers to Philip Morris International Inc. and its subsidiaries.

Trademarks and service marks in this report are the registered property of, or licensed by, the subsidiaries of Philip Morris International Inc. and are italicized.

PART I

Item 1. *Business.*

General Development of Business

General

Philip Morris International Inc. is a Virginia holding company incorporated in 1987. We are a leading international tobacco company engaged in the manufacture and sale of cigarettes, smoke-free products and associated electronic devices and accessories, and other nicotine-containing products in markets outside the United States of America. In addition, we ship a version of our Platform 1 device and its consumables authorized by the U.S. Food and Drug Administration ("FDA") to Altria Group, Inc., for sale in the United States under license.

We are leading a transformation in the tobacco industry to create a smoke-free future, based on a new category of reduced-risk products that, while not risk free, are a much better choice than continuing to smoke. Our goal is to ultimately replace cigarettes with smoke-free products to the benefit of adults who would otherwise continue to smoke, society, the company and its shareholders.

Reduced-risk products ("RRPs") is the term we use to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continuing smoking. We have a range of RRPs in various stages of development, scientific assessment and commercialization. Because our RRPs do not burn tobacco, they produce an aerosol that contains far lower quantities of harmful and potentially harmful constituents than found in cigarette smoke. Through multidisciplinary capabilities in product development, state-of-the-art facilities and scientific substantiation, we aim to ensure that our RRPs meet adult consumer preferences and rigorous regulatory requirements.

Our *IQOS* smoke-free product brand portfolio includes heated tobacco and nicotine-containing vapor products. Our leading smoke-free platform ("Platform 1") is a precisely controlled device into which a specially designed heated tobacco unit is inserted and heated to generate an aerosol. We market our heated tobacco units under the brand names *HEETS*, *HEETS Marlboro* and *HEETS FROM MARLBORO*, defined collectively as *HEETS*, as well as *Marlboro HeatSticks* and *Parliament HeatSticks*. Platform 1 was first introduced in Nagoya, Japan, in 2014. As of December 31, 2019, Platform 1 is available for sale in 52 markets in key cities or nationwide.

Our cigarettes are sold in more than 180 markets, and in many of these markets they hold the number one or number two market share position. We have a wide range of premium, mid-price and low-price brands. Our portfolio comprises both international and local brands and is led by *Marlboro*, the world's best-selling international cigarette, which accounted for approximately 37% of our total 2019 cigarette shipment volume. *Marlboro* is complemented in the premium-price category by *Parliament*. Our other leading international cigarette brands are *Bond Street, Chesterfield, L&M*, *Lark* and *Philip Morris.* These seven international cigarette brands contributed approximately 78% of our cigarette shipment volume in 2019. We also own a number of important local cigarette brands, such as *Dji Sam Soe*, *Sampoerna A* and *Sampoerna U* in Indonesia, and *Fortune* and *Jackpot* in the Philippines.

Source of Funds — Dividends

We are a legal entity separate and distinct from our direct and indirect subsidiaries. Accordingly, our right, and thus the right of our creditors and stockholders, to participate in any distribution of the assets or earnings of any subsidiary is subject to the prior rights of creditors of such subsidiary, except to the extent that claims of our company itself as a creditor may be recognized. As a holding company, our principal sources of funds, including funds to make payment on our debt securities, are from the receipt of dividends and repayment of debt from our subsidiaries. Our principal wholly owned and majority-owned subsidiaries currently are not limited by long-term debt or other agreements in their ability to pay cash dividends or to make other distributions with respect to their common stock that are otherwise compliant with law.

Description of Business

We manage our business in six operating segments as follows:

- The European Union Region (“EU”) is headquartered in Lausanne, Switzerland, and covers all the European Union countries and also Switzerland, Norway, Iceland and the United Kingdom;

- The Eastern Europe Region (“EE”) is also headquartered in Lausanne and includes Southeast Europe, Central Asia, Ukraine, Israel and Russia;

- The Middle East & Africa Region ("ME&A") is also headquartered in Lausanne and covers the African continent, the Middle East, Turkey and our international duty free business;

- The South & Southeast Asia Region ("S&SA") is headquartered in Hong Kong and includes Indonesia, the Philippines and other markets in this region;

- The East Asia & Australia Region ("EA&A") is also headquartered in Hong Kong and includes Australia, Japan, South Korea, the People's Republic of China and other markets in this region, as well as Malaysia and Singapore; and

- The Latin America & Canada Region ("LA&C") is headquartered in New York and covers the South American continent, Central America, Mexico, the Caribbean and Canada. LA&C also includes transactions under license with Altria Group, Inc., for the distribution of our Platform 1 product in the United States.

As of March 22, 2019, we deconsolidated the financial results of our Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH") from our financial statements. For further details, see Item 8, Note 22. *Deconsolidation of RBH*.

Following the deconsolidation of our Canadian subsidiary, we will continue to report the volume of brands sold by RBH for which other PMI subsidiaries are the trademark owners. These include *HEETS*, *Next*, *Philip Morris* and *Rooftop*, which together accounted for approximately 40% of RBH's total shipment volume in 2018.

References to total international market, defined as worldwide cigarette and heated tobacco unit volume excluding the United States, total industry, total market and market shares in this Form 10-K are our estimates for tax-paid products based on the latest available data from a number of internal and external sources and may, in defined instances, exclude the People's Republic of China and/or our duty free business. In addition, to reflect the deconsolidation of RBH, effective March 22, 2019, PMI's total market share has been restated for previous periods.

Our total shipments, including cigarettes and heated tobacco units, decreased by 2.0% in 2019 to 766.4 billion units. We estimate that international industry volumes, including cigarettes and heated tobacco units, were approximately 5.1 trillion units in 2019, a 0.9% decrease from 2018. Excluding the People's Republic of China ("PRC"), we estimate that international cigarette and heated tobacco unit volume was 2.7 trillion units in 2019, a 2.0% decrease from 2018. We estimate that our reported share of the international market (which is defined as worldwide cigarette and heated tobacco unit volume, excluding the United States of America) was approximately 15.1% in 2019, 15.2% in 2018 and 15.1% in 2017. Excluding the PRC, we estimate that our reported share of the international market was approximately 28.4%, 28.3%, and 27.8% in 2019, 2018 and 2017, respectively.

Shipments of our principal cigarette brand, *Marlboro*, decreased by 0.6% in 2019 and represented approximately 10.0% of the international cigarette market, excluding the PRC, in 2019, 9.7% in 2018 and 9.7% in 2017.

Total shipment volume of heated tobacco units reached 59.7 billion units in 2019, up from 41.4 billion units in 2018.

We have a market share of at least 15% and, in a number of instances, substantially more than 15%, in approximately 95 markets, including Algeria, Argentina, Australia, Austria, Belgium, Brazil, the Czech Republic, Egypt, France, Germany, Hong Kong, Hungary, Indonesia, Israel, Italy, Japan, Kazakhstan, Korea, Kuwait, Mexico, the Netherlands, the Philippines, Poland, Portugal, Russia, Saudi Arabia, the Slovak Republic, Spain, Switzerland, Turkey and Ukraine.

Distribution & Sales

Our main types of distribution are tailored to the characteristics of each market and are often used simultaneously:

- Direct sales and distribution, where we have set up our own distribution selling directly to the retailers (including gas stations and other key accounts);
- Distribution through independent distributors that often distribute other fast-moving consumer goods and are responsible for distribution in a particular market;
- Exclusive zonified distribution, where the distributors are dedicated to us in tobacco products distribution and assigned to exclusive territories within a market;
- Distribution through national or regional wholesalers that then supply the retail trade; and
- Our own brand retail and e-commerce infrastructures for our RRP products and accessories.

Competition

We are subject to highly competitive conditions in all aspects of our business. We compete primarily on the basis of product quality, brand recognition, brand loyalty, taste, R&D, innovation, packaging, customer service, marketing, advertising and retail price and, increasingly, adult smoker willingness to convert to our RRPs. In the combustible product category, we predominantly sell American blend cigarette brands, such as *Marlboro*, *L&M*, *Parliament, Philip Morris* and *Chesterfield*, which are the most popular across many of our markets. In the RRP product category, we predominantly sell Platform 1 devices and heated tobacco units under the *IQOS* brand umbrella. We seek to compete in all profitable retail price categories, although our brand portfolio is weighted towards the premium-price category.

The competitive environment and our competitive position can be significantly influenced by weak economic conditions, erosion of consumer confidence, competitors' introduction of lower-price products or innovative products, higher tobacco product taxes, higher absolute prices and larger gaps between retail price categories, and product regulation that diminishes the ability to differentiate tobacco products and restricts adult consumer access to truthful and non-misleading information about our RRPs. Competitors include three large international tobacco companies, new market entrants, particularly with respect to innovative products, several regional and local tobacco companies and, in some instances, state-owned tobacco enterprises, principally in Algeria, Egypt, the PRC, Taiwan, Thailand and Vietnam. Industry consolidation and privatizations of state-owned enterprises have led to an overall increase in competitive pressures. Some competitors have different profit and volume objectives, and some international competitors are susceptible to changes in different currency exchange rates. Certain new market entrants may alienate consumers from innovative products through inappropriate marketing campaigns and messaging and inferior product satisfaction, while not relying on scientific substantiation based on appropriate R&D protocols and standards. The growing use of digital media could increase the speed and extent of the dissemination of inaccurate and misleading information about our RRPs.

Procurement and Raw Materials

We purchase tobacco leaf of various types, grades and styles throughout the world, mostly through independent tobacco suppliers. In 2019, we also contracted directly with farmers in several countries, including Argentina, Brazil, Colombia, Ecuador, Italy, Pakistan, the Philippines and Poland. In 2019, direct sourcing from farmers represented approximately 23% of PMI's global leaf requirements. The largest supplies of tobacco leaf are sourced from Argentina, Brazil, China, Italy, Indonesia (mostly for domestic use in kretek products), Malawi, Mozambique, the Philippines, Turkey and the United States.

We believe that there is an adequate supply of tobacco leaf in the world markets to satisfy our current and anticipated production requirements.

In addition to tobacco leaf, we purchase a wide variety of direct materials from a total of approximately 400 suppliers. In 2019, our top ten suppliers of direct materials combined represented approximately 50% of our total direct materials purchases. The three most significant direct materials that we purchase are printed paper board used

in packaging, acetate tow used in filter making and fine paper used in the manufacturing of cigarettes and heated tobacco units. In addition, the adequate supply and procurement of cloves are of particular importance to our Indonesian business.

The adequate supply chain for our RRP portfolio, including the supply of electronic devices, is important to our business. We work with two electronics manufacturing service providers for the supply of our Platform 1 devices and a small number of other providers for other products in our RRP portfolio and related accessories. Although we work closely with these service providers on monitoring their

production capability and financial health, the commercialization of our RRPs could be adversely affected if they are unable to meet their commitments. The production of our RRP portfolio requires various metals, and we believe that there is an adequate supply of such metals in the world markets to satisfy our current and anticipated production requirements. However, some components and materials necessary for the production of our RRPs are obtained from single or limited sources, and can be subject to industry-wide shortages and price fluctuations. Our inability to secure an adequate supply of such components and materials could negatively impact the commercialization of our RRPs.

Our *IQOS* devices are subject to product warranties, which are described in more detail in Item 8. *Financial Statements and Supplementary Data* of this Annual Report on Form 10-K ("Item 8") in Note 5. *Product Warranty* to our consolidated financial statements. We discuss our RRP products in more detail in Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations* of this Annual Report on Form 10-K ("Item 7") in *Business Environment—Reduced-Risk Products*.

Business Environment

Information called for by this Item is hereby incorporated by reference to the paragraphs in Item 7, *Business Environment*.

Other Matters

Customers

As described in more detail in "*Distribution & Sales*" above, in many of our markets we sell our products to distributors. In 2019, sales to a distributor in the European Union Region and a distributor in the East Asia & Australia Region each amounted to 10 percent or more of our consolidated net revenues. See Item 8, Note 12. *Segment Reporting* for more information. We believe that none of our business segments is dependent upon a single customer or a few customers, the loss of which would have a material adverse effect on our consolidated results of operations. In some of our markets, particularly in the European Union and in the East Asia & Australia Regions, a loss of a distributor may result in a temporary market disruption.

Employees

At December 31, 2019, we employed approximately 73,500 people worldwide, including full-time, temporary and part-time staff. Our businesses are subject to a number of laws and regulations relating to our relationship with our employees. Generally, these laws and regulations are specific to the location of each business. In addition, in accordance with European Union requirements, we have established a European Works Council composed of management and elected members of our workforce. We believe that our relations with our employees and their representative organizations are excellent.

Information About Our Executive Officers

The disclosure regarding executive officers is hereby incorporated by reference to the discussion under the heading "Information about our Executive Officers as of February 6, 2020" in Part III, Item 10. *Directors, Executive Officers and Corporate Governance* of this Annual Report on Form 10-K ("Item 10").

Intellectual Property

Our trademarks are valuable assets, and their protection and reputation are essential to us. We own the trademark rights to all of our principal brands, including *Marlboro*, *HEETS* and *IQOS*, or have the right to use them in all countries where we use them.

In addition, we have a large number of granted patents and pending patent applications worldwide. Our patent portfolio, as a whole, is material to our business. However, no one patent, or group of related patents, is material to us. We also have registered industrial designs, as well as unregistered proprietary trade secrets, technology, know-how, processes and other unregistered intellectual property rights.

Effective January 1, 2008, PMI entered into an Intellectual Property Agreement with Philip Morris USA Inc. ("PM USA"), a wholly owned subsidiary of Altria Group, Inc. The Intellectual Property Agreement allocates ownership of jointly funded intellectual property as follows:

- PMI owns all rights to jointly funded intellectual property outside the United States, its territories and possessions; and

- PM USA owns all rights to jointly funded intellectual property in the United States, its territories and possessions.

The parties agreed to submit disputes under the Intellectual Property Agreement first to negotiation between senior executives and then to binding arbitration.

Seasonality

Our business segments are not significantly affected by seasonality, although in certain markets cigarette consumption trends may rise during the summer months due to outdoor use, longer daylight, and tourism.

Environmental Regulation

We are subject to international, national and local environmental laws and regulations in the countries in which we do business. We have specific programs across our business units designed to meet applicable environmental compliance requirements and reduce our carbon footprint and wastage as well as water and energy consumption. We report externally about our climate change mitigation strategy, together with associated targets and results in reducing our carbon footprint, through CDP (formerly, the Carbon Disclosure Project), the leading international non-governmental organization assessing the work of thousands of companies worldwide in the area of environmental impact, including climate change. Our environmental and occupational health and safety management system includes policies, standard practices and procedures at all our manufacturing centers. We also conduct regular safety assessments at our offices, warehouses and car fleet organizations. Furthermore, we have engaged an external certification body to validate the effectiveness of this management system at our manufacturing centers around the world, in accordance with internationally recognized standards for safety and environmental management. The environmental performance data we report externally is also verified by a qualified third party. Our subsidiaries expect to continue to make investments in order to drive improved performance and maintain compliance with environmental laws and regulations. We assess and report the compliance status of all our legal entities on a regular basis. Based on the management and controls we have in place and our review of climate change risks (both physical and regulatory), environmental expenditures have not had, and are not expected to have, a material adverse effect on our consolidated results of operations, capital expenditures, financial position, earnings or competitive position.

Available Information

We are required to file with the SEC annual, quarterly and current reports, proxy statements and other information required by the Securities Exchange Act of 1934, as amended (the "Exchange Act"). The SEC maintains an Internet website at http://www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, from which investors can electronically access our SEC filings.

We make available free of charge on, or through, our website at www.pmi.com our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. Investors can access our filings with the SEC by visiting www.pmi.com.

The information on our website is not, and shall not be deemed to be, a part of this report or incorporated into any other filings we make with the SEC.

Item 1A. *Risk Factors.*

The following risk factors should be read carefully in connection with evaluating our business and the forward-looking statements contained in this Annual Report on Form 10-K. Any of the following risks could materially adversely affect our business, our operating results, our financial condition and the actual outcome of matters as to which forward-looking statements are made in this Annual Report on Form 10-K.

Forward-Looking and Cautionary Statements

We may from time to time make written or oral forward-looking statements, including statements contained in this Annual Report on Form 10-K and other filings with the SEC, in reports to stockholders and in press releases and investor webcasts. You can identify these forward-looking statements by use of words such as "strategy," "expects," "continues," "plans," "anticipates," "believes," "will," "estimates," "intends," "projects," "goals," "targets" and other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts.

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Our RRPs constitute a new product category in its early stages that is less predictable than our mature cigarette business. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from those anticipated, estimated or projected. Investors should bear this in mind as they consider forward-looking statements and whether to invest in or remain invested in our securities. In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, we are identifying important factors that, individually or in the aggregate, could cause actual results and outcomes to differ materially from those contained in any forward-looking statements made by us; any such statement is qualified by reference to the following cautionary statements. We elaborate on these and other risks we face throughout this document, particularly in Item 7, *Business Environment*. You should understand that it is not possible to predict or identify all risk factors. Consequently, you should not consider the following to be a complete discussion of all potential risks or uncertainties. We do not undertake to update any forward-looking statement that we may make from time to time, except in the normal course of our public disclosure obligations.

Risks Related to Our Business and Industry

- **Consumption of tax-paid cigarettes continues to decline in many of our markets.**

This decline is due to multiple factors, including increased taxes and pricing, governmental actions, the diminishing social acceptance of smoking, continuing economic and geopolitical uncertainty, and the continuing prevalence of illicit products. These factors and their potential consequences are discussed more fully below and in Item 7, *Business Environment*.

- **Cigarettes are subject to substantial taxes. Significant increases in cigarette-related taxes have been proposed or enacted and are likely to continue to be proposed or enacted in numerous jurisdictions. These tax increases may disproportionately affect our profitability and make us less competitive versus certain of our competitors.**

Tax regimes, including excise taxes, sales taxes and import duties, can disproportionately affect the retail price of cigarettes versus other combustible tobacco products, or disproportionately affect the relative retail price of our cigarette brands versus cigarette brands manufactured by certain of our competitors. Because our portfolio is weighted toward the premium-price cigarette category, tax regimes based on sales price can place us at a competitive disadvantage in certain markets. As a result, our volume and profitability may be adversely affected in these markets.

Increases in cigarette taxes are expected to continue to have an adverse impact on our sales of cigarettes, due to resulting lower consumption levels, a shift in sales from manufactured cigarettes to other combustible tobacco products and from the premium-price to the mid-price or low-price cigarette categories, where we may be under-represented, from local sales to legal cross-border purchases of lower price products, or to illicit products such as contraband, counterfeit and "illicit whites."

- **Our business faces significant governmental action aimed at increasing regulatory requirements with the goal of reducing or preventing the use of tobacco products.**

Governmental actions, combined with the diminishing social acceptance of smoking and private actions to restrict smoking, have resulted in reduced industry volume in many of our markets, and we expect that such factors will continue to reduce consumption levels and will increase down-trading and the risk of counterfeiting, contraband, "illicit whites" and legal cross-border purchases. Significant regulatory developments will continue to take place over the next few years in most of our markets, driven principally by the World Health Organization's Framework Convention on Tobacco Control ("FCTC"). Since it came into force in 2005, the FCTC has led to increased efforts by tobacco control advocates and public health organizations to promote increasingly restrictive regulatory measures on the marketing and sale of tobacco products to adult smokers. Regulatory initiatives that have been proposed, introduced or enacted include:

- restrictions on or licensing of outlets permitted to sell cigarettes;

- the levying of substantial and increasing tax and duty charges;
- restrictions or bans on advertising, marketing and sponsorship;
- the display of larger health warnings, graphic health warnings and other labeling requirements;
- restrictions on packaging design, including the use of colors, and plain packaging;
- restrictions on packaging and cigarette formats and dimensions;
- restrictions or bans on the display of tobacco product packaging at the point of sale and restrictions or bans on cigarette vending machines;

- requirements regarding testing, disclosure and performance standards for tar, nicotine, carbon monoxide and other smoke constituents;
- disclosure, restrictions, or bans of tobacco product ingredients;
- increased restrictions on smoking in public and work places and, in some instances, in private places and outdoors;
- regulation, restrictions or prohibitions of novel tobacco or nicotine-containing products;
- elimination of duty free sales and duty free allowances for travelers;
- encouraging litigation against tobacco companies; and
- excluding tobacco companies from transparent public dialogue regarding public health and other policy matters.

Our financial results could be significantly affected by regulatory initiatives resulting in a significant decrease in demand for our brands, in particular requirements that lead to a commoditization of tobacco products or impede adult consumers' ability to convert to our RRPs, as well as any significant increase in the cost of complying with new regulatory requirements.

- **Litigation related to tobacco use and exposure to environmental tobacco smoke could substantially reduce our profitability and could severely impair our liquidity.**

There is litigation related to tobacco products pending in certain jurisdictions. Damages claimed in some tobacco-related litigation are significant and, in certain cases in Brazil, Canada, and Nigeria, range into the billions of U.S. dollars. We anticipate that new cases will continue to be filed. The FCTC encourages litigation against tobacco product manufacturers. It is possible that our consolidated results of operations, cash flows or financial position could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. See Item 8, Note 18. *Contingencies* to our consolidated financial statements for a discussion of pending litigation and Item 7, *Business Environment—Reduced-Risk Products (RRPs)—Legal Challenges to RRPs.*

- **We face intense competition, and our failure to compete effectively could have a material adverse effect on our profitability and results of operations.**

We compete primarily on the basis of product quality, brand recognition, brand loyalty, taste, R&D, innovation, packaging, customer service, marketing, advertising and retail price and, increasingly, adult smoker willingness to convert to our RRPs. We are subject to highly competitive conditions in all aspects of our business. The competitive environment and our competitive position can be significantly influenced by weak economic conditions, erosion of consumer confidence, competitors' introduction of lower-price products or innovative products, higher tobacco product taxes, higher absolute prices and larger gaps between retail price categories, and product regulation that diminishes the ability to differentiate tobacco products and restricts adult consumer access to truthful and non-misleading information about our RRPs. Competitors include three large international tobacco companies, new market entrants, particularly with respect to innovative products, several regional and local tobacco companies and, in some instances, state-owned tobacco enterprises, principally in Algeria, Egypt, the PRC, Taiwan, Thailand and Vietnam. Industry consolidation and privatizations of state-owned enterprises have led to an overall increase in competitive pressures. Some competitors have different profit and volume objectives, and some international competitors are susceptible to changes in different currency exchange rates. Certain new market entrants may alienate consumers from innovative products through inappropriate marketing campaigns and messaging and inferior product satisfaction, while not relying on scientific substantiation based on appropriate R&D protocols and standards. The growing use of digital media could increase the speed and extent of the dissemination of inaccurate and misleading information about our RRPs.

- **Because we have operations in numerous countries, our results may be influenced by economic, regulatory and political developments, natural disasters, pandemics or conflicts.**

Some of the countries in which we operate face the threat of civil unrest and can be subject to regime changes. In others, nationalization, terrorism, conflict and the threat of war may have a significant impact on the business environment. Natural disasters, pandemics, economic, political, regulatory or other developments could disrupt our supply chain, manufacturing capabilities or distribution capabilities. In addition, such developments could lead to loss of property or equipment that are critical to our business in certain markets and difficulty in staffing and managing our operations, which could reduce our volumes, revenues and net earnings.

In certain markets, we are dependent on governmental approvals of various actions such as price changes, and failure to obtain such approvals could impair growth of our profitability.

In addition, despite our high ethical standards and rigorous control and compliance procedures aimed at preventing and detecting unlawful conduct, given the breadth and scope of our international operations, we may not be able to detect all potential improper or unlawful conduct by our employees and partners.

- **We may be unable to anticipate changes in adult consumer preferences.**

Our business is subject to changes in adult consumer preferences, which may be influenced by local economic conditions. To be successful, we must:

- promote brand equity successfully;
- anticipate and respond to new adult consumer trends;
- develop new products and markets and broaden brand portfolios;
- improve productivity;
- convince adult smokers to convert to our RRPs;
- ensure adequate production capacity to meet demand for our products; and
- be able to protect or enhance margins through price increases.

In periods of economic uncertainty, adult consumers may tend to purchase lower-price brands, and the volume of our premium-price and mid-price brands and our profitability could suffer accordingly. Such down-trading trends may be reinforced by regulation that limits branding, communication and product differentiation.

- **The financial and business performance of our reduced-risk products is less predictable than our cigarette business.**

Our RRPs are novel products in a new category, and the pace at which adult smokers adopt them may vary, depending on the competitive, regulatory, fiscal and cultural environment, and other factors in a specific market. There may be periods of accelerated growth and periods of slower growth for these products, the timing and drivers of which may be more difficult for us to predict versus our mature cigarette business. The impact of this lower predictability on our projected results for a specific period may be significant, particularly during the early stages of this new product category.

- **We lose revenues as a result of counterfeiting, contraband, cross-border purchases, "illicit whites," non-tax-paid volume produced by local manufacturers, and counterfeiting of our Platform 1 device and heated tobacco units.**

Large quantities of counterfeit cigarettes are sold in the international market. We believe that *Marlboro* is the most heavily counterfeited international cigarette brand, although we cannot quantify the revenues we lose as a result of this activity. In addition, our revenues are reduced by contraband, legal cross-border purchases, "illicit whites" and non-tax-paid volume produced by local manufacturers. Our revenues and consumer satisfaction with our Platform 1 device and heated tobacco units may be adversely affected by counterfeit products that do not meet our product quality standards and scientific validation procedures.

- **From time to time, we are subject to governmental investigations on a range of matters.**

Investigations include allegations of contraband shipments of cigarettes, allegations of unlawful pricing activities within certain markets, allegations of underpayment of income taxes, customs duties and/or excise taxes, allegations of false and misleading usage of descriptors, allegations of unlawful advertising, and allegations of unlawful labor practices. We cannot predict the outcome of those investigations or whether additional investigations may be commenced, and it is possible that our business could be materially affected by an unfavorable outcome of pending or future investigations. See Item, 8, Note 18. *Contingencies—Other Litigation* and Item 7, *Business Environment—Governmental Investigations* for a description of certain governmental investigations to which we are subject.

- **We may be unsuccessful in our attempts to introduce reduced-risk products, and regulators may not permit the commercialization of these products or the communication of scientifically substantiated risk-reduction claims.**

Our key strategic priorities are: to develop and commercialize products that present less risk of harm to adult smokers who switch to those products versus continued smoking; and to convince current adult smokers who would otherwise continue to smoke to switch to those RRPs. For our efforts to be successful, we must: develop RRPs that such adult smokers find acceptable alternatives to smoking; conduct rigorous scientific studies to substantiate that they reduce exposure to harmful and potentially harmful constituents in smoke and, ultimately, that these products present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to them versus continued smoking; and effectively advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs, including communication of scientifically substantiated information to enable adult smokers to make better consumer choices. We might not succeed in our efforts. If we do not succeed, but others do, or if heat-not-burn products are inequitably regulated compared to other RRP categories without regard to the totality of the scientific evidence available for such products, we may be at a competitive disadvantage. In addition, actions of some market entrants, such as the inappropriate marketing of e-vapor products to youth, as well as alleged health consequences associated with the use of certain e-vapor products, may unfavorably impact public opinion and/or mischaracterize all e-vapor products or other RRPs to consumers, regulators and policy makers

without regard to the totality of scientific evidence for specific products. This may impede our efforts to advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs. We cannot predict whether regulators will permit the sale and/or marketing of RRPs with scientifically substantiated risk-reduction claims. Such restrictions could limit the success of our RRPs. Moreover, the FDA's premarket tobacco product authorization of a version of our Platform 1 product is subject to strict marketing, reporting and other requirements and is not a guarantee that the product will remain authorized, particularly if there is a significant uptake in youth initiation.

- **We may be unsuccessful in our efforts to differentiate reduced-risk products and cigarettes with respect to taxation.**

To date, we have been largely successful in demonstrating to regulators that our RRPs are not cigarettes, and as such they are generally taxed either as a separate category or as other tobacco products, which typically yields more favorable tax rates than cigarettes. If we cease to be successful in these efforts, RRP unit margins may be adversely affected.

- **Our reported results could be adversely affected by unfavorable currency exchange rates, and currency devaluations could impair our competitiveness.**

We conduct our business primarily in local currency and, for purposes of financial reporting, the local currency results are translated into U.S. dollars based on average exchange rates prevailing during a reporting period. During times of a strengthening U.S. dollar, our reported net revenues, operating income and EPS will be reduced because the local currency translates into fewer U.S. dollars. During periods of local economic crises, foreign currencies may be devalued significantly against the U.S. dollar, reducing our margins. Actions to recover margins may result in lower volume and a weaker competitive position.

- **Changes in the earnings mix and changes in tax laws may result in significant variability in our effective tax rates. Our ability to receive payments from foreign subsidiaries or to repatriate royalties and dividends could be restricted by local country currency exchange controls.**

The Tax Cuts and Jobs Act that was signed into law in December 2017 constitutes a major change to the U.S. tax system. Our estimated impact of the Tax Cuts and Jobs Act is based on management's current interpretations, and our analysis is ongoing. Our final tax liability may be materially different from current estimates due to developments such as implementing regulations and clarifications. In future periods, our effective tax rate and our ability to recover deferred tax assets could be subject to additional uncertainty as a result of such developments. Furthermore, changes in the earnings mix or applicable foreign tax laws may result in significant variability in our effective tax rates. Because we are a U.S. holding company, our most significant source of funds is distributions from our non-U.S. subsidiaries. Certain countries in which we operate have adopted or could institute currency exchange controls that limit or prohibit our local subsidiaries' ability to convert local currency into U.S. dollars or to make payments outside the country. This could subject us to the risks of local currency devaluation and business disruption.

- **Our ability to grow profitability may be limited by our inability to introduce new products, enter new markets or improve our margins through higher pricing and improvements in our brand and geographic mix.**

Our profit growth may suffer if we are unable to introduce new products or enter new markets successfully, to raise prices or to improve the proportion of our sales of higher margin products and in higher margin geographies.

- **We may be unable to expand our brand portfolio through successful acquisitions or the development of strategic business relationships.**

One element of our growth strategy is to strengthen our brand portfolio and market positions through selective acquisitions and the development of strategic business relationships. Acquisition and strategic business development opportunities are limited and present risks of failing to achieve efficient and effective integration, strategic objectives and anticipated revenue improvements and cost savings. There is no assurance that we will be able to acquire

attractive businesses on favorable terms, or that future acquisitions or strategic business developments will be accretive to earnings.

- **Government mandated prices, production control programs, shifts in crops driven by economic conditions and the impact of climate change may increase the cost or reduce the quality of the tobacco and other agricultural products used to manufacture our products.**

As with other agricultural commodities, the price of tobacco leaf and cloves can be influenced by imbalances in supply and demand, and crop quality can be influenced by variations in weather patterns, including those caused by climate change. Tobacco production in certain countries is subject to a variety of controls, including government mandated prices and production control programs. Changes in the

patterns of demand for agricultural products could cause farmers to produce less tobacco or cloves. Any significant change in tobacco leaf and clove prices, quality and quantity could affect our profitability and our business.

- **Our ability to achieve our strategic goals may be impaired if we fail to attract and retain the best global talent.**

To be successful, we must continue transforming our culture and ways of working, align our talent with our business needs, innovate and transform to a consumer-centric business. We compete for talent, including in areas that are new to us, such as digital and technical solutions, with companies in the consumer products, technology and other sectors that enjoy greater societal acceptance. As a result, we may be unable to attract and retain the best global talent with the right degree of diversity, experience and skills to achieve our strategic goals.

- **The failure of our information systems to function as intended or their penetration by outside parties with the intent to corrupt them or our failure to comply with privacy laws and regulations could result in business disruption, litigation and regulatory action, and loss of revenue, assets or personal or other confidential data.**

We use information systems to help manage business processes, collect and interpret data and communicate internally and externally with employees, suppliers, consumers, customers and others. Some of these information systems are managed by third-party service providers. We have backup systems and business continuity plans in place, and we take care to protect our systems and data from unauthorized access. Nevertheless, failure of our systems to function as intended, or penetration of our systems by outside parties intent on extracting or corrupting information or otherwise disrupting business processes, could place us at a competitive disadvantage, result in a loss of revenue, assets or personal or other sensitive data, litigation and regulatory action, cause damage to our reputation and that of our brands and result in significant remediation and other costs. Failure to protect personal data, respect the rights of data subjects, and adhere to strict cybersecurity protocols could subject us to substantial fines and other legal challenges under regulations such as the EU General Data Protection Regulation. As we are increasingly relying on digital platforms in our business, the magnitude of these risks is likely to increase.

- **We may be unable to adequately protect our intellectual property rights, and disputes relating to intellectual property rights could harm our business.**

Our intellectual property rights are valuable assets, and their protection is important to our business. If the steps we take to protect our intellectual property rights globally, including through a combination of trademark, design, patent and other intellectual property rights, are inadequate, or if others infringe or misappropriate our intellectual property rights, notwithstanding legal protection, our business could suffer. Intellectual property rights of third parties may limit our ability to introduce new products or improve the quality of existing products in one or more markets. Competitors or other third parties may claim that we infringe their intellectual property rights. Any such claims, regardless of merit, could divert management's attention, be costly, disruptive, time-consuming and unpredictable and expose us to litigation costs and damages, and impede our ability to manufacture and sell new products or improve existing products. If, as a result, we are unable to manufacture or sell our RRPs or improve their quality in one or more markets, our ability to convert adult smokers to our RRPs in such markets would be adversely affected.

- **We may be required to replace third-party contract manufacturers or service providers with our own resources.**

In certain instances, we contract with third parties to manufacture some of our products or product parts or to provide other services. We may be unable to renew these agreements on satisfactory terms for numerous reasons, including government regulations. Accordingly, our costs may increase significantly if we must replace such third parties with our own resources.

Item 1B. *Unresolved Staff Comments.*

None.

Item 2. *Properties.*

We own or lease various manufacturing, office and research and development facilities in locations primarily outside the United States. We own properties in Switzerland where our operations center and state-of-the-art research and development facility are located.

At December 31, 2019, we operated and owned a total of 38 manufacturing facilities across our six operating segments. Among them, 7 factories produced heated tobacco units.

In 2019, certain facilities each manufactured over 30 billion units (cigarettes and heated tobacco units combined). The largest manufacturing facilities, in terms of volume, are located in Indonesia (S&SA), Turkey (ME&A), the Philippines (S&SA), Russia (EE), Poland (EU), Lithuania (EU), and Italy (EU). As part of our global operating model, products manufactured in a particular manufacturing facility are not necessarily distributed in the operating segment where the facility is located.

We have integrated the production of our heated tobacco units into a number of our existing manufacturing facilities, and we are progressing with our plans to build manufacturing capacity for our other RRP platforms. We will continue to optimize our manufacturing infrastructure.

We believe the properties owned or leased by our subsidiaries are maintained in good condition and are believed to be suitable and adequate for our present needs.

Item 3. *Legal Proceedings.*

The information called for by this Item is incorporated herein by reference to Item 8, Note 18. *Contingencies*.

Item 4. *Mine Safety Disclosures.*

Not applicable.

PART II

Item 5. *Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.*

The principal stock exchange on which our common stock (no par value) is listed is the New York Stock Exchange (ticker symbol "PM"). At January 31, 2020, there were approximately 50,800 holders of record of our common stock.

Performance Graph

The graph below compares the cumulative total shareholder return on PMI's common stock with the cumulative total return for the same period of PMI's Peer Group and the S&P 500 Index. The graph assumes the investment of $100 as of December 31, 2014, in PMI common stock (at prices quoted on the New York Stock Exchange) and each of the indices as of the market close and reinvestment of dividends on a quarterly basis.

chart-a1095974eeba597aa2c.jpg

Date	PMI	PMI Peer Group [1]	S&P 500 Index
December 31, 2014	$100.00	$100.00	$100.00
December 31, 2015	$113.40	$108.20	$101.40
December 31, 2016	$123.10	$109.70	$113.50
December 31, 2017	$147.60	$130.20	$138.30
December 31, 2018	$98.60	$118.30	$132.20
December 31, 2019	$133.00	$146.40	$173.90

[1] The PMI Peer Group presented in this graph is the same as that used in the prior year. The PMI Peer Group was established based on a review of four characteristics: global presence; a focus on consumer products; and net revenues and a market capitalization of a similar size to those of PMI. The review also considered the primary international tobacco companies. As a result of this review, the following companies constitute the PMI Peer Group: Altria Group, Inc., Anheuser-Busch InBev SA/NV, British American Tobacco p.l.c., The Coca-Cola Company, Colgate-Palmolive Co., Diageo plc, Heineken N.V., Imperial Brands PLC, Japan Tobacco Inc., Johnson & Johnson, Kimberly-Clark Corporation, The Kraft-Heinz Company, McDonald's Corp., Mondelēz International, Inc., Nestlé S.A., PepsiCo, Inc., The Procter & Gamble Company, Roche Holding AG, and Unilever NV and PLC.

Note: Figures are rounded to the nearest $0.10.

Issuer Purchases of Equity Securities During the Quarter Ended December 31, 2019

Our share repurchase activity for each of the three months in the quarter ended December 31, 2019, was as follows:

Period	Total Number of Shares Repurchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Programs
October 1, 2019 – October 31, 2019 (1)	—	$ —	—	$ —
November 1, 2019 – November 30, 2019 (1)	—	$ —	—	$ —
December 1, 2019 – December 31, 2019 (1)	—	$ —	—	$ —
Pursuant to Publicly Announced Plans or Programs	—	$ —		
October 1, 2019 – October 31, 2019 (2)	897	$ 75.37		
November 1, 2019 – November 30, 2019 (2)	690	$ 81.33		
December 1, 2019 – December 31, 2019 (2)	1,186	$ 82.69		
For the Quarter Ended December 31, 2019	2,773	$ 79.98		

(1) During this reporting period, we did not have an authorized share repurchase program.

(2) Shares repurchased represent shares tendered to us by employees who vested in restricted and performance share unit awards and used shares to pay all, or a portion of, the related taxes.

Item 6. *Selected Financial Data.*

(in millions of dollars, except per share data)

	2019	2018	2017	2016	2015
Summary of Operations:					
Revenues including excise taxes	**$ 77,921**	$ 79,823	$ 78,098	$ 74,953	$ 73,908
Excise taxes on products	**48,116**	50,198	49,350	48,268	47,114
Net revenues	**29,805**	29,625	28,748	26,685	26,794
Operating income	**10,531**	11,377	11,581	10,903	10,745
Net earnings attributable to PMI	**7,185**	7,911	6,035	6,967	6,873
Basic earnings per share	**4.61**	5.08	3.88	4.48	4.42
Diluted earnings per share	**4.61**	5.08	3.88	4.48	4.42
Dividends declared per share	**4.62**	4.49	4.22	4.12	4.04
Total assets	**42,875**	39,801	42,968	36,851	33,956
Long-term debt [1]	**26,656**	26,975	31,334	25,851	25,250
Total debt	**31,045**	31,759	34,339	29,067	28,480

[1] Excluding current portion of long-term debt.

This Selected Financial Data should be read in conjunction with Item 7 and Item 8.

Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations.*

The following discussion should be read in conjunction with the other sections of this Annual Report on Form 10-K, including the consolidated financial statements and related notes contained in Item 8, and the discussion of risks and cautionary factors that may affect future results in Item 1A. *Risk Factors*.

Description of Our Company

We are leading a transformation in the tobacco industry to create a smoke-free future and ultimately replace cigarettes with smoke-free products to the benefit of adults who would otherwise continue to smoke, society, the company and its shareholders. We are a leading international tobacco company engaged in the manufacture and sale of cigarettes, as well as smoke-free products and associated electronic devices and accessories, and other nicotine-containing products in markets outside the United States. In addition, we ship a version of our Platform 1 device and its consumables authorized by the U.S. Food and Drug Administration ("FDA") to Altria Group, Inc., for sale in the United States under license. We are building a future on a new category of smoke-free products that, while not risk free, are a much better choice than continuing to smoke. Through multidisciplinary capabilities in product development, state-of-the-art facilities and scientific substantiation, we aim to ensure that our smoke-free products meet adult consumer preferences and rigorous regulatory requirements. Our *IQOS* smoke-free product brand portfolio includes heat-not-burn tobacco and nicotine-containing vapor products.

We manage our business in six operating segments:

- European Union ("EU");
- Eastern Europe ("EE");
- Middle East & Africa ("ME&A"), which includes our international duty free business;
- South & Southeast Asia ("S&SA");
- East Asia & Australia ("EA&A"); and
- Latin America & Canada ("LA&C"), which includes transactions under license with Altria Group, Inc. for the distribution of our Platform 1 product in the United States.

Our cigarettes are sold in more than 180 markets, and in many of these markets they hold the number one or number two market share position. We have a wide range of premium, mid-price and low-price brands. Our portfolio comprises both international and local brands. In addition to the manufacture and sale of cigarettes, we are engaged in the development and commercialization of reduced-risk products ("RRPs"). RRPs is the term we use to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continuing smoking.

We use the term net revenues to refer to our operating revenues from the sale of our products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. Our net revenues and operating income are affected by various factors, including the volume of products we sell, the price of our products, changes in currency exchange rates and the mix of products we sell. Mix is a term used to refer to the proportionate value of premium-price brands to mid-price or low-price brands in any given market (product mix). Mix can also refer to the proportion of shipment volume in more profitable markets versus shipment volume in less profitable markets (geographic mix).

Our cost of sales consists principally of: tobacco leaf, non-tobacco raw materials, labor and manufacturing costs; shipping and handling costs; and the cost of the *IQOS* devices produced by third-party electronics manufacturing service providers. Estimated costs associated with *IQOS* warranty programs are generally provided for in cost of sales in the period the related revenues are recognized.

Our marketing, administration and research costs include the costs of marketing and selling our products, other costs generally not related to the manufacture of our products (including general corporate expenses), and costs incurred to develop new products. The most significant components of our marketing, administration and research costs are marketing and sales expenses and general and administrative expenses.

Philip Morris International Inc. is a legal entity separate and distinct from its direct and indirect subsidiaries. Accordingly, our right, and thus the right of our creditors and stockholders, to participate in any distribution of the assets or earnings of any subsidiary is subject to the prior rights of creditors of such subsidiary, except to the extent that claims of our company itself as a creditor may be recognized. As a holding company, our principal sources of funds, including funds to make payment on our debt securities, are from the receipt of

dividends and repayment of debt from our subsidiaries. Our principal wholly owned and majority-owned subsidiaries currently are not limited by long-term debt or other agreements in their ability to pay cash dividends or to make other distributions with respect to their common stock that are otherwise compliant with law.

Executive Summary

The following executive summary provides significant highlights from the Discussion and Analysis that follows.

Consolidated Operating Results

- **Net Revenues –** Net revenues of $29.8 billion for the year ended December 31, 2019, increased by $0.2 billion, or 0.6%, from the comparable 2018 amount. The change in our net revenues from the comparable 2018 amount was driven by the following (variances not to scale with year-to-date results):

  chart-d5a1373d21214890bb8.jpg

  Net revenues, excluding unfavorable currency, increased by 3.8%, mainly reflecting: a favorable pricing variance, notably in Germany, Indonesia, Japan, the Philippines and Turkey; and favorable volume/mix, mainly driven by heated tobacco unit and *IQOS* device volume in the EU and Russia, and heated tobacco unit volume in Japan, partly offset by unfavorable volume/mix of cigarettes, notably in Australia, the EU, Indonesia, Japan and Russia, unfavorable heated tobacco unit volume in PMI Duty Free, and unfavorable *IQOS* device volume in Japan and Korea. The currency-neutral growth in net revenues of 3.8% came despite the unfavorable impact of $763 million, shown in "Other" above, predominantly resulting from the deconsolidation of our Canadian subsidiary, Rothmans, Benson & Hedges, Inc. ("RBH"), effective March 22, 2019. For further details on the deconsolidation of RBH, see Item 8, Note 18. *Contingencies* and Note 22. *Deconsolidation of RBH*.

  Net revenues by product category for the years ended December 31, 2019 and 2018, are shown below:

  chart-0e35503389a8527f975.jpg chart-866bd228fe9e54f5801.jpg

- **Diluted Earnings Per Share –** The changes in our reported diluted earnings per share ("diluted EPS") for the year ended December 31, 2019, from the comparable 2018 amounts, were as follows:

	Diluted EPS	% Growth (Decline)
For the year ended December 31, 2018	**$ 5.08**	
2018 Asset impairment and exit costs	**—**	
2018 Tax items	**0.02**	
Subtotal of 2018 items	**0.02**	
2019 Asset impairment and exit costs	**(0.23)**	
2019 Canadian tobacco litigation-related expense	**(0.09)**	
2019 Loss on deconsolidation of RBH	**(0.12)**	
2019 Russia excise and VAT audit charge	**(0.20)**	
2019 Fair value adjustment for equity security investments	**0.02**	
2019 Tax items	**0.04**	
Subtotal of 2019 items	**(0.58)**	
Currency	**(0.13)**	
Interest	**0.04**	
Change in tax rate	**(0.04)**	
Operations	**0.22**	
For the year ended December 31, 2019	**$ 4.61**	**(9.3)%**

Income taxes – The 2018 Tax items that decreased our 2018 diluted EPS by $0.02 per share in the table above represented a current income tax charge of $185 million primarily due to an increase in our final 2017 transition tax liability, mostly offset by a deferred income tax benefit of $154 million primarily due to the recognition of deferred tax assets for net operating losses in the state of New York.

The 2019 Tax items that increased our 2019 diluted EPS by $0.04 per share in the table above was primarily due to a reduction in estimated U.S. federal income tax on dividend repatriation for the years 2015-2018 ($67 million).

The change in the tax rate that decreased our diluted EPS by $0.04 per share in the table above was primarily due to changes in earnings mix by taxing jurisdiction and U.S. state deferred income tax expense, partially offset by repatriation cost differences.

For further details, see Item 8, Note 11. *Income Taxes*.

Asset impairment and exit costs – As a part of the optimization of our global manufacturing infrastructure, we recorded pre-tax asset impairment and exit costs of $422 million during 2019, representing $362 million net of income tax and a diluted EPS charge of $0.23 per share. This charge primarily related to a cigarette plant closure in Berlin, Germany (approximately $0.19 per share), as well as the closure of a cigarette plant in Argentina, Colombia and Pakistan. The total pre-tax charge was included in marketing, administration and research costs on the consolidated statements of earnings. For further details, see Item 8, Note 21. *Asset Impairment and Exit Costs*.

Canadian tobacco litigation-related expense – In the first quarter of 2019, we recorded a pre-tax charge of $194 million, representing $142 million net of tax, relating to the judgment against RBH in two Québec smoking and health class actions. The charge of $0.09 per share reflects our assessment of the portion of the judgment that

represents probable and estimable loss prior to the deconsolidation of RBH and corresponds to the trust account deposit required by the judgment. The total pre-tax charge was included in marketing, administration and research costs on the consolidated statements of earnings and was included in the operating income of the Latin America & Canada segment. For further details, see Item 8, Note 18. *Contingencies* and Item 8, Note 22. *Deconsolidation of RBH*.

Loss on deconsolidation of RBH – Following the judgment in the two Québec smoking and health class actions, RBH obtained an initial order from the Ontario Superior Court of Justice granting it protection under the Companies' Creditors Arrangement Act ("CCAA"), which is a Canadian federal law that permits a Canadian business to restructure its affairs while carrying on its business in the ordinary course with minimal disruption to its customers, suppliers and employees. The administration of the CCAA process, principally relating to the powers provided to the court and the court appointed monitor, removes certain elements of control of the business from both PMI and RBH. As a result, we have determined that we no longer have a controlling financial interest over RBH and that we do not exert "significant influence" over RBH under U.S. GAAP. Therefore, we deconsolidated RBH as of the date of the CCAA filing on March 22, 2019, and will account for our continuing investment in RBH as an equity security, without readily determinable fair value.

A loss on the deconsolidation of RBH of $239 million was included in marketing, administration and research costs on the consolidated statements of earnings and was included in the operating income of the Latin America & Canada segment. The $0.12 per share impact also included a tax benefit of $49 million within the provision for income taxes, as discussed above, related to the reversal of a deferred tax liability on the unremitted earnings of RBH. For further details, see Item 8, Note 18. *Contingencies* and Item 8, Note 22. *Deconsolidation of RBH*.

Russia excise and VAT audit charge – As a result of the final tax assessment for the 2015-2017 financial years received by our Russian affiliate, in the third quarter of 2019, PMI recorded a pre-tax charge of $374 million in marketing, administration and research costs in the consolidated statements of earnings, representing $315 million net of income tax and a diluted EPS charge of $0.20. The pre-tax charge of $374 million was included in the operating income of the Eastern Europe segment. For further details, see Item 8, Note 18. *Contingencies.*

Fair Value adjustment for equity security investments – In the fourth quarter of 2019, PMI recorded a favorable fair value adjustment for its equity security investments of $35 million after tax (or $0.02 per share increase in diluted EPS). The fair value adjustment for its equity security investments was included in equity investments and securities (income)/loss, net ($44 million income) and provision for income taxes ($9 million expense) on the consolidated statements of earnings in 2019. For further details, see Item 8, Note 16. *Fair Value Measurements.*

Currency – The unfavorable currency impact during 2019 results from the fluctuations of the U.S. dollar, especially against the Euro, Russian ruble and Turkish lira. This unfavorable currency movement has impacted our profitability across our primary revenue markets and local currency cost bases.

Interest – The favorable impact of interest was due primarily to our ongoing efforts to optimize our capital structure following the passage of the U.S. Tax Cuts and Jobs Act. This included the decision to use existing cash to repay $2.5 billion and $4.0 billion of long-term debt that matured in 2018 and in 2019, respectively.

Operations – The increase in diluted EPS of $0.22 from our operations in the table above was due primarily to the following segments:

- European Union: Favorable volume/mix and favorable pricing, partially offset by higher marketing, administration and research costs and higher manufacturing costs;

- South & Southeast Asia: Favorable pricing and lower manufacturing costs, partially offset by unfavorable volume/mix and higher marketing, administration and research costs;

- Middle East & Africa: Favorable pricing, lower manufacturing costs and lower marketing, administration and research costs, partially offset by unfavorable volume/mix; and

- East Asia & Australia: Favorable pricing and lower manufacturing costs, partially offset by unfavorable volume/mix and higher marketing, administration and research costs;

partially offset by

-

Latin America & Canada: Unfavorable impact resulting from the deconsolidation of RBH, as well as unfavorable volume/mix, partially offset by lower marketing, administration and research costs, favorable pricing and lower manufacturing costs; and

- Eastern Europe: Higher marketing, administration and research costs and higher manufacturing costs, partially offset by favorable volume/mix and favorable pricing.

For further details, see the *Consolidated Operating Results* and *Operating Results by Business Segment* sections of the following *Discussion and Analysis*.

Discussion and Analysis

Critical Accounting Estimates

Item 8, Note 2. *Summary of Significant Accounting Policies* to our consolidated financial statements includes a summary of the significant accounting policies and methods used in the preparation of our consolidated financial statements. In most instances, we must use a particular accounting policy or method because it is the only one that is permitted under U.S. GAAP.

The preparation of financial statements requires that we use estimates and assumptions that affect the reported amounts of our assets, liabilities, net revenues and expenses, as well as our disclosure of contingencies. If actual amounts differ from previous estimates, we include the revisions in our consolidated results of operations in the period during which we know the actual amounts. Historically, aggregate differences, if any, between our estimates and actual amounts in any year have not had a significant impact on our consolidated financial statements.

The selection and disclosure of our critical accounting estimates have been discussed with our Audit Committee. The following is a discussion of the more significant assumptions, estimates, accounting policies and methods used in the preparation of our consolidated financial statements:

Revenue Recognition - We recognize revenue as performance obligations are satisfied. Our primary performance obligation is the distribution and sales of cigarettes and other nicotine-containing products, including reduced-risk products. Our performance obligations are typically satisfied upon shipment or delivery to our customers. The company estimates the cost of sales returns based on historical experience, and these estimates are immaterial. Estimated costs associated with warranty programs for *IQOS* devices are generally provided for in cost of sales in the period the related revenues are recognized, based on a number of factors, including historical experience, product failure rates and warranty policies. The transaction price is typically based on the amount billed to the customer and includes estimated variable consideration where applicable. Such variable consideration is typically not constrained and is estimated based on the most likely amount that PMI expects to be entitled to under the terms of the contracts with customers, historical experience of discount or rebate redemption, where relevant, and the terms of any underlying discount or rebate programs, which may change from time to time as the business and product categories evolve.

Inventories - Our inventories are valued at the lower of cost or market based upon assumptions about future demand and market conditions. The valuation of inventory also requires us to estimate obsolete and excess inventory. We perform regular reviews of our inventory on hand, as well as our future purchase commitments with our suppliers, considering multiple factors, including demand forecasts, product life cycle, current sales levels, pricing strategy and cost trends. If our review indicates that inventories of raw materials, components or finished products have become obsolete or are in excess of anticipated demand or that inventory cost exceeds net realizable value, we may be required to make adjustments that will impact the results of operations.

Goodwill and Non-Amortizable Intangible Assets Valuation - We test goodwill and non-amortizable intangible assets for impairment annually or more frequently if events occur that would warrant such review. While the company has the option to perform a qualitative assessment for both goodwill and non-amortizable intangible assets to determine if it is more likely than not that an impairment exists, the company elects to perform the quantitative assessment for our annual impairment analysis. The impairment analysis involves comparing the fair value of each reporting unit or non-amortizable intangible asset to the carrying value. If the carrying value exceeds the fair value, goodwill or a non-amortizable intangible asset is considered impaired. To determine the fair value of goodwill, we primarily use a discounted cash flow model, supported by the market approach using earnings multiples of comparable global and local companies within the tobacco industry. At December 31, 2019, the carrying value of our goodwill was $5.9 billion, which is related to ten reporting units, each of which consists of a group of markets with similar economic characteristics. The estimated fair value of each of our ten reporting units exceeded the carrying value as of December 31, 2019. To determine the fair value of non-amortizable intangible assets, we primarily use a discounted cash flow model applying the relief-from-royalty method. We concluded that the fair value of our non-amortizable intangible assets exceeded the carrying value. These discounted cash flow models include management assumptions relevant for forecasting operating cash flows, which are subject to changes in business conditions, such as volumes and prices, costs to produce, discount rates and estimated capital needs. Management considers historical experience and all available information at the time the fair values are estimated, and we believe these assumptions are consistent with the assumptions a hypothetical marketplace participant would use. Since the March 28, 2008,

spin-off from Altria Group, Inc., we have not recorded a charge to earnings for an impairment of goodwill or non-amortizable intangible assets.

Marketing Costs - We incur certain costs to support our products through programs that include advertising, marketing, consumer engagement and trade promotions. The costs of our advertising and marketing programs are expensed in accordance with U.S. GAAP. Recognition of the cost related to our consumer engagement and trade promotion programs contain uncertainties due to the judgment

required in estimating the potential performance and compliance for each program. For volume-based incentives provided to customers, management continually assesses and estimates, by customer, the likelihood of the customer's achieving the specified targets, and records the reduction of revenue as the sales are made. For other trade promotions, management relies on estimated utilization rates that have been developed from historical experience. Changes in the assumptions used in estimating the cost of any individual marketing program would not result in a material change in our financial position, results of operations or operating cash flows.

Employee Benefit Plans - As discussed in Item 8, Note 13. *Benefit Plans* to our consolidated financial statements, we provide a range of benefits to our employees and retired employees, including pensions, postretirement health care and postemployment benefits (primarily severance). We record annual amounts relating to these plans based on calculations specified by U.S. GAAP. These calculations include various actuarial assumptions, such as discount rates, assumed rates of return on plan assets, compensation increases, mortality, turnover rates and health care cost trend rates. We review actuarial assumptions on an annual basis and make modifications to the assumptions based on current rates and trends when it is deemed appropriate to do so. As permitted by U.S. GAAP, any effect of the modifications is generally amortized over future periods. We believe that the assumptions utilized in calculating our obligations under these plans are reasonable based upon our historical experience and advice from our actuaries.

Weighted-average discount rate assumptions for pension and postretirement plan obligations at December 31, 2019 and 2018 are as follows:

	2019	2018
Pension plans	**0.83%**	1.61%
Postretirement plans	**3.28%**	3.97%

We anticipate that assumption changes will increase 2020 pre-tax pension and postretirement expense to approximately $256 million as compared with approximately $201 million in 2019, excluding amounts related to employee severance and early retirement programs. The anticipated increase is primarily due to higher amortization of unrecognized actuarial gains/losses of $73 million, coupled with higher service cost of $48 million, partially offset by lower interest cost of $49 million and higher expected return on plan assets of $18 million and other movements of $1 million.

Weighted-average expected rate of return and discount rate assumptions have a significant effect on the amount of expense reported for the employee benefit plans. A fifty-basis-point decrease in our discount rate would increase our 2020 pension and postretirement expense by approximately $65 million, and a fifty-basis-point increase in our discount rate would decrease our 2020 pension and postretirement expense by approximately $58 million. Similarly, a fifty-basis-point decrease (increase) in the expected return on plan assets would increase (decrease) our 2020 pension expense by approximately $36 million.

Income Taxes - Income tax provisions for jurisdictions outside the United States, as well as state and local income tax provisions, are determined on a separate company basis, and the related assets and liabilities are recorded in our consolidated balance sheets.

The extent of our operations involves dealing with uncertainties and judgments in the application of complex tax regulations in a multitude of jurisdictions. The final taxes paid are dependent upon many factors, including negotiations with taxing authorities in various jurisdictions and resolution of disputes arising from federal, state, and international tax audits. In accordance with the authoritative guidance for income taxes, we evaluate potential tax exposures and record tax liabilities for anticipated tax audit issues based on our estimate of whether, and the extent to which, additional taxes will be due. We adjust these reserves in light of changing facts and circumstances; however, due to the complexity of some of these uncertainties, the ultimate resolution may result in a payment that is materially different from our current estimate of the tax liabilities. If our estimate of tax liabilities proves to be less than the ultimate assessment, an additional charge to expense would result. If payment of these amounts ultimately proves to be less than the recorded amounts, the reversal of the liabilities would result in tax benefits being recognized in the period when we determine the liabilities are no longer necessary.

We are required to assess the likelihood of recovering deferred tax assets against future sources of taxable income. If we determine, using all available evidence, that we do not reach the more likely than not threshold for recovery, a valuation allowance is recorded. Significant judgment is required in determining the need for and amount of valuation allowances for deferred tax assets including estimates of future taxable income in the applicable jurisdictions and the feasibility of on-going tax planning strategies, as applicable.

The effective tax rates used for interim reporting are based on our full-year geographic earnings mix projections. Changes in currency exchange rates or earnings mix by taxing jurisdiction could have an impact on the effective tax rates. Significant judgment is required in determining income tax provisions and in evaluating tax positions.

For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements.

Hedging - As discussed below in "Market Risk," we use derivative financial instruments principally to reduce exposures to market risks resulting from fluctuations in foreign currency exchange and interest rates by creating offsetting exposures. For derivatives to which we have elected to apply hedge accounting, gains and losses on these derivatives are initially deferred in accumulated other comprehensive losses on the consolidated balance sheet and recognized in the consolidated statement of earnings into the same line item as the impact of the underlying transaction and in the periods when the related hedged transactions are also recognized in operating results. If we had elected not to use the hedge accounting provisions, gains (losses) deferred in stockholders' (deficit) equity would have been recorded in our net earnings for these derivatives.

Fair value of non-marketable equity securities - For further details, see Item 8, Note 22. *Deconsolidation of RBH.*

Contingencies - As discussed in Item 8, Note 18. *Contingencies* to our consolidated financial statements, legal proceedings covering a wide range of matters are pending or threatened against us, and/or our subsidiaries, and/or our indemnitees in various jurisdictions. We and our subsidiaries record provisions in the consolidated financial statements for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. The variability in pleadings in multiple jurisdictions, together with the actual experience of management in litigating claims, demonstrate that the monetary relief that may be specified in a lawsuit bears little relevance to the ultimate outcome. Much of the tobacco-related litigation is in its early stages, and litigation is subject to uncertainty. At the present time, except as stated otherwise in Item 8, Note 18. *Contingencies,* while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available to it: (i) management has not concluded that it is probable that a loss has been incurred in any of the pending tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any. Legal defense costs are expensed as incurred.

Consolidated Operating Results

Our net revenues and operating income by segment were as follows:

(in millions)	2019	2018	2017
Net Revenues			
European Union	**$ 9,817**	$ 9,298	$ 8,318
Eastern Europe	**3,282**	2,921	2,711
Middle East & Africa	**4,042**	4,114	3,988
South & Southeast Asia	**5,094**	4,656	4,417
East Asia & Australia	**5,364**	5,580	6,373
Latin America & Canada	**2,206**	3,056	2,941
Net revenues	**$ 29,805**	$ 29,625	$ 28,748
Operating Income			
European Union	**$ 3,970**	$ 4,105	$ 3,691
Eastern Europe	**547**	902	887
Middle East & Africa	**1,684**	1,627	1,884
South & Southeast Asia	**2,163**	1,747	1,514
East Asia & Australia	**1,932**	1,851	2,608
Latin America & Canada	**235**	1,145	997
Operating income	**$ 10,531**	$ 11,377	$ 11,581

Items affecting the comparability of results from operations were as follows:

- **Russia excise and VAT audit charge** - See Item 8, Note 18. *Contingencies* for details of the $374 million pre-tax charge included in the Eastern Europe segment for the year ended December 31, 2019.

-

Asset impairment and exit costs - See Item 8, Note 21. *Asset Impairment and Exit Costs* for details of the $422 million pre-tax charge for the year ended December 31, 2019, as well as a breakdown of these costs by segment.

- **Canadian tobacco litigation-related expense** - See Item 8, Note 18. *Contingencies* and Note 22. *Deconsolidation of RBH* for details of the $194 million pre-tax charge included in the Latin America & Canada segment for the year ended December 31, 2019.

- **Loss on deconsolidation of RBH** - See Item 8, Note 22. *Deconsolidation of RBH* for details of the $239 million loss included in the Latin America & Canada segment for the year ended December 31, 2019.

Our net revenues by product category were as follows:

PMI Net Revenues by Product Category

(in millions)	2019	2018	2017
Combustible Products			
European Union	**$ 8,093**	$ 8,433	$ 8,048
Eastern Europe	**2,438**	2,597	2,657
Middle East & Africa	**3,721**	3,732	3,893
South & Southeast Asia	**5,094**	4,656	4,417
East Asia & Australia	**2,693**	3,074	3,156
Latin America & Canada	**2,179**	3,037	2,937
Total Combustible Products	**$ 24,218**	$ 25,529	$ 25,107
Reduced-Risk Products			
European Union	**$ 1,724**	$ 865	$ 269
Eastern Europe	**844**	324	55
Middle East & Africa	**321**	382	94
South & Southeast Asia	**—**	—	—
East Asia & Australia	**2,671**	2,506	3,218
Latin America & Canada	**27**	19	4
Total Reduced-Risk Products	**$ 5,587**	$ 4,096	$ 3,640
Total PMI Net Revenues	**$ 29,805**	$ 29,625	$ 28,748

Note: Sum of product categories or Regions might not foot to total PMI due to rounding.

Net revenues related to combustible products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of our cigarettes and other tobacco products combined. Other tobacco products primarily include roll-your-own and make-your-own cigarettes, pipe tobacco, cigars and cigarillos and do not include reduced-risk products.

Net revenues related to reduced-risk products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of our heated tobacco units, *IQOS* devices and related accessories, and other nicotine-containing products, which primarily include our e-vapor products.

We recognize revenue when control is transferred to the customer, typically either upon shipment or delivery of goods.

Revenues from shipments of Platform 1 devices, heated tobacco units and accessories to Altria Group, Inc., commencing in the third quarter of 2019, for sale under license in the United States, are included in Net Revenues of the Latin America & Canada segment.

References to "Cost/Other" in the Consolidated Financial Summary table of total PMI and the six operating segments throughout this *"Discussion and Analysis"* reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs (including asset impairment and exit costs, the Canadian tobacco litigation-related expense, the charge related to the deconsolidation of RBH in Canada, and the Russia excise and VAT audit charge); and amortization of intangibles. “Cost/Other” also includes the currency-neutral net revenue variance, unrelated to volume/mix and price components, attributable to fees for certain distribution rights billed to customers in certain markets in the ME&A Region, as well as the impact of the deconsolidation in RBH.

Our shipment volume by segment for cigarettes and heated tobacco units was as follows:

PMI Shipment Volume (Million Units)

	2019	2018	2017
Cigarettes			
European Union	**174,319**	179,622	187,293
Eastern Europe	**100,644**	108,718	119,398
Middle East & Africa	**134,568**	136,605	136,759
South & Southeast Asia	**174,934**	178,469	171,600
East Asia & Australia	**49,951**	56,163	62,653
Latin America & Canada	**72,293**	80,738	84,223
Total Cigarettes	**706,709**	740,315	761,926
Heated Tobacco Units			
European Union	**12,569**	5,977	1,889
Eastern Europe	**13,453**	4,979	674
Middle East & Africa	**2,654**	3,403	907
South & Southeast Asia	**—**	—	—
East Asia & Australia	**30,677**	26,866	32,729
Latin America & Canada [1]	**299**	147	27
Total Heated Tobacco Units	**59,652**	41,372	36,226
Cigarettes and Heated Tobacco Units			
European Union	**186,888**	185,599	189,182
Eastern Europe	**114,097**	113,697	120,072
Middle East & Africa	**137,222**	140,008	137,666
South & Southeast Asia	**174,934**	178,469	171,600
East Asia & Australia	**80,628**	83,029	95,382
Latin America & Canada	**72,592**	80,885	84,250
Total Cigarettes and Heated Tobacco Units	**766,361**	781,687	798,152

[1] *Includes shipments to Altria Group, Inc., commencing in the third quarter of 2019, for sale in the United States under license.*

Following the deconsolidation of our Canadian subsidiary, we will continue to report the volume of brands sold by RBH for which other PMI subsidiaries are the trademark owners. These include *HEETS*, *Next*, *Philip Morris* and *Rooftop*, which together accounted for approximately 40% of RBH's total shipment volume in 2018.

Heated tobacco units ("HTU") is the term we use to refer to heated tobacco consumables, which for us include our *HEETS*, *HEETS Marlboro* and *HEETS FROM MARLBORO*, defined collectively as *HEETS*, as well as *Marlboro HeatSticks* and *Parliament HeatSticks.*

Shipment volume of heated tobacco units to the United States is included in the heated tobacco unit shipment volume of the Latin America & Canada segment.

References to total international market, defined as worldwide cigarette and heated tobacco unit volume excluding the United States, total industry, total market and market shares throughout this *"Discussion and Analysis"* are our estimates for tax-paid products based on the latest available data from a number of internal and external sources and may, in defined instances, exclude the People's Republic of China and/or our duty free business. In addition, to reflect the deconsolidation of RBH, effective March 22, 2019, PMI's total market share has been restated for previous periods.

In-market sales ("IMS") is defined as sales to the retail channel, depending on the market and distribution model.

North Africa is defined as Algeria, Egypt, Libya, Morocco and Tunisia.

The Gulf Cooperation Council ("GCC") is defined as Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates (UAE).

Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units.

From time to time, PMI's shipment volumes are subject to the impact of distributor inventory movements, and estimated total industry/market volumes are subject to the impact of inventory movements in various trade channels that include estimated trade inventory movements of PMI's competitors arising from market-specific factors that significantly distort reported volume disclosures. Such factors may include changes to the manufacturing supply chain, shipment methods, consumer demand, timing of excise tax increases or other influences that may affect the timing of sales to customers. In such instances, in addition to reviewing PMI shipment volumes and certain estimated total industry/market volumes on a reported basis, management reviews these measures on an adjusted basis that excludes the impact of distributor and/or estimated trade inventory movements. Management also believes that disclosing PMI shipment volumes and estimated total industry/market volumes in such circumstances on a basis that excludes the impact of distributor and/or estimated trade inventory movements improves the comparability of performance and trends for these measures over different reporting periods.

2019 compared with 2018

The following discussion compares our consolidated operating results for the year ended December 31, 2019, with the year ended December 31, 2018.

Estimated international industry cigarette and heated tobacco unit volume, excluding China and the United States, of 2.7 trillion, decreased by 2.0%, due to the EU, EE, S&SA, EA&A and LA&C, as described in the Regional sections below.

Our total shipment volume decreased by 2.0%, due to:

- Middle East & Africa, primarily reflecting lower cigarette shipment volume, notably in Turkey, partly offset by Egypt and Saudi Arabia, and lower heated tobacco unit shipment volume in PMI Duty Free;

- South & Southeast Asia, reflecting lower cigarette shipment volume, primarily in Indonesia, Pakistan and the Philippines, partly offset by Thailand;

- East Asia & Australia, primarily reflecting lower cigarette shipment volume in Japan and lower cigarette and heated tobacco unit shipment volume in Korea, partly offset by higher heated tobacco unit shipment volume in Japan; and

- Latin America & Canada, reflecting lower cigarette shipment volume, principally in Argentina, Canada (primarily due to the impact of the deconsolidation of RBH) and Venezuela. Excluding the volume impact from the RBH deconsolidation of approximately 4.3 billion units (reflecting the volume of RBH-owned brands from March 22, 2018 through December 31, 2018), our total shipment volume in the Region decreased by 5.2%;

partly offset by

- the EU, reflecting higher heated tobacco unit shipment volume across the Region, notably in Italy, partly offset by lower cigarette shipment volume, primarily in France, Germany and Italy; and

- Eastern Europe, reflecting higher heated tobacco unit shipment volume across the Region, notably in Kazakhstan, Russia and Ukraine, partly offset by lower cigarette shipment volume, primarily in Russia and Ukraine.

Excluding the volume impact from the RBH deconsolidation of approximately 4.3 billion units (reflecting the volume of RBH-owned brands from March 22, 2018 through December 31, 2018 and including Duty-Free sales of these brands in Canada), PMI's total shipment volume decreased by 1.4%.

Impact of Inventory Movements

Excluding the volume impact from the deconsolidation of RBH, and the net favorable impact of estimated distributor inventory movements of approximately 1.1 billion units, our total in-market sales declined by 1.5%, due to a 3.7% decline of cigarettes, partly offset by a 35.3% increase in heated tobacco units.

The net favorable impact of estimated distributor inventory movements of approximately 1.1 billion units reflected a 2.7 billion favorable impact from heated tobacco units (driven primarily by Japan, mainly reflecting a favorable comparison with 2018 in which *IQOS* consumable inventories were reduced, partly offset by PMI Duty Free), partially offset by a 1.6 billion unfavorable impact from cigarettes (due primarily to Japan, North Africa and Thailand, partly offset by the EU Region and Saudi Arabia).

Our cigarette shipment volume by brand and heated tobacco unit shipment volume was as follows:

PMI Shipment Volume by Brand (Million Units)

		Full-Year	
	2019	**2018**	**Change**
Cigarettes			
Marlboro	**262,908**	264,423	(0.6%)
L&M	**92,873**	89,789	3.4 %
Chesterfield	**57,185**	59,452	(3.8%)
Philip Morris	**49,164**	49,864	(1.4%)
Parliament	**38,723**	41,697	(7.1%)
Sampoerna A	**35,133**	39,522	(11.1%)
Dji Sam Soe	**32,435**	29,195	11.1 %
Bond Street	**28,025**	32,173	(12.9%)
Lark	**19,602**	23,021	(14.9%)
Fortune	**12,831**	16,596	(22.7%)
Others	**77,830**	94,583	(17.7%)
Total Cigarettes	**706,709**	740,315	(4.5%)
Heated Tobacco Units [1]	**59,652**	41,372	44.2 %
Total Cigarettes and Heated Tobacco Units	**766,361**	781,687	(2.0%)

[1] *Includes shipments to Altria Group, Inc., commencing in the third quarter of 2019, for sale in the United States under license.*

Note: *Sampoerna A* includes *Sampoerna*; *Philip Morris* includes *Philip Morris/Dubliss*; and *Lark* includes *Lark Harmony*.

Our cigarette shipment volume of the following brands decreased:

- *Marlboro,* mainly due to Italy and Japan, partly reflecting the impact of out-switching to heated tobacco units, as well as France, partially offset by the Philippines, Saudi Arabia and Turkey;
- *Chesterfield*, mainly due to Argentina, Italy, Russia and Venezuela, partly offset by Brazil;
- *Philip Morris*, notably due to Argentina, partly offset by Indonesia and Russia;
- *Parliament*, mainly due to Japan, Korea and Russia;
- *Sampoerna A* in Indonesia, mainly reflecting the impact of retail price increases resulting in widened price gaps with competitors' products;
- *Bond Street*, mainly due to Russia and Ukraine;

- *Lark*, mainly due to Japan and Turkey;

- *Fortune* in the Philippines, mainly reflecting up-trading to *Marlboro* resulting from narrowed price gaps with the below premium price segment; and

- "Others," notably due to: the impact of the deconsolidation of RBH in Canada; mid-price *Sampoerna U* in Indonesia, partly reflecting the impact of above-inflation retail price increases; and low-price brands, notably *Morven* in Pakistan and *Next/Dubliss* in Russia, partly offset by *Jackpot* in the Philippines.

The increase in our heated tobacco unit shipment volume was mainly driven by: the EU (notably Italy and Poland), Eastern Europe (notably Kazakhstan, Russia and Ukraine) and Japan, partly offset by Korea and PMI Duty Free.

Our cigarette shipment volume of the following brands increased:

- *L&M*, mainly driven by Egypt and Thailand, partly offset by Russia and Turkey; and
- *Dji Sam Soe* in Indonesia, driven by the strong performance of the *DSS Magnum Mild 16* variant and the introduction of 20s and 50s variants.

2019 International Share of Market (excluding China and the United States)

Our total international market share (excluding China and the United States), defined as our cigarette and heated tobacco unit sales volume as a percentage of total industry cigarette and heated tobacco unit sales volume, increased by 0.1 point to 28.4%, reflecting:

- Total international heated tobacco unit market share of 2.2%, up by 0.6 points; and
- Total international cigarette market share of 26.2%, down by 0.5 points.

Our total international cigarette market share, defined as our cigarette sales volume as a percentage of total industry cigarette sales volume, was down by 0.3 points to 26.9%, mainly reflecting: out-switching to heated tobacco units, notably in the EU and Japan; and lower cigarette market share, notably in Argentina, Indonesia, Korea and Turkey.

In 2019, we owned six of the world's top 15 international cigarette brands, with international cigarette market shares as follows: *Marlboro*, 10.0%; *L&M*, 3.5%; *Chesterfield*, 2.2%; *Philip Morris*, 1.9%; *Parliament*, 1.5%; and *Bond Street*, 1.1%.

Key Market Data

Key market data regarding total market size, our shipments and market share were as follows:

Market	Total Market (billion units)		PMI Shipments (billion units)						PMI Market Share (%)[1]			
			Total		Cigarette		Heated Tobacco Unit		Total		Heated Tobacco Unit	
	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018
Total	2,703.6	2,757.7	766.4	781.7	706.7	740.3	59.7	41.4	28.4	28.3	2.2	1.6
European Union												
France	37.9	40.9	17.0	18.5	16.9	18.4	0.1	—	45.0	45.5	0.2	0.1
Germany	73.3	75.2	27.9	28.1	27.0	27.7	0.9	0.4	38.0	37.3	1.2	0.5
Italy	67.9	69.0	34.9	35.2	31.4	33.5	3.5	1.7	51.8	51.8	4.8	2.2
Poland	46.2	43.2	19.0	17.9	17.9	17.6	1.1	0.4	41.2	41.5	2.5	0.9
Spain	45.3	45.0	14.5	14.1	14.1	13.9	0.3	0.2	31.3	32.1	0.7	0.4
Eastern Europe												
Russia	226.5	238.9	68.0	68.0	58.8	64.6	9.2	3.4	30.1	28.3	3.8	1.0
Middle East & Africa												
Saudi Arabia	20.8	20.6	9.2	7.4	9.2	7.4	—	—	43.0	41.5	—	—
Turkey	118.9	118.5	51.9	55.0	51.9	55.0	—	—	43.7	46.4	—	—
South & Southeast Asia												
Indonesia	306.8	303.6	98.5	101.4	98.5	101.4	—	—	32.1	33.4	—	—
Philippines	70.5	73.2	49.7	51.2	49.7	51.2	—	—	70.5	69.9	—	—
East Asia & Australia												
Australia	12.0	12.8	3.3	3.8	3.3	3.8	—	—	27.5	29.7	—	—
Japan	158.0	167.3	52.4	52.3	26.6	30.8	25.8	21.4	34.5	34.0	17.1	15.5
Korea	68.6	69.5	15.5	17.4	10.8	12.0	4.6	5.4	22.6	25.0	6.8	7.8
Latin America & Canada												
Argentina	33.4	35.0	23.3	25.8	23.3	25.8	—	—	70.0	73.8	—	—
Mexico	35.5	35.5	23.8	24.2	23.8	24.2	—	—	67.1	68.0	—	—

(1) Market share estimates are calculated using IMS data

Note: % change for Total Market and PMI shipments is computed based on millions of units; PMI Market Share estimates for previous periods are restated to reflect RBH deconsolidation and exclude RBH-owned brands.

Financial Summary

Financial Summary - Years Ended December 31, (in millions)	2019	2018	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Cur-rency	Price	Vol/ Mix	Cost/ Other[1]
Net Revenues	**$ 29,805**	$ 29,625	0.6 %	3.8 %	$180	$ (937)	$ 1,483	$ 397	$ (763)
Cost of Sales	**(10,513)**	(10,758)	2.3 %	(0.5)%	245	302	—	(309)	252
Marketing, Administration and Research Costs [2]	**(8,695)**	(7,408)	(17.4)%	(22.0)%	(1,287)	340	—	—	(1,627)
Amortization of Intangibles	**(66)**	(82)	19.5 %	15.9 %	16	3	—	—	13
Operating Income	**$ 10,531**	$ 11,377	(7.4)%	(4.9)%	$(846)	$ (292)	$ 1,483	$ 88	$ (2,125)

[1] *Cost/Other variance includes the impact of the RBH deconsolidation.*

[2] *Unfavorable Cost/Other variance includes asset impairment and exit costs of $422 million in 2019, the Russia excise and VAT audit charge of $374 million in 2019, the 2019 loss on deconsolidation of RBH of $239 million, and the 2019 Canadian tobacco litigation-related expense of $194 million, as well as the impact of the RBH deconsolidation.*

Note: Net Revenues include revenues from shipments of Platform 1 devices, heated tobacco units and accessories to Altria Group, Inc., commencing in the third quarter of 2019, for sale under license in the United States.

Net revenues, excluding unfavorable currency, increased by 3.8%, mainly reflecting: a favorable pricing variance, notably in Germany, Indonesia, Japan, the Philippines and Turkey; and favorable volume/mix, mainly driven by heated tobacco unit and *IQOS* device volume in the EU and Russia, and heated tobacco unit volume in Japan, partly offset by unfavorable volume/mix of cigarettes, notably in Australia, the EU, Indonesia, Japan and Russia, unfavorable heated tobacco unit volume in PMI Duty Free, and unfavorable *IQOS* device volume in Japan and Korea. The currency-neutral growth in net revenues of 3.8% came despite the unfavorable impact of $763 million, shown in "Cost/Other," predominantly resulting from the deconsolidation of RBH.

The unfavorable currency in net revenues was due primarily to the Euro, Russian ruble and Turkish lira.

Net revenues include $5.6 billion in 2019 and $4.1 billion in 2018 related to the sale of RRPs. In 2019, approximately $0.7 billion of our $5.6 billion in RRP net revenues were from *IQOS* devices.

Operating income decreased by 7.4%. Excluding unfavorable currency ($292 million), asset impairment and exit costs ($422 million) in 2019 related to plant closures in Argentina, Colombia, Germany and Pakistan as part of global manufacturing infrastructure optimization, the 2019 Russia excise and VAT audit charge ($374 million), the 2019 loss on deconsolidation of RBH ($239 million) and the 2019 Canadian tobacco litigation-related expense ($194 million), operating income increased by 5.9%, primarily reflecting: a favorable pricing variance; favorable volume/mix, mainly driven by heated tobacco units in the EU, Japan and Russia, partly offset by unfavorable volume/mix of cigarettes, notably in Australia, the EU, Indonesia, Japan and Russia, as well as unfavorable heated tobacco unit volume in PMI Duty Free; and lower manufacturing costs; partly offset by higher marketing, administration and research costs, reflecting increased investment behind reduced-risk products (mainly in the EU and Eastern Europe), and the net unfavorable impact resulting from the deconsolidation of RBH shown in "Cost/Other."

Interest expense, net, of $570 million decreased by $95 million (14.3%), due primarily to our ongoing efforts to optimize our capital structure following the passage of the Tax Cuts and Jobs Act. This included the decision to use existing cash to repay $2.5 billion and $4.0 billion of long-term debt that matured in 2018 and 2019, respectively.

Our effective tax rate increased by 0.3 percentage points to 23.2%. The effective tax rate for the year ended December 31, 2019, was unfavorably impacted by changes in earnings mix by taxing jurisdiction and U.S. state deferred income tax expense, partially offset by the reversal of a deferred tax liability on the unremitted earnings of our Canadian subsidiary, RBH ($49 million), a reduction in estimated U.S. federal income tax on dividend repatriation for the years 2015-2018 ($67 million), and other repatriation cost differences. We estimate that our 2020 effective tax rate will be approximately 23%, excluding discrete tax events. Changes in currency exchange rates, earnings mix by taxing jurisdiction, or dividend repatriation costs may have an impact on the effective tax rates,

which we monitor each quarter. Significant judgment is required in determining income tax provisions and in evaluating tax positions. For further details, see Item 8, Note 11. *Income Taxes*.

We are regularly examined by tax authorities around the world, and we are currently under examination in a number of jurisdictions. It is reasonably possible that within the next 12 months certain tax examinations will close, which could result in a change in unrecognized tax benefits along with related interest and penalties. An estimate of any possible change cannot be made at this time.

Net earnings attributable to PMI of $7.2 billion decreased by $726 million or 9.2%. This decrease was due primarily to lower operating income as discussed above, partially offset by a lower interest expense, net. Diluted and basic EPS of $4.61 decreased by 9.3%. Excluding an unfavorable currency impact of $0.13, diluted EPS decreased by 6.7%.

2018 compared with 2017

For a discussion comparing our consolidated operating results for the year ended December 31, 2018, with the year ended December 31, 2017, refer to Part II, Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operation - Discussion and Analysis - Consolidated Operating Results* in our Annual Report on Form 10-K for the year ended December 31, 2018, which was filed with the U.S. Securities and Exchange Commission on February 7, 2019.

Operating Results by Business Segment

Business Environment

Taxes, Legislation, Regulation and Other Matters Regarding the Manufacture, Marketing, Sale and Use of Tobacco Products

The tobacco industry and our company face a number of challenges that may adversely affect our business, volume, results of operations, cash flows and financial position. These challenges, which are discussed below and in "*Cautionary Factors That May Affect Future Results*," include:

- regulatory restrictions on our products, including restrictions on the packaging, marketing, and sale of tobacco or other nicotine-containing products that could reduce our competitiveness, eliminate our ability to communicate with adult consumers, or even ban certain of our products;
- fiscal challenges, such as excessive excise tax increases and discriminatory tax structures;
- illicit trade in cigarettes and other tobacco products, including counterfeit, contraband and so-called "illicit whites";
- intense competition, including from non-tax paid volume by certain local manufacturers;
- pending and threatened litigation as discussed in Item 8, Note 18. *Contingencies*; and
- governmental investigations.

Regulatory Restrictions: The tobacco industry operates in a highly regulated environment. The well-known risks of smoking have led regulators to impose significant restrictions and high excise taxes on cigarettes.

We support a comprehensive regulatory framework for tobacco products based on the principle of harm reduction, including mandated health warnings, minimum age laws, restrictions on advertising, and public place smoking restrictions. We also support regulatory measures that help reduce illicit trade.

Much of the regulation that shapes the business environment in which we operate is driven by the World Health Organization's ("WHO") Framework Convention on Tobacco Control ("FCTC"), which entered into force in 2005. The FCTC has as its main objective to establish a global agenda for tobacco regulation, with the purpose of reducing tobacco use. To date, 180 countries and the European Union are Parties to the FCTC. The treaty requires Parties to have in place various tobacco control measures and recommends others. The FCTC governing body, the Conference of the Parties ("CoP"), has also adopted non-binding guidelines and policy recommendations related to certain

articles of the FCTC that go beyond the text of the treaty. In October 2018, the CoP recognized the need for more scientific assessment and improved reporting to define policy on heated tobacco products. Similar to its previous policy recommendations on e-cigarettes, the CoP invited countries to regulate, restrict or prohibit heated tobacco products, as appropriate under their national laws.

In July 2019, the WHO issued the Report on the Global Tobacco Epidemic 2019. While citing insufficient independent studies regarding the benefits and the unknown long-term health impacts of electronic nicotine delivery systems and heated tobacco products, the WHO has taken the position that such products are not risk-free and should be regulated in the same manner as cigarettes and in line with the FCTC provisions.

It is not possible to predict whether or to what extent measures recommended by the WHO, including the FCTC guidelines, will be implemented.

We agree that all tobacco and nicotine-containing products, including our RRPs, need to be regulated; however, we continue to seek to engage in a dialogue with regulators with respect to those measures that we do not believe would protect public health and, if implemented, could disrupt competition, severely limit our ability to market and sell our products (including our RRPs) to adult smokers, or increase illicit trade. We advocate for measures that would accelerate switching to better alternatives to continued smoking and embrace a regulatory framework that recognizes a risk continuum of tobacco and other nicotine-containing products.

Certain measures are discussed in more detail below and in the *Reduced-Risk Products (RRPs)* section.

Fiscal Challenges: Excessive and disruptive excise, sales and other tax increases and discriminatory tax structures are expected to continue to have an adverse impact on our profitability, due to lower consumption and consumer down-trading to non-premium, discount, other low-price or low-taxed combustible tobacco products such as fine cut tobacco and illicit cigarettes. In addition, in certain jurisdictions, some of our combustible products are subject to tax structures that discriminate against premium-price products and manufactured cigarettes. We believe that such tax policies undermine public health by encouraging consumers to turn to illicit trade, and ultimately undercut government revenue objectives, disrupt the competitive environment, and encourage criminal activity. Other jurisdictions have imposed, or are seeking to impose, levies or other taxes specifically on tobacco companies, such as taxes on revenues and/or profits.

EU Tobacco Products Directive: In April 2014, the EU adopted a significantly revised EU Tobacco Products Directive (TPD), which entered into force in May 2016. All Member States have adopted laws transposing the TPD. The TPD sets forth a comprehensive set of regulatory requirements for tobacco products, including:

- health warnings covering 65% of the front and back panels of cigarette packs, with an option for Member States to further standardize tobacco packaging, including the introduction of plain packaging;
- a ban on characterizing flavors in some tobacco products, with a transition period for menthol expiring in May 2020;
- security features and tracking and tracing measures that became effective on May 20, 2019; and
- a framework for the regulation of novel tobacco products and e-cigarettes, including requirements for health warnings and information leaflets, a prohibition on product packaging text related to reduced risk, and the introduction of notification requirements or authorization procedures in advance of commercialization.

Plain Packaging and Other Packaging Restrictions: Plain packaging legislation bans the use of branding, logos and colors on packaging other than the brand name and variant that may be printed only in specified locations and in a uniform font. To date, plain packaging laws have been adopted in certain markets in all of our operating segments, including the key markets of Australia, France, Saudi Arabia and Turkey, and are in various degrees of implementation. Some countries, such as Canada, New Zealand and Israel, adopted plain packaging regulations that apply to all tobacco products, including RRPs. Other countries are also considering plain packaging legislation.

Some countries have adopted, or are considering adopting, packaging restrictions that could have an impact similar to plain packaging. Examples of such restrictions include standardizing the shape and size of packages, prohibiting certain colors or the use of certain descriptive phrases on packaging, and requiring very large graphic health warnings that leave little space for branding.

Restrictions and Bans on the Use of Ingredients: The WHO and others in the public health community have recommended restrictions or total bans on the use of some or all ingredients in tobacco products, including menthol. Broad restrictions and ingredient bans would require us to reformulate our American blend tobacco products and could reduce our ability to differentiate these products in the market in the long term. Menthol bans would eliminate the entire category of mentholated tobacco products. The European Union has banned flavored tobacco products, subject to an exemption until May 2020 for menthol. Other countries may follow the EU's approach. For instance, Turkey has banned menthol as of May 2020. Broader ingredient bans have been adopted by Canada and Brazil. In

Brazil, an ingredient ban is currently on appeal by a tobacco industry union, of which our Brazilian subsidiary is a member. It is not possible to predict the outcome of these legal proceedings.

Bans on Display of Tobacco Products at Retail: In a number of our markets, including, but not limited to, Australia and Russia, governments have banned the display of tobacco products at the point of sale. Other countries are considering similar bans.

Bans and Restrictions on Advertising, Marketing, Promotions and Sponsorships: For many years, the FCTC has called for, and countries have imposed, partial or total bans on tobacco advertising, marketing, promotions and sponsorships, including bans and restrictions on advertising on radio and television, in print and on the Internet. The FCTC's non-binding guidelines recommend that governments prohibit all forms of communication with adult smokers.

Restrictions on Product Design: Some members of the public health community are calling for the further standardization of tobacco products by requiring, for example, that cigarettes have a certain minimum diameter, which would amount to a ban on slim cigarettes, or requiring the use of standardized filter and cigarette paper designs. In addition, at its meeting in November 2016, the CoP adopted non-binding guidelines recommending that countries regulate product design features that increase the attractiveness of tobacco products, such as the diameter of cigarettes and the use of flavor capsules.

Restrictions on Public Smoking: The pace and scope of public smoking restrictions have increased significantly in most of our markets. Many countries around the world have adopted, or are likely to adopt, regulations that restrict or ban smoking in public and/or work places, restaurants, bars and nightclubs. Some public health groups have called for, and some countries, regional governments and municipalities have adopted or proposed, bans on smoking in outdoor places, as well as bans on smoking in cars (typically, when minors are present) and private homes.

Other Regulatory Issues: Some regulators are considering, or in some cases have adopted, regulatory measures designed to reduce the supply of tobacco products. These include regulations intended to reduce the number of retailers selling tobacco products by, for example, reducing the overall number of tobacco retail licenses available or banning the sale of tobacco products within specified distances of certain public facilities.

In a limited number of markets, most notably Japan, we are dependent on governmental approvals that may limit our pricing flexibility.

The EU Single-Use Plastics Directive, which will require tobacco manufacturers and importers to cover the costs of public collection systems for tobacco product filters, entered into force on July 2, 2019, after which Member States will have two years to transpose it into national law. While we cannot predict the impact of this initiative on our business at this time, we are monitoring developments in this area.

Illicit Trade: Illicit tobacco trade creates a cheap and unregulated supply of tobacco products, undermines efforts to reduce smoking prevalence, especially among youth, damages legitimate businesses, stimulates organized crime, increases corruption and reduces government tax revenue. Excluding China and the U.S., illicit trade may account for as much as 10% of global cigarette consumption; this includes counterfeit, contraband and the growing problem of "illicit whites," which are cigarettes legally produced in one jurisdiction for the sole purpose of being exported and illegally sold in another jurisdiction where they have no legitimate market. We estimate that illicit trade in the European Union accounted for approximately 10% of total cigarette consumption in 2019.

A number of jurisdictions are considering actions to prevent illicit trade. In November 2012, the FCTC adopted the Protocol to Eliminate Illicit Trade in Tobacco Products (the "Protocol"), which includes supply chain control measures, such as licensing of manufacturers and distributors, enforcement in free trade zones, controls on duty free and Internet sales and the implementation of tracking and tracing technologies. To date, 58 Parties, including the European Union, have ratified it. The Protocol came into force in September 2018. Parties must now start implementing its measures via national legislation. In October 2018, the first Meeting of the Parties to the Protocol decided to produce a comprehensive report on good practices for the implementation of tracking and tracing systems and to prepare a conceptual framework for global information sharing to combat illicit tobacco trade. We welcome this decision and expect that other Parties will ratify the Protocol.

We devote substantial resources to help prevent illicit trade in combustible tobacco products and RRPs. For example, we engage with governments, our business partners and other stakeholders to implement effective measures to combat illicit trade and, in some instances, pursue legal remedies to protect our intellectual property rights.

The tracking and tracing regulations for cigarettes and roll-your-own products manufactured or destined for the EU became effective on May 20, 2019. The effective date for other tobacco-containing products, including some of our RRPs such as heated tobacco units, is May 20, 2024. While we expect that this regulation will increase our operating expenses, we do not expect this increase to be significant.

In 2009, our Colombian subsidiaries entered into an Investment and Cooperation Agreement with the national and regional governments of Colombia to promote investment in, and cooperation on, anti-contraband and anti-counterfeit efforts. The agreement provides $200

million in funding over a 20-year period to address issues such as combating illegal cigarette trade and increasing the quality and quantity of locally-grown tobacco.

In May 2016, PMI launched PMI IMPACT, a global initiative that supports third-party projects dedicated to fighting illegal trade and related crimes such as corruption, organized criminal networks and money laundering. The centerpiece of PMI IMPACT is a council of external independent experts in the fields of law, anti-corruption and law enforcement. The experts are responsible for evaluating and approving funding proposals for PMI IMPACT grants. PMI has pledged $100 million to fund projects within PMI IMPACT over three funding rounds.

Reduced-Risk Products (RRPs)

Our Approach to RRPs: We recognize that smoking cigarettes causes serious diseases and that the best way to avoid the harms of smoking is never to start or to quit. Nevertheless, it is predicted that over the next decade the number of smokers will remain largely unchanged from the current estimate of 1.1 billion, despite the considerable efforts to discourage smoking.

Cigarettes burn tobacco, which produces smoke. As a result of the combustion process, the smoker inhales various toxic substances. In contrast, RRPs do not burn tobacco and produce an aerosol that contains significantly lower levels of harmful and potentially harmful constituents ("HPHCs") than found in cigarette smoke.

For smokers who would otherwise continue to smoke, we believe that RRPs, while not risk-free, offer a much better consumer choice. Accordingly, our key strategic priorities are: to develop and commercialize products that present less risk of harm to adult smokers who switch to those products versus continued smoking; and to convince current adult smokers who would otherwise continue to smoke to switch to those products.

We recognize that this transformation from cigarettes to RRPs will take time and that the speed of transformation will depend in part upon factors beyond our control, such as the willingness of governments, regulators and other policy groups to embrace RRPs as a desired alternative to continued cigarette smoking. We also recognize that our part in this transformation must be funded from our existing cigarette business. For as long as a significant number of adult smokers continues to smoke, it is critical that the industry be led by responsible and ethical manufacturers. Therefore, during the transformation, we intend to remain a leading international cigarette manufacturer.

We have a range of RRPs in various stages of development, scientific assessment and commercialization. We conduct rigorous scientific assessments of our RRP platforms to substantiate that they reduce exposure to HPHCs and, ultimately, that these products present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to them versus continued smoking. We draw upon a team of expert scientists and engineers from a broad spectrum of scientific disciplines and our extensive learnings of adult consumer preferences to develop and assess our RRPs. Our efforts are guided by the following key objectives:

- to develop RRPs that adult smokers who would otherwise continue to smoke find to be satisfying alternatives to smoking;
- for those adult smokers, our goal is to offer RRPs with a scientifically substantiated risk-reduction profile that approaches as closely as possible that associated with smoking cessation;
- to substantiate the reduction of risk for the individual adult smoker and the reduction of harm to the population as a whole, based on scientific evidence of the highest standard that is made available for scrutiny and review by external independent scientists and relevant regulatory bodies; and
- to advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs, including the communication of scientifically substantiated information to enable adult smokers to make better consumer choices.

Our RRP Platforms: Our product development is based on the elimination of combustion via tobacco heating and other innovative systems for aerosol generation, which we believe is the most promising path to providing a better consumer choice for those who would otherwise continue to smoke. We recognize that no single product will appeal to all adult smokers. Therefore, we are developing a portfolio of products intended to appeal to a variety of distinct adult consumer preferences.

Four RRP platforms are in various stages of development and commercialization readiness:

Platform 1 uses a precisely controlled heating device incorporating our *IQOS HeatControl* technology, into which a specially designed and proprietary tobacco unit is inserted and heated to generate an aerosol. We have conducted a series of clinical studies for this platform, the results of which were included in our submission to the U.S. Food and Drug Administration ("FDA") described below.

The results of the first six-month term of the 6+6 month exposure response study were received at the end of 2017, and the related report was completed and submitted to the FDA in the second quarter of 2018. The study showed that all eight of the co-primary clinical risk endpoints moved in the same direction in the group that switched to our Platform 1 product as observed for smoking cessation, with statistically significant changes in five of the eight endpoints compared with on-going smoking. The results of the second six-month term of the 6+6 month exposure response study were received for analysis in the second quarter of 2018; we are analyzing the results, and expect to finalize the report later this year. In addition, as set out in our submission to the FDA referenced above, we completed an 18-month combined chronic toxicity and carcinogenicity study in mice, which was on-going at the time of our FDA submission. We shared the results with the FDA in August 2018.

Platform 2 uses a pressed carbon heat source which, when ignited, generates a nicotine-containing aerosol by heating tobacco. The results of our pharmacokinetic study (that measured the nicotine pharmacokinetic profile as well as subjective effects) and of our five-day reduced exposure study indicate that this platform could be an acceptable substitute for adult smokers who seek an alternative to cigarettes. The reduced exposure study results showed a substantial reduction in relevant biomarkers of exposure to the measured HPHCs in those who switched to Platform 2 compared to those who continued to smoke cigarettes over a five-day period. The sustainability of this reduction as well as changes in clinical risk markers were assessed in a three-month reduced exposure study. The results of this study were received at the end of 2017, and the related report was finalized in the second quarter of 2018.

Platform 3 provides an aerosol of nicotine salt. We have explored two routes for this platform, one with electronics and one without, and conducted nicotine pharmacokinetic studies with both versions. The results of the pharmacokinetic study related to the version without electronics were received, and the related report was finalized in the fourth quarter of 2018. The results indicate this product's potential as an acceptable alternative to continued cigarette smoking in terms of product satisfaction. We are conducting a product use and adaptation study in adult smokers and expect the results in 2020.

Platform 4 covers e-vapor products, which are battery-powered devices that produce an aerosol by vaporizing a nicotine-containing liquid solution. Our e-vapor products comprise devices using current generation technology and our new e-vapor mesh technology that addresses certain challenges presented by some e-vapor products currently on the market. Our *IQOS MESH* products are designed to ensure the consistency and quality of the generated aerosol. We conducted a nicotine pharmacokinetic study in 2017. The results of this study were received in the second quarter of 2018 for analysis, and the related report was finalized in the fourth quarter of 2018. The results of this study indicate that *IQOS MESH* products are an effective means of nicotine delivery while being a satisfying alternative for e-cigarette users. In March 2019, a six-month pre-clinical study in mice evaluating the impact of e-cigarette vapor on the risks of pulmonary and cardiovascular disease compared to cigarette smoke was completed; this study did not pertain to a specific product. The study demonstrated that e-cigarette vapors induce significantly lower biological responses associated with cardiovascular and pulmonary diseases compared with cigarette smoke. We will also initiate a clinical study to measure selected biomarkers of exposure to HPHCs and assess changes in clinical risk markers.

After we receive the results of our scientific studies mentioned above, in accordance with standard scientific practices, we intend to share the conclusions in scientific forums and to submit them for inclusion in peer-reviewed publications.

The research and development expense for our RRP portfolio accounted for 98%, 92% and 74% of our total research and development expense for the years ended December 31, 2019, 2018 and 2017, respectively. The research and development expense for the years ended December 31, 2019, 2018 and 2017, is set forth in Item 8, Note 14. *Additional Information* to the consolidated financial statements.

Commercialization of RRPs: We are building a new product category and tailor our commercialization strategy to the characteristics of each specific market. We focus our commercialization efforts on consumer retail experience, guided consumer trials and customer care, as well as digital communication programs. In order to accelerate switching to our Platform 1 product, our initial market introductions typically entail one-on-one consumer engagement and introductory device discounts. These initial commercialization efforts require substantial investment, which we believe will moderate over time.

In 2014, we introduced our Platform 1 product in pilot city launches in Nagoya, Japan, and in Milan, Italy. Since then, we have continuously expanded our commercialization activities, and the product is currently available for sale in 52 markets in key cities or nationwide.

We estimate that only a very small percentage of adult smokers who convert to our Platform 1 product switch back to cigarettes.

We have integrated the production of our heated tobacco units into a number of our existing manufacturing facilities, are progressing with our plans to build manufacturing capacity for our other RRP platforms, and continue to optimize our manufacturing infrastructure.

An adequate supply chain for our RRP portfolio, including the supply of electronic devices, is important to our business. We work with two electronics manufacturing service providers for the supply of our Platform 1 and *IQOS MESH* devices and a small number of other

providers for other products in our RRP portfolio and related accessories. Although we work closely with these service providers on monitoring their production capability and financial health, the commercialization of our RRPs could be adversely affected if they are unable to meet their commitments. The production of our RRP portfolio requires various metals, and we believe that there is an adequate supply of such metals in the world markets to satisfy our current and anticipated production requirements. However, some components and materials necessary for the production of our RRPs, including those for the electronic devices, are obtained from single or limited sources, and can be subject to industry-wide shortages and price fluctuations. Our inability to secure an adequate supply of such components and materials could negatively impact the commercialization of our RRPs.

Our Platform 1 and *IQOS MESH* devices are subject to standard product warranties generally for a period of 12 months from the date of purchase or such other periods as required by law. We discuss product warranties in more detail in Item 8, Note 5. *Product Warranty*. The significance of warranty claims is dependent on a number of factors, including device version mix, product failure rates, logistics and service delivery costs, and warranty policies, and may increase with the number of devices sold.

Product quality may affect consumer acceptance of our RRPs.

Our commercialization efforts for the other RRP platforms are as follows:

- We currently market our e-vapor products in Ireland and the U.K. In July 2018, we pilot-launched *IQOS MESH*, one of our Platform 4 products, in London, U.K. In light of the current confusion in the e-vapor category, we have postponed our planned launch of an improved version of this product until the third quarter of 2020, when we expect to reach the optimal capacity for commercialization at scale.

- We completed a small-scale city test of *TEEPS*, our Platform 2 product, that we had initiated in December 2017 in Santo Domingo, the Dominican Republic. We are finalizing our improvements to this product and plan to conduct a consumer test by the end of 2020.

- Depending on the outcome of the use and adaptation study described above as well as consumer research, we plan to conduct a consumer test of our Platform 3 product by the end of 2020.

RRP Regulation and Taxation: RRPs contain nicotine and are not risk-free. We therefore support science-based regulation and taxation of RRPs. Regulation and taxation should differentiate between cigarettes and products that present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to these products versus continued smoking and should recognize a continuum of risk for tobacco and other nicotine-containing products. Regulation should provide minimum standards for all RRP categories and specific rules for product assessment methodologies, ingredients, labeling and consumer communication, and should ensure that the public is informed about the health risks of all combustible and non-combustible tobacco and nicotine-containing products. Regulation, as well as industry practices, should reflect the fact that youth should not consume nicotine in any form.

Some governments have banned or are seeking to ban or severely restrict emerging tobacco and nicotine-containing products such as our RRPs and communication of truthful and non-misleading information about such products. These regulations might foreclose or unreasonably restrict adult consumer access even to products that might be shown to be a better consumer choice than continuing to smoke. We oppose such blanket bans and unreasonable restrictions of products that have the potential to present less risk of harm compared to continued smoking. By contrast, we support regulation that sets clear standards for all RRP categories and propels innovation to benefit adult smokers who would otherwise continue to smoke.

In the United States, an established regulatory framework for assessing "Modified Risk Tobacco Products" and "New Tobacco Products" exists under the jurisdiction of the FDA. We submitted to the FDA a Modified Risk Tobacco Product Application ("MRTPA") for our Platform 1 product in December 2016, and a Premarket Tobacco Product Application ("PMTA") for our Platform 1 product in March 2017.

On April 30, 2019, the FDA determined that a version of our Platform 1 product is appropriate for the protection of public health and authorized it for sale in the United States. The FDA's decision followed its comprehensive assessment of our PMTA.

The FDA's marketing order does not mean that the agency "approved" our Platform 1 product. The authorization is subject to strict marketing, reporting and other requirements and is not a guarantee that the product will remain authorized, particularly if there is a significant uptake in youth initiation. The FDA will monitor the marketing of the product.

We plan to file a PMTA application for the *IQOS 3* device in the coming months.

In May 2017, the FDA formally accepted and filed our MRTPA for substantive scientific review and, in June 2017, the FDA opened the period for the public to provide comments on our application. The FDA closed the public comment period on February 11, 2019. In late 2019, we provided a response to the FDA's request for clarification regarding our mice study described above. Following our response, the FDA re-opened a public comment period ending February 24, 2020.

The FDA referred our MRTPA to the Tobacco Product Scientific Advisory Committee ("TPSAC"). TPSAC held a meeting on January 24 and January 25, 2018 to discuss our MRTPA. The recommendations and votes of TPSAC are not binding on the FDA. By regulation, the FDA's decision on our MRTPA will take into account, in addition to the views of TPSAC, scientific evidence as well as comments, data and information submitted by interested persons.

The FDA review of our MRTPA is on-going.

Separately, in July 2017, the FDA issued a policy announcement aiming to explore the potential of nicotine reduction in cigarettes in conjunction with the availability of less harmful products that deliver nicotine for adults who choose to use such products. In July 2018, as part of a public consultation procedure, we submitted our views on this topic to the FDA. It is not possible to predict the regulatory measures that may be recommended by the FDA as a result of this policy.

In the U.S., tobacco and nicotine-containing products that were not commercially marketed as of February 15, 2007 are subject to review and authorization by the FDA. Following a rise in the use of e-vapor products among minors in the U.S. and an outbreak of lung injuries alleged to be associated with the use of certain e-vapor products in many states, on January 2, 2020, the FDA announced an enforcement policy against the sale of e-vapor products sold without FDA authorization, prioritizing enforcement against the sale of cartridge-based e-vapor products with flavors other than tobacco and menthol, and sale of any nicotine-containing products to minors and where the manufacturer fails to take adequate measures to prevent access by minors.

While we do not sell e-vapor products in the U.S. and therefore are not subject to these actions, we continue to support regulation and industry practices that reflect the fact that youth should not consume nicotine in any form.

Future FDA actions may influence the regulatory approach of other governments.

Until recently, there were no countries with specific product standards for heat-not-burn products. Effective July 2017 and March 2018, respectively, Russia and Ukraine adopted standards that set minimum quality and safety requirements for the consumables and defined methods for demonstrating the absence of combustion, and the product standards in Kazakhstan that came into force in March 2019 also cover devices. In the UAE, a product standard on minimum quality and safety of electronic nicotine-containing products, including heat-not-burn products, was approved in March 2019. Effective December 2019, Jordan adopted a national standard for heat-not-burn products (both devices and consumables), and defined a method for demonstrating the absence of combustion in these products. We expect and encourage other governments to consider similar product standards going forward.

In the EU, all EU Member States have transposed the EU Tobacco Products Directive, including the provisions on novel tobacco products, such as heated tobacco units, and e-cigarettes. Most of the EU Member States require a notification submitted six months before the intended placing on the market of a novel tobacco product, while some require pre-market authorizations for the introduction of such products. To date, we have filed a comprehensive dossier summarizing our scientific assessment of our Platform 1 product in over 20 Member States.

In addition, in Italy, in April 2018, we submitted under recent legislation an application for *HEETS*, used with the *IQOS* device, requesting regulatory recognition of the reduction of toxic substances and potential risk reduction resulting from switching to this product compared to continued cigarette smoking. In January 2019, our application was not granted primarily on the grounds of insufficient data and questions of methodology. Due to the constraints of the review process, we had been unable to supplement the application with all the data we subsequently filed with the FDA and to address methodological questions during the review. We plan to submit a new application where we will clarify the concerns raised by the decision and further strengthen our application by submitting additional evidence that became available since we submitted our first application, consistent with our FDA filing. We are confident that our evidence supports our application.

To date, several governmental agencies have published their scientific findings that analyze the harm-reduction potential of certain RRPs versus continuing smoking, including:

In December 2017, at the request of the U.K. Department of Health and Public Health England, the U.K. Committee on Toxicity published its assessment of the risk of heat-not-burn products relative to cigarette smoking. This assessment included analysis of scientific data for two heat-not-burn products, one of which was our Platform 1 product. The assessment concluded that, while still harmful to health,

compared with the known risks from cigarettes, heat-not-burn products are probably less harmful. Subsequently, in February 2018, Public Health England published a report stating that the available evidence suggests that heat-not-burn products may be considerably less harmful than cigarettes and more harmful than e-cigarettes.

In May 2018, the German Federal Institute for Risk Assessment ("BfR") published a study on the Platform 1 aerosol relative to cigarette smoke using the Health Canada Intense Smoking Regimen. BfR found reductions in selected HPHCs in a range of 80-99%. This publication indicates that significant reductions in the levels of selected toxicants are likely to reduce toxicant exposure, which BfR stated might be regarded as a discrete benefit compared to combustible cigarettes.

In May 2018, the Dutch National Institute for Public Health and Environment ("RIVM") published a factsheet on novel tobacco products that heat rather than burn tobacco, focusing on our Platform 1 product. RIVM analyzed the aerosol generated by our Platform 1 product and concluded that the use of this product, while still harmful to health, is probably less harmful than continued smoking.

In June 2018, the Korean Food and Drug Administration ("KFDA") issued a statement on products that heat rather than burn tobacco. The KFDA tested three heat-not-burn products, one of which was our Platform 1 product. The KFDA confirmed that the levels of the nine HPHCs tested in the aerosol of these products were on average approximately 90% lower compared to those measured in the cigarette smoke of the top five cigarette brands in South Korea. However, the KFDA stated that it could not establish that the tested heat-not-burn products are less harmful than cigarettes. In October 2018, our Korean affiliate filed a request with a local court seeking information underlying KFDA's analysis, conclusions and public statements.

In August 2018, the Science & Technology Committee of the U.K. House of Commons published a report of its inquiry into e-cigarettes and heat-not-burn products. The report concluded that e-cigarettes are significantly less harmful to health than smoking tobacco. The report also observed that for those smokers who don't accept e-cigarettes, heat-not-burn products may offer a public health benefit despite their relative risk. The report called for a risk-proportionate regulatory environment for both e-cigarettes and heat-not-burn products and noted that e-cigarettes should remain the least taxed, cigarettes the most taxed, with heat-not-burn products falling between the two. The U.K. Committee on Advertising Practice announced the removal of a prohibition of health claims in the advertising of e-cigarettes in the U.K. effective November 2018, with a review of the impact of this decision on market practices 12 months thereafter.

In November 2018, the Eurasian Economic Commission (regulatory body of the Eurasian Union consisting of Armenia, Belarus, Kazakhstan, Kyrgyzstan and Russia) published the results of its commissioned study on novel nicotine-containing products, including our Platform 1 product. The study confirms significantly lower levels of HPHCs in the aerosol generated by this product compared to cigarette smoke.

In January 2019, scientific media published the results of the study of the China National Tobacco Quality Supervision and Test Centre ("CNTQST") comparing the aerosol generated by our Platform 1 product with cigarette smoke. The CNTQST found that the former contained fewer, and lower levels of, harmful constituents than the latter and concluded that the lower temperature of heating tobacco in our Platform 1 product contributed to the difference. The CNTQST stated that the reduction in emissions of harmful constituents cannot be interpreted as equivalent to a proportionate harm/risk reduction for smokers.

We make our scientific findings publicly available for scrutiny and peer review through several channels, including our websites. From time to time, adult consumers, competitors, members of the scientific community, and others inquire into our scientific methodologies, challenge our scientific conclusions or request further study of certain aspects of our RRPs and their health effects. We are committed to a robust and open scientific debate but believe that such debate should be based on accurate and reliable scientific information. We seek to provide accurate and reliable scientific information about our RRPs; nonetheless, we may not be able to prevent third-party dissemination of false, misleading or unsubstantiated information about these products. The dissemination of scientifically unsubstantiated information or studies with a strong confirmation bias by third parties may cause confusion among adult smokers and affect their decision to switch to better alternatives to continued smoking, such as our RRPs.

To date, we have been largely successful in demonstrating to regulators that our heated tobacco units are not cigarettes due to the absence of combustion, and as such they are generally taxed either as a separate category or as other tobacco products, which typically yields more favorable tax rates than cigarettes. Although we believe that this is sensible from the public health perspective, we cannot guarantee that regulators will continue this approach.

There can be no assurance that we will succeed in our efforts to replace cigarettes with RRPs or that regulation will allow us to commercialize RRPs in all markets, to communicate about our RRPs, including making scientifically substantiated risk-reduction claims, or to treat RRPs differently from cigarettes.

Legal Challenges to RRPs: We face various administrative and legal challenges related to certain RRP activities, including allegations concerning product classification, advertising restrictions, corporate communications, product coach activities, scientific substantiation, product liability, and unfair competition. While we design our programs to comply with relevant regulations, we expect these or similar challenges to continue as we expand our efforts to commercialize RRPs and to communicate publicly. The outcomes of these matters may affect our RRP commercialization and public communication activities and performance in one or more countries.

Our RRP Business Development Initiatives: In December 2013, we established a strategic framework with Altria Group, Inc. ("Altria") setting out terms on how the parties would collaborate to develop and commercialize e-vapor products and commercialize two of our RRPs in the U.S. In late 2018, Altria announced that it will participate in the e-vapor category only through another e-vapor company in which Altria acquired a minority interest. Regarding heat-not-burn products, as discussed above, the FDA has authorized a version of our Platform 1 product for sale in the U.S., and we are seeking authorization for our MRTP submission. These efforts are not affected by Altria's e-vapor announcement. In September 2019, Altria's subsidiary, Philip Morris USA Inc., began commercialization of a version of our Platform 1 product in the U.S.

In January 2020, we announced an agreement with KT&G, a leading tobacco and nicotine company in South Korea, for the commercialization of KT&G's smoke-free products outside of South Korea on an exclusive basis. For more information, see *Acquisitions and Other Business Arrangements* below.

Other Developments: In September 2017, we announced our support of the Foundation for a Smoke-Free World. We agreed to contribute $80 million per year over the next 12 years, as specified in the agreement. We made an initial contribution of $4.5 million in 2017, the first annual contribution of $80 million in the first quarter of 2018 and the second annual contribution of $80 million in the first quarter of 2019. The Foundation is an independent body and is governed by its independent Board of Directors. The Foundation's role, as set out in its corporate charter, includes funding research in the field of tobacco harm reduction, encouraging measures that reduce the harm caused by smoking, and assessing the effect of reduced cigarette consumption on the industry value chain.

Governmental Investigations

From time to time, we are subject to governmental investigations on a range of matters, including tax, customs, antitrust, advertising, and labor practices. We describe certain matters pending in Thailand, Russia and South Korea in Item 8, Note 18. *Contingencies*.

In November 2010, a WTO panel issued its decision in a dispute relating to facts that arose from August 2006 between the Philippines and Thailand concerning a series of Thai customs and tax measures affecting cigarettes imported by PM Thailand into Thailand (see Item 8, Note 18. *Contingencies* for additional information). The WTO panel decision, which was upheld by the WTO Appellate Body, concluded that Thailand had no basis to find that PM Thailand's declared customs values and taxes paid were too low, as alleged by the DSI in 2009. The decision also created obligations for Thailand to revise its laws, regulations, or practices affecting the customs valuation and tax treatment of future cigarette imports. Thailand agreed in September 2011 to fully comply with the decision by October 2012. The Philippines asserts that to date Thailand has not fully complied with the WTO panel decision. The Philippines has repeatedly expressed concerns with ongoing investigations by Thailand of PM Thailand, including those that led to the criminal charges described in Item 8, Note 18. *Contingencies*, and has commenced two formal proceedings at the WTO to challenge criminal charges against PM Thailand arguing that the criminal charges appear to be based on grounds not supported by WTO customs valuation rules and inconsistent with several decisions already taken by Thai Customs and other Thai governmental agencies. On November 12, 2018 and July 12, 2019, the WTO issued its decisions agreeing with the Philippines that the criminal charges against PM Thailand and its former and current employees in connection with import entries of cigarettes from the Philippines and Indonesia, respectively, described in Item 8, Note 18. *Contingencies*, are inconsistent with WTO customs valuation rules. In January 2019 and September 2019, Thailand appealed the WTO's decision related to the criminal charges in connection with import entries of cigarettes from the Philippines and Indonesia, respectively. It is not possible to predict any future developments in these proceedings while the WTO Appellate Body is not operational.

U.S. GAAP Treatment of Argentina as a Highly Inflationary Economy

Following the categorization of Argentina by the International Practices Task Force of the Center for Audit Quality as a country with a three-year cumulative inflation rate greater than 100%, the country is considered highly inflationary

in accordance with U.S. GAAP. Consequently, we began to account for the operations of our Argentinian affiliates as highly inflationary, and to treat the U.S. dollar as the functional currency of the affiliates, effective July 1, 2018.

Asset Impairment and Exit Costs

We discuss asset impairment and exit costs in Item 8, Note 21. *Asset Impairment and Exit Costs* to our consolidated financial statements.

As part of our transformation to a smoke-free future, we also seek to optimize our organizational design. In January 2020, we commenced the first phase of a two-phase restructuring project in Switzerland. This phase may impact approximately 265 existing positions that will be eliminated or relocated, and we initiated consultation procedures for the impacted employees as required under the law. The second phase of this restructuring project is expected to commence in the second quarter of 2020.

Acquisitions and Other Business Arrangements

We discuss our acquisitions in Item 8, Note 6. *Acquisitions* to our consolidated financial statements.

On August 27, 2019, we announced that we were in discussions with Altria Group, Inc. regarding a potential all-stock, no premium merger of equals, and on September 25, 2019, we announced that the merger discussions had ended and that both companies agreed to focus on launching our Platform 1 product in the United States.

Global Collaboration Agreement with KT&G

In January 2020, PMI announced a global collaboration agreement with the leading tobacco and nicotine company in South Korea, KT&G, to commercialize KT&G's smoke-free products outside of the country. The agreement will run for an initial period of three years. The two companies plan for global collaboration with the intention to actively expand to cover many markets, based on commercial success. The agreement allows PMI to distribute current KT&G smoke-free products, and their evolutions, on an exclusive basis, and does not restrict PMI from distributing its own or third-party products. KT&G's smoke-free product brand portfolio includes heat-not-burn tobacco products (e.g., *Lil Mini* and *Lil Plus*), hybrid technologies that combine heat-not-burn tobacco and e-vapor technologies (e.g., *Lil Hybrid*), and e-vapor products (e.g., *Lil Vapor*). PMI will be responsible for the commercialization of smoke-free products supplied under the agreement.

Products sold under the agreement will be subject to careful assessment to ensure they meet the regulatory requirements in the markets where they are launched, as well as our standards of quality and scientific substantiation of their harm reduction potential. PMI and KT&G will seek any necessary regulatory approvals that may be required on a market-by-market basis. There are no current plans to commercialize KT&G products in the United States.

Investments in Unconsolidated Subsidiaries and Equity Securities

We discuss our investments in unconsolidated subsidiaries and equity securities in Item 8, Note 4. *Related Parties - Investments in Unconsolidated Subsidiaries, Equity Securities and Other* and Item 8, Note 16. *Fair Value Measurements* to our consolidated financial statements.

Trade Policy

We are subject to various trade restrictions imposed by the United States of America and countries in which we do business ("Trade Sanctions"), including the trade and economic sanctions administered by the U.S. Department of the Treasury's Office of Foreign Assets Control and the U.S. Department of State. It is our policy to comply fully with these Trade Sanctions.

Tobacco products are agricultural products under U.S. law and are not technological or strategic in nature. From time to time we make sales in countries subject to Trade Sanctions, either where such sanctions do not apply to our business or pursuant to exemptions or licenses.

A subsidiary sells products to distributors that, in turn, sell those products to duty free customers that supply U.N. peacekeeping forces around the world, including those in the U.N. peacekeeping mission located in Abyei, a special administrative territory in Sudan. We do not believe that these sales, which are not subject to Trade Sanctions, and

are *de minimis* in volume and value, present a material risk to our shareholders, our reputation or the value of our shares. We have no employees, operations or assets in the Sudan.

To our knowledge, none of our commercial arrangements results in the governments of any country identified by the U.S. government

as a state sponsor of terrorism, nor entities controlled by those governments, receiving cash or acting as intermediaries in violation of U.S. laws.

We do not sell products in Iran, North Korea and Syria. From time to time, we explore opportunities to sell our products in one or more of these countries, as permitted by law.

Certain states within the U.S. have enacted legislation permitting or requiring state pension funds to divest or abstain from future investment in stocks of companies that do business with certain countries that are sanctioned by the U.S. We do not believe such legislation has had a material effect on the price of our shares.

2019 compared with 2018

The following discussion compares operating results within each of our operating segments for 2019 with 2018.

Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units.

European Union:

Financial Summary - Years Ended December 31, (in millions)	**2019**	**2018**	**Change Fav./(Unfav.)**		**Variance Fav./(Unfav.)**				
			Total	**Excl. Curr.**	**Total**	**Cur-rency**	**Price**	**Vol/ Mix**	**Cost/ Other**
Net Revenues	**$ 9,817**	$ 9,298	5.6 %	11.6 %	$ 519	$ (563)	$ 288	$ 794	$ —
Operating Income	**$ 3,970**	$ 4,105	) (3.3 %	4.8 %	$ (135)	$ (330)	$ 288	$ 587	$ (680)

Net revenues, excluding unfavorable currency, increased by 11.6%, reflecting a favorable pricing variance, driven principally by France and Germany, partly offset by Poland; and favorable volume/mix, primarily driven by heated tobacco unit and *IQOS* device volume, notably in the Czech Republic, Germany, Greece, Italy and Poland, partly offset by lower cigarette volume, notably in France and Italy, and unfavorable cigarette volume/mix in Germany.

The net revenues of the European Union segment include $1,724 million in 2019 and $865 million in 2018 related to the sale of RRPs.

Operating income decreased by 3.3%. Excluding asset impairment and exit charges of $342 million in 2019 related to the plant closure in Germany and unfavorable currency of $330 million, operating income increased by 13.1% mainly reflecting: a favorable pricing variance; favorable volume/mix, primarily driven by heated tobacco unit volume, notably in the Czech Republic, Germany, Greece, Italy and Poland, partly offset by lower cigarette volume, notably in France and Italy, and unfavorable cigarette volume/mix in Germany; partially offset by higher manufacturing costs and higher marketing, administration and research costs, notably related to increased investment behind reduced-risk products.

European Union - Total Market, PMI Shipment and Market Share Commentaries

Total market, PMI shipment volume and market share performance are shown in the table below:

European Union Key Data	**Full-Year**		
	2019	**2018**	**Change % / pp**
Total Market (billion units)	**482.5**	484.5	(0.4 %)
PMI Shipment Volume (million units)			
Cigarettes	**174,319**	179,622	(3.0 %)
Heated Tobacco Units	**12,569**	5,977	+100.0%
Total European Union	**186,888**	185,599	0.7 %
PMI Market Share			
Marlboro	**18.0 %**	18.5 %	(0.5)
L&M	**6.7 %**	6.9 %	(0.2)
Chesterfield	**5.8 %**	5.9 %	(0.1)
Philip Morris	**2.7 %**	2.9 %	(0.2)
HEETS	**2.5 %**	1.2 %	1.3
Others	**3.1 %**	3.1 %	—
Total European Union	**38.8 %**	38.5 %	0.3

The estimated total market in the EU decreased by 0.4% to 482.5 billion units, notably due to:

- France, down by 7.4%, primarily reflecting the impact of significant excise tax-driven price increases and a higher prevalence of illicit trade;
- Germany, down by 2.5%, primarily reflecting the impact of price increases in 2018 and March 2019; and
- Italy, down by 1.5%, primarily reflecting the impact of price increases in 2018 and the first quarter of 2019;

partly offset by

- Poland, up by 6.8%, primarily reflecting a lower prevalence of illicit trade; and
- Spain, up by 0.8%, partly reflecting a lower prevalence of illicit trade.

Our total shipment volume increased by 0.7% to 186.9 billion units, reflecting:

- higher heated tobacco unit shipment volume across the Region (notably Italy), driven by higher market share;

partly offset by

- lower cigarette shipment volume, mainly in France, due to the lower total market and lower cigarette market share, as well as Germany and Italy, partly reflecting out-switching to heated tobacco units.

Our Regional market share increased by 0.3 points to 38.8%, with gains in the Czech Republic, Germany, Greece and Portugal, partly offset by declines in France, Poland and Spain.

Eastern Europe:

Financial Summary - Years Ended December 31, (in millions)	2019	2018	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Cur-rency	Price	Vol/ Mix	Cost/ Other
Net Revenues	**$ 3,282**	$ 2,921	12.4 %	16.1 %	$ 361	$ (108)	$ 85	$ 384	$ —
Operating Income	**$ 547**	$ 902	(39.4 %)	(41.9 %)	$ (355)	$ 23	$ 85	$ 109	$ (572)

Net revenues, excluding unfavorable currency, increased by 16.1%, reflecting a favorable pricing variance, mainly driven by Russia and Ukraine, and favorable volume/mix, predominantly driven by heated tobacco unit and *IQOS* device volume in Russia and Ukraine, and heated tobacco unit volume in Kazakhstan, partly offset by unfavorable cigarette volume/mix in Russia and lower cigarette volume in Ukraine.

The net revenues of the Eastern Europe segment include $844 million in 2019 and $324 million in 2018 related to the sale of RRPs.

Operating income decreased by 39.4%. Excluding the unfavorable impact of $374 million related to the Russia excise and VAT audit charge, and favorable currency of $23 million, operating income decreased by 0.4%, due to: higher marketing, administration and research costs, notably reflecting increased investments behind reduced-risk products (primarily in Russia in support of geographic expansion); and higher manufacturing costs; partly offset by a favorable pricing variance; and favorable volume/mix, predominantly driven by heated tobacco unit volume in Kazakhstan, Russia and Ukraine, partly offset by unfavorable cigarette volume/mix in Russia.

Eastern Europe - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in Eastern Europe decreased by 5.4% to 397.4 billion units, notably due to:

- Russia, down by 5.2%, primarily reflecting the impact of price increases, as well as an increase in the prevalence of illicit trade; and

- Ukraine, down by 12.0%, primarily reflecting the impact of excise tax-driven price increases, as well as an increase in the prevalence of illicit trade;

partly offset by

- Kazakhstan, up by 5.7%, partly reflecting a lower prevalence of illicit trade.

Our Regional market share increased by 1.6 points to 28.7%.

PMI Shipment Volume (million units)	Full-Year 2019	2018	Change
Cigarettes	**100,644**	108,718	(7.4 %)
Heated Tobacco Units	**13,453**	4,979	+100.0%
Total Eastern Europe	**114,097**	113,697	0.4 %

PMI's total shipment volume increased by 0.4% to 114.1 billion units, notably reflecting:

- Kazakhstan, up by 11.6%, reflecting the higher total market and a higher market share of heated tobacco units;

partly offset by

- Ukraine, down by 3.0%, reflecting the lower total market, partly offset by a higher market share of heated tobacco units.

Middle East & Africa:

Financial Summary - Years Ended December 31, (in millions)	2019	2018	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Currency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/Mix	Variance Fav./(Unfav.) Cost/Other
Net Revenues	**$ 4,042**	$ 4,114	(1.8)%	2.2%	$ (72)	$ (162)	$ 207	$ (113)	$ (4)
Operating Income	**$ 1,684**	$ 1,627	3.5 %	6.8%	$ 57	$ (53)	$ 207	$ (128)	$ 31

Net revenues, excluding unfavorable currency, increased by 2.2%, mainly reflecting: a favorable pricing variance, primarily driven by Egypt, the GCC, PMI Duty Free and Turkey, partly offset by Morocco; partially offset by unfavorable volume/mix, mainly due to heated tobacco unit and cigarette volume in PMI Duty Free, as well as cigarette volume in Kuwait, partly offset by favorable cigarette volume in Egypt and favorable cigarette volume/mix in Algeria and Saudi Arabia.

The net revenues of the Middle East & Africa segment include $321 million in 2019 and $382 million in 2018 related to the sale of RRPs.

Operating income, excluding unfavorable currency, increased by 6.8%, mainly reflecting a favorable pricing variance; lower manufacturing costs; and lower marketing, administration and research costs, notably in the GCC; partly offset by unfavorable volume/mix, mainly due to the same factors as for net revenues noted above.

Middle East & Africa - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in the Middle East & Africa was essentially flat at 592.4 billion units, notably reflecting:

- Algeria, up by 7.0%, partly reflecting the timing of estimated trade inventory movements in 2019 compared to 2018; and
- Egypt, up by 1.6%, mainly due to the timing of estimated trade inventory movements in 2019 related to anticipated price increases;

offset by

- Duty Free, down by 1.6%, mainly reflecting lower purchases by travelers to China; and
- Morocco, down by 16.0%, primarily reflecting the impact of significant excise tax-driven price increases in 2019.

Our Regional market share decreased by 0.2 points to 23.5%.

PMI Shipment Volume (million units)	Full-Year 2019	Full-Year 2018	Change
Cigarettes	**134,568**	136,605	(1.5)%
Heated Tobacco Units	**2,654**	3,403	(22.0)%
Total Middle East & Africa	**137,222**	**140,008**	**(2.0)%**

Our total shipment volume decreased by 2.0% to 137.2 billion units, notably in:

-

PMI Duty Free, down by 7.0%. Excluding the net unfavorable impact of estimated distributor inventory movements of 0.4 billion units, PMI's in-market sales decline was 4.6%, mainly reflecting lower market share and the lower total market; and

- Turkey, down by 5.6%, mainly reflecting lower market share, primarily driven by the timing of retail price increases in April 2019 compared to competition;

partly offset by

- Egypt, up by 12.2%, primarily reflecting higher market share, driven by *L&M*, as well as the higher total market; and

- Saudi Arabia, up by 24.9%. Excluding the net favorable impact of estimated distributor inventory movements of 1.5 billion units, mainly attributable to the timing of shipments compared to 2018, PMI's in-market sales grew by 4.1%, primarily reflecting higher market share.

South & Southeast Asia:

Financial Summary - Years Ended December 31, (in millions)	2019	2018	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Currency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/Mix	Variance Fav./(Unfav.) Cost/Other
Net Revenues	**$ 5,094**	$ 4,656	9.4%	9.6%	$ 438	$ (10)	$ 583	$ (135)	$ —
Operating Income	**$ 2,163**	$ 1,747	23.8%	22.8%	$ 416	$ 17	$ 583	$ (99)	$ (85)

Net revenues, excluding unfavorable currency, increased by 9.6%, reflecting: a favorable pricing variance, principally driven by Indonesia and the Philippines, partly offset by unfavorable volume/mix, largely due to Indonesia, partly offset by favorable volume in India and Thailand, as well as favorable mix in the Philippines.

Operating income increased by 23.8%. Excluding asset impairment and exit costs of $20 million related to a plant closure in Pakistan in the first quarter of 2019 as part of our global manufacturing infrastructure optimization, and favorable currency of $17 million, operating income increased by 24.0%, mainly reflecting: a favorable pricing variance and lower manufacturing costs, partly offset by unfavorable volume/mix, reflecting the same factors as for net revenues noted above, and higher marketing, administration and research costs, partly due to the Philippines.

South & Southeast Asia - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in South & Southeast Asia decreased by 1.2% to 738.1 billion units, notably due to:

- Pakistan, down by 14.0%, mainly reflecting the impact of excise tax-driven price increases;
- the Philippines, down by 3.7%, primarily reflecting the impact of price increases in the below premium segment in the fourth quarter of 2018, as well as price increases in the third quarter of 2019; and
- Vietnam, down by 5.2%, mainly reflecting the impact of excise tax-driven price increases;

partly offset by

- Indonesia, up by 1.1%, reflecting the absence of an excise tax increase in 2019; and
- Thailand, up by 5.8%, primarily reflecting on-going recovery from the September 2017 excise tax reform.

Our Regional market share decreased by 0.1 point to 23.7%.

PMI Shipment Volume (million units)	Full-Year 2019	Full-Year 2018	Change
Cigarettes	**174,934**	178,469	(2.0%)
Heated Tobacco Units	—	—	— %
Total South & Southeast Asia	**174,934**	**178,469**	**(2.0%)**

Our total shipment volume decreased by 2.0% to 174.9 billion units, notably due to:

-

Indonesia, down by 2.9%, mainly reflecting lower market share, primarily due to the widened retail price gap of *Sampoerna A* to competitive brands following its price increase in October 2018, partly offset by the higher total market;

- Pakistan, down by 8.6%, mainly reflecting the lower total market, partly offset by higher market share driven by favorable retail price gaps with competitors' brands; and

- the Philippines, down by 2.9%, mainly reflecting the lower total market, partly offset by higher market share, notably of *Marlboro*;

partly offset by

- Thailand, up by 18.0%, mainly reflecting higher market share, driven by the continued strong performance of *L&M 7.1* and the favorable impact of distribution expansion in 2018, as well as the higher total market.

East Asia & Australia:

Financial Summary - Years Ended December 31, (in millions)	2019	2018	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Cur-rency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/ Mix	Variance Fav./(Unfav.) Cost/ Other
Net Revenues	**$ 5,364**	$ 5,580	(3.9%)	(3.4%)	$ (216)	$ (26)	$ 230	$ (420)	$ —
Operating Income	**$ 1,932**	$ 1,851	4.4 %	2.4 %	$ 81	$ 37	$ 230	$ (292)	$ 106

Net revenues, excluding unfavorable currency, decreased by 3.4%, reflecting: unfavorable volume/mix, mainly due to lower cigarette volume in Australia, Japan and Korea, lower *IQOS* device volume in Japan, and lower heated tobacco unit volume and *IQOS* device volume in Korea, partly offset by higher heated tobacco unit volume in Japan. The unfavorable volume/mix was partly offset by a favorable pricing variance, predominantly driven by Australia and Japan.

The net revenues of the East Asia & Australia segment include $2,671 million in 2019 and $2,506 million in 2018 related to the sale of RRPs.

Operating income, excluding favorable currency, increased by 2.4%, mainly reflecting: a favorable pricing variance and lower manufacturing costs, primarily related to Japan and Korea, partly offset by unfavorable volume/mix, mainly reflecting the same drivers as for net revenues noted above, as well as higher marketing, administration and research costs.

East Asia & Australia - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in East Asia & Australia, excluding China, decreased by 4.0% to 299.2 billion units, notably due to:

- Australia, down by 5.9%, or by 8.9% excluding the impact of estimated trade inventory movements, mainly reflecting the impact of excise tax-driven retail price increases;

- Japan, down by 5.6%, mainly reflecting the impact of the October 1, 2018 excise tax-driven retail price increases, as well as out-switching to the cigarillo category;

- Korea, down by 1.4%, reflecting the secular decline of the cigarette category, partly offset by the growth of the heat-not-burn category; and

- Taiwan, down by 1.9%, continuing to reflect the impact of significant excise tax-driven retail price increases in June 2017, as well as an increase in the prevalence of illicit trade.

Our Regional market share, excluding China, decreased by 0.5 points to 26.9%.

PMI Shipment Volume (million units)	Full-Year 2019	Full-Year 2018	Change
Cigarettes	**49,951**	56,163	(11.1%)

Heated Tobacco Units	**30,677**	26,866	14.2 %
Total East Asia & Australia	**80,628**	83,029	(2.9 %)

PMI's total shipment volume decreased by 2.9% to 80.6 billion units, notably in:

- Korea, down by 11.1%, principally due to lower cigarette and heated tobacco unit market share, as well as the lower total market;

partly offset by

- Japan, up by 0.3%, reflecting the net favorable impact of estimated distributor inventory movements of approximately 2.6 billion units (comprised of approximately 3.4 billion heated tobacco units, partially offset by approximately 0.8 billion cigarettes), mainly due to a favorable comparison with 2018 in which *IQOS* consumable inventories in Japan were reduced. Excluding the impact of these inventory movements, PMI's in-market sales declined by 4.2%, primarily reflecting the lower total market, partly offset by higher heated tobacco unit market share.

Latin America & Canada:

Financial Summary - Years Ended December 31, (in millions)	**2019**	**2018**	**Change Fav./(Unfav.) Total**	**Change Fav./(Unfav.) Excl. Curr.**	**Variance Fav./(Unfav.) Total**	**Variance Fav./(Unfav.) Currency**	**Variance Fav./(Unfav.) Price**	**Variance Fav./(Unfav.) Vol/Mix**	**Variance Fav./(Unfav.) Cost/Other[1]**
Net Revenues	**$ 2,206**	$ 3,056	(27.8)%	(25.6)%	$ (850)	$ (68)	$ 90	$ (113)	$ (759)
Operating Income	**$ 235**	$ 1,145	(79.5)%	(80.7)%	$ (910)	$ 14	$ 90	$ (89)	$ (925)

[1] Unfavorable Cost/Other variance includes the impact of the RBH deconsolidation.

Note: Net Revenues include revenues from shipments of Platform 1 devices, heated tobacco units and accessories to Altria Group, Inc., commencing in the third quarter of 2019, for sale under license in the United States.

Net revenues, excluding unfavorable currency, decreased by 25.6%, predominantly due to: the unfavorable impact shown in "Cost/Other," resulting from the deconsolidation of RBH; and unfavorable volume/mix, mainly due to lower cigarette volume in Argentina and Canada, partly offset by a favorable pricing variance, notably in Brazil, Canada, Colombia and Mexico, partially offset by Argentina, mainly due to the adoption of highly inflationary accounting.

The net revenues of the Latin America & Canada segment include $27 million in 2019 and $19 million in 2018 related to the sale of RRPs.

Operating income decreased by 79.5%. Excluding the loss on deconsolidation of RBH ($239 million), the Canadian tobacco litigation-related expense ($194 million), asset impairment and exit costs ($60 million) related to plant closures in Argentina and Colombia as part of our global manufacturing infrastructure optimization, and favorable currency ($14 million), operating income decreased by 37.6%. This decline was predominantly due to the unfavorable impact, shown in "Cost/Other," resulting from the deconsolidation of RBH; an unfavorable volume/mix, mainly due to lower cigarette volume in Argentina and Canada, partially offset by a favorable pricing variance, lower manufacturing costs and lower marketing, administration and research costs.

Latin America & Canada - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in Latin America & Canada decreased by 4.3% to 194.1 billion units, notably due to:

- Argentina, down by 4.6%, primarily due to the impact of cumulative price increases and the impact of the economic downturn as of the second half of 2018;

- Canada, down by 7.7%, primarily due to the impact of cumulative price increases, as well as the growing prevalence of e-vapor products; and

-

Venezuela, down by 61.6%, mainly reflecting the deterioration of the socioeconomic environment and the impact of inflation-driven price increases.

Our Regional market share decreased by 0.4 points to 36.9%.

PMI Shipment Volume (million units)	Full-Year		
	2019	**2018**	**Change**
Cigarettes	**72,293**	80,738	(10.5 %)
Heated Tobacco Units	**299**	147	+100.0%
Total Latin America & Canada	**72,592**	80,885	(10.3 %)

Our total shipment volume decreased by 10.3% to 72.6 billion units, or by 5.2% excluding the impact of the RBH deconsolidation, notably due to:

- Argentina, down by 9.4%, primarily reflecting the lower total market, as well as lower market share; and
- Venezuela, down by 74.8%, primarily reflecting the lower total market.

2018 compared with 2017

For a discussion comparing our consolidated operating results within each of our operating segments for the year ended December 31, 2018, with the year ended December 31, 2017, refer to Part II, Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operation - Operating Results by Business Segment* in our Annual Report on Form 10-K for the year ended December 31, 2018, which was filed with the U.S. Securities and Exchange Commission on February 7, 2019.

Financial Review

chart-7afa3067cb17c8da6dc.jpgchart-6a2df93042cb84ab17b.jpgchart-5cdaf24be4761f417f9.jpg

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Net cash provided by operating activities	$ 10,090	$ 9,478	$ 8,912
Net cash used in investing activities	(1,811)	(998)	(3,083)
Net cash used in financing activities	(8,061)	(9,651)	(2,769)

2019 compared with 2018

- *Net Cash Provided by Operating Activities*

Net cash provided by operating activities of $10.1 billion for the year ended December 31, 2019, increased by $0.6 billion from the comparable 2018 period. Excluding unfavorable currency movements of $1.0 billion, net cash provided by operating activities increased by $1.6 billion, due to lower working capital requirements of $1.3 billion and other movements of $0.3 billion. The unfavorable currency movements represented the impacts on net earnings coupled with the currency impacts on subsidiary working capital movements and the related inter-company positions from the fluctuations of the U.S. dollar in 2018 and 2019, especially against the Euro, Mexican peso, Russian ruble and Turkish lira.

The lower working capital requirements were primarily due to higher cash provided by accrued liabilities and other current assets related to the timing of excise tax-paid inventory movements and excise tax payments, and higher cash provided by accounts payable reflecting a combination of extended payment terms from vendors in 2019 and higher 2018 payments for *IQOS* device purchases in the fourth quarter of 2017, partially offset by more cash used for accounts receivable primarily due to the timing of cash collections.

The other movements of $0.3 billion, excluding currency, was driven by the net impact of the net earnings decline of $0.4 billion adjusted for the add-back of the non-cash items of $0.7 billion, comprised of $0.3 billion related to the 2019 Canadian tobacco litigation-related expense and the 2019 loss on deconsolidation of RBH and $0.4 billion related to the 2019 asset impairment and exit costs. While the asset impairment and exit costs were largely non-cash charges in 2019, approximately $0.2 billion of employee separation costs will be paid by the end of 2021 - see Item 8, Note 21. *Asset Impairment and Exit Costs* for additional information.

- *Net Cash Used in Investing Activities*

Net cash used in investing activities of $1.8 billion for the year ended December 31, 2019, increased by $0.8 billion from the comparable 2018 period. This increase in net cash used in investing activities was due principally to the reduction of cash resulting from the deconsolidation of RBH, partly offset by lower capital expenditures. For further details on deconsolidation of RBH, see Item 8. Note 22. *Deconsolidation of RBH*.

Our capital expenditures were $0.9 billion in 2019 and $1.4 billion in 2018. The 2019 expenditures were primarily related to our ongoing investments in RRPs. We expect total capital expenditures in 2020 of approximately $1.0 billion (including capital expenditures related to our ongoing investment in RRPs), to be funded by operating cash flows.

- *Net Cash Used in Financing Activities*

Net cash used in financing activities of $8.1 billion for the year ended December 31, 2019, decreased by $1.6 billion from the comparable 2018 period. The decrease in net cash used in financing activities was due primarily to 2019 proceeds from long-term debt issuances ($3.8 billion proceeds from our U.S. dollar and Euro debt issuances in 2019) and the purchase of the remaining 49% interest in our Costa Rican affiliates in 2018, partially offset by higher long-term debt repayments and higher repayments of short-term borrowing. For further details on the purchase of the remaining 49% interest in our Costa Rican affiliates, see Item 8, Note 6. *Acquisitions*.

Dividends paid in 2019 and 2018 were $7.2 billion and $6.9 billion, respectively.

2018 compared with 2017

For a discussion comparing our net cash activities (operating, investing and financing) for the year ended December 31, 2018, with the year ended December 31, 2017, refer to Part II, Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation - Financial Review in our Annual Report on Form 10-K for the year ended December 31, 2018, which was filed with the U.S. Securities and Exchange Commission on February 7, 2019.

Ÿ **Debt and Liquidity**

We define cash and cash equivalents as short-term, highly liquid investments, readily convertible to known amounts of cash that mature within a maximum of three months and have an insignificant risk of change in value due to interest rate or credit risk changes. As a policy, we do not hold any investments in structured or equity-linked products. Our cash and cash equivalents are predominantly held in demand deposits with institutions that have investment-grade long-term credit rating. As part of our cash management strategy and in order to

manage counterparty exposure, we also enter into reverse repurchase agreements. Such agreements are collateralized with government or corporate securities held by a custodial bank and, at maturity, cash is paid back to PMI, and the collateral is returned to the bank. For 2018, we had an average balance of $0.3 billion, and we had a zero balance at December 31, 2018. For 2019, the activity for such reverse repurchase agreements was not material.

We utilize long-term and short-term debt financing, including a commercial paper program that is regularly used to finance ongoing liquidity requirements, as part of our overall cash management strategy. Our ability to access the capital and credit markets as well as overall dynamics of these markets may impact borrowing costs. We expect that the combination of our long-term and short-term debt financing, the commercial paper program and the committed credit facilities, coupled with our operating cash flows, will enable us to meet our liquidity requirements.

Credit Ratings – The cost and terms of our financing arrangements as well as our access to commercial paper markets may be affected by applicable credit ratings. At February 6, 2020, our credit ratings and outlook by major credit rating agencies were as follows:

	Short-term	**Long-term**	**Outlook**
Moody's	P-1	A2	Stable
Standard & Poor's	A-1	A	Stable
Fitch	F1	A	Stable

Credit Facilities – On January 31, 2020, we entered into an agreement to amend and extend the term of our $2.0 billion 364-day revolving credit facility from February 4, 2020, to February 2, 2021.

At February 6, 2020, our committed credit facilities were as follows:

(in billions)

Type	**Committed Credit Facilities**
364-day revolving credit, expiring February 2, 2021	**$ 2.0**
Multi-year revolving credit, expiring February 28, 2021	**2.5**
Multi-year revolving credit, expiring October 1, 2022	**3.5**
Total facilities	**$ 8.0**

At February 6, 2020, there were no borrowings under the committed credit facilities, and the entire committed amounts were available for borrowing.

All banks participating in our committed credit facilities have an investment-grade long-term credit rating from the credit rating agencies. We continuously monitor the credit quality of our banking group, and at this time we are not aware of any potential non-performing credit provider.

All but the $2.0 billion 364-day revolving credit facility in the table above require us to maintain a ratio of consolidated earnings before interest, taxes, depreciation and amortization ("consolidated EBITDA") to consolidated interest expense of not less than 3.5 to 1.0 on a rolling four-quarter basis. At December 31, 2019, our ratio calculated in accordance with the agreements was 11.2 to 1.0. These facilities do not include any credit rating triggers, material adverse change clauses or any provisions that could require us to post collateral. We expect to continue to meet our covenants. The terms "consolidated EBITDA" and "consolidated interest expense," both of which include certain adjustments, are defined in the facility agreements previously filed with the U.S. Securities and Exchange Commission.

We plan to replace our existing $2.5 billion multi-year revolving credit facility, expiring February 28, 2021 with a new $2.0 billion revolving credit facility expiring February 10, 2025. The new credit facility, which is expected to close on February 10, 2020, will not include the consolidated EBITDA to consolidated interest expense ratio covenant discussed above.

In addition to the committed credit facilities discussed above, certain of our subsidiaries maintain short-term credit arrangements to meet their respective working capital needs. These credit arrangements, which amounted to approximately $2.7 billion at December 31, 2019,

and $3.3 billion at December 31, 2018, are for the sole use of our subsidiaries. Borrowings under these arrangements amounted to $338 million at December 31, 2019, and $730 million at December 31, 2018.

Commercial Paper Program – We continue to have access to liquidity in the commercial paper market through programs in place in the U.S. and in Europe having an aggregate issuance capacity of $8.0 billion. At December 31, 2019, and December 31, 2018, we had no commercial paper outstanding. The average commercial paper balance outstanding during 2019 and 2018 was $2.3 billion and $3.4 billion, respectively.

Sale of Accounts Receivable – To mitigate credit risk and enhance cash and liquidity management we sell trade receivables to unaffiliated financial institutions. These arrangements allow us to sell, on an ongoing basis, certain trade receivables without recourse. The trade receivables sold are generally short-term in nature and are removed from the consolidated balance sheets. We sell trade receivables under two types of arrangements, servicing and nonservicing.

Our operating cash flows were positively impacted by the amount of the trade receivables sold and derecognized from the consolidated balance sheets, which remained outstanding with the unaffiliated financial institutions. The trade receivables sold that remained outstanding under these arrangements as of December 31, 2019, 2018 and 2017, were $0.9 billion, $1.0 billion and $1.1 billion, respectively. The net proceeds received are included in cash provided by operating activities in the consolidated statements of cash flows.

For further details, see Item 8, Note 20. *Sale of Accounts Receivable* to our consolidated financial statements.

Debt – Our total debt was $31.0 billion at December 31, 2019, and $31.8 billion at December 31, 2018. Our total debt is primarily fixed rate in nature. For further details, see Item 8, Note 7. *Indebtedness*. The weighted-average all-in financing cost of our total debt was 2.5% in 2019 and 2018. See Item 8, Note 16. *Fair Value Measurements* to our consolidated financial statements for a discussion of our disclosures related to the fair value of debt. The amount of debt that we can issue is subject to approval by our Board of Directors.

On February 14, 2017, we filed a shelf registration statement with the U.S. Securities and Exchange Commission, under which we may from time to time sell debt securities and/or warrants to purchase debt securities over a three-year period. During February 2020, we plan to file a new shelf registration statement with the Securities and Exchange Commission.

Our debt issuances in 2019 were as follows:

(in millions)

Type		Face Value		Interest Rate	Issuance	Maturity
U.S. dollar notes	(a)	$900		2.875%	May 2019	May 2024
U.S. dollar notes	(b)	$750		3.375%	May 2019	August 2029
EURO notes	(c)	€500 (approximately $557)	(d)	0.125%	August 2019	August 2026
EURO notes	(c)	€750 (approximately $835)	(d)	0.800%	August 2019	August 2031
EURO notes	(c)	€750 (approximately $835)	(d)	1.450%	August 2019	August 2039

(a) Interest on these notes is payable semi-annually in arrears beginning in November 2019.
(b) Interest on these notes is payable semi-annually in arrears beginning in August 2019.
(c) Interest on these notes is payable annually in arrears beginning in August 2020.
(d) USD equivalents for foreign currency notes were calculated based on exchange rates on the date of issuance.

The net proceeds from the sale of the securities listed in the table above have been and will be used for general corporate purposes, including repayment of outstanding commercial paper and refinancing of outstanding 2.000% Notes due 2020, outstanding Floating Rate Notes due 2020 and outstanding Euro denominated 1.750% Notes due 2020.

The weighted-average time to maturity of our long-term debt was 10.2 years at the end of 2019 and 9.6 years at the end of 2018.

- **Off-Balance Sheet Arrangements and Aggregate Contractual Obligations**

We have no off-balance sheet arrangements, including special purpose entities, other than guarantees and contractual obligations discussed below.

Guarantees – At December 31, 2019, we were contingently liable for $0.5 billion of guarantees of our own performance, of which $0.3 billion related to our obligations under indemnity agreements to enable appeals of customs assessments against our distributors, and $0.2 billion were primarily related to excise taxes on the shipment of our products. There is no liability in the consolidated financial statements associated with these guarantees. At December 31, 2019, our third-party guarantees were insignificant.

Aggregate Contractual Obligations – The following table summarizes our contractual obligations at December 31, 2019:

		Payments Due			
(in millions)	**Total**	**2020**	**2021-2022**	**2023-2024**	**2025 and Thereafter**
Long-term debt [1]	$30,962	$4,051	$5,779	$4,890	$16,242
Interest on borrowings [2]	10,124	877	1,534	1,273	6,440
Operating leases [3]	949	222	286	158	283
Purchase obligations [4]:					
Inventory and production costs	3,493	2,199	885	409	—
Other	2,180	977	578	213	412
	5,673	3,176	1,463	622	412
Other long-term liabilities [5]	1,992	278	408	661	645
	$49,700	$8,604	$9,470	$7,604	$24,022

[1] Amounts represent the expected cash payments at the face value of our long-term debt and finance lease obligations. For further details, see Item 8, Note 7. *Indebtedness* to our consolidated financial statements.

[2] Amounts represent the expected cash payments of our interest expense on our long-term debt, including the current portion of long-term debt. Interest on our fixed-rate debt is presented using the stated interest rate. Interest on our variable debt is estimated using the rate in effect at December 31, 2019. Amounts exclude the amortization of debt discounts, the amortization of loan fees and fees for lines of credit that would be included in interest expense in the consolidated statements of earnings.

[3] Amounts represent the maturity of PMI"s operating lease liabilities, on an undiscounted basis.

[4] Purchase obligations for inventory and production costs (such as raw materials, indirect materials and supplies, packaging, co-manufacturing arrangements, storage and distribution) are commitments for projected needs to be utilized in the normal course of business. Other purchase obligations include commitments for marketing, advertising, capital expenditures, information technology and professional services. Other purchase obligations also include the expected future contributions to the Foundation for a Smoke-Free World. For further details see *Business Environment—Other Developments*. Arrangements are considered purchase obligations if a contract specifies all significant terms, including fixed or minimum quantities to be purchased, a pricing structure and approximate timing of the transaction. Amounts represent the minimum commitments under non-cancelable contracts. Any amounts reflected on the consolidated balance sheet as accounts payable and accrued liabilities are excluded from the table above.

[5] Other long-term liabilities consist primarily of transition tax (as discussed in Item 8, Note 11. *Income Taxes* to our consolidated financial statements), postretirement health care costs, accruals established for employment costs and accruals established for Exit activities (for further details, see Note 21. *Asset impairment and Exit Costs*). The following long-term liabilities included on the consolidated balance sheet are excluded from the table above: accrued pension and postemployment costs, tax contingencies, insurance accruals and other accruals. We are unable to estimate the timing of payments (or contributions in the case of accrued pension costs) for these items. Currently, we anticipate making pension contributions of approximately $77 million in 2020, based on current tax and benefit laws (as discussed in Item 8, Note 13. *Benefit Plans* to our consolidated financial statements).

Ÿ Equity and Dividends

We discuss our stock awards as of December 31, 2019, in Item 8, Note 9. *Stock Plans* to our consolidated financial statements.

During 2019, 2018 and 2017, we did not repurchase any shares under a share repurchase program, and we do not presently intend to repurchase shares of our common stock in 2020.

Dividends paid in 2019 were $7.2 billion. During the third quarter of 2019, our Board of Directors approved a 2.6% increase in the quarterly dividend to $1.17 per common share. As a result, the present annualized dividend rate is $4.68 per common share.

Market Risk

Ÿ ***Counterparty Risk*** **-** We predominantly work with financial institutions with strong short- and long-term credit ratings as assigned by Standard & Poor's and Moody's. These banks are also part of a defined group of relationship banks. Non-investment grade institutions are only used in certain emerging markets to the extent required by local business needs. We have a conservative approach when it comes to choosing financial counterparties and financial instruments. As such we do not invest or hold investments in any structured or equity-linked products. The majority of our cash and cash equivalents is currently invested in demand deposits maturing within less than 30 days.

We continuously monitor and assess the credit worthiness of all our counterparties.

Ÿ ***Derivative Financial Instruments*** **-** We operate in markets outside of the U.S., with manufacturing and sales facilities in various locations throughout the world. Consequently, we use certain financial instruments to manage our foreign currency and interest rate exposure. We use derivative financial instruments principally to reduce our exposure to market risks resulting from fluctuations in foreign exchange and interest rates by creating offsetting exposures. We are not a party to leveraged derivatives and, by policy, do not use derivative financial instruments for speculative purposes.

See Item 8, Note 15. *Financial Instruments,* Item 8, Note 16. *Fair Value Measurements* and Item 8, Note 19. *Balance Sheet Offsetting* to our consolidated financial statements for further details on our derivative financial instruments and the related collateral arrangements.

Ÿ ***Value at Risk*** **-** We use a value at risk computation to estimate the potential one-day loss in the fair value of our interest-rate-sensitive and foreign currency price-sensitive derivative financial instruments. This computation includes our debt and foreign currency forwards, swaps and options. Anticipated transactions, foreign currency trade payables and receivables, and net investments in foreign subsidiaries, which the foregoing instruments are intended to hedge, were excluded from the computation.

The computation estimates were made assuming normal market conditions, using a 95% confidence interval and a one-day holding period using a "parametric delta-gamma" approximation technique to determine the observed interrelationships between movements in interest rates and various currencies and in calculating the risk of the underlying positions in the portfolio. These interrelationships were determined by observing interest rate and forward currency rate movements primarily over the preceding quarter for determining value at risk at December 31, 2019 and 2018, and primarily over each of the four preceding quarters for the calculation of average value at risk amounts during each year.

	Fair Value Impact			
(in millions)	**At December 31, 2019**	**Average**	**High**	**Low**
Instruments sensitive to:				
Foreign currency rates	**$18**	**$20**	**$24**	**$18**
Interest rates	**$301**	**$247**	**$346**	**$169**

	Fair Value Impact			
(in millions)	**At December 31, 2018**	**Average**	**High**	**Low**
Instruments sensitive to:				
Foreign currency rates	$19	$20	$23	$19
Interest rates	$142	$132	$152	$96

The value at risk computation is a risk analysis tool designed to statistically estimate the maximum probable daily loss from adverse movements in interest and foreign currency rates under normal market conditions. The computation does not purport to represent actual losses in fair value or earnings to be incurred by us, nor does it consider the effect of favorable changes in market rates. We cannot predict actual future movements in such market rates and do not present these results to be indicative of future movements in market rates or to

be representative of any actual impact that future changes in market rates may have on our future results of operations or financial position.

Contingencies

See Item 3 and Item 8, Note 18. *Contingencies* to our consolidated financial statements for a discussion of contingencies.

Cautionary Factors That May Affect Future Results

Forward-Looking and Cautionary Statements

We may from time to time make written or oral forward-looking statements, including statements contained in filings with the SEC, in reports to stockholders and in press releases and investor webcasts. You can identify these forward-looking statements by use of words such as "strategy," "expects," "continues," "plans," "anticipates," "believes," "will," "estimates," "intends," "projects," "goals," "targets" and other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts.

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Our RRPs constitute a new product category in its early stages that is less predictable than our mature cigarette business. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from those anticipated, estimated or projected. Investors should bear this in mind as they consider forward-looking statements and whether to invest in or remain invested in our securities. In connection with the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995, we are identifying important factors that, individually or in the aggregate, could cause actual results and outcomes to differ materially from those contained in any forward-looking statements made by us; any such statement is qualified by reference to the following cautionary statements. We elaborate on these and other risks we face throughout this document, particularly in Item 1A. *Risk Factors* and *Business Environment* of this section. You should understand that it is not possible to predict or identify all risk factors. Consequently, you should not consider this discussion of potential risks or uncertainties to be complete. We do not undertake to update any forward-looking statement that we may make from time to time, except in the normal course of our public disclosure obligations.

Item 7A. *Quantitative and Qualitative Disclosures About Market Risk.*

The information called for by this Item is included in Item 7, *Market Risk*.

Item 8. ***Financial Statements and Supplementary Data.***

Consolidated Statements of Earnings

(in millions of dollars, except per share data)

for the years ended December 31,	2019	2018	2017
Revenues including excise taxes	**$ 77,921**	$ 79,823	$ 78,098
Excise taxes on products	**48,116**	50,198	49,350
Net revenues	**29,805**	29,625	28,748
Cost of sales	**10,513**	10,758	10,432
Gross profit	**19,292**	18,867	18,316
Marketing, administration and research costs (Notes 18, 21 & 22)	**8,695**	7,408	6,647
Amortization of intangibles	**66**	82	88
Operating income	**10,531**	11,377	11,581
Interest expense, net (Note 14)	**570**	665	914
Pension and other employee benefit costs (Note 13)	**89**	41	78
Earnings before income taxes	**9,872**	10,671	10,589
Provision for income taxes (Note 11)	**2,293**	2,445	4,307
Equity investments and securities (income)/loss, net	**(149)**	(60)	(59)
Net earnings	**7,728**	8,286	6,341
Net earnings attributable to noncontrolling interests	**543**	375	306
Net earnings attributable to PMI	**$ 7,185**	$ 7,911	$ 6,035
Per share data (Note 10):			
Basic earnings per share	**$ 4.61**	$ 5.08	$ 3.88
Diluted earnings per share	**$ 4.61**	$ 5.08	$ 3.88

See notes to consolidated financial statements.

Consolidated Statements of Comprehensive Earnings
(in millions of dollars)

for the years ended December 31,	2019	2018	2017
Net earnings	**$ 7,728**	$ 8,286	$ 6,341
Other comprehensive earnings (losses), net of income taxes:			
Change in currency translation adjustments:			
Unrealized gains (losses), net of income taxes of ($161) in 2019, ($47) in 2018 and $620 in 2017	**505**	(812)	330
(Gains)/losses transferred to earnings, net of income taxes of $0 in 2019, 2018 and 2017	**—**	—	(2)
(Gains)/losses transferred to earnings - deconsolidation of RBH, net of income taxes of $0 in 2019, 2018 and 2017 (Note 22)	**502**	—	—
Change in net loss and prior service cost:			
Net gains (losses) and prior service costs, net of income taxes of $247 in 2019, $65 in 2018 and ($17) in 2017	**(454)**	(1,046)	523
Amortization of net losses, prior service costs and net transition costs, net of income taxes of ($69) in 2019, ($43) in 2018 and ($31) in 2017	**243**	218	228
(Gains)/losses transferred to earnings - deconsolidation of RBH, net of income taxes of ($15) in 2019, $0 in 2018 and $0 in 2017 (Note 22)	**27**	—	—
Change in fair value of derivatives accounted for as hedges:			
Gains (losses) recognized, net of income taxes of $2 in 2019, ($4) in 2018 and $8 in 2017	**(18)**	24	(44)
(Gains) losses transferred to earnings, net of income taxes of $3 in 2019, $5 in 2018 and $2 in 2017	**(14)**	(31)	(11)
Total other comprehensive earnings (losses)	791	(1,647)	1,024
Total comprehensive earnings	**8,519**	6,639	7,365
Less comprehensive earnings attributable to:			
Noncontrolling interests	**586**	304	306
Comprehensive earnings attributable to PMI	**$ 7,933**	$ 6,335	$ 7,059

See notes to consolidated financial statements.

Consolidated Balance Sheets
(in millions of dollars, except share data)

at December 31,	2019	2018
Assets		
Cash and cash equivalents	**$ 6,861**	$ 6,593
Trade receivables (less allowances of $20 in 2019 and $25 in 2018)	**3,080**	2,950
Other receivables	**637**	614
Inventories:		
Leaf tobacco	**2,052**	2,318
Other raw materials	**1,596**	1,405
Finished product	**5,587**	5,081
	9,235	8,804
Other current assets	**701**	481
Total current assets	**20,514**	19,442
Property, plant and equipment, at cost:		
Land and land improvements	**566**	600
Buildings and building equipment	**4,132**	3,975
Machinery and equipment	**9,354**	9,096
Construction in progress	**394**	886
	14,446	14,557
Less: accumulated depreciation	**7,815**	7,356
	6,631	7,201
Goodwill (Note 3)	**5,858**	7,189
Other intangible assets, net (Note 3)	**2,113**	2,278
Investments in unconsolidated subsidiaries and equity securities (Notes 4 & 16)	**4,635**	1,269
Deferred income taxes	**1,153**	977
Other assets	**1,971**	1,445
Total Assets	**$ 42,875**	$ 39,801

See notes to consolidated financial statements.

at December 31,	2019	2018
Liabilities		
Short-term borrowings (Note 7)	**$ 338**	$ 730
Current portion of long-term debt (Note 7)	**4,051**	4,054
Accounts payable	**2,299**	2,068
Accrued liabilities:		
Marketing and selling	**666**	732
Taxes, except income taxes	**5,837**	5,088
Employment costs	**1,042**	794
Dividends payable	**1,831**	1,783
Other	**1,973**	1,366
Income taxes (Note 11)	**796**	576
Total current liabilities	**18,833**	17,191
Long-term debt (Note 7)	**26,656**	26,975
Deferred income taxes	**908**	898
Employment costs	**3,634**	3,083
Income taxes and other liabilities (Note 11)	**2,443**	2,393
Total liabilities	**52,474**	50,540
Contingencies (Note 18)		
Stockholders' (Deficit) Equity		
Common stock, no par value (2,109,316,331 shares issued in 2019 and 2018)	**—**	—
Additional paid-in capital	**2,019**	1,939
Earnings reinvested in the business	**30,987**	31,014
Accumulated other comprehensive losses	**(9,363)**	(10,111)
	23,643	22,842
Less: cost of repurchased stock (553,421,668 and 554,736,610 shares in 2019 and 2018, respectively)	**35,220**	35,301
Total PMI stockholders' deficit	**(11,577)**	(12,459)
Noncontrolling interests	**1,978**	1,720
Total stockholders' deficit	**(9,599)**	(10,739)
Total Liabilities and Stockholders' (Deficit) Equity	**$ 42,875**	$ 39,801

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows
(in millions of dollars)

for the years ended December 31,	2019	2018	2017
CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES			
Net earnings	**$ 7,728**	$ 8,286	$ 6,341
Adjustments to reconcile net earnings to operating cash flows:			
Depreciation and amortization	**964**	989	875
Deferred income tax (benefit) provision	**(141)**	(100)	(501)
Asset impairment and exit costs, net of cash paid (Note 21)	**371**	(3)	(10)
Cash effects of changes in:			
Receivables, net	**(331)**	53	(92)
Inventories	**(548)**	(613)	730
Accounts payable	**451**	(51)	425
Accrued liabilities and other current assets	**1,108**	910	(554)
Income taxes	**75**	(135)	1,370
Pension plan contributions	**(200)**	(110)	(66)
Other	**613** [1]	252	394
Net cash provided by operating activities	**10,090**	9,478	8,912
CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES			
Capital expenditures	**(852)**	(1,436)	(1,548)
Investments in unconsolidated subsidiaries and equity securities	**(31)**	(63)	(111)
Deconsolidation of RBH (Note 22)	**(1,346)** [2]	—	—
Net investment hedges	**386**	416	(1,527)
Other	**32**	85	103
Net cash used in investing activities	**(1,811)**	(998)	(3,083)

See notes to consolidated financial statements.

for the years ended December 31,	2019	2018	2017
CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES			
Short-term borrowing activity by original maturity:			
Net issuances (repayments) - maturities of 90 days or less	**$ (364)**	$ 255	$ (127)
Issuances - maturities longer than 90 days	**989**	—	1,634
Repayments - maturities longer than 90 days	**(989)**	—	(1,634)
Long-term debt proceeds	**3,819**	—	6,850
Long-term debt repaid	**(3,998)**	(2,484)	(2,551)
Dividends paid	**(7,161)**	(6,885)	(6,520)
Sale (purchase) of subsidiary shares to/(from) noncontrolling interests (Note 6)	**51**	(81)	5
Other	**(408)**	(456)	(426)
Net cash used in financing activities	**(8,061)**	(9,651)	(2,769)
Effect of exchange rate changes on cash, cash equivalents and restricted cash	**27**	(685)	1,085
Cash, cash equivalents and restricted cash[3]:			
Increase (Decrease)	**245**	(1,856)	4,145
Balance at beginning of year	**6,620**	8,476	4,331
Balance at end of year	**$ 6,865**	$ 6,620	$ 8,476
Cash Paid:			
Interest	**$ 800**	$ 882	$ 1,050
Income taxes	**$ 2,430**	$ 2,749	$ 3,403

[1] Includes the Loss on Deconsolidation of RBH ($239 million) and the Canadian tobacco litigation-related charge ($194 million) that were included in marketing, administration and research costs in the consolidated statements of earnings for the year ended December 31, 2019. For further details on these charges, see Note 22. *Deconsolidation of RBH*.

[2] Includes deconsolidation of RBH cash and cash equivalents of $1,323 million and restricted cash of $23 million.

[3] The amounts for cash and cash equivalents shown above include restricted cash of $4 million, $27 million and $29 million as of December 31, 2019, 2018 and 2017, respectively, which were included in other current assets in the consolidated balance sheets.

See notes to consolidated financial statements.

Consolidated Statements of Stockholders' (Deficit) Equity

(in millions of dollars, except per share data)

	PMI Stockholders' (Deficit) Equity						
	Common Stock	Additional Paid-in Capital	Earnings Reinvested in the Business	Accumulated Other Comprehensive Losses	Cost of Repurchased Stock	Noncontrolling Interests	Total
Balances, January 1, 2017	$ —	$ 1,964	$ 30,397	$ (9,559)	$ (35,490)	$ 1,788	$ (10,900)
Net earnings			6,035			306	6,341
Other comprehensive earnings (losses), net of income taxes				1,024			1,024
Issuance of stock awards		20			108		128
Dividends declared ($4.22 per share)			(6,573)				(6,573)
Payments to noncontrolling interests						(255)	(255)
Other		(12)				17	5
Balances, December 31, 2017	—	1,972	29,859	(8,535)	(35,382)	1,856	(10,230)
Net earnings			7,911			375	8,286
Other comprehensive earnings (losses), net of income taxes				(1,572)		(75)	(1,647)
Issuance of stock awards		47			81		128
Dividends declared ($4.49 per share)			(6,994)				(6,994)
Payments to noncontrolling interests						(435)	(435)
Adoption of new accounting standards [1]			238				238
Other (Note 6)		(80)		(4)		(1)	(85)
Balances, December 31, 2018	—	1,939	31,014	(10,111)	(35,301)	1,720	(10,739)
Net earnings			**7,185**			**543**	**7,728**
Other comprehensive earnings (losses), net of income taxes				**219**		**43**	**262**
Issuance of stock awards		**79**			**81**		**160**
Dividends declared ($4.62 per share)			**(7,212)**				**(7,212)**
Payments to noncontrolling interests						**(378)**	**(378)**
Deconsolidation of RBH (Note 22)				**529**			**529**
Other		**1**		**—**		**50**	**51**
Balances, December 31, 2019	**$ —**	**$ 2,019**	**$ 30,987**	**$ (9,363)**	**$ (35,220)**	**$ 1,978**	**$ (9,599)**

[1] Financial Accounting Standard Update ASU 2016-01, "Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities"

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Note 1.

Background and Basis of Presentation:

Background

Philip Morris International Inc. is a holding company incorporated in Virginia, U.S.A., whose subsidiaries and affiliates and their licensees are engaged in the manufacture and sale of cigarettes and other nicotine-containing products, including reduced-risk products, in markets outside of the United States of America. In addition, PMI ships a version of its Platform 1 device and its consumables authorized by the U.S. Food and Drug Administration ("FDA") to Altria Group, Inc., for sale in the United States under license. Throughout these financial statements, the term "PMI" refers to Philip Morris International Inc. and its subsidiaries.

Reduced-risk products ("RRPs") is the term PMI uses to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continuing smoking. PMI has a range of RRPs in various stages of development, scientific assessment and commercialization.

"Platform 1" is the term PMI uses to refer to PMI's reduced-risk product that uses a precisely controlled heating device incorporating our *IQOS HeatControl* technology, into which a specially designed and proprietary tobacco unit is inserted and heated to generate an aerosol.

Basis of presentation

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities at the dates of the financial statements and the reported amounts of net revenues and expenses during the reporting periods. Significant estimates and assumptions include, among other things: pension and benefit plan assumptions; useful lives and valuation assumptions of goodwill and other intangible assets; valuation assumptions for non-marketable equity securities; marketing programs, and income taxes. Actual results could differ from those estimates.

The consolidated financial statements include PMI, as well as its wholly owned and majority-owned subsidiaries. Investments in which PMI exercises significant influence (generally 20%-50% ownership interest) are accounted for under the equity method of accounting. Investments not accounted for under the equity method of accounting are measured at fair value, if it is readily determinable, with changes in fair value recognized in net income. Investments without readily determinable fair values, non-marketable equity securities, are measured and recorded using a measurement alternative that values the security at cost minus any impairment. All intercompany transactions and balances have been eliminated.

As of March 22, 2019, PMI deconsolidated the financial results of its Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH") from PMI's financial statements. For further details, see Note 22. *Deconsolidation of RBH*.

Note 2.

Summary of Significant Accounting Policies:

Cash and cash equivalents

Cash equivalents include demand deposits with banks and all highly liquid investments with original maturities of three months or less.

Depreciation

Property, plant and equipment are stated at historical cost and depreciated by the straight-line method over the estimated useful lives of the assets. Machinery and equipment are depreciated over periods ranging from 3 to 15 years, and buildings and building improvements over periods up to 40 years.

Employee benefit plans

PMI provides a range of benefits to its employees and retired employees, including pensions, postretirement health care and postemployment benefits (primarily severance). PMI records annual amounts relating to these plans based on calculations specified under U.S. GAAP. PMI recognizes the funded status of its defined pension and postretirement plans on the consolidated balance sheets. The funded status is measured as the difference between the fair value of the plans assets and the benefit obligation. PMI measures the plan assets and liabilities at the end of the fiscal year. For defined benefit pension plans, the benefit obligation is the projected benefit obligation. For the postretirement health care plans, the benefit obligation is the accumulated postretirement benefit obligation. Any plan with an overfunded status is recognized as an asset, and any plan with an underfunded status is recognized as a liability. Any gains or losses and prior service costs or credits that have not been recognized as a component of net periodic benefit costs are recorded as a component of other comprehensive earnings (losses), net of deferred taxes. PMI elects to recognize actuarial gains/(losses) using the corridor approach.

Foreign currency translation

PMI translates the results of operations of its subsidiaries and affiliates using average exchange rates during each period, whereas balance sheet accounts are translated using exchange rates at the end of each period. Currency translation adjustments are recorded as a component of stockholders' (deficit) equity. In addition, some of PMI's subsidiaries have assets and liabilities denominated in currencies other than their functional currencies, and to the extent those are not designated as net investment hedges, these assets and liabilities generate transaction gains and losses when translated into their respective functional currencies.

Goodwill and non-amortizable intangible assets valuation

PMI tests goodwill and non-amortizable intangible assets for impairment annually or more frequently if events occur that would warrant such review. PMI performs its annual impairment analysis in the second quarter of each year. The impairment analysis involves comparing the fair value of each reporting unit or non-amortizable intangible asset to the carrying value. If the carrying value exceeds the fair value, goodwill or a non-amortizable intangible asset is considered impaired.

Hedging instruments

Derivative financial instruments are recorded at fair value on the consolidated balance sheets as either assets or liabilities. Changes in the fair value of derivatives are recorded each period either in accumulated other comprehensive losses on the consolidated balance sheet or in earnings, depending on whether a derivative is designated and effective as part of a hedge transaction and, if it is, the type of hedge transaction. Gains and losses on derivative instruments reported in accumulated other comprehensive losses are reclassified to the consolidated statements of earnings, into the same line item as the impact of the underlying transaction, in the periods in which operating results are affected by the hedged item. Cash flows from hedging instruments are classified in the same manner as the affected hedged item in the consolidated statements of cash flows.

Impairment of long-lived assets

PMI reviews long-lived assets, including amortizable intangible assets, for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable. PMI performs undiscounted operating cash flow analyses to determine if an impairment exists. For purposes of recognition and measurement of an impairment for assets held for use, PMI groups assets and liabilities at the lowest level for which cash flows are separately identifiable. If an impairment is determined to exist, any related impairment loss is calculated based on fair value. Impairment losses on assets to be disposed of, if any, are based on the estimated proceeds to be received, less costs of disposal.

Impairment of investment in non-marketable equity securities

Non-marketable equity securities are subject to periodic impairment reviews during which PMI considers both qualitative and quantitative factors that may have a significant impact on the investees' fair value. Upon determining that an impairment may exist, the security's fair value is calculated and compared to its carrying value, and an impairment is recognized immediately if the carrying value exceeds the fair value. For further details see Note 22. *Deconsolidation of RBH*.

Impairment of investments in unconsolidated subsidiaries

Investments in unconsolidated subsidiaries are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of the investments may not be recoverable. An impairment loss would be recorded whenever a decline in value of an equity investment below its carrying amount is determined to be other than temporary. PMI determines whether a loss is other than temporary by considering the length of time and extent to which the fair value of the equity investment has been less than the carrying amount, the financial condition of the equity investment, and the intent to retain the investment for a period of time is sufficient to allow for any anticipated recovery in market value.

Income taxes

Income taxes are provided on all earnings for jurisdictions outside the United States. These provisions, as well as state and local income tax provisions, are determined on a separate company basis, and the related assets and liabilities are recorded in PMI's consolidated balance sheets. Significant judgment is required in determining income tax provisions and in evaluating tax positions. PMI recognizes accrued interest and penalties associated with uncertain tax positions as part of the provision for income taxes on the consolidated statements of earnings. PMI recognizes income taxes associated with Global Intangible Low-Taxed Income ("GILTI") taxes as current period expense rather than including these amounts in the measurement of deferred taxes.

Inventories

Inventories are stated at the lower of cost or market. The first-in, first-out and average cost methods are used to cost substantially all inventories. It is a generally recognized industry practice to classify leaf tobacco inventory as a current asset, although part of such inventory, because of the duration of the aging process, ordinarily would not be utilized within one year.

Leases

PMI determines that a contract contains a lease if the contract conveys a right to control the use of the identified asset for a period of time in exchange for consideration. Lease expense is recognized on a straight-line basis over the lease term. At lease commencement, PMI recognizes lease liabilities and the corresponding right-of-use assets (at the present value of future payments) for predominately all of its operating leases. The recognition of the right-of-use asset and lease liability includes renewal options when it is reasonably certain that they will be exercised. Certain of PMI's leases include payments that are based on changes to an index or on actual usage. These lease payments are adjusted periodically and are included within variable lease costs. PMI accounts for lease and nonlease components as a single-lease component with the exception of its vehicle leases, of which PMI accounts for the lease components separately from the nonlease components. Additionally, leases with an initial term of 12 months or less are not included in the right-of-use asset or lease liability on the consolidated statement of financial position.

Marketing costs

PMI supports its products with advertising, adult consumer engagement and trade promotions. Such programs include, but are not limited to, discounts, rebates, in-store display incentives, e-commerce, mobile and other digital platforms, adult consumer activation and promotion activities, as well as costs associated with adult consumer experience outlets and other adult consumer touchpoints and volume-based incentives. Advertising, as well as certain consumer engagement and trade activities costs, are expensed as incurred. Trade promotions are recorded as a reduction of revenues based on amounts estimated as being due to customers at the end of a period, based principally on historical utilization. For interim reporting purposes, advertising and certain consumer engagement expenses are charged to earnings based on estimated sales and related expenses for the full year.

Revenue recognition

PMI recognizes revenue primarily through the manufacture and sale of cigarettes and other nicotine-containing products, including reduced-risk products. The majority of PMI revenues are generated by sales through direct and indirect distribution networks with short-term payment conditions and where control is typically transferred to the customer either upon shipment or delivery of goods. PMI evaluates the transfer of control through evidence of the customer's receipt and acceptance, transfer of title, PMI's right to payment for those products and the customer's

ability to direct the use of those products upon receipt. Typically, PMI's performance obligations are satisfied and revenue is recognized either upon shipment or delivery of goods.

In certain instances, PMI facilitates shipping and handling activities after control has transferred to the customer. PMI has elected to record all shipping and handling activities as costs to fulfill a contract. The shipping and handling costs that have not been incurred at the time revenue is recognized are accrued. The transaction price is typically based on the amount billed to the customer and includes estimated variable consideration, where applicable. Such variable consideration is typically not constrained and is estimated based on the most likely amount that PMI expects to be entitled to under the terms of the contracts with customers, historical experience of discount

or rebate redemption, where relevant, and the terms of any underlying discount or rebate programs, which may change from time to time as the business and product categories evolve. PMI has elected to exclude excise taxes collected from customers from the measurement of the transaction price, thereby presenting revenues net of excise taxes. Estimated costs associated with warranty programs are generally provided for in cost of sales in the period the related revenues are recognized.

Stock-based compensation

PMI measures compensation cost for all stock-based awards at fair value on date of grant and recognizes the compensation costs over the service periods for awards expected to vest. PMI's accounting policy is to estimate the number of awards expected to be forfeited and adjust the expense when it is no longer probable that the employee will fulfill the service condition. For further details, see Note 9. *Stock Plans*.

Note 3.

Goodwill and Other Intangible Assets, net:

The movements in goodwill were as follows:

(in millions)	European Union	Eastern Europe	Middle East & Africa	South & Southeast Asia	East Asia & Australia	Latin America & Canada	Total
Balance at January 1, 2018	$ 1,419	$ 321	$ 102	$ 3,010	$ 567	$ 2,247	$ 7,666
Changes due to:							
Currency	(62)	(18)	(15)	(215)	(31)	(136)	(477)
Balances, December 31, 2018	1,357	303	87	2,795	536	2,111	7,189
Changes due to:							
Currency	**(19)**	**(3)**	**2**	**103**	**15**	**34**	**132**
Deconsolidation of RBH						**(1,463)**	**(1,463)**
Balances, December 31, 2019	**$ 1,338**	**$ 300**	**$ 89**	**$ 2,898**	**$ 551**	**$ 682**	**$ 5,858**

At December 31, 2019, goodwill primarily reflects PMI's acquisitions in Colombia, Greece, Indonesia, Mexico, Pakistan and Serbia, as well as the business combination in the Philippines.

For details on the deconsolidation of RBH, see Note 22. *Deconsolidation of RBH.*

Details of other intangible assets were as follows:

		December 31, 2019			December 31, 2018		
(in millions)	Weighted-Average Remaining Useful Life	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Non-amortizable intangible assets		**$ 1,319**		**$ 1,319**	$ 1,269		$ 1,269
Amortizable intangible assets:							
Trademarks	**14 years**	**1,217**	**$ 526**	**691**	1,488	$ 608	880

Distribution networks	**8 years**	**113**	**72**	**41**	141	82	59
Other*	**9 years**	**106**	**44**	**62**	107	37	70
Total other intangible assets		**$ 2,755**	**$ 642**	**$ 2,113**	$ 3,005	$ 727	$ 2,278

* Includes farmer contracts and intellectual property rights

Non-amortizable intangible assets substantially consist of trademarks from PMI's acquisitions in Indonesia and Mexico. The increase since December 31, 2018, was due to currency movements of $50 million.

The decrease in the gross carrying amount of amortizable intangible assets from December 31, 2018, was mainly due to the deconsolidation of RBH's trademarks of ($275 million) and distribution network of ($29 million), partially offset by currency movements of $6 million.

The change in the accumulated amortization from December 31, 2018 was mainly due to the deconsolidation of RBH's trademarks of ($133 million) and distribution network of ($18 million), partially offset by the 2019 amortization of $66 million and by currency movements of $2 million.

Amortization expense for each of the next five years is estimated to be $73 million or less, assuming no additional transactions occur that require the amortization of intangible assets.

During the second quarter of 2019, PMI completed its annual review of goodwill and non-amortizable intangible assets for potential impairment, and no impairment charges were required as a result of this review.

Note 4.

Related Parties - Investments in Unconsolidated Subsidiaries, Equity Securities and Other:

Investments in unconsolidated subsidiaries:

At December 31, 2019 and 2018, PMI had total investments in unconsolidated subsidiaries of $1,053 million and $981 million, respectively, which were accounted for under the equity method of accounting. Equity method investments are initially recorded at cost. Under the equity method of accounting, the investment is adjusted for PMI's proportionate share of earnings or losses, dividends, capital contributions, changes in ownership interests and movements in currency translation adjustments. The carrying value of our equity method investments at December 31, 2019 and 2018, exceeded our share of the unconsolidated subsidiaries' book value by $901 million and $835 million, respectively. The difference between the investment carrying value and the amount of underlying equity in net assets, excluding $863 million and $793 million attributable to goodwill as of December 31, 2019 and 2018, respectively, is being amortized on a straight-line basis over the underlying assets' estimated useful lives of 10 to 20 years. At December 31, 2019 and 2018, PMI received year-to-date dividends from unconsolidated subsidiaries of $100 million and $118 million, respectively.

PMI holds a 23% equity interest in Megapolis Distribution BV, the holding company of CJSC TK Megapolis, PMI's distributor in Russia (Eastern Europe segment).

PMI holds a 49% equity interest in United Arab Emirates-based Emirati Investors-TA (FZC) ("EITA"). PMI holds an approximate 25% economic interest in Société des Tabacs Algéro-Emiratie ("STAEM"), an Algerian joint venture that is 51% owned by EITA and 49% by the Algerian state-owned enterprise Management et Développement des Actifs et des Ressources Holding ("MADAR Holding"), which is part of the Middle East & Africa segment, manufactures and distributes under license some of PMI's brands.

The initial investments in Megapolis Distribution BV and EITA were recorded at cost and are included in investments in unconsolidated subsidiaries and equity securities on the consolidated balance sheets.

Equity securities:

Following the deconsolidation of RBH, PMI recorded the continuing investment in RBH, PMI's wholly owned subsidiary, at fair value of $3,280 million at the date of deconsolidation, within investments in unconsolidated subsidiaries and equity securities. For further details, see Note 22. *Deconsolidation of RBH*. Transactions between PMI and RBH are considered to be related-party transactions from the date of deconsolidation and are included in the tables below.

Other related parties:

United Arab Emirates-based Trans-Emirates Trading and Investments (FZC) ("TTI") holds a 33% non-controlling interest in Philip Morris Misr LLC ("PMM"), an entity incorporated in Egypt which is consolidated in PMI's financial statements in the Middle East & Africa segment. PMM sells, under license, PMI brands in Egypt through an exclusive distribution agreement with a local entity that is also controlled by TTI.

IPM India, PMI's consolidated subsidiary in the South & Southeast Asia segment, has a non-controlling interest of 43.7% held by Godfrey Phillips India Ltd, who also acts as contract manufacturer and distributor for IPM. Amounts in the tables below include transactions between these related parties, beginning in 2019. Prior periods do not include these transactions as they were not material.

Financial activity with the above related parties:

PMI's net revenues and expenses with the above related parties were as follows:

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Net revenues			
Megapolis Group	**$ 2,236**	$ 1,994	$ 1,874
Other	**1,015**	720	647
Net revenues [a]	**$ 3,251**	$ 2,714	$ 2,521
Expenses:			
Other	**$ 63**	$ 21	$ 23
Expenses	**$ 63**	$ 21	$ 23

[a] Net revenues exclude excise taxes and VAT billed to customers. Prior year's amounts have been reclassified to conform with the current year's presentation.

PMI's balance sheet activity with the above related parties was as follows:

	At December 31,	
(in millions)	**2019**	**2018**
Receivables:		
Megapolis Group	**$ 375**	$ 172
Other	**148**	136
Receivables	**$ 523**	$ 308
Payables:		
Other	**$ 20**	$ 8
Payables	**$ 20**	$ 8

The activities with the above related parties are in the ordinary course of business, and are primarily for distribution, service fees, contract manufacturing and license agreements. PMI eliminated its respective share of all significant intercompany transactions with the equity method investees.

Note 5.

Product Warranty:

PMI's *IQOS* devices are subject to standard product warranties generally for a period of 12 months from the date of purchase or such other periods as required by law. PMI generally provides in cost of sales for the estimated cost of warranty in the period the related revenue is recognized. PMI assesses the adequacy of its accrued product warranties and adjusts the amounts as necessary based on actual experience and changes in future estimates. Factors that affect product warranties may vary across markets but typically include device version mix, product failure rates, logistics and service delivery costs, and warranty policies. PMI accounts for its product warranties within other accrued liabilities. At December 31, 2019 and December 31, 2018, these amounts were as follows:

	At December 31,	
(in millions)	**2019**	**2018**
Balance at beginning of period	**$ 67**	$ 71
Changes due to:		
Warranties issued	**303**	179
Settlements	**(230)**	(183)
Currency	**—**	—
Balance at end of period	**$ 140**	$ 67

Note 6.

Acquisitions:

On March 21, 2018, PMI acquired the remaining 49% interest in Tabacalera Costarricense, S.A. and Mendiola y Compañía, S.A. for a net purchase price of $95 million, which includes $2 million of contingent consideration. As a result, PMI now owns 100% of these Costa Rican affiliates. The purchase of the remaining 49% interest resulted in a decrease to PMI's additional paid-in capital of $86 million.

Note 7.

Indebtedness:

Short-Term Borrowings

At December 31, 2019 and 2018, PMI's short-term borrowings and related average interest rates consisted of the following:

	December 31, 2019		December 31, 2018	
(in millions)	**Amount Outstanding**	**Average Year-End Rate**	**Amount Outstanding**	**Average Year-End Rate**
Commercial paper	**$ —**	**— %**	$ —	— %
Bank loans	**338**	**5.5**	730	5.8
	$ 338		$ 730	

Given the mix of subsidiaries and their respective local economic environments, the average interest rate for bank loans above can vary significantly from day to day and country to country.

The fair values of PMI's short-term borrowings at December 31, 2019 and 2018, based upon current market interest rates, approximate the amounts disclosed above.

Long-Term Debt

At December 31, 2019 and 2018, PMI's long-term debt consisted of the following:

(in millions)	December 31, 2019	December 31, 2018
U.S. dollar notes, 1.875% to 6.375% (average interest rate 3.516%), due through 2044	**$ 19,783**	$ 20,819
Foreign currency obligations:		
Euro notes, 0.125% to 3.125% (average interest rate 1.950%), due through 2039	**9,822**	8,656
Swiss franc notes, 1.000% to 2.000% (average interest rate 1.521%), due through 2024	**899**	1,374
Other (average interest rate 3.125%), due through 2025	**203**	180
	30,707	31,029
Less current portion of long-term debt	**4,051**	4,054
	$ 26,656	$ 26,975

Other debt:

Other foreign currency debt above includes mortgage debt in Switzerland and finance lease obligations at December 31, 2019 and December 31, 2018.

Debt Issuances Outstanding:

PMI's debt issuances outstanding at December 31, 2019, were as follows:

(in millions)

Type	Face Value	Interest Rate	Issuance	Maturity
U.S. dollar notes	**$300**	**Floating**	February 2017	February 2020
U.S. dollar notes	**$1,000**	**2.000%**	February 2017	February 2020
U.S. dollar notes	**$1,000**	**4.500%**	March 2010	March 2020
U.S. dollar notes	**$750**	**1.875%**	February 2016	February 2021
U.S. dollar notes	**$350**	**4.125%**	May 2011	May 2021
U.S. dollar notes	**$750**	**2.900%**	November 2011	November 2021
U.S. dollar notes	**$500**	**2.625%**	February 2017	February 2022
U.S. dollar notes	**$750**	**2.375%**	August 2017	August 2022
U.S. dollar notes	**$750**	**2.500%**	August 2012	August 2022
U.S. dollar notes	**$750**	**2.500%**	November 2017	November 2022
U.S. dollar notes	**$600**	**2.625%**	March 2013	March 2023
U.S. dollar notes	**$500**	**2.125%**	May 2016	May 2023
U.S. dollar notes	**$500**	**3.600%**	November 2013	November 2023
U.S. dollar notes	**$900**	**2.875%**	May 2019	May 2024
U.S. dollar notes	**$750**	**3.250%**	November 2014	November 2024
U.S. dollar notes	**$750**	**3.375%**	August 2015	August 2025
U.S. dollar notes	**$750**	**2.750%**	February 2016	February 2026
U.S. dollar notes	**$500**	**3.125%**	August 2017	August 2027
U.S. dollar notes	**$500**	**3.125%**	November 2017	March 2028
U.S. dollar notes	**$750**	**3.375%**	May 2019	August 2029
U.S. dollar notes	**$1,500**	**6.375%**	May 2008	May 2038
U.S. dollar notes	**$750**	**4.375%**	November 2011	November 2041
U.S. dollar notes	**$700**	**4.500%**	March 2012	March 2042
U.S. dollar notes	**$750**	**3.875%**	August 2012	August 2042
U.S. dollar notes	**$850**	**4.125%**	March 2013	March 2043
U.S. dollar notes	**$750**	**4.875%**	November 2013	November 2043
U.S. dollar notes	**$750**	**4.250%**	November 2014	November 2044
U.S. dollar notes [a]	**$500**	**4.250%**	May 2016	November 2044
EURO notes [b]	**€1,250 (approximately $1,621)**	**1.750%**	March 2013	March 2020
EURO notes [b]	**€750 (approximately $1,029)**	**1.875%**	March 2014	March 2021

EURO notes	(b)	**€600 (approximately $761)**	**2.875%**	May 2012	May 2024
EURO notes	(b)	**€500 (approximately $582)**	**0.625%**	November 2017	November 2024
EURO notes	(b)	**€750 (approximately $972)**	**2.750%**	March 2013	March 2025
EURO notes	(b)	**€1,000 (approximately $1,372)**	**2.875%**	March 2014	March 2026
EURO notes	(b)	**€500 (approximately $557)**	**0.125%**	August 2019	August 2026
EURO notes	(b)	**€500 (approximately $697)**	**2.875%**	May 2014	May 2029
EURO notes	(b)	**€750 (approximately $835)**	**0.800%**	August 2019	August 2031
EURO notes	(b)	**€500 (approximately $648)**	**3.125%**	June 2013	June 2033
EURO notes	(b)	**€500 (approximately $578)**	**2.000%**	May 2016	May 2036
EURO notes	(b)	**€500 (approximately $582)**	**1.875%**	November 2017	November 2037
Euro notes	(b)	**€750 (approximately $835)**	**1.450%**	August 2019	August 2039
Swiss franc notes	(b)	**CHF325 (approximately $334)**	**1.000%**	September 2012	September 2020
Swiss franc notes	(b)	**CHF300 (approximately $335)**	**2.000%**	December 2011	December 2021
Swiss franc notes	(b)	**CHF250 (approximately $283)**	**1.625%**	May 2014	May 2024

[a] These notes are a further issuance of the 4.250% notes issued by PMI in November 2014.
[b] USD equivalents for foreign currency notes were calculated based on exchange rates on the date of issuance.

The net proceeds from the sale of the securities listed in the table above were used for general corporate purposes, including working capital requirements and repurchase of PMI's common stock until 2015.

Aggregate maturities:

Aggregate maturities of long-term debt are as follows:

(in millions)	
2020	$ 4,051
2021	3,015
2022	2,764
2023	1,607
2024	3,283
2025-2029	6,332
2030-2034	1,400
Thereafter	8,510
	30,962
Debt discounts	(255)
Total long-term debt	$ 30,707

See Note 16. *Fair Value Measurements* for additional disclosures related to the fair value of PMI's debt.

Credit Facilities

On January 28, 2019, PMI entered into an agreement to extend the term of its $2.0 billion 364-day revolving credit facility from February 5, 2019, to February 4, 2020.

At December 31, 2019, PMI's total committed credit facilities and commercial paper outstanding were as follows:

Type (in billions of dollars)	**Committed Credit Facilities**	**Commercial Paper**
364-day revolving credit, expiring February 4, 2020	**$ 2.0**	
Multi-year revolving credit, expiring February 28, 2021	**2.5**	
Multi-year revolving credit, expiring October 1, 2022	**3.5**	
Total facilities	**$ 8.0**	
Commercial paper outstanding		**$ —**

At December 31, 2019, there were no borrowings under these committed credit facilities, and the entire committed amounts were available for borrowing.

Each of these facilities requires PMI to maintain a ratio of consolidated earnings before interest, taxes, depreciation and amortization ("consolidated EBITDA") to consolidated interest expense of not less than 3.5 to 1.0 on a rolling four-quarter basis. At December 31, 2019, PMI's ratio calculated in accordance with the agreements was 11.2 to 1.0. These facilities do not include any credit rating triggers, material adverse change clauses or any provisions that could require PMI to post collateral. The terms "consolidated EBITDA" and "consolidated interest expense," both of which include certain adjustments, are defined in the facility agreements previously filed with the Securities and Exchange Commission.

On January 31, 2020, PMI entered into an agreement to amend and extend the term of its $2 billion 364-day revolving credit facility from February 4, 2020, to February 2, 2021.

In addition to the committed credit facilities discussed above, certain subsidiaries maintain short-term credit arrangements to meet their respective working capital needs. These credit arrangements, which amounted to approximately $2.7 billion at December 31, 2019, and $3.3 billion at December 31, 2018, are for the sole use of the subsidiaries. Borrowings under these arrangements amounted to $338 million at December 31, 2019, and $730 million at December 31, 2018.

Note 8.

Capital Stock:

Shares of authorized common stock are 6.0 billion; issued, repurchased and outstanding shares were as follows:

	Shares Issued	Shares Repurchased	Shares Outstanding
Balances, January 1, 2017	2,109,316,331	(557,930,784)	1,551,385,547
Issuance of stock awards		1,832,215	1,832,215
Balances, December 31, 2017	2,109,316,331	(556,098,569)	1,553,217,762
Issuance of stock awards		1,361,959	1,361,959
Balances, December 31, 2018	2,109,316,331	(554,736,610)	1,554,579,721
Issuance of stock awards		**1,314,942**	**1,314,942**
Balances, December 31, 2019	**2,109,316,331**	**(553,421,668)**	**1,555,894,663**

At December 31, 2019, 27,371,404 shares of common stock were reserved for stock awards under PMI's stock plans, and 250 million shares of preferred stock, without par value, were authorized but unissued. PMI currently has no plans to issue any shares of preferred stock.

Note 9.

Stock Plans:

In May 2017, PMI's shareholders approved the Philip Morris International Inc. 2017 Performance Incentive Plan (the "2017 Plan"). Under the 2017 Plan, PMI may grant to eligible employees restricted shares and restricted share units, performance-based cash incentive awards and performance-based equity awards. Up to 25 million shares of PMI's common stock may be issued under the 2017 Plan. At December 31, 2019, shares available for grant under the 2017 Plan were 20,127,360.

In May 2017, PMI's shareholders also approved the Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors (the "2017 Non-Employee Directors Plan"). A non-employee director is defined as a member of the PMI Board of Directors who is not a full-time employee of PMI or of any corporation in which PMI owns, directly or indirectly, stock possessing at least 50% of the total combined voting power of all classes of stock entitled to vote in the election of directors in such corporation. Up to 1 million shares of PMI common stock may be

awarded under the 2017 Non-Employee Directors Plan. At December 31, 2019, shares available for grant under the plan were 954,084.

Restricted share unit (RSU) awards

PMI may grant RSU awards to eligible employees; recipients may not sell, assign, pledge or otherwise encumber such awards. Such awards are subject to forfeiture if certain employment conditions are not met. RSU awards generally vest on the third anniversary of the grant date. RSU awards do not carry voting rights, although they do earn dividend equivalents.

During 2019, the activity for RSU awards was as follows:

	Number of Shares	Weighted-Average Grant Date Fair Value Per Share
Balance at January 1, 2019	**3,318,795**	**$ 96.26**
Granted	**1,726,760**	**77.28**
Vested	**(1,126,057)**	**89.56**
Forfeited	**(193,628)**	**89.36**
Balance at December 31, 2019	**3,725,870**	**$ 89.85**

During the years ended December 31, 2019, 2018 and 2017, the weighted-average grant date fair value of the RSU awards granted to PMI employees and the recorded compensation expense related to RSU awards were as follows:

(in millions, except per RSU award granted)	Total Weighted-Average Grant Date Fair Value of RSU Awards Granted	Weighted-Average Grant Date Fair Value Per RSU Award Granted	Compensation Expense related to RSU Awards
2019	**$ 133**	**$ 77.28**	**$ 118**
2018	$ 129	$ 100.19	$ 114
2017	$ 119	$ 98.59	$ 111

The fair value of the RSU awards at the date of grant is amortized to expense over the restriction period, typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2019, PMI had $124 million of total unrecognized compensation costs related to non-vested RSU awards. These costs are expected to be recognized over a weighted-average period of approximately two years, or upon death, disability or reaching the age of 58.

During the years ended December 31, 2019, 2018 and 2017, share and fair value information for PMI RSU awards that vested were as follows:

(dollars in millions)	Shares of RSU Awards that Vested	Grant Date Fair Value of Vested Shares of RSU Awards	Total Fair Value of RSU Awards that Vested
2019	**1,126,057**	**$ 101**	**$ 95**
2018	1,451,876	$ 121	$ 149
2017	2,022,856	$ 158	$ 208

Performance share unit (PSU) awards

PMI may grant PSU awards to certain executives; recipients may not sell, assign, pledge or otherwise encumber such awards. The PSU awards require the achievement of certain performance factors, which are predetermined at the time of grant, typically over a three-year performance cycle with performance metrics for such PSUs consisting of

PMI’s Total Shareholder Return (TSR) relative to a predetermined peer group and on an absolute basis (50% weight), PMI’s currency-neutral compound annual adjusted operating income growth rate, excluding acquisitions (30% weight), and PMI’s performance against specific measures of PMI's transformation (20% weight). The aggregate of the weighted performance factors for the three metrics determines the percentage of PSUs that will vest at the end of the three-year performance cycle. The minimum percentage of such PSUs that can vest is zero, with a target percentage of 100 and a maximum percentage of 200. Each such vested PSU entitles the participant to one share of common stock. An aggregate weighted PSU performance factor of 100 will result in the targeted number of PSUs being vested. At the end of the performance cycle, participants are entitled to an amount equivalent to the accumulated dividends paid on common stock during the performance cycle for the number of shares earned. PSU awards do not carry voting rights.

During 2019, the activity for PSU awards was as follows:

	Number of Shares	Grant Date Fair Value Subject to Other Performance Factors Per Share	Grant Date Fair Value Subject to TSR Performance Factor Per Share
Balance at January 1, 2019	**1,194,970**	**$ 95.85**	**$ 117.09**
Granted	**647,700**	**77.23**	**83.59**
Vested	**(330,616)**	**89.02**	**104.60**
Forfeited	**(164,594)**	**90.28**	**107.09**
Balance at December 31, 2019	**1,347,460**	**$ 88.19**	**$ 107.61**

During the years ended December 31, 2019, 2018 and 2017, the grant date fair value of the PSU awards granted to PMI employees and the recorded compensation expense related to PSU awards were as follows:

(in millions, except per PSU award granted)	PSU Grant Date Fair Value Subject to Other Performance Factors		PSU Grant Date Fair Value Subject to TSR Performance Factor		Compensation Expense related to PSU Awards
	Total	Per PSU Award	Total	Per PSU Award	Total
2019	**$ 30**	**$ 77.23**	**$ 21**	**$ 83.59**	**$ 54**
2018	$ 20	$ 100.69	$ 24	$ 118.98	$ 24
2017	$ 19	$ 98.29	$ 25	$ 128.72	$ 37

The grant date fair value of the PSU awards subject to the other performance factors was determined by using the average of the high and low market price of PMI's stock at the date of the grant. The grant date fair value of the PSU market-based awards subject to the TSR performance factor was determined by using the Monte Carlo simulation model. The following assumptions were used to determine the grant date fair value of the PSU awards subject to the TSR performance factor for the years ended December 31, 2019, 2018 and 2017:

	For the Years Ended December 31,		
	2019	2018	2017
Risk-free interest rate [a]	**2.4 %**	2.3 %	1.5 %
Expected volatility	**21.4 %** [b]	19.6 % [c]	15.8 % [c]

[a] Based on the U.S. Treasury yield curve.
[b] Determined using the observed historical volatility.
[c] Determined using a weighted-average of historical and implied volatility.

The fair value of the PSU award at the date of grant is amortized to expense over the performance period, which is typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2019, PMI had $33 million of total unrecognized compensation cost related to non-vested PSU awards. This cost is recognized over a weighted-average performance cycle period of approximately two years, or upon death, disability or reaching the age of 58.

During the year ended December 31, 2019, share and fair value information for PMI PSU awards that vested were as follows:

(dollars in millions)	Shares of PSU Awards that Vested	Grant Date Fair Value of Vested Shares of PSU Awards	Total Fair Value of PSU Awards that Vested
2019	**330,616**	**$ 32**	**$ 28**

During the years ended December 31, 2018 and 2017, there were no PSU awards that vested.

Note 10.

Earnings per Share:

Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are participating securities and therefore are included in PMI's earnings per share calculation pursuant to the two-class method.

Basic and diluted earnings per share ("EPS") were calculated using the following:

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Net earnings attributable to PMI	**$ 7,185**	$ 7,911	$ 6,035
Less distributed and undistributed earnings attributable to share-based payment awards	**17**	16	14
Net earnings for basic and diluted EPS	**$ 7,168**	$ 7,895	$ 6,021
Weighted-average shares for basic EPS	**1,555**	1,555	1,552
Plus contingently issuable performance stock units (PSUs)	**1**	—	1
Weighted-average shares for	**1,556**	1,555	1,553

diluted
EPS

For the 2019, 2018 and 2017 computations, there were no antidilutive stock options.

Note 11.

Income Taxes:

Earnings before income taxes and provision for income taxes consisted of the following for the years ended December 31, 2019, 2018 and 2017:

(in millions)	2019	2018	2017
Earnings before income taxes	**$ 9,872**	$ 10,671	$ 10,589
Provision for income taxes:			
United States federal and state:			
Current	**$ 17**	$ 120	$ 1,662
Deferred	**24**	(113)	(384)
Total United States	**41**	7	1,278
Outside United States:			
Current	**2,417**	2,425	3,146
Deferred	**(165)**	13	(117)
Total outside United States	**2,252**	2,438	3,029
Total provision for income taxes	**$ 2,293**	$ 2,445	$ 4,307

In December 2017, the Tax Cuts and Jobs Act was signed into law. Accordingly, PMI recorded a provisional charge of $1.6 billion in its 2017 income tax provision, including a charge for the transition tax on accumulated foreign earnings of $1.4 billion (which represented the transition tax of $2.2 billion, net of a reversal of $0.7 billion of previously recorded deferred tax liabilities on part of its accumulated foreign earnings and other items of $0.1 billion) and $0.2 billion due to the re-measurement of U.S. deferred tax assets and liabilities applying the U.S. federal corporate tax rate of 21%.

PMI completed its analysis of the Tax Cuts and Jobs Act during 2018 and adjusted the 2017 provisional estimates to the final amounts based on its 2017 U.S. federal income tax return as filed. Accordingly, PMI recorded in its income tax provision a charge of $31 million

representing a current income tax charge of $185 million, primarily due to an increase in its aggregate foreign cash position used to determine PMI's final 2017 transition tax liability, mostly offset by a deferred income tax benefit of $154 million primarily due to the recognition of deferred tax assets for net operating losses in the state of New York. Updates to the provisional estimates have been recorded in accordance with Staff Accounting Bulletin No. 118 ("SAB 118").

At December 31, 2017, PMI recorded an income tax payable of $1.7 billion attributable to the Tax Cuts and Jobs Act, of which $1.6 billion was recorded in "income taxes and other liabilities" on PMI's consolidated balance sheet. The income tax payable of $1.7 billion represented the transition tax of $2.2 billion, partially offset by foreign tax credits related to foreign withholding taxes previously paid of $0.5 billion. The income tax payable is due over an eight-year period beginning in 2018. In December 2018, PMI recorded an increase to income tax payable of $0.1 billion related to PMI's transition tax liability, in accordance with SAB 118. At December 31, 2019 and December 31, 2018, $1.2 billion and $1.5 billion of PMI's remaining transition tax liability, respectively, was recorded in "income taxes and other liabilities" on PMI's consolidated balance sheet.

At December 31, 2019 and December 31, 2018, U.S. federal and foreign deferred income taxes have been provided on all accumulated earnings of PMI's foreign subsidiaries.

In accordance with the alternatives provided by ASU 2018-02 "Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income," PMI has elected not to reclassify the income tax effects of the Tax Cuts and Jobs Act from accumulated other comprehensive losses to retained earnings.

PMI is regularly examined by tax authorities around the world and is currently under examination in a number of jurisdictions. The U.S. federal statute of limitations remains open for the years 2015 and onward. Foreign and U.S. state jurisdictions have statutes of limitations generally ranging from three to five years. Years still open to examination by foreign tax authorities in major jurisdictions include Germany (2015 onward), Indonesia (2014 onward), Russia (2017 onward), Switzerland (2017 onward), and Turkey (2014 onward).

It is reasonably possible that within the next 12 months certain tax examinations will close, which could result in a change in unrecognized tax benefits, along with related interest and penalties. An estimate of any possible change cannot be made at this time.

A reconciliation of the beginning and ending amount of unrecognized tax benefits was as follows:

(in millions)	**2019**	**2018**	**2017**
Balance at January 1,	**$ 56**	$ 145	$ 79
Additions based on tax positions related to the current year	**10**	10	71
Additions for tax positions of previous years	**1**	15	5
Reductions for tax positions of prior years	**(2)**	(94)	—
Reductions due to lapse of statute of limitations	**(1)**	(3)	(7)
Settlements	**—**	(19)	(4)
Other	**(1)**	2	1
Balance at December 31,	**$ 63**	$ 56	$ 145

Unrecognized tax benefits and PMI's liability for contingent income taxes, interest and penalties were as follows:

(in millions)	**December 31, 2019**	**December 31, 2018**	**December 31, 2017**
Unrecognized tax benefits	**$ 63**	$ 56	$ 145
Accrued interest and penalties	**16**	12	23

Tax credits and other indirect benefits	**(12)**	(14)	(35)
Liability for tax contingencies	**$ 67**	$ 54	$ 133

The amount of unrecognized tax benefits that, if recognized, would impact the effective tax rate was $50 million at December 31, 2019. The remainder, if recognized, would principally affect deferred taxes.

For the years ended December 31, 2019, 2018 and 2017, PMI recognized income (expense) in its consolidated statements of earnings of $(4) million, $4 million and $(11) million, respectively, related to interest and penalties associated with uncertain tax positions.

The effective income tax rate on pre-tax earnings differed from the U.S. federal statutory rate for the following reasons for the years ended December 31, 2019, 2018 and 2017:

	2019	2018	2017
U.S. federal statutory rate	**21.0 %**	21.0 %	35.0 %
Increase (decrease) resulting from:			
Foreign rate differences	**1.8**	1.3	(12.2)
Dividend repatriation cost	**(0.5)**	2.5	16.4
Global intangible low-taxed income	**1.4**	1.2	
U.S. state taxes	**0.7**	(1.1)	
Foreign derived intangible income	**(1.2)**	(1.1)	
Other	**—**	(0.9)	1.5
Effective tax rate	**23.2 %**	22.9 %	40.7 %

The 2019 effective tax rate increased 0.3 percentage points to 23.2%. The change in the effective tax rate for 2019, as compared to 2018, was unfavorably impacted by changes in earnings mix by taxing jurisdiction and U.S. state deferred income tax expense, partially offset by the reversal of a deferred tax liability on the unremitted earnings of PMI's Canadian subsidiary, RBH ($49 million), a reduction in estimated U.S. federal income tax on dividend repatriation for the years 2015-2018 ($67 million), and other repatriation cost differences.

The 2018 effective tax rate decreased 17.8 percentage points to 22.9%. The change in the effective tax rate for 2018, as compared to 2017, was primarily due to the Tax Cuts and Jobs Act, which reduced the U.S. federal income tax rate from 35% to 21%, in addition to repatriation cost differences and earnings mix by taxing jurisdiction.

The 2017 effective tax rate increased 12.8 percentage points to 40.7%. The change in the effective tax rate for 2017, as compared to 2016, was primarily due to the Tax Cuts and Jobs Act. In addition to the transition tax, which resulted in a net tax charge of $1.4 billion, the Tax Cuts and Jobs Act also included a reduction in the U.S. income tax rate from 35% to 21%, as of January 1, 2018. This change in income tax rate required a re-measurement of PMI's U.S. deferred tax assets and liabilities at December 31, 2017, resulting in a tax charge of $0.2 billion.

The tax effects of temporary differences that gave rise to deferred income tax assets and liabilities consisted of the following:

(in millions)	At December 31, 2019	At December 31, 2018
Deferred income tax assets:		
Accrued postretirement and postemployment benefits	**$ 184**	$ 193
Accrued pension costs	**620**	390
Inventory	**176**	136
Accrued liabilities	**130**	138
Net operating loss carryforwards and tax credits	**486**	452

Other	**101**	37
Total deferred income tax assets	**1,697**	1,346
Less: valuation allowance	**(304)**	(257)
Deferred income tax assets, net of valuation allowance	**1,393**	1,089
Deferred income tax liabilities:		
Trade names	**(469)**	(508)
Property, plant and equipment	**(180)**	(222)
Unremitted earnings	**(243)**	(123)
Foreign exchange	**(256)**	(157)
Total deferred income tax liabilities	**(1,148)**	(1,010)
Net deferred income tax assets	**$ 245**	$ 79

At December 31, 2019, PMI recorded deferred tax assets for net operating loss carryforwards and tax credits of $486 million, with varying dates of expiration, primarily after 2024, including $98 million with an unlimited carryforward period. At December 31, 2019, PMI has recorded a valuation allowance of $304 million against deferred tax assets that do not meet the more-likely-than not recognition threshold.

At December 31, 2018, PMI recorded deferred tax assets for net operating loss carryforwards of $452 million, with varying dates of expiration, primarily after 2023, including $87 million with an unlimited carryforward period. At December 31, 2018, PMI has recorded a valuation allowance of $257 million against deferred tax assets that do not meet the more-likely-than-not recognition threshold. The increases in deferred tax assets for net operating loss carryforwards and the valuation allowance during 2018 are primarily due to law changes associated with the Tax Cuts and Jobs Act, as discussed above.

Note 12.

Segment Reporting:

PMI's subsidiaries and affiliates are engaged in the manufacture and sale of cigarettes and other nicotine-containing products, including RRPs, in markets outside of the United States of America. In addition, PMI ships a version of its Platform 1 device and its consumables authorized by the FDA to Altria Group, Inc. for sale in the United States under license. Operating segments for PMI are organized by geographic region and managed by segment managers who are responsible for the operating and financial results of the regions inclusive of all product categories sold in the region. PMI's operating segments are the European Union; Eastern Europe; Middle East & Africa; South & Southeast Asia; East Asia & Australia; and Latin America & Canada. PMI records net revenues and operating income to its segments based upon the geographic area in which the customer resides. Revenues from shipments of Platform 1 devices, heated tobacco units and accessories to Altria Group, Inc. for sale under license in the United States are included in Net Revenues of the Latin America & Canada segment.

PMI's chief operating decision maker evaluates segment performance and allocates resources based on regional operating income, which includes results from all product categories sold in each region. Interest expense, net, and provision for income taxes are centrally managed and, accordingly, such items are not presented by segment since they are excluded from the measure of segment profitability reviewed by management. Information about total assets by segment is not disclosed because such information is not reported to or used by PMI's chief operating decision maker. Segment goodwill and other intangible assets, net, are disclosed in Note 3. *Goodwill and Other Intangible Assets, net.* The accounting policies of the segments are the same as those described in Note 2. *Summary of Significant Accounting Policies.*

PMI disaggregates its net revenue from contracts with customers by both geographic location and product category for each of PMI's six operating segments, as PMI believes this best depicts how the nature, amount, timing and uncertainty of its revenue and cash flows are affected by economic factors.

Net revenues by segment were as follows:

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Net revenues:			
European Union	**$ 9,817**	$ 9,298	$ 8,318
Eastern Europe	**3,282**	2,921	2,711
Middle East & Africa	**4,042**	4,114	3,988
South & Southeast Asia	**5,094**	4,656	4,417
East Asia & Australia	**5,364**	5,580	6,373
Latin America & Canada	**2,206**	3,056	2,941
Net revenues	**$ 29,805**	$ 29,625	$ 28,748

Total net revenues attributable to customers located in Japan, PMI's largest market in terms of net revenues, were $3.9 billion, $3.8 billion and $4.7 billion in 2019, 2018 and 2017, respectively. Total net revenues attributable to customers located in Indonesia were $3.1 billion, $3.1 billion and $3.2 billion in 2019, 2018 and 2017, respectively. PMI had one customer in the East Asia & Australia segment that accounted for 13%, 13% and 16% of PMI's consolidated net revenues, and one customer in the European Union segment that accounted for 10%, 10% and 10% of PMI's consolidated net revenues in 2019, 2018 and 2017, respectively.

PMI's net revenues by product category were as follows:

(in millions)	For the Years Ended December 31, 2019	2018	2017
Combustible products:			
European Union	**$ 8,093**	$ 8,433	$ 8,048
Eastern Europe	**2,438**	2,597	2,657
Middle East & Africa	**3,721**	3,732	3,893
South & Southeast Asia	**5,094**	4,656	4,417
East Asia & Australia	**2,693**	3,074	3,156
Latin America & Canada	**2,179**	3,037	2,937
Total combustible products	**$ 24,218**	$ 25,529	$ 25,107
Reduced-risk products:			
European Union	**$ 1,724**	$ 865	$ 269
Eastern Europe	**844**	324	55
Middle East & Africa	**321**	382	94
South & Southeast Asia	**—**	—	—
East Asia & Australia	**2,671**	2,506	3,218
Latin America & Canada	**27**	19	4
Total reduced-risk products	**$ 5,587**	$ 4,096	$ 3,640
Total PMI net revenues	**$ 29,805**	$ 29,625	$ 28,748

Note: Sum of product categories or Regions might not foot to total PMI due to roundings.

Net revenues related to combustible products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of PMI's cigarettes and other tobacco products combined. Other tobacco products primarily include roll-your-own and make-your-own cigarettes, pipe tobacco, cigars and cigarillos and do not include reduced-risk products.

Net revenues related to reduced-risk products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of PMI's heated tobacco units, *IQOS* devices and related accessories, and other nicotine-containing products, which primarily include PMI's e-vapor products.

PMI recognizes revenue, when control is transferred to the customer, typically either upon shipment or delivery of goods.

Operating income by segment were as follows:

(in millions)	For the Years Ended December 31, 2019	2018	2017
Operating income:			
European Union	**$ 3,970**	$ 4,105	$ 3,691
Eastern Europe	**547**	902	887
Middle East & Africa	**1,684**	1,627	1,884
South & Southeast Asia	**2,163**	1,747	1,514
East Asia & Australia	**1,932**	1,851	2,608
Latin America & Canada	**235**	1,145	997
Operating income	**$ 10,531**	$ 11,377	$ 11,581

Items affecting the comparability of results from operations were as follows:

- **Russia excise and VAT audit charge** - See Note 18. *Contingencies* for details of the $374 million pre-tax charge included in the Eastern Europe segment for the year ended December 31, 2019.

- **Asset impairment and exit costs** - See Note 21. *Asset Impairment and Exit Costs* for details of the $422 million pre-tax charge for the year ended December 31, 2019, as well as a breakdown of these costs by segment.

- **Canadian tobacco litigation-related expense** - See Note 18. *Contingencies* and Note 22. *Deconsolidation of RBH* for details of the $194 million pre-tax charge included in the Latin America & Canada segment for the year ended December 31, 2019.

- **Loss on deconsolidation of RBH** - See Note 22. *Deconsolidation of RBH* for details of the $239 million loss included in the Latin America & Canada segment for the year ended December 31, 2019.

Other segment data were as follows:

(in millions)	**For the Years Ended December 31,**		
	2019	**2018**	**2017**
Depreciation expense:			
European Union	**$ 254**	$ 269	$ 213
Eastern Europe	**147**	101	76
Middle East & Africa	**90**	105	88
South & Southeast Asia	**142**	154	153
East Asia & Australia	**185**	173	160
Latin America & Canada	**69**	94	85
	887	896	775
Other	**11**	11	12
Total depreciation expense	**$ 898**	$ 907	$ 787

(in millions)	**For the Years Ended December 31,**		
	2019	**2018**	**2017**
Capital expenditures:			
European Union	**$ 466**	$ 813	$ 956
Eastern Europe	**132**	136	97
Middle East & Africa	**35**	65	85
South & Southeast Asia	**100**	129	140
East Asia & Australia	**67**	215	87
Latin America & Canada	**52**	74	175
	852	1,432	1,540
Other	**—**	4	8
Total capital expenditures	**$ 852**	$ 1,436	$ 1,548

(in millions)	At December 31, 2019	2018	2017
Long-lived assets:			
European Union	**$ 4,275**	$ 4,216	$ 4,130
Eastern Europe	**774**	547	546
Middle East & Africa	**369**	362	430
South & Southeast Asia	**1,361**	1,297	1,419
East Asia & Australia	**829**	781	659
Latin America & Canada	**478**	779	885
Total long-lived assets	**8,086**	7,982	8,069
Other	**516**	664	1,126
Total property, plant and equipment, net and Other assets	**$ 8,602**	$ 8,646	$ 9,195

Long-lived assets consist of non-current assets other than goodwill; other intangible assets, net; deferred tax assets, investments in unconsolidated subsidiaries and equity securities, and financial instruments. PMI's largest markets in terms of long-lived assets are Italy, Switzerland and Indonesia. Total long-lived assets located in Italy, which is reflected in the European Union segment above, were $1.1 billion, $1.1 billion and $1.2 billion at December 31, 2019, 2018 and 2017, respectively. Total long-lived assets located in Switzerland, which is reflected in the European Union segment above, were $1.1 billion, $1.0 billion and $0.9 billion at December 31, 2019, 2018 and 2017, respectively. Total long-lived assets located in Indonesia, which is reflected in the South & Southeast Asia segment above, were $0.8 billion, $0.7 billion and $0.8 billion at December 31, 2019, 2018 and 2017, respectively.

Note 13.

Benefit Plans:

Pension coverage for employees of PMI's subsidiaries is provided, to the extent deemed appropriate, through separate plans, many of which are governed by local statutory requirements. In addition, PMI provides health care and other benefits to substantially all U.S. retired employees and certain non-U.S. retired employees. In general, health care benefits for non-U.S. retired employees are covered through local government plans.

Pension and other employee benefit costs per the consolidated statements of earnings consisted of the following for December 31, 2019, 2018 and 2017:

(in millions)	2019	2018	2017
Net pension costs (income)	**$ (18)**	$ (51)	$ (20)
Net postemployment costs	**100**	80	85
Net postretirement costs	**7**	12	13
Total pension and other employee benefit costs	**$ 89**	$ 41	$ 78

Pension and Postretirement Benefit Plans

Obligations and Funded Status

The postretirement health care plans are not funded. The projected benefit obligations, plan assets and funded status of PMI's pension plans, and the accumulated benefit obligation and net amount accrued for PMI's postretirement health care plans, at December 31, 2019 and 2018, were as follows:

(in millions)	Pension[1]		Postretirement	
	2019	**2018**	**2019**	**2018**
Benefit obligation at January 1	**$ 9,152**	$ 9,028	**$ 209**	$ 248
Service cost	**214**	210	**2**	4
Interest cost	**118**	109	**7**	9
Net benefits paid	**(250)**	(218)	**(8)**	(8)
Settlement and curtailment	**50**	1		—
Actuarial losses (gains)	**1,430**	210	**27**	(34)
Currency	**29**	(196)	**—**	(9)
Deconsolidation of RBH	**(166)**	—	**(42)**	—
Other	**35**	8	**(5)**	(1)
Benefit obligation at December 31,	**10,612**	9,152	**190**	209
Fair value of plan assets at January 1,	**6,888**	7,598		
Actual return on plan assets	**1,211**	(447)		
Employer contributions	**200**	110		
Standard employee contributions	**44**	24		
Net benefits paid	**(250)**	(218)		
Settlement and curtailment	**—**	—		
Currency	**7**	(179)		
Deconsolidation of RBH	**(172)**	—		
Fair value of plan assets at December 31,	**7,928**	6,888		
Net pension and postretirement liability recognized at December 31,	**$ (2,684)**	$ (2,264)	**$ (190)**	$ (209)

(1) Primarily non-U.S. based defined benefit retirement plans.

At December 31, 2019, actuarial losses (gains) consisted primarily of losses for assumption changes related to lower discount rate for Swiss, German and Dutch plans. At December 31, 2018, actuarial losses (gains) consisted of losses for experience differences related to the change in population profile, coupled with updated mortality table assumptions for the Swiss plan.

At December 31, 2019 and 2018, the Swiss pension plan represented 62% and 60% of the benefit obligation, respectively, and approximately 59% and 57% of the fair value of plan assets at December 31, 2019 and 2018,

respectively. At December 31, 2019 and 2018, the U.S. pension plan represented 4% and 4% of the benefit obligation, respectively, and approximately 4% and 4% of the fair value of plan assets at December 31, 2019 and 2018, respectively.

At December 31, 2019 and 2018, the amounts recognized on PMI's consolidated balance sheets for the pension and postretirement plans were as follows:

	Pension		Postretirement	
(in millions)	**2019**	**2018**	**2019**	**2018**
Other assets	**$ 43**	$ 37		
Accrued liabilities — employment costs	**(23)**	(20)	**$ (8)**	$ (10)
Long-term employment costs	**(2,704)**	(2,281)	**(182)**	(199)
	$ (2,684)	$ (2,264)	**$ (190)**	$ (209)

The accumulated benefit obligation, which represents benefits earned to date, for the pension plans was $9,969 million and $8,557 million at December 31, 2019 and 2018, respectively.

For pension plans with accumulated benefit obligations in excess of plan assets, the accumulated benefit obligation and fair value of plan assets were $8,962 million and $6,825 million, respectively, as of December 31, 2019. The accumulated benefit obligation and fair value of plan assets were $7,641 million and $5,866 million, respectively, as of December 31, 2018.

For pension plans with projected benefit obligations in excess of plan assets, the projected benefit obligation and fair value of plan assets were $10,364 million and $7,654 million, respectively, as of December 31, 2019. The projected benefit obligation and fair value of plan assets were $8,807 million and $6,504 million, respectively, as of December 31, 2018.

The following weighted-average assumptions were used to determine PMI's pension and postretirement benefit obligations at December 31:

	Pension		Postretirement	
	2019	**2018**	**2019**	**2018**
Discount rate	**0.83 %**	1.61 %	**3.28 %**	3.97 %
Rate of compensation increase	**1.82**	1.86		
Interest crediting rate	**3.20**	3.40		
Health care cost trend rate assumed for next year			**6.21**	6.17
Ultimate trend rate			**5.09**	4.59
Year that rate reaches the ultimate trend rate			**2023**	2040

The discount rate for the largest pension plans is based on a yield curve constructed from a portfolio of high quality corporate bonds that produces a cash flow pattern equivalent to each plan's expected benefit payments. The discount rate for the remaining plans is developed from local bond indices that match local benefit obligations as closely as possible.

Components of Net Periodic Benefit Cost

Net periodic pension and postretirement health care costs consisted of the following for the years ended December 31, 2019, 2018 and 2017:

(in millions)	Pension			Postretirement		
	2019	**2018**	**2017**	**2019**	**2018**	**2017**
Service cost	**$ 214**	$ 210	$ 208	**$ 2**	$ 4	$ 4
Interest cost	**118**	109	108	**7**	9	8
Expected return on plan assets	**(328)**	(349)	(326)	**—**	—	—
Amortization:						
Net losses	**189**	172	186	**—**	4	5
Prior service cost	**(1)**	2	6	**—**	(1)	—
Settlement and curtailment	**4**	15	6	**—**	—	—
Net periodic pension and postretirement costs	**$ 196**	$ 159	$ 188	**$ 9**	$ 16	$ 17

Settlement and curtailment charges were due primarily to employee severance and early retirement programs.

The following weighted-average assumptions were used to determine PMI's net pension and postretirement health care costs:

	Pension			Postretirement		
	2019	**2018**	**2017**	**2019**	**2018**	**2017**
Discount rate - service cost	**2.14 %**	1.92 %	1.68 %	**3.97 %**	3.79 %	3.68 %
Discount rate - interest cost	**1.35**	1.25	1.27	**3.97**	3.79	3.68
Expected rate of return on plan assets	**4.70**	4.76	4.80			
Rate of compensation increase	**1.86**	1.65	1.68			
Interest crediting rate	**3.40**	3.40	3.40			
Health care cost trend rate				**6.17**	6.17	7.15

PMI's expected rate of return on pension plan assets is determined by the plan assets' historical long-term investment performance, current asset allocation and estimates of future long-term returns by asset class.

PMI and certain of its subsidiaries sponsor defined contribution plans. Amounts charged to expense for defined contribution plans totaled $63 million, $66 million and $58 million for the years ended December 31, 2019, 2018 and 2017, respectively.

Plan Assets

PMI's investment strategy for pension plans is based on an expectation that equity securities will outperform debt securities over the long term. Accordingly, the target allocation of PMI's plan assets is broadly characterized as

approximately 60% in equity securities and approximately 40% in debt securities and other assets. The strategy primarily utilizes indexed U.S. equity securities, international equity securities and investment-grade debt securities. PMI's plans have no investments in hedge funds, private equity or derivatives. PMI attempts to mitigate investment risk by rebalancing between equity and debt asset classes once a year or as PMI's contributions and benefit payments are made.

The fair value of PMI's pension plan assets at December 31, 2019 and 2018, by asset category was as follows:

Asset Category (in millions)	At December 31, 2019	Quoted Prices In Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	**$ 276**	**$ 276**		
Equity securities:				
U.S. securities	**170**	**170**		
International securities	**563**	**563**		
Investment funds[a]	**6,125**	**4,625**	**$ 1,500**	
International government bonds	**197**	**137**	**60**	
Corporate bonds	**282**	**282**		
Other	**6**	**6**		
Total assets in the fair value hierarchy	**$ 7,619**	**$ 6,059**	**$ 1,560**	**$ —**
Investment funds measured at net asset value[b]	**309**			
Total assets	**$ 7,928**			

[a] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and JP Morgan EMBI for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 63% are invested in U.S. and international equities; 16% are invested in U.S. and international government bonds; 12% are invested in real estate and other money markets, and 9% are invested in corporate bonds.

[b] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Asset Category (in millions)	At December 31, 2018	Quoted Prices In Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$ 84	$ 84		
Equity securities:				
U.S. securities	139	139		
International securities	442	442		
Investment funds[a]	5,508	3,595	$ 1,913	

International government bonds	176	120	56	
Corporate bonds	232	232		
Other	19	19		
Total assets in the fair value hierarchy	$ 6,600	$ 4,631	$ 1,969	$ —
Investment funds measured at net asset value[b]	288			
Total assets	$ 6,888			

[a] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and Barclays Capital U.S. for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 57% were invested in U.S. and international equities; 20% were invested in U.S. and international government bonds; 12% were invested in real estate and other money markets, and 11% were invested in corporate bonds.

[b] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

See Note 16. *Fair Value Measurements* for a discussion of the fair value of pension plan assets.

PMI makes, and plans to make, contributions to the extent that they are tax deductible and to meet specific funding requirements of its funded pension plans. Currently, PMI anticipates making contributions of approximately $77 million in 2020 to its pension plans, based on current tax and benefit laws. However, this estimate is subject to change as a result of changes in tax and other benefit laws, as well as asset performance significantly above or below the assumed long-term rate of return on pension assets, or changes in interest and currency rates.

The estimated future benefit payments from PMI pension plans at December 31, 2019, are as follows:

(in millions)	
2020	$ 317
2021	340
2022	341
2023	351
2024	361
2025 - 2029	2,008

PMI's expected future annual benefit payments for its postretirement health care plans are estimated to be not material through 2029.

Postemployment Benefit Plans

PMI and certain of its subsidiaries sponsor postemployment benefit plans covering substantially all salaried and certain hourly employees. The cost of these plans is charged to expense over the working life of the covered employees. Net postemployment costs were $171 million, $158 million and $144 million for the years ended December 31, 2019, 2018 and 2017, respectively.

The amounts recognized in accrued postemployment costs on PMI's consolidated balance sheets at December 31, 2019 and 2018, were $751 million and $708 million, respectively. The change in the liability is primarily due to actuarial losses of $152 million in 2019 resulting from increased employee severance rate primarily in countries in the European Union segment, coupled with the periodic expense, partially offset by cash payments.

The accrued postemployment costs were determined using a weighted-average discount rate of 3.0% and 3.1% in 2019 and 2018, respectively; an assumed ultimate annual weighted-average turnover rate of 3.0% and 3.2% in 2019 and 2018, respectively; assumed compensation cost increases of 2.6% in 2019 and 2.6% in 2018, and assumed benefits as defined in the respective plans. In accordance with local regulations, certain postemployment plans are funded. As a result, the accrued postemployment costs disclosed above are presented net of the related assets of $40 million and $38 million at December 31, 2019 and 2018, respectively. Postemployment costs arising from actions that offer employees benefits in excess of those specified in the respective plans are charged to expense when incurred.

Comprehensive Earnings (Losses)

The amounts recorded in accumulated other comprehensive losses at December 31, 2019, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (3,718)	$ (63)	$ (775)	$ (4,556)
Prior service cost	3	2	—	5
Net transition obligation	(4)	—	—	(4)
Deferred income taxes	520	24	182	726
Losses to be amortized	$ (3,199)	$ (37)	$ (593)	$ (3,829)

The amounts recorded in accumulated other comprehensive losses at December 31, 2018, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (3,438)	$ (41)	$ (702)	$ (4,181)
Prior service cost	(27)	3	—	(24)
Net transition obligation	(4)	—	—	(4)
Deferred income taxes	379	20	164	563
Losses to be amortized	$ (3,090)	$ (18)	$ (538)	$ (3,646)

The amounts recorded in accumulated other comprehensive losses at December 31, 2017, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (2,624)	$ (80)	$ (617)	$ (3,321)
Prior service cost	(35)	4	—	(31)
Net transition obligation	(5)	—	—	(5)
Deferred income taxes	327	28	186	541
Losses to be amortized	$ (2,337)	$ (48)	$ (431)	$ (2,816)

The movements in other comprehensive earnings (losses) during the year ended December 31, 2019, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	**$ 198**	**$ 3**	**$ 77**	**$ 278**
Prior service cost	**32**	**(1)**	**—**	**31**
Other income/expense:				
Net losses	**3**	**—**	**—**	**3**
Deferred income taxes	**(51)**	**(1)**	**(17)**	**(69)**
	182	**1**	**60**	**243**
Other movements during the year:				
Net losses	**(521)**	**(27)**	**(150)**	**(698)**
Prior service cost	**(2)**	**—**	**—**	**(2)**
Deconsolidation of RBH (net of deferred income taxes)	**26**	**1**		**27**
Deferred income taxes	**206**	**6**	**35**	**247**

	(291)	**(20)**	**(115)**	**(426)**
Total movements in other comprehensive earnings (losses)	**$ (109)**	**$ (19)**	**$ (55)**	**$ (183)**

The movements in other comprehensive earnings (losses) during the year ended December 31, 2018, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	$ 180	$ 5	$ 62	$ 247
Prior service cost	—	(1)	—	(1)
Net transition obligation	1	—	—	1
Other income/expense:				
Net losses	14	—	—	14
Deferred income taxes	(28)	(1)	(14)	(43)
	167	3	48	218
Other movements during the year:				
Net losses	(1,008)	34	(147)	(1,121)
Prior service cost	8	—	—	8
Deferred income taxes	80	(7)	(8)	65
	(920)	27	(155)	(1,048)
Total movements in other comprehensive earnings (losses)	$ (753)	$ 30	$ (107)	$ (830)

The movements in other comprehensive earnings (losses) during the year ended December 31, 2017, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	$ 175	$ 5	$ 68	$ 248
Prior service cost	5	—	—	5
Other income/expense:				
Net losses	6	—	—	6
Deferred income taxes	(10)	(1)	(20)	(31)
	176	4	48	228
Other movements during the year:				
Net losses	509	(12)	28	525
Prior service cost	13	—	—	13
Deferred income taxes	(13)	5	(9)	(17)
	509	(7)	19	521
Total movements in other comprehensive earnings (losses)	$ 685	$ (3)	$ 67	$ 749

Note 14.

Additional Information:

(in millions)	For the Years Ended December 31, 2019	2018	2017
Research and development expense	**$ 465**	$ 383	$ 453
Advertising expense	**$ 730**	$ 896	$ 830
Foreign currency net transaction (gains)/losses	**$ (95)**	$ 21	$ 49
Interest expense	**$ 796**	$ 855	$ 1,096
Interest income	**(226)**	(190)	(182)
Interest expense, net	**$ 570**	$ 665	$ 914
Total lease cost	**$ 332** [1]	$ 312	$ 313

[1] For additional information on total lease costs, see Note 23. *Leases.*

Note 15.

Financial Instruments:

Overview

PMI operates in markets outside of the United States of America, with manufacturing and sales facilities in various locations around the world. PMI utilizes certain financial instruments to manage foreign currency and interest rate exposure. Derivative financial instruments are used by PMI principally to reduce exposures to market risks resulting from fluctuations in foreign currency exchange and interest rates by creating offsetting exposures. PMI is not a party to leveraged derivatives and, by policy, does not use derivative financial instruments for speculative purposes. Financial instruments qualifying for hedge accounting must maintain a specified level of effectiveness between the hedging instrument and the item being hedged, both at inception and throughout the hedged period. PMI formally documents the nature and relationships between the hedging instruments and hedged items, as well as its risk-management objectives, strategies for undertaking the various hedge transactions and method of assessing hedge effectiveness. Additionally, for hedges of forecasted transactions, the significant characteristics and expected terms of the forecasted transaction must be specifically identified, and it must be probable that each forecasted transaction will

occur. If it were deemed probable that the forecasted transaction would not occur, the gain or loss would be recognized in earnings.

PMI uses deliverable and non-deliverable forward foreign exchange contracts, foreign currency swaps and foreign currency options, collectively referred to as foreign exchange contracts ("foreign exchange contracts"), and interest rate contracts to mitigate its exposure to changes in exchange and interest rates from third-party and intercompany actual and forecasted transactions. Both foreign exchange contracts and interest rate contracts are collectively referred to as derivative contracts ("derivative contracts"). The primary currencies to which PMI is exposed include the Euro, Indonesian rupiah, Japanese yen, Mexican peso, Philippine peso, Russian ruble and Swiss franc. At December 31, 2019 and 2018, PMI had contracts with aggregate notional amounts of $24.1 billion and $27.4 billion, respectively. Of the $24.1 billion aggregate notional amount at December 31, 2019, $2.8 billion related to cash flow hedges, $9.9 billion related to hedges of net investments in foreign operations and $11.4 billion related to other derivatives that primarily offset currency exposures on intercompany financing. Of the $27.4 billion aggregate notional amount at December 31, 2018, $3.2 billion related to cash flow hedges, $10.1 billion related to hedges of net investments in foreign operations and $14.1 billion related to other derivatives that primarily offset currency exposures on intercompany financing.

The fair value of PMI's derivative exchange contracts included in the consolidated balance sheet as of December 31, 2019 and 2018, were as follows:

	Derivative Assets			Derivative Liabilities		
		Fair Value			Fair Value	
(in millions)	Balance Sheet Classification	2019	2018	Balance Sheet Classification	2019	2018
Derivative contracts designated as hedging instruments	Other current assets	**$ 319**	$ 54	Other accrued liabilities	**$ 23**	$ 47
	Other assets	**21**	99	Income taxes and other liabilities	**301**	525
Derivative contracts not designated as hedging instruments	Other current assets	**50**	67	Other accrued liabilities	**70**	46
	Other assets	**—**	—	Income taxes and other liabilities	**25**	13
Total derivatives		**$ 390**	$ 220		**$ 419**	$ 631

For the years ended December 31, 2019, 2018 and 2017, PMI's cash flow and net investment hedging instruments impacted the consolidated statements of earnings and comprehensive earnings as follows:

(pre-tax, in millions)	For the Year Ended December 31,							
	Amount of Gain/(Loss) Recognized in Other Comprehensive Earnings/ (Losses) on Derivatives			Statement of Earnings Classification of Gain/ (Loss) Reclassified from Other Comprehensive Earnings/(Losses) into Earnings	Amount of Gain/(Loss) Reclassified from Other Comprehensive Earnings/ (Losses) into Earnings		
	2019	2018	2017		2019	2018	2017
Derivatives in Cash Flow Hedging Relationship							
Derivative contracts	**$ (20)**	$ 28	$ (52)				
				Net revenues	**$ 22**	$ 18	$ 60
				Cost of sales	**1**	—	1
				Marketing, administration and research costs	**2**	6	(7)
				Interest expense, net	**(8)**	(1)	(41)
Derivatives in Net Investment Hedging Relationship							
Derivative contracts	**369**	324	(1,644)				
Total	**$ 349**	$ 352	$ (1,696)		**$ 17**	$ 23	$ 13

Cash Flow Hedges

PMI has entered into derivative contracts to hedge the foreign currency exchange and interest rate risks related to certain forecasted transactions. Gains and losses associated with qualifying cash flow hedge contracts are deferred as components of accumulated other comprehensive losses until the underlying hedged transactions are reported in PMI's consolidated statements of earnings. As of December 31, 2019, PMI has hedged forecasted transactions for periods not exceeding the next twelve months, with the exception of one derivative contract that expires in May 2024. The impact of these hedges is primarily included in operating cash flows on PMI's consolidated statements of cash flows.

Hedges of Net Investments in Foreign Operations

PMI designates certain foreign currency denominated debt and derivative contracts as net investment hedges, primarily of its Euro net assets. For the years ended December 31, 2019, 2018 and 2017, these hedges of net investments resulted in gains (losses), net of income taxes, of $470 million, $521 million and $(1,725) million, respectively, principally related to changes in the exchange rates between the Euro and U.S. dollar. These gains (losses) were reported as a component of accumulated other comprehensive losses within currency translation adjustments and were substantially offset by the losses and gains generated on the underlying assets. For the years ended December 31, 2019 and 2018, the gains for amounts excluded from the effectiveness testing recognized in earnings were $230 million and $260 million, respectively. These gains were accounted for in interest expense, net, on the consolidated statement of earnings. The premiums paid for, and settlements of, net investment hedges are included in investing cash flows on PMI's consolidated statements of cash flows.

Other Derivatives

PMI has entered into derivative contracts to hedge the foreign currency exchange and interest rate risks related to intercompany loans between certain subsidiaries, and third-party loans. While effective as economic hedges, no hedge accounting is applied for these contracts; therefore, the unrealized gains (losses) relating to these contracts are reported in marketing, administration and research costs in PMI's consolidated statements of earnings. For the years ended December 31, 2019, 2018 and 2017, the gains (losses) from contracts for which PMI did not apply hedge accounting were $(57) million, $405 million and $382 million, respectively. The gains (losses) from these contracts substantially offset the losses and gains generated by the underlying intercompany and third-party loans being hedged.

As a result, for the years ended December 31, 2019, 2018 and 2017, these items impacted the consolidated statement of earnings as follows:

(pre-tax, in millions)

Derivatives not Designated as Hedging Instruments	**Statement of Earnings Classification of Gain/ (Loss)**	**Amount of Gain/(Loss) Recognized in Earnings**		
		2019	**2018**	**2017**
Derivative contracts				
	Interest expense, net	**$ 94**	$ 62	$ (60)
Total		**$ 94**	$ 62	$ (60)

Qualifying Hedging Activities Reported in Accumulated Other Comprehensive Losses

Derivative gains or losses reported in accumulated other comprehensive losses are a result of qualifying hedging activity. Transfers of these gains or losses to earnings are offset by the corresponding gains or losses on the underlying hedged item. Hedging activity affected accumulated other comprehensive losses, net of income taxes, as follows:

(in millions)	**For the Years Ended December 31,**		
	2019	**2018**	**2017**
Gain as of January 1,	**$ 35**	$ 42	$ 97
Derivative (gains)/losses transferred to earnings	**(14)**	(31)	(11)
Change in fair value	**(18)**	24	(44)

Gain as of December 31,	**$ 3**	$ 35	$ 42

At December 31, 2019, PMI expects $22 million of derivative gains that are included in accumulated other comprehensive losses to be reclassified to the consolidated statement of earnings within the next 12 months. These gains are expected to be substantially offset by the statement of earnings impact of the respective hedged transactions.

Contingent Features

PMI's derivative instruments do not contain contingent features.

Credit Exposure and Credit Risk

PMI is exposed to credit loss in the event of non-performance by counterparties. While PMI does not anticipate non-performance, its risk is limited to the fair value of the financial instruments less any cash collateral received or pledged. PMI actively monitors its exposure to credit risk through the use of credit approvals and credit limits and by selecting and continuously monitoring a diverse group of major international banks and financial institutions as counterparties.

Fair Value

See Note 16. *Fair Value Measurements* and Note 19. *Balance Sheet Offsetting* for additional discussion of derivative financial instruments.

Note 16.

Fair Value Measurements:

The authoritative guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The guidance also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of input that may be used to measure fair value, which are as follows:

Level 1 — Quoted prices in active markets for identical assets or liabilities;

Level 2 — Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Equity Securities

The fair value of PMI's equity securities, which are determined by using quoted prices in active markets, have been classified within Level 1.

Derivative Financial Instruments

PMI assesses the fair value of its foreign exchange contracts and interest rate contracts using standard valuation models that use, as their basis, readily observable market inputs. The fair value of PMI's foreign exchange forward contracts is determined by using the prevailing foreign exchange spot rates and interest rate differentials, and the respective maturity dates of the instruments. The fair value of PMI's currency options is determined by using a Black-Scholes methodology based on foreign exchange spot rates and interest rate differentials, currency volatilities and maturity dates. PMI's derivative financial instruments have been classified within Level 2 at December 31, 2019 and 2018. See Note 15. *Financial Instruments* for additional discussion of derivative financial instruments.

Pension Plan Assets

The fair value of pension plan assets, determined by using readily available quoted market prices in active markets, has been classified within Level 1 of the fair value hierarchy at December 31, 2019 and 2018. The fair value of pension plan assets, determined by using quoted prices in markets that are not active, has been classified within Level 2 at December 31, 2019 and 2018. See Note 13. *Benefit Plans* for additional discussion of pension plan assets.

Debt

The fair value of PMI's outstanding debt, which is utilized solely for disclosure purposes, is determined using quotes and market interest rates currently available to PMI for issuances of debt with similar terms and remaining maturities. The aggregate carrying value of PMI's debt, excluding short-term borrowings and $56 million of finance leases, was $30,651 million at December 31, 2019. The aggregate carrying value of PMI's debt, excluding short-term borrowings and $33 million of finance leases, was $30,996 million at December 31,

2018. The fair value of PMI's outstanding debt, excluding the aforementioned short-term borrowings and finance leases, was classified within Level 1 and Level 2 at December 31, 2019 and 2018.

The aggregate fair values of PMI's investments in equity securities, derivative financial instruments, pension plan assets and PMI's debt as of December 31, 2019, were as follows:

(in millions)	Fair Value at December 31, 2019	Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Equity securities [1]	$ 332	$ 332	$ —	$ —
Derivative contracts	390	$ —	390	—
Pension plan assets	7,619	6,059	1,560	—
Total assets in fair value hierarchy	$ 8,341	$ 6,391	$ 1,950	$ —
Pension plan assets measured at net asset value [2]	309			
Total assets	$ 8,650			
Liabilities:				
Debt	$ 32,988	$ 32,821	$ 167	$ —
Derivative contracts	419	—	419	—
Total liabilities	$ 33,407	$ 32,821	$ 586	$ —

[1] Unrealized pre-tax gain of $44 million ($35 million net of tax) on equity securities was recorded in the consolidated statement of earnings for the year ended December 31, 2019.

[2] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in these tables are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

The aggregate fair values of PMI's investments in equity securities, derivative financial instruments, pension plan assets and PMI's debt as of December 31, 2018 , were as follows:

(in millions)	Fair Value at December 31, 2018	Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Equity securities	$ 288	$ 288	$ —	$ —
Derivative contracts	220	—	220	—
Pension plan assets	6,600	4,631	1,969	—
Total assets in fair value hierarchy	$ 7,108	$ 4,919	$ 2,189	$ —
Pension plan assets measured at net asset value [1]	288			
Total assets	$ 7,396			
Liabilities:				
Debt	$ 31,162	$ 30,997	$ 165	$ —
Derivative contracts	631	—	631	—
Total liabilities	$ 31,793	$ 30,997	$ 796	$ —

[1] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in these tables are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Note 17.

Accumulated Other Comprehensive Losses:

PMI's accumulated other comprehensive losses, net of taxes, consisted of the following:

(Losses) Earnings (in millions)	At December 31, 2019	2018	2017
Currency translation adjustments	**$ (5,537)**	$ (6,500)	$ (5,761)
Pension and other benefits	**(3,829)**	(3,646)	(2,816)
Derivatives accounted for as hedges	**3**	35	42
Total accumulated other comprehensive losses	**$ (9,363)**	$ (10,111)	$ (8,535)

Reclassifications from Other Comprehensive Earnings

The movements in accumulated other comprehensive losses and the related tax impact, for each of the components above, that are due to current period activity and reclassifications to the income statement, including those related to the deconsolidation of RBH, are shown on the consolidated statements of comprehensive earnings for the years ended December 31, 2019, 2018, and 2017. For the year ended 2017, $2 million of net currency translation adjustment gains/(losses) were transferred from other comprehensive earnings to marketing, administration and research costs in the consolidated statements of earnings, respectively, upon liquidation of subsidiaries. For additional information, see Note 13. *Benefit Plans* for disclosures related to PMI's pension and other benefits, Note 15. *Financial Instruments* for disclosures related to derivative financial instruments and Note 22. *Deconsolidation of RBH* for disclosures related to the deconsolidation of RBH.

Note 18.

Contingencies:

Tobacco-Related Litigation

Legal proceedings covering a wide range of matters are pending or threatened against us, and/or our subsidiaries, and/or our indemnitees in various jurisdictions. Our indemnitees include distributors, licensees, and others that have been named as parties in certain cases and that we have agreed to defend, as well as to pay costs and some or all of judgments, if any, that may be entered against them. Pursuant to the terms of the Distribution Agreement between Altria Group, Inc. ("Altria") and PMI, PMI will indemnify Altria and Philip Morris USA Inc. ("PM USA"), a U.S. tobacco subsidiary of Altria, for tobacco product claims based in substantial part on products manufactured by PMI or contract manufactured for PMI by PM USA, and PM USA will indemnify PMI for tobacco product claims based in substantial part on products manufactured by PM USA, excluding tobacco products contract manufactured for PMI.

It is possible that there could be adverse developments in pending cases against us and our subsidiaries. An unfavorable outcome or settlement of pending tobacco-related litigation could encourage the commencement of additional litigation.

Damages claimed in some of the tobacco-related litigation are significant and, in certain cases in Brazil, Canada and Nigeria, range into the billions of U.S. dollars. The variability in pleadings in multiple jurisdictions, together with the actual experience of management in litigating claims, demonstrate that the monetary relief that may be specified in a lawsuit bears little relevance to the ultimate outcome. Much of the tobacco-related litigation is in its early stages, and litigation is subject to uncertainty. However, as discussed below, we have to date been largely successful in defending tobacco-related litigation.

We and our subsidiaries record provisions in the consolidated financial statements for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. At the present time, except as stated otherwise in this Note 18. *Contingencies,* while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available to it (i) management has not concluded that it is probable that a loss has been incurred in any of the pending tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any. Legal defense costs are expensed as incurred.

It is possible that our consolidated results of operations, cash flows or financial position could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. Nevertheless, although litigation is subject to uncertainty, we and each of our subsidiaries named as a defendant believe, and each has been so advised by counsel handling the respective cases, that we have valid defenses to the litigation pending against us, as well as valid bases for appeal of adverse verdicts. All such cases are, and will continue to be, vigorously defended. However, we and our subsidiaries may enter into settlement discussions in particular cases if we believe it is in our best interests to do so.

CCAA Proceedings and Stay of Tobacco-Related Cases Pending in Canada

As a result of the Court of Appeal of Quebec's decision in both the *Létourneau* and *Blais* cases described below, our subsidiary, Rothmans, Benson & Hedges Inc. ("RBH"), and the other defendants, JTI Macdonald Corp., and Imperial Tobacco Canada Limited, sought protection in the Ontario Superior Court of Justice under the Companies' Creditors Arrangement Act ("CCAA") on March 22, March 8, and March 12, respectively. CCAA is a Canadian federal law that permits a Canadian business to restructure its affairs while carrying on its business in the ordinary course. The initial CCAA order made by the Ontario Superior Court on March 22, 2019 authorizes RBH to pay all expenses incurred in carrying on its business in the ordinary course after the CCAA filing, including obligations to employees, vendors, and suppliers. As further described in Note 22. *Deconsolidation of RBH*, RBH is now deconsolidated from our consolidated financial statements. As part of the CCAA proceedings, there is currently a comprehensive stay up to and including March 12, 2020 of all tobacco-related litigation pending in Canada against RBH and the other

defendants, including PMI and our indemnitees (PM USA and Altria), namely, the smoking and health class actions filed in various Canadian provinces and health care cost recovery actions. These proceedings are presented below under the caption "*Stayed Litigation — Canada*." Ernst & Young Inc. has been appointed as monitor of RBH in the CCAA proceedings. In accordance with the CCAA process, as the parties work towards a plan of arrangement or compromise in a confidential mediation, it is anticipated that the court will set additional hearings and further extend the stay of proceedings. On April 17, 2019, the Ontario Superior Court ruled that RBH and the other defendants will not be allowed to file an application to the Supreme Court of Canada for leave to appeal the Court of Appeal's decision in the *Létourneau* and the *Blais* cases so long as the comprehensive stay of all tobacco-related litigation in Canada remains in effect and that the time period to file the application would be extended by the stay period. While RBH believes that the findings of liability and damages in both *Létourneau* and the *Blais* cases were incorrect, the CCAA proceedings will provide a forum for RBH to seek resolution through a plan of arrangement or compromise of all tobacco-related

litigation pending in Canada. It is not possible to predict the resolution of the underlying legal proceedings or the length of the CCAA process.

Stayed Litigation — Canada

Smoking and Health Litigation — Canada

In the first class action pending in Canada, *Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI-Macdonald Corp., Quebec Superior Court, Canada*, filed in November 1998, RBH and other Canadian manufacturers (Imperial Tobacco Canada Ltd. and JTI-Macdonald Corp.) are defendants. The plaintiffs, an anti-smoking organization and an individual smoker, sought compensatory and punitive damages for each member of the class who allegedly suffers from certain smoking-related diseases. The class was certified in 2005. The trial court issued its judgment on May 27, 2015. The trial court found RBH and two other Canadian manufacturers liable and found that the class members' compensatory damages totaled approximately CAD 15.5 billion, including pre-judgment interest (approximately $11.7 billion). The trial court awarded compensatory damages on a joint and several liability basis, allocating 20% to our subsidiary (approximately CAD 3.1 billion, including pre-judgment interest (approximately $2.34 billion)). In addition, the trial court awarded CAD 90,000 (approximately $67,980) in punitive damages, allocating CAD 30,000 (approximately $22,660) to RBH. The trial court estimated the disease class at 99,957 members. RBH appealed to the Court of Appeal of Quebec. In October 2015, the Court of Appeal ordered RBH to furnish security totaling CAD 226 million (approximately $170.7 million) to cover both the *Létourneau* and *Blais* cases, which RBH has paid in installments through March 2017. The Court of Appeal ordered Imperial Tobacco Canada Ltd. to furnish security totaling CAD 758 million (approximately $573 million) in installments through June 2017. JTI Macdonald Corp. was not required to furnish security in accordance with plaintiffs' motion. The Court of Appeal ordered that the security is payable upon a final judgment of the Court of Appeal affirming the trial court's judgment or upon further order of the Court of Appeal. On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's findings of liability and the compensatory and punitive damages award while reducing the total amount of compensatory damages to approximately CAD 13.5 billion including interest (approximately $10.2 billion) due to the trial court's error in the calculation of interest. The compensatory damages award is on a joint and several basis with an allocation of 20% to RBH (approximately CAD 2.7 billion, including pre-judgment interest (approximately $2.04 billion)). The Court of Appeal upheld the trial court's findings that defendants violated the Civil Code of Quebec, the Quebec Charter of Human Rights and Freedoms, and the Quebec Consumer Protection Act by failing to warn adequately of the dangers of smoking and by conspiring to prevent consumers from learning of the dangers of smoking. The Court of Appeal further held that the plaintiffs either need not prove, or had adequately proven, that these faults were a cause of the class members' injuries. In accordance with the judgment, defendants are required to deposit their respective portions of the damages awarded in both the *Létourneau* case described below and the *Blais* case, approximately CAD 1.1 billion (approximately $831 million), into trust accounts within 60 days. RBH's share of the deposit is approximately CAD 257 million (approximately $194.1 million). PMI recorded a pre-tax charge of $194 million in its consolidated results, representing $142 million net of tax, as tobacco litigation-related expense, in the first quarter of 2019. The charge reflects PMI's assessment of the portion of the judgment that represents probable and estimable loss prior to the deconsolidation of RBH and corresponds to the trust account deposit required by the judgment.

In the second class action pending in Canada, *Cecilia Létourneau v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI-Macdonald Corp., Quebec Superior Court, Canada,* filed in September 1998, RBH and other Canadian manufacturers (Imperial Tobacco Canada Ltd. and JTI-Macdonald Corp.) are defendants. The plaintiff, an individual smoker, sought compensatory and punitive damages for each member of the class who is deemed addicted to smoking. The class was certified in 2005. The trial court issued its judgment on May 27, 2015. The trial court found RBH and two other Canadian manufacturers liable and awarded a total of CAD 131 million (approximately $99 million) in punitive damages, allocating CAD 46 million (approximately $34.7 million) to RBH. The trial court estimated the size of the addiction class at 918,000 members but declined to award compensatory damages to the addiction class because the evidence did not establish the claims with sufficient accuracy. The trial court found that a claims process to allocate the awarded punitive damages to individual class members would be too expensive and difficult to administer. On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's findings of liability and the total amount of punitive damages awarded allocating CAD 57 million including interest (approximately $43.1 million) to RBH. See the *Blais* description above and Note 22. *Deconsolidation of RBH* below for further detail concerning the security order pertaining to both *Létourneau* and *Blais* cases and the impact of the decision on PMI's financial statements.

RBH and PMI believe the findings of liability and damages in both *Létourneau* and the *Blais* cases were incorrect and in contravention of applicable law on several grounds including the following: (i) defendants had no obligation to warn class members who knew, or should have known, of the risks of smoking; (ii) defendants cannot be liable to class members who would have smoked regardless of what warnings were given; and (iii) defendants cannot be liable to all class members given the individual differences between class members.

In the third class action pending in Canada, *Kunta v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Winnipeg, Canada*, filed June 12, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic obstructive pulmonary disease ("COPD"),

severe asthma, and mild reversible lung disease resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products.

In the fourth class action pending in Canada, *Adams v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Saskatchewan, Canada*, filed July 10, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, emphysema, heart disease, or cancer, as well as restitution of profits.

In the fifth class action pending in Canada, *Semple v. Canadian Tobacco Manufacturers' Council, et al., The Supreme Court (trial court), Nova Scotia, Canada*, filed June 18, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and COPD resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products.

In the sixth class action pending in Canada, *Dorion v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Alberta, Canada,* filed June 15, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic bronchitis and severe sinus infections resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products. To date, we, our subsidiaries, and our indemnitees have not been properly served with the complaint.

In the seventh class action pending in Canada, *McDermid v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and heart disease resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from heart disease allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed.

In the eighth class action pending in Canada, *Bourassa v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, the heir to a deceased smoker, alleges that the decedent was addicted to tobacco products and suffered from emphysema resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from chronic respiratory diseases allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed. In December 2014, plaintiff filed an amended statement of claim.

In the ninth class action pending in Canada, *Suzanne Jacklin v. Canadian Tobacco Manufacturers' Council, et al., Ontario Superior Court of Justice,* filed June 20, 2012, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, heart disease, or cancer, as well as restitution of profits.

Health Care Cost Recovery Litigation — Canada

In the first health care cost recovery case pending in Canada, *Her Majesty the Queen in Right of British Columbia v. Imperial Tobacco Limited, et al., Supreme Court, British Columbia, Vancouver Registry, Canada,* filed January 24, 2001, we, RBH, our indemnitee (PM USA), and other members of the industry are defendants. The plaintiff, the government of the province of British Columbia, brought a claim based upon legislation enacted by the province

authorizing the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, resulting from a "tobacco related wrong."

In the second health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of New Brunswick v. Rothmans Inc., et al., Court of Queen's Bench of New Brunswick, Trial Court, New Brunswick, Fredericton, Canada,* filed March 13, 2008, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of New Brunswick based on legislation enacted in the province. This legislation is similar to the law introduced in British Columbia that authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the third health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of Ontario v. Rothmans Inc., et al., Ontario Superior Court of Justice, Toronto, Canada*, filed September 29, 2009, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Ontario based on legislation enacted in the province. This legislation is similar to the laws introduced in British Columbia and New Brunswick that authorize the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the fourth health care cost recovery case filed in Canada, *Attorney General of Newfoundland and Labrador v. Rothmans Inc., et al., Supreme Court of Newfoundland and Labrador, St. Johns, Canada*, filed February 8, 2011, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Newfoundland and Labrador based on legislation enacted in the province that is similar to the laws introduced in British Columbia, New Brunswick and Ontario. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the fifth health care cost recovery case filed in Canada, *Attorney General of Quebec v. Imperial Tobacco Limited, et al., Superior Court of Quebec, Canada*, filed June 8, 2012, we, RBH, our indemnitee (PM USA), and other members of the industry are defendants. The claim was filed by the government of the province of Quebec based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the sixth health care cost recovery case filed in Canada, *Her Majesty in Right of Alberta v. Altria Group, Inc., et al., Supreme Court of Queen's Bench Alberta, Canada*, filed June 8, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Alberta based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the seventh health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Manitoba v. Rothmans, Benson & Hedges, Inc., et al., The Queen's Bench, Winnipeg Judicial Centre, Canada*, filed May 31, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Manitoba based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the eighth health care cost recovery case filed in Canada, *The Government of Saskatchewan v. Rothmans, Benson & Hedges Inc., et al., Queen's Bench, Judicial Centre of Saskatchewan, Canada*, filed June 8, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Saskatchewan based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the ninth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Prince Edward Island v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Prince Edward Island (General Section), Canada*, filed September 10, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Prince Edward Island based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the tenth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Nova Scotia v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Nova Scotia, Canada*, filed January 2, 2015, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Nova Scotia based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action

against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

The table below lists the number of tobacco-related cases pertaining to combustible products pending against us and/or our subsidiaries or indemnitees as of February 3, 2020, February 4, 2019 and February 9, 2018:[1]

Type of Case	Number of Cases Pending as of February 3, 2020	Number of Cases Pending as of February 4, 2019	Number of Cases Pending as of February 9, 2018
Individual Smoking and Health Cases	50	55	57
Smoking and Health Class Actions	10	10	11
Health Care Cost Recovery Actions	17	16	16
Label-Related Class Actions	—	1	1
Individual Label-Related Cases	5	7	1
Public Civil Actions	2	2	2

Since 1995, when the first tobacco-related litigation was filed against a PMI entity, 501 Smoking and Health, Label-Related, Health Care Cost Recovery, and Public Civil Actions in which we and/or one of our subsidiaries and/or indemnitees were a defendant have been terminated in our favor. Thirteen cases have had decisions in favor of plaintiffs. Nine of these cases have subsequently reached final resolution in our favor and four remain on appeal.

The table below lists the verdict and significant post-trial developments in the four pending cases where a verdict was returned in favor of the plaintiff:

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
February 2004	Brazil/The Smoker Health Defense Association	Class Action	The Civil Court of São Paulo found defendants liable without hearing evidence. In April 2004, the court awarded "moral damages" of R$1,000 (approximately $233) per smoker per full year of smoking plus interest at the rate of 1% per month, as of the date of the ruling. The court did not assess actual damages, which were to be assessed in a second phase of the case. The size of the class was not defined in the ruling.	Defendants appealed to the São Paulo Court of Appeals, which annulled the ruling in November 2008, finding that the trial court had inappropriately ruled without hearing evidence and returned the case to the trial court for further proceedings. In May 2011, the trial court dismissed the claim. In March 2017, plaintiff filed an *en banc* appeal to the Superior Court of Justice. In addition, the defendants filed a constitutional appeal to the Federal Supreme Tribunal on the basis that plaintiff did not have standing to bring the lawsuit. Both appeals are still pending.

[1] Includes cases pending in Canada.

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
May 27, 2015	Canada/Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec ruled in favor of the *Blais* class on liability and found the class members' compensatory damages totaled approximately CAD 15.5 billion (approximately $11.7 billion), including pre-judgment interest. The trial court awarded compensatory damages on a joint and several liability basis, allocating 20% to our subsidiary (approximately CAD 3.1 billion including pre-judgment interest (approximately $2.34 billion)). The trial court awarded CAD 90,000 (approximately $67,980) in punitive damages, allocating CAD 30,000 (approximately $22,660) to our subsidiary. The trial court ordered defendants to pay CAD 1 billion (approximately $755.3 million) of the compensatory damage award, CAD 200 million (approximately $151.1 million) of which is our subsidiary's portion, into a trust within 60 days.	In June 2015, RBH commenced the appellate process with the Court of Appeal of Quebec. On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's decision. (See "*Stayed Litigation — Canada*" for further detail.)

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
May 27, 2015	Canada/Cecilia Létourneau	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec ruled in favor of the *Létourneau* class on liability and awarded a total of CAD 131 million (approximately $99 million) in punitive damages, allocating CAD 46 million (approximately $34.7 million) to RBH. The trial court ordered defendants to pay the full punitive damage award into a trust within 60 days. The court did not order the payment of compensatory damages.	In June 2015, RBH commenced the appellate process with the Court of Appeal of Quebec. On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's decision. (See "*Stayed Litigation — Canada*" for further detail.)

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
August 5, 2016	Argentina/Hugo Lespada	Individual Action	On August 5, 2016, the Civil Court No. 14 - Mar del Plata, issued a verdict in favor of plaintiff, an individual smoker, and awarded him ARS 110,000 (approximately $1,825), plus interest, in compensatory and moral damages. The trial court found that our subsidiary failed to warn plaintiff of the risk of becoming addicted to cigarettes.	On August 23, 2016, our subsidiary filed its notice of appeal. On October 31, 2017, the Civil and Commercial Court of Appeals of Mar del Plata ruled that plaintiff's claim was barred by the statute of limitations and it reversed the trial court's decision. On November 28, 2017, plaintiff filed an extraordinary appeal of the reversal of the trial court's decision to the Supreme Court of the Province of Buenos Aires.

Pending claims related to tobacco products generally fall within the following categories:

Smoking and Health Litigation: These cases primarily allege personal injury and are brought by individual plaintiffs or on behalf of a class or purported class of individual plaintiffs. Plaintiffs' allegations of liability in these cases are based on various theories of recovery, including negligence, gross negligence, strict liability, fraud, misrepresentation, design defect, failure to warn, breach of express and implied warranties, violations of deceptive trade practice laws and consumer protection statutes. Plaintiffs in these cases seek various forms of relief, including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include licit activity, failure to state a claim, lack of defect, lack of proximate cause, assumption of the risk, contributory negligence, and statute of limitations.

As of February 3, 2020, there were a number of smoking and health cases pending against us, our subsidiaries or indemnitees, as follows:

- 50 cases brought by individual plaintiffs in Argentina (31), Brazil (5), Canada (2), Chile (5), Costa Rica (1), Italy (1), the Philippines (1), Poland (2), Turkey (1) and Scotland (1), compared with 55 such cases on February 4, 2019, and 57 cases on February 9, 2018; and

- 10 cases brought on behalf of classes of individual plaintiffs in Brazil (1) and Canada (9), compared with 10 such cases on February 4, 2019 and 11 such cases on February 9, 2018.

The class actions pending in Canada are described above under the caption "*Smoking and Health Litigation — Canada.*"

In the class action pending in Brazil, *The Smoker Health Defense Association (ADESF) v. Souza Cruz, S.A. and Philip Morris Marketing, S.A., Nineteenth Lower Civil Court of the Central Courts of the Judiciary District of São Paulo, Brazil*, filed July 25, 1995, our subsidiary and another member of the industry are defendants. The plaintiff, a consumer organization, is seeking damages for all addicted smokers and former smokers, and injunctive relief. In 2004, the trial court found defendants liable without hearing evidence and awarded "moral damages" of R$1,000 (approximately $233) per smoker per full year of smoking plus interest at the rate of 1% per month, as of the date of the ruling. The court did not award actual damages, which were to be assessed in the second phase of the case. The size of the class was not estimated. Defendants appealed to the São Paulo Court of Appeals, which annulled the ruling in November 2008, finding that the trial court had inappropriately ruled without hearing evidence and returned the case to the trial court for further proceedings. In May 2011, the trial court dismissed the claim. In February 2015, the appellate court unanimously dismissed plaintiff's appeal. In September 2015, plaintiff appealed to the Superior Court of Justice. In February 2017, the Chief Justice of the Superior Court of Justice denied plaintiff's appeal. In March 2017, plaintiff filed an *en banc* appeal to the Superior Court of Justice. In addition, the defendants filed a constitutional appeal to the Federal Supreme Tribunal on the basis that plaintiff did not have standing to bring the lawsuit. Both appeals are still pending.

Health Care Cost Recovery Litigation: These cases, brought by governmental and non-governmental plaintiffs, seek reimbursement of health care cost expenditures allegedly caused by tobacco products. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including unjust enrichment, negligence, negligent design, strict liability, breach of express and implied warranties, violation of a voluntary undertaking or special duty, fraud, negligent misrepresentation, conspiracy, public nuisance, defective product, failure to warn, sale of cigarettes to minors, and claims under statutes governing competition and deceptive trade practices. Plaintiffs in these cases seek various forms of relief including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include lack of proximate cause, remoteness of injury, failure to state a claim, adequate remedy at law, "unclean hands" (namely, that plaintiffs cannot obtain equitable relief because they participated in, and benefited from, the sale of cigarettes), and statute of limitations.

As of February 3, 2020, there were 17 health care cost recovery cases pending against us, our subsidiaries or indemnitees in Brazil (1), Canada (10), Korea (1) and Nigeria (5), compared with 16 such cases on February 4, 2019 and 16 such cases on February 9, 2018.

The health care cost recovery actions pending in Canada are described above under the caption "*Health Care Cost Recovery Litigation — Canada.*"

In the health care cost recovery case in Brazil, *The Attorney General of Brazil v. Souza Cruz Ltda., et al., Federal Trial Court, Porto Alegre, Rio Grande do Sul, Brazil*, filed May 21, 2019, we, our subsidiaries, and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past five years, payment of anticipated costs of treating future alleged smoking-related diseases, and moral damages. Our subsidiaries were served with the complaint. A challenge to the service of PMI as improper is pending.

In the first health care cost recovery case in Nigeria, *The Attorney General of Lagos State v. British American Tobacco (Nigeria) Limited, et al., High Court of Lagos State, Lagos, Nigeria,* filed March 13, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of making challenges to service and the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the second health care cost recovery case in Nigeria, *The Attorney General of Kano State v. British American Tobacco (Nigeria) Limited, et al., High Court of Kano State, Kano, Nigeria,* filed May 9, 2007, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of making challenges to service and the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the third health care cost recovery case in Nigeria, *The Attorney General of Gombe State v. British American Tobacco (Nigeria) Limited, et al., High Court of Gombe State, Gombe, Nigeria,* filed October 17, 2008, we and other members of the industry are defendants. Plaintiff

seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In February 2011, the court ruled that the plaintiff had not complied with the procedural steps necessary to serve us. As a result of this ruling, plaintiff must re-serve its claim. We have not yet been re-served.

In the fourth health care cost recovery case in Nigeria, *The Attorney General of Oyo State, et al., v. British American Tobacco (Nigeria) Limited, et al., High Court of Oyo State, Ibadan, Nigeria,* filed May 25, 2007, we and other members of the industry are defendants. Plaintiffs seek reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We challenged service as improper. In June 2010, the court ruled that plaintiffs did not have leave to serve the writ of summons on the defendants and that they must re-serve the writ. We have not yet been re-served.

In the fifth health care cost recovery case in Nigeria, *The Attorney General of Ogun State v. British American Tobacco (Nigeria) Limited, et al., High Court of Ogun State, Abeokuta, Nigeria*, filed February 26, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In May 2010, the trial court rejected our service objections. We have appealed.

In the health care cost recovery case in Korea, the *National Health Insurance Service v. KT&G, et. al.,* filed April 14, 2014, our subsidiary and other Korean manufacturers are defendants. Plaintiff alleges that defendants concealed the health hazards of smoking, marketed to youth, added ingredients to make their products more harmful and addictive, and misled consumers into believing that *Lights* cigarettes are safer than regular cigarettes. The National Health Insurance Service seeks to recover damages allegedly incurred in treating 3,484 patients with small cell lung cancer, squamous cell lung cancer, and squamous cell laryngeal cancer from 2003 to 2012. The case is now in the evidentiary phase.

Label-Related Cases: These cases, brought by individual plaintiffs, or on behalf of a class or purported class of individual plaintiffs, allege that the use of the descriptor “Lights” or other alleged misrepresentations or omissions of labeling information constitute fraudulent and misleading conduct. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including misrepresentation, deception, and breach of consumer protection laws. Plaintiffs seek various forms of relief including restitution, injunctive relief, and compensatory and other damages. Defenses raised include lack of causation, lack of reliance, assumption of the risk, and statute of limitations.

As of February 3, 2020, there were 5 label-related cases brought by individual plaintiffs in Italy (1) and Chile (4) pending against our subsidiaries, compared with 7 such case on February 4, 2019, and 1 such case on February 9, 2018.

An individual plaintiff filed a purported class action certification motion, *Aharon Ringer v. Philip Morris Ltd. and Globrands Ltd.,* on July 18, 2017, in the Central District Court of Israel. Our Israeli affiliate and an Israeli importer and distributor for other multinational tobacco companies were defendants. Plaintiff sought to represent a class of smokers in Israel who have purchased cigarettes imported by defendants since July 18, 2010. Plaintiff estimated the class size to be 7,000,000 smokers. Plaintiff alleged that defendants misled consumers by not disclosing sufficient information about carbon monoxide, tar, and nicotine yields of, and tobacco contained in, the imported cigarettes. Plaintiff sought various forms of relief, including an order for defendants to label cigarette packs in accordance with plaintiff’s demands, and damages for misleading consumers, breach of autonomy and unjust enrichment. In September 2019, plaintiff voluntarily withdrew the class certification motion, and the trial court dismissed the case with prejudice.

Public Civil Actions: Claims have been filed either by an individual, or a public or private entity, seeking to protect collective or individual rights, such as the right to health, the right to information or the right to safety. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including product defect, concealment, and misrepresentation. Plaintiffs in these cases seek various forms of relief including injunctive relief such as banning cigarettes, descriptors, smoking in certain places and advertising, as well as implementing communication campaigns and reimbursement of medical expenses incurred by public or private institutions.

As of February 3, 2020, there were 2 public civil actions pending against our subsidiaries in Argentina (1) and Venezuela (1), compared with 2 such cases on February 4, 2019, and 2 such cases on February 9, 2018.

In the public civil action in Argentina, *Asociación Argentina de Derecho de Danos v. Massalin Particulares S.A., et al., Civil Court of Buenos Aires, Argentina,* filed February 26, 2007, our subsidiary and another member of the industry are defendants. The plaintiff, a consumer association, seeks the establishment of a relief fund for reimbursement of medical costs associated with diseases allegedly caused by smoking. Our subsidiary filed its answer in September 2007. In March 2010, the case file was transferred to the Federal Court on Administrative Matters after the Civil Court granted plaintiff's request to add the national government as a co-plaintiff in the case. The case is currently awaiting a court decision on the merits.

In the public civil action in Venezuela, *Federation of Consumers and Users Associations ("FEVACU"), et al. v. National Assembly of Venezuela and the Venezuelan Ministry of Health, Constitutional Chamber of the Venezuelan Supreme Court*, filed April 29, 2008, we were not named as a defendant, but the plaintiffs published a notice pursuant to court order, notifying all interested parties to appear in the case. In January 2009, our subsidiary appeared in the case in response to this notice. The plaintiffs purport to represent the right to health of the citizens of Venezuela and claim that the government failed to protect adequately its citizens' right to health. The claim asks the court to order the government to enact stricter regulations on the manufacture and sale of tobacco products. In addition, the plaintiffs ask the court to order companies involved in the tobacco industry to allocate a percentage of their "sales or benefits" to establish a fund to pay for the health care costs of treating smoking-related diseases. In October 2008, the court ruled that plaintiffs have standing to file the claim and that the claim meets the threshold admissibility requirements. In December 2012, the court admitted our subsidiary and BAT's subsidiary as interested third parties. In February 2013, our subsidiary answered the complaint.

Reduced-Risk Products

In Colombia, an individual filed a purported class action, *Ana Ferrero Rebolledo vs. Philip Morris Colombia S.A., et al.*, in April 2019 against our subsidiaries with the Civil Court of Bogota related to the marketing of our Platform 1 product. Plaintiff alleges that our subsidiaries advertise the product in contravention of law and in a manner that misleads consumers by portraying the product in a positive light, and further asserts that the Platform 1 vapor contains many toxic compounds, creates a high level of dependence, and has damaging second-hand effects. Plaintiff seeks injunctive relief and damages on her behalf and on a behalf of two classes (class 1 - all Platform 1 consumers in Colombia who seek damages for the purchase price of the product and personal injuries related to the alleged addiction, and class 2 - all residents of the neighborhood where the advertising allegedly took place who seek damages for exposure to the alleged illegal advertising). Our subsidiaries answered the complaint in January 2020.

Other Litigation

The Department of Special Investigations of the government of Thailand ("DSI") conducted an investigation into alleged underpayment by our subsidiary, Philip Morris (Thailand) Limited ("PM Thailand"), of customs duties and excise taxes relating to imports from the Philippines covering the period 2003-2007. On January 18, 2016, the Public Prosecutor filed charges against our subsidiary and seven former and current employees in the Bangkok Criminal Court alleging that PM Thailand and the individual defendants jointly and with the intention to defraud the Thai government, under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries of cigarettes from the Philippines during the period of July 2003 to June 2006. The government is seeking a fine of approximately THB 80.8 billion (approximately $2.58 billion). In May 2017, Thailand enacted a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and other Thai governmental agencies. Trial in the case began in November 2017 and concluded in September 2019. In November 2019, the trial court found our subsidiary guilty of under-declaration of the prices and imposed a fine of approximately THB 1.2 billion (approximately $38.4 million). The trial court dismissed all charges against the individual defendants. In December 2019, as required by the Thai law, our subsidiary paid the fine. This payment is included in other assets on the consolidated balance sheets and in cash used in operating activities in the consolidated statements of cash flows. Our subsidiary will appeal the trial court's decision. If our subsidiary ultimately prevails on appeal, then Thailand will be required to return this payment to our subsidiary.

The DSI also conducted an investigation into alleged underpayment by PM Thailand of customs duties and excise taxes relating to imports from Indonesia covering the period 2000-2003. On January 26, 2017, the Public Prosecutor filed charges against PM Thailand and its former Thai employee in the Bangkok Criminal Court alleging that PM Thailand and its former employee jointly and with the intention to defraud the Thai government under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries during the period from January 2002 to July 2003. The government is seeking a fine of approximately THB 19.8 billion (approximately $633 million). In May 2017, Thailand enacted a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law, and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and a Thai court. Trial in the case began in November 2018 and concluded in December 2019. The case is awaiting a court decision in March 2020.

The South Korean Board of Audit and Inspection (“BAI”) conducted an audit of certain Korean government agencies and the tobacco industry into whether inventory movements ahead of the January 1, 2015 increase of cigarette-related taxes by tobacco companies, including Philip Morris Korea Inc. ("PM Korea"), our South Korean affiliate, were in compliance with South Korean tax laws. In November 2016, the tax authorities completed their audit and assessed allegedly underpaid taxes and penalties. In order to avoid nonpayment financial costs, PM Korea paid approximately KRW 272 billion (approximately $227 million), of which KRW 100 billion (approximately $83.5 million) was paid in 2016 and KRW 172 billion (approximately $143.7 million) was paid in the first quarter of 2017. These amounts are included in other assets in the consolidated balance sheets and in cash used in operating activities in the consolidated statements of cash flows. PM Korea appealed the assessments. In January 2020, a trial court ruled that PM Korea did not

underpay the approximately KRW 218 billion (approximately $182 million) in taxes that were subject to its jurisdiction. The tax authorities have appealed this decision. If the tax authorities ultimately lose, then they would be required to return the paid amounts to PM Korea. PM Korea's appeal of approximately KRW 54 billion of alleged underpayments (approximately $45 million) is pending at another court. The tax authorities have also referred the matter to the Public Prosecutor. On June 19, 2018, the Public Prosecutor decided not to file criminal charges against PM Korea and/or other alleged co-offenders. The Public Prosecutor also decided not to prosecute PM Korea and its managing director in connection with a criminal complaint against them that had been filed by the South Korean Ministry of Strategy and Finance ("MOSF"). In the criminal complaint, the MOSF alleged that PM Korea exceeded the monthly product withdrawal limits that the MOSF had set in its notice. In March 2019, the Supreme Prosecutor's Office dismissed both the tax authorities' and the MOSF's appeals on the decisions of the Public Prosecutor, concluding the criminal investigations in these matters.

The Moscow Tax Inspectorate for Major Taxpayers ("MTI") conducted an audit of AO Philip Morris Izhora ("PM Izhora"), our Russian affiliate, for the 2015-2017 financial years. On July 26, 2019, MTI issued its initial assessment, claiming that intercompany sales of cigarettes between PM Izhora and another Russian affiliate prior to excise tax increases and submission by PM Izhora of the maximum retail sales price notifications for cigarettes to the tax authorities were improper under Russian tax laws and resulted in underpayment of excise taxes and VAT. In August 2019, PM Izhora submitted its objections disagreeing with MTI's allegations set forth in the initial assessment and MTI's methodology for calculating the alleged underpayments. MTI accepted some of PM Izhora's arguments and in September 2019, issued the final tax assessment claiming an underpayment of RUB 24.3 billion (approximately $374 million), including penalties and interest. In accordance with Russian tax laws, PM Izhora paid the entire amount of MTI's final assessment. This amount was neither imposed on, nor concurrent with, the specific revenue-producing transaction, nor was it collected from customers of our Russian affiliates. PMI believes that the loss of $374 million in this matter is probable and estimable. Consequently, in the third quarter of 2019, PMI recorded a pre-tax charge of $374 million, in marketing, administration and research costs in the consolidated statements of earnings, representing $315 million net of income tax. Under the Russian law, PM Izhora has until mid-September 2020 to challenge the final tax assessment to the Federal Tax Service and is considering whether to pursue such challenge.

A putative shareholder class action lawsuit, *In re Philip Morris International Inc. Securities Litigation*, is pending in the United States District Court for the Southern District of New York, purportedly on behalf of purchasers of Philip Morris International Inc. stock between July 26, 2016 and April 18, 2018. The lawsuit names Philip Morris International Inc. and certain officers and employees as defendants and includes allegations that the defendants made false and/or misleading statements and/or failed to disclose information about PMI's business, operations, financial condition, and prospects, related to product sales of, and alleged irregularities in clinical studies of, PMI's Platform 1 product. The lawsuit seeks various forms of relief, including damages. In November 2018, the court consolidated three putative shareholder class action lawsuits with similar allegations previously filed in the Southern District of New York (namely, *City of Westland Police and Fire Retirement System v. Philip Morris International Inc., et al, Greater Pennsylvania Carpenters' Pension Fund v. Philip Morris International Inc., et al., and Gilchrist v. Philip Morris International Inc., et al.*) into these proceedings. A putative shareholder class action lawsuit, *Rubenstahl v. Philip Morris International Inc., et al.*, that had been previously filed in December 2017 in the United States District Court for the District of New Jersey, was voluntarily dismissed by the plaintiff due to similar allegations in these proceedings. On February 4, 2020, the court granted defendants' motion in its entirety, dismissing all but one of the plaintiffs' claims with prejudice. The court noted that one of plaintiffs' claims (allegations relating to four non-clinical studies of PMI's Platform 1 product) did not state a viable claim but allowed plaintiffs to replead that claim by March 3, 2020. We believe that this lawsuit is without merit and, in the event that plaintiffs take further action, will continue to defend it vigorously.

We are also involved in additional litigation arising in the ordinary course of our business. While the outcomes of these proceedings are uncertain, management does not expect that the ultimate outcomes of other litigation, including any reasonably possible losses in excess of current accruals, will have a material adverse effect on our consolidated results of operations, cash flows or financial position.

Note 19.

Balance Sheet Offsetting:

Derivative Financial Instruments

PMI uses foreign exchange contracts and interest rate contracts to mitigate its exposure to changes in exchange and interest rates from third-party and intercompany actual and forecasted transactions. Substantially all of PMI's derivative financial instruments are subject to master netting arrangements, whereby the right to offset occurs in the event of default by a participating party. While these contracts contain the enforceable right to offset through close-out netting rights, PMI elects to present them on a gross basis in the consolidated balance sheets. Collateral associated with these arrangements is in the form of cash and is unrestricted. See Note 15. *Financial Instruments* for disclosures related to PMI's derivative financial instruments.

The effects of these derivative financial instrument assets and liabilities on PMI's consolidated balance sheets were as follows:

(in millions)	Gross Amounts Recognized	Gross Amount Offset in the Consolidated Balance Sheet	Net Amounts Presented in the Consolidated Balance Sheet	Gross Amounts Not Offset in the Consolidated Balance Sheet		Net Amount
				Financial Instruments	Cash Collateral Received/ Pledged	
At December 31, 2019						
Assets						
Derivative contracts	**$ 390**	**$ —**	**$ 390**	**$ (297)**	**$ (91)**	**$ 2**
Liabilities						
Derivative contracts	**$ 419**	**$ —**	**$ 419**	**$ (297)**	**$ (59)**	**$ 63**
At December 31, 2018						
Assets						
Derivative contracts	$ 220	$ —	$ 220	$ (124)	$ (80)	$ 16
Liabilities						
Derivative contracts	$ 631	$ —	$ 631	$ (124)	$ (427)	$ 80

Note 20.

Sale of Accounts Receivable:

To mitigate risk and enhance cash and liquidity management PMI sells trade receivables to unaffiliated financial institutions. These arrangements allow PMI to sell, on an ongoing basis, certain trade receivables without recourse. The trade receivables sold are generally short-term in nature and are removed from the consolidated balance sheets. PMI sells trade receivables under two types of arrangements, servicing and non-servicing. For servicing arrangements, PMI continues to service the sold trade receivables on an administrative basis and does not act on behalf of the unaffiliated financial institutions. When applicable, a servicing liability is recorded for the estimated fair value of the servicing. The amounts associated with the servicing liability were not material for the years ended December 31, 2019 and 2018. Under the non-servicing arrangements, PMI does not provide any administrative support or servicing after the trade receivables have been sold to the unaffiliated financial institutions.

Cumulative trade receivables sold, including excise taxes, for the years ended December 31, 2019 and 2018, were $10.7 billion and $11.0 billion, respectively. PMI’s operating cash flows were positively impacted by the amount of the trade receivables sold and derecognized from the consolidated balance sheets, which remained outstanding with the unaffiliated financial institutions. The trade receivables sold that remained outstanding under these arrangements as of December 31, 2019, 2018 and 2017, were $0.9 billion, $1.0 billion and $1.1 billion, respectively. The net proceeds received are included in cash provided by operating activities in the consolidated statements of cash flows. The difference between the carrying amount of the trade receivables sold and the sum of the cash received is recorded as a loss on sale of trade receivables within marketing, administration and research costs in the consolidated statements of earnings. For the years ended December 31, 2019, 2018 and 2017 the loss on sale of trade receivables was immaterial.

Note 21.

Asset Impairment and Exit Costs:

Global Manufacturing Infrastructure Optimization

In light of declining PMI cigarette volumes resulting from lower total industry volumes and the shift to smoke-free alternatives, PMI continues to optimize its global manufacturing infrastructure.

Germany

On November 4, 2019, PMI announced that, as part of its global manufacturing infrastructure optimization, its German affiliate, Philip Morris Manufacturing GmbH ("PMMG"), reached an agreement with employee representatives to end cigarette production in its factory in Berlin, Germany, by January 1, 2020. As a result of this agreement, during 2019, PMI recorded pre-tax asset impairment and exit costs of $342 million in the European Union segment. This amount included pension and employee separation costs of $251 million, which will be paid in cash, and asset impairment costs of $91 million, primarily related to machinery and equipment, which are non-cash charges.

Other

During 2019, PMI also recorded pre-tax asset impairment and exit costs of $80 million as part of its global manufacturing infrastructure optimization. These costs were related to a cigarette plant closure in Argentina ($15 million), Colombia ($45 million) and Pakistan ($20 million). The charges were reflected in the Latin America & Canada segment (Argentina and Colombia) and the South & Southeast Asia segment (Pakistan).

Asset Impairment and Exit Costs by Segment

During 2019, pre-tax asset impairment and exit costs consisted of the following:

(in millions)		2019
Separation programs:		
European Union	$	251
South & Southeast Asia		3
Latin America & Canada		49
Total separation programs		303
Asset impairment charges		
European Union		91
South & Southeast Asia		17
Latin America & Canada		11
Total asset impairment charges		119
Asset impairment and exit costs	$	422

The total pre-tax asset impairment and exit costs above were included in marketing, administration and research costs on the consolidated statements of earnings. During 2018 and 2017, PMI did not incur asset impairment and exit costs.

Movement in Exit Cost Liabilities

The movement in exit cost liabilities for the year ended December 31, 2019 was as follows:

(in millions)		
Liability balance, January 1, 2019	$	—
Charges, net		303
Cash spent		(49)
Currency/other[(a)]		(63)
Liability balance, December 31, 2019	$	191

[(a)] Relates primarily to the reclassification of pension amounts.

Future cash payments for exit costs incurred to date are anticipated to be substantially paid by the end of 2021, with approximately $115 million expected to be paid in 2020.

Note 22.

Deconsolidation of RBH:

As discussed in Note 18. *Contingencies,* following the March 1, 2019, judgment of the Court of Appeal of Québec in two class action lawsuits against PMI's Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH"), PMI recorded in its consolidated results a pre-tax charge of $194 million, representing $142 million net of tax, in the first quarter of 2019. This pre-tax Canadian tobacco litigation-related expense was included in marketing, administration and research costs on PMI's consolidated statement of earnings for the year ended December 31, 2019. The charge reflects PMI's assessment of the portion of the judgment that represents probable and estimable loss prior to the deconsolidation of RBH and corresponds to the trust account deposit required by the judgment. RBH's share of the deposit is approximately CAD 257 million.

On March 22, 2019, RBH obtained an initial order from the Ontario Superior Court of Justice granting it protection under the Companies' Creditors Arrangement Act ("CCAA"), which is a Canadian federal law that permits a Canadian business to restructure its affairs while carrying on its business in the ordinary course with minimal disruption to its customers, suppliers and employees.

The administration of the CCAA process, principally relating to the powers provided to the court and the court appointed monitor, removes certain elements of control of the business from both PMI and RBH. As a result, PMI has determined that it no longer has a controlling financial interest over RBH as defined in ASC 810 (Consolidation), and PMI deconsolidated RBH as of the date of the CCAA filing. PMI has also determined that it does not exert "significant influence" over RBH as that term is defined in ASC 323 (Investments-Equity Method and Joint Ventures). Therefore, as of March 22, 2019, PMI accounted for its continuing investment in RBH in accordance with ASC 321 (Investments-Equity Securities) as an equity security, without readily determinable fair value.

Following the deconsolidation, the carrying value of assets and liabilities of RBH was removed from the consolidated balance sheet of PMI, and the continuing investment in RBH was recorded at fair value at the date of deconsolidation. The total amount deconsolidated from PMI's balance sheet was $3,519 million, including $1,323 million of cash, $1,463 million of goodwill, $529 million of accumulated other comprehensive earnings, primarily related to historical currency translation and $204 million of other assets and liabilities, net. While PMI is accounting for its investment in RBH as an equity security, PMI would recognize dividends as income upon receipt. However, while it remains under creditor protection, RBH does not anticipate paying dividends.

The fair value of PMI's continuing investment in RBH of $3,280 million was determined at the date of deconsolidation, recorded within Investments in unconsolidated subsidiaries and equity securities and is assessed for impairment on an ongoing basis. The estimated fair value of the underlying business was determined based on an income approach using a discounted cash flow analysis, as well as a market approach for certain contingent liabilities. The information used in the estimate includes observable inputs, primarily a discount rate of 8%, a terminal growth rate of 2.5% and information about total tobacco market size in Canada and RBH's share of the market, as well as unobservable inputs such as operating budgets and strategic plans, various inflation scenarios, estimated shipment volumes, and expected product pricing and projected margins.

The difference between the carrying value of the assets and liabilities of RBH that were deconsolidated and the fair value of the continuing investment, as determined at the date of deconsolidation, was $239 million, before tax, and this loss on deconsolidation is reflected within marketing, administration and research costs on PMI's consolidated statement of earnings for the year ended December 31, 2019. PMI also recorded a tax benefit of $49 million within the provision for income taxes for the year ended December 31, 2019, related to the reversal of a deferred tax liability on unremitted earnings of RBH.

RBH is party to transactions with PMI and its consolidated subsidiaries entered into in the normal course of business; these transactions include royalty payments and recharge of various corporate expenses for services benefiting RBH. Up to the date of CCAA filing, these transactions were eliminated on consolidation and had no impact on PMI's consolidated statement of earnings. After deconsolidating RBH, these transactions are treated as third-party transactions in PMI's financial statements. The amount of these related-party transactions is included within Note 4. *Related Parties - Investments in Unconsolidated Subsidiaries, Equity Securities and Other.*

Developments in the CCAA process, including resolution through a plan of arrangement or compromise of all pending tobacco-related litigation currently stayed in Canada, as discussed in Note 18. *Contingencies*, could result in a material change in the fair value of PMI's continuing investment in RBH.

Note 23.

Leases:

PMI's operating leases are principally for real estate (office space, warehouses and retail store space) and vehicles. Lease terms range from 1 year to 74 years, some of which include options to renew, which are reasonably certain to be renewed. Lease terms may also include options to terminate the lease. The exercise of a lease renewal or termination option is at PMI's discretion.
PMI's operating leases at December 31, 2019, were as follows:

(in millions)		December 31, 2019
Assets:		
Other assets	$	766
Liabilities:		
Current		
Accrued liabilities - Other	$	194
Noncurrent		
Income taxes and other liabilities		569
Total lease liabilities	$	763

For information regarding PMI's immaterial finance leases, see Note 16. *Fair Value Measurements*.

The components of PMI's lease cost were as follows for the year ended December 31, 2019:

(in millions)		December 31, 2019
Operating lease cost	$	242
Short-term lease cost		61
Variable lease cost		29
Total lease cost	$	332

For the year ended December 31, 2019, lease cost of $79 million was recorded in cost of sales and $253 million was recorded in marketing, administration and research cost.

Maturity of PMI's operating lease liabilities, on an undiscounted basis, as of December 31, 2019, was as follows (as calculated under the new guidance ASC 842 (Leases)):

(in millions)		Total
2020	$	222
2021		162
2022		124
2023		92
2024		66

Thereafter		**283**
Total lease payments		**949**
Less: Interest		**186**
Present value of lease liabilities	**$**	**763**

Minimum rental commitments under non-cancelable operating leases in effect at December 31, 2018, were as follows (as calculated under legacy guidance ASC 840 (Leases)):

(in millions)		Total
2019	$	147
2020		103
2021		73
2022		52
2023		43
Thereafter		354
	$	772

Other information related to PMI's operating leases was as follows for the year ended December 31, 2019:

(in millions)		December 31, 2019
Cash paid for amounts included in the measurement of lease liabilities in Operating cash flows	**$**	**240**
Leased assets obtained in exchange for new operating lease liabilities	**$**	**221**
Weighted-average remaining lease term (years)		**9.6**
Weighted-average discount rate[1]		**4.4 %**

[1] PMI's weighted-average discount rate is based on its estimated pre-tax cost of debt adjusted for country-specific risk.

For further details, see Note 24. *New Accounting Standards*.

Note 24.

New Accounting Standards:

Recently adopted

On February 25, 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ASU 2016-02, "Leases" ("ASU 2016-02"). ASU 2016-02 requires organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases. Additionally, ASU 2016-02 modifies current guidance for lessors' accounting. ASU 2016-02 is effective for interim and annual reporting periods beginning on or after January 1, 2019, with early adoption permitted. PMI has identified its lease management system and has identified and evaluated the applicable leases. In addition to the guidance in ASU 2016-02, PMI has evaluated ASU 2018-11, which was issued in July 2018 and provides an optional transitional method. As a result of this evaluation, PMI elected to use the optional transition method, which allows companies to use the effective date as the date of initial application on transition and not adjust comparative period financial information or make the new required disclosures for periods prior to the effective date. Additionally, PMI elected to use the hindsight practical expedient, as well as the package of practical expedients permitted under the transition guidance within the new standard. Upon adoption, PMI recognized lease liabilities and the corresponding right-of-use assets (at the present value of future payments) for predominately all of its operating leases in place at that time. At January 1, 2019, PMI's adoption of ASU 2016-02 resulted in an increase of approximately $0.7 billion on its assets and liabilities in its statement of financial position. ASU 2016-02 did not have a material impact on its results of operations or cash flows. For further details, see Note 23. *Leases*.

On January 1, 2019, PMI elected to early adopt ASU 2018-15 “Intangibles - Goodwill and Other - Internal - Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract.” The adoption of ASU 2018-15 did not have a material impact on PMI's consolidated financial position or results of operations.

Note 25.

Quarterly Financial Data (Unaudited):

(in millions, except per share data)	2019 Quarters			
	1st	2nd	3rd	4th
Net revenues	**$ 6,751**	**$ 7,699**	**$ 7,642**	**$ 7,713**
Gross profit	**$ 4,286**	**$ 5,034**	**$ 5,037**	**$ 4,935**
Net earnings attributable to PMI	**$ 1,354**	**$ 2,319**	**$ 1,896**	**$ 1,616**
Per share data:				
Basic EPS	**$ 0.87**	**$ 1.49**	**$ 1.22**	**$ 1.04**
Diluted EPS	**$ 0.87**	**$ 1.49**	**$ 1.22**	**$ 1.04**
Dividends declared	**$ 1.14**	**$ 1.14**	**$ 1.17**	**$ 1.17**

(in millions, except per share data)	2018 Quarters			
	1st	2nd	3rd	4th
Net revenues	$ 6,896	$ 7,726	$ 7,504	$ 7,499
Gross profit	$ 4,281	$ 4,982	$ 4,886	$ 4,718
Net earnings attributable to PMI	$ 1,556	$ 2,198	$ 2,247	$ 1,910
Per share data:				
Basic EPS	$ 1.00	$ 1.41	$ 1.44	$ 1.23
Diluted EPS	$ 1.00	$ 1.41	$ 1.44	$ 1.23
Dividends declared	$ 1.07	$ 1.14	$ 1.14	$ 1.14

Basic and diluted EPS are computed independently for each of the periods presented. Accordingly, the sum of the quarterly EPS amounts may not agree to the total for the year.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of
Philip Morris International Inc.:

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Philip Morris International Inc. and its subsidiaries (the "Company") as of December 31, 2019 and 2018, and the related consolidated statements of earnings, comprehensive earnings, stockholders' (deficit) equity and of cash flows for each of the three years in the period ended December 31, 2019, including the related notes (collectively referred to as the "consolidated financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2019, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2019 and 2018, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2019 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2019, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the COSO.

Basis for Opinions

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Report of Management on Internal Control over Financial Reporting. Our responsibility is to express opinions on the Company's consolidated financial statements and on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that

transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Critical Audit Matters

The critical audit matters communicated below are matters arising from the current period audit of the consolidated financial statements that were communicated or required to be communicated to the audit committee and that (i) relate to accounts or disclosures that are material to the consolidated financial statements and (ii) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the consolidated financial statements, taken as a whole, and we are not, by communicating the critical audit matters below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

Fair Value of Equity Investment in Rothmans, Benson & Hedges Inc. ("RBH")

As described in Note 22 to the consolidated financial statements, the Company recorded the fair value of its continuing investment in RBH of $3.28 billion within Investments in unconsolidated subsidiaries and equity securities in the consolidated balance sheets. This investment was recorded as of March 22, 2019, which represented the fair value at the date of deconsolidation. The estimated fair value of the underlying business was determined based on an income approach using a discounted cash flow analysis, as well as a market approach for certain contingent liabilities. The discounted cash flow analysis and market approach include management assumptions relevant for forecasting operating cash flows, which are subject to changes in business conditions, such as volumes, pricing, the terminal growth rate, discount rates, inflation scenarios, and other strategic plans. The difference between the carrying value of the assets and liabilities of RBH that were deconsolidated and the fair value of the continuing investment was recorded as a $239 million pre-tax loss on deconsolidation within marketing, administration and research costs on the Company's consolidated statement of earnings.

The principal considerations for our determination that performing procedures relating to the deconsolidation of RBH is a critical audit matter are that there was significant judgment by management required when developing the fair value measurement of the continuing investment in RBH. This led to a high degree of auditor subjectivity, judgment and effort in performing procedures and evaluating the estimated fair value of RBH which included significant assumptions related to the terminal growth rate, discount rates, inflation scenarios, and operating cash flow projections; and to evaluate management's estimate of the value of certain contingent liabilities. The audit effort involved the use of professionals with specialized skill and knowledge to assist in evaluating the audit evidence obtained from these procedures.

Addressing the matter involved performing procedures and evaluating audit evidence in connection with forming our overall opinion on the consolidated financial statements. These procedures included testing the effectiveness of controls relating to the estimated fair value of the RBH investment, including controls over the discounted cash flow analysis and market approach, input data and key assumptions utilized in determination of the fair value. These procedures also included, among others, testing management's process for determining the fair value of the continuing investment in RBH as of the date of deconsolidation. This included evaluating the appropriateness of the discounted cash flow analysis and market approach to value the contingent liabilities including the reasonableness of the input data and significant assumptions used by management in developing the fair value measurement including the terminal growth rate, discount rates, inflation scenarios, operating cash flow projections, market size and market share data. Professionals with specialized skill and knowledge were used to assist in evaluating the Company's discounted cash flow analysis and market approach, and evaluation of significant assumptions, including the terminal growth rate, discount rates and inflation scenarios utilized by the Company. Evaluating whether the significant assumptions were reasonable involved considering (i) the past performance of the associated Canadian reporting unit, and (ii) whether they were consistent with evidence obtained in other areas of the audit.

Smoking and Health and Health Care Cost Recovery Contingencies

As described in Note 18 to the consolidated financial statements, the Company has 77 smoking and health cases and health care cost recovery actions pending. The Company records provisions in the consolidated financial statements for pending litigation when they determine that an unfavorable outcome is probable and the amount of the loss can be

reasonably estimated. Except as stated otherwise in Note 18, while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available, (i) management has not concluded that it is probable that a loss has been incurred in any of the pending smoking and health and health care cost recovery tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending smoking and health and health care cost recovery tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any.

The principal considerations for our determination that performing procedures relating to smoking and health and health care cost recovery contingencies is a critical audit matter are that there was significant judgment by management when determining the probability of a loss being incurred and an estimate of the amount or range of the potential loss for each case, which in turn led to a high degree of auditor

subjectivity, judgment and effort in evaluating management's assessment related to the loss contingencies associated with smoking and health and health care cost recovery related claims.

Addressing the matter involved performing procedures and evaluating audit evidence in connection with forming our overall opinion on the consolidated financial statements. These procedures included testing the effectiveness of controls relating to management's evaluation of smoking and health and health care cost recovery litigation matters, including controls over determining the probability and range of loss as well as financial statement disclosures. These procedures also included, among others, evaluating the completeness of the Company's description of smoking and health and health care cost recovery contingencies, obtaining and evaluating the letters of audit inquiry with external and internal legal counsel, evaluating the reasonableness of management's assessment regarding whether an unfavorable outcome is reasonably possible or probable and reasonably estimable, and evaluating the sufficiency of the Company's smoking and health and health care cost recovery contingencies disclosures.

/S/ PRICEWATERHOUSECOOPERS SA
PricewaterhouseCoopers SA

/S/ CHAD MUELLER
Chad Mueller

/S/ CLAUDIA BENZ
Claudia Benz

Lausanne, Switzerland
February 7, 2020

PricewaterhouseCoopers SA has served as the Company's auditor since 2008.

Report of Management on Internal Control Over Financial Reporting

Management of Philip Morris International Inc. ("PMI") is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended. PMI's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes those written policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of PMI;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America;
- provide reasonable assurance that receipts and expenditures of PMI are being made only in accordance with the authorization of management and directors of PMI; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets that could have a material effect on the consolidated financial statements.

Internal control over financial reporting includes the controls themselves, monitoring and internal auditing practices and actions taken to correct deficiencies as identified.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of PMI's internal control over financial reporting as of December 31, 2019. Management based this assessment on criteria for effective internal control over financial reporting described in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management's assessment included an evaluation of the design of PMI's internal control over financial reporting and testing of the operational effectiveness of its internal control over financial reporting. Management reviewed the results of its assessment with the Audit Committee of our Board of Directors.

Based on this assessment, management determined that, as of December 31, 2019, PMI maintained effective internal control over financial reporting.

PricewaterhouseCoopers SA, an independent registered public accounting firm, who audited and reported on the consolidated financial statements of PMI included in this report, has audited the effectiveness of PMI's internal control over financial reporting as of December 31, 2019, as stated in their report herein.

February 7, 2020

Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.*

None.

Item 9A. *Controls and Procedures.*

PMI carried out an evaluation, with the participation of PMI's management, including PMI's Chief Executive Officer and Chief Financial Officer, of the effectiveness of PMI's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based upon that evaluation, PMI's Chief Executive Officer and Chief Financial Officer concluded that PMI's disclosure controls and procedures are effective. There have been no changes in PMI's internal control over financial reporting during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, PMI's internal control over financial reporting.

The Report of Management on Internal Control over Financial Reporting and the Report of Independent Registered Public Accounting Firm are included in Item 8.

Item 9B. *Other Information.*

None.

PART III

Except for the information relating to the executive officers set forth in Item 10 and the information relating to equity compensation plans set forth in Item 12, the information called for by Items 10-14 is hereby incorporated by reference to PMI's definitive proxy statement for use in connection with its annual meeting of stockholders to be held on May 6, 2020, that will be filed with the SEC on or about March 26, 2020 (the "proxy statement"), and, except as indicated therein, made a part hereof.

Item 10. *Directors, Executive Officers and Corporate Governance.*

Information About Our Executive Officers as of February 6, 2020:

Name	Office	Age
André Calantzopoulos	Chief Executive Officer	62
Massimo Andolina	Senior Vice President, Operations	51
Drago Azinovic	President, Middle East & Africa Region and PMI Duty Free	57
Werner Barth	Senior Vice President, Commercial	55
Charles Bendotti	Senior Vice President, People and Culture	47
Frank de Rooij	Vice President, Treasury and Corporate Finance	54
Frederic de Wilde	President, European Union Region	52
Marc S. Firestone	President, External Affairs and General Counsel	60
Stacey Kennedy	President, South and Southeast Asia Region	47
Martin G. King	Chief Financial Officer	55
Michael Kunst	Senior Vice President, Commercial Transformation	51
Andreas Kurali	Vice President and Controller	54
Bin Li	Chief Product Officer	48
Marco Mariotti	President, Eastern Europe Region	55
Mario Masseroli	President, Latin America & Canada Region	49
Deepak Mishra	Chief Strategy Officer	48
John O'Mullane	Chief Life Sciences Officer	66
Jacek Olczak	Chief Operating Officer	55
Paul Riley	President, East Asia and Australia Region	54
Marian Salzman	Senior Vice President, Global Communications	61
Jaime Suarez	Chief Digital Officer	46
Michael Voegele	Chief Technology Officer	47
Stefano Volpetti	Chief Consumer Officer	48
Jerry E. Whitson	Deputy General Counsel and Corporate Secretary	64
Miroslaw Zielinski	Chief New Ventures Officer	58

All of the above-mentioned officers, except Ms. Salzman, Mr. Mishra, Mr. Kunst, Mr. Voegele, Mr. O'Mullane, Mr. Volpetti and Mr. Li, have been employed by us in various capacities during the past five years.

Before joining Philip Morris International Inc. in April 2018, Ms. Salzman headed Havas PR North America, where she had served as Chief Executive Officer from 2011.

Before joining Philip Morris International Inc. in September 2018, Mr. Mishra was Managing Director, Portfolio Operations at Centerbridge Partners, a private equity firm, from 2014, where he led commercial, operational and digital transformation in various business sectors. From 2001 to 2014, Mr. Mishra was Partner and part of the Consumer Goods, Retail and Operations leadership team of McKinsey & Co, where he supported clients in their transformation projects.

Before joining Philip Morris International Inc. in January 2019, Mr. Kunst was Partner at Bain & Company from 2009, most recently working with us on our transformation projects.

Before joining Philip Morris International Inc. in February 2019, Mr. Voegele had served in various senior capacities at Adidas Group from 2011, most recently, as Global CIO and part of the core leadership team at Adidas Group.

Before joining Philip Morris International Inc. in May 2019, Mr. O'Mullane was Global Head SVP Innovation and Development for Consumer Health at Bayer AG from 2014.

Before joining Philip Morris International Inc. in June 2019, Mr. Volpetti served in various executive capacities at the Procter & Gamble Company from 1996, most recently, as Vice President of a global business unit. He also served as Chief Marketing Officer at Luxottica Group S.p.A. in 2015.

Before joining Philip Morris International Inc. in August 2019, Mr. Li served in various executive capacities at Harman International, a subsidiary of Samsung Electronics Co. Ltd., from 2010, most recently, as Senior Vice President and General Manager, Consumer Audio Product Development and Operations.

Codes of Conduct and Corporate Governance

We have adopted the Philip Morris International Code of Conduct, which complies with requirements set forth in Item 406 of Regulation S-K. This Code of Conduct applies to all of our employees, including our principal executive officer, principal financial officer, principal accounting officer or controller, and persons performing similar functions. We have also adopted a code of business conduct and ethics that applies to the members of our Board of Directors. These documents are available free of charge on our website at www.pmi.com.

In addition, we have adopted corporate governance guidelines and charters for our Audit, Finance, Compensation and Leadership Development, Product Innovation and Regulatory Affairs and Nominating and Corporate Governance committees of the Board of Directors. All of these documents are available free of charge on our website at www.pmi.com. Any waiver granted by Philip Morris International Inc. to its principal executive officer, principal financial officer or controller or any person performing similar functions under the Code of Conduct, or certain amendments to the Code of Conduct, will be disclosed on our website at www.pmi.com.

The information on our website is not, and shall not be deemed to be, a part of this Report or incorporated into any other filings made with the SEC.

Also refer to *Board Operations and Governance—Committees of the Board*, *Election of Directors—Process for Nominating Directors* and *Election of Directors—Director Nominees* and *Delinquent Section 16(a) Reports* sections of the proxy statement.

Item 11. *Executive Compensation.*

Refer to *Compensation Discussion and Analysis* and *Compensation of Directors* sections of the proxy statement.

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.*

The number of shares to be issued upon exercise or vesting and the number of shares remaining available for future issuance under PMI's equity compensation plans at December 31, 2019, were as follows:

	Number of Securities to be Issued upon Exercise of Outstanding Options and Vesting of RSUs (a)	Weighted Average Exercise Price of Outstanding Options (b)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (excluding Securities reflected in column (a)) (c)
Equity compensation plans approved by stockholders	6,289,960 [1]	$ —	21,081,444

[1] Represents 3,725,870 shares of common stock that may be issued upon vesting of the restricted share units and 2,564,090 shares that may be issued upon vesting of the performance share units if maximum performance targets are achieved for each performance cycle. PMI has not granted options since the spin-off from Altria on March 28, 2008.

Also refer to *Stock Ownership Information—Ownership of Equity Securities* section of the proxy statement.

Item 13. *Certain Relationships and Related Transactions, and Director Independence.*

Refer to *Related Person Transactions and Code of Conduct* and *Election of Directors—Independence of Nominees* sections of the proxy statement.

Item 14. *Principal Accounting Fees and Services.*

Refer to *Audit Committee Matters* section of the proxy statement.

PART IV

Item 15. *Exhibits and Financial Statement Schedules.*

(a) Index to Consolidated Financial Statements and Schedules

	Page
Consolidated Statements of Earnings for the years ended December 31, 2019, 2018 and 2017	53
Consolidated Statements of Comprehensive Earnings for the years ended December 31, 2019, 2018 and 2017	54
Consolidated Balance Sheets at December 31, 2019 and 2018	55 - 56
Consolidated Statements of Cash Flows for the years ended December 31, 2019, 2018 and 2017	57 - 58
Consolidated Statements of Stockholders' (Deficit) Equity for the years ended December 31, 2019, 2018 and 2017	59
Notes to Consolidated Financial Statements	60 - 109
Report of Independent Registered Public Accounting Firm	110 - 112
Report of Management on Internal Control Over Financial Reporting	113

Schedules have been omitted either because such schedules are not required or are not applicable.

(b) The following exhibits are filed as part of this Report:

2.1	—	Distribution Agreement between Altria Group, Inc. and Philip Morris International Inc. dated January 30, 2008 (incorporated by reference to Exhibit 2.1 to the Registration Statement on Form 10 filed February 7, 2008).
3.1	—	Amended and Restated Articles of Incorporation of Philip Morris International Inc. (incorporated by reference to Exhibit 3.1 to the Registration Statement on Form 10 filed February 7, 2008).
3.2	—	Amended and Restated By-Laws of Philip Morris International Inc., effective as of March 7, 2019 (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed March 7, 2019).
4.1	—	Specimen Stock Certificate of Philip Morris International Inc. (incorporated by reference to Exhibit 4.1 to the Registration Statement on Form 10 filed February 7, 2008).
4.2	—	Indenture dated as of April 25, 2008, between Philip Morris International Inc. and HSBC Bank USA, National Association, as Trustee (incorporated by reference to Exhibit 4.3 to the Registration Statement on Form S-3, dated April 25, 2008).
4.3	—	Description of Common Stock.
4.4	—	Description of Debt Securities.
4.6	—	The Registrant agrees to furnish copies of any instruments defining the rights of holders of long-term debt of the Registrant and its consolidated subsidiaries that does not exceed 10 percent of the total assets of the Registrant and its consolidated subsidiaries to the Commission upon request.
10.1	—	Employee Matters Agreement between Altria Group, Inc. and Philip Morris International Inc., dated as of March 28, 2008 (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed March 31, 2008).
10.2	—	Intellectual Property Agreement between Philip Morris International Inc. and Philip Morris USA Inc., dated as of January 1, 2008 (incorporated by reference to Exhibit 10.4 to the Registration Statement on Form 10 filed March 5, 2008).

10.3	—	Credit Agreement relating to a US$3,500,000,000 Revolving Credit Facility (including a US$800,000,000 swingline option) dated as of October 25, 2011, among Philip Morris International Inc. and the Initial Lenders named therein and Citibank International plc, as Facility Agent, and Citibank, N.A., as Swingline Agent, and Citigroup Global Markets Limited, Barclays Capital, BNP Paribas, Credit Suisse AG, Cayman Islands Branch, Deutsche Bank Securities Inc., Goldman Sachs International, HSBC Bank PLC, J.P. Morgan Limited, RBS Securities Inc. and Société Générale as Mandated Lead Arrangers and Bookrunners (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed October 26, 2011).
10.4	—	Amendment No. 1, dated as of August 31, 2012, to the Credit Agreement, dated as of October 25, 2011, among Philip Morris International Inc., the lenders named therein and Citibank International plc, as Facility Agent (incorporated by reference to Exhibit 10.6 to the Quarterly Report on Form 10-Q for the quarter ended September 30, 2012).
10.5	—	Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 15, 2013).
10.6	—	Extension Agreement, effective February 7, 2017, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders party thereto, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 30, 2017).
10.7	—	Extension Agreement, effective January 31, 2014, to Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders party thereto and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.3 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2014).
10.8	—	Credit Agreement, dated as of February 28, 2014, among Philip Morris International Inc., the lenders named therein, J.P. Morgan Europe Limited, as Facility Agent, and JPMorgan Chase Bank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed March 3, 2014).
10.9	—	Extension Agreement, effective as of February 10, 2015, to Credit Agreement dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2015).
10.10	—	Extension Agreement, effective as of February 28, 2015, to the Credit Agreement, dated as of February 28, 2014, among Philip Morris International Inc., the lenders named therein, J.P. Morgan Europe Limited, as Facility Agent, and JPMorgan Chase Bank, N.A. as Swingline Agent (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed January 29, 2015).
10.11	—	Amendment No. 1, dated as of July 20, 2015, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, The Royal Bank of Scotland plc, as resigning administrative agent, and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as successor administrative agent (incorporated by reference to Exhibit 10.52 to the Annual Report on Form 10-K for the year ended December 31, 2015).
10.12	—	Credit Agreement, dated as of October 1, 2015, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as Facility Agent, and Citibank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed October 5, 2015).
10.13	—	Amendment No. 2, effective as of February 9, 2016, to the Credit Agreement dated as of February 12, 2013, with the lenders named therein and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 28, 2016).

10.14	—	Extension Agreement, effective as of February 28, 2016, to the Credit Agreement, dated as of February 28, 2014, among Philip Morris International Inc., each lender named therein, J.P. Morgan Europe Limited, as facility agent, and JPMorgan Chase Bank, N.A., as swingline agent (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed January 28, 2016).
10.15	—	Extension Agreement, effective as of October 1, 2016, to the Credit Agreement dated as of October 1, 2015, among Philip Morris International Inc., lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as facility agent, and Citibank, N.A., as swingline agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 31, 2016).
10.16	—	Extension Agreement, effective as of October 1, 2017, to the Credit Agreement, dated as of October 1, 2015, among Philip Morris International Inc., the lenders party thereto and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as facility agent, and Citibank N.A., as swingline agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 29, 2017).
10.17	—	Extension Agreement, effective as of February 6, 2018, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2018).
10.18	—	Extension Agreement, effective as of February 5, 2019, to the Credit Agreement dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2019).
10.19	—	Philip Morris International Inc. Automobile Policy (incorporated by reference to Exhibit 10.8 to the Registration Statement on Form 10 filed February 7, 2008).*
10.20	—	Philip Morris International Inc. Amended and Restated Automobile Policy, dated as of October 1, 2019.*
10.21	—	Philip Morris International Benefit Equalization Plan, amended and restated (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2019).*
10.22	—	Philip Morris International Inc. 2012 Performance Incentive Plan, effective May 9, 2012 (incorporated by reference to Exhibit A to the Definitive Proxy Statement filed on March 30, 2012).*
10.23	—	Philip Morris International Inc. 2017 Performance Incentive Plan, effective May 3, 2017 (incorporated by reference to Exhibit B to the Definitive Proxy Statement filed on March 23, 2017).*
10.24	—	Pension Fund of Philip Morris in Switzerland (IC) (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2015).*
10.25	—	Summary of Supplemental Pension Plan of Philip Morris in Switzerland (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).*
10.26	—	Form of Restated Employee Grantor Trust Enrollment Agreement (Executive Trust Arrangement) (incorporated by reference to Exhibit 10.18 to the Registration Statement on Form 10 filed February 7, 2008).*
10.27	—	Form of Restated Employee Grantor Trust Enrollment Agreement (Secular Trust Arrangement) (incorporated by reference to Exhibit 10.19 to the Registration Statement on Form 10 filed February 7, 2008).*
10.28	—	Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors (as amended and restated as of January 1, 2018) (incorporated by reference to Exhibit 10.26 to the Annual Report on Form 10-K for the year ended December 31, 2017).*
10.29	—	Philip Morris International Inc. 2008 Deferred Fee Plan for Non-Employee Directors (incorporated by reference to Exhibit 10.21 to the Registration Statement on Form 10 filed February 7, 2008).*

10.30	—	Supplemental Letter to the Employment Agreement (as amended) with André Calantzopoulos (incorporated by reference to Exhibit 10.4 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017). The Employment Agreement was previously filed as Exhibit 10.22 to the Registration Statement on Form 10 filed February 7, 2008 and is incorporated by reference to this Exhibit 10.30. The Amendment to the Employment Agreement was previously filed as Exhibit 10.1 to the Current Report on Form 8-K/A filed June 13, 2013, and is incorporated by reference to this Exhibit 10.30.*
10.31	—	Supplemental Letter to Employment Agreement with Marc S. Firestone (incorporated by reference to Exhibit 10.5 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017). The Employment Agreement was previously filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 and is incorporated by reference to this Exhibit 10.31. The Amendment to the Employment Agreement was previously filed as Exhibit 10.25 to the Annual Report on Form 10-K for the year ended December 31, 2013, and is incorporated by reference to this Exhibit 10.31.*
10.32	—	Employment Agreement,with Martin G. King, as of January 1, 2018 (incorporated by reference to Exhibit 10.30 to the Annual Report on Form 10-K for the year ended December 31, 2017).*
10.33	—	Supplemental Letter to the Employment Agreement (as amended) with Jacek Olczak (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2019. The Employment Agreement was previously filed as Exhibit 10.4 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, and is incorporated by reference to this Exhibit 10.33. The Amendment to the Employment Agreement was previously filed as Exhibit 10.33 to the Annual Report on Form 10-K for the year ended December 31, 2013 and is incorporated by reference to this Exhibit 10.33.*
10.34	—	Supplemental Letter to the Employment Agreement (as amended) with Miroslaw Zielinski (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2019). The Employment Agreement was previously filed as Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 and is incorporated by reference to this Exhibit 10.34. The Amendment to the Employment Agreement was previously filed as Exhibit 10.28 to the Annual Report on Form 10-K for the year ended December 31, 2013 and is incorporated by reference to this Exhibit 10.34.*
10.35	—	Time Sharing Agreement between PMI Global Services Inc. and Louis C. Camilleri dated August 18, 2010 (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 19, 2010).*
10.36	—	Time Sharing Agreement between PMI Global Services Inc. and André Calantzopoulos, dated May 8, 2013 (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2013).*
10.37	—	Amendment No. 1 to the Time Sharing Agreement between PMI Global Services Inc. and André Calantzopoulos, dated December 23, 2014 (incorporated by reference to Exhibit 10.36 to the Annual Report on Form 10-K for the year ended December 31, 2014).*
10.38	—	Termination of the Time Sharing Agreement between PMI Global Services Inc. and André Calantzopoulos, dated November 12, 2019.*
10.39	—	Agreement with Louis C. Camilleri (incorporated by reference to Exhibit 10.25 to the Registration Statement on Form 10 filed February 7, 2008).*
10.40	—	Amended and Restated Supplemental Management Employees' Retirement Plan (incorporated by reference to Exhibit 10.27 to the Annual Report on Form 10-K for the year ended December 31, 2008).*
10.41	—	Supplemental Equalization Plan, amended and restated as of June 29, 2015 (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).*
10.42	—	Form of Supplemental Equalization Plan Employee Grantor Trust Enrollment Agreement (Secular Trust) (incorporated by reference to Exhibit 10.31 to the Annual Report on Form 10-K for the year ended December 31, 2008).*

10.43	—	Form of Supplemental Equalization Plan Employee Grantor Trust Enrollment Agreement (Executive Trust) (incorporated by reference to Exhibit 10.32 to the Annual Report on Form 10-K for the year ended December 31, 2008).*
10.44	—	Philip Morris International Inc. Form of Indemnification Agreement with Directors and Executive Officers (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed September 18, 2009).*
10.45	—	Form of Deferred Stock Agreement (2015 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 10, 2015).*
10.46	—	Philip Morris International Inc. Tax Return Preparation Services Policy (incorporated by reference to Exhibit 10.51 to the Annual Report on Form 10-K for the year ended December 31, 2014).*
10.47	—	Form of Restricted Stock Unit Agreement (2017 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 7, 2017).*
10.48	—	Form of Performance Share Unit Agreement (2017 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 7, 2017).*
10.49	—	Form of Restricted Stock Unit Agreement (2018 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 13, 2018).*
10.50	—	Form of Performance Share Unit Agreement (2018 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 13, 2018).*
10.51	—	Form of Restricted Stock Unit Agreement (2019 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 12, 2019).*
10.52	—	Form of Performance Share Unit Agreement (2019 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 12, 2019).*
21	—	Subsidiaries of Philip Morris International Inc.
23	—	Consent of independent registered public accounting firm.
24	—	Powers of attorney.
31.1	—	Certification of the Registrant's Chief Executive Officer pursuant to Rule 13a-14(a)/ 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	—	Certification of the Registrant's Chief Financial Officer pursuant to Rule 13a-14(a)/ 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	—	Certification of the Registrant's Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	—	Certification of the Registrant's Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	—	XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.
101.SCH	—	XBRL Taxonomy Extension Schema.
101.CAL	—	XBRL Taxonomy Extension Calculation Linkbase.
101.DEF	—	XBRL Taxonomy Extension Definition Linkbase.
101.LAB	—	XBRL Taxonomy Extension Label Linkbase.
101.PRE	—	XBRL Taxonomy Extension Presentation Linkbase.
104	—	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

* Denotes management contract or compensatory plan or arrangement in which directors or executive officers are eligible to participate.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PHILIP MORRIS INTERNATIONAL INC.

By: /s/ ANDRÉ CALANTZOPOULOS
(André Calantzopoulos
Chief Executive Officer)

Date: February 7, 2020

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated:

Signature	Title	Date
/s/ ANDRÉ CALANTZOPOULOS (André Calantzopoulos)	Chief Executive Officer	February 7, 2020
/s/ MARTIN G. KING (Martin G. King)	Chief Financial Officer	February 7, 2020
/s/ ANDREAS KURALI (Andreas Kurali)	Vice President and Controller	February 7, 2020
*LOUIS C. CAMILLERI, MASSIMO FERRAGAMO, WERNER GEISSLER, LISA A. HOOK, JENNIFER LI, JUN MAKIHARA, KALPANA MORPARIA, LUCIO A. NOTO, FREDERIK PAULSEN, ROBERT B. POLET, STEPHEN M. WOLF	Directors	
*By: /s/ ANDRÉ CALANTZOPOULOS (André Calantzopoulos Attorney-in-fact)		February 7, 2020

10-K 1 pm123118form10kwrapinclfsm.htm 10-K

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2018

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

Commission File Number: 001-33708

PHILIP MORRIS INTERNATIONAL INC.

(Exact name of registrant as specified in its charter)

Virginia	**13-3435103**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
120 Park Avenue, New York, New York	**10017**
(Address of principal executive offices)	**(Zip Code)**

917-663-2000

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, no par value	New York Stock Exchange
1.625% Notes due 2019	New York Stock Exchange
1.375% Notes due 2019	New York Stock Exchange
2.125% Notes due 2019	New York Stock Exchange
1.875% Notes due 2019	New York Stock Exchange
2.000% Notes due 2020	New York Stock Exchange
Floating Notes due 2020	New York Stock Exchange
1.750% Notes due 2020	New York Stock Exchange
4.500% Notes due 2020	New York Stock Exchange
1.875% Notes due 2021	New York Stock Exchange
1.875% Notes due 2021	New York Stock Exchange
4.125% Notes due 2021	New York Stock Exchange
2.900% Notes due 2021	New York Stock Exchange
2.625% Notes due 2022	New York Stock Exchange
2.375% Notes due 2022	New York Stock Exchange
2.500% Notes due 2022	New York Stock Exchange
2.500% Notes due 2022	New York Stock Exchange
2.625% Notes due 2023	New York Stock Exchange
2.125% Notes due 2023	New York Stock Exchange
3.600% Notes due 2023	New York Stock Exchange

Title of each class	Name of each exchange on which registered
2.875% Notes due 2024	New York Stock Exchange
0.625% Notes due 2024	New York Stock Exchange
3.250% Notes due 2024	New York Stock Exchange
2.750% Notes due 2025	New York Stock Exchange
3.375% Notes due 2025	New York Stock Exchange
2.750% Notes due 2026	New York Stock Exchange
2.875% Notes due 2026	New York Stock Exchange
3.125% Notes due 2027	New York Stock Exchange
3.125% Notes due 2028	New York Stock Exchange
2.875% Notes due 2029	New York Stock Exchange
3.125% Notes due 2033	New York Stock Exchange
2.000% Notes due 2036	New York Stock Exchange
1.875% Notes due 2037	New York Stock Exchange
6.375% Notes due 2038	New York Stock Exchange
4.375% Notes due 2041	New York Stock Exchange
4.500% Notes due 2042	New York Stock Exchange
3.875% Notes due 2042	New York Stock Exchange
4.125% Notes due 2043	New York Stock Exchange
4.875% Notes due 2043	New York Stock Exchange
4.250% Notes due 2044	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☑ No ☐

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☑

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☑ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☑ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☑

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☑
Accelerated filer ☐
Non-accelerated filer ☐
Smaller reporting company ☐
Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ☐ No ☑

As of June 30, 2018, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was approximately $126 billion based on the closing sale price of the common stock as reported on the New York Stock Exchange.

Class	Outstanding at January 31, 2019
Common Stock, no par value	1,554,584,344 shares

DOCUMENTS INCORPORATED BY REFERENCE

Document	Parts Into Which Incorporated
Portions of the registrant's definitive proxy statement for use in connection with its annual meeting of shareholders to be held on May 1, 2019, to be filed with the Securities and Exchange Commission ("SEC") on or about March 21, 2019.	Part III

TABLE OF CONTENTS

		Page
PART I		
Item 1.	Business	1
Item 1A.	Risk Factors	5
Item 1B.	Unresolved Staff Comments	10
Item 2.	Properties	11
Item 3.	Legal Proceedings	11
Item 4.	Mine Safety Disclosures	11
PART II		
Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	11
Item 6.	Selected Financial Data	14
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	15
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	56
Item 8.	Financial Statements and Supplementary Data	57
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	113
Item 9A.	Controls and Procedures	113
Item 9B.	Other Information	113
PART III		
Item 10.	Directors, Executive Officers and Corporate Governance	114
Item 11.	Executive Compensation	115
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	115
Item 13.	Certain Relationships and Related Transactions, and Director Independence	115
Item 14.	Principal Accounting Fees and Services	115
PART IV		
Item 15.	Exhibits and Financial Statement Schedules	116
Signatures		122

In this report, "PMI," "we," "us" and "our" refers to Philip Morris International Inc. and its subsidiaries.

PART I

Item 1. *Business.*

General Development of Business

General

Philip Morris International Inc. is a Virginia holding company incorporated in 1987. We are a leading international tobacco company engaged in the manufacture and sale of cigarettes, smoke-free products and associated electronic devices and accessories, and other nicotine-containing products in markets outside the United States of America.

We are leading a transformation in the tobacco industry to create a smoke-free future, based on a new category of reduced-risk products that, while not risk-free, are a much better choice than continuing to smoke. Our goal is to ultimately replace cigarettes with smoke-free products to the benefit of adults who would otherwise continue to smoke, society, the company and its shareholders.

Reduced-risk products ("RRPs") is the term we use to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continued smoking. We have a range of RRPs in various stages of development, scientific assessment and commercialization. Because our RRPs do not burn tobacco, they produce an aerosol that contains far lower quantities of harmful and potentially harmful constituents than found in cigarette smoke. Through multidisciplinary capabilities in product development, state-of-the-art facilities and scientific substantiation, we aim to ensure that our RRPs meet adult consumer preferences and rigorous regulatory requirements.

Our *IQOS* smoke-free product brand portfolio includes heated tobacco and nicotine-containing vapor products. Our leading smoke-free platform is a precisely controlled device into which a specially designed heated tobacco unit is inserted and heated to generate an aerosol. We market our heated tobacco units under the brand names *HEETS*, *HEETS Marlboro* and *HEETS FROM MARLBORO*, defined collectively as *HEETS*, as well as *Marlboro HeatSticks* and *Parliament HeatSticks*. *IQOS* was first introduced in Nagoya, Japan in 2014. To date, *IQOS* is available for sale in 44 markets in key cities or nationwide.

Our cigarettes are sold in more than 180 markets, and in many of these markets they hold the number one or number two market share position. We have a wide range of premium, mid-price and low-price brands. Our portfolio comprises both international and local brands and is led by *Marlboro*, the world's best-selling international cigarette, which accounted for approximately 36% of our total 2018 cigarette shipment volume. *Marlboro* is complemented in the premium-price category by *Parliament*. Our other leading international cigarette brands are *Bond Street, Chesterfield, L&M*, *Lark* and *Philip Morris.* These seven international cigarette brands contributed approximately 76% of our cigarette shipment volume in 2018. We also own a number of important local cigarette brands, such as *Dji Sam Soe*, *Sampoerna A* and *Sampoerna U* in Indonesia; *Fortune* and *Jackpot* in the Philippines; and *Belmont* and *Canadian Classics* in Canada.

Source of Funds — Dividends

We are a legal entity separate and distinct from our direct and indirect subsidiaries. Accordingly, our right, and thus the right of our creditors and stockholders, to participate in any distribution of the assets or earnings of any subsidiary is subject to the prior rights of creditors of such subsidiary, except to the extent that claims of our company itself as a creditor may be recognized. As a holding company, our principal sources of funds, including funds to make payment on our debt securities, are from the receipt of dividends and repayment of debt from our subsidiaries. Our principal wholly owned and majority-owned subsidiaries currently are not limited by long-term debt or other agreements in their ability to pay cash dividends or to make other distributions with respect to their common stock that are otherwise compliant with law.

Description of Business

To provide a greater focus on both parts of our business — combustible and reduced-risk products — and to support our transformation toward a smoke-free future, effective January 1, 2018, we began managing our business in six reportable segments as follows:

- The European Union Region ("EU") is headquartered in Lausanne, Switzerland, and covers all the European Union countries and also Switzerland, Norway and Iceland, which are linked to the European Union through trade agreements;

- The Eastern Europe Region ("EE") is also headquartered in Lausanne and includes Southeast Europe, Central Asia, Ukraine, Israel and Russia;

- The Middle East & Africa Region ("ME&A") is also headquartered in Lausanne and covers the African continent, the Middle East, Turkey and our international duty free business;

- The South & Southeast Asia Region ("S&SA") is headquartered in Hong Kong and includes Indonesia, the Philippines and other markets in this region;

- The East Asia & Australia Region ("EA&A") is also headquartered in Hong Kong and includes Australia, Japan, South Korea, the People's Republic of China and other markets in this region, as well as Malaysia and Singapore; and

- The Latin America & Canada Region ("LA&C") is headquartered in New York and covers the South American continent, Central America, Mexico, the Caribbean and Canada.

Our total shipments, including cigarettes and heated tobacco units, decreased by 2.1% in 2018 to 781.7 billion units. We estimate that international industry volumes, including cigarettes and heated tobacco units, were approximately 5.1 trillion units in 2018, a 0.8% decrease over 2017. Excluding the People's Republic of China ("PRC"), we estimate that the international cigarette and heated tobacco unit volume was 2.8 trillion units in 2018, a 1.6% decrease over 2017. We estimate that our reported share of the international market (which is defined as worldwide cigarette and heated tobacco unit volume, excluding the United States of America) was approximately 15.3% in 2018, 15.2% in 2017 and 15.5% in 2016. Excluding the PRC, we estimate that our reported share of the international market was approximately 28.4%, 27.9%, and 28.1% in 2018, 2017 and 2016, respectively.

Shipments of our principal cigarette brand, *Marlboro*, decreased by 2.2% in 2018 and represented approximately 9.7% of the international cigarette market, excluding the PRC, in 2018, 9.7% in 2017 and 9.6% in 2016.

We have a market share of at least 15% and, in a number of instances, substantially more than 15%, in approximately 100 markets, including Algeria, Argentina, Australia, Austria, Belgium, Brazil, Canada, Canary Islands, the Czech Republic, Egypt, France, Germany, Hong Kong, Indonesia, Israel, Italy, Japan, Korea, Kuwait, Mexico, the Netherlands, the Philippines, Poland, Portugal, Russia, Saudi Arabia, Singapore, Spain, Switzerland, Turkey and Ukraine.

Heated tobacco units is the term we use to refer to heated tobacco consumables, which for us include our *HEETS*, *HEETS Marlboro* and *HEETS FROM MARLBORO*, defined collectively as *HEETS*, as well as *Marlboro HeatSticks* and *Parliament HeatSticks.* Total shipment volume of heated tobacco units reached 41.4 billion units in 2018, up from 36.2 billion units in 2017.

References to total international market, defined as worldwide cigarette and heated tobacco unit volume excluding the United States, total industry, total market and market shares in this Form 10-K are our estimates for tax-paid products based on the latest available data from a number of internal and external sources.

Distribution & Sales

Our main types of distribution are tailored to the characteristics of each market and are often used simultaneously:

- Direct sales and distribution, where we have set up our own distribution selling directly to the retailers (including gas stations and other key accounts);

- Distribution through independent distributors that often distribute other fast-moving consumer goods and are responsible for distribution in a particular market;

- Exclusive zonified distribution, where the distributors are dedicated to us in tobacco products distribution and assigned to exclusive territories within a market;

- Distribution through national or regional wholesalers that then supply the retail trade; and

- Our own brand retail and e-commerce infrastructures for our RRP products and accessories.

Competition

We are subject to highly competitive conditions in all aspects of our business. We compete primarily on the basis of product quality, brand recognition, brand loyalty, taste, R&D, innovation, packaging, customer service, marketing, advertising and retail price and, increasingly, adult smoker willingness to convert to our RRPs. Our competitors include three large international tobacco companies and several regional and local tobacco companies and, in some instances, state-owned tobacco enterprises, principally in Algeria, Egypt, the PRC, Taiwan, Thailand and Vietnam. Industry consolidation and privatizations of state-owned enterprises have led to an overall increase in competitive pressures. Some competitors have different profit and volume objectives, and some international competitors are susceptible to changes in different currency exchange rates. In the combustible product category, we predominantly sell American blend cigarette brands, such as *Marlboro*, *L&M*, *Parliament, Philip Morris* and *Chesterfield*, which are the most popular across many of our markets. In the RRP product category, we predominantly sell *IQOS* devices and heated tobacco units. We seek to compete in all profitable retail price categories, although our brand portfolio is weighted towards the premium-price category.

Procurement and Raw Materials

We purchase tobacco leaf of various types, grades and styles throughout the world, mostly through independent tobacco suppliers. We also contract directly with farmers in several countries, including Argentina, Brazil, Colombia, Ecuador, Italy, Pakistan, the Philippines and Poland. In 2018, direct sourcing from farmers represented approximately 24% of PMI's global leaf requirements. The largest supplies of tobacco leaf are sourced from Argentina, Brazil, China, Italy, Indonesia (mostly for domestic use in kretek products), Malawi, Mozambique, Philippines, Turkey and the United States.

We believe that there is an adequate supply of tobacco leaf in the world markets to satisfy our current and anticipated production requirements.

In addition to tobacco leaf, we purchase a wide variety of direct materials from a total of approximately 500 suppliers. In 2018, our top ten suppliers of direct materials combined represented approximately 50% of our total direct materials purchases. The three most significant direct materials that we purchase are printed paper board used in packaging, acetate tow used in filter making and fine paper used in the manufacturing of cigarettes and heated tobacco units. In addition, the adequate supply and procurement of cloves are of particular importance to our Indonesian business.

The adequate supply chain for our RRP portfolio, including the supply of electronic devices, is important to our business. We work with two electronics manufacturing service providers for the supply of our *IQOS* devices and a small number of other providers for other products in our RRP portfolio and related accessories. Although we work closely with these service providers on monitoring their production capability and financial health, the commercialization of our RRPs could be adversely affected if they are unable to meet their commitments. The production of our RRP portfolio requires various metals, and we believe that there is an adequate supply of such metals in the world markets to satisfy our current and anticipated production requirements. However, some components and materials necessary for the production of our RRPs are obtained from single or limited sources, and can be subject to industry-wide shortages and price fluctuations. Our inability to secure an adequate supply of such components and materials could negatively impact the commercialization of our RRPs.

Our *IQOS* devices are subject to product warranties, which are described in more detail in Item 8. *Financial Statements and Supplementary Data* of this Annual Report on Form 10-K ("Item 8") in Note 5. *Product Warranty* to our consolidated financial statements. We discuss our RRP products in more detail in Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations* of this Annual Report on Form 10-K ("Item 7") in *Business Environment—Reduced Risk Products*.

Business Environment

Information called for by this Item is hereby incorporated by reference to the paragraphs in Item 7, *Business Environment*.

Other Matters

Customers

As described in more detail in "*Distribution & Sales*" above, in many of our markets we sell our products to distributors. In 2018, sales to a distributor in the European Union Region and a distributor in the East Asia & Australia Region each amounted to 10 percent or more of our consolidated net revenues. See Item 8, Note 12. *Segment Reporting* for more information. We believe that none of our business segments is dependent upon a single customer or a few customers, the loss of which would have a material adverse effect on our consolidated results of operations. In some of our markets, particularly in the European Union and in the East Asia & Australia Regions, a loss of a distributor may result in a temporary market disruption.

Employees

At December 31, 2018, we employed approximately 77,400 people worldwide, including full-time, temporary and part-time staff. Our businesses are subject to a number of laws and regulations relating to our relationship with our employees. Generally, these laws and regulations are specific to the location of each business. In addition, in accordance with European Union requirements, we have established a European Works Council composed of management and elected members of our workforce. We believe that our relations with our employees and their representative organizations are excellent.

Executive Officers of the Registrant

The disclosure regarding executive officers is set forth under the heading "Executive Officers as of February 7, 2019" in Item 10. *Directors, Executive Officers and Corporate Governance* of this Annual Report on Form 10-K ("Item 10").

Intellectual Property

Our trademarks are valuable assets, and their protection and reputation are essential to us. We own the trademark rights to all of our principal brands, including *Marlboro* and *IQOS*, or have the right to use them in all countries where we use them.

In addition, we have approximately 10,300 granted patents worldwide and approximately 9,300 pending patent applications. Our patent portfolio, as a whole, is material to our business. However, no one patent, or group of related patents, is material to us. We also have registered industrial designs, as well as unregistered proprietary trade secrets, technology, know-how, processes and other unregistered intellectual property rights.

Effective January 1, 2008, PMI entered into an Intellectual Property Agreement with Philip Morris USA Inc. ("PM USA"). The Intellectual Property Agreement allocates ownership of jointly funded intellectual property as follows:

- PMI owns all rights to jointly funded intellectual property outside the United States, its territories and possessions; and
- PM USA owns all rights to jointly funded intellectual property in the United States, its territories and possessions.

The parties agreed to submit disputes under the Intellectual Property Agreement first to negotiation between senior executives and then to binding arbitration.

Seasonality

Our business segments are not significantly affected by seasonality, although in certain markets cigarette consumption trends rise during the summer months due to longer daylight time and tourism.

Environmental Regulation

We are subject to international, national and local environmental laws and regulations in the countries in which we do business. We have specific programs across our business units designed to meet applicable environmental compliance requirements and reduce our carbon footprint and wastage as well as water and energy consumption. We report externally about our climate change mitigation strategy, together with associated targets and results in reducing our carbon footprint, through CDP (formerly, the Carbon Disclosure Project), the leading international non-governmental organization assessing the work of thousands of companies worldwide in the area of climate change. Our environmental and occupational health and safety management system includes policies, standard practices and procedures at all our manufacturing centers. We also conduct regular safety assessments at our offices, warehouses and car fleet organizations. Furthermore, we have engaged an external certification body to validate the effectiveness of this management system at our manufacturing centers around the world, in accordance with internationally recognized standards for safety and environmental management. The environmental performance data we report externally is also verified by a qualified third party. Our subsidiaries expect to continue to make investments in order to drive improved performance and maintain compliance with environmental laws and regulations. We assess and report the compliance status of all our legal entities on a regular basis. Based on the management and controls we have in place and our review of climate change risks (both physical and regulatory), environmental expenditures have not had, and are not expected to have, a material adverse effect on our consolidated results of operations, capital expenditures, financial position, earnings or competitive position.

Available Information

We are required to file with the SEC annual, quarterly and current reports, proxy statements and other information required by the Securities Exchange Act of 1934, as amended (the "Exchange Act"). The SEC maintains an Internet website at http://www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, from which investors can electronically access our SEC filings.

We make available free of charge on, or through, our website at www.pmi.com our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. Investors can access our filings with the SEC by visiting www.pmi.com.

The information on our website is not, and shall not be deemed to be, a part of this report or incorporated into any other filings we make with the SEC.

Item 1A. *Risk Factors.*

The following risk factors should be read carefully in connection with evaluating our business and the forward-looking statements contained in this Annual Report on Form 10-K. Any of the following risks could materially adversely affect our business, our operating results, our financial condition and the actual outcome of matters as to which forward-looking statements are made in this Annual Report on Form 10-K.

Forward-Looking and Cautionary Statements

We may from time to time make written or oral forward-looking statements, including statements contained in this Annual Report on Form 10-K and other filings with the SEC, in reports to stockholders and in press releases and investor webcasts. You can identify these forward-looking statements by use of words such as "strategy," "expects," "continues," "plans," "anticipates," "believes," "will," "estimates," "intends," "projects," "goals," "targets" and other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts.

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Our RRPs constitute a new product category in its early stages that is less predictable than our mature cigarette business. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from those anticipated, estimated or projected. Investors should bear this in mind as they consider forward-looking statements and whether to invest in or remain invested in our securities. In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995,

we are identifying important factors that, individually or in the aggregate, could cause actual results and outcomes to differ materially from those contained in any forward-looking statements made by us; any such statement is qualified by reference to the following cautionary statements. We elaborate on these and other risks we face throughout this document, particularly in Item 7, *Business Environment*. You should understand that it is not possible to predict or identify all risk factors. Consequently, you should not consider the following to be a complete discussion

of all potential risks or uncertainties. We do not undertake to update any forward-looking statement that we may make from time to time, except in the normal course of our public disclosure obligations.

Risks Related to Our Business and Industry

- **Consumption of tax-paid cigarettes continues to decline in many of our markets.**

This decline is due to multiple factors, including increased taxes and pricing, governmental actions, the diminishing social acceptance of smoking, continuing economic and geopolitical uncertainty, and the continuing prevalence of illicit products. These factors and their potential consequences are discussed more fully below and in Item 7, *Business Environment*.

- **Cigarettes are subject to substantial taxes. Significant increases in cigarette-related taxes have been proposed or enacted and are likely to continue to be proposed or enacted in numerous jurisdictions. These tax increases may disproportionately affect our profitability and make us less competitive versus certain of our competitors.**

Tax regimes, including excise taxes, sales taxes and import duties, can disproportionately affect the retail price of cigarettes versus other combustible tobacco products, or disproportionately affect the relative retail price of our cigarette brands versus cigarette brands manufactured by certain of our competitors. Because our portfolio is weighted toward the premium-price cigarette category, tax regimes based on sales price can place us at a competitive disadvantage in certain markets. As a result, our volume and profitability may be adversely affected in these markets.

Increases in cigarette taxes are expected to continue to have an adverse impact on our sales of cigarettes, due to resulting lower consumption levels, a shift in sales from manufactured cigarettes to other combustible tobacco products and from the premium-price to the mid-price or low-price cigarette categories, where we may be under-represented, from local sales to legal cross-border purchases of lower price products, or to illicit products such as contraband, counterfeit and "illicit whites."

- **Our business faces significant governmental action aimed at increasing regulatory requirements with the goal of reducing or preventing the use of tobacco products.**

Governmental actions, combined with the diminishing social acceptance of smoking and private actions to restrict smoking, have resulted in reduced industry volume in many of our markets, and we expect that such factors will continue to reduce consumption levels and will increase down-trading and the risk of counterfeiting, contraband, "illicit whites" and legal cross-border purchases. Significant regulatory developments will continue to take place over the next few years in most of our markets, driven principally by the World Health Organization's Framework Convention on Tobacco Control ("FCTC"). Since it came into force in 2005, the FCTC has led to increased efforts by tobacco control advocates and public health organizations to promote increasingly restrictive regulatory measures on the marketing and sale of tobacco products to adult smokers. Regulatory initiatives that have been proposed, introduced or enacted include:

- restrictions on or licensing of outlets permitted to sell cigarettes;
- the levying of substantial and increasing tax and duty charges;
- restrictions or bans on advertising, marketing and sponsorship;
- the display of larger health warnings, graphic health warnings and other labeling requirements;
- restrictions on packaging design, including the use of colors, and plain packaging;
- restrictions on packaging and cigarette formats and dimensions;
- restrictions or bans on the display of tobacco product packaging at the point of sale and restrictions or bans on cigarette vending machines;

- requirements regarding testing, disclosure and performance standards for tar, nicotine, carbon monoxide and other smoke constituents;
- disclosure, restrictions, or bans of tobacco product ingredients;
- increased restrictions on smoking in public and work places and, in some instances, in private places and outdoors;
- regulation, restrictions or prohibitions of novel tobacco or nicotine-containing products;
- elimination of duty free sales and duty free allowances for travelers;
- encouraging litigation against tobacco companies; and
- excluding tobacco companies from transparent public dialogue regarding public health and other policy matters.

Our financial results could be significantly affected by regulatory initiatives resulting in a significant decrease in demand for our brands, in particular requirements that lead to a commoditization of tobacco products or impede adult consumers' ability to convert to our RRPs, as well as any significant increase in the cost of complying with new regulatory requirements.

- **Litigation related to tobacco use and exposure to environmental tobacco smoke could substantially reduce our profitability and could severely impair our liquidity.**

There is litigation related to tobacco products pending in certain jurisdictions. Damages claimed in some tobacco-related litigation are significant and, in certain cases in Brazil, Canada, Israel and Nigeria, range into the billions of U.S. dollars. We anticipate that new cases will continue to be filed. The FCTC encourages litigation against tobacco product manufacturers. It is possible that our consolidated results of operations, cash flows or financial position could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. See Item 8, Note 18. *Contingencies* to our condensed consolidated financial statements for a discussion of pending litigation and Item 7, *Business Environment—Reduced-Risk Products (RRPs)—Legal Challenges to RRPs.*

- **We face intense competition, and our failure to compete effectively could have a material adverse effect on our profitability and results of operations.**

We compete primarily on the basis of product quality, brand recognition, brand loyalty, taste, R&D, innovation, packaging, customer service, marketing, advertising and retail price and, increasingly, adult smoker willingness to convert to our RRPs. We are subject to highly competitive conditions in all aspects of our business. The competitive environment and our competitive position can be significantly influenced by weak economic conditions, erosion of consumer confidence, competitors' introduction of lower-price products or innovative products, higher tobacco product taxes, higher absolute prices and larger gaps between retail price categories, and product regulation that diminishes the ability to differentiate tobacco products and restricts adult consumer access to truthful and non-misleading information about our RRPs. Competitors include three large international tobacco companies, new market entrants, particularly with respect to innovative products, several regional and local tobacco companies and, in some instances, state-owned tobacco enterprises, principally in Algeria, Egypt, the PRC, Taiwan, Thailand and Vietnam. Industry consolidation and privatizations of state-owned enterprises have led to an overall increase in competitive pressures. Some competitors have different profit and volume objectives, and some international competitors are susceptible to changes in different currency exchange rates. Certain new market entrants may alienate consumers from innovative products through inappropriate marketing campaigns and messaging and inferior product satisfaction, while not relying on scientific substantiation based on appropriate R&D protocols and standards. The growing use of digital media could increase the speed and extent of the dissemination of inaccurate and misleading information about our RRPs.

- **Because we have operations in numerous countries, our results may be influenced by economic, regulatory and political developments, natural disasters, pandemics or conflicts.**

Some of the countries in which we operate face the threat of civil unrest and can be subject to regime changes. In others, nationalization, terrorism, conflict and the threat of war may have a significant impact on the business environment. Natural disasters, pandemics, economic, political, regulatory or other developments could disrupt our supply chain, manufacturing capabilities or distribution capabilities. In addition, such developments could lead to loss of property or equipment that are critical to our business in certain markets and difficulty in staffing and managing our operations, which could reduce our volumes, revenues and net earnings.

In certain markets, we are dependent on governmental approvals of various actions such as price changes, and failure to obtain such approvals could impair growth of our profitability.

In addition, despite our high ethical standards and rigorous control and compliance procedures aimed at preventing and detecting unlawful conduct, given the breadth and scope of our international operations, we may not be able to detect all potential improper or unlawful conduct by our employees and partners.

- **We may be unable to anticipate changes in adult consumer preferences.**

Our business is subject to changes in adult consumer preferences, which may be influenced by local economic conditions. To be successful, we must:

- promote brand equity successfully;
- anticipate and respond to new adult consumer trends;
- develop new products and markets and broaden brand portfolios;
- improve productivity;
- convince adult smokers to convert to our RRPs;
- ensure adequate production capacity to meet demand for our products; and
- be able to protect or enhance margins through price increases.

In periods of economic uncertainty, adult consumers may tend to purchase lower-price brands, and the volume of our premium-price and mid-price brands and our profitability could suffer accordingly. Such down-trading trends may be reinforced by regulation that limits branding, communication and product differentiation.

- **The financial and business performance of our reduced-risk products is less predictable than our cigarette business.**

Our RRPs are novel products in a new category, and the pace at which adult smokers adopt them may vary, depending on the competitive, regulatory, fiscal and cultural environment, and other factors in a specific market. There may be periods of accelerated growth and periods of slower growth for these products, the timing and drivers of which may be more difficult for us to predict versus our mature cigarette business. The impact of this lower predictability on our projected results for a specific period may be significant, particularly during the early stages of this new product category.

- **We lose revenues as a result of counterfeiting, contraband, cross-border purchases, "illicit whites," non-tax-paid volume produced by local manufacturers, and counterfeiting of our *IQOS* device and heated tobacco units.**

Large quantities of counterfeit cigarettes are sold in the international market. We believe that *Marlboro* is the most heavily counterfeited international cigarette brand, although we cannot quantify the revenues we lose as a result of this activity. In addition, our revenues are reduced by contraband, legal cross-border purchases, "illicit whites" and non-tax-paid volume produced by local manufacturers. Our revenues and consumer satisfaction with our *IQOS* device and heated tobacco units may be adversely affected by counterfeit products that do not meet our product quality standards and scientific validation procedures.

- **From time to time, we are subject to governmental investigations on a range of matters.**

Investigations include allegations of contraband shipments of cigarettes, allegations of unlawful pricing activities within certain markets, allegations of underpayment of customs duties and/or excise taxes, allegations of false and misleading usage of descriptors and allegations of unlawful advertising. We cannot predict the outcome of those investigations or whether additional investigations may be commenced, and it is possible that our business could be materially affected by an unfavorable outcome of pending or future investigations. See Item, 8, Note 18. *Contingencies—Other Litigation* and Item 7, *Business Environment—Governmental Investigations* for a description of certain governmental investigations to which we are subject.

- **We may be unsuccessful in our attempts to introduce reduced-risk products, and regulators may not permit the commercialization of these products or the communication of scientifically substantiated risk-reduction claims.**

Our key strategic priorities are: to develop and commercialize products that present less risk of harm to adult smokers who switch to those products versus continued smoking; and to convince current adult smokers who would otherwise continue to smoke to switch to those RRPs. For our efforts to be successful, we must: develop RRPs that such adult smokers find acceptable alternatives to smoking; conduct rigorous scientific studies to substantiate that they reduce exposure to harmful and potentially harmful constituents in smoke and, ultimately, that these products present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to them versus continued smoking; and effectively advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs, including communication of scientifically substantiated information to enable adult smokers to make better consumer choices. We might not succeed in our efforts. If we do not succeed, but others do, we may be at a competitive disadvantage. Furthermore, we cannot predict whether regulators will permit the sale and/or marketing of RRPs with scientifically substantiated risk-reduction claims. Such restrictions could limit the success of our RRPs.

- **We may be unsuccessful in our efforts to differentiate reduced-risk products and cigarettes with respect to taxation.**

To date, we have been largely successful in demonstrating to regulators that our RRPs are not cigarettes, and as such they are generally taxed either as a separate category or as other tobacco products, which typically yields more favorable tax rates than cigarettes. If we cease to be successful in these efforts, RRP unit margins may be adversely affected.

- **Our reported results could be adversely affected by unfavorable currency exchange rates, and currency devaluations could impair our competitiveness.**

We conduct our business primarily in local currency and, for purposes of financial reporting, the local currency results are translated into U.S. dollars based on average exchange rates prevailing during a reporting period. During times of a strengthening U.S. dollar, our reported net revenues, operating income and EPS will be reduced because the local currency translates into fewer U.S. dollars. During periods of local economic crises, foreign currencies may be devalued significantly against the U.S. dollar, reducing our margins. Actions to recover margins may result in lower volume and a weaker competitive position.

- **Changes in the earnings mix and changes in tax laws may result in significant variability in our effective tax rates. Our ability to receive payments from foreign subsidiaries or to repatriate royalties and dividends could be restricted by local country currency exchange controls.**

The Tax Cuts and Jobs Act that was signed into law in December 2017 constitutes a major change to the U.S. tax system. Our estimated impact of the Tax Cuts and Jobs Act is based on management's current interpretations, and our analysis is ongoing. Our final tax liability may be materially different from current estimates due to developments such as implementing regulations and clarifications. In future periods, our effective tax rate and our ability to recover deferred tax assets could be subject to additional uncertainty as a result of such developments. Furthermore, changes in the earnings mix or applicable foreign tax laws may result in significant variability in our effective tax rates. Because we are a U.S. holding company, our most significant source of funds is distributions from our non-U.S. subsidiaries. Certain countries in which we operate have adopted or could institute currency exchange controls that limit or prohibit our local subsidiaries' ability to convert local currency into U.S. dollars or to make payments outside the country. This could subject us to the risks of local currency devaluation and business disruption.

- **Our ability to grow profitability may be limited by our inability to introduce new products, enter new markets or improve our margins through higher pricing and improvements in our brand and geographic mix.**

Our profit growth may suffer if we are unable to introduce new products or enter new markets successfully, to raise prices or to improve the proportion of our sales of higher margin products and in higher margin geographies.

- **We may be unable to expand our brand portfolio through successful acquisitions or the development of strategic business relationships.**

One element of our growth strategy is to strengthen our brand portfolio and market positions through selective acquisitions and the development of strategic business relationships. Acquisition and strategic business development opportunities are limited and present risks of failing to achieve efficient and effective integration, strategic objectives and anticipated revenue improvements and cost savings. There is no assurance that we will be able to acquire attractive businesses on favorable terms, or that future acquisitions or strategic business developments will be accretive to earnings.

- **Government mandated prices, production control programs, shifts in crops driven by economic conditions and the impact of climate change may increase the cost or reduce the quality of the tobacco and other agricultural products used to manufacture our products.**

As with other agricultural commodities, the price of tobacco leaf and cloves can be influenced by imbalances in supply and demand, and crop quality can be influenced by variations in weather patterns, including those caused by climate change. Tobacco production in certain countries is subject to a variety of controls, including government mandated prices and production control programs. Changes in the patterns of demand for agricultural products could cause farmers to produce less tobacco or cloves. Any significant change in tobacco leaf and clove prices, quality and quantity could affect our profitability and our business.

- **Our ability to achieve our strategic goals may be impaired if we fail to attract and retain the best global talent.**

To be successful, we must continue transforming our culture and ways of working, align our talent with our business needs, innovate and transform to a consumer-centric business. We compete for talent, including in areas that are new to us, such as digital and technical solutions, with companies in the consumer products, technology and other sectors that enjoy greater societal acceptance. As a result, we may be unable to attract and retain the best global talent with the right degree of diversity, experience and skills to achieve our strategic goals.

- **The failure of our information systems to function as intended or their penetration by outside parties with the intent to corrupt them or our failure to comply with privacy laws and regulations could result in business disruption, litigation and regulatory action, and loss of revenue, assets or personal or other confidential data.**

We use information systems to help manage business processes, collect and interpret data and communicate internally and externally with employees, suppliers, consumers, customers and others. Some of these information systems are managed by third-party service providers. We have backup systems and business continuity plans in place, and we take care to protect our systems and data from unauthorized access. Nevertheless, failure of our systems to function as intended, or penetration of our systems by outside parties intent on extracting or corrupting information or otherwise disrupting business processes, could place us at a competitive disadvantage, result in a loss of revenue, assets or personal or other sensitive data, litigation and regulatory action, cause damage to our reputation and that of our brands and result in significant remediation and other costs. Failure to protect personal data, respect the rights of data subjects, and adhere to strict cybersecurity protocols could subject us to substantial fines and other legal challenges under regulations such as the EU General Data Protection Regulation. As we are increasingly relying on digital platforms in our business, the magnitude of these risks is likely to increase.

- **We may be required to replace third-party contract manufacturers or service providers with our own resources.**

In certain instances, we contract with third parties to manufacture some of our products or product parts or to provide other services. We may be unable to renew these agreements on satisfactory terms for numerous reasons, including government regulations. Accordingly, our costs may increase significantly if we must replace such third parties with our own resources.

Item 1B. *Unresolved Staff Comments.*

None.

Item 2. *Properties.*

At December 31, 2018, we operated and owned 44 manufacturing facilities and maintained contract manufacturing relationships with 26 third-party manufacturers across 23 markets. In addition, we work with 38 third-party operators in Indonesia who manufacture our hand-rolled cigarettes.

PMI-Owned Manufacturing Facilities

	EU [1]	EE [1]	ME&A	S&SA	EA&A [1]	LA&C	TOTAL
Fully integrated	8	5	3	8	1	6	31
Make-pack	2	—	—	1	—	2	5
Other	3	—	1	1	1	2	8
Total	13	5	4	10	2	10	44

[1] Includes facilities that produced heated tobacco units in 2018.

In 2018, 23 of our facilities each manufactured over 10 billion units (cigarettes and heated tobacco units combined), of which eight facilities each produced over 30 billion units. Our largest factories are in Karawang and Sukorejo (Indonesia), Izmir (Turkey), St. Petersburg and Krasnodar (Russia), Krakow (Poland), Batangas and Marikina (Philippines), Berlin (Germany), Crespellano (Italy), and Klaipeda (Lithuania). Our smallest factories are mostly in Latin America and Asia, where due to tariff and other constraints we have established small manufacturing units in individual markets. We will continue to optimize our manufacturing base.

The plants and properties owned or leased and operated by our subsidiaries are maintained in good condition and are believed to be suitable and adequate for our present needs.

We are integrating the production of heated tobacco units into a number of our existing manufacturing facilities and progressing with our plans to build manufacturing capacity for our other RRP platforms.

Item 3. *Legal Proceedings.*

The information called for by this Item is incorporated herein by reference to Item 8, Note 18. *Contingencies*.

Item 4. *Mine Safety Disclosures.*

Not applicable.

PART II

Item 5. *Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.*

The principal stock exchange on which our common stock (no par value) is listed is the New York Stock Exchange (ticker symbol "PM"). At January 31, 2019, there were approximately 54,100 holders of record of our common stock.

Performance Graph

The graph below compares the cumulative total shareholder return on PMI's common stock with the cumulative total return for the same period of PMI's Peer Group and the S&P 500 Index. The graph assumes the investment of $100 as of December 31, 2013, in PMI common stock (at prices quoted on the New York Stock Exchange) and each of the indices as of the market close and reinvestment of dividends on a quarterly basis.

chart-fc8da3dafbd95b5eb4ba09.jpg

Date	PMI	PMI Peer Group [1]	S&P 500 Index
December 31, 2013	$100.00	$100.00	$100.00
December 31, 2014	$97.90	$107.80	$113.70
December 31, 2015	$111.00	$116.80	$115.30
December 31, 2016	$120.50	$118.40	$129.00
December 31, 2017	$144.50	$140.50	$157.20
December 31, 2018	$96.50	$127.70	$150.30

[1] The PMI Peer Group presented in this graph is the same as that used in the prior year. The PMI Peer Group was established based on a review of four characteristics: global presence; a focus on consumer products; and net revenues and a market capitalization of a similar size to those of PMI. The review also considered the primary international tobacco companies. As a result of this review, the following companies constitute the PMI Peer Group: Altria Group, Inc., Anheuser-Busch InBev SA/NV, British American Tobacco p.l.c., The Coca-Cola Company, Colgate-Palmolive Co., Diageo plc, Heineken N.V., Imperial Brands PLC, Japan Tobacco Inc., Johnson & Johnson, Kimberly-Clark Corporation, The Kraft-Heinz Company, McDonald's Corp., Mondelēz International, Inc., Nestlé S.A., PepsiCo, Inc., The Procter & Gamble Company, Roche Holding AG, and Unilever NV and PLC.

Note: Figures are rounded to the nearest $0.10.

Issuer Purchases of Equity Securities During the Quarter Ended December 31, 2018

Our share repurchase activity for each of the three months in the quarter ended December 31, 2018, was as follows:

Period	Total Number of Shares Repurchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Programs
October 1, 2018 – October 31, 2018 (1)	—	$ —	—	$ —
November 1, 2018 – November 30, 2018 (1)	—	$ —	—	$ —
December 1, 2018 – December 31, 2018 (1)	—	$ —	—	$ —
Pursuant to Publicly Announced Plans or Programs	—	$ —		
October 1, 2018 – October 31, 2018 (2)	439	$ 82.22		
November 1, 2018 – November 30, 2018 (2)	872	$ 88.80		
December 1, 2018 – December 31, 2018 (2)	1,482	$ 72.28		
For the Quarter Ended December 31, 2018	2,793	$ 79.00		

(1) During this reporting period, we did not have an authorized share repurchase program.

(2) Shares repurchased represent shares tendered to us by employees who vested in restricted share unit awards and used shares to pay all, or a portion of, the related taxes.

Item 6. *Selected Financial Data*

(in millions of dollars, except per share data)

	2018	2017	2016	2015	2014
Summary of Operations:					
Revenues including excise taxes	**$ 79,823**	$ 78,098	$ 74,953	$ 73,908	$ 80,106
Excise taxes on products	**50,198**	49,350	48,268	47,114	50,339
Net revenues [1]	**29,625**	28,748	26,685	26,794	29,767
Operating income [1]	**11,377**	11,581	10,903	10,745	11,787
Net earnings attributable to PMI	**7,911**	6,035	6,967	6,873	7,493
Basic earnings per share	**5.08**	3.88	4.48	4.42	4.76
Diluted earnings per share	**5.08**	3.88	4.48	4.42	4.76
Dividends declared per share	**4.49**	4.22	4.12	4.04	3.88
Total assets	**39,801**	42,968	36,851	33,956	35,187
Long-term debt [2]	**26,975**	31,334	25,851	25,250	26,929
Total debt	**31,759**	34,339	29,067	28,480	29,455

[1] Certain prior years' amounts in the table above have been reclassified to conform with the current year's presentation, due primarily to new accounting guidance related to revenue recognition and pension costs. For further details, see Item 8, Note 2. *Summary of Significant Accounting Policies* - Revenue Recognition, Item 8, Note 13. *Benefit Plans* and Item 8, Note 21. *New Accounting Standards*.

[2] Excluding current portion of long-term debt.

This Selected Financial Data should be read in conjunction with Item 7 and Item 8.

Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations.*

The following discussion should be read in conjunction with the other sections of this Annual Report on Form 10-K, including the consolidated financial statements and related notes contained in Item 8, and the discussion of risks and cautionary factors that may affect future results in Item 1A. *Risk Factors*.

Description of Our Company

We are leading a transformation in the tobacco industry to create a smoke-free future and ultimately replace cigarettes with smoke-free products to the benefit of adults who would otherwise continue to smoke, society, the company and its shareholders. We are a leading international tobacco company engaged in the manufacture and sale of cigarettes, smoke-free products and associated electronic devices and accessories, and other nicotine-containing products in markets outside the United States of America. We are building a future on a new category of smoke-free products that, while not risk-free, are a much better choice than continuing to smoke. Through multidisciplinary capabilities in product development, state-of-the-art facilities and scientific substantiation, we aim to ensure that our smoke-free products meet adult consumer preferences and rigorous regulatory requirements. Our *IQOS* smoke-free product brand portfolio includes heated tobacco and nicotine-containing vapor products.

To provide a greater focus on both parts of our business — combustible and reduced-risk products — and to support our transformation toward a smoke-free future, effective January 1, 2018, we began managing our business in six reportable segments as follows:

- European Union ("EU");
- Eastern Europe ("EE");
- Middle East & Africa ("ME&A"), which includes our international duty free business;
- South & Southeast Asia ("S&SA");
- East Asia & Australia ("EA&A"); and
- Latin America & Canada ("LA&C").

Our cigarettes are sold in more than 180 markets, and in many of these markets they hold the number one or number two market share position. We have a wide range of premium, mid-price and low-price brands. Our portfolio comprises both international and local brands. In addition to the manufacture and sale of cigarettes, we are engaged in the development and commercialization of reduced-risk products ("RRPs"). RRPs is the term we use to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continued smoking.

We use the term net revenues to refer to our operating revenues from the sale of our products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. As discussed in Item 8, Note 21. *New Accounting Standards*, on January 1, 2018, we adopted Financial Accounting Standards Update ASU 2014-09, "Revenue from Contracts with Customers." We adopted this standard retrospectively to each prior period presented. We made an accounting policy election to exclude excise taxes collected from customers from the measurement of the transaction price, thereby presenting revenues net of excise taxes in all prior periods. Our net revenues and operating income are affected by various factors, including the volume of products we sell, the price of our products, changes in currency exchange rates and the mix of products we sell. Mix is a term used to refer to the proportionate value of premium-price brands to mid-price or low-price brands in any given market (product mix). Mix can also refer to the proportion of shipment volume in more profitable markets versus shipment volume in less profitable markets (geographic mix).

Our cost of sales consists principally of: tobacco leaf, non-tobacco raw materials, labor and manufacturing costs; shipping and handling costs; and the cost of the *IQOS* devices produced by third-party electronics manufacturing

service providers. Estimated costs associated with *IQOS* warranty programs are generally provided for in cost of sales in the period the related revenues are recognized.

Our marketing, administration and research costs include the costs of marketing and selling our products, other costs generally not related to the manufacture of our products (including general corporate expenses), and costs incurred to develop new products. The most significant components of our marketing, administration and research costs are marketing and sales expenses and general and administrative expenses.

Philip Morris International Inc. is a legal entity separate and distinct from its direct and indirect subsidiaries. Accordingly, our right, and thus the right of our creditors and stockholders, to participate in any distribution of the assets or earnings of any subsidiary is subject to the prior rights of creditors of such subsidiary, except to the extent that claims of our company itself as a creditor may be recognized. As a holding company, our principal sources of funds, including funds to make payment on our debt securities, are from the receipt of

dividends and repayment of debt from our subsidiaries. Our principal wholly owned and majority-owned subsidiaries currently are not limited by long-term debt or other agreements in their ability to pay cash dividends or to make other distributions with respect to their common stock that are otherwise compliant with law.

Executive Summary

The following executive summary provides significant highlights from the Discussion and Analysis that follows.

Consolidated Operating Results

- **Net Revenues –** Net revenues of $29.6 billion for the year ended December 31, 2018, increased by $0.9 billion, or 3.1%, from the comparable 2017 amount. The change in our net revenues from the comparable 2017 amount was driven by the following:

  chart-d755157f6b66b6d4cc3a09.jpg

  Net revenues, excluding unfavorable currency, increased by 3.4%, reflecting: a favorable pricing variance, notably in Argentina, Australia, Canada, Egypt, Germany, Indonesia, Italy, Japan, Mexico, the Philippines, Russia, Turkey, and Ukraine, partly offset by France, Korea, Saudi Arabia and Thailand; as well as a favorable "Other" variance attributable to 2018 fees for certain distribution rights billed to customers in certain markets in the ME&A Region.

  These favorable variances were partly offset by unfavorable volume/mix, primarily reflecting unfavorable cigarette volume/mix, notably in Australia, the Gulf Cooperation Council ("GCC"), notably Saudi Arabia and the United Arab Emirates ("UAE"), Indonesia, Italy, Japan and Russia, partly offset by Pakistan, Thailand and Turkey. The unfavorable cigarette volume/mix was partly offset by favorable heated tobacco unit volume in the EU, notably the Czech Republic, Germany and Italy, as well as Korea, PMI Duty Free and Russia, partly offset by unfavorable heated tobacco unit volume in Japan, reflecting the net impact of estimated distributor inventory movements.

  Net revenues by product category for the years ended December 31, 2018 and 2017, are shown below:

  chart-259bafaa39775a140d4a09.jpg chart-d2d6b5aa51af2f21f32.jpg

- **Diluted Earnings Per Share** – The changes in our reported diluted earnings per share ("diluted EPS") for the year ended December 31, 2018, from the comparable 2017 amounts, were as follows:

	Diluted EPS	% Growth (Decline)
For the year ended December 31, 2017	$ 3.88	
2017 Asset impairment and exit costs	—	
2017 Tax items	0.84	
Subtotal of 2017 items	0.84	
2018 Asset impairment and exit costs	—	
2018 Tax items	(0.02)	
Subtotal of 2018 items	(0.02)	
Currency	(0.11)	
Interest	0.13	
Change in tax rate	0.40	
Operations	(0.04)	
For the year ended December 31, 2018	$ 5.08	30.9 %

Income Taxes – Our effective income tax rate for 2018 decreased by 17.8 percentage points to 22.9%. The 2018 tax items that decreased our 2018 diluted EPS by $0.02 per share in the table above represented a current income tax charge of $185 million primarily due to an increase in our final 2017 transition tax liability, mostly offset by a deferred income tax benefit of $154 million primarily due to the recognition of deferred tax assets for net operating losses in the state of New York. The 2017 tax items that decreased our 2017 diluted EPS by $0.84 per share in the table above were primarily due to the impact of the Tax Cuts and Jobs Act, which was signed into law in December 2017. The change in the effective tax rate that increased our diluted EPS by $0.40 per share in the table above was primarily due to the impact from the Tax Cuts and Jobs Act, which reduced the U.S. federal income tax rate from 35% to 21%, in addition to repatriation cost differences and earnings mix by taxing jurisdiction. For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements.

Currency – The unfavorable currency impact during 2018 results from the fluctuations of the U.S. dollar, especially against the Indonesian rupiah, Russian ruble and Turkish lira, partially offset by the Euro and Japanese yen. This unfavorable currency movement has impacted our profitability across our primary revenue markets and local currency cost bases.

Interest – The favorable impact of interest was due primarily to our ongoing efforts to optimize our capital structure following the passage of the Tax Cuts and Jobs Act. This included the decision to use existing cash to repay the $2.5 billion principal for our matured May 2018 ten-year U.S. bond, which had a coupon of 5.65%.

Operations – The decrease in diluted EPS of $0.04 from our operations in the table above was due primarily to the following segments:

- East Asia & Australia: Unfavorable volume/mix and higher marketing, administration and research costs, partially offset by lower manufacturing costs and favorable pricing;

partially offset by

- South & Southeast Asia: Favorable pricing, partially offset by unfavorable volume/mix, higher marketing, administration and research costs, and higher manufacturing costs;

- Latin America & Canada: Favorable pricing, partially offset by unfavorable volume/mix and higher marketing, administration and research costs;

- Eastern Europe: Favorable pricing, partially offset by unfavorable volume/mix and higher marketing, administration and research costs;

- European Union: Favorable pricing and favorable volume/mix, partially offset by higher marketing, administration and research costs, and higher manufacturing costs; and

- Middle East & Africa: Favorable pricing, favorable volume/mix and lower marketing, administration and research costs, partially offset by higher manufacturing costs.

For further details, see the *Consolidated Operating Results* and *Operating Results by Business Segment* sections of the following *Discussion and Analysis*.

Tax Items and Impact of U.S. Tax Reform

We completed our analysis of the Tax Cuts and Jobs Act during 2018 and adjusted the 2017 provisional estimates to the final amounts based on our 2017 U.S. federal income tax return as filed. Accordingly, in the fourth quarter 2018, we recorded in our income tax provision a charge of $31 million representing a current income tax charge of $185 million, primarily due to an increase in our aggregate foreign cash position used to determine our final 2017 transition tax liability, mostly offset by a deferred income tax benefit of $154 million primarily due to the recognition of deferred tax assets for net operating losses in the state of New York. Updates to the provisional estimates have been recorded in accordance with Staff Accounting Bulletin No. 118 ("SAB 118").

We estimate that our 2019 effective tax rate will be approximately 23%, reflecting the current analysis, interpretation and clarifications of the scope and impact of the Tax Cuts and Jobs Act.

The Tax Cuts and Jobs Act has significant complexity, and our final full-year effective tax rate may differ from this estimate, due to, among other things, additional guidance that may be issued by the U.S. Treasury Department and the Internal Revenue Service, related interpretations and clarifications of tax law, in addition to repatriation costs differences and earnings mix by taxing jurisdiction.

Discussion and Analysis

Critical Accounting Estimates

Item 8, Note 2. *Summary of Significant Accounting Policies* to our consolidated financial statements includes a summary of the significant accounting policies and methods used in the preparation of our consolidated financial statements. In most instances, we must use a particular accounting policy or method because it is the only one that is permitted under U.S. GAAP.

The preparation of financial statements requires that we use estimates and assumptions that affect the reported amounts of our assets, liabilities, net revenues and expenses, as well as our disclosure of contingencies. If actual amounts differ from previous estimates, we include the revisions in our consolidated results of operations in the period during which we know the actual amounts. Historically, aggregate differences, if any, between our estimates and actual amounts in any year have not had a significant impact on our consolidated financial statements.

The selection and disclosure of our critical accounting estimates have been discussed with our Audit Committee. The following is a discussion of the more significant assumptions, estimates, accounting policies and methods used in the preparation of our consolidated financial statements:

Revenue Recognition - We recognize revenue as performance obligations are satisfied. Our primary performance obligation is the distribution and sales of cigarettes and other nicotine-containing products, including reduced-risk products. Our performance obligations are typically satisfied upon shipment or delivery to our customers. The company estimates the cost of sales returns based on historical experience, and these estimates are immaterial. Estimated costs associated with warranty programs for *IQOS* devices are generally provided for in cost of sales in the period the related revenues are recognized, based on a number of factors, including historical experience, product failure rates and warranty policies. The transaction price is typically based on the amount billed to the customer and includes estimated variable consideration where applicable. Such variable consideration is typically not constrained and is estimated based on the most likely amount that PMI expects to be entitled to under the terms of the contracts with customers, historical experience of discount or rebate redemption, where relevant, and the terms of any

underlying discount or rebate programs, which may change from time to time as the business and product categories evolve.

Inventories - Our inventories are valued at the lower of cost or market based upon assumptions about future demand and market conditions. The valuation of inventory also requires us to estimate obsolete and excess inventory. We perform regular reviews of our

inventory on hand, as well as our future purchase commitments with our suppliers, considering multiple factors, including demand forecasts, product life cycle, current sales levels, pricing strategy and cost trends. If our review indicates that inventories of raw materials, components or finished products have become obsolete or are in excess of anticipated demand or that inventory cost exceeds net realizable value, we may be required to make adjustments that will impact the results of operations.

Goodwill and Non-Amortizable Intangible Assets Valuation - We test goodwill and non-amortizable intangible assets for impairment annually or more frequently if events occur that would warrant such review. While the company has the option to perform a qualitative assessment for both goodwill and non-amortizable intangible assets to determine if it is more likely than not that an impairment exists, the company elects to perform the quantitative assessment for our annual impairment analysis. The impairment analysis involves comparing the fair value of each reporting unit or non-amortizable intangible asset to the carrying value. If the carrying value exceeds the fair value, goodwill or a non-amortizable intangible asset is considered impaired. To determine the fair value of goodwill, we primarily use a discounted cash flow model, supported by the market approach using earnings multiples of comparable global and local companies within the tobacco industry. At December 31, 2018, the carrying value of our goodwill was $7.2 billion, which is related to ten reporting units, each of which consists of a group of markets with similar economic characteristics. The estimated fair value of each of our ten reporting units exceeded the carrying value as of December 31, 2018. To determine the fair value of non-amortizable intangible assets, we primarily use a discounted cash flow model applying the relief-from-royalty method. We concluded that the fair value of our non-amortizable intangible assets exceeded the carrying value. These discounted cash flow models include management assumptions relevant for forecasting operating cash flows, which are subject to changes in business conditions, such as volumes and prices, costs to produce, discount rates and estimated capital needs. Management considers historical experience and all available information at the time the fair values are estimated, and we believe these assumptions are consistent with the assumptions a hypothetical marketplace participant would use. Since the March 28, 2008, spin-off from Altria Group, Inc., we have not recorded a charge to earnings for an impairment of goodwill or non-amortizable intangible assets.

Marketing Costs - We incur certain costs to support our products through programs that include advertising, marketing, consumer engagement and trade promotions. The costs of our advertising and marketing programs are expensed in accordance with U.S. GAAP. Recognition of the cost related to our consumer engagement and trade promotion programs contain uncertainties due to the judgment required in estimating the potential performance and compliance for each program. For volume-based incentives provided to customers, management continually assesses and estimates, by customer, the likelihood of the customer's achieving the specified targets, and records the reduction of revenue as the sales are made. For other trade promotions, management relies on estimated utilization rates that have been developed from historical experience. Changes in the assumptions used in estimating the cost of any individual marketing program would not result in a material change in our financial position, results of operations or operating cash flows.

Employee Benefit Plans - As discussed in Item 8, Note 13. *Benefit Plans* to our consolidated financial statements, we provide a range of benefits to our employees and retired employees, including pensions, postretirement health care and postemployment benefits (primarily severance). We record annual amounts relating to these plans based on calculations specified by U.S. GAAP. These calculations include various actuarial assumptions, such as discount rates, assumed rates of return on plan assets, compensation increases, mortality, turnover rates and health care cost trend rates. We review actuarial assumptions on an annual basis and make modifications to the assumptions based on current rates and trends when it is deemed appropriate to do so. As permitted by U.S. GAAP, any effect of the modifications is generally amortized over future periods. We believe that the assumptions utilized in calculating our obligations under these plans are reasonable based upon our historical experience and advice from our actuaries.

Weighted-average discount rate assumptions for pension and postretirement plan obligations at December 31, 2018 and 2017 are as follows:

	2018	2017
Pension plans	**1.61%**	1.51%
Postretirement plans	**3.97%**	3.79%

We anticipate that assumption changes will increase 2019 pre-tax pension and postretirement expense to approximately $205 million as compared with approximately $160 million in 2018, excluding amounts related to employee severance and early retirement programs. The anticipated increase is primarily due to higher amortization out of other comprehensive earnings for unrecognized actuarial gains/losses of $14 million, coupled with lower

return on assets of $16 million, higher interest and service cost of $12 million and $4 million respectively, partially offset by other movements of $1 million.

Weighted-average expected rate of return and discount rate assumptions have a significant effect on the amount of expense reported for the employee benefit plans. A fifty-basis-point decrease in our discount rate would increase our 2019 pension and postretirement expense by approximately $50 million, and a fifty-basis-point increase in our discount rate would decrease our 2019 pension and postretirement

expense by approximately $44 million. Similarly, a fifty-basis-point decrease (increase) in the expected return on plan assets would increase (decrease) our 2019 pension expense by approximately $33 million.

Income Taxes - Income tax provisions for jurisdictions outside the United States, as well as state and local income tax provisions, are determined on a separate company basis, and the related assets and liabilities are recorded in our consolidated balance sheets.

The extent of our operations involves dealing with uncertainties and judgments in the application of complex tax regulations in a multitude of jurisdictions. The final taxes paid are dependent upon many factors, including negotiations with taxing authorities in various jurisdictions and resolution of disputes arising from federal, state, and international tax audits. In accordance with the authoritative guidance for income taxes, we evaluate potential tax exposures and record tax liabilities for anticipated tax audit issues based on our estimate of whether, and the extent to which, additional taxes will be due. We adjust these reserves in light of changing facts and circumstances; however, due to the complexity of some of these uncertainties, the ultimate resolution may result in a payment that is materially different from our current estimate of the tax liabilities. If our estimate of tax liabilities proves to be less than the ultimate assessment, an additional charge to expense would result. If payment of these amounts ultimately proves to be less than the recorded amounts, the reversal of the liabilities would result in tax benefits being recognized in the period when we determine the liabilities are no longer necessary.

We are required to assess the likelihood of recovering deferred tax assets against future sources of taxable income. If we determine, using all available evidence, that we do not reach the more likely than not threshold for recovery, a valuation allowance is recorded. Significant judgment is required in determining the need for and amount of valuation allowances for deferred tax assets including estimates of future taxable income in the applicable jurisdictions and the feasibility of on-going tax planning strategies, as applicable.

The effective tax rates used for interim reporting are based on our full-year geographic earnings mix projections. Changes in currency exchange rates or earnings mix by taxing jurisdiction could have an impact on the effective tax rates. Significant judgment is required in determining income tax provisions and in evaluating tax positions.

For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements.

Hedging - As discussed below in "Market Risk," we use derivative financial instruments principally to reduce exposures to market risks resulting from fluctuations in foreign currency exchange and interest rates by creating offsetting exposures. For derivatives to which we have elected to apply hedge accounting, gains and losses on these derivatives are initially deferred in accumulated other comprehensive losses on the consolidated balance sheet and recognized in the consolidated statement of earnings into the same line item as the impact of the underlying transaction, the periods when the related hedged transactions are also recognized in operating results. If we had elected not to use the hedge accounting provisions, gains (losses) deferred in stockholders' (deficit) equity would have been recorded in our net earnings for these derivatives.

Contingencies - As discussed in Item 8, Note 18. *Contingencies* to our consolidated financial statements, legal proceedings covering a wide range of matters are pending or threatened against us, and/or our subsidiaries, and/or our indemnitees in various jurisdictions. We and our subsidiaries record provisions in the consolidated financial statements for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. The variability in pleadings in multiple jurisdictions, together with the actual experience of management in litigating claims, demonstrate that the monetary relief that may be specified in a lawsuit bears little relevance to the ultimate outcome. Much of the tobacco-related litigation is in its early stages, and litigation is subject to uncertainty. At the present time, while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available to it: (i) management has not concluded that it is probable that a loss has been incurred in any of the pending tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any. Legal defense costs are expensed as incurred.

Consolidated Operating Results

Our net revenues and operating income by segment were as follows:

(in millions)	2018	2017	2016
Net Revenues			
European Union	**$ 9,298**	$ 8,318	$ 8,162
Eastern Europe	**2,921**	2,711	2,484
Middle East & Africa	**4,114**	3,988	4,516
South & Southeast Asia	**4,656**	4,417	4,396
East Asia & Australia	**5,580**	6,373	4,285
Latin America & Canada	**3,056**	2,941	2,842
Net revenues	**$ 29,625**	$ 28,748	$ 26,685
Operating Income			
European Union	**$ 4,105**	$ 3,691	$ 3,920
Eastern Europe	**902**	887	890
Middle East & Africa	**1,627**	1,884	1,990
South & Southeast Asia	**1,747**	1,514	1,474
East Asia & Australia	**1,851**	2,608	1,691
Latin America & Canada	**1,145**	997	938
Operating income	**$ 11,377**	$ 11,581	$ 10,903

As discussed in Item 8, Note 12. *Segment Reporting* to our consolidated financial statements, effective January 1, 2018, we began using operating income to evaluate segment performance and allocate resources, replacing operating companies income used previously.

Our net revenues by product category were as follows:

PMI Net Revenues by Product Category

(in millions)	2018	2017	2016
Combustible Products			
European Union	**$ 8,433**	$ 8,048	$ 8,105
Eastern Europe	**2,597**	2,657	2,478
Middle East & Africa	**3,732**	3,893	4,513
South & Southeast Asia	**4,656**	4,417	4,396
East Asia & Australia	**3,074**	3,156	3,619
Latin America & Canada	**3,037**	2,937	2,841
Total Combustible Products	**$ 25,529**	$ 25,107	$ 25,952
Reduced-Risk Products			
European Union	**$ 865**	$ 269	$ 57
Eastern Europe	**324**	55	6
Middle East & Africa	**382**	94	4
South & Southeast Asia	**—**	—	—
East Asia & Australia	**2,506**	3,218	666
Latin America & Canada	**19**	4	1
Total Reduced-Risk Products	**$ 4,096**	$ 3,640	$ 733
Total PMI Net Revenues	**$ 29,625**	$ 28,748	$ 26,685

Note: Sum of product categories or Regions might not foot to total PMI due to rounding.

Net revenues related to combustible products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of our cigarettes and other tobacco products combined. Other tobacco products primarily include roll-your-own and make-your-own cigarettes, pipe tobacco, cigars and cigarillos and do not include reduced-risk products.

Net revenues related to reduced-risk products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of our heated tobacco units, *IQOS* devices and related accessories, and other nicotine-containing products, which primarily include our e-vapor products.

We recognize revenue when control is transferred to the customer, typically either upon shipment or delivery of goods.

Our shipment volume by segment for cigarettes and heated tobacco units was as follows:

PMI Shipment Volume (Million Units)

	2018	2017	2016
Cigarettes			
European Union	**179,622**	187,293	193,586
Eastern Europe	**108,718**	119,398	129,456
Middle East & Africa	**136,605**	136,759	141,937
South & Southeast Asia	**178,469**	171,600	185,279
East Asia & Australia	**56,163**	62,653	74,750
Latin America & Canada	**80,738**	84,223	87,938
Total Cigarettes	**740,315**	761,926	812,946
Heated Tobacco Units			
European Union	**5,977**	1,889	224
Eastern Europe	**4,979**	674	64
Middle East & Africa	**3,403**	907	36
South & Southeast Asia	**—**	—	—
East Asia & Australia	**26,866**	32,729	7,070
Latin America & Canada	**147**	27	—
Total Heated Tobacco Units	**41,372**	36,226	7,394
Cigarettes and Heated Tobacco Units			
European Union	**185,599**	189,182	193,810
Eastern Europe	**113,697**	120,072	129,520
Middle East & Africa	**140,008**	137,666	141,973
South & Southeast Asia	**178,469**	171,600	185,279
East Asia & Australia	**83,029**	95,382	81,820
Latin America & Canada	**80,885**	84,250	87,938
Total Cigarettes and Heated Tobacco Units	**781,687**	798,152	820,340

Heated tobacco units ("HTU") is the term we use to refer to heated tobacco consumables, which for us include our *HEETS*, *HEETS Marlboro* and *HEETS FROM MARLBORO*, defined collectively as *HEETS*, as well as *Marlboro HeatSticks* and *Parliament HeatSticks.*

References to total international market, defined as worldwide cigarette and heated tobacco unit volume excluding the United States, total industry, total market and market shares throughout this *"Discussion and Analysis"* are our estimates for tax-paid products based on the latest available data from a number of internal and external sources and may, in defined instances, exclude the People's Republic of China and/or our duty free business.

In-market sales ("IMS") is defined as sales to the retail channel, depending on the market and distribution model.

North Africa is defined as Algeria, Egypt, Libya, Morocco and Tunisia.

Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units.

From time to time, PMI's shipment volumes are subject to the impact of distributor inventory movements, and estimated total industry/market volumes are subject to the impact of inventory movements in various trade channels that include estimated trade inventory movements of PMI's competitors arising from market-specific factors that significantly distort reported volume disclosures. Such factors may include changes to the manufacturing supply chain, shipment methods, consumer demand, timing of excise tax increases or other influences that may affect the timing of sales to customers. In such instances, in addition to reviewing PMI shipment volumes and certain estimated total industry/market volumes on a reported basis, management reviews these measures on an adjusted basis that excludes the impact of distributor and/or estimated trade inventory movements. Management also believes that disclosing PMI shipment volumes and estimated total industry/market volumes in such circumstances on a basis that excludes the impact of distributor and/or estimated trade inventory movements improves the comparability of performance and trends for these measures over different reporting periods.

2018 compared with 2017

The following discussion compares our consolidated operating results for the year ended December 31, 2018, with the year ended December 31, 2017.

Estimated international cigarette and heated tobacco unit volume, excluding China and the United States, of 2.8 trillion, decreased by 1.6%, mainly due to the EU, EE, EA&A and LA&C, partly offset by ME&A and S&SA, as described in the Regional sections below.

Our total shipment volume decreased by 2.1%, principally due to:

- the EU, primarily reflecting lower cigarette shipment volume in France, Germany and Italy, partly offset by higher heated tobacco unit shipment volume across the Region, notably in Italy;
- Eastern Europe, reflecting lower cigarette shipment volume, principally in Russia and Ukraine, partly offset by higher heated tobacco unit shipment volume across the Region, notably in Russia;
- East Asia & Australia, reflecting lower cigarette shipment volume, principally in Japan and Korea; lower heated tobacco unit shipment volume in Japan, reflecting the net impact of estimated distributor inventory movements described in the East Asia & Australia Region section below; partly offset by higher heated tobacco unit shipment volume in Korea; and
- Latin America & Canada, reflecting lower cigarette shipment volume, notably in Argentina and Colombia;

partly offset by

- Middle East & Africa, reflecting essentially flat cigarette shipment volume, with declines, notably in Saudi Arabia and the UAE, almost completely offset by higher cigarette shipment volume, notably in Turkey, as well as by higher heated tobacco unit shipment volume, mainly in PMI Duty Free; and
- South & Southeast Asia, reflecting higher cigarette shipment volume, principally in Pakistan, the Philippines and Thailand.

Excluding the net impact of estimated distributor inventory movements of approximately 16.6 billion units, due primarily to heated tobacco unit inventories in Japan, reflecting unfavorable cigarette and heated tobacco unit inventory movements of approximately 0.4 billion and 16.2 billion units, respectively, our total shipment volume was flat.

Our cigarette shipment volume by brand and heated tobacco unit shipment volume was as follows:

PMI Shipment Volume by Brand (Million Units)

	Full-Year		
	2018	**2017**	**Change**
Cigarettes			
Marlboro	**264,423**	270,366	(2.2%)
L&M	**89,789**	90,817	(1.1%)
Chesterfield	**59,452**	55,075	7.9 %
Philip Morris	**49,864**	48,522	2.8 %
Sampoerna A	**39,522**	42,736	(7.5%)
Parliament	**41,697**	43,965	(5.2%)
Bond Street	**32,173**	37,987	(15.3%)
Dji Sam Soe	**29,195**	22,757	28.3 %
Lark	**23,021**	24,530	(6.2%)
Fortune	**16,596**	13,451	23.4 %
Others	**94,583**	111,720	(15.3%)
Total Cigarettes	**740,315**	761,926	(2.8%)
Heated Tobacco Units	**41,372**	36,226	14.2 %
Total Cigarettes and Heated Tobacco Units	**781,687**	798,152	(2.1%)

Note: *Sampoerna A* includes *Sampoerna*; *Philip Morris* includes *Philip Morris/Dubliss*; and *Lark* includes *Lark Harmony*.

Our cigarette shipment volume decreased, partly reflecting the impact of out-switching to heated tobacco units largely from premium and mid-price cigarette brands. Our cigarette shipment volume of the following brands decreased:

- *Marlboro*, mainly due to France, the GCC, notably Saudi Arabia and the UAE, Italy, Japan and Korea, partly offset by Indonesia, North Africa and Turkey;
- *L&M*, mainly due to the GCC, notably Saudi Arabia, as well as North Africa, Russia and Turkey, partly offset by Kazakhstan, Serbia and Thailand;
- *Sampoerna A* in Indonesia, mainly reflecting the impact of its retail price increasing past its round pack price point in the fourth quarter of 2017;
- *Parliament*, mainly due to Korea and Russia, partly offset by Turkey;
- *Bond Street*, mainly due to Kazakhstan, Russia and Ukraine;
- *Lark*, mainly due to Japan, partly offset by Turkey; and
- "Others," mainly due to: mid-price brands, notably *Sampoerna U* in Indonesia, partly reflecting the impact of above-inflation retail price increases; the successful portfolio consolidation of local brands into international trademarks, notably in Brazil, Colombia, Mexico and Russia; low-price *Jackpot* in the Philippines, reflecting up-trading as a result of narrowed price gaps; partly offset by low-price *Hope* in the Philippines and *Morven* in Pakistan.

Our cigarette shipment volume of the following brands increased:

- *Chesterfield,* mainly driven by Argentina, Brazil, Colombia, the GCC, notably Saudi Arabia, Mexico and Turkey, partly offset by Portugal, Russia and Venezuela;
- *Philip Morris*, mainly driven by Russia, partly offset by Argentina, Italy and the Philippines;
- *Dji Sam Soe* in Indonesia, notably reflecting the continued strong performance of its *Magnum Mild 16s* variant launched in the second quarter of 2017; and
- *Fortune* in the Philippines, reflecting the favorable impact of its narrowed retail price gap to competitors' products.

Our heated tobacco unit shipment volume increased, reflecting favorable heated tobacco unit volume across the EU, notably Italy, as well as Korea, PMI Duty Free and Russia, partly offset by unfavorable heated tobacco unit volume in Japan, reflecting the net impact of estimated distributor inventory movements.

2018 International Share of Market (excluding China and the United States)

Our 2018 total international market share, defined as our cigarette and heated tobacco unit sales volume as a percentage of total industry cigarette and heated tobacco unit sales volume, increased by 0.5 points to 28.4%, reflecting:

- Total international cigarette market share of 26.8%, down by 0.3 points; and
- Total international heated tobacco unit market share of 1.6%, up by 0.8 points.

Our total international cigarette market share, defined as our cigarette sales volume as a percentage of total industry cigarette sales volume, was flat at 27.4%.

In 2018, we owned six of the world's top 15 international cigarette brands, with international cigarette market shares as follows: *Marlboro*, 9.7%; *L&M*, 3.3%; *Chesterfield*, 2.2%; *Philip Morris*, 1.8%; *Parliament*, 1.6%; and *Bond Street*, 1.2%.

Key Market Data

Key market data regarding total market size, our shipments and market share were as follows:

Market	Total Market (billion units)		PMI Shipments (billion units)						PMI Market Share (%)[1]			
			Total		Cigarette		Heated Tobacco Unit		Total		Heated Tobacco Unit	
	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
European Union												
France	40.9	45.1	18.5	19.7	18.4	19.7	—	—	45.5	43.5	0.1	—
Germany	75.2	76.9	28.1	28.6	27.7	28.5	0.4	0.1	37.3	37.2	0.5	0.2
Italy	69.0	69.8	35.2	36.8	33.5	36.1	1.7	0.7	51.8	52.2	2.2	0.7
Poland	43.2	41.7	17.9	17.8	17.6	17.7	0.4	0.1	41.5	42.7	0.9	0.2
Spain	45.0	45.0	14.1	14.5	13.9	14.4	0.2	0.1	32.1	32.3	0.4	0.1
Eastern Europe												
Russia	238.1	260.0	68.0	72.4	64.6	72.1	3.4	0.3	28.4	27.8	1.0	0.1
Middle East & Africa												
Saudi Arabia	20.6	26.1	7.4	10.9	7.4	10.9	—	—	41.5	45.2	—	—
Turkey	118.5	106.2	55.0	49.6	55.0	49.6	—	—	46.4	46.7	—	—
South & Southeast Asia												
Indonesia	307.0	307.4	101.4	101.3	101.4	101.3	—	—	33.0	33.0	—	—
Philippines	73.2	74.9	51.2	50.6	51.2	50.6	—	—	69.9	67.6	—	—
East Asia & Australia												
Australia	12.8	13.9	3.8	4.3	3.8	4.3	—	—	29.7	30.6	—	—
Japan	167.3	171.5	52.3	66.1	30.8	34.9	21.4	31.3	34.0	32.1	15.5	10.8
Korea	69.5	70.6	17.4	14.9	12.0	13.5	5.4	1.4	25.0	21.2	7.8	2.0
Latin America & Canada												
Argentina	35.0	36.2	25.8	27.0	25.8	27.0	—	—	73.7	74.7	—	—
Canada	23.4	24.6	8.9	9.3	8.9	9.3	—	—	38.1	37.3	0.1	—

Mexico	35.5	35.8	24.2	24.4	24.2	24.4	—	—	68.0	68.1	—	—

(1) Market share estimates are calculated using IMS data
Note: % change for Total Market and PMI shipments in the discussion below is computed based on millions of units

Financial Summary

Financial Summary - Years Ended December 31, (in millions)	2018	2017	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Cur-rency	Price	Vol/ Mix	Cost/ Other
Net Revenues	**$ 29,625**	$ 28,748	3.1 %	3.4 %	$ 877	$ (103)	$ 1,488	$ (724)	$ 216
Cost of Sales	**(10,758)**	(10,432)	(3.1)%	(2.3)%	(326)	(83)	—	(180)	(63)
Marketing, Administration and Research Costs	**(7,408)**	(6,647)	(11.4)%	(11.0)%	(761)	(29)	—	—	(732)
Amortization of Intangibles	**(82)**	(88)	6.8 %	5.7 %	6	1	—	—	5
Operating Income	**$ 11,377**	$ 11,581	(1.8)%	0.1 %	$ (204)	$ (214)	$ 1,488	$ (904)	$ (574)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles. "Cost/Other" also includes the currency-neutral net revenue variance, unrelated to volume/mix and price components, attributable to fees for certain distribution rights billed to customers in certain markets in the ME&A Region. This immaterial presentational change, made in conjunction with the new revenue recognition standard, is prospective only.

Net revenues, excluding unfavorable currency, increased by 3.4%, reflecting: a favorable pricing variance, notably in Argentina, Australia, Canada, Egypt, Germany, Indonesia, Italy, Japan, Mexico, the Philippines, Russia, Turkey, and Ukraine, partly offset by France, Korea, Saudi Arabia and Thailand; as well as a favorable "cost/other" variance as described above.

These favorable variances were partly offset by unfavorable volume/mix, primarily reflecting unfavorable cigarette volume/mix, notably in Australia, the GCC, notably Saudi Arabia and the UAE, Indonesia, Italy, Japan and Russia, partly offset by Pakistan, Thailand and Turkey. The unfavorable cigarette volume/mix was partly offset by favorable heated tobacco unit volume in the EU, notably the Czech Republic, Germany and Italy, as well as Korea, PMI Duty Free and Russia, partly offset by unfavorable heated tobacco unit volume in Japan, reflecting the net impact of estimated distributor inventory movements.

The unfavorable currency in net revenues was due primarily to the Argentine peso, Indonesian rupiah, Philippine peso, Russian ruble and Turkish lira, partially offset by the Euro, Japanese yen and Polish zloty.

Net revenues include $4.1 billion in 2018 and $3.6 billion in 2017 related to the sale of RRPs. In 2018, approximately $0.9 billion of our $4.1 billion in RRP net revenues were from *IQOS* devices and accessories.

Operating income, excluding unfavorable currency, was essentially flat, reflecting: a favorable pricing variance; partly offset by unfavorable volume/mix, due mainly to lower volume in Japan and Saudi Arabia and lower mix in Indonesia and Russia, partly offset by higher volume in the EU, driven by heated tobacco units, as well as Korea, PMI Duty Free, Thailand and Turkey. The favorable pricing variance was also partly offset by higher marketing, administration and research costs, primarily related to increased investment behind reduced-risk products across all Regions, predominantly the EU and EA&A.

Interest expense, net, of $665 million decreased by $249 million (27.2%), due primarily to our ongoing efforts to optimize our capital structure following the passage of the Tax Cuts and Jobs Act. This included the decision to use existing cash to repay the $2.5 billion principal for our matured May 2018 ten-year U.S. bond, which had a coupon of 5.65%.

Our effective tax rate decreased by 17.8 percentage points to 22.9%. The change in the effective tax rate for 2018, as compared to 2017, was primarily due to the Tax Cuts and Jobs Act, which reduced the U.S. federal income tax rate from 35% to 21%, in addition to repatriation cost differences and earnings mix by taxing jurisdiction. We completed our analysis of the Tax Cuts and Jobs Act during 2018 and adjusted the 2017 provisional estimates to the final amounts based on our 2017 U.S. federal income tax return as filed. Accordingly, we recorded in our income tax provision a charge of $31 million representing a current income tax charge of $185 million primarily due to an increase in our final 2017 transition tax liability, mostly offset by a deferred income tax benefit of $154 million

primarily due to the recognition of deferred tax assets for net operating losses in the state of New York. The effective tax rate in 2017 was unfavorably impacted by $1.6 billion due to the Tax Cuts and Jobs Act. We estimate that our 2019 effective tax rate will be approximately 23%, subject to future regulatory developments and earnings mix by taxing jurisdiction. For further details, see Item 8, Note 11. *Income Taxes*.

We are regularly examined by tax authorities around the world, and we are currently under examination in a number of jurisdictions. It is reasonably possible that within the next 12 months certain tax examinations will close, which could result in a change in unrecognized tax benefits along with related interest and penalties. An estimate of any possible change cannot be made at this time.

Net earnings attributable to PMI of $7.9 billion increased by $1.9 billion (31.1%). This increase was due primarily to a lower effective tax rate and lower interest expense, net, partially offset by lower operating income. Diluted and basic EPS of $5.08 increased by 30.9%. Excluding a net favorable tax impact of $0.82 primarily related to the implementation of the Tax Cuts and Jobs Act and an unfavorable currency impact of $0.11, diluted EPS increased by 10.4%.

2017 compared with 2016

The following discussion compares our consolidated operating results for the year ended December 31, 2017, with the year ended December 31, 2016.

Estimated international cigarette and heated tobacco unit volume, excluding China and the United States, of 2.8 trillion was down by 2.8%.

Our total shipment volume decreased by 2.7%, principally due to:

- European Union, notably reflecting lower cigarette shipment volume in Greece, Italy and Spain, partly offset by higher heated tobacco unit shipment volume;
- Eastern Europe, notably reflecting lower cigarette shipment volume in Russia and Ukraine; partly offset by higher heated tobacco unit shipment volume;
- Middle East & Africa, notably reflecting lower cigarette shipment volume in Saudi Arabia - where our cigarette shipment volume declined by 35.8%, impacted by the new excise tax implemented in June 2017 that resulted in the doubling of retail prices; partly offset by higher cigarette shipment volume in North Africa, notably Algeria, and higher heated tobacco unit shipment volume;
- South & Southeast Asia, notably reflecting lower cigarette shipment volume in Indonesia and Pakistan - impacted by excise tax-driven price increases and an increase in the prevalence of illicit trade - and the Philippines; and
- Latin America & Canada, notably reflecting lower cigarette shipment volume in Argentina, Brazil, Canada, Colombia and Mexico;

partially offset by:

- East Asia & Australia, notably reflecting higher heated tobacco unit shipment volume, mainly in Japan and Korea, partly offset by lower cigarette shipment volume in Japan and Korea.

Excluding the favorable net impact of estimated cigarette and heated tobacco unit inventory movements of approximately 3.3 billion units, our total shipment volume decreased by 3.1%. The favorable inventory movements were driven primarily by approximately 8.5 billion units net in Japan reflecting: the increasing demand for *HeatSticks*, anticipated to further increase in the first quarter of 2018 following a planned lifting of the restriction on *IQOS* device sales; the establishment of appropriate distributor inventory levels of heated tobacco units, given the current high dependence on a single manufacturing center; and the transition from air freight to sea freight of heated tobacco units, largely completed in the fourth quarter of 2017. These favorable inventory movements were partly offset by a reduction of combustible product inventory levels, mainly in Italy, North Africa, Russia, Saudi Arabia and Spain.

Our cigarette shipment volume by brand and heated tobacco unit shipment volume was as follows:

PMI Cigarette Shipment Volume by Brand (Million Units)

	Full-Year		
	2017	**2016**	**Change**
Cigarettes			
Marlboro	270,366	281,720	(4.0
L&M	90,817	96,770	(6.2
Chesterfield	55,075	46,291	19.0
Philip Morris	48,522	35,914	35.1
Parliament	43,965	45,671	(3.7
Bond Street	37,987	44,567	(14.8
Lark	24,530	27,571	(11.0
Others*	190,664	234,442	(18.7
Total Cigarettes	761,926	812,946	(6.3
Heated Tobacco Units	36,226	7,394	+100.0%
Total Cigarettes and Heated Tobacco Units	798,152	820,340	(2.7

*Others above also include cigarette shipment volumes of *Sampoerna A* (including *Sampoerna*) of 42,736 million units in 2017 and 44,548 million units in 2016; *Dji Sam Soe* of 22,757 million units in 2017 and 20,411 million units in 2016; and *Fortune* of 13,451 million units in 2017 and 18,570 million units in 2016.

Note: *Philip Morris* includes *Philip Morris/Dubliss*; and *Lark* includes *Lark Harmony*.

Cigarette shipment volume of *Marlboro* decreased in: the EU, mainly due to Greece, Italy and Spain; ME&A, predominantly due to Saudi Arabia, reflecting the impact of the new excise tax implemented in June 2017 that resulted in the doubling of the retail price of *Marlboro* from SAR 12 to SAR 24 per pack, partly offset by North Africa, notably Algeria and Egypt, and Turkey; EA&A, mainly due to Japan and Korea, principally reflecting out-switching to heated tobacco products; and LA&C, mainly due to Argentina and Brazil; partly offset by an increase in S&SA, mainly due to Indonesia and the Philippines.

Cigarette shipment volume of the following brands decreased: *L&M*, mainly due to Russia, Saudi Arabia and Turkey, partly offset by Algeria, Argentina, Colombia and Kazakhstan; *Parliament*, mainly due to Japan, Russia and Saudi Arabia, partly offset by Kazakhstan; *Bond Street*, mainly due to Kazakhstan, Russia and Ukraine; *Lark*, principally due to Japan; and "Others," mainly due to low-price brands in Indonesia, Pakistan, the Philippines, Russia and Ukraine.

Cigarette shipment volume of the following brands increased: *Chesterfield,* notably driven by Argentina, Brazil, Colombia, Saudi Arabia, Turkey and Venezuela, partly offset by Italy and Russia; and *Philip Morris*, mainly driven by Russia and Ukraine, notably reflecting successful portfolio consolidation of local, low-price brands in "Others," partly offset by Argentina and Italy.

Key market data regarding total market size, our shipments and market share were as follows:

Market	Total Market (billion units)		PMI Shipments (billion units)						PMI Market Share (%)[1]			
			Total		Cigarette		Heated Tobacco Unit		Total		Heated Tobacco Unit	
	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
European Union												
France	45.1	45.7	19.7	19.7	19.7	19.7	—	—	43.5	42.8	—	—
Germany	76.9	78.1	28.6	29.0	28.5	29.0	0.1	—	37.2	37.1	0.2	—
Italy	69.8	72.1	36.8	38.7	36.1	38.6	0.7	0.1	52.2	52.5	0.7	0.1
Poland	41.7	41.3	17.8	17.5	17.7	17.5	0.1	—	42.7	42.3	0.2	—
Spain	45.0	46.7	14.5	16.4	14.4	16.4	0.1	—	32.3	33.9	0.1	—
Eastern Europe												
Russia	260.0	280.0	72.4	79.7	72.1	79.7	0.3	0.1	27.8	27.9	0.1	—
Middle East & Africa												
Saudi Arabia	26.1	31.6	10.9	17.0	10.9	17.0	—	—	45.2	52.1	—	—
Turkey	106.2	105.5	49.6	49.6	49.6	49.6	—	—	46.7	47.0	—	—
South & Southeast Asia												
Indonesia	307.4	315.6	101.3	105.5	101.3	105.5	—	—	33.0	33.4	—	—
Philippines	74.9	79.3	50.6	56.6	50.6	56.6	—	—	67.6	71.3	—	—
East Asia & Australia												
Australia	13.9	15.7	4.3	5.1	4.3	5.1	—	—	30.6	32.8	—	—
Japan	171.5	179.0	66.1	51.0	34.9	43.9	31.3	7.1	32.1	27.1	10.8	2.9
Korea	70.6	73.6	14.9	15.5	13.5	15.5	1.4	—	21.2	21.0	2.0	—
Latin America & Canada												
Argentina	36.2	36.1	27.0	27.5	27.0	27.5	—	—	74.7	76.3	—	—
Canada	24.6	26.3	9.3	10.0	9.3	10.0	—	—	37.3	38.4	—	—
Mexico	35.8	36.2	24.4	25.1	24.4	25.1	—	—	68.1	69.3	—	—

(1) Market share estimates are calculated using IMS data
Note: % change for Total Market and PMI shipments in the discussion below is computed based on millions of units

Financial Summary - Years Ended December 31, (in millions)	2017	2016	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Cur-rency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/ Mix
Net Revenues	$ 28,748	$ 26,685	7.7 %	9.4 %	$ 2,063	$ (437)	$ 1,386	$ 1,114
Cost of Sales	(10,432)	(9,391)	(11.1)%	(11.4)%	(1,041)	30	—	(1,107
Marketing, Administration and Research Costs	(6,647)	(6,317)	(5.2)%	(9.2)%	(330)	250	—	—
Amortization of Intangibles	(88)	(74)	(18.9)%	(18.9)%	(14)	—	—	—
Operating Income	$ 11,581	$ 10,903	6.2 %	7.7 %	$ 678	$ (157)	$ 1,386	$ 7

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues increased by 7.7%, due to price increases and favorable volume/mix, partially offset by unfavorable currency.

The unfavorable currency in net revenues was due primarily to the Argentine peso, Egyptian pound, Japanese yen, Philippine peso and Turkish lira, partially offset by the Russian ruble.

Net revenues for RRPs were $3.6 billion in 2017 and $733 million in 2016 mainly in Japan. In 2017, approximately $0.9 billion of our $3.6 billion in RRP net revenues were from *IQOS* devices and accessories.

Cost of sales increased by 11.1%, due to higher cost of sales resulting from volume/mix, partly offset by lower manufacturing costs and favorable currency.

Marketing, administration and research costs increased by 5.2%, largely reflecting increased investment behind reduced-risk products, predominately in the European Union and East Asia & Australia, partly offset by favorable currency.

Operating income increased by 6.2%, due primarily to price increases, partly offset by higher marketing, administration and research costs and unfavorable currency.

Interest expense, net, of $914 million increased by $23 million, due primarily to unfavorable currency and higher average debt levels, partly offset by higher interest income.

Our effective tax rate increased by 12.8 percentage points to 40.7%. The 2017 effective tax rate was unfavorably impacted by $1.6 billion due to the Tax Cuts and Jobs Act. For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements.

Net earnings attributable to PMI of $6.0 billion decreased by $932 million (13.4%). This decrease was due primarily to a higher effective tax rate as discussed above, partly offset by higher operating income. Diluted and basic EPS of $3.88 decreased by 13.4%. Excluding an unfavorable tax impact of $0.84 primarily related to the implementation of the Tax Cuts and Jobs Act and an unfavorable currency impact of $0.21, diluted EPS increased by 10.0%.

Operating Results by Business Segment

Business Environment

Taxes, Legislation, Regulation and Other Matters Regarding the Manufacture, Marketing, Sale and Use of Tobacco Products

The tobacco industry and our business face a number of challenges that may adversely affect our business, volume, results of operations, cash flows and financial position. These challenges, which are discussed below and in "*Cautionary Factors That May Affect Future Results*," include:

- regulatory restrictions on our products, including restrictions on the packaging, marketing, and sale of tobacco or other nicotine-containing products that could reduce our competitiveness, eliminate our ability to communicate with adult consumers, or even ban certain of our products;
- fiscal challenges, such as excessive excise tax increases and discriminatory tax structures;
- illicit trade in cigarettes and other tobacco products, including counterfeit, contraband and so-called "illicit whites";
- intense competition, including from non-tax paid volume by certain local manufacturers;
- pending and threatened litigation as discussed in Item 8, Note 18. *Contingencies*; and
- governmental investigations.

Regulatory Restrictions: The tobacco industry operates in a highly regulated environment. The well-known risks of smoking have led regulators to impose significant restrictions and high excise taxes on cigarettes.

We support a comprehensive regulatory framework for tobacco products based on the principle of harm reduction, including mandated health warnings, minimum age laws, restrictions on advertising, and public place smoking restrictions. We also support regulatory measures that help reduce illicit trade.

Much of the regulation that shapes the business environment in which we operate is driven by the World Health Organization's ("WHO") Framework Convention on Tobacco Control ("FCTC"), which entered into force in 2005. The FCTC has as its main objective to establish a global agenda for tobacco regulation, with the purpose of reducing tobacco use. To date, 180 countries and the European Union are Parties to the FCTC. The treaty requires Parties to have in place various tobacco control measures and recommends others. The FCTC governing body, the Conference of the Parties ("CoP"), has also adopted non-binding guidelines and policy recommendations related to certain articles of the FCTC that go beyond the text of the treaty. In October 2018, the CoP recognized the need for more scientific assessment and improved reporting to define policy on heated tobacco products. Similar to its previous policy recommendations on e-cigarettes, the CoP invited countries to regulate, restrict or prohibit heated tobacco products, as appropriate under their national laws. It is not possible to predict whether or to what extent measures recommended by CoP, including the FCTC guidelines, will be implemented.

We continue to seek to engage in a dialogue with regulators with respect to those measures that we do not believe would protect public health and, if implemented, could disrupt competition, severely limit our ability to market and sell our products (including our RRPs) to adult smokers, or increase illicit trade. We advocate for measures that would accelerate switching to better alternatives to continued smoking and embrace a regulatory framework that recognizes a risk continuum of tobacco and other nicotine-containing products.

Certain measures are discussed in more detail below and in the *Reduced-Risk Products (RRPs)* section.

Fiscal Challenges: Excessive and disruptive excise, sales and other tax increases and discriminatory tax structures are expected to continue to have an adverse impact on our profitability, due to lower consumption and consumer down-trading to non-premium, discount, other low-price or low-taxed combustible tobacco products such as fine cut tobacco and illicit cigarettes. In addition, in certain jurisdictions, some of our combustible products are subject to tax structures that discriminate against premium-price products and manufactured cigarettes. We believe that such tax policies undermine public health by encouraging consumers to turn to illicit trade, and ultimately undercut government revenue objectives, disrupt the competitive environment, and encourage criminal activity. Other jurisdictions have imposed, or are seeking to impose, levies or other taxes specifically on tobacco companies, such as taxes on revenues and/or profits.

EU Tobacco Products Directive: In April 2014, the EU adopted a significantly revised EU Tobacco Products Directive (TPD), which entered into force in May 2016. All 28 Member States and Norway have adopted laws transposing the TPD. The TPD sets forth a comprehensive set of regulatory requirements for tobacco products, including:

- health warnings covering 65% of the front and back panels of cigarette packs, with an option for Member States to further standardize tobacco packaging, including the introduction of plain packaging;
- a ban on characterizing flavors in some tobacco products, with a transition period for menthol expiring in May 2020;
- security features and tracking and tracing measures that will become effective on May 20, 2019, and will increase our operating expenses; and
- a framework for the regulation of novel tobacco products and e-cigarettes, including requirements for health warnings and information leaflets, a prohibition on product packaging text related to reduced risk, and the introduction of notification requirements or authorization procedures in advance of commercialization.

Plain Packaging and Other Packaging Restrictions: Plain packaging legislation bans the use of branding, logos and colors on packaging other than the brand name and variant that may be printed only in specified locations and in a uniform font. To date, plain packaging

laws have been adopted in certain markets in all of our reporting segments, including the key markets of Australia, France, Saudi Arabia and Turkey, and are in various degrees of implementation. Some countries, such as New Zealand and Israel, adopted plain packaging regulations that apply to all tobacco products, including RRPs. Other countries, including Canada, are also considering plain packaging legislation.

Some countries have adopted, or are considering adopting, packaging restrictions that could have an impact similar to plain packaging. Examples of such restrictions include standardizing the shape and size of packages, prohibiting certain colors or the use of certain descriptive phrases on packaging, and requiring very large graphic health warnings that leave little space for branding.

Restrictions and Bans on the Use of Ingredients: The WHO and others in the public health community have recommended restrictions or total bans on the use of some or all ingredients in tobacco products, including menthol. Broad restrictions and ingredient bans would require us to reformulate our American blend tobacco products and could reduce our ability to differentiate these products in the market in the long term. Menthol bans would eliminate the entire category of mentholated tobacco products. The European Union has banned flavored tobacco products, subject to an exemption until May 2020 for menthol. Other countries may follow the EU's approach. For instance, Turkey has banned menthol as of May 2020. Broader ingredient bans have been adopted by Canada and Brazil. Canada banned menthol in cigarettes as of October 2017 and in all tobacco products as of November 2018. In Brazil, an ingredient ban is currently on appeal by a tobacco industry union, of which our Brazilian subsidiary is a member. The tobacco union requested a stay of the enforcement of the ingredient ban while the appeal is pending. It is not possible to predict the outcome of these legal proceedings.

Bans on Display of Tobacco Products at Retail: In a number of our markets, including, but not limited to, Australia, Canada, Norway, Russia, and Singapore, governments have banned the display of tobacco products at the point of sale. Other countries are considering similar bans.

Bans and Restrictions on Advertising, Marketing, Promotions and Sponsorships: For many years, the FCTC has called for, and countries have imposed, partial or total bans on tobacco advertising, marketing, promotions and sponsorships, including bans and restrictions on advertising on radio and television, in print and on the Internet. The FCTC's non-binding guidelines recommend that governments prohibit all forms of communication with adult smokers.

Restrictions on Product Design: Some members of the public health community are calling for the further standardization of tobacco products by requiring, for example, that cigarettes have a certain minimum diameter, which would amount to a ban on slim cigarettes, or requiring the use of standardized filter and cigarette paper designs. In addition, at its meeting in November 2016, the CoP adopted non-binding guidelines recommending that countries regulate product design features that increase the attractiveness of tobacco products, such as the diameter of cigarettes and the use of flavor capsules.

Restrictions on Public Smoking: The pace and scope of public smoking restrictions have increased significantly in most of our markets. Many countries around the world have adopted, or are likely to adopt, regulations that restrict or ban smoking in public and/or work places, restaurants, bars and nightclubs. Some public health groups have called for, and some countries, regional governments and municipalities have adopted or proposed, bans on smoking in outdoor places, as well as bans on smoking in cars (typically, when minors are present) and private homes.

Other Regulatory Issues: Some regulators are considering, or in some cases have adopted, regulatory measures designed to reduce the supply of tobacco products. These include regulations intended to reduce the number of retailers selling tobacco products by, for example, reducing the overall number of tobacco retail licenses available or banning the sale of tobacco products within specified distances of certain public facilities.

In a limited number of markets, most notably Japan, we are dependent on governmental approvals that may limit our pricing flexibility.

On December 19, 2018, the EU Council and the EU Parliament provisionally agreed on the Single-Use Plastics Directive, which would require tobacco manufacturers and importers to cover the costs of public collection systems for cigarette butts. The directive is expected to be finalized in the first half of 2019 and subsequently transposed by Member States into national law within two years. We cannot predict the impact of this initiative on our business at this time.

Illicit Trade: The illicit tobacco trade creates a cheap and unregulated supply of tobacco products, undermines efforts to reduce smoking prevalence, especially among youth, damages legitimate businesses, stimulates organized crime, increases corruption and reduces government tax revenue. Illicit trade may account for as much as 10% of global cigarette consumption; this includes counterfeit, contraband and the growing problem of "illicit whites," which are cigarettes legally produced in one jurisdiction for the sole purpose of being exported and illegally sold in another jurisdiction where they have no legitimate market. We estimate that illicit trade in the European Union accounted for approximately 10% of total cigarette consumption in 2018.

A number of jurisdictions are considering actions to prevent illicit trade. In November 2012, the FCTC adopted the Protocol to Eliminate Illicit Trade in Tobacco Products (the "Protocol"), which includes supply chain control measures, such as licensing of manufacturers and distributors, enforcement in free trade zones, controls on duty free and Internet sales and the implementation of tracking and tracing technologies. To date, 54 Parties have signed the Protocol, and 48 Parties, including the European Union, have ratified it. The Protocol came into force on September 25, 2018. Parties must now start implementing its measures via national legislation. In October 2018, the first Meeting of the Parties to the Protocol decided to produce a comprehensive report on good practices for the implementation of tracking and tracing systems and to prepare a conceptual framework for global information sharing to combat illicit tobacco trade. We welcome this decision and expect that other Parties will ratify the Protocol.

The tracking and tracing regulations for cigarettes and roll-your-own products manufactured or destined for the EU will become effective on May 20, 2019. The effective date for other tobacco-containing products, including some of our RRPs such as the heated tobacco units used with *IQOS*, is May 20, 2024.

In 2009, our Colombian subsidiaries entered into an Investment and Cooperation Agreement with the national and regional governments of Colombia to promote investment in, and cooperation on, anti-contraband and anti-counterfeit efforts. The agreement provides $200 million in funding over a 20-year period to address issues such as combating the illegal cigarette trade and increasing the quality and quantity of locally-grown tobacco.

In May 2016, PMI launched PMI IMPACT, a global initiative that supports third-party projects dedicated to fighting illegal trade and related crimes such as corruption, organized criminal networks and money laundering. The centerpiece of PMI IMPACT is a council of external independent experts in the fields of law, anti-corruption and law enforcement. The experts are responsible for evaluating and approving funding proposals for PMI IMPACT grants. PMI has pledged $100 million to fund projects within PMI IMPACT over three funding rounds. Substantially all grants under the first and second funding round were awarded in 2017 and 2018, respectively.

Reduced-Risk Products (RRPs)

Our Approach to RRPs: We recognize that smoking cigarettes causes serious diseases and that the best way to avoid the harms of smoking is never to start or to quit. Nevertheless, it is predicted that over the next decade the number of smokers will remain largely unchanged from the current estimate of 1.1 billion, despite the considerable efforts to discourage smoking.

Cigarettes burn tobacco, which produces smoke. As a result of the combustion process, the smoker inhales various toxic substances. In contrast, RRPs do not burn tobacco and produce an aerosol that contains significantly lower levels of harmful and potentially harmful constituents ("HPHCs") than found in cigarette smoke.

For smokers who would otherwise continue to smoke, we believe that RRPs, while not risk-free, offer a much better consumer choice. Accordingly, our key strategic priorities are: to develop and commercialize products that present less risk of harm to adult smokers who switch to those products versus continued smoking; and to convince current adult smokers who would otherwise continue to smoke to switch to those products.

We recognize that this transformation from cigarettes to RRPs will take time and that the speed of transformation will depend in part upon factors beyond our control, such as the willingness of governments, regulators and other policy groups to embrace RRPs as a desired alternative to continued cigarette smoking. We also recognize that our part in this transformation must be funded from our existing cigarette business. For as long as a significant number of adult smokers continues to smoke, it is critical that the industry be led by responsible and ethical manufacturers. Therefore, during the transformation, we intend to remain a leading international cigarette manufacturer.

We have a range of RRPs in various stages of development, scientific assessment and commercialization. We conduct rigorous scientific assessments of our RRP platforms to substantiate that they reduce exposure to HPHCs and, ultimately, that these products present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to them versus continued smoking. We draw upon a team of expert scientists and engineers from a broad spectrum of scientific disciplines and our extensive learnings of adult consumer preferences to develop and assess our RRPs. Our efforts are guided by the following key objectives:

- to develop RRPs that adult smokers who would otherwise continue to smoke find to be satisfying alternatives to smoking;
- for those adult smokers, our goal is to offer RRPs with a scientifically substantiated risk-reduction profile that approaches as closely as possible that associated with smoking cessation;
- to substantiate the reduction of risk for the individual adult smoker and the reduction of harm to the population as a whole, based on scientific evidence of the highest standard that is made available for scrutiny and review by external independent scientists and relevant regulatory bodies; and
- to advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs, including the communication of scientifically substantiated information to enable adult smokers to make better consumer choices.

Our RRP Platforms: Our product development is based on the elimination of combustion via tobacco heating and other innovative systems for aerosol generation, which we believe is the most promising path to providing a better consumer choice for those who would otherwise continue to smoke. We recognize that no single product will appeal to all adult smokers. Therefore, we are developing a portfolio of products intended to appeal to a variety of distinct adult consumer preferences.

Four RRP platforms are in various stages of development and commercialization readiness:

Platform 1 uses a precisely controlled heating device that we are commercializing under the *IQOS* brand name, into which a specially designed and proprietary tobacco unit is inserted and heated to generate an aerosol. We have conducted a series of clinical studies for this platform, the results of which were included in our submission to the U.S. Food and Drug Administration ("FDA") described below. The results of the first six-month term of the 6+6 month exposure response study were received at the end of 2017, and the related report was completed and submitted to the FDA in the second quarter of 2018. The study showed that all eight of the co-primary clinical risk endpoints moved in the same direction in the group that switched to *IQOS* as observed for smoking cessation, with statistically significant changes in five of the eight endpoints compared with on-going smoking. The results of the second six-month term of the 6+6 month exposure response study were received for analysis in the second quarter of 2018; the related report is under preparation. In addition, as set out in our submission to the FDA referenced above, we completed an 18-month combined chronic toxicity and carcinogenicity study in mice, which was ongoing at the time of our FDA submission. We shared the results with the FDA in August 2018.

Platform 2 uses a pressed carbon heat source which, when ignited, generates a nicotine-containing aerosol by heating tobacco. The results of our pharmacokinetic study (that measured the nicotine pharmacokinetic profile as well as subjective effects) and of our five-day reduced exposure study indicate that this platform could be an acceptable substitute for adult smokers who seek an alternative to cigarettes. The reduced exposure study results showed a substantial reduction in relevant biomarkers of exposure to the measured HPHCs in those who switched to *Platform 2* compared to those who continued to smoke cigarettes over a five-day period. The sustainability of this reduction as well as changes in clinical risk markers were assessed in a three-month reduced exposure study. The results of this study were received at the end of 2017, and the related report was finalized in the second quarter of 2018.

Platform 3 provides an aerosol of nicotine salt formed by the chemical reaction of nicotine with a weak organic acid. We have explored two routes for this platform, one with electronics and one without, and conducted nicotine pharmacokinetic studies with both versions. The results of the pharmacokinetic study related to the version without electronics were received, and the related report was finalized in the fourth quarter of 2018. The results indicate this product's potential as an acceptable alternative to continued cigarette smoking in terms of product satisfaction. We will also initiate a clinical product use and adaptation study.

Platform 4 covers e-vapor products, which are battery-powered devices that produce an aerosol by vaporizing a nicotine-containing liquid solution. Our e-vapor products comprise devices using current generation technology and our new e-vapor mesh technology that addresses certain challenges presented by some e-vapor products currently on the market. Our *IQOS MESH* products are designed to ensure the consistency and quality of the generated aerosol. We conducted a nicotine pharmacokinetic study in 2017. The results of this study were received in the second quarter of 2018 for analysis, and the related report was finalized in the fourth quarter of 2018. The results of this study

indicate that *IQOS MESH* products are an effective means of nicotine delivery while being a satisfying alternative for e-cigarette users. We will also initiate a clinical reduced exposure study to measure selected biomarkers of exposure to HPHCs and assess changes in clinical risk markers.

After we receive the results of our scientific studies mentioned above, in accordance with standard scientific practices, we intend to share the conclusions in scientific forums and to submit them for inclusion in peer-reviewed publications.

The research and development expense for our RRP portfolio accounted for 92%, 74% and 72% of our total research and development expense for the years ended December 31, 2018, 2017 and 2016, respectively. The research and development expense for the years ended December 31, 2018, 2017 and 2016, is set forth in Item 8, Note 14. *Additional Information* to the consolidated financial statements.

Commercialization of RRPs: We are building a new product category and tailor our commercialization strategy to the characteristics of each specific market. We focus our commercialization efforts on consumer retail experience, guided consumer trials and customer care, as well as digital communication programs. In order to accelerate switching to *IQOS*, our initial market introductions typically entail one-on-one consumer engagement and introductory device discounts. These initial commercialization efforts require substantial investment, which we believe will moderate over time.

In 2014, we introduced the *IQOS* heated tobacco system in pilot city launches in Nagoya, Japan, and in Milan, Italy. Since then, we have continuously expanded our commercialization activities, and *IQOS* is currently available for sale in 44 markets in key cities or nationwide.

In Japan, we observed a slower-than-initially-projected growth in the first half of 2018, as we are now reaching different socio-economic strata with more conservative consumers who show a slower pace of adoption than early adopters. In late 2018 we began implementing a number of initiatives intended to specifically address the needs of these adult smokers.

We estimate that while some *IQOS* users are experimenting with competitive products, only a very small percentage of converted *IQOS* users in Japan switch to those products.

We estimate that only a very small percentage of adult smokers who convert to *IQOS* switch back to cigarettes.

We have been integrating the production of our heated tobacco units into a number of our existing manufacturing facilities and progressing with our plans to build manufacturing capacity for our other RRP platforms.

An adequate supply chain for our RRP portfolio, including the supply of electronic devices, is important to our business. We work with two electronics manufacturing service providers for the supply of our *IQOS* devices and a small number of other providers for other products in our RRP portfolio and related accessories. Although we work closely with these service providers on monitoring their production capability and financial health, the commercialization of our RRPs could be adversely affected if they are unable to meet their commitments. The production of our RRP portfolio requires various metals, and we believe that there is an adequate supply of such metals in the world markets to satisfy our current and anticipated production requirements. However, some components and materials necessary for the production of our RRPs, including those for the electronic devices, are obtained from single or limited sources, and can be subject to industry-wide shortages and price fluctuations. Our inability to secure an adequate supply of such components and materials could negatively impact the commercialization of our RRPs.

Our *IQOS* devices are subject to standard product warranties generally for a period of 12 months from the date of purchase or such other periods as required by law. We discuss product warranties in more detail in Note 5. *Product Warranty*. The significance of warranty claims is dependent on a number of factors including warranty policies and product failure rates and may increase with the number of devices sold.

Our commercialization efforts for the other RRP platforms are as follows:

- We currently market our e-vapor products in several markets, including Ireland and the U.K. In July 2018, we pilot-launched *IQOS MESH*, one of our Platform 4 products, in London, U.K.

- We completed a small-scale city test of *TEEPS*, our Platform 2 product, that we had initiated in December 2017 in Santo Domingo, the Dominican Republic, and are working on improving this product and incorporating our learnings into our future plans.

- Depending on the outcome of the use and adaptation study described above, we plan to conduct a consumer test of our Platform 3 product.

RRP Regulation and Taxation: RRPs contain nicotine and are not risk-free. We therefore support science-based regulation and taxation of RRPs. Regulation and taxation should differentiate between cigarettes and products that present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to these products versus continued smoking and recognize a continuum of risk for tobacco and other nicotine-containing products. Regulation should provide minimum standards for RRPs and specific rules for product assessment methodologies, ingredients, labelling and consumer communication, and should ensure that the public is informed about the health risks of all combustible and non-combustible tobacco and nicotine-containing products. Regulation, as well as industry practices, should reflect the fact that youth should not consume nicotine in any form.

Some governments have banned or are seeking to ban or severely restrict emerging tobacco and nicotine-containing products such as our RRPs and communication of truthful and non-misleading information about such products. These regulations might foreclose or unreasonably restrict adult consumer access even to products that might be shown to be a better consumer choice than continuing to smoke. We oppose such blanket bans and unreasonable restrictions of products that have the potential to present less risk of harm compared to continued smoking. By contrast, we support regulation that sets clear standards and propels innovation to benefit adult smokers who would otherwise continue to smoke.

In the United States, an established regulatory framework for assessing "Modified Risk Tobacco Products" and "New Tobacco Products" exists under the jurisdiction of the FDA. We submitted to the FDA a Modified Risk Tobacco Product Application ("MRTPA") for *IQOS* in December 2016, and a Premarket Tobacco Product Application ("PMTA") for *IQOS* in March 2017. In May 2017, the FDA formally accepted and filed our MRTPA for substantive scientific review and, in June 2017, the FDA opened the period for the public to provide comments on our application. The FDA recently announced the public comment period would close on February 11, 2019. In August 2017, the FDA completed a preliminary review of our PMTA and accepted our application for substantive review. The FDA referred our MRTPA to the Tobacco Product Scientific Advisory Committee ("TPSAC"). TPSAC held a meeting on January 24 and January 25, 2018 to discuss our MRTPA. The recommendations and votes of TPSAC are not binding on the FDA. By regulation, the FDA's decision on our MRTPA will take into account, in addition to the views of TPSAC, scientific evidence as well as comments, data and information submitted by interested persons.

Separately, in July 2017, the FDA issued a policy announcement aiming to explore the potential of nicotine reduction in cigarettes in conjunction with the availability of less harmful products that deliver nicotine for adults who choose to use such products. In July 2018, as part of a public consultation procedure, we submitted our views on this topic to the FDA.

Following a rise in the use of e-vapor products among minors in the U.S., in November 2018, the FDA announced a policy framework for the prevention of the use of tobacco and nicotine-containing products by youth. Under the policy framework, flavored e-vapor products, other than tobacco, mint and menthol flavors, may be sold only in age-restricted retail outlets or through online sites with heightened age verification requirements. The FDA also announced its intention to remove from the market certain e-vapor products that are appealing or marketed to youth. While we do not sell products in the U.S. and therefore are not subject to these actions, we continue to support regulation and industry practices that reflect the fact that youth should not consume nicotine in any form.

Future FDA actions may influence the regulatory approach of other governments.

Until recently, there were no countries with specific product standards for heated tobacco products. Effective July 2017 and March 2018, respectively, Russia and Ukraine adopted standards that set minimum quality and safety requirements for the consumables and defined methods for demonstrating the absence of combustion, and the product standards in Kazakhstan that come into force in March 2019, also cover devices. We expect and encourage other governments to consider similar product standards going forward.

In the EU, all EU Member States and Norway have transposed the EU Tobacco Products Directive, including the provisions on novel tobacco products, such as heated tobacco units, and e-cigarettes. Most of the EU Member States require a notification submitted six months before the intended placing on the market of a novel tobacco product, while some require pre-market authorizations for the introduction of such products. To date, we have filed a comprehensive dossier summarizing our scientific assessment of *IQOS* in 22 Member States.

In addition, in Italy, in April 2018, we submitted under recent legislation an application for *HEETS*, used with the *IQOS* device, requesting regulatory recognition of the reduction of toxic substances and potential risk reduction resulting from switching to this product compared to continued cigarette smoking. In January 2019, our application was not granted primarily on the grounds of insufficient data and questions of methodology. Due to the constraints of the review process, we had been unable to supplement the application with all the data we subsequently filed with the FDA and to address methodological questions during the review. We plan to submit a new application where we will clarify the concerns raised by the decision and further strengthen our application by submitting additional evidence that became available since we submitted our first application, consistent with our FDA filing. We are confident that our evidence supports our application.

Also, pursuant to local regulations, in May 2018, we submitted a scientific dossier to regulatory authorities in Bulgaria with the notification of our intent to communicate to adult smokers the reduction of measured HPHCs and potential risk reduction resulting from switching to *IQOS* compared to continued cigarette smoking.

To date, several governmental agencies published their scientific findings that pertain to our RRPs.

On December 12, 2017, at the request of the U.K. Department of Health and Public Health England, the U.K. Committee on Toxicity published its assessment of the risk of heated tobacco products relative to cigarette smoking. This assessment included analysis of scientific data for two heated tobacco products, one of which was *IQOS*. The assessment concluded that, while still harmful to health, compared with the known risks from cigarettes, heated tobacco products are probably less harmful. Subsequently, on February 6, 2018, Public Health England published a report stating that the available evidence suggests that heated tobacco products may be considerably less harmful than cigarettes and more harmful than e-cigarettes.

On May 5, 2018, the German Federal Institute for Risk Assessment ("BfR") published a study on the *IQOS* aerosol relative to cigarette smoke using the Health Canada Intense Smoking Regimen. BfR found reductions in selected HPHCs in a range of 80-99%. This publication indicates that significant reductions in the levels of selected toxicants are likely to reduce toxicant exposure, which BfR stated might be regarded as a discrete benefit compared to combustible cigarettes.

On May 15, 2018, the Dutch National Institute for Public Health and Environment ("RIVM") published a factsheet on novel tobacco products that heat rather than burn tobacco, focusing on *IQOS*. RIVM analyzed the *IQOS* aerosol and concluded that the use of heated tobacco units with *IQOS*, while still harmful to health, is probably less harmful than continued smoking.

On June 7, 2018, the Korean Food and Drug Administration ("KFDA") issued a statement on products that heat rather than burn tobacco. The KFDA tested three heat-not-burn products, one of which was *IQOS*. The KFDA confirmed that the levels of the nine HPHCs tested in the aerosol of these products were on average approximately 90% lower compared to those measured in the cigarette smoke of the top five cigarette brands in South Korea. However, the KFDA stated that it could not establish that the tested heat-not-burn products are less harmful than cigarettes. In October 2018, our Korean affiliate filed a request with a local court seeking information underlying KFDA's analysis, conclusions and public statements.

On August 17, 2018, the Science & Technology Committee of the U.K. House of Commons published a report of its inquiry into e-cigarettes and heat-not-burn tobacco products. The report concluded that e-cigarettes are significantly less harmful to health than smoking tobacco. The report also observed that for those smokers who don't accept e-cigarettes, heat-not-burn tobacco products may offer a public health benefit despite their relative risk. The report called for a risk-proportionate regulatory environment for both e-cigarettes and heat-not-burn tobacco products and noted that e-cigarettes should remain the least taxed, cigarettes the most taxed, with heat-not-burn products falling between the two. The U.K. Committee on Advertising Practice announced the removal of a prohibition of health claims in the advertising of e-cigarettes in the U.K. effective November 2018, with a review of the impact of this decision on market practices 12 months thereafter.

We make our scientific findings publicly available for scrutiny and peer review through several channels, including our websites. From time to time, adult consumers, competitors, members of the scientific community, and others inquire into our scientific methodologies, challenge our scientific conclusions or request further study of certain aspects of our RRPs and their health effects. We are committed to a robust and open scientific debate but believe that such debate should be based on accurate and reliable scientific information. We seek to provide accurate and reliable scientific information about our RRPs; nonetheless, we may not be able to prevent third-party dissemination of false, misleading or unsubstantiated information about these products. The dissemination of scientifically unsubstantiated information or studies with a strong confirmation bias by third parties may cause confusion among adult smokers and affect their decision to switch to better alternatives to continued smoking, such as our RRPs.

To date, we have been largely successful in demonstrating to regulators that our RRPs are not cigarettes due to the absence of combustion, and as such they are generally taxed either as a separate category or as other tobacco products, which typically yields more favorable tax rates than cigarettes. Although we believe that this is sensible from the public health perspective, we cannot guarantee that regulators will continue this approach.

There can be no assurance that we will succeed in our efforts to replace cigarettes with RRPs or that regulation will allow us to commercialize RRPs in all markets, to communicate scientifically substantiated risk-reduction claims, or to treat RRPs differently from cigarettes.

Legal Challenges to RRPs: We face various administrative and legal challenges related to certain RRP activities, including allegations concerning product classification, advertising restrictions, corporate communications, *IQOS* coach activities, scientific substantiation, product liability, and unfair competition. While we design our programs to

comply with relevant regulations, we expect these or similar challenges to continue as we expand our efforts to commercialize RRPs and to communicate publicly. The outcomes of these matters may affect our RRP commercialization and public communication activities and performance in one or more countries.

Our RRP Business Development Initiatives: In December 2013, we established a strategic framework with Altria Group, Inc. ("Altria") setting out terms on how the parties would collaborate to develop and commercialize e-vapor products and commercialize two of our RRPs in the U.S. In late 2018, Altria announced that it will participate in the e-vapor category only through another e-vapor company in

which Altria has agreed to acquire a minority interest. We intend to hold discussions with Altria about e-vapor products following completion of its investment. Regarding heated tobacco products, as discussed above, we are seeking regulatory approval from the FDA to market *IQOS* in the U.S., and these efforts are not affected by Altria's e-vapor announcement.

Other Developments: On September 12, 2017, we announced our support of the Foundation for a Smoke-Free World. We agreed to contribute $80 million per year over the next 12 years, as specified in the agreement. We made an initial contribution of $4.5 million in 2017, the first annual contribution of $80 million in the first quarter of 2018 and the second annual contribution of $80 million in the first quarter of 2019. The Foundation is an independent body and is governed by its independent Board of Directors. The Foundation's role, as set out in its corporate charter, includes funding research in the field of tobacco harm reduction, encouraging measures that reduce the harm caused by smoking, and assessing the effect of reduced cigarette consumption on the industry value chain.

Governmental Investigations

From time to time, we are subject to governmental investigations on a range of matters, including tax, customs, antitrust, advertising, and labor practices. We describe certain matters pending in Thailand and South Korea in Item 8, Note 18. *Contingencies*.

In November 2010, a WTO panel issued its decision in a dispute relating to facts that arose from August 2006 between the Philippines and Thailand concerning a series of Thai customs and tax measures affecting cigarettes imported by PM Thailand into Thailand (see Item 8, Note 18. *Contingencies* for additional information). The WTO panel decision, which was upheld by the WTO Appellate Body, concluded that Thailand had no basis to find that PM Thailand's declared customs values and taxes paid were too low, as alleged by the DSI in 2009. The decision also created obligations for Thailand to revise its laws, regulations, or practices affecting the customs valuation and tax treatment of future cigarette imports. Thailand agreed in September 2011 to fully comply with the decision by October 2012. The Philippines asserts that to date Thailand has not fully complied with the WTO panel decision. The Philippines has repeatedly expressed concerns with ongoing investigations by Thailand of PM Thailand, including those that led to the criminal charges described in Item 8, Note 18. *Contingencies*, and has commenced two formal proceedings at the WTO to challenge criminal charges against PM Thailand arguing that the criminal charges appear to be based on grounds not supported by WTO customs valuation rules and inconsistent with several decisions already taken by Thai Customs and other Thai governmental agencies. The Philippines has also asserted that the demand notices received by PM Thailand from the Thai Customs Department in November 2017, described in Note 8. *Contingencies*, are inconsistent with Thailand's WTO obligations. On November 12, 2018, the WTO issued its decision agreeing with the Philippines that criminal charges against PM Thailand and seven former and current employees in connection with import entries of cigarettes from the Philippines during the period of July 2003 to June 2006 are inconsistent with WTO customs valuation rules. In January 2019, Thailand appealed this decision.

U.S. GAAP Treatment of Argentina as a Highly Inflationary Economy

Following the categorization of Argentina by the International Practices Task Force of the Center for Audit Quality as a country with a three-year cumulative inflation rate greater than 100%, the country is considered highly inflationary in accordance with U.S. GAAP. Consequently, we began to account for the operations of our Argentinian affiliates as highly inflationary, and to treat the U.S. dollar as the functional currency of the affiliates, effective July 1, 2018. The move to highly inflationary accounting in Argentina reduced our currency-neutral net revenue growth by approximately 0.6 points in 2018.

Acquisitions

We discuss our acquisitions in Item 8, Note 6. *Acquisitions* to our consolidated financial statements.

Investments in Unconsolidated Subsidiaries and Equity Securities

We discuss our investments in unconsolidated subsidiaries and equity securities in Item 8, Note 4. *Investments in Unconsolidated Subsidiaries and Other Related Party* and Item 8, Note 16. *Fair Value Measurements* to our consolidated financial statements.

Trade Policy

We are subject to various trade restrictions imposed by the United States of America and countries in which we do business (“Trade Sanctions”), including the trade and economic sanctions administered by the U.S. Department of the Treasury's Office of Foreign Assets Control and the U.S. Department of State. It is our policy to comply fully with these Trade Sanctions.

Tobacco products are agricultural products under U.S. law and are not technological or strategic in nature. From time to time we make sales in countries subject to Trade Sanctions, either where such sanctions do not apply to our business or pursuant to exemptions or licenses.

To our knowledge, none of our commercial arrangements results in the governments of any country identified by the U.S. government as a state sponsor of terrorism, nor entities controlled by those governments, receiving cash or acting as intermediaries in violation of U.S. laws.

We do not sell products in Iran, Sudan, North Korea and Syria. From time to time, we explore opportunities to sell our products in one or more of these countries, as permitted by law.

Certain states within the U.S. have enacted legislation permitting state pension funds to divest or abstain from future investment in stocks of companies that do business with certain countries that are sanctioned by the U.S. We do not believe such legislation has had a material effect on the price of our shares.

2018 compared with 2017

The following discussion compares operating results within each of our reportable segments for 2018 with 2017.

Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units.

European Union:

Financial Summary - Years Ended December 31, (in millions)	**2018**	**2017**	**Change Fav./(Unfav.) Total**	**Change Fav./(Unfav.) Excl. Curr.**	**Variance Fav./(Unfav.) Total**	**Variance Fav./(Unfav.) Cur-rency**	**Variance Fav./(Unfav.) Price**	**Variance Fav./(Unfav.) Vol/ Mix**	**Variance Fav./(Unfav.) Cost/ Other**
Net Revenues	**$ 9,298**	$ 8,318	11.8%	5.9%	$ 980	$ 489	$ 248	$ 243	$ —
Operating Income	**$ 4,105**	$ 3,691	11.2%	2.9%	$ 414	$ 308	$ 248	$ 116	$ (258)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues, excluding favorable currency, increased by 5.9%, reflecting a favorable pricing variance, driven notably by Germany and Italy, partly offset by France, and favorable volume/mix, driven predominantly by heated tobacco unit volume, notably in the Czech Republic, Germany and Italy, partly offset by unfavorable cigarette volume in France, Germany and Italy.

The net revenues of the European Union segment include $865 million in 2018 and $269 million in 2017 related to the sale of RRPs.

Operating income, excluding favorable currency, increased by 2.9%, reflecting: a favorable pricing variance; favorable volume/mix, notably in Bulgaria, the Czech Republic and Poland, partly offset by France, Norway and the United Kingdom; partly offset by higher manufacturing costs and marketing, administration and research costs, primarily related to investments behind reduced-risk products across the Region.

European Union - Total Market, PMI Shipment & Market Share Commentaries

Total market, PMI shipment volume and market share performance are shown in the table below:

European Union Key Data	**Full-Year**		
	2018	**2017**	**Change % / pp**
Total Market (billion units)	**484.3**	492.4	(1.7%)
PMI Shipment Volume (million units)			
Cigarettes	**179,622**	187,293	(4.1%)
Heated Tobacco Units	**5,977**	1,889	+100.0%
Total European Union	**185,599**	189,182	(1.9%)
PMI Market Share			
Marlboro	**18.5%**	18.8%	(0.3)
L&M	**6.9%**	6.9%	—
Chesterfield	**5.9%**	6.0%	(0.1)
Philip Morris	**2.9%**	3.1%	(0.2)
HEETS	**1.2%**	0.3%	0.9
Others	**3.1%**	3.2%	(0.1)
Total European Union	**38.5%**	38.3%	0.2

The estimated total market in the EU decreased by 1.7% to 484.3 billion units, or by 1.5% excluding the net impact of estimated trade inventory movements, notably due to:

- France, down by 9.2%, primarily reflecting the impact of significant excise tax-driven price increases and an increase in the prevalence of illicit trade;
- Germany, down by 2.2%, primarily reflecting the impact of price increases;
- Italy, down by 1.3%, primarily reflecting the impact of price increases; and
- the United Kingdom, down by 6.9%, primarily reflecting the impact of price increases;

partly offset by

- Poland, up by 3.7%, primarily driven by a decrease in the prevalence of illicit trade.

Our total shipment volume decreased by 1.9% to 185.6 billion units, or by 1.0% excluding the net impact of estimated distributor inventory movements, notably due to:

- France, down by 6.4%, or by 5.0% excluding the net impact of estimated distributor inventory movements, primarily due to a lower total market, partly offset by higher market share, notably of *Marlboro* and *Philip Morris*;
- Germany, down by 1.8%, primarily due to the lower total market, partly offset by higher market share; and

- Italy, down by 4.1%, or by 1.9% excluding the net impact of estimated distributor inventory movements, primarily due to the lower total market and lower cigarette market share.

Our Regional market share increased by 0.2 points to 38.5%, with gains in Belgium, Bulgaria, the Canary Islands, Croatia, Denmark, France, Germany, Greece, Hungary, Latvia, Lithuania, Luxembourg, Portugal, Romania, the Slovak Republic and Slovenia.

Eastern Europe:

Financial Summary - Years Ended December 31, (in millions)	2018	2017	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Cur-rency	Price	Vol/ Mix	Cost/ Other
Net Revenues	**$ 2,921**	$ 2,711	7.7%	12.1%	$ 210	$ (118)	$ 286	$ 42	$ —
Operating Income	**$ 902**	$ 887	1.7%	13.1%	$ 15	$ (101)	$ 286	$ (92)	$ (78)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues, excluding unfavorable currency, increased by 12.1%, reflecting a favorable pricing variance, mainly driven by Russia and Ukraine, and favorable volume/mix, primarily driven by heated tobacco unit volume, notably in Russia, partly offset by unfavorable cigarette volume/mix, notably in Russia.

The net revenues of the Eastern Europe segment include $324 million in 2018 and $55 million in 2017 related to the sale of RRPs.

Operating income, excluding unfavorable currency, increased by 13.1%, mainly reflecting a favorable pricing variance, partly offset by: unfavorable volume/mix, predominantly due to unfavorable mix in Russia, and higher manufacturing and marketing, administration and research costs, notably reflecting increased investments behind reduced-risk products, primarily in Russia.

Eastern Europe - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in Eastern Europe decreased by 7.1% to 416.7 billion units, notably due to:

- Russia, down by 8.4%, primarily reflecting the timing and impact of excise tax-driven retail price increases, as well as an increase in the prevalence of illicit trade; and

- Ukraine, down by 8.1%, primarily reflecting the timing and impact of excise tax-driven retail price increases and an increase in the prevalence of illicit trade.

Our Regional market share increased by 0.6 points to 27.3%.

PMI Shipment Volume (million units)	Full-Year 2018	2017	Change
Cigarettes	**108,718**	119,398	(8.9%)
Heated Tobacco Units	**4,979**	674	+100.0%
Total Eastern Europe	**113,697**	120,072	(5.3%)

Our total shipment volume decreased by 5.3% to 113.7 billion units, notably in:

- Russia, down by 6.1%, due to the lower total market, partly offset by higher total market share driven by heated tobacco unit share, partially offset by lower cigarette market share, notably due to mid-price *L&M* and low-price *Bond Street*, reflecting the impact of down-trading to competitive products, partly offset by *Philip Morris*; and

- Ukraine, down by 8.8%, mainly due to the lower total market, partly offset by higher total market share driven by heated tobacco unit volume.

Middle East & Africa:

Financial Summary - Years Ended December 31, (in millions)	2018	2017	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Currency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/Mix	Variance Fav./(Unfav.) Cost/Other
Net Revenues	**$ 4,114**	$ 3,988	3.2 %	8.0 %	$ 126	$ (193)	$ 19	$ 84	$ 216
Operating Income	**$ 1,627**	$ 1,884	(13.6 %)	0.3 %	$ (257)	$ (263)	$ 19	$ 13	$ (26)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles. "Cost/Other" also includes the currency-neutral net revenue variance, unrelated to volume/mix and price components, attributable to fees for certain distribution rights billed to customers in certain markets in the ME&A Region. This immaterial presentational change, made in conjunction with the new revenue recognition standard, is prospective only.

Net revenues, excluding unfavorable currency, increased by 8.0%, reflecting: a favorable "cost/other" variance, as described above; a favorable pricing variance, driven notably by Egypt and Turkey, partly offset by Saudi Arabia; and favorable volume/mix, primarily driven by PMI Duty Free, reflecting higher heated tobacco unit volume, and Turkey, partly offset by the GCC, notably Saudi Arabia and the UAE, reflecting the impact of retail price increases following the introduction of excise tax in June and October 2017, respectively, and VAT in January 2018.

The net revenues of the Middle East & Africa segment include $382 million in 2018 and $94 million in 2017 related to the sale of RRPs.

Operating income, excluding unfavorable currency, increased by 0.3%, mainly reflecting: a favorable pricing variance, and favorable volume/mix, primarily driven by PMI Duty Free and Turkey, partly offset by Saudi Arabia and the UAE. These favorable variances were partly offset by higher manufacturing costs predominantly related to reduced-risk products, partly offset by lower marketing, administration and research costs.

Middle East & Africa - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in the Middle East & Africa increased by 0.4% to 590.1 billion units, notably driven by:

- Turkey, up by 11.6%, primarily reflecting a reduction in the prevalence of illicit trade;

partly offset by

- Algeria, down by 8.5%, or by 0.6% excluding the net impact of estimated trade inventory movements mainly associated with the timing of excise tax announcements in 2018 compared to 2017; and

- The GCC, notably Saudi Arabia and the UAE, down by 21.1% and 23.9%, respectively, primarily reflecting the impact of price increases and the introduction of the new excise tax in 2017, and VAT in January 2018.

Our Regional market share increased by 0.3 points to 23.8%.

PMI Shipment Volume (million units)	Full-Year 2018	Full-Year 2017	Change
Cigarettes	**136,605**	136,759	(0.1)%
Heated Tobacco Units	**3,403**	907	+100.0%
Total Middle East & Africa	**140,008**	**137,666**	**1.7 %**

Our total shipment volume increased by 1.7% to 140.0 billion units, notably in:

- Turkey, up by 10.8%, reflecting a higher total market, partly offset by lower market share; and

- PMI Duty Free, up by 6.6%, reflecting higher heated tobacco shipment volume;

partly offset by

- the GCC, notably Saudi Arabia and the UAE, down by 32.5% and 55.6%, respectively, reflecting the lower total market and market share due to the impact of excise tax and VAT-driven price increases.

South & Southeast Asia:

Financial Summary - Years Ended December 31, (in millions)	2018	2017	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Cur-rency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/ Mix	Variance Fav./(Unfav.) Cost/ Other
Net Revenues	**$ 4,656**	$ 4,417	5.4%	10.9%	$ 239	$ (244)	$ 548	$ (65)	$ —
Operating Income	**$ 1,747**	$ 1,514	15.4%	23.6%	$ 233	$ (124)	$ 548	$ (126)	$ (65)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues, excluding unfavorable currency, increased by 10.9%, reflecting: a favorable pricing variance, driven principally by Indonesia and the Philippines, partly offset by Thailand; partly offset by unfavorable volume/mix, mainly due to unfavorable mix in Indonesia, partly offset by favorable volume in Pakistan, the Philippines and Thailand.

Operating income, excluding unfavorable currency, increased by 23.6%, mainly driven by a favorable pricing variance, partly offset by unfavorable volume/mix, mainly due to Indonesia, partly offset by Pakistan and Thailand, and higher manufacturing and marketing, administration and research costs.

South & Southeast Asia - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in South & Southeast Asia increased by 1.8% to 756.7 billion, notably driven by:

- Pakistan, up by 31.2% or approximately 14.1 billion units, notably reflecting an increase in the duty-paid market driven by a reduction in the prevalence of illicit trade. Excluding the net impact of estimated trade inventory movements, the total market was up by 17.7%;

partly offset by

- the Philippines, down by 2.2%, primarily reflecting the impact of excise tax-driven retail price increases; and

- Thailand, down by 2.7%, primarily reflecting the impact of excise tax-driven price increases.

Our Regional market share increased by 0.4 points to 23.5%.

PMI Shipment Volume (million units)	Full-Year 2018	Full-Year 2017	Change
Cigarettes	**178,469**	171,600	4.0%
Heated Tobacco Units	**—**	—	—%
Total South & Southeast Asia	**178,469**	**171,600**	**4.0%**

Our total shipment volume increased by 4.0% to 178.5 billion units, notably driven by:

- Pakistan, up by 27.0%, reflecting the higher total market, partly offset by lower market share;

- the Philippines, up by 1.1%, mainly reflecting higher market share, driven by *Marlboro* and *Fortune*, partly offset by a lower total market; and

-

Thailand, up by 67.1%, mainly reflecting higher market share driven by the price repositioning of the *L&M 7.1* variant in 2017 and its subsequent distribution expansion during 2018.

East Asia & Australia:

Financial Summary - Years Ended December 31, (in millions)	2018	2017	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Currency	Price	Vol/ Mix	Cost/ Other
Net Revenues	**$ 5,580**	$ 6,373	(12.4%)	(13.4%)	$ (793)	$ 62	$ 55	$ (910)	$ —
Operating Income	**$ 1,851**	$ 2,608	(29.0%)	(28.9%)	$ (757)	$ (2)	$ 55	$ (704)	$ (106)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues, excluding favorable currency, decreased by 13.4%, reflecting an unfavorable volume/mix, substantially due to Japan, primarily related to the net impact of estimated distributor inventory movements described below, as well as Australia, partly offset by favorable heated tobacco unit volume in Korea. The unfavorable volume/mix was partly offset by a favorable pricing variance, driven by: Australia and Japan; partly offset by Korea, mainly due to higher excise tax.

The net revenues of the East Asia & Australia segment include $2,506 million in 2018 and $3,218 million in 2017 related to the sale of RRPs.

Operating income, excluding unfavorable currency, decreased by 28.9%, mainly reflecting: unfavorable volume/mix, substantially due to Japan, as well as Australia, partly offset by favorable heated tobacco unit volume in Korea; and higher marketing, administration and research costs, primarily related to investments behind reduced-risk products. These unfavorable variances were partly offset by a favorable pricing variance, as well as favorable manufacturing costs related to Japan.

East Asia & Australia - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in East Asia & Australia, excluding China, decreased by 3.4% to 311.5 billion units, notably due to:

- Australia, down by 8.4%, primarily reflecting the impact of excise tax-driven retail price increases;
- Japan, down by 2.4%, or down by 2.8% excluding the impact of estimated trade and consumer inventory movements following the October 1 excise tax-driven retail price increases;
- Korea, down by 1.5%, or by 2.2% excluding the net impact of estimated trade inventory movements, partly related to the implementation of graphic health warnings in December 2018; and
- Taiwan, down by 13.5%, or by 12.7% excluding the net impact of estimated trade inventory movements, mainly due to excise tax-driven retail price increases in 2017.

Our Regional market share, excluding China, increased by 2.0 points to 27.4%.

PMI Shipment Volume (million units)	Full-Year 2018	Full-Year 2017	Change
Cigarettes	**56,163**	62,653	(10.4%)
Heated Tobacco Units	**26,866**	32,729	(17.9%)
Total East Asia & Australia	**83,029**	95,382	(13.0%)

Our total shipment volume decreased by 13.0% to 83.0 billion units, due to lower cigarette shipment volume, principally in Japan and Korea, and lower heated tobacco unit shipment volume in Japan, reflecting the net impact of estimated distributor inventory movements, partly offset by higher heated tobacco unit shipment volume in Korea.

Excluding the net impact of an estimated 15.5 billion units of total distributor inventory movements, primarily due to Japan, reflecting net unfavorable heated tobacco unit inventory movements of approximately 17.3 billion units, partly offset by net favorable cigarette inventory movements of approximately 1.8 billion units, our total shipment volume increased by 3.7%.

Our total shipment volume in Japan was down by 21.0%. Excluding the net impact of estimated distributor inventory movements of approximately 15.6 billion units, our total shipment volume in Japan was up by 3.1%, reflecting an increase of heated tobacco unit volume of 40.3%, partly offset by a decline of cigarette volume of 15.8%.

Latin America & Canada:

Financial Summary - Years Ended December 31,			**Change Fav./(Unfav.)**		**Variance Fav./(Unfav.)**				
(in millions)	**2018**	**2017**	**Total**	**Excl. Curr.**	**Total**	**Cur-rency**	**Price**	**Vol/ Mix**	**Cost/ Other**
Net Revenues	**$ 3,056**	$ 2,941	3.9%	7.3%	$ 115	$ (99)	$ 332	$ (118)	$ —
Operating Income	**$ 1,145**	$ 997	14.8%	18.1%	$ 148	$ (32)	$ 332	$ (111)	$ (41)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues, excluding unfavorable currency, increased by 7.3%, reflecting a favorable pricing variance across the Region, notably in Argentina, Canada and Mexico, partly offset by unfavorable volume/mix, mainly due to Argentina and Canada.

The net revenues of the Latin America & Canada segment include $19 million in 2018 and $4 million in 2017 related to the sale of RRPs.

Operating income, excluding unfavorable currency, increased by 18.1%, largely reflecting a favorable pricing variance, partly offset by: unfavorable volume/mix, mainly in Argentina and Canada, as well as higher marketing, administration and research costs, primarily related to increased investment behind reduced-risk products in the Region, coupled with an unfavorable comparison to 2017 related to the sale of assets, primarily in the Dominican Republic.

Latin America & Canada - Total Market, PMI Shipment Volume and Market Share Commentaries

The estimated total market in Latin America & Canada decreased by 4.8% to 202.7 billion units, primarily due to the impact of cumulative price increases in Argentina, down by 3.2%, Brazil, down by 6.2%, Canada, down by 5.1% and Colombia, down by 12.1%, where excise tax reform drove an approximate 25% increase in retail prices in January 2018.

Our Regional market share increased by 0.4 points to 40.0%.

PMI Shipment Volume (million units)	**Full-Year**		
	2018	**2017**	**Change**
Cigarettes	**80,738**	84,223	(4.1%)
Heated Tobacco Units	**147**	27	+100.0%
Total Latin America & Canada	**80,885**	84,250	(4.0%)

Our total shipment volume decreased by 4.0% to 80.9 billion units, notably due to:

- Argentina, down by 4.6%, reflecting the lower total market and lower market share; and
- Colombia, down by 11.0%, reflecting the lower total market.

2017 compared with 2016

The following discussion compares operating results within each of our reportable segments for 2017 with 2016.

Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units.

European Union:

Financial Summary - Years Ended December 31, (in millions)	2017	2016	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Currency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/Mix
Net Revenues	$ 8,318	$ 8,162	1.9 %	1.4 %	$ 156	$ 45	$ 156	$ (45)
Operating Income	$ 3,691	$ 3,920	(5.8)%	(4.7)%	$ (229)	$ (43)	$ 156	$ (119)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues, excluding favorable currency, increased by 1.4%, due to price increases, partially offset by unfavorable volume/mix.

The net revenues of the European Union segment include $269 million in 2017 and $57 million in 2016 related to the sale of RRPs.

Operating income, excluding unfavorable currency, decreased by 4.7%, due primarily to higher marketing, administration and research costs (primarily related to increased investment behind reduced-risked products) and unfavorable volume/mix, partly offset by price increases and lower manufacturing costs.

European Union - Total Market, PMI Shipment & Market Share Commentaries

Total market, PMI shipment volume and market share performance were as follows:

European Union Key Data	Full-Year 2017	Full-Year 2016	Change % / pp
Total Market (billion units)	492.4	501.8	(1.9)%
PMI Shipment Volume (million units)			
Cigarettes	187,293	193,586	(3.3)%
Heated Tobacco Units	1,889	224	+100.0%
Total European Union	189,182	193,810	(2.4)%
PMI Market Share			
Marlboro	18.8 %	19.0 %	(0.2)
L&M	6.9 %	6.9 %	—
Chesterfield	6.0 %	5.9 %	0.1
Philip Morris	3.1 %	3.2 %	(0.1)
HEETS	0.3 %	— %	0.3
Others	3.2 %	3.3 %	(0.1)
Total European Union	38.3 %	38.3 %	—

The estimated total market in the European Union decreased by 1.9% to 492.4 billion units. Our Regional market share was flat at 38.3%, with gains in France, Germany and Poland offset by declines in Italy and Spain.

Our total shipment volume decreased by 2.4% to 189.2 billion units, or by 1.9% excluding estimated net inventory movements, notably in Italy and Spain.

Eastern Europe:

Financial Summary - Years Ended December 31, (in millions)	2017	2016	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Cur-rency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/ Mix
Net Revenues	$ 2,711	$ 2,484	9.1 %	(0.1)%	$ 227	$ 229	$ 157	$ (159)
Operating Income	$ 887	$ 890	(0.3)%	(9.8)%	$ (3)	$ 84	$ 157	$ (164)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues, excluding favorable currency, decreased by 0.1%, due to unfavorable volume/mix, partially offset by price increases.

The net revenues of the Eastern Europe segment include $55 million in 2017 and $6 million in 2016 related to the sale of RRPs.

Operating income, excluding favorable currency, decreased by 9.8%, due primarily to unfavorable volume/mix and higher marketing, administration and research costs, partly offset by price increases.

Eastern Europe - Total Market, PMI Shipment Volume & Market Share Commentaries

The estimated total market in Eastern Europe decreased by 6.2% to 448.4 billion units. Our Regional market share was down at 26.7%.

PMI Shipment Volume (million units)	Full-Year 2017	Full-Year 2016	Change
Cigarettes	119,398	129,456	(7.8)%
Heated Tobacco Units	674	64	+100.0%
Total Eastern Europe	120,072	129,520	(7.3)%

Our total shipment volume decreased by 7.3% to 120.1 billion units, mainly reflecting: lower cigarette shipment volume in Russia and Ukraine; partly offset by higher heated tobacco unit shipment volume.

Middle East & Africa:

Financial Summary - Years Ended December 31, (in millions)	2017	2016	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Cur-rency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/ Mix
Net Revenues	$ 3,988	$ 4,516	(11.7)%	(0.2)%	$ (528)	$ (520)	$ 207	$ (215)
Operating Income	$ 1,884	$ 1,990	(5.3)%	(5.0)%	$ (106)	$ (6)	$ 207	$ (180)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues, excluding unfavorable currency, decreased by 0.2% due to unfavorable volume/mix, partially offset by price increases.

The net revenues of the Middle East & Africa segment include $94 million in 2017 and $4 million in 2016 related to the sale of RRPs.

Operating income, excluding unfavorable currency, decreased by 5.0%, due primarily to unfavorable volume/mix and higher marketing, administration and research costs, partly offset by price increases.

Middle East & Africa - Total Market, PMI Shipment Volume & Market Share Commentaries

The estimated total market in Middle East & Africa was flat at 587.5 billion units. Our Regional market share decreased by 0.4 points to 23.5%.

PMI Shipment Volume (million units)	**Full-Year**		
	2017	**2016**	**Change**
Cigarettes	136,759	141,937	(3.6%)
Heated Tobacco Units	907	36	+100.0%
Total Middle East & Africa	137,666	141,973	(3.0%)

Our total shipment volume decreased by 3.0% to 137.7 billion units, mainly reflecting: lower cigarette shipment volume in Saudi Arabia - where our cigarette shipment volume declined by 35.8%, impacted by the new excise tax implemented in June 2017 that resulted in the doubling of retail prices; partly offset by higher cigarette shipment volume in North Africa, notably Algeria, and higher heated tobacco unit shipment volume.

South & Southeast Asia:

Financial Summary - Years Ended December 31,			**Change Fav./(Unfav.)**		**Variance Fav./(Unfav.)**			
(in millions)	**2017**	**2016**	**Total**	**Excl. Curr.**	**Total**	**Cur-rency**	**Price**	**Vol/ Mix**
Net Revenues	$ 4,417	$ 4,396	0.5%	1.9%	$ 21	$ (63)	$ 353	$ (269)
Operating Income	$ 1,514	$ 1,474	2.7%	5.9%	$ 40	$ (47)	$ 353	$ (236)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues, excluding unfavorable currency, increased by 1.9%, due to price increases, partially offset by unfavorable volume/mix.

Operating income, excluding unfavorable currency, increased by 5.9%, due primarily to price increases, partially offset by unfavorable volume/mix, higher marketing, administration and research costs and higher manufacturing costs.

South & Southeast Asia - Total Market, PMI Shipment Volume & Market Share Commentaries

The estimated total market in South & Southeast Asia decreased by 2.5% to 743.6 billion units. Our Regional market share decreased by 1.2 points to 23.1%.

PMI Shipment Volume (million units)	Full-Year		
	2017	2016	Change
Cigarettes	171,600	185,279	(7.4%)
Heated Tobacco Units	—	—	— %
Total South & Southeast Asia	171,600	185,279	(7.4%)

Our total shipment volume decreased by 7.4% to 171.6 billion units, mainly reflecting: lower cigarette shipment volume in Indonesia, Pakistan - impacted by excise tax-driven price increases in 2017 and an increase in the prevalence of illicit trade - and the Philippines.

East Asia & Australia:

Financial Summary - Years Ended December 31, (in millions)	2017	2016	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Currency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/Mix
Net Revenues	$ 6,373	$ 4,285	48.7%	50.5%	$ 2,088	$ (74)	$ 206	$ 1,956
Operating Income	$ 2,608	$ 1,691	54.2%	58.7%	$ 917	$ (75)	$ 206	$ 858

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues, excluding unfavorable currency, increased by 50.5%, due to favorable volume/mix and price increases.

The net revenues of the East Asia & Australia segment include $3.2 billion in 2017 and $666 million in 2016 related to the sale of RRPs.

Operating income, excluding unfavorable currency, increased by 58.7%, due primarily to favorable volume/mix, price increases and lower manufacturing costs, partially offset by higher marketing, administration and research costs (principally related to increased investment behind reduced-risk products).

East Asia & Australia - Total Market, PMI Shipment Volume & Market Share Commentaries

The estimated total market in East Asia & Australia, excluding China, decreased by 4.5% to 322.5 billion units. Our Regional market share, excluding China, increased by 2.6 points to 25.4%.

PMI Shipment Volume (million units)	Full-Year		
	2017	2016	Change
Cigarettes	62,653	74,750	(16.2%)
Heated Tobacco Units	32,729	7,070	+100.0%
Total East Asia & Australia	95,382	81,820	16.6 %

Our total shipment volume increased by 16.6% to 95.4 billion units, reflecting: higher heated tobacco unit shipment volume, mainly in Japan and Korea, partly offset by lower cigarette shipment volume in Japan and Korea.

Our total shipment volume benefited from the favorable net impact of estimated combustible and heated tobacco unit inventory movements, which were driven by approximately 8.5 billion units net in Japan, reflecting: the increasing demand for *HeatSticks*, anticipated to further increase in the first quarter of 2018 following a planned lifting of the restriction on *IQOS* device sales; the establishment of appropriate distributor inventory levels of heated tobacco units, given the current high dependence on a single manufacturing center; and the transition

from air freight to sea freight of heated tobacco units, largely completed in the fourth quarter of 2017. Excluding the impact of total estimated net inventory movements, our total shipment volume increased by 6.3%.

Latin America & Canada:

Financial Summary - Years Ended December 31, (in millions)	2017	2016	Change Fav./(Unfav.) Total	Change Fav./(Unfav.) Excl. Curr.	Variance Fav./(Unfav.) Total	Variance Fav./(Unfav.) Cur-rency	Variance Fav./(Unfav.) Price	Variance Fav./(Unfav.) Vol/ Mix
Net Revenues	$ 2,941	$ 2,842	3.5%	5.4%	$ 99	$ (54)	$ 307	$ (154)
Operating Income	$ 997	$ 938	6.3%	13.8%	$ 59	$ (70)	$ 307	$ (152)

"Cost/Other" in the above table reflects the currency-neutral variances of: cost of sales (excluding the volume/mix cost component); marketing, administration and research costs; asset impairment and exit costs; and amortization of intangibles.

Net revenues, excluding unfavorable currency, increased by 5.4%, due to price increases, partially offset by unfavorable volume/mix.

The net revenues of the Latin America & Canada segment include $4 million in 2017 and $1 million in 2016 related to the sale of RRPs.

Operating income, excluding unfavorable currency, increased by 13.8%, due primarily to price increases, partially offset by unfavorable volume/mix and higher manufacturing costs.

Latin America & Canada - Total Market, PMI Shipment Volume & Market Share Commentaries

The estimated total market in Latin America & Canada decreased by 3.9% to 212.9 billion units. Our Regional market share decreased by 0.1 point to 39.6%.

PMI Shipment Volume (million units)	Full-Year 2017	Full-Year 2016	Change
Cigarettes	84,223	87,938	(4.2%)
Heated Tobacco Units	27	—	— %
Total Latin America & Canada	84,250	87,938	(4.2%)

Our total shipment volume decreased by 4.2% to 84.3 billion units, mainly due to lower cigarette shipment volume in Argentina, Brazil, Canada, Colombia and Mexico.

Financial Review

Ÿ Net Cash Provided by Operating Activities

Net cash provided by operating activities of $9.5 billion for the year ended December 31, 2018, increased by $0.6 billion from the comparable 2017 period. Excluding the 2017 cash flow movements resulting from the Tax Cuts and Jobs Act as described below, as well as unfavorable currency movements of $0.2 billion, the increase in cash flows provided by operating activities was attributable to higher net earnings and the 2017 payment in the South Korean tax matter (see Item 8, Note 18. *Contingencies* for additional information), partially offset by other movements.

The variance in our working capital movements was essentially flat, excluding the 2017 movements related to the Tax Cuts and Jobs Act, as the positive impact of timing of receivables collections and the timing of inventory movements and related excise tax payments were largely offset by the transition tax installment payments in 2018 of $0.2 billion and cash used for accounts payable in 2018 reflecting higher *IQOS* device purchases in the fourth quarter of 2017.

Net cash provided by operating activities of $8.9 billion for the year ended December 31, 2017, increased by $0.8 billion from the comparable 2016 period. While the impacts of the Tax Cuts and Jobs Act reduced net earnings by $1.6 billion, there was no net impact on operating cash flows for the year, as the changes in deferred taxes and income taxes payable offset the net earnings impact. Excluding the impact of the Tax Cuts and Jobs Act as well as favorable currency movements of $0.4 billion, the increase in cash flows provided by operating activities can be attributed to higher net earnings offset by working capital and other movements.

At December 31, 2017, PMI recorded an income tax payable of $1.7 billion representing the transition tax of $2.2 billion, partially offset by foreign tax credits related to foreign withholding taxes previously paid of $0.5 billion. The income tax payable is due over an 8-year period beginning in 2018. For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements.

Ÿ Net Cash Used in Investing Activities

Net cash used in investing activities of $1.0 billion for the year ended December 31, 2018, decreased by $2.1 billion from the comparable 2017 period. This decrease was due principally to lower cash collateral posted to secure derivatives designated as net investment hedges of Euro assets principally related to changes in exchange rates between the Euro and the U.S. dollar, and lower capital expenditures. For further details on our derivatives designated as net investment hedges, see Item 8, Note 15. *Financial Instruments*.

Net cash used in investing activities of $3.1 billion for the year ended December 31, 2017, increased by $2.2 billion from the comparable 2016 period. This increase in net cash used of $2.2 billion was due principally to cash collateral posted to secure derivatives designated as net investment hedges of Euro assets following the strengthening of the Euro versus the U.S. dollar, and higher capital expenditures. For further details on our derivatives designated as net investment hedges, see Item 8, Note 15. *Financial Instruments*.

Our capital expenditures were $1.4 billion in 2018, $1.5 billion in 2017 and $1.2 billion in 2016. The 2018 expenditures were primarily related to our ongoing investments in RRPs to support capacity expansion (notably for heated tobacco units). We expect total capital expenditures in 2019 of approximately $1.1 billion (including capital expenditures related to our ongoing investment in RRPs), to be funded by operating cash flows.

Ÿ Net Cash Used in Financing Activities

During 2018, net cash used in financing activities was $9.7 billion, compared with net cash used in financing activities of $2.8 billion during 2017 and $5.4 billion in 2016.

The 2018 change was due primarily to lower proceeds from long-term debt issuances (primarily the $6.9 billion proceeds in 2017 from our U.S. dollar and Euro debt issuances), and the purchase of the remaining 49% interest in our Costa Rican affiliates in 2018. For further details on the purchase of the remaining 49% interest in our Costa Rican affiliates, see Item 8, Note 6. *Acquisitions*.

The 2017 change was due primarily to higher proceeds from long-term debt issuances (primarily the $6.9 billion proceeds in 2017 from our U.S. dollar and Euro debt issuances versus the $3.5 billion proceeds in 2016 from our U.S. dollar and Euro debt issuances).

Dividends paid in 2018, 2017 and 2016 were $6.9 billion, $6.5 billion and $6.4 billion, respectively.

Ÿ Debt and Liquidity

We define cash and cash equivalents as short-term, highly liquid investments, readily convertible to known amounts of cash that mature within a maximum of three months and have an insignificant risk of change in value due to interest rate or credit risk changes. As a policy, we do not hold any investments in structured or equity-linked products. Our cash and cash equivalents are predominantly held in demand deposits with institutions that have investment-grade long-term credit rating. As part of our cash management strategy and in order to manage counterparty exposure, we also enter into reverse repurchase agreements. Such agreements are collateralized with government or corporate securities held by a custodial bank and, at maturity, cash is paid back to PMI, and the collateral is returned to the bank. While we entered into these agreements during the periods and had an average balance during 2018 and 2017 of $0.3 billion and $0.9 billion, respectively, we had a zero balance both at December 31, 2018, and December 31, 2017.

We utilize long-term and short-term debt financing, including a commercial paper program that is regularly used to finance ongoing liquidity requirements, as part of our overall cash management strategy. Our ability to access the capital and credit markets as well as overall dynamics of these markets may impact borrowing costs. We expect that the combination of our long-term and short-term debt financing, the commercial paper program and the committed credit facilities, coupled with our operating cash flows, will enable us to meet our liquidity requirements.

Credit Ratings – The cost and terms of our financing arrangements as well as our access to commercial paper markets may be affected by applicable credit ratings. On March 1, 2018, Standard & Poor's affirmed our long-term credit rating at "A" and short-term at "A-1", and revised our outlook to "Stable" from "Negative." On August 3, 2018, Fitch affirmed our long-term credit rating at "A" and short-term at "F1", and revised our outlook to "Stable" from "Negative." At February 7, 2019, our credit ratings and outlook by major credit rating agencies were as follows:

	Short-term	Long-term	Outlook
Moody's	P-1	A2	Stable
Standard & Poor's	A-1	A	Stable
Fitch	F1	A	Stable

Credit Facilities – On January 28, 2019, we entered into an agreement to extend the term of our $2.0 billion 364-day revolving credit facility from February 5, 2019, to February 4, 2020.

At February 7, 2019, our committed credit facilities were as follows:

(in billions)

Type	Committed Credit Facilities
364-day revolving credit, expiring February 4, 2020	**$ 2.0**
Multi-year revolving credit, expiring February 28, 2021	**2.5**
Multi-year revolving credit, expiring October 1, 2022	**3.5**
Total facilities	**$ 8.0**

At February 7, 2019, there were no borrowings under the committed credit facilities, and the entire committed amounts were available for borrowing.

All banks participating in our committed credit facilities have an investment-grade long-term credit rating from the credit rating agencies. We continuously monitor the credit quality of our banking group, and at this time we are not aware of any potential non-performing credit provider.

Each of these facilities requires us to maintain a ratio of consolidated earnings before interest, taxes, depreciation and amortization ("consolidated EBITDA") to consolidated interest expense of not less than 3.5 to 1.0 on a rolling four-quarter basis. At December 31, 2018, our ratio calculated in accordance with the agreements was 10.5 to 1.0. These facilities do not include any credit rating triggers, material adverse change clauses or any provisions that could require us to post collateral. We expect to continue to meet our covenants. The terms "consolidated EBITDA" and "consolidated interest expense," both of which include certain adjustments, are defined in the facility agreements previously filed with the U.S. Securities and Exchange Commission.

In addition to the committed credit facilities discussed above, certain of our subsidiaries maintain short-term credit arrangements to meet their respective working capital needs. These credit arrangements, which amounted to approximately $3.3 billion at December 31, 2018, and $2.8 billion at December 31, 2017, are for the sole use of our subsidiaries. Borrowings under these arrangements amounted to $730 million at December 31, 2018, and $499 million at December 31, 2017.

Commercial Paper Program – We continue to have access to liquidity in the commercial paper market through programs in place in the U.S. and in Europe having an aggregate issuance capacity of $8.0 billion. At December 31, 2018, and December 31, 2017, we had no commercial paper outstanding. The average commercial paper balance outstanding during 2018 and 2017 was $3.4 billion and $5.2 billion, respectively.

Sale of Accounts Receivable – To mitigate credit risk and enhance cash and liquidity management we sell trade receivables to unaffiliated financial institutions. These arrangements allow us to sell, on an ongoing basis, certain trade receivables without recourse. The trade receivables sold are generally short-term in nature and are removed

from the consolidated balance sheets. We sell trade receivables under two types of arrangements, servicing and nonservicing.

Our operating cash flows were positively impacted by the amount of the trade receivables sold and derecognized from the consolidated balance sheets, which remained outstanding with the unaffiliated financial institutions. The trade receivables sold that remained outstanding under these arrangements as of December 31, 2018, 2017 and 2016, were $1.0 billion, $1.1 billion and $0.7 billion, respectively. The net proceeds received are included in cash provided by operating activities in the consolidated statements of cash flows.

For further details, see Item 8, Note 20. *Sale of Accounts Receivable* to our consolidated financial statements.

Debt – Our total debt was $31.8 billion at December 31, 2018, and $34.3 billion at December 31, 2017. Our total debt is primarily fixed rate in nature. For further details, see Item 8, Note 7. *Indebtedness*. The weighted-average all-in financing cost of our total debt was 2.5% in 2018, compared to 2.6% in 2017. See Item 8, Note 16. *Fair Value Measurements* to our consolidated financial statements for a discussion of our disclosures related to the fair value of debt. The amount of debt that we can issue is subject to approval by our Board of Directors.

On February 14, 2017, we filed a shelf registration statement with the U.S. Securities and Exchange Commission, under which we may from time to time sell debt securities and/or warrants to purchase debt securities over a three-year period.

During 2018, we had no public debt issuances.

The weighted-average time to maturity of our long-term debt was 9.6 years at the end of 2018 and 9.4 years at the end of 2017.

- **Off-Balance Sheet Arrangements and Aggregate Contractual Obligations**

We have no off-balance sheet arrangements, including special purpose entities, other than guarantees and contractual obligations discussed below.

Guarantees – At December 31, 2018, we were contingently liable for $0.3 billion of guarantees of our own performance, which were primarily related to excise taxes on the shipment of our products. There is no liability in the consolidated financial statements associated with these guarantees. At December 31, 2018, our third-party guarantees were insignificant.

Aggregate Contractual Obligations – The following table summarizes our contractual obligations at December 31, 2018:

		Payments Due			
(in millions)	**Total**	**2019**	**2020-2021**	**2022-2023**	**2024 and Thereafter**
Long-term debt [1]	$31,268	$4,054	$7,098	$4,358	$15,758
Interest on borrowings [2]	10,360	902	1,542	1,258	6,658
Operating leases [3]	772	147	176	95	354
Purchase obligations [4]:					
Inventory and production costs	4,217	2,492	1,165	406	154
Other	2,629	1,070	842	227	490
	6,846	3,562	2,007	633	644
Other long-term liabilities [5]	1,916	78	346	448	1,044
	$51,162	$8,743	$11,169	$6,792	$24,458

[1] Amounts represent the expected cash payments at the face value of our long-term debt and capital lease obligations. For further details, see Item 8, Note 7. *Indebtedness* to our consolidated financial statements.

[2] Amounts represent the expected cash payments of our interest expense on our long-term debt, including the current portion of long-term debt. Interest on our fixed-rate debt is presented using the stated interest rate. Interest on our variable debt is estimated using the rate in effect at December 31, 2018. Amounts exclude the amortization of debt discounts, the amortization of loan fees and fees for lines of credit that would be included in interest expense in the consolidated statements of earnings.

[3] Amounts represent the minimum rental commitments under non-cancelable operating leases.

[4] Purchase obligations for inventory and production costs (such as raw materials, indirect materials and supplies, packaging, co-manufacturing arrangements, storage and distribution) are commitments for projected needs to be utilized in the normal course of business. Other purchase obligations include commitments for marketing, advertising, capital expenditures, information technology and professional services. Other purchase obligations also include the expected future contributions to the Foundation for a Smoke-Free World. For further details see *Business Environment—Other Developments*. Arrangements are considered purchase obligations if a contract specifies all significant terms, including fixed or minimum quantities to be purchased, a pricing structure and approximate timing of the transaction. Amounts represent the minimum commitments under non-cancelable contracts. Any amounts reflected on the consolidated balance sheet as accounts payable and accrued liabilities are excluded from the table above.

[5] Other long-term liabilities consist primarily of transition tax (as discussed in Item 8, Note 11. *Income Taxes* to our consolidated financial statements), postretirement health care costs and accruals established for employment costs. The following long-term liabilities included on the consolidated balance sheet are excluded from the table above: accrued pension and postemployment costs, tax contingencies, insurance accruals and other accruals. We are unable to estimate the timing of payments (or contributions in the case of accrued pension costs) for these items. Currently, we anticipate making pension contributions of approximately $119 million in 2019, based on current tax and benefit laws (as discussed in Item 8, Note 13. *Benefit Plans* to our consolidated financial statements).

Ÿ **Equity and Dividends**

We discuss our stock awards as of December 31, 2018, in Item 8, Note 9. *Stock Plans* to our consolidated financial statements.

During 2018, 2017 and 2016, we did not repurchase any shares under a share repurchase program, and we do not presently intend to repurchase shares of our common stock in 2019.

Dividends paid in 2018 were $6.9 billion. During the second quarter of 2018, our Board of Directors approved a 6.5% increase in the quarterly dividend to $1.14 per common share. As a result, the present annualized dividend rate is $4.56 per common share.

Market Risk

Ÿ ***Counterparty Risk*** **-** We predominantly work with financial institutions with strong short- and long-term credit ratings as assigned by Standard & Poor's and Moody's. These banks are also part of a defined group of relationship banks. Non-investment grade institutions are only used in certain emerging markets to the extent required by local business needs. We have a conservative approach when it comes to choosing financial counterparties and financial instruments. As such we do not invest or hold investments in any structured or equity-linked products. The majority of our cash and cash equivalents is currently invested in demand deposits maturing within less than 30 days.

We continuously monitor and assess the credit worthiness of all our counterparties.

Ÿ ***Derivative Financial Instruments -*** We operate in markets outside of the U.S., with manufacturing and sales facilities in various locations throughout the world. Consequently, we use certain financial instruments to manage our foreign currency and interest rate exposure. We use derivative financial instruments principally to reduce our exposure to market risks resulting from fluctuations in foreign exchange and interest rates by creating offsetting exposures. We are not a party to leveraged derivatives and, by policy, do not use derivative financial instruments for speculative purposes.

See Item 8, Note 15. *Financial Instruments,* Item 8, Note 16. *Fair Value Measurements* and Item 8, Note 19. *Balance Sheet Offsetting* to our consolidated financial statements for further details on our derivative financial instruments and the related collateral arrangements.

Ÿ ***Value at Risk -*** We use a value at risk computation to estimate the potential one-day loss in the fair value of our interest-rate-sensitive financial instruments and to estimate the potential one-day loss in pre-tax earnings of our foreign currency price-sensitive derivative financial instruments. This computation includes our debt, short-term investments, and foreign currency forwards, swaps and options. Anticipated transactions, foreign currency trade payables and receivables, and net investments in foreign subsidiaries, which the foregoing instruments are intended to hedge, were excluded from the computation.

The computation estimates were made assuming normal market conditions, using a 95% confidence interval. We use a "variance/co-variance" model to determine the observed interrelationships between movements in interest rates and various currencies. These interrelationships were determined by observing interest rate and forward currency rate movements over the preceding quarter for determining value at risk at December 31, 2018 and 2017, and over each of the four preceding quarters for the calculation of average value at risk amounts during each year. The values of foreign currency options do not change on a one-to-one basis with the underlying currency and were valued accordingly in the computation.

The estimated potential one-day loss in fair value of our interest-rate-sensitive instruments, primarily debt, under normal market conditions and the estimated potential one-day loss in pre-tax earnings from foreign currency instruments under normal market conditions, as calculated in the value at risk model, were as follows:

	Pre-Tax Earnings Impact			
(in millions)	**At December 31, 2018**	**Average**	**High**	**Low**
Instruments sensitive to:				
Foreign currency rates	**$19**	**$20**	**$23**	**$19**

	Fair Value Impact			
(in millions)	**At December 31, 2018**	**Average**	**High**	**Low**
Instruments sensitive to:				
Interest rates	**$142**	**$132**	**$152**	**$96**

	Pre-Tax Earnings Impact			
(in millions)	**At December 31, 2017**	**Average**	**High**	**Low**
Instruments sensitive to:				
Foreign currency rates	$27	$49	$58	$27

	Fair Value Impact			
(in millions)	**At December 31, 2017**	**Average**	**High**	**Low**

Instruments sensitive to:				
Interest rates	$118	$150	$173	$118

The value at risk computation is a risk analysis tool designed to statistically estimate the maximum probable daily loss from adverse movements in interest and foreign currency rates under normal market conditions. The computation does not purport to represent actual losses in fair value or earnings to be incurred by us, nor does it consider the effect of favorable changes in market rates. We cannot predict

actual future movements in such market rates and do not present these results to be indicative of future movements in market rates or to be representative of any actual impact that future changes in market rates may have on our future results of operations or financial position.

Contingencies

See Item 3 and Item 8, Note 18. *Contingencies* to our consolidated financial statements for a discussion of contingencies.

Cautionary Factors That May Affect Future Results

Forward-Looking and Cautionary Statements

We may from time to time make written or oral forward-looking statements, including statements contained in filings with the SEC, in reports to stockholders and in press releases and investor webcasts. You can identify these forward-looking statements by use of words such as "strategy," "expects," "continues," "plans," "anticipates," "believes," "will," "estimates," "intends," "projects," "goals," "targets" and other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts.

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Our RRPs constitute a new product category in its early stages that is less predictable than our mature cigarette business. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from those anticipated, estimated or projected. Investors should bear this in mind as they consider forward-looking statements and whether to invest in or remain invested in our securities. In connection with the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995, we are identifying important factors that, individually or in the aggregate, could cause actual results and outcomes to differ materially from those contained in any forward-looking statements made by us; any such statement is qualified by reference to the following cautionary statements. We elaborate on these and other risks we face throughout this document, particularly in Item 1A. *Risk Factors* and *Business Environment* of this section. You should understand that it is not possible to predict or identify all risk factors. Consequently, you should not consider this discussion of potential risks or uncertainties to be complete. We do not undertake to update any forward-looking statement that we may make from time to time, except in the normal course of our public disclosure obligations.

Item 7A. *Quantitative and Qualitative Disclosures About Market Risk.*

The information called for by this Item is included in Item 7, *Market Risk*.

Item 8. ***Financial Statements and Supplementary Data.***

Consolidated Statements of Earnings

(in millions of dollars, except per share data)

for the years ended December 31,	2018	2017	2016
Revenues including excise taxes	**$ 79,823**	$ 78,098	$ 74,953
Excise taxes on products	**50,198**	49,350	48,268
Net revenues (Notes 2 & 21)	**29,625**	28,748	26,685
Cost of sales	**10,758**	10,432	9,391
Gross profit	**18,867**	18,316	17,294
Marketing, administration and research costs	**7,408**	6,647	6,317
Amortization of intangibles	**82**	88	74
Operating income	**11,377**	11,581	10,903
Interest expense, net (Note 14)	**665**	914	891
Pension and other employee benefit costs (Note 13)	**41**	78	88
Earnings before income taxes	**10,671**	10,589	9,924
Provision for income taxes (Note 11)	**2,445**	4,307	2,768
Equity investments and securities (income)/loss, net	**(60)**	(59)	(94)
Net earnings	**8,286**	6,341	7,250
Net earnings attributable to noncontrolling interests	**375**	306	283
Net earnings attributable to PMI	**$ 7,911**	$ 6,035	$ 6,967
Per share data (Note 10):			
Basic earnings per share	**$ 5.08**	$ 3.88	$ 4.48
Diluted earnings per share	**$ 5.08**	$ 3.88	$ 4.48

See notes to consolidated financial statements.

Consolidated Statements of Comprehensive Earnings

(in millions of dollars)

for the years ended December 31,	2018	2017	2016
Net earnings	**$ 8,286**	$ 6,341	$ 7,250
Other comprehensive earnings (losses), net of income taxes:			
Change in currency translation adjustments:			
Unrealized gains (losses), net of income taxes of ($47) in 2018, $620 in 2017 and ($101) in 2016	**(812)**	330	(14)
(Gains)/losses transferred to earnings, net of income taxes of $0 in 2018, 2017 and 2016	**—**	(2)	5
Change in net loss and prior service cost:			
Net gains (losses) and prior service costs, net of income taxes of $65 in 2018, ($17) in 2017 and $78 in 2016	**(1,046)**	523	(460)
Amortization of net losses, prior service costs and net transition costs, net of income taxes of ($43) in 2018, ($31) in 2017 and ($43) in 2016	**218**	228	224
Change in fair value of derivatives accounted for as hedges:			
Gains (losses) recognized, net of income taxes of ($4) in 2018, $8 in 2017 and ($4) in 2016	**24**	(44)	8
(Gains) losses transferred to earnings, net of income taxes of $5 in 2018, $2 in 2017 and ($3) in 2016	**(31)**	(11)	30
Total other comprehensive earnings (losses)	**(1,647)**	1,024	(207)
Total comprehensive earnings	**6,639**	7,365	7,043
Less comprehensive earnings attributable to:			
Noncontrolling interests	**304**	306	233
Comprehensive earnings attributable to PMI	**$ 6,335**	$ 7,059	$ 6,810

See notes to consolidated financial statements.

Consolidated Balance Sheets
(in millions of dollars, except share data)

at December 31,	2018	2017
Assets		
Cash and cash equivalents	**$ 6,593**	$ 8,447
Trade receivables (less allowances of $25 in 2018 and $25 in 2017)	**2,950**	3,194
Other receivables	**614**	544
Inventories:		
Leaf tobacco	**2,318**	2,606
Other raw materials	**1,405**	1,563
Finished product	**5,081**	4,637
	8,804	8,806
Other current assets	**481**	603
Total current assets	**19,442**	21,594
Property, plant and equipment, at cost:		
Land and land improvements	**600**	639
Buildings and building equipment	**3,975**	3,989
Machinery and equipment	**9,096**	8,976
Construction in progress	**886**	962
	14,557	14,566
Less: accumulated depreciation	**7,356**	7,295
	7,201	7,271
Goodwill (Note 3)	**7,189**	7,666
Other intangible assets, net (Note 3)	**2,278**	2,432
Investments in unconsolidated subsidiaries and equity securities (Notes 4 & 16)	**1,269**	1,074
Deferred income taxes	**977**	1,007
Other assets	**1,445**	1,924
Total Assets	**$ 39,801**	$ 42,968

See notes to consolidated financial statements.

at December 31,	2018	2017
Liabilities		
Short-term borrowings (Note 7)	**$ 730**	$ 499
Current portion of long-term debt (Note 7)	**4,054**	2,506
Accounts payable	**2,068**	2,242
Accrued liabilities:		
Marketing and selling	**732**	708
Taxes, except income taxes	**5,088**	5,324
Employment costs	**794**	856
Dividends payable	**1,783**	1,669
Other	**1,366**	1,346
Income taxes (Note 11)	**576**	812
Total current liabilities	**17,191**	15,962
Long-term debt (Note 7)	**26,975**	31,334
Deferred income taxes	**898**	799
Employment costs	**3,083**	2,271
Income taxes and other liabilities (Note 11)	**2,393**	2,832
Total liabilities	**50,540**	53,198
Contingencies (Note 18)		
Stockholders' (Deficit) Equity		
Common stock, no par value (2,109,316,331 shares issued in 2018 and 2017)	**—**	—
Additional paid-in capital	**1,939**	1,972
Earnings reinvested in the business	**31,014**	29,859
Accumulated other comprehensive losses	**(10,111)**	(8,535)
	22,842	23,296
Less: cost of repurchased stock (554,736,610 and 556,098,569 shares in 2018 and 2017, respectively)	**35,301**	35,382
Total PMI stockholders' deficit	**(12,459)**	(12,086)
Noncontrolling interests	**1,720**	1,856
Total stockholders' deficit	**(10,739)**	(10,230)
Total Liabilities and Stockholders' (Deficit) Equity	**$ 39,801**	$ 42,968

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(in millions of dollars)

for the years ended December 31,	2018	2017	2016
CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES			
Net earnings	**$ 8,286**	$ 6,341	$ 7,250
Adjustments to reconcile net earnings to operating cash flows:			
Depreciation and amortization	**989**	875	743
Deferred income tax (benefit) provision	**(100)**	(501)	182
Cash effects of changes in:			
Receivables, net	**53**	(92)	(1,009)
Inventories	**(613)**	730	(695)
Accounts payable	**(51)**	425	373
Accrued liabilities and other current assets	**910**	(554)	1,477
Income taxes	**(135)**	1,370	(209)
Pension plan contributions	**(110)**	(66)	(191)
Other	**249**	384	156
Net cash provided by operating activities	**9,478**	8,912	8,077
CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES			
Capital expenditures	**(1,436)**	(1,548)	(1,172)
Investments in unconsolidated subsidiaries and equity securities	**(63)**	(111)	(41)
Net investment hedges	**416**	(1,527)	295
Other	**85**	103	84
Net cash used in investing activities	**(998)**	(3,083)	(834)

See notes to consolidated financial statements.

for the years ended December 31,	2018	2017	2016
CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES			
Short-term borrowing activity by original maturity:			
Net issuances (repayments) - maturities of 90 days or less	**$ 255**	$ (127)	$ (12)
Issuances - maturities longer than 90 days	**—**	1,634	—
Repayments - maturities longer than 90 days	**—**	(1,634)	—
Long-term debt proceeds	**—**	6,850	3,536
Long-term debt repaid	**(2,484)**	(2,551)	(2,393)
Dividends paid	**(6,885)**	(6,520)	(6,378)
Sale (purchase) of subsidiary shares to/(from) noncontrolling interests (Note 6)	**(81)**	5	7
Other	**(456)**	(426)	(173)
Net cash used in financing activities	**(9,651)**	(2,769)	(5,413)
Effect of exchange rate changes on cash, cash equivalents and restricted cash	**(685)**	1,085	(965)
Cash, cash equivalents and restricted cash[1]:			
Increase (Decrease)	**(1,856)**	4,145	865
Balance at beginning of year	**8,476**	4,331	3,466
Balance at end of year	**$ 6,620**	$ 8,476	$ 4,331
Cash Paid:			
Interest	**$ 882**	$ 1,050	$ 1,052
Income taxes	**$ 2,749**	$ 3,403	$ 2,829

[1] Following the adoption of Financial Accounting Standards Update ASU 2016-18, "Statement of Cash Flows: Restricted Cash," the amounts for cash and cash equivalents shown above include restricted cash of $27 million, $29 million and $92 million as of December 31, 2018, 2017 and 2016, respectively, which were included in other current assets in the consolidated balance sheets.

See notes to consolidated financial statements.

Consolidated Statements of Stockholders' (Deficit) Equity

(in millions of dollars, except per share data)

	PMI Stockholders' (Deficit) Equity						
	Common Stock	Additional Paid-in Capital	Earnings Reinvested in the Business	Accumulated Other Comprehensive Losses	Cost of Repurchased Stock	Noncontrolling Interests	Total
Balances, January 1, 2016	$ —	$ 1,929	$ 29,842	$ (9,402)	$ (35,613)	$ 1,768	$ (11,476)
Net earnings			6,967			283	7,250
Other comprehensive earnings (losses), net of income taxes				(157)		(50)	(207)
Issuance of stock awards		37			123		160
Dividends declared ($4.12 per share)			(6,412)				(6,412)
Payments to noncontrolling interests						(219)	(219)
Other		(2)				6	4
Balances, December 31, 2016	—	1,964	30,397	(9,559)	(35,490)	1,788	(10,900)
Net earnings			6,035			306	6,341
Other comprehensive earnings (losses), net of income taxes				1,024			1,024
Issuance of stock awards		20			108		128
Dividends declared ($4.22 per share)			(6,573)				(6,573)
Payments to noncontrolling interests						(255)	(255)
Other		(12)				17	5
Balances, December 31, 2017	—	1,972	29,859	(8,535)	(35,382)	1,856	(10,230)
Net earnings			**7,911**			**375**	**8,286**
Other comprehensive earnings (losses), net of income taxes				**(1,572)**		**(75)**	**(1,647)**
Issuance of stock awards		**47**			**81**		**128**
Dividends declared ($4.49 per share)			**(6,994)**				**(6,994)**
Payments to noncontrolling interests						**(435)**	**(435)**
Adoption of new accounting standards (Note 21)			**238**				**238**
Other (Note 6)		**(80)**		**(4)**		**(1)**	**(85)**
Balances, December 31, 2018	**$ —**	**$ 1,939**	**$ 31,014**	**$ (10,111)**	**$ (35,301)**	**$ 1,720**	**$ (10,739)**

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Note 1.

Background and Basis of Presentation:

Background

Philip Morris International Inc. is a holding company incorporated in Virginia, U.S.A., whose subsidiaries and affiliates and their licensees are engaged in the manufacture and sale of cigarettes and other nicotine-containing products, including reduced-risk products, in markets outside of the United States of America. Throughout these financial statements, the term "PMI" refers to Philip Morris International Inc. and its subsidiaries.

Reduced-risk products ("RRPs") is the term PMI uses to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continued smoking. PMI has a range of RRPs in various stages of development, scientific assessment and commercialization.

Basis of presentation

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities at the dates of the financial statements and the reported amounts of net revenues and expenses during the reporting periods. Significant estimates and assumptions include, among other things: pension and benefit plan assumptions; useful lives and valuation assumptions of goodwill and other intangible assets; marketing programs, and income taxes. Actual results could differ from those estimates.

The consolidated financial statements include PMI, as well as its wholly owned and majority-owned subsidiaries. Investments in which PMI exercises significant influence (generally 20%-50% ownership interest) are accounted for under the equity method of accounting. Investments not accounted for under the equity method of accounting are measured at fair value, if it is readily determinable, with changes in fair value recognized in net income. All intercompany transactions and balances have been eliminated.

To provide a greater focus on both parts of PMI's business — combustible and reduced-risk products — and to support PMI's transformation towards a smoke-free future, effective January 1, 2018, PMI began managing its business in six reportable segments as follows: European Union; Eastern Europe; Middle East & Africa; South & Southeast Asia; East Asia & Australia; and Latin America & Canada. For further details, see Note 12. *Segment Reporting*.

Certain prior years' amounts have been reclassified to conform with the current year's presentation, due primarily to new accounting guidance related to revenue recognition, pension costs and restricted cash and PMI's decision to reorganize its reportable segments. For further details, see the consolidated statements of cash flows, Note 3. *Goodwill and Other Intangible Assets, net*, Note 4. *Investments in Unconsolidated Subsidiaries and Other Related Party*, Note 12. *Segment Reporting,* Note 13. *Benefit Plans* and Note 21. *New Accounting Standards*. The changes did not have a material impact on PMI's consolidated financial position, results of operations or cash flows in any of the periods presented.

Note 2.

Summary of Significant Accounting Policies:

Cash and cash equivalents

Cash equivalents include demand deposits with banks and all highly liquid investments with original maturities of three months or less.

Depreciation

Property, plant and equipment are stated at historical cost and depreciated by the straight-line method over the estimated useful lives of the assets. Machinery and equipment are depreciated over periods ranging from 3 to 15 years, and buildings and building improvements over periods up to 40 years.

Employee benefit plans

PMI provides a range of benefits to its employees and retired employees, including pensions, postretirement health care and postemployment benefits (primarily severance). PMI records annual amounts relating to these plans based on calculations specified under U.S. GAAP. PMI recognizes the funded status of its defined pension and postretirement plans on the consolidated balance sheets. The funded status is measured as the difference between the fair value of the plans assets and the benefit obligation. PMI measures the plan assets and liabilities at the end of the fiscal year. For defined benefit pension plans, the benefit obligation is the projected benefit obligation. For the postretirement health care plans, the benefit obligation is the accumulated postretirement benefit obligation. Any plan with an overfunded status is recognized as an asset, and any plan with an underfunded status is recognized as a liability. Any gains or losses and prior service costs or credits that have not been recognized as a component of net periodic benefit costs are recorded as a component of other comprehensive earnings (losses), net of deferred taxes. PMI elects to recognize actuarial gains/(losses) using the corridor approach.

Foreign currency translation

PMI translates the results of operations of its subsidiaries and affiliates using average exchange rates during each period, whereas balance sheet accounts are translated using exchange rates at the end of each period. Currency translation adjustments are recorded as a component of stockholders' (deficit) equity. In addition, some of PMI's subsidiaries have assets and liabilities denominated in currencies other than their functional currencies, and to the extent those are not designated as net investment hedges, these assets and liabilities generate transaction gains and losses when translated into their respective functional currencies.

Goodwill and non-amortizable intangible assets valuation

PMI tests goodwill and non-amortizable intangible assets for impairment annually or more frequently if events occur that would warrant such review. PMI performs its annual impairment analysis in the second quarter of each year. The impairment analysis involves comparing the fair value of each reporting unit or non-amortizable intangible asset to the carrying value. If the carrying value exceeds the fair value, goodwill or a non-amortizable intangible asset is considered impaired.

Hedging instruments

Derivative financial instruments are recorded at fair value on the consolidated balance sheets as either assets or liabilities. Changes in the fair value of derivatives are recorded each period either in accumulated other comprehensive losses on the consolidated balance sheet or in earnings, depending on whether a derivative is designated and effective as part of a hedge transaction and, if it is, the type of hedge transaction. Gains and losses on derivative instruments reported in accumulated other comprehensive losses are reclassified to the consolidated statements of earnings, into the same line item as the impact of the underlying transaction, in the periods in which operating results are affected by the hedged item. Cash flows from hedging instruments are classified in the same manner as the affected hedged item in the consolidated statements of cash flows.

Impairment of long-lived assets

PMI reviews long-lived assets, including amortizable intangible assets, for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable. PMI performs undiscounted operating cash flow analyses to determine if an impairment exists. For purposes of recognition and measurement of an impairment for assets held for use, PMI groups assets and liabilities at the lowest level for which cash flows are separately identifiable. If an impairment is determined to exist, any related impairment loss is calculated based on fair value. Impairment losses on assets to be disposed of, if any, are based on the estimated proceeds to be received, less costs of disposal.

Impairment of investments in unconsolidated subsidiaries

Investments in unconsolidated subsidiaries are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of the investments may not be recoverable. An impairment loss would be recorded whenever a decline in value of an equity investment below its carrying amount is determined to be other than temporary. PMI determines whether a loss is other than temporary by considering the length of time and extent to which the fair value of the equity investment has been less than the carrying amount, the financial condition of the equity investment, and the intent to retain the investment for a period of time is sufficient to allow for any anticipated recovery in market value.

Income taxes

Income taxes are provided on all earnings for jurisdictions outside the United States. These provisions, as well as state and local income tax provisions, are determined on a separate company basis, and the related assets and liabilities are recorded in PMI's consolidated balance sheets. Significant judgment is required in determining income tax provisions and in evaluating tax positions. PMI recognizes accrued interest and penalties associated with uncertain tax positions as part of the provision for income taxes on the consolidated statements of earnings.

Inventories

Inventories are stated at the lower of cost or market. The first-in, first-out and average cost methods are used to cost substantially all inventories. It is a generally recognized industry practice to classify leaf tobacco inventory as a current asset, although part of such inventory, because of the duration of the aging process, ordinarily would not be utilized within one year.

Marketing costs

PMI supports its products with advertising, adult consumer engagement and trade promotions. Such programs include, but are not limited to, discounts, rebates, in-store display incentives, e-commerce, mobile and other digital platforms, adult consumer activation and promotion activities, as well as costs associated with adult consumer experience outlets and other adult consumer touchpoints and volume-based incentives. Advertising, as well as certain consumer engagement and trade activities costs, are expensed as incurred. Trade promotions are recorded as a reduction of revenues based on amounts estimated as being due to customers at the end of a period, based principally on historical utilization. For interim reporting purposes, advertising and certain consumer engagement expenses are charged to earnings based on estimated sales and related expenses for the full year.

Revenue recognition

PMI recognizes revenue primarily through the manufacture and sale of cigarettes and other nicotine-containing products, including reduced-risk products. The majority of PMI revenues are generated by sales through direct and indirect distribution networks with short-term payment conditions and where control is typically transferred to the customer either upon shipment or delivery of goods. PMI evaluates the transfer of control through evidence of the customer's receipt and acceptance, transfer of title, PMI's right to payment for those products and the customer's ability to direct the use of those products upon receipt. Typically, PMI's performance obligations are satisfied and revenue is recognized either upon shipment or delivery of goods.

In certain instances, PMI facilitates shipping and handling activities after control has transferred to the customer. PMI has elected to record all shipping and handling activities as costs to fulfill a contract. The shipping and handling costs that have not been incurred at the time revenue is recognized are accrued. The transaction price is typically based on the amount billed to the customer and includes estimated variable consideration, where applicable. Such variable consideration is typically not constrained and is estimated based on the most likely amount that PMI expects to be entitled to under the terms of the contracts with customers, historical experience of discount or rebate redemption, where relevant, and the terms of any underlying discount or rebate programs, which may change from time to time as the business and product categories evolve. PMI has elected to exclude excise taxes collected from customers from the measurement of the transaction price, thereby presenting revenues net of excise taxes. Estimated costs associated with warranty programs are generally provided for in cost of sales in the period the related revenues are recognized.

On May 28, 2014, the Financial Accounting Standards Board issued Accounting Standards Update ASU 2014-09, "Revenue from Contracts with Customers." For further details, see Note 21. *New Accounting Standards*.

Stock-based compensation

PMI measures compensation cost for all stock-based awards at fair value on date of grant and recognizes the compensation costs over the service periods for awards expected to vest. PMI's accounting policy is to estimate the number of awards expected to be forfeited and adjust the expense when it is no longer probable that the employee will fulfill the service condition. For further details, see Note 9. *Stock Plans*.

Note 3.

Goodwill and Other Intangible Assets, net:

The movements in goodwill were as follows:

(in millions)	European Union	Eastern Europe	Middle East & Africa	South & Southeast Asia	East Asia & Australia	Latin America & Canada	Total
Balance at January 1, 2017	$ 1,238	$ 281	$ 91	$ 3,030	$ 566	$ 2,118	$ 7,324
Changes due to:							
Currency	181	40	11	(20)	1	129	342
Balances, December 31, 2017	1,419	321	102	3,010	567	2,247	7,666
Changes due to:							
Currency	**(62)**	**(18)**	**(15)**	**(215)**	**(31)**	**(136)**	**(477)**
Balances, December 31, 2018	**$ 1,357**	**$ 303**	**$ 87**	**$ 2,795**	**$ 536**	**$ 2,111**	**$ 7,189**

Goodwill primarily reflects PMI's acquisitions in Canada, Colombia, Greece, Indonesia, Mexico, Pakistan and Serbia, as well as the business combination in the Philippines.

Details of other intangible assets were as follows:

		December 31, 2018			December 31, 2017		
(in millions)	Weighted-Average Remaining Useful Life	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Non-amortizable intangible assets		**$ 1,269**		**$ 1,269**	$ 1,323		$ 1,323
Amortizable intangible assets:							
Trademarks	**19 years**	**1,488**	**$ 608**	**880**	1,559	$ 575	984
Distribution networks	**8 years**	**141**	**82**	**59**	152	79	73
Other*	**10 years**	**107**	**37**	**70**	87	35	52
Total other intangible assets		**$ 3,005**	**$ 727**	**$ 2,278**	$ 3,121	$ 689	$ 2,432

* Includes farmer contracts and intellectual property rights

Non-amortizable intangible assets substantially consist of trademarks from PMI's acquisitions in Indonesia and Mexico.

The decrease in the gross carrying amount of other intangible assets from December 31, 2017, was due primarily to currency movements, partially offset by the purchase of additional intellectual property rights related to PMI's reduced-risk products.

Amortization expense for each of the next five years is estimated to be $82 million or less, assuming no additional transactions occur that require the amortization of intangible assets.

During the second quarter of 2018, PMI completed its annual review of goodwill and non-amortizable intangible assets for potential impairment, and no impairment charges were required as a result of this review.

Note 4.

Investments in Unconsolidated Subsidiaries and Other Related Party:

Investments in unconsolidated subsidiaries:

At December 31, 2018 and 2017, PMI had total investments in unconsolidated subsidiaries of $981 million and $1,074 million, respectively, which were accounted for under the equity method of accounting. Equity method investments are initially recorded at cost. Under the equity method of accounting, the investment is adjusted for PMI's proportionate share of earnings or losses, dividends, capital contributions and movements in currency translation adjustments. The carrying value of our equity method investments at December 31, 2018 and 2017, exceeded our share of the unconsolidated subsidiaries' book value by $835 million and $927 million, respectively. The difference between the investment carrying value and the amount of underlying equity in net assets, excluding $793 million and $873 million attributable to goodwill as of December 31, 2018 and 2017, respectively, is being amortized on a straight-line basis over the underlying assets' estimated useful lives of 10 to 20 years. At December 31, 2018 and 2017, PMI received year-to-date dividends from unconsolidated subsidiaries of $118 million and $120 million, respectively.

PMI holds a 49% equity interest in United Arab Emirates-based Emirati Investors-TA (FZC) (“EITA”). PMI holds an approximate 25% economic interest in Société des Tabacs Algéro-Emiratie (“STAEM”), an Algerian joint venture that is 51% owned by EITA and 49% by the Algerian state-owned enterprise Management et Développement des Actifs et des Ressources Holding ("MADAR Holding"), formerly known as Société Nationale des Tabacs et Allumettes SpA. STAEM manufactures and distributes under license some of PMI’s brands.

PMI holds a 23% equity interest in Megapolis Distribution BV, the holding company of CJSC TK Megapolis, PMI's distributor in Russia.

The initial investments in EITA and Megapolis Distribution BV were recorded at cost and are included in investments in unconsolidated subsidiaries and equity securities on the consolidated balance sheets.

Other related party:

United Arab Emirates-based Trans-Emirates Trading and Investments (FZC) ("TTI") holds a 33% non-controlling interest in Philip Morris Misr LLC ("PMM"), an entity incorporated in Egypt which is consolidated in PMI’s financial statements. PMM sells, under license, PMI brands in Egypt through an exclusive distribution agreement with a local entity that is also controlled by TTI. Amounts in the tables below have been updated to reflect the transactions with this other related party for all periods.

Additionally net revenues in the table below have been updated for all periods to reflect the adoption of ASU 2014-09 "Revenue from Contracts with Customers." For further details, see Note 21. *New Accounting Standards*.

Financial activity with unconsolidated subsidiaries and other related party:

PMI’s net revenues with unconsolidated subsidiaries and the other related party were as follows:

	For the Years Ended December 31,		
(in millions)	**2018**	**2017**	**2016**
Net revenues [(a)]	**$ 2,714**	$ 2,521	$ 2,465

[(a)] Net revenues excludes excise taxes and VAT billed to customers.

PMI’s balance sheet activity related to unconsolidated subsidiaries and the other related party was as follows:

	At December 31,

(in millions)	2018	2017
Receivables	**$ 308**	$ 358

The activity primarily related to agreements with PMI's unconsolidated subsidiaries and the other related party within the Eastern Europe segment and the Middle East & Africa segment. These agreements, which are in the ordinary course of business, are primarily for distribution, contract manufacturing and licenses. PMI eliminated its respective share of all significant intercompany transactions with the equity method investees.

Note 5.

Product Warranty:

PMI's *IQOS* devices are subject to standard product warranties generally for a period of 12 months from the date of purchase or such other periods as required by law. PMI generally provides in cost of sales for the estimated cost of warranty in the period the related revenue is recognized. PMI assesses the adequacy of its accrued product warranties and adjusts the amounts as necessary based on actual experience and changes in future estimates. Factors that affect product warranties may vary across markets but typically include product failure rates, logistics and service delivery costs, and warranty policies. PMI accounts for its product warranties within other accrued liabilities. At December 31, 2018 and December 31, 2017, these amounts were as follows:

	At December 31,	
(in millions)	**2018**	**2017**
Balance at beginning of period	**$ 71**	$ 51
Changes due to:		
Warranties issued	**179**	168
Settlements	**(183)**	(148)
Balance at end of period	**$ 67**	$ 71

Note 6.

Acquisitions:

On March 21, 2018, PMI acquired the remaining 49% interest in Tabacalera Costarricense, S.A. and Mendiola y Compañía, S.A. for a net purchase price of $95 million, which includes $2 million of contingent consideration. As a result, PMI now owns 100% of these Costa Rican affiliates. The purchase of the remaining 49% interest resulted in a decrease to PMI's additional paid-in capital of $86 million.

Note 7.

Indebtedness:

Short-Term Borrowings

At December 31, 2018 and 2017, PMI's short-term borrowings and related average interest rates consisted of the following:

	December 31, 2018		December 31, 2017	
(in millions)	**Amount Outstanding**	**Average Year-End Rate**	**Amount Outstanding**	**Average Year-End Rate**
Commercial paper	**$ —**	**— %**	$ —	— %
Bank loans	**730**	**5.8**	499	5.7

	$	**730**	$ 499

Given the mix of subsidiaries and their respective local economic environments, the average interest rate for bank loans above can vary significantly from day to day and country to country.

The fair values of PMI's short-term borrowings at December 31, 2018 and 2017, based upon current market interest rates, approximate the amounts disclosed above.

Long-Term Debt

At December 31, 2018 and 2017, PMI's long-term debt consisted of the following:

(in millions)	December 31, 2018	December 31, 2017
U.S. dollar notes, 1.375% to 6.375% (average interest rate 3.328%), due through 2044	**$ 20,819**	$ 23,291
Foreign currency obligations:		
Euro notes, 0.625% to 3.125% (average interest rate 2.250%), due through 2037	**8,656**	8,997
Swiss franc notes, 0.750% to 2.000% (average interest rate 1.269%), due through 2024	**1,374**	1,376
Other (average interest rate 3.351%), due through 2024	**180**	176
	31,029	33,840
Less current portion of long-term debt	**4,054**	2,506
	$ 26,975	$ 31,334

Other debt:

Other foreign currency debt above includes mortgage debt in Switzerland and capital lease obligations at December 31, 2018 and December 31, 2017.

Debt Issuances Outstanding:

PMI's debt issuances outstanding at December 31, 2018, were as follows:

(in millions)

Type	Face Value	Interest Rate	Issuance	Maturity
U.S. dollar notes	**$750**	**1.875%**	November 2013	January 2019
U.S. dollar notes	**$700**	**1.625%**	February 2017	February 2019
U.S. dollar notes	**$500**	**1.375%**	February 2016	February 2019
U.S. dollar notes	**$750**	**1.875%**	November 2017	November 2019
U.S. dollar notes	**$300**	**Floating**	February 2017	February 2020
U.S. dollar notes	**$1,000**	**2.000%**	February 2017	February 2020
U.S. dollar notes	**$1,000**	**4.500%**	March 2010	March 2020
U.S. dollar notes	**$750**	**1.875%**	February 2016	February 2021
U.S. dollar notes	**$350**	**4.125%**	May 2011	May 2021
U.S. dollar notes	**$750**	**2.900%**	November 2011	November 2021
U.S. dollar notes	**$500**	**2.625%**	February 2017	February 2022
U.S. dollar notes	**$750**	**2.375%**	August 2017	August 2022

U.S. dollar notes	**$750**	**2.500%**	August 2012	August 2022
U.S. dollar notes	**$750**	**2.500%**	November 2017	November 2022
U.S. dollar notes	**$600**	**2.625%**	March 2013	March 2023
U.S. dollar notes	**$500**	**2.125%**	May 2016	May 2023
U.S. dollar notes	**$500**	**3.600%**	November 2013	November 2023
U.S. dollar notes	**$750**	**3.250%**	November 2014	November 2024
U.S. dollar notes	**$750**	**3.375%**	August 2015	August 2025
U.S. dollar notes	**$750**	**2.750%**	February 2016	February 2026
U.S. dollar notes	**$500**	**3.125%**	August 2017	August 2027
U.S. dollar notes	**$500**	**3.125%**	November 2017	March 2028

(in millions)

Type	Face Value	Interest Rate	Issuance	Maturity
U.S. dollar notes	**$1,500**	**6.375%**	May 2008	May 2038
U.S. dollar notes	**$750**	**4.375%**	November 2011	November 2041
U.S. dollar notes	**$700**	**4.500%**	March 2012	March 2042
U.S. dollar notes	**$750**	**3.875%**	August 2012	August 2042
U.S. dollar notes	**$850**	**4.125%**	March 2013	March 2043
U.S. dollar notes	**$750**	**4.875%**	November 2013	November 2043
U.S. dollar notes	**$750**	**4.250%**	November 2014	November 2044
U.S. dollar notes [a]	**$500**	**4.250%**	May 2016	November 2044
EURO notes [b]	**€750 (approximately $951)**	**2.125%**	May 2012	May 2019
EURO notes [b]	**€1,250 (approximately $1,621)**	**1.750%**	March 2013	March 2020
EURO notes [b]	**€750 (approximately $1,029)**	**1.875%**	March 2014	March 2021
EURO notes [b]	**€600 (approximately $761)**	**2.875%**	May 2012	May 2024
EURO notes [b]	**€500 (approximately $582)**	**0.625%**	November 2017	November 2024
EURO notes [b]	**€750 (approximately $972)**	**2.750%**	March 2013	March 2025
EURO notes [b]	**€1,000 (approximately $1,372)**	**2.875%**	March 2014	March 2026
EURO notes [b]	**€500 (approximately $697)**	**2.875%**	May 2014	May 2029
EURO notes [b]	**€500 (approximately $648)**	**3.125%**	June 2013	June 2033
EURO notes [b]	**€500 (approximately $578)**	**2.000%**	May 2016	May 2036
EURO notes [b]	**€500 (approximately $582)**	**1.875%**	November 2017	November 2037
Swiss franc notes [b]	**CHF200 (approximately $217)**	**0.875%**	March 2013	March 2019
Swiss franc notes [b]	**CHF275 (approximately $311)**	**0.750%**	May 2014	December 2019
Swiss franc notes [b]	**CHF325 (approximately $334)**	**1.000%**	September 2012	September 2020
Swiss franc notes [b]	**CHF300 (approximately $335)**	**2.000%**	December 2011	December 2021
Swiss franc notes [b]	**CHF250 (approximately $283)**	**1.625%**	May 2014	May 2024

[a] These notes are a further issuance of the 4.250% notes issued by PMI in November 2014.
[b] USD equivalents for foreign currency notes were calculated based on exchange rates on the date of issuance.

The net proceeds from the sale of the securities listed in the table above were used for general corporate purposes, including working capital requirements and repurchase of PMI's common stock until 2015.

Aggregate maturities:

Aggregate maturities of long-term debt are as follows:

(in millions)	
2019	$ 4,054
2020	4,074
2021	3,024
2022	2,756
2023	1,602
2024-2028	6,913
2029-2033	1,147
Thereafter	7,698
	31,268
Debt discounts	(239)
Total long-term debt	$ 31,029

See Note 16. *Fair Value Measurements* for additional disclosures related to the fair value of PMI's debt.

Credit Facilities

On January 29, 2018, PMI entered into an agreement to extend the term of its $2.0 billion 364-day revolving credit facility from February 6, 2018 to February 5, 2019.

At December 31, 2018, PMI's total committed credit facilities and commercial paper outstanding were as follows:

Type (in billions of dollars)	Committed Credit Facilities	Commercial Paper
364-day revolving credit, expiring February 5, 2019	**$ 2.0**	
Multi-year revolving credit, expiring February 28, 2021	**2.5**	
Multi-year revolving credit, expiring October 1, 2022	**3.5**	
Total facilities	**$ 8.0**	
Commercial paper outstanding		**$ —**

At December 31, 2018, there were no borrowings under these committed credit facilities, and the entire committed amounts were available for borrowing.

On January 28, 2019, PMI entered into an agreement to extend the term of its $2.0 billion 364-day revolving credit facility from February 5, 2019, to February 4, 2020.

Each of these facilities requires PMI to maintain a ratio of consolidated earnings before interest, taxes, depreciation and amortization ("consolidated EBITDA") to consolidated interest expense of not less than 3.5 to 1.0 on a rolling four-quarter basis. At December 31, 2018, PMI's ratio calculated in accordance with the agreements was 10.5 to 1.0.

These facilities do not include any credit rating triggers, material adverse change clauses or any provisions that could require PMI to post collateral. The terms “consolidated EBITDA” and “consolidated interest expense,” both of which include certain adjustments, are defined in the facility agreements previously filed with the Securities and Exchange Commission.

In addition to the committed credit facilities discussed above, certain subsidiaries maintain short-term credit arrangements to meet their respective working capital needs. These credit arrangements, which amounted to approximately $3.3 billion at December 31, 2018, and

$2.8 billion at December 31, 2017, are for the sole use of the subsidiaries. Borrowings under these arrangements amounted to $730 million at December 31, 2018, and $499 million at December 31, 2017.

Note 8.

Capital Stock:

Shares of authorized common stock are 6.0 billion; issued, repurchased and outstanding shares were as follows:

	Shares Issued	Shares Repurchased	Shares Outstanding
Balances, January 1, 2016	2,109,316,331	(559,972,262)	1,549,344,069
Issuance of stock awards		2,041,478	2,041,478
Balances, December 31, 2016	2,109,316,331	(557,930,784)	1,551,385,547
Issuance of stock awards		1,832,215	1,832,215
Balances, December 31, 2017	2,109,316,331	(556,098,569)	1,553,217,762
Issuance of stock awards		**1,361,959**	**1,361,959**
Balances, December 31, 2018	**2,109,316,331**	**(554,736,610)**	**1,554,579,721**

At December 31, 2018, 29,594,929 shares of common stock were reserved for stock awards under PMI's stock plans, and 250 million shares of preferred stock, without par value, were authorized but unissued. PMI currently has no plans to issue any shares of preferred stock.

Note 9.

Stock Plans:

In May 2017, PMI's shareholders approved the Philip Morris International Inc. 2017 Performance Incentive Plan (the "2017 Plan"). The 2017 Plan replaced the 2012 Performance Incentive Plan, and there will be no additional grants under the replaced plan. Under the 2017 Plan, PMI may grant to eligible employees restricted shares and restricted share units, performance-based cash incentive awards and performance-based equity awards. Up to 25 million shares of PMI's common stock may be issued under the 2017 Plan. At December 31, 2018, shares available for grant under the 2017 Plan were 22,911,850.

In May 2017, PMI's shareholders also approved the Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors (the "2017 Non-Employee Directors Plan"). The 2017 Non-Employee Directors Plan replaced the 2008 Stock Compensation Plan for Non-Employee Directors, and there will be no additional grants under the replaced plan. A non-employee director is defined as a member of the PMI Board of Directors who is not a full-time employee of PMI or of any corporation in which PMI owns, directly or indirectly, stock possessing at least 50% of the total combined voting power of all classes of stock entitled to vote in the election of directors in such corporation. Up to 1 million shares of PMI common stock may be awarded under the 2017 Non-Employee Directors Plan. At December 31, 2018, shares available for grant under the plan were 974,344.

Restricted share unit (RSU) awards

PMI may grant RSU awards to eligible employees; recipients may not sell, assign, pledge or otherwise encumber such awards. Such awards are subject to forfeiture if certain employment conditions are not met. RSU awards

generally vest on the third anniversary of the grant date. RSU awards do not carry voting rights, although they do earn dividend equivalents.

During 2018, the activity for RSU awards was as follows:

	Number of Shares	Weighted-Average Grant Date Fair Value Per Share
Balance at January 1, 2018	**3,612,400**	**$ 89.65**
Granted	**1,288,700**	**100.19**
Vested	**(1,451,876)**	**83.29**
Forfeited	**(130,429)**	**96.24**
Balance at December 31, 2018	**3,318,795**	**$ 96.26**

During the years ended December 31, 2018, 2017 and 2016, the weighted-average grant date fair value of the RSU awards granted to PMI employees and the recorded compensation expense related to RSU awards were as follows:

(in millions, except per RSU award granted)	Total Weighted-Average Grant Date Fair Value of RSU Awards Granted	Weighted-Average Grant Date Fair Value Per RSU Award Granted	Compensation Expense related to RSU Awards
2018	**$ 129**	**$ 100.19**	**$ 114**
2017	$ 119	$ 98.59	$ 111
2016	$ 108	$ 89.03	$ 126

The fair value of the RSU awards at the date of grant is amortized to expense over the restriction period, typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2018, PMI had $118 million of total unrecognized compensation costs related to non-vested RSU awards. These costs are expected to be recognized over a weighted-average period of two years, or upon death, disability or reaching the age of 58.

During the years ended December 31, 2018, 2017 and 2016, share and fair value information for PMI RSU awards that vested were as follows:

(dollars in millions)	Shares of RSU Awards that Vested	Grant Date Fair Value of Vested Shares of RSU Awards	Total Fair Value of RSU Awards that Vested
2018	**1,451,876**	**$ 121**	**$ 149**
2017	2,022,856	$ 158	$ 208
2016	2,302,525	$ 202	$ 210

Performance share unit (PSU) awards

PMI may grant PSU awards to certain executives; recipients may not sell, assign, pledge or otherwise encumber such awards. The PSU awards require the achievement of certain performance factors, which are predetermined at the time of grant, over a three-year performance cycle. PMI's performance metrics consist of PMI's Total Shareholder Return (TSR) relative to a predetermined peer group and on an absolute basis (50% weight), PMI's currency-neutral compound annual adjusted operating income growth rate, excluding acquisitions (30% weight), and PMI's performance against specific measures of PMI's transformation (20% weight). The aggregate of the weighted

performance factors for the three metrics determines the percentage of PSUs that will vest at the end of the three-year performance cycle. The minimum percentage of PSUs that can vest is zero, with a target percentage of 100 and a maximum percentage of 200. Each vested PSU entitles the participant to one share of common stock. An aggregate weighted PSU performance factor of 100 will result in the targeted number of PSUs being vested. At the end of the performance cycle, participants are entitled to an amount equivalent to the accumulated dividends paid on common stock during the performance cycle for the number of shares earned. PSU awards do not carry voting rights.

During 2018, the activity for PSU awards was as follows:

	Number of Shares	Grant Date Fair Value Subject to Other Performance Factors Per Share	Grant Date Fair Value Subject to TSR Performance Factor Per Share
Balance at January 1, 2018	**821,030**	**$ 93.46**	**$ 116.16**
Granted	**401,500**	**100.69**	**118.98**
Vested	**—**	**—**	**—**
Forfeited	**(27,560)**	**94.98**	**116.71**
Balance at December 31, 2018	**1,194,970**	**$ 95.85**	**$ 117.09**

During the years ended December 31, 2018, 2017 and 2016, the grant date fair value of the PSU awards granted to PMI employees and the recorded compensation expense related to PSU awards were as follows:

(in millions, except per PSU award granted)	PSU Grant Date Fair Value Subject to Other Performance Factors		PSU Grant Date Fair Value Subject to TSR Performance Factor		Compensation Expense related to PSU Awards
	Total	Per PSU Award	Total	Per PSU Award	Total
2018	**$ 20**	**$ 100.69**	**$ 24**	**$ 118.98**	**$ 24**
2017	$ 19	$ 98.29	$ 25	$ 128.72	$ 37
2016	$ 19	$ 89.02	$ 22	$ 104.60	$ 27

The grant date fair value of the PSU awards subject to the other performance factors was determined by using the average of the high and low market price of PMI's stock at the date of the grant. The grant date fair value of the PSU market based awards subject to the TSR performance factor was determined by using the Monte Carlo simulation model. The following assumptions were used to determine the grant date fair value of the PSU awards subject to the TSR performance factor for the years ended December 31, 2018, 2017 and 2016:

	For the Years Ended December 31,		
	2018	2017	2016
Risk-free interest rate [(a)]	**2.3 %**	1.5 %	1.0 %
Expected volatility [(b)]	**19.6 %**	15.8 %	17.5 %

[(a)] Based on the U.S. Treasury yield curve.
[(b)] Determined using a weighted-average of historical and implied volatility.

The fair value of the PSU award at the date of grant is amortized to expense over the performance period, which is typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2018, PMI had $25 million of total unrecognized compensation cost related to non-vested PSU awards. This cost is recognized over a weighted-average performance cycle period of two years, or upon death, disability or reaching the age of 58.

During the years ended December 31, 2018, 2017 and 2016, there were no PSU awards that vested.

Note 10.

Earnings per Share:

Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are participating securities and therefore are included in PMI's earnings per share calculation pursuant to the two-class method.

Basic and diluted earnings per share ("EPS") were calculated using the following:

(in millions)	For the Years Ended December 31, 2018	2017	2016
Net earnings attributable to PMI	**$ 7,911**	$ 6,035	$ 6,967
Less distributed and undistributed earnings attributable to share-based payment awards	**16**	14	19
Net earnings for basic and diluted EPS	**$ 7,895**	$ 6,021	$ 6,948
Weighted-average shares for basic EPS	**1,555**	1,552	1,551
Plus contingently issuable performance stock units (PSUs)	**—**	1	—
Weighted-average shares for diluted EPS	**1,555**	1,553	1,551

For the 2018, 2017 and 2016 computations, there were no antidilutive stock options.

Note 11.

Income Taxes:

Earnings before income taxes and provision for income taxes consisted of the following for the years ended December 31, 2018, 2017 and 2016:

(in millions)	2018	2017	2016
Earnings before income taxes	**$ 10,671**	$ 10,589	$ 9,924
Provision for income taxes:			
United States federal and state:			
Current	**$ 120**	$ 1,662	$ (39)
Deferred	**(113)**	(384)	293
Total United States	**7**	1,278	254
Outside United States:			
Current	**2,425**	3,146	2,625
Deferred	**13**	(117)	(111)
Total outside United States	**2,438**	3,029	2,514
Total provision for income taxes	**$ 2,445**	$ 4,307	$ 2,768

In December 2017, the Tax Cuts and Jobs Act was signed into law. Accordingly, PMI recorded a provisional charge of $1.6 billion in its 2017 income tax provision, including a charge for the transition tax on accumulated foreign earnings of $1.4 billion (which represented the transition tax of $2.2 billion, net of a reversal of $0.7 billion of previously recorded deferred tax liabilities on part of its accumulated foreign earnings and other items of $0.1 billion) and $0.2 billion due to the re-measurement of U.S. deferred tax assets and liabilities applying the U.S. federal corporate tax rate of 21%.

PMI completed its analysis of the Tax Cuts and Jobs Act during 2018 and adjusted the 2017 provisional estimates to the final amounts based on its 2017 U.S. federal income tax return as filed. Accordingly, PMI recorded in its income tax provision a charge of $31 million representing a current income tax charge of $185 million, primarily due to an increase in its aggregate foreign cash position used to determine PMI's final 2017 transition tax liability, mostly offset by a deferred income tax benefit of $154 million primarily due to the recognition of deferred tax assets for net operating losses in the state of New York. Updates to the provisional estimates have been recorded in accordance with Staff Accounting Bulletin No. 118 ("SAB 118").

At December 31, 2017, PMI recorded an income tax payable of $1.7 billion attributable to the Tax Cuts and Jobs Act, of which $1.6 billion was recorded in "income taxes and other liabilities" on PMI's consolidated balance sheet. The income tax payable of $1.7 billion

represented the transition tax of $2.2 billion, partially offset by foreign tax credits related to foreign withholding taxes previously paid of $0.5 billion. The income tax payable is due over an 8-year period beginning in 2018. In December 2018, PMI recorded an increase to income tax payable of $0.1 billion related to PMI's transition tax liability, in accordance with SAB 118. At December 31, 2018, $1.5 billion of PMI's remaining transition tax liability was recorded in "income taxes and other liabilities" on PMI's consolidated balance sheet.

At December 31, 2018, U.S. federal and foreign deferred income taxes have been provided on all accumulated earnings of PMI's foreign subsidiaries.

In accordance with the alternatives provided by ASU 2018-02 "Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income," PMI has elected not to reclassify the income tax effects of the Tax Cuts and Jobs Act from accumulated other comprehensive losses to retained earnings.

PMI has made an accounting policy election to treat Global Intangible Low-Taxed Income ("GILTI") taxes as a current period expense rather than including these amounts in the measurement of deferred taxes.

PMI is regularly examined by tax authorities around the world and is currently under examination in a number of jurisdictions. The U.S. federal statute of limitations remains open for the years 2015 and onward. Foreign and U.S. state jurisdictions have statutes of limitations generally ranging from three to five years. Years still open to examination by foreign tax authorities in major jurisdictions include Germany (2015 onward), Indonesia (2014 onward), Russia (2015 onward) and Switzerland (2017 onward).

It is reasonably possible that within the next 12 months certain tax examinations will close, which could result in a change in unrecognized tax benefits, along with related interest and penalties. An estimate of any possible change cannot be made at this time.

A reconciliation of the beginning and ending amount of unrecognized tax benefits was as follows:

(in millions)	**2018**	**2017**	**2016**
Balance at January 1,	**$ 145**	$ 79	$ 88
Additions based on tax positions related to the current year	**10**	71	13
Additions for tax positions of previous years	**15**	5	1
Reductions for tax positions of prior years	**(94)**	—	(7)
Reductions due to lapse of statute of limitations	**(3)**	(7)	(14)
Settlements	**(19)**	(4)	(2)
Other	**2**	1	—
Balance at December 31,	**$ 56**	$ 145	$ 79

Unrecognized tax benefits and PMI's liability for contingent income taxes, interest and penalties were as follows:

(in millions)	**December 31, 2018**	**December 31, 2017**	**December 31, 2016**
Unrecognized tax benefits	**$ 56**	$ 145	$ 79
Accrued interest and penalties	**12**	23	15
Tax credits and other indirect benefits	**(14)**	(35)	(31)
Liability for tax contingencies	**$ 54**	$ 133	$ 63

The amount of unrecognized tax benefits that, if recognized, would impact the effective tax rate was $41 million at December 31, 2018. The remainder, if recognized, would principally affect deferred taxes.

For the years ended December 31, 2018, 2017 and 2016, PMI recognized income (expense) in its consolidated statements of earnings of $4 million, $(11) million and $13 million, respectively, related to interest and penalties.

The effective income tax rate on pre-tax earnings differed from the U.S. federal statutory rate for the following reasons for the years ended December 31, 2018, 2017 and 2016:

	2018	2017	2016
U.S. federal statutory rate	**21.0 %**	35.0 %	35.0 %
Increase (decrease) resulting from:			
Foreign rate differences	**1.3**	(12.2)	(12.6)
Dividend repatriation cost	**2.5**	16.4	5.8
Global intangible low-taxed income	**1.2**		
Net operating losses	**(1.1)**		
Foreign derived intangible income	**(1.1)**		
Other	**(0.9)**	1.5	(0.3)
Effective tax rate	**22.9 %**	40.7 %	27.9 %

The 2018 effective tax rate decreased 17.8 percentage points to 22.9%. The change in the effective tax rate for 2018, as compared to 2017, was primarily due to the Tax Cuts and Jobs Act, which reduced the U.S. federal income tax rate from 35% to 21%, in addition to repatriation cost differences and earnings mix by taxing jurisdiction.

The 2017 effective tax rate increased 12.8 percentage points to 40.7%. The change in the effective tax rate for 2017, as compared to 2016, was primarily due to the Tax Cuts and Jobs Act. In addition to the transition tax, which resulted in a net tax charge of $1.4 billion, the Tax Cuts and Jobs Act also included a reduction in the U.S. income tax rate from 35% to 21%, as of January 1, 2018. This change in income tax rate required a re-measurement of PMI's U.S. deferred tax assets and liabilities at December 31, 2017, resulting in a tax charge of $0.2 billion.

The 2016 effective tax rate decreased 0.1 percentage point to 27.9%. The change in the effective tax rate for 2016, as compared to 2015, was primarily due to earnings mix by taxing jurisdiction and repatriation cost differences.

The tax effects of temporary differences that gave rise to deferred income tax assets and liabilities consisted of the following:

(in millions)	**At December 31,**	
	2018	**2017**
Deferred income tax assets:		
Accrued postretirement and postemployment benefits	**$ 193**	$ 239
Accrued pension costs	**390**	334
Inventory	**136**	131
Accrued liabilities	**138**	117
Net operating losses	**452**	213
Foreign exchange	**—**	91
Other	**37**	57

Total deferred income tax assets	**1,346**	1,182
Less: valuation allowance	**(257)**	(156)
Deferred income tax assets, net of valuation allowance	**1,089**	1,026
Deferred income tax liabilities:		
Trade names	**(508)**	(546)
Property, plant and equipment	**(222)**	(223)
Unremitted earnings	**(123)**	(49)
Foreign exchange	**(157)**	—
Total deferred income tax liabilities	**(1,010)**	(818)
Net deferred income tax assets	**$ 79**	$ 208

At December 31, 2018, PMI has recorded deferred tax assets for net operating loss carryforwards of $452 million, with varying dates of expiration, primarily after 2023, including $87 million with an unlimited carryforward period. At December 31, 2018, PMI has recorded a valuation allowance of $257 million against deferred tax assets that do not meet the more-likely-than-not recognition threshold. The increases in deferred tax assets for net operating loss carryforwards and the valuation allowance during 2018 are primarily due to law changes associated with the Tax Cuts and Jobs Act, as discussed above.

Note 12.

Segment Reporting:

PMI's subsidiaries and affiliates are engaged in the manufacture and sale of cigarettes and other nicotine-containing products, including RRPs, in markets outside of the United States of America. Reportable segments for PMI are organized by geographic region and managed by segment managers who are responsible for the operating and financial results of the regions inclusive of all product categories sold in the region. Effective January 1, 2018, PMI began managing its business in six reportable segments. PMI's reportable segments are the European Union; Eastern Europe; Middle East & Africa; South & Southeast Asia; East Asia & Australia; and Latin America & Canada. PMI records net revenues and operating income to its segments based upon the geographic area in which the customer resides.

PMI's chief operating decision maker evaluates segment performance and allocates resources based on regional operating income, which includes results from all product categories sold in each region. Effective January 1, 2018, PMI began using operating income to evaluate business segment performance and allocate resources, replacing operating companies income used previously. Interest expense, net, and provision for income taxes are centrally managed and, accordingly, such items are not presented by segment since they are excluded from the measure of segment profitability reviewed by management. Information about total assets by segment is not disclosed because such information is not reported to or used by PMI's chief operating decision maker. Segment goodwill and other intangible assets, net, are disclosed in Note 3. *Goodwill and Other Intangible Assets, net.* The accounting policies of the segments are the same as those described in Note 2. *Summary of Significant Accounting Policies.*

On January 1, 2018, PMI adopted Financial Accounting Standards Update ASU 2014-09, "Revenue from Contracts with Customers." PMI adopted this standard retrospectively to each prior period presented. For further details on this standard and its impact on PMI, see Note 21. *New Accounting Standards.* The amounts presented for the reportable segments reflect this adoption.

PMI disaggregates its net revenue from contracts with customers by both geographic location and product category for each of PMI's six reportable segments, as PMI believes this best depicts how the nature, amount, timing and uncertainty of its revenue and cash flows are affected by economic factors.

Net revenues by segment were as follows:

	For the Years Ended December 31,		
(in millions)	**2018**	**2017**	**2016**
Net revenues:			
European Union	**$ 9,298**	$ 8,318	$ 8,162
Eastern Europe	**2,921**	2,711	2,484
Middle East & Africa	**4,114**	3,988	4,516
South & Southeast Asia	**4,656**	4,417	4,396
East Asia & Australia	**5,580**	6,373	4,285
Latin America & Canada	**3,056**	2,941	2,842
Net revenues	**$ 29,625**	$ 28,748	$ 26,685

Total net revenues attributable to customers located in Japan, PMI's largest market in terms of net revenues, were $3.8 billion, $4.7 billion and $2.8 billion in 2018, 2017 and 2016, respectively. Total net revenues attributable to customers located in Indonesia were $3.1 billion, $3.2 billion and $3.2 billion in 2018, 2017 and 2016, respectively.

PMI had one customer in the East Asia & Australia segment that accounted for 13%, 16% and 11% of PMI's consolidated net revenues, and one customer in the European Union segment that accounted for 10%, 10% and 11% of PMI's consolidated net revenues in 2018, 2017 and 2016, respectively.

PMI's net revenues by product category were as follows:

(in millions)	For the Years Ended December 31, 2018	2017	2016
Combustible products:			
European Union	**$ 8,433**	$ 8,048	$ 8,105
Eastern Europe	**2,597**	2,657	2,478
Middle East & Africa	**3,732**	3,893	4,513
South & Southeast Asia	**4,656**	4,417	4,396
East Asia & Australia	**3,074**	3,156	3,619
Latin America & Canada	**3,037**	2,937	2,841
Total combustible products	**$ 25,529**	$ 25,107	$ 25,952
Reduced-risk products:			
European Union	**$ 865**	$ 269	57
Eastern Europe	**324**	55	6
Middle East & Africa	**382**	94	4
South & Southeast Asia	**—**	—	—
East Asia & Australia	**2,506**	3,218	666
Latin America & Canada	**19**	4	1
Total reduced-risk products	**$ 4,096**	$ 3,640	$ 733
Total PMI net revenues	**$ 29,625**	$ 28,748	$ 26,685

Note: Sum of product categories or Regions might not foot to total PMI due to roundings.

Net revenues related to combustible products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of PMI's cigarettes and other tobacco products combined. Other tobacco products primarily include roll-your-own and make-your-own cigarettes, pipe tobacco, cigars and cigarillos and do not include reduced-risk products.

Net revenues related to reduced-risk products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of PMI's heated tobacco units, *IQOS* devices and related accessories, and other nicotine-containing products, which primarily include our e-vapor products.

PMI recognizes revenue, when control is transferred to the customer, typically either upon shipment or delivery of goods.

Other segment data were as follows:

(in millions)	For the Years Ended December 31, 2018	2017	2016
Operating income:			
European Union	**$ 4,105**	$ 3,691	$ 3,920
Eastern Europe	**902**	887	890
Middle East & Africa	**1,627**	1,884	1,990
South & Southeast Asia	**1,747**	1,514	1,474
East Asia & Australia	**1,851**	2,608	1,691
Latin America & Canada	**1,145**	997	938
Operating income	**$ 11,377**	$ 11,581	$ 10,903

(in millions)	For the Years Ended December 31,		
	2018	2017	2016
Depreciation expense:			
European Union	**$ 269**	$ 213	$ 184
Eastern Europe	**101**	76	62
Middle East & Africa	**105**	88	88
South & Southeast Asia	**154**	153	147
East Asia & Australia	**173**	160	100
Latin America & Canada	**94**	85	79
	896	775	660
Other	**11**	12	9
Total depreciation expense	**$ 907**	$ 787	$ 669

(in millions)	For the Years Ended December 31,		
	2018	2017	2016
Capital expenditures:			
European Union	**$ 813**	$ 956	$ 665
Eastern Europe	**136**	97	69
Middle East & Africa	**65**	85	154
South & Southeast Asia	**129**	140	156
East Asia & Australia	**215**	87	24
Latin America & Canada	**74**	175	103
	1,432	1,540	1,171
Other	**4**	8	1
Total capital expenditures	**$ 1,436**	$ 1,548	$ 1,172

(in millions)	At December 31,		
	2018	2017	2016
Long-lived assets:			
European Union	**$ 4,216**	$ 4,130	$ 3,282
Eastern Europe	**547**	546	466
Middle East & Africa	**362**	430	400
South & Southeast Asia	**1,297**	1,419	1,413
East Asia & Australia	**781**	659	503
Latin America & Canada	**779**	885	765
Total long-lived assets	**7,982**	8,069	6,829
Other	**664**	1,126	750
Total property, plant and equipment, net and Other assets	**$ 8,646**	$ 9,195	$ 7,579

Long-lived assets consist of non-current assets other than goodwill; other intangible assets, net; deferred tax assets, investments in unconsolidated subsidiaries and equity securities, and financial instruments. PMI's largest markets in terms of long-lived assets are Italy, Switzerland and Indonesia. Total long-lived assets located in Italy, which is reflected in the European Union segment above, were $1.1 billion, $1.2 billion and $0.7 billion at December 31,

2018, 2017 and 2016, respectively. Total long-lived assets located in Switzerland, which is reflected in the European Union segment above, were $1.0 billion, $0.9 billion and $0.9 billion at December 31, 2018, 2017 and 2016, respectively. Total long-lived assets located in Indonesia, which is reflected in the South & Southeast Asia segment above, were $0.7 billion, $0.8 billion and $0.8 billion at December 31, 2018, 2017 and 2016, respectively.

Note 13.

Benefit Plans:

Pension coverage for employees of PMI's subsidiaries is provided, to the extent deemed appropriate, through separate plans, many of which are governed by local statutory requirements. In addition, PMI provides health care and other benefits to substantially all U.S. retired employees and certain non-U.S. retired employees. In general, health care benefits for non-U.S. retired employees are covered through local government plans.

In the fourth quarter of 2018, PMI elected to early adopt ASU 2018-14 "Compensation-Retirement Benefits-Defined Benefit Plans-General (Subtopic 715-20): Disclosure Framework-Changes to the Disclosure Requirements for Defined Benefit Plans." The adoption of ASU 2018-14 did not have a material impact on PMI's consolidated financial position or results of operations.

PMI adopted ASU 2017-07 "Compensation - Retirement Benefits" on January 1, 2018, retrospectively for all periods. Following adoption, the service cost component of net periodic benefit cost continues to be included within operating income, while all other cost components are included below operating income, within pension and other employee benefit costs. Pension and other employee benefit costs per the consolidated statements of earnings consisted of the following for December 31, 2018, 2017 and 2016:

(in millions)	**2018**	**2017**	**2016**
Net pension costs (income)	**$ (51)**	$ (20)	$ (6)
Net postemployment costs	**80**	85	83
Net postretirement costs	**12**	13	11
Total pension and other employee benefit costs	**$ 41**	$ 78	$ 88

Pension and Postretirement Benefit Plans

Obligations and Funded Status

The postretirement health care plans are not funded. The projected benefit obligations, plan assets and funded status of PMI's pension plans, and the accumulated benefit obligation and net amount accrued for PMI's postretirement health care plans, at December 31, 2018 and 2017, were as follows:

(in millions)	Pension[1]		Postretirement	
	2018	**2017**	**2018**	**2017**
Benefit obligation at January 1,	**$ 9,028**	$ 8,387	**$ 248**	$ 227
Service cost	**210**	208	**4**	4
Interest cost	**109**	108	**9**	8
Benefits paid	**(218)**	(226)	**(8)**	(10)
Settlement and curtailment	**1**	—	**—**	—
Actuarial losses (gains)	**210**	(93)	**(34)**	12
Currency	**(196)**	621	**(9)**	7
Other	**8**	23	**(1)**	—
Benefit obligation at December 31,	**9,152**	9,028	**209**	248
Fair value of plan assets at January 1,	**7,598**	6,457		
Actual return on plan assets	**(447)**	742		
Employer contributions	**110**	66		
Employee contributions	**24**	40		
Benefits paid	**(218)**	(226)		
Settlement and curtailment	**—**	—		
Currency	**(179)**	519		
Fair value of plan assets at December 31,	**6,888**	7,598		
Net pension and postretirement liability recognized at December 31,	**$ (2,264)**	$ (1,430)	**$ (209)**	$ (248)

(1) Primarily non-U.S. based defined benefit retirement plans.

At December 31, 2018, actuarial losses (gains) consisted of losses for experience differences related to the change in population profile, coupled with updated mortality table assumptions for the Swiss plan. At December 31, 2017, actuarial losses (gains) consisted of gains due to changes in the pension indexation rate assumption for the Holland plan, which was partially offset by losses for experience differences related to the change in population profile, primarily for the Swiss plan.

At December 31, 2018 and 2017, the Swiss pension plan represented 60% and 57% of the benefit obligation, respectively, and approximately 57% of the fair value of plan assets for each of the years. At December 31, 2018 and 2017, the U.S. pension plan represented 4% and 5% of the benefit obligation, respectively, and approximately 4% and 4% of the fair value of plan assets at December 31, 2018 and 2017, respectively.

At December 31, 2018 and 2017, the amounts recognized on PMI's consolidated balance sheets for the pension and postretirement plans were as follows:

	Pension		Postretirement	
(in millions)	**2018**	**2017**	**2018**	**2017**
Other assets	**$ 37**	$ 47		
Accrued liabilities — employment costs	**(20)**	(26)	**$ (10)**	$ (10)
Long-term employment costs	**(2,281)**	(1,451)	**(199)**	(238)
	$ (2,264)	$ (1,430)	**$ (209)**	$ (248)

The accumulated benefit obligation, which represents benefits earned to date, for the pension plans was $8,557 million and $8,496 million at December 31, 2018 and 2017, respectively.

For pension plans with accumulated benefit obligations in excess of plan assets, the accumulated benefit obligation and fair value of plan assets were $7,641 million and $5,866 million, respectively, as of December 31, 2018. The accumulated benefit obligation and fair value of plan assets were $6,953 million and $5,835 million, respectively, as of December 31, 2017.

For pension plans with projected benefit obligations in excess of plan assets, the projected benefit obligation and fair value of plan assets were $8,807 million and $6,504 million, respectively, as of December 31, 2018. The projected benefit obligation and fair value of plan assets were $8,609 million and $7,135 million, respectively, as of December 31, 2017.

The following weighted-average assumptions were used to determine PMI's pension and postretirement benefit obligations at December 31:

	Pension		**Postretirement**	
	2018	**2017**	**2018**	**2017**
Discount rate	**1.61 %**	1.51 %	**3.97 %**	3.79 %
Rate of compensation increase	**1.86**	1.65		
Interest crediting rate	**3.40**	3.40		
Health care cost trend rate assumed for next year			**6.17**	6.17
Ultimate trend rate			**4.59**	4.62
Year that rate reaches the ultimate trend rate			**2040**	2029

The discount rate for the largest pension plans is based on a yield curve constructed from a portfolio of high quality corporate bonds that produces a cash flow pattern equivalent to each plan's expected benefit payments. The discount rate for the remaining plans is developed from local bond indices that match local benefit obligations as closely as possible.

Components of Net Periodic Benefit Cost

Net periodic pension and postretirement health care costs consisted of the following for the years ended December 31, 2018, 2017 and 2016:

	Pension			**Postretirement**		
(in millions)	**2018**	**2017**	**2016**	**2018**	**2017**	**2016**
Service cost	**$ 210**	$ 208	$ 207	**$ 4**	$ 4	$ 3
Interest cost	**109**	108	146	**9**	8	9
Expected return on plan assets	**(349)**	(326)	(346)	**—**	—	—
Amortization:						
Net losses	**172**	186	186	**4**	5	2
Prior service cost	**2**	6	4	**(1)**	—	—
Settlement and curtailment	**15**	6	4	**—**	—	—
	$ 159	$ 188	$ 201	**$ 16**	$ 17	$ 14

Net periodic pension and postretirement costs

As of December 31, 2016, PMI elected to change the method used to calculate the service and interest cost components of the net periodic pension benefit costs. Historically, these costs were determined utilizing a single weighted-average discount rate based on a yield curve used to measure the benefit obligation at the beginning of the period. As of January 1, 2017, PMI utilized a full yield curve approach in the estimation of the service and interest costs by applying the specific spot rates along the yield curve to the relevant projected cash flows. Specifically, service costs were determined based on duration-specific spot rates applied to service cost cash flows, and interest costs were determined by applying duration-specific spot rates to the year-by-year projected benefit payments. PMI changed to the new

method to provide a more precise measurement of service and interest costs by improving the correlation between the projected benefit cash flows to the corresponding spot rates along the yield curve. PMI accounted for this change as a change in accounting estimate on a prospective basis. This change did not affect the measurement of PMI's pension plan obligations and did not have a material impact on PMI's consolidated results of operations, financial position or cash flows.

Settlement and curtailment charges were due primarily to employee severance and early retirement programs.

The following weighted-average assumptions were used to determine PMI's net pension and postretirement health care costs:

	Pension			Postretirement		
	2018	**2017**	**2016**	**2018**	**2017**	**2016**
Discount rate - service cost	**1.92 %**	1.68 %	1.81 %	**3.79 %**	3.68 %	4.45 %
Discount rate - interest cost	**1.25**	1.27	1.81	**3.79**	3.68	4.45
Expected rate of return on plan assets	**4.76**	4.80	5.36			
Rate of compensation increase	**1.65**	1.68	2.03			
Interest crediting rate	**3.40**	3.40	3.00			
Health care cost trend rate				**6.17**	7.15	6.23

PMI's expected rate of return on pension plan assets is determined by the plan assets' historical long-term investment performance, current asset allocation and estimates of future long-term returns by asset class.

PMI and certain of its subsidiaries sponsor defined contribution plans. Amounts charged to expense for defined contribution plans totaled $66 million, $58 million and $56 million for the years ended December 31, 2018, 2017 and 2016, respectively.

Plan Assets

PMI's investment strategy for pension plans is based on an expectation that equity securities will outperform debt securities over the long term. Accordingly, the target allocation of PMI's plan assets is broadly characterized as approximately a 60%/40% split between equity and debt securities. The strategy primarily utilizes indexed U.S. equity securities, international equity securities and investment-grade debt securities. PMI's plans have no investments in hedge funds, private equity or derivatives. PMI attempts to mitigate investment risk by rebalancing between equity and debt asset classes once a year or as PMI's contributions and benefit payments are made.

The fair value of PMI's pension plan assets at December 31, 2018 and 2017, by asset category was as follows:

Asset Category (in millions)	At December 31, 2018	Quoted Prices In Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	**$ 84**	**$ 84**		
Equity securities:				
U.S. securities	**139**	**139**		
International securities	**442**	**442**		
Investment funds[a]	**5,508**	**3,595**	**$ 1,913**	
International government bonds	**176**	**120**	**56**	
Corporate bonds	**232**	**232**		
Other	**19**	**19**		
Total assets in the fair value hierarchy	**$ 6,600**	**$ 4,631**	**$ 1,969**	**$ —**
Investment funds measured at net asset value[b]	**288**			
Total assets	**$ 6,888**			

[a] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and Barclays Capital U.S. for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 57% are invested in U.S. and international equities; 20% are invested in U.S. and international government bonds; 12% are invested in real estate and other money markets, and 11% are invested in corporate bonds.

[b] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Asset Category (in millions)	At December 31, 2017	Quoted Prices In Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$ 17	$ 17		
Equity securities:				
U.S. securities	146	146		
International securities	518	518		
Investment funds[a]	6,219	4,191	$ 2,028	

International government bonds	119	119		
Corporate bonds	247	247		
Other	22	22		
Total assets in the fair value hierarchy	$ 7,288	$ 5,260	$ 2,028	$ —
Investment funds measured at net asset value[b]	310			
Total assets	$ 7,598			

[a] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and Barclays Capital U.S. for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 60% were invested in U.S. and international equities; 20% were invested in U.S. and international government bonds; 10% were invested in real estate and other money markets, and 10% were invested in corporate bonds.

[b] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

See Note 16. *Fair Value Measurements* for a discussion of the fair value of pension plan assets.

PMI makes, and plans to make, contributions to the extent that they are tax deductible and to meet specific funding requirements of its funded pension plans. Currently, PMI anticipates making contributions of approximately $119 million in 2019 to its pension plans, based on current tax and benefit laws. However, this estimate is subject to change as a result of changes in tax and other benefit laws, as well as asset performance significantly above or below the assumed long-term rate of return on pension assets, or changes in interest and currency rates.

The estimated future benefit payments from PMI pension plans at December 31, 2018, are as follows:

(in millions)	
2019	$ 290
2020	315
2021	319
2022	329
2023	347
2024 - 2028	1,971

PMI's expected future annual benefit payments for its postretirement health care plans are estimated to be not material through 2028.

Postemployment Benefit Plans

PMI and certain of its subsidiaries sponsor postemployment benefit plans covering substantially all salaried and certain hourly employees. The cost of these plans is charged to expense over the working life of the covered employees. Net postemployment costs were $158 million, $144 million and $166 million for the years ended December 31, 2018, 2017 and 2016, respectively.

The amounts recognized in accrued postemployment costs on PMI's consolidated balance sheets at December 31, 2018 and 2017, were $708 million and $671 million, respectively. The change in the liability is primarily due to actuarial losses of $147 in 2018 resulting from increased employee severance cost in Switzerland and countries in the European Union segment, coupled with the periodic expense, partially offset by cash payments.

The accrued postemployment costs were determined using a weighted-average discount rate of 3.1% and 3.0% in 2018 and 2017, respectively; an assumed ultimate annual weighted-average turnover rate of 3.2% and 2.6% in 2018 and 2017, respectively; assumed compensation cost increases of 2.6% in 2018 and 2.3% in 2017, and assumed benefits as defined in the respective plans. In accordance with local regulations, certain postemployment plans are funded. As a result, the accrued postemployment costs disclosed above are presented net of the related assets of $38 million and $33 million at December 31, 2018 and 2017, respectively. Postemployment costs arising from actions that offer employees benefits in excess of those specified in the respective plans are charged to expense when incurred.

Comprehensive Earnings (Losses)

The amounts recorded in accumulated other comprehensive losses at December 31, 2018, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (3,438)	$ (41)	$ (702)	$ (4,181)
Prior service cost	(27)	3	—	(24)
Net transition obligation	(4)	—	—	(4)
Deferred income taxes	379	20	164	563
Losses to be amortized	$ (3,090)	$ (18)	$ (538)	$ (3,646)

The amounts recorded in accumulated other comprehensive losses at December 31, 2017, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (2,624)	$ (80)	$ (617)	$ (3,321)
Prior service cost	(35)	4	—	(31)
Net transition obligation	(5)	—	—	(5)
Deferred income taxes	327	28	186	541
Losses to be amortized	$ (2,337)	$ (48)	$ (431)	$ (2,816)

The amounts recorded in accumulated other comprehensive losses at December 31, 2016, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (3,314)	$ (73)	$ (713)	$ (4,100)
Prior service cost	(53)	4	—	(49)
Net transition obligation	(5)	—	—	(5)
Deferred income taxes	350	24	215	589
Losses to be amortized	$ (3,022)	$ (45)	$ (498)	$ (3,565)

The movements in other comprehensive earnings (losses) during the year ended December 31, 2018, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	**$ 180**	**$ 5**	**$ 62**	**$ 247**
Prior service cost	**—**	**(1)**	**—**	**(1)**
Net transition obligation	**1**	**—**	**—**	**1**
Other income/expense:				
Net losses	**14**	**—**	**—**	**14**
Prior service cost	**—**	**—**	**—**	**—**
Deferred income taxes	**(28)**	**(1)**	**(14)**	**(43)**
	167	**3**	**48**	**218**
Other movements during the year:				
Net losses	**(1,008)**	**34**	**(147)**	**(1,121)**
Prior service cost	**8**	**—**	**—**	**8**
Deferred income taxes	**80**	**(7)**	**(8)**	**65**

	(920)	**27**	**(155)**	**(1,048)**
Total movements in other comprehensive earnings (losses)	**$ (753)**	**$ 30**	**$ (107)**	**$ (830)**

The movements in other comprehensive earnings (losses) during the year ended December 31, 2017, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	$ 175	$ 5	$ 68	$ 248
Prior service cost	5	—	—	5
Other income/expense:				
Net losses	6	—	—	6
Prior service cost	—	—	—	—
Deferred income taxes	(10)	(1)	(20)	(31)
	176	4	48	228
Other movements during the year:				
Net losses	509	(12)	28	525
Prior service cost	13	—	—	13
Deferred income taxes	(13)	5	(9)	(17)
	509	(7)	19	521
Total movements in other comprehensive earnings (losses)	$ 685	$ (3)	$ 67	$ 749

The movements in other comprehensive earnings (losses) during the year ended December 31, 2016, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	$ 193	$ 2	$ 62	$ 257
Prior service cost	6	—	—	6
Other income/expense:				
Net losses	4	—	—	4
Prior service cost	—	—	—	—
Deferred income taxes	(26)	—	(17)	(43)
	177	2	45	224
Other movements during the year:				
Net losses	(437)	(15)	(65)	(517)
Prior service cost	(18)	—	—	(18)
Deferred income taxes	55	4	19	78
	(400)	(11)	(46)	(457)
	$ (223)	$ (9)	$ (1)	$ (233)

Total movements in other comprehensive earnings (losses)	

Note 14.

Additional Information:

(in millions)	For the Years Ended December 31, 2018	2017	2016
Research and development expense	**$ 383**	$ 453	$ 429
Advertising expense	**$ 896**	$ 830	$ 405
Foreign currency net transaction losses	**$ 21**	$ 49	$ 272
Interest expense	**$ 855**	$ 1,096	$ 1,069
Interest income	**(190)**	(182)	(178)
Interest expense, net	**$ 665**	$ 914	$ 891
Rent expense	**$ 312**	$ 313	$ 284

Minimum rental commitments under non-cancelable operating leases in effect at December 31, 2018, were as follows:

(in millions)	
2019	$ 147
2020	103
2021	73
2022	52
2023	43
Thereafter	354
	$ 772

Note 15.

Financial Instruments:

Overview

PMI operates in markets outside of the United States of America, with manufacturing and sales facilities in various locations around the world. PMI utilizes certain financial instruments to manage foreign currency and interest rate exposure. Derivative financial instruments are used by PMI principally to reduce exposures to market risks resulting from fluctuations in foreign currency exchange and interest rates by creating offsetting exposures. PMI is not a party to leveraged derivatives and, by policy, does not use derivative financial instruments for speculative purposes. Financial instruments qualifying for hedge accounting must maintain a specified level of effectiveness between the hedging instrument and the item being hedged, both at inception and throughout the hedged period. PMI formally

documents the nature and relationships between the hedging instruments and hedged items, as well as its risk-management objectives, strategies for undertaking the various hedge transactions and method of assessing hedge effectiveness. Additionally, for hedges of forecasted transactions, the significant characteristics and expected terms of the forecasted transaction must be specifically identified, and it must be probable that each forecasted transaction will occur. If it were deemed probable that the forecasted transaction would not occur, the gain or loss would be recognized in earnings.

PMI uses deliverable and non-deliverable forward foreign exchange contracts, foreign currency swaps and foreign currency options, collectively referred to as foreign exchange contracts ("foreign exchange contracts"), and interest rate contracts to mitigate its exposure to changes in exchange and interest rates from third-party and intercompany actual and forecasted transactions. The primary currencies to which PMI is exposed include the Australian dollar, Canadian dollar, Euro, Indonesian rupiah, Japanese yen, Mexican peso, Philippine

peso, Russian ruble, Swiss franc and Turkish lira. At December 31, 2018 and 2017, PMI had contracts with aggregate notional amounts of $27.4 billion and $26.1 billion, respectively. Of the $27.4 billion aggregate notional amount at December 31, 2018, $3.2 billion related to cash flow hedges, $10.1 billion related to hedges of net investments in foreign operations and $14.1 billion related to other derivatives that primarily offset currency exposures on intercompany financing. Of the $26.1 billion aggregate notional amount at December 31, 2017, $3.4 billion related to cash flow hedges, $11.3 billion related to hedges of net investments in foreign operations and $11.4 billion related to other derivatives that primarily offset currency exposures on intercompany financing.

Effective January 1, 2018, PMI elected to early adopt Accounting Standard Update 2017-12 "Derivatives and Hedging (Topic 815) Targeted Improvements to Accounting for Hedging Activities," which did not have a material impact on PMI's consolidated financial position or results of operations.

The fair value of PMI's foreign exchange contracts included in the consolidated balance sheet as of December 31, 2018 and 2017, were as follows:

	Derivative Assets			Derivative Liabilities		
		Fair Value			Fair Value	
(in millions)	**Balance Sheet Classification**	**2018**	**2017**	**Balance Sheet Classification**	**2018**	**2017**
Foreign exchange contracts designated as hedging instruments	Other current assets	**$ 54**	$ 84	Other accrued liabilities	**$ 47**	$ 197
	Other assets	**99**	34	Other liabilities	**525**	880
Foreign exchange contracts not designated as hedging instruments	Other current assets	**67**	22	Other accrued liabilities	**46**	37
	Other assets	**—**	—	Other liabilities	**13**	14
Total derivatives		**$ 220**	$ 140		**$ 631**	$ 1,128

For the years ended December 31, 2018, 2017 and 2016, PMI's cash flow and net investment hedging instruments impacted the consolidated statements of earnings and comprehensive earnings as follows:

(pre-tax, millions)	**For the Year Ended December 31,**						
	Amount of Gain/(Loss) Recognized in Other Comprehensive Earnings/ (Losses) on Derivatives			**Statement of Earnings Classification of Gain/ (Loss) Reclassified from Other Comprehensive Earnings/(Losses) into Earnings**	**Amount of Gain/(Loss) Reclassified from Other Comprehensive Earnings/ (Losses) into Earnings**		
	2018	**2017**	**2016**		**2018**	**2017**	**2016**
Derivatives in Cash Flow Hedging Relationship							
Foreign exchange contracts	**$ 28**	$ (52)	$ 12				
				Net revenues	**$ 18**	$ 60	$ (38)

					Cost of sales		—		1	46
					Marketing, administration and research costs		**6**		(7)	(11)
					Interest expense, net		**(1)**		(41)	(30)
Derivatives in Net Investment Hedging Relationship										
Foreign exchange contracts		**324**	(1,644)	296						
Total	**$**	**352**	$ (1,696)	$ 308		**$**	**23**	$ 13	$	(33)

Cash Flow Hedges

PMI has entered into foreign exchange contracts to hedge the foreign currency exchange and interest rate risks related to certain forecasted transactions. Gains and losses associated with qualifying cash flow hedge contracts is deferred as a component of accumulated other comprehensive losses until the underlying hedged transactions are reported in PMI's consolidated statements of earnings. Amounts reclassified from other comprehensive losses into earnings as a result of the discontinuance of cash flow hedges when the originally forecasted transaction is no longer probable of occurring were not material during the periods presented. As of December 31, 2018, PMI has hedged forecasted transactions for periods not exceeding the next eighteen months, with the exception of one foreign exchange contract that expires in May 2024. The impact of these hedges is primarily included in operating cash flows on PMI's consolidated statements of cash flows.

Hedges of Net Investments in Foreign Operations

PMI designates certain foreign currency denominated debt and foreign exchange contracts as net investment hedges, primarily of its Euro net assets. For the years ended December 31, 2018, 2017 and 2016, these hedges of net investments resulted in gains (losses), net of income taxes, of $521 million, $(1,725) million and $430 million, respectively, principally related to changes in the exchange rates between the Euro and U.S. dollar. These gains (losses) were reported as a component of accumulated other comprehensive losses within currency translation adjustments and were substantially offset by the losses and gains generated on the underlying assets. For the year ended December 31, 2018, the gains for amounts excluded from the effectiveness testing recognized in earnings were $260 million and were accounted for in interest expense, net, on the consolidated statement of earnings. The premiums paid for, and settlements of, net investment hedges are included in investing cash flows on PMI's consolidated statements of cash flows.

Other Derivatives

PMI has entered into foreign exchange contracts to hedge the foreign currency exchange and interest rate risks related to intercompany loans between certain subsidiaries, and third-party loans. While effective as economic hedges, no hedge accounting is applied for these contracts; therefore, the unrealized gains (losses) relating to these contracts are reported in marketing, administration and research costs in PMI's consolidated statements of earnings. For the years ended December 31, 2018, 2017 and 2016, the gains (losses) from contracts for which PMI did not apply hedge accounting were $405 million, $382 million and $(85) million, respectively. The gains (losses) from these contracts substantially offset the losses and gains generated by the underlying intercompany and third-party loans being hedged.

As a result, for the years ended December 31, 2018, 2017 and 2016, these items impacted the consolidated statement of earnings as follows:

(pre-tax, in millions)

Derivatives not Designated as Hedging Instruments	**Statement of Earnings Classification of Gain/(Loss)**	**Amount of Gain/(Loss) Recognized in Earnings**		
		2018	**2017**	**2016**
Foreign exchange contracts				
	Interest expense, net	**$ 62**	$ (60)	$ (24)
Total		**$ 62**	$ (60)	$ (24)

Qualifying Hedging Activities Reported in Accumulated Other Comprehensive Losses

Derivative gains or losses reported in accumulated other comprehensive losses are a result of qualifying hedging activity. Transfers of these gains or losses to earnings are offset by the corresponding gains or losses on the underlying hedged item. Hedging activity affected accumulated other comprehensive losses, net of income taxes, as follows:

(in millions)	For the Years Ended December 31,		
	2018	**2017**	**2016**
Gain as of January 1,	**$ 42**	$ 97	$ 59
Derivative (gains)/losses transferred to earnings	**(31)**	(11)	30
Change in fair value	**24**	(44)	8
Gain as of December 31,	**$ 35**	$ 42	$ 97

At December 31, 2018, PMI expects $21 million of derivative gains that are included in accumulated other comprehensive losses to be reclassified to the consolidated statement of earnings within the next 12 months. These gains are expected to be substantially offset by the statement of earnings impact of the respective hedged transactions.

Contingent Features

PMI's derivative instruments do not contain contingent features.

Credit Exposure and Credit Risk

PMI is exposed to credit loss in the event of non-performance by counterparties. While PMI does not anticipate non-performance, its risk is limited to the fair value of the financial instruments less any cash collateral received or pledged. PMI actively monitors its exposure to credit risk through the use of credit approvals and credit limits and by selecting and continuously monitoring a diverse group of major international banks and financial institutions as counterparties.

Fair Value

See Note 16. *Fair Value Measurements* and Note 19. *Balance Sheet Offsetting* for additional discussion of derivative financial instruments.

Note 16.

Fair Value Measurements:

The authoritative guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The guidance also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of input that may be used to measure fair value, which are as follows:

Level 1 — Quoted prices in active markets for identical assets or liabilities;

Level 2 — Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

In the fourth quarter of 2018, PMI elected to early adopt ASU 2018-13 "Fair Value Measurement (Topic 820): Disclosure Framework-Changes to the Disclosure Requirements for Fair Value Measurement." The adoption of ASU 2018-13 did not have a material impact on PMI's consolidated financial position or results of operations.

Equity Securities

The fair value of PMI's equity securities, which are determined by using quoted prices in active markets, have been classified within Level 1.

Derivative Financial Instruments

PMI assesses the fair value of its foreign exchange contracts and interest rate contracts using standard valuation models that use, as their basis, readily observable market inputs. The fair value of PMI's foreign exchange forward contracts is determined by using the prevailing foreign exchange spot rates and interest rate differentials, and the respective maturity dates of the instruments. The fair value of PMI's currency options is determined by using a

Black-Scholes methodology based on foreign exchange spot rates and interest rate differentials, currency volatilities and maturity dates. PMI's derivative financial instruments have been classified within Level 2 at December 31, 2018 and 2017. See Note 15. *Financial Instruments* for additional discussion of derivative financial instruments.

Pension Plan Assets

The fair value of pension plan assets determined by using readily available quoted market prices in active markets has been classified within Level 1 of the fair value hierarchy at December 31, 2018 and 2017. The fair value of pension plan assets determined by using quoted prices in markets that are not active has been classified within Level 2 at December 31, 2018 and 2017. See Note 13. *Benefit Plans* for additional discussion of pension plan assets.

Debt

The fair value of PMI's outstanding debt, which is utilized solely for disclosure purposes, is determined using quotes and market interest rates currently available to PMI for issuances of debt with similar terms and remaining maturities. The aggregate carrying value of PMI's debt, excluding short-term borrowings and $33 million of capital lease obligations, was $30,996 million at December 31, 2018. The aggregate carrying value of PMI's debt, excluding short-term borrowings and $28 million of capital lease obligations, was $33,812 million at December 31, 2017. The fair value of PMI's outstanding debt, excluding the aforementioned short-term borrowings and capital lease obligations, was classified within Level 1 and Level 2 at December 31, 2018 and 2017.

The aggregate fair values of PMI's equity securities, derivative financial instruments, pension plan assets and debt as of December 31, 2018, were as follows:

(in millions)	Fair Value At December 31, 2018	Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Equity securities	$ 288	$ 288	$ —	$ —
Foreign exchange contracts	220	$ —	220	—
Pension plan assets	6,600	4,631	1,969	—
Total assets in fair value hierarchy	$ 7,108	$ 4,919	$ 2,189	$ —
Pension plan assets measured at net asset value[(a)]	288			
Total assets	$ 7,396			
Liabilities:				
Debt	$ 31,162	$ 30,997	$ 165	$ —
Foreign exchange contracts	631	—	631	—
Total liabilities	$ 31,793	$ 30,997	$ 796	$ —

[(a)] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in these tables are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

The aggregate fair values of PMI's derivative financial instruments, pension plan assets and debt as of December 31, 2017, were as follows:

(in millions)	Fair Value At December 31, 2017	Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Foreign exchange contracts	$ 140	$ —	$ 140	$ —
Pension plan assets	7,288	5,260	2,028	—
Total assets in fair value hierarchy	$ 7,428	$ 5,260	$ 2,168	$ —
Pension plan assets measured at net asset value[(a)]	310			
Total assets	$ 7,738			
Liabilities:				
Debt	$ 35,856	$ 35,685	$ 171	$ —
Foreign exchange contracts	1,128	—	1,128	—
Total liabilities	$ 36,984	$ 35,685	$ 1,299	$ —

[(a)] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in these tables are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Note 17.

Accumulated Other Comprehensive Losses:

PMI's accumulated other comprehensive losses, net of taxes, consisted of the following:

(Losses) Earnings (in millions)	At December 31, 2018	2017	2016
Currency translation adjustments	**$ (6,500)**	$ (5,761)	$ (6,091)
Pension and other benefits	**(3,646)**	(2,816)	(3,565)
Derivatives accounted for as hedges	**35**	42	97
Total accumulated other comprehensive losses	**$ (10,111)**	$ (8,535)	$ (9,559)

Reclassifications from Other Comprehensive Earnings

The movements in accumulated other comprehensive losses and the related tax impact, for each of the components above, that are due to current period activity and reclassifications to the income statement are shown on the consolidated statements of comprehensive earnings for the years ended December 31, 2018, 2017, and 2016. For the years ended December 31, 2017, and 2016, $2 million and $(5) million of net currency translation adjustment gains/(losses) were transferred from other comprehensive earnings to marketing, administration and research costs in the consolidated statements of earnings, respectively, upon liquidation of subsidiaries. For additional information, see Note 13. *Benefit Plans* and Note 15. *Financial Instruments* for disclosures related to PMI's pension and other benefits and derivative financial instruments.

Note 18.

Contingencies:

Tobacco-Related Litigation

Legal proceedings covering a wide range of matters are pending or threatened against us, and/or our subsidiaries, and/or our indemnitees in various jurisdictions. Our indemnitees include distributors, licensees, and others that have been named as parties in certain cases and that we have agreed to defend, as well as to pay costs and some or all of judgments, if any, that may be entered against them. Pursuant to the terms of the Distribution Agreement between Altria Group, Inc. ("Altria") and PMI, PMI will indemnify Altria and Philip Morris USA Inc. ("PM USA"), a U.S. tobacco subsidiary of Altria, for tobacco product claims based in substantial part on products manufactured by PMI or contract manufactured for PMI by PM USA, and PM USA will indemnify PMI for tobacco product claims based in substantial part on products manufactured by PM USA, excluding tobacco products contract manufactured for PMI.

It is possible that there could be adverse developments in pending cases against us and our subsidiaries. An unfavorable outcome or settlement of pending tobacco-related litigation could encourage the commencement of additional litigation.

Damages claimed in some of the tobacco-related litigation are significant and, in certain cases in Brazil, Canada, Israel and Nigeria, range into the billions of U.S. dollars. The variability in pleadings in multiple jurisdictions, together with the actual experience of management in litigating claims, demonstrate that the monetary relief that may be specified in a lawsuit bears little relevance to the ultimate outcome. Much of the tobacco-related litigation is in its early stages, and litigation is subject to uncertainty. However, as discussed below, we have to date been largely successful in defending tobacco-related litigation.

We and our subsidiaries record provisions in the consolidated financial statements for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. At the present time, while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available to it (i) management has not concluded that it is probable that a loss has been incurred in any of the pending tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any. Legal defense costs are expensed as incurred.

It is possible that our consolidated results of operations, cash flows or financial position could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. Nevertheless, although litigation is subject to uncertainty, we and each of our subsidiaries named as a defendant believe, and each has been so advised by counsel handling the respective cases, that we have valid defenses to the litigation pending against us, as well as valid bases for appeal of adverse verdicts. All such cases are, and will continue to be, vigorously defended. However, we and our subsidiaries may enter into settlement discussions in particular cases if we believe it is in our best interests to do so.

To date, no tobacco-related case has been finally resolved in favor of a plaintiff against us, our subsidiaries or indemnitees.

The table below lists the number of tobacco-related cases pertaining to combustible products pending against us and/or our subsidiaries or indemnitees as of February 4, 2019, February 9, 2018 and December 31, 2016:

Type of Case	Number of Cases Pending as of February 4, 2019	Number of Cases Pending as of February 9, 2018	Number of Cases Pending as of December 31, 2016
Individual Smoking and Health Cases	**55**	57	64
Smoking and Health Class Actions	**10**	11	11
	16	16	16

Health Care Cost Recovery Actions			
Label-Related Class Actions	**1**	1	—
Individual Label-Related Cases	**7**	1	3
Public Civil Actions	**2**	2	2

Since 1995, when the first tobacco-related litigation was filed against a PMI entity, 491 Smoking and Health, Label-Related, Health Care Cost Recovery, and Public Civil Actions in which we and/or one of our subsidiaries and/or indemnitees were a defendant have been terminated in our favor. Thirteen cases have had decisions in favor of plaintiffs. Nine of these cases have subsequently reached final resolution in our favor and four remain on appeal.

The table below lists the verdict and significant post-trial developments in the four pending cases where a verdict was returned in favor of the plaintiff:

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
February 2004	Brazil/The Smoker Health Defense Association	Class Action	The Civil Court of São Paulo found defendants liable without hearing evidence. In April 2004, the court awarded "moral damages" of R$1,000 (approximately $273) per smoker per full year of smoking plus interest at the rate of 1% per month, as of the date of the ruling. The court did not assess actual damages, which were to be assessed in a second phase of the case. The size of the class was not defined in the ruling.	Defendants appealed to the São Paulo Court of Appeals, which annulled the ruling in November 2008, finding that the trial court had inappropriately ruled without hearing evidence and returned the case to the trial court for further proceedings. In May 2011, the trial court dismissed the claim. In March 2017, plaintiff filed an *en banc* appeal to the Superior Court of Justice. In addition, the defendants filed a constitutional appeal to the Federal Supreme Tribunal on the basis that plaintiff did not have standing to bring the lawsuit. Both appeals are still pending.

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
May 27, 2015	Canada/Cecilia Létourneau	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec ruled in favor of the *Létourneau* class on liability and awarded a total of CAD 131 million (approximately $100 million) in punitive damages, allocating CAD 46 million (approximately $35 million) to our subsidiary. The trial court ordered defendants to pay the full punitive damage award into a trust within 60 days. The court did not order the payment of compensatory damages.	In June 2015, our subsidiary commenced the appellate process with the Court of Appeal of Quebec. Our subsidiary also filed a motion to cancel the trial court's order for payment into a trust notwithstanding appeal. In July 2015, the Court of Appeal granted the motion to cancel and overturned the trial court's ruling that our subsidiary make the payment into a trust. In August 2015, plaintiffs filed a motion for security with the Court of Appeal covering both the *Létourneau* case and the *Blais* case described below. In October 2015, the Court of Appeal granted the motion and ordered our subsidiary to furnish security totaling CAD 226 million (approximately $172.5 million) to cover both the *Létourneau* and *Blais* cases. The hearing for the merits appeal took place

in November 2016. (See below for further detail.)

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
May 27, 2015	Canada/Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec ruled in favor of the *Blais* class on liability and found the class members' compensatory damages totaled approximately CAD 15.5 billion (approximately $11.8 billion), including pre-judgment interest. The trial court awarded compensatory damages on a joint and several liability basis, allocating 20% to our subsidiary (approximately CAD 3.1 billion including pre-judgment interest (approximately $2.37 billion)). The trial court awarded CAD 90,000 (approximately $69,000) in punitive damages, allocating CAD 30,000 (approximately $23,000) to our subsidiary. The trial court ordered defendants to pay CAD 1 billion (approximately $763 million) of the compensatory damage award, CAD 200 million (approximately $153 million) of which is our subsidiary's portion, into a trust within 60 days.	In June 2015, our subsidiary commenced the appellate process with the Court of Appeal of Quebec. Our subsidiary also filed a motion to cancel the trial court's order for payment into a trust notwithstanding appeal. In July 2015, the Court of Appeal granted the motion to cancel and overturned the trial court's ruling that our subsidiary make the payment into a trust. In August 2015, plaintiffs filed a motion for security with the Court of Appeal. In October 2015, the Court of Appeal granted the motion and ordered our subsidiary to furnish security totaling, together with the *Létourneau* case, CAD 226 million (approximately $172.5 million). The hearing for the merits appeal took place in November 2016. (See below for further detail.)

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
August 5, 2016	Argentina/Hugo Lespada	Individual Action	On August 5, 2016, the Civil Court No. 14 - Mar del Plata, issued a verdict in favor of plaintiff, an individual smoker, and awarded him ARS 110,000	On August 23, 2016, our subsidiary filed its notice of appeal. On October 31, 2017, the Civil and Commercial Court of Appeals of Mar del Plata ruled that plaintiff's claim

	(approximately $2,960), plus interest, in compensatory and moral damages. The trial court found that our subsidiary failed to warn plaintiff of the risk of becoming addicted to cigarettes.	was barred by the statute of limitations and it reversed the trial court's decision. On November 28, 2017, plaintiff filed an extraordinary appeal of the reversal of the trial court's decision to the Supreme Court of the Province of Buenos Aires.

Pending claims related to tobacco products generally fall within the following categories:

Smoking and Health Litigation: These cases primarily allege personal injury and are brought by individual plaintiffs or on behalf of a class or purported class of individual plaintiffs. Plaintiffs' allegations of liability in these cases are based on various theories of recovery, including negligence, gross negligence, strict liability, fraud, misrepresentation, design defect, failure to warn, breach of express and implied warranties, violations of deceptive trade practice laws and consumer protection statutes. Plaintiffs in these cases seek various forms of relief, including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include licit activity, failure to state a claim, lack of defect, lack of proximate cause, assumption of the risk, contributory negligence, and statute of limitations.

As of February 4, 2019, there were a number of smoking and health cases pending against us, our subsidiaries or indemnitees, as follows:

- 55 cases brought by individual plaintiffs in Argentina (32), Brazil (8), Canada (2), Chile (4), Costa Rica (1), Italy (3), the Philippines (1), Poland (2), Turkey (1) and Scotland (1), compared with 57 such cases on February 9, 2018, and 64 cases on December 31, 2016; and

- 10 cases brought on behalf of classes of individual plaintiffs in Brazil (1) and Canada (9), compared with 11 such cases on February 9, 2018, and 11 such cases on December 31, 2016.

In the class action pending in Brazil, *The Smoker Health Defense Association (ADESF) v. Souza Cruz, S.A. and Philip Morris Marketing, S.A., Nineteenth Lower Civil Court of the Central Courts of the Judiciary District of São Paulo, Brazil*, filed July 25, 1995, our subsidiary and another member of the industry are defendants. The plaintiff, a consumer organization, is seeking damages for all addicted smokers and former smokers, and injunctive relief. In 2004, the trial court found defendants liable without hearing evidence and awarded "moral damages" of R$1,000 (approximately $273) per smoker per full year of smoking plus interest at the rate of 1% per month, as of the date of the ruling. The court did not award actual damages, which were to be assessed in the second phase of the case. The size of the class was not estimated. Defendants appealed to the São Paulo Court of Appeals, which annulled the ruling in November 2008, finding that the trial court had inappropriately ruled without hearing evidence and returned the case to the trial court for further proceedings. In May 2011, the trial court dismissed the claim. In February 2015, the appellate court unanimously dismissed plaintiff's appeal. In September 2015, plaintiff appealed to the Superior Court of Justice. In February 2017, the Chief Justice of the Superior Court of Justice denied plaintiff's appeal. In March 2017, plaintiff filed an *en banc* appeal to the Superior Court of Justice. In addition, the defendants filed a constitutional appeal to the Federal Supreme Tribunal on the basis that plaintiff did not have standing to bring the lawsuit. Both appeals are still pending.

In the first class action pending in Canada, *Cecilia Létourneau v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI Macdonald Corp., Quebec Superior Court, Canada,* filed in September 1998, our subsidiary and other Canadian manufacturers (Imperial Tobacco Canada Ltd. and JTI-MacDonald Corp.) are defendants. The plaintiff, an individual smoker, sought compensatory and punitive damages for each member of the class who is deemed addicted to smoking. The class was certified in 2005. Trial began in March 2012 and concluded in December 2014. The trial court issued its judgment on May 27, 2015. The trial court found our subsidiary and two other Canadian manufacturers liable and awarded a total of CAD 131 million (approximately $100 million) in punitive damages, allocating CAD 46 million (approximately $35 million) to our subsidiary. The trial court found that defendants violated the Civil Code of Quebec, the Quebec Charter of Human Rights and Freedoms, and the Quebec Consumer Protection Act by failing to warn adequately of the dangers of smoking. The trial court also found that defendants conspired to prevent consumers from learning the dangers of smoking. The trial court further held that these civil faults were a cause of the class members' addiction. The trial court rejected other grounds of fault advanced by the class, holding that: (i) the evidence was insufficient to show that defendants marketed to youth, (ii) defendants' advertising did not convey false information about the characteristics of cigarettes, and (iii) defendants did not commit a fault by using the descriptors light or mild for cigarettes with a lower tar delivery. The trial court estimated the size of the addiction class at 918,000 members but declined to award compensatory damages to the addiction class because the evidence did not establish the claims with sufficient accuracy. The trial court ordered defendants to pay the full punitive damage award into a trust within 60 days and found that a claims process to allocate the awarded damages to individual class members would be too expensive and difficult to administer. The

trial court ordered a briefing on the proposed process for the distribution of sums remaining from the punitive damage award after payment of attorneys' fees and legal costs. In June 2015, our subsidiary commenced the appellate process by filing its inscription of appeal of the trial court's judgment with the Court of Appeal of Quebec. Our subsidiary also filed a motion to cancel the trial court's order for payment into a trust within 60 days notwithstanding appeal. In July 2015, the Court of Appeal granted the motion to cancel and overturned the trial court's ruling that our subsidiary make the payment into a trust within 60 days. In August 2015, plaintiffs filed a motion with the Court of Appeal seeking security in both the *Létourneau* case and the *Blais* case described below. In October 2015, the Court of Appeal granted the motion and ordered our subsidiary to furnish security totaling CAD 226 million (approximately $172.5 million), in the form of cash into a court trust or letters of credit, in six equal consecutive quarterly installments of approximately CAD 37.6 million (approximately $28.7 million) beginning in December 2015 through March 2017. See the *Blais* description for further detail concerning

the security order. The Court of Appeal heard oral arguments on the merits appeal in November 2016. Our subsidiary and PMI believe that the findings of liability and damages were incorrect and should ultimately be set aside on any one of many grounds, including the following: (i) holding that defendants violated Quebec law by failing to warn class members of the risks of smoking even after the court found that class members knew, or should have known, of the risks, (ii) finding that plaintiffs were not required to prove that defendants' alleged misconduct caused injury to each class member in direct contravention of binding precedent, (iii) creating a factual presumption, without any evidence from class members or otherwise, that defendants' alleged misconduct caused all smoking by all class members, (iv) holding that the addiction class members' claims for punitive damages were not time-barred even though the case was filed more than three years after a prominent addiction warning appeared on all packages, and (v) awarding punitive damages to punish defendants without proper consideration as to whether punitive damages were necessary to deter future misconduct.

In the second class action pending in Canada, *Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI Macdonald Corp., Quebec Superior Court, Canada*, filed in November 1998, our subsidiary and other Canadian manufacturers (Imperial Tobacco Canada Ltd. and JTI-MacDonald Corp.) are defendants. The plaintiffs, an anti-smoking organization and an individual smoker, sought compensatory and punitive damages for each member of the class who allegedly suffers from certain smoking-related diseases. The class was certified in 2005. Trial began in March 2012 and concluded in December 2014. The trial court issued its judgment on May 27, 2015. The trial court found our subsidiary and two other Canadian manufacturers liable and found that the class members' compensatory damages totaled approximately CAD 15.5 billion, including pre-judgment interest (approximately $11.8 billion). The trial court awarded compensatory damages on a joint and several liability basis, allocating 20% to our subsidiary (approximately CAD 3.1 billion, including pre-judgment interest (approximately $2.37 billion)). In addition, the trial court awarded CAD 90,000 (approximately $69,000) in punitive damages, allocating CAD 30,000 (approximately $23,000) to our subsidiary and found that defendants violated the Civil Code of Quebec, the Quebec Charter of Human Rights and Freedoms, and the Quebec Consumer Protection Act by failing to warn adequately of the dangers of smoking. The trial court also found that defendants conspired to prevent consumers from learning the dangers of smoking. The trial court further held that these civil faults were a cause of the class members' diseases. The trial court rejected other grounds of fault advanced by the class, holding that: (i) the evidence was insufficient to show that defendants marketed to youth, (ii) defendants' advertising did not convey false information about the characteristics of cigarettes, and (iii) defendants did not commit a fault by using the descriptors light or mild for cigarettes with a lower tar delivery. The trial court estimated the disease class at 99,957 members. The trial court ordered defendants to pay CAD 1 billion (approximately $763 million) of the compensatory damage award into a trust within 60 days, CAD 200 million (approximately $153 million) of which is our subsidiary's portion and ordered briefing on a proposed claims process for the distribution of damages to individual class members and for payment of attorneys' fees and legal costs. In June 2015, our subsidiary commenced the appellate process by filing its inscription of appeal of the trial court's judgment with the Court of Appeal of Quebec. Our subsidiary also filed a motion to cancel the trial court's order for payment into a trust within 60 days notwithstanding appeal. In July 2015, the Court of Appeal granted the motion to cancel and overturned the trial court's ruling that our subsidiary make an initial payment within 60 days. In August 2015, plaintiffs filed a motion with the Court of Appeal seeking an order that defendants place irrevocable letters of credit totaling CAD 5 billion (approximately $3.8 billion) into trust, to secure the judgments in both the *Létourneau* and *Blais* cases. Plaintiffs subsequently withdrew their motion for security against JTI-MacDonald Corp. and proceeded only against our subsidiary and Imperial Tobacco Canada Ltd. In October 2015, the Court of Appeal granted the motion and ordered our subsidiary to furnish security totaling CAD 226 million (approximately $172.5 million) to cover both the *Létourneau* and *Blais* cases. Such security may take the form of cash into a court trust or letters of credit, in six equal consecutive quarterly installments of approximately CAD 37.6 million (approximately $28.7 million) beginning in December 2015 through March 2017. The Court of Appeal ordered Imperial Tobacco Canada Ltd. to furnish security totaling CAD 758 million (approximately $578 million) in seven equal consecutive quarterly installments of approximately CAD 108 million (approximately $82.4 million) beginning in December 2015 through June 2017. In March 2017, our subsidiary made its sixth and final quarterly installment of security for approximately CAD 37.6 million (approximately $28.7 million) into a court trust. This payment is included in other assets on the consolidated balance sheets and in cash used in operating activities in the consolidated statements of cash flows. The Court of Appeal ordered that the security is payable upon a final judgment of the Court of Appeal affirming the trial court's judgment or upon further order of the Court of Appeal. The Court of Appeal heard oral arguments on the merits appeal in November 2016. Our subsidiary and PMI believe that the findings of liability and damages were incorrect and should ultimately be set aside on any one of many grounds, including the following: (i) holding that defendants violated Quebec law by failing to warn class members of the risks of smoking even after the court found that class members knew, or should have known, of the risks, (ii) finding that plaintiffs were not required to prove that defendants' alleged misconduct caused injury to each class member in direct contravention of binding

precedent, (iii) creating a factual presumption, without any evidence from class members or otherwise, that defendants' alleged misconduct caused all smoking by all class members, (iv) relying on epidemiological evidence that did not meet recognized scientific standards, and (v) awarding punitive damages to punish defendants without proper consideration as to whether punitive damages were necessary to deter future misconduct.

In the third class action pending in Canada, *Kunta v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Winnipeg, Canada*, filed June 12, 2009, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic obstructive pulmonary disease ("COPD"), severe asthma, and mild reversible lung disease resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products. In September 2009,

plaintiff's counsel informed defendants that he did not anticipate taking any action in this case while he pursues the class action filed in Saskatchewan (see description of *Adams*, below).

In the fourth class action pending in Canada, *Adams v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Saskatchewan, Canada*, filed July 10, 2009, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, emphysema, heart disease, or cancer, as well as restitution of profits. Preliminary motions are pending.

In the fifth class action pending in Canada, *Semple v. Canadian Tobacco Manufacturers' Council, et al., The Supreme Court (trial court), Nova Scotia, Canada*, filed June 18, 2009, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and COPD resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products. No activity in this case is anticipated while plaintiff's counsel pursues the class action filed in Saskatchewan (see description of *Adams*, above).

In the sixth class action pending in Canada, *Dorion v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Alberta, Canada,* filed June 15, 2009, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic bronchitis and severe sinus infections resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products. To date, we, our subsidiaries, and our indemnitees have not been properly served with the complaint. No activity in this case is anticipated while plaintiff's counsel pursues the class action filed in Saskatchewan (see description of *Adams*, above).

In the seventh class action pending in Canada, *McDermid v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and heart disease resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from heart disease allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed.

In the eighth class action pending in Canada, *Bourassa v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, the heir to a deceased smoker, alleges that the decedent was addicted to tobacco products and suffered from emphysema resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from chronic respiratory diseases allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed. In December 2014, plaintiff filed an amended statement of claim.

In the ninth class action pending in Canada, *Suzanne Jacklin v. Canadian Tobacco Manufacturers' Council, et al., Ontario Superior Court of Justice,* filed June 20, 2012, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, heart disease, or cancer, as well as restitution of profits. Plaintiff's counsel has indicated that he does not intend to take any action in this case in the near future.

Health Care Cost Recovery Litigation: These cases, brought by governmental and non-governmental plaintiffs, seek reimbursement of health care cost expenditures allegedly caused by tobacco products. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including unjust enrichment, negligence, negligent design, strict liability, breach of express and implied warranties, violation of a voluntary undertaking or special duty,

fraud, negligent misrepresentation, conspiracy, public nuisance, defective product, failure to warn, sale of cigarettes to minors, and claims under statutes governing competition and deceptive trade practices. Plaintiffs in these cases seek various forms of relief including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include lack of proximate cause, remoteness of injury, failure to state a claim, adequate remedy at law, "unclean hands" (namely, that plaintiffs cannot obtain equitable relief because they participated in, and benefited from, the sale of cigarettes), and statute of limitations.

As of February 4, 2019, there were 16 health care cost recovery cases pending against us, our subsidiaries or indemnitees in Canada (10), Korea (1) and Nigeria (5), compared with 16 such cases on February 9, 2018 and 16 such cases on December 31, 2016.

In the first health care cost recovery case pending in Canada, *Her Majesty the Queen in Right of British Columbia v. Imperial Tobacco Limited, et al., Supreme Court, British Columbia, Vancouver Registry, Canada,* filed January 24, 2001, we, our subsidiaries, our indemnitee (PM USA), and other members of the industry are defendants. The plaintiff, the government of the province of British Columbia, brought a claim based upon legislation enacted by the province authorizing the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, resulting from a "tobacco related wrong." The Supreme Court of Canada has held that the statute is constitutional. We and certain other non-Canadian defendants challenged the jurisdiction of the court. The court rejected the jurisdictional challenge. Pre-trial discovery is ongoing.

In the second health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of New Brunswick v. Rothmans Inc., et al., Court of Queen's Bench of New Brunswick, Trial Court, New Brunswick, Fredericton, Canada,* filed March 13, 2008, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of New Brunswick based on legislation enacted in the province. This legislation is similar to the law introduced in British Columbia that authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Pre-trial discovery is ongoing. In June 2017, the trial court set a trial date for November 4, 2019.

In the third health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of Ontario v. Rothmans Inc., et al., Ontario Superior Court of Justice, Toronto, Canada*, filed September 29, 2009, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Ontario based on legislation enacted in the province. This legislation is similar to the laws introduced in British Columbia and New Brunswick that authorize the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Pre-trial discovery is ongoing.

In the fourth health care cost recovery case filed in Canada, *Attorney General of Newfoundland and Labrador v. Rothmans Inc., et al., Supreme Court of Newfoundland and Labrador, St. Johns, Canada*, filed February 8, 2011, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Newfoundland and Labrador based on legislation enacted in the province that is similar to the laws introduced in British Columbia, New Brunswick and Ontario. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Pre-trial discovery is ongoing.

In the fifth health care cost recovery case filed in Canada, *Attorney General of Quebec v. Imperial Tobacco Limited, et al., Superior Court of Quebec, Canada*, filed June 8, 2012, we, our subsidiary, our indemnitee (PM USA), and other members of the industry are defendants. The claim was filed by the government of the province of Quebec based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Pre-trial discovery is ongoing.

In the sixth health care cost recovery case filed in Canada, *Her Majesty in Right of Alberta v. Altria Group, Inc., et al., Supreme Court of Queen's Bench Alberta, Canada*, filed June 8, 2012, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Alberta based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Pre-trial discovery is ongoing.

In the seventh health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Manitoba v. Rothmans, Benson & Hedges, Inc., et al., The Queen's Bench, Winnipeg Judicial Centre, Canada*, filed May 31, 2012, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Manitoba based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and

will incur, as a result of a “tobacco related wrong.” Defendants filed their defenses in September 2014. Pre-trial discovery is ongoing.

In the eighth health care cost recovery case filed in Canada, *The Government of Saskatchewan v. Rothmans, Benson & Hedges Inc., et al., Queen's Bench, Judicial Centre of Saskatchewan, Canada*, filed June 8, 2012, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Saskatchewan based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a

result of a “tobacco related wrong.” Defendants filed their defenses in February 2015. While discovery initially was scheduled to begin in 2017 by agreement of the parties, to date, the discovery process has not started.

In the ninth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Prince Edward Island v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Prince Edward Island (General Section), Canada*, filed September 10, 2012, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Prince Edward Island based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a “tobacco related wrong.” Defendants filed their defenses in February 2015. While discovery initially was scheduled to begin in 2017 by agreement of the parties, to date, the discovery process has not started.

In the tenth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Nova Scotia v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Nova Scotia, Canada*, filed January 2, 2015, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Nova Scotia based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a “tobacco related wrong.” Defendants filed their defenses in July 2015. Pre-trial discovery is ongoing.

In the first health care cost recovery case in Nigeria, *The Attorney General of Lagos State v. British American Tobacco (Nigeria) Limited, et al., High Court of Lagos State, Lagos, Nigeria,* filed March 13, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of making challenges to service and the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the second health care cost recovery case in Nigeria, *The Attorney General of Kano State v. British American Tobacco (Nigeria) Limited, et al., High Court of Kano State, Kano, Nigeria,* filed May 9, 2007, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of making challenges to service and the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the third health care cost recovery case in Nigeria, *The Attorney General of Gombe State v. British American Tobacco (Nigeria) Limited, et al., High Court of Gombe State, Gombe, Nigeria,* filed October 17, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In February 2011, the court ruled that the plaintiff had not complied with the procedural steps necessary to serve us. As a result of this ruling, plaintiff must re-serve its claim. We have not yet been re-served.

In the fourth health care cost recovery case in Nigeria, *The Attorney General of Oyo State, et al., v. British American Tobacco (Nigeria) Limited, et al., High Court of Oyo State, Ibadan, Nigeria,* filed May 25, 2007, we and other members of the industry are defendants. Plaintiffs seek reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We challenged service as improper. In June 2010, the court ruled that plaintiffs did not have leave to serve the writ of summons on the defendants and that they must re-serve the writ. We have not yet been re-served.

In the fifth health care cost recovery case in Nigeria, *The Attorney General of Ogun State v. British American Tobacco (Nigeria) Limited, et al., High Court of Ogun State, Abeokuta, Nigeria*, filed February 26, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In May 2010, the trial court rejected our service objections. We have appealed.

In the health care cost recovery case in Korea, the *National Health Insurance Service v. KT&G, et. al.,* filed April 14, 2014, our subsidiary and other Korean manufacturers are defendants. Plaintiff alleges that defendants concealed the health hazards of smoking, marketed to youth, added ingredients to make their products more harmful and addictive, and misled consumers into believing that *Lights* cigarettes are safer than regular cigarettes. The National Health Insurance Service seeks to recover approximately $53.7 million allegedly incurred in treating 3,484 patients with small cell lung cancer, squamous cell lung cancer, and squamous cell laryngeal cancer from 2003 to 2012. The case is now in the evidentiary phase.

Label-Related Cases: These cases, brought by individual plaintiffs, or on behalf of a class or purported class of individual plaintiffs, allege that the use of the descriptor "Lights" or other alleged misrepresentations or omissions of labeling information constitute fraudulent and misleading conduct. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including misrepresentation, deception, and breach of consumer protection laws. Plaintiffs seek various forms of relief including restitution, injunctive relief, and compensatory and other damages. Defenses raised include lack of causation, lack of reliance, assumption of the risk, and statute of limitations.

As of February 4, 2019, there were 7 cases brought by individual plaintiffs in Italy (1) and Chile (6) pending against our subsidiaries, compared with 1 such case on February 9, 2018, and 3 such cases on December 31, 2016, and one purported class action in Israel (1).

An individual plaintiff filed a purported class action certification motion, *Aharon Ringer v. Philip Morris Ltd. and Globrands Ltd.,* on July 18, 2017, in the Central District Court of Israel. Our Israeli affiliate and an Israeli importer and distributor for other multinational tobacco companies are defendants. Plaintiff seeks to represent a class of smokers in Israel who have purchased cigarettes imported by defendants since July 18, 2010. Plaintiff estimates the class size to be 7,000,000 smokers. Plaintiff alleges that defendants misled consumers by not disclosing sufficient information about carbon monoxide, tar, and nicotine yields of, and tobacco contained in, the imported cigarettes. Plaintiff seeks various forms of relief, including an order for defendants to label cigarette packs in accordance with plaintiff's demands, and damages for misleading consumers, breach of autonomy and unjust enrichment. Pre-class certification hearings have been scheduled to begin in March 2019.

Public Civil Actions: Claims have been filed either by an individual, or a public or private entity, seeking to protect collective or individual rights, such as the right to health, the right to information or the right to safety. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including product defect, concealment, and misrepresentation. Plaintiffs in these cases seek various forms of relief including injunctive relief such as banning cigarettes, descriptors, smoking in certain places and advertising, as well as implementing communication campaigns and reimbursement of medical expenses incurred by public or private institutions.

As of February 4, 2019, there were 2 public civil actions pending against our subsidiaries in Argentina (1) and Venezuela (1), compared with 2 such cases on February 9, 2018, and 2 such cases on December 31, 2016.

In the public civil action in Argentina, *Asociación Argentina de Derecho de Danos v. Massalin Particulares S.A., et al., Civil Court of Buenos Aires, Argentina,* filed February 26, 2007, our subsidiary and another member of the industry are defendants. The plaintiff, a consumer association, seeks the establishment of a relief fund for reimbursement of medical costs associated with diseases allegedly caused by smoking. Our subsidiary filed its answer in September 2007. In March 2010, the case file was transferred to the Federal Court on Administrative Matters after the Civil Court granted plaintiff's request to add the national government as a co-plaintiff in the case. The case is currently in the evidentiary stage.

In the public civil action in Venezuela, *Federation of Consumers and Users Associations ("FEVACU"), et al. v. National Assembly of Venezuela and the Venezuelan Ministry of Health, Constitutional Chamber of the Venezuelan Supreme Court*, filed April 29, 2008, we were not named as a defendant, but the plaintiffs published a notice pursuant to court order, notifying all interested parties to appear in the case. In January 2009, our subsidiary appeared in the case in response to this notice. The plaintiffs purport to represent the right to health of the citizens of Venezuela and claim that the government failed to protect adequately its citizens' right to health. The claim asks the court to order the government to enact stricter regulations on the manufacture and sale of tobacco products. In addition, the plaintiffs ask the court to order companies involved in the tobacco industry to allocate a percentage of their "sales or benefits" to establish a fund to pay for the health care costs of treating smoking-related diseases. In October 2008, the court ruled that plaintiffs have standing to file the claim and that the claim meets the threshold admissibility requirements. In December 2012, the court admitted our subsidiary and BAT's subsidiary as interested third parties. In February 2013, our subsidiary answered the complaint.

Reduced-Risk Products

In Israel, an individual filed a purported class action certification motion in June 2017 against our subsidiary with the Israeli District Court of Haifa related to the marketing of *IQOS*. Plaintiff alleges that our affiliate misleads consumers by marketing *IQOS* as a "better alternative to smoking" and as a reduced-risk product, while not disclosing the risks associated with the product. Plaintiff alleges that *IQOS* is more addictive and more dangerous than cigarettes.

Plaintiff claims that the first time he used *IQOS*, he experienced tightness in the chest, difficulty breathing, chills, nausea and dizziness. Plaintiff seeks damages on his behalf, and on behalf of the class (defined as all *IQOS* consumers in Israel), for personal injuries, emotional distress, breach of autonomy, and unjust enrichment. Pre-class certification hearings have been scheduled to begin in May 2019.

Other Litigation

The Department of Special Investigations of the government of Thailand ("DSI") conducted an investigation into alleged underpayment by our subsidiary, Philip Morris (Thailand) Limited ("PM Thailand"), of customs duties and excise taxes relating to imports from the Philippines covering the period 2003-2007. On January 18, 2016, the Public Prosecutor filed charges against our subsidiary and seven former and current employees in the Bangkok Criminal Court alleging that PM Thailand and the individual defendants jointly and with the intention to defraud the Thai government, under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries of cigarettes from the Philippines during the period of July 2003 to June 2006. The government is seeking a fine of approximately THB 80.8 billion (approximately $2.57 billion). In May 2017, the King of Thailand signed a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and other Thai governmental agencies. Trial in the case began in November 2017. In March 2018, acting on a request from the Public Prosecutor, the court suspended the trial proceedings indefinitely and struck the case from the court list. In June 2018, the court reinstated the case and scheduled the remaining trial proceedings for May 2019.

The DSI also conducted an investigation into alleged underpayment by PM Thailand of customs duties and excise taxes relating to imports from Indonesia covering the period 2000-2003. On January 26, 2017, the Public Prosecutor filed charges against PM Thailand and its former Thai employee in the Bangkok Criminal Court alleging that PM Thailand and its former employee jointly and with the intention to defraud the Thai government under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries during the period from January 2002 to July 2003. The government is seeking a fine of approximately THB 19.8 billion (approximately $630 million). In May 2017, the King of Thailand signed a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law, and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and a Thai court. Trial in the case began in November 2018.

On November 29, 2017, PM Thailand received notices of assessment in the aggregate amount of approximately THB 25.6 billion (approximately $814 million) from the Thai Customs Department alleging that PM Thailand under-declared customs values for the imports from Indonesia covering the period 2001-2003. The notices include the Indonesian import entries subject to the proceedings discussed above and are in addition to the fine sought by the government in the criminal proceedings. PM Thailand filed its appeal against the notices with the Thai Customs Board of Appeal in December 2017, asserting that all of the notices of assessment are barred by the applicable statutes of limitations and are otherwise without merit. On August 30, 2018, the Thai Customs Board of Appeal issued a ruling striking out or revoking all notices of assessment. Accordingly, there are no pending notices of assessment in the matter.

The South Korean Board of Audit and Inspection ("BAI") conducted an audit of certain Korean government agencies and the tobacco industry into whether inventory movements ahead of the January 1, 2015 increase of cigarette-related taxes by tobacco companies, including Philip Morris Korea Inc. ("PM Korea"), our South Korean affiliate, were in compliance with South Korean tax laws. In November 2016, the tax authorities completed their audit and assessed allegedly underpaid taxes and penalties. In order to avoid nonpayment financial costs, PM Korea paid approximately KRW 272 billion (approximately $243 million), of which KRW 100 billion (approximately $89 million) was paid in 2016 and KRW 172 billion (approximately $154 million) was paid in the first quarter of 2017. These amounts are included in other assets in the consolidated balance sheets and in cash used in operating activities in the consolidated statements of cash flows. PM Korea is appealing the assessments. The tax authorities have also referred the matter to the Public Prosecutor. On June 19, 2018, the Public Prosecutor decided not to file criminal charges against PM Korea and/or other alleged co-offenders. This decision is being appealed by the tax authorities and, if reversed, the Public Prosecutor may seek up to three times the underpaid tax for company criminal penalties and up to five times the underpaid tax for individual criminal penalties. The Public Prosecutor also decided not to prosecute PM Korea and its managing director in connection with a criminal complaint against them that had been filed by the South Korean Ministry of Strategy and Finance ("MOSF"). In this criminal complaint, the MOSF alleged that PM Korea exceeded the monthly product withdrawal limits that the MOSF had set in its notice. This decision is being appealed by the MOSF. PM Korea believes that it has paid cigarette-related taxes in compliance with the South Korean tax laws and disagrees with the MOSF's allegations.

A putative shareholder class action lawsuit, *Rubenstahl v. Philip Morris International Inc., et al.,* was filed in December 2017, in the United States District Court for the District of New Jersey, purportedly on behalf of purchasers of Philip Morris International Inc. stock between July 26, 2016 and December 20, 2017. The lawsuit names Philip Morris International Inc. and certain officers as defendants and includes allegations that the defendants made false and/or misleading statements and/or failed to disclose information about PMI's business, operations, financial condition, and prospects related to alleged irregularities in clinical studies of PMI's *IQOS* tobacco heating system. The lawsuit seeks various forms of relief, including damages. We believe that this lawsuit is without merit and intend to defend it vigorously.

A putative shareholder class action lawsuit, *City of Westland Police and Fire Retirement System v. Philip Morris International Inc., et al.,* was filed in September 2018, in the United States District Court for the Southern District of New York, purportedly on behalf of purchasers of Philip Morris International Inc. stock between February 8, 2018 and April 18, 2018. The lawsuit names Philip Morris International Inc. and certain officers as defendants and includes allegations that the defendants made false and/or misleading statements and/or failed to disclose information about PMI's business, operations, financial condition, and prospects related to product sales, including those of PMI's *IQOS* tobacco heating system. The lawsuit seeks various forms of relief, including damages. We believe that this lawsuit is without merit and intend to defend it vigorously. In November 2018, the Court consolidated this lawsuit with the other putative shareholder class action lawsuits pending in the Southern District of New York.

A putative shareholder class action lawsuit, *Greater Pennsylvania Carpenters' Pension Fund v. Philip Morris International Inc., et al.,* was filed in September 2018, in the United States District Court for the Southern District of New York, purportedly on behalf of purchasers of Philip Morris International Inc. stock between July 26, 2016 and April 18, 2018. The lawsuit names Philip Morris International Inc. and certain officers as defendants and seeks to combine the allegations and putative classes of the two cases discussed immediately above. The lawsuit seeks various forms of relief, including damages. We believe that this lawsuit is without merit and intend to defend it vigorously.

A putative shareholder class action lawsuit, *Gilchrist v. Philip Morris International Inc., et al.,* was filed in October 2018, in the United States District Court for the Southern District of New York, purportedly on behalf of purchasers of Philip Morris International Inc. stock between February 8, 2018 and April 18, 2018. The lawsuit names Philip Morris International Inc. and certain officers as defendants and includes allegations that the defendants made false and/or misleading statements and/or failed to disclose information about PMI's business, operations, financial condition, and prospects related to product sales, including those of PMI's *IQOS* tobacco heating system. The lawsuit seeks various forms of relief, including damages. We have not yet been served with the complaint, but believe this lawsuit is without merit and intend to defend it vigorously.

We are also involved in additional litigation arising in the ordinary course of our business. While the outcomes of these proceedings are uncertain, management does not expect that the ultimate outcomes of other litigation, including any reasonably possible losses in excess of current accruals, will have a material adverse effect on our consolidated results of operations, cash flows or financial position.

Note 19.

Balance Sheet Offsetting:

Derivative Financial Instruments

PMI uses foreign exchange contracts and interest rate contracts to mitigate its exposure to changes in exchange and interest rates from third-party and intercompany actual and forecasted transactions. Substantially all of PMI's derivative financial instruments are subject to master netting arrangements, whereby the right to offset occurs in the event of default by a participating party. While these contracts contain the enforceable right to offset through close-out netting rights, PMI elects to present them on a gross basis in the consolidated balance sheets. Collateral associated with these arrangements is in the form of cash and is unrestricted. See Note 15. *Financial Instruments* for disclosures related to PMI's derivative financial instruments.

The effects of these derivative financial instrument assets and liabilities on PMI's consolidated balance sheets were as follows:

(in millions)	Gross Amounts Recognized	Gross Amount Offset in the Consolidated Balance Sheet	Net Amounts Presented in the Consolidated Balance Sheet	Gross Amounts Not Offset in the Consolidated Balance Sheet		Net Amount
				Financial Instruments	Cash Collateral Received/ Pledged	
At December 31, 2018						
Assets						
Foreign exchange contracts	**$ 220**	**$ —**	**$ 220**	**$ (124)**	**$ (80)**	**$ 16**
Liabilities						
Foreign exchange contracts	**$ 631**	**$ —**	**$ 631**	**$ (124)**	**$ (427)**	**$ 80**
At December 31, 2017						
Assets						
Foreign exchange contracts	$ 140	$ —	$ 140	$ (50)	$ (78)	$ 12
Liabilities						
Foreign exchange contracts	$ 1,128	$ —	$ 1,128	$ (50)	$ (1,004)	$ 74

Note 20.

Sale of Accounts Receivable:

To mitigate risk and enhance cash and liquidity management PMI sells trade receivables to unaffiliated financial institutions. These arrangements allow PMI to sell, on an ongoing basis, certain trade receivables without recourse. The trade receivables sold are generally short-term in nature and are removed from the consolidated balance sheets. PMI sells trade receivables under two types of arrangements, servicing and non-servicing. For servicing arrangements, PMI continues to service the sold trade receivables on an administrative basis and does not act on behalf of the unaffiliated financial institutions. When applicable, a servicing liability is recorded for the estimated fair value of the servicing. The amounts associated with the servicing liability were not material for the years ended December 31, 2018 and 2017. Under the non-servicing arrangements, PMI does not provide any administrative support or servicing after the trade receivables have been sold to the unaffiliated financial institutions.

Cumulative trade receivables sold, including excise taxes, for the years ended December 31, 2018 and 2017, were $11.0 billion and $10.0 billion, respectively. PMI’s operating cash flows were positively impacted by the amount of the trade receivables sold and derecognized from the consolidated balance sheets, which remained outstanding with the unaffiliated financial institutions. The trade receivables sold that remained outstanding under these arrangements as of December 31, 2018, 2017 and 2016, were $1.0 billion, $1.1 billion and $0.7 billion, respectively. The net proceeds received are included in cash provided by operating activities in the consolidated statements of cash flows. The difference between the carrying amount of the trade receivables sold and the sum of the cash received is recorded as a loss on sale of trade receivables within marketing, administration and research costs in the consolidated statements of earnings. For the years ended December 31, 2018, 2017 and 2016 the loss on sale of trade receivables was immaterial.

Note 21.

New Accounting Standards:

Recently adopted

On January 1, 2018, PMI adopted Financial Accounting Standards Update ASU 2014-09, "Revenue from Contracts with Customers" ("ASU 2014-09"). ASU 2014-09 contains principles that an entity will need to apply to determine the measurement of revenue and timing of when it is recognized. The underlying principle is that an entity will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for these goods or services. PMI adopted ASU 2014-09 retrospectively to each prior period presented. PMI elected this transition method solely to reflect the change in excise tax presentation in all prior periods presented resulting from PMI's accounting policy election to exclude excise taxes collected from customers from the measurement of the transaction price, thereby presenting revenues net of excise taxes. Based on PMI's assessment, the underlying principles of the new standard, relating to the measurement of revenue and the timing of recognition, are closely aligned with PMI's current business model and practices. As a result, the adoption of ASU 2014-09 did not have a material impact on the consolidated financial position or results of operations.

The adoption of ASU 2014-09 resulted in the following changes for net revenues to reflect the net presentation for revenues, excluding excise taxes, for the years ended December 31, 2017 and 2016:

(in millions)	For the Year Ended December 31, 2017			For the Year Ended December 31, 2016		
Net Revenues:						
	As reported		Retrospective Adoption	As reported		Retrospective Adoption
	Net revenues	Excises taxes	Net revenues	Net revenues	Excises taxes	Net revenues
	$ 78,098	$ 49,350	$ 28,748	$ 74,953	$ 48,268	$ 26,685

The change in presentation of net revenues also impacts segment disclosure requirements, primarily information for significant customers and geographic areas. While there is no change in the underlying business or customers, the amounts used to calculate what is disclosed are different following the change in presentation of revenues net of excise taxes and the associated segment revenues. Prior to this change, revenues including excise taxes were the basis for determining if sales to a customer or in a foreign country met the thresholds for disclosure. On the basis of revenues including excise taxes and due to the fact that PMI is not responsible for collecting excise taxes in certain markets, no customers met the requirements for disclosure. For the effects of the change in presentation using net revenue excluding excise taxes as the basis for determining the disclosure, see Note 12. *Segment Reporting*.

On January 1, 2018, PMI adopted Financial Accounting Standard Update ASU 2016-01, "Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities" ("ASU 2016-01"), on a prospective basis. ASU 2016-01 requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. Additionally, ASU 2016-01 also changed certain disclosure requirements and other aspects of current U.S. GAAP. PMI identified certain cost investments, which are applicable to ASU 2016-01 requiring them to be measured at fair value with the changes in fair value recognized in net income. At January 1, 2018, the cumulative effect of this change resulted in an increase to investments in unconsolidated subsidiaries and equity securities, deferred income tax liability and earnings reinvested in the business of $301 million, $63 million and $238 million, respectively.

Recently issued

On February 25, 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ASU 2016-02, "Leases" ("ASU 2016-02"). ASU 2016-02 requires organizations that lease assets to recognize on the

balance sheet the assets and liabilities for the rights and obligations created by those leases. Additionally, ASU 2016-02 modifies current guidance for lessors' accounting. ASU 2016-02 is effective for interim and annual reporting periods beginning on or after January 1, 2019, with early adoption permitted. PMI has identified its lease management system and has identified and evaluated the applicable leases. In addition to the guidance in ASU 2016-02, PMI has evaluated ASU 2018-11, which was issued in July 2018 and provides an optional transitional method. As a result of this evaluation, PMI elected to use the optional transition method, which allows companies to use the effective date as the date of initial application

on transition and not adjust comparative period financial information or make the new required disclosures for periods prior to the effective date. Additionally, PMI elected to use the hindsight practical expedient, as well as the package of practical expedients permitted under the transition guidance within the new standard. Upon adoption, PMI recognized lease liabilities and the corresponding right-of-use assets (at the present value of future payments) for predominately all of its operating leases in place at that time. At January 1, 2019, PMI's adoption of ASU 2016-02 resulted in an increase of approximately $0.7 billion on its assets and liabilities in its statement of financial position. ASU 2016-02 did not have a material impact on its results of operations or cash flows.

Note 22.

Quarterly Financial Data (Unaudited):

	2018 Quarters			
(in millions, except per share data)	**1st**	**2nd**	**3rd**	**4th**
Net revenues	**$ 6,896**	**$ 7,726**	**$ 7,504**	**$ 7,499**
Gross profit	**$ 4,281**	**$ 4,982**	**$ 4,886**	**$ 4,718**
Net earnings attributable to PMI	**$ 1,556**	**$ 2,198**	**$ 2,247**	**$ 1,910**
Per share data:				
Basic EPS	**$ 1.00**	**$ 1.41**	**$ 1.44**	**$ 1.23**
Diluted EPS	**$ 1.00**	**$ 1.41**	**$ 1.44**	**$ 1.23**
Dividends declared	**$ 1.07**	**$ 1.14**	**$ 1.14**	**$ 1.14**

	2017 Quarters			
(in millions, except per share data)	**1st**	**2nd**	**3rd**	**4th**
Net revenues	$ 6,064	$ 6,917	$ 7,473	$ 8,294
Gross profit	$ 3,887	$ 4,398	$ 4,738	$ 5,293
Net earnings attributable to PMI	$ 1,590	$ 1,781	$ 1,970	$ 694
Per share data:				
Basic EPS	$ 1.02	$ 1.14	$ 1.27	$ 0.44
Diluted EPS	$ 1.02	$ 1.14	$ 1.27	$ 0.44
Dividends declared	$ 1.04	$ 1.04	$ 1.07	$ 1.07

Basic and diluted EPS are computed independently for each of the periods presented. Accordingly, the sum of the quarterly EPS amounts may not agree to the total for the year.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of
Philip Morris International Inc. and Subsidiaries:

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Philip Morris International Inc. and its subsidiaries (PMI) as of December 31, 2018 and 2017, and the related consolidated statements of earnings, comprehensive earnings, stockholders' (deficit) equity and of cash flows for each of the three years in the periods ended December 31, 2018, including the related notes (collectively referred to as the "consolidated financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of PMI as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, PMI maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Basis for Opinions

PMI's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Report of Management on Internal Control over Financial Reporting. Our responsibility is to express opinions on PMI's consolidated financial statements and on PMI's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/S/ PRICEWATERHOUSECOOPERS SA
PricewaterhouseCoopers SA

/S/ CHAD MUELLER
Chad Mueller

/S/ DR. MICHAEL ABRESCH
Dr. Michael Abresch

Lausanne, Switzerland
February 7, 2019

We have served as the Company's auditor since 2008.

Report of Management on Internal Control Over Financial Reporting

Management of Philip Morris International Inc. ("PMI") is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended. PMI's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes those written policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of PMI;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America;
- provide reasonable assurance that receipts and expenditures of PMI are being made only in accordance with the authorization of management and directors of PMI; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets that could have a material effect on the consolidated financial statements.

Internal control over financial reporting includes the controls themselves, monitoring and internal auditing practices and actions taken to correct deficiencies as identified.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of PMI's internal control over financial reporting as of December 31, 2018. Management based this assessment on criteria for effective internal control over financial reporting described in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management's assessment included an evaluation of the design of PMI's internal control over financial reporting and testing of the operational effectiveness of its internal control over financial reporting. Management reviewed the results of its assessment with the Audit Committee of our Board of Directors.

Based on this assessment, management determined that, as of December 31, 2018, PMI maintained effective internal control over financial reporting.

PricewaterhouseCoopers SA, an independent registered public accounting firm, who audited and reported on the consolidated financial statements of PMI included in this report, has audited the effectiveness of PMI's internal control over financial reporting as of December 31, 2018, as stated in their report herein.

February 7, 2019

Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.*

None.

Item 9A. *Controls and Procedures.*

PMI carried out an evaluation, with the participation of PMI's management, including PMI's Chief Executive Officer and Chief Financial Officer, of the effectiveness of PMI's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based upon that evaluation, PMI's Chief Executive Officer and Chief Financial Officer concluded that PMI's disclosure controls and procedures are effective. There have been no changes in PMI's internal control over financial reporting during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, PMI's internal control over financial reporting.

The Report of Management on Internal Control over Financial Reporting and the Report of Independent Registered Public Accounting Firm are included in Item 8.

Item 9B. *Other Information.*

None.

PART III

Except for the information relating to the executive officers set forth in Item 10 and the information relating to equity compensation plans set forth in Item 12, the information called for by Items 10-14 is hereby incorporated by reference to PMI's definitive proxy statement for use in connection with its annual meeting of stockholders to be held on May 1, 2019, that will be filed with the SEC on or about March 21, 2019 (the "proxy statement"), and, except as indicated therein, made a part hereof.

Item 10. *Directors, Executive Officers and Corporate Governance.*

Executive Officers as of February 7, 2019:

Name	Office	Age
André Calantzopoulos	Chief Executive Officer	61
Massimo Andolina	Senior Vice President, Operations	50
Drago Azinovic	President, Middle East & Africa Region and PMI Duty Free	56
Werner Barth	Senior Vice President, Commercial	54
Charles Bendotti	Senior Vice President, People and Culture	46
Frank de Rooij	Vice President, Treasury and Corporate Finance	53
Frederic de Wilde	President, European Union Region	51
Marc S. Firestone	President, External Affairs and General Counsel	59
Stacey Kennedy	President, South and Southeast Asia Region	46
Martin G. King	Chief Financial Officer	54
Michael Kunst	Senior Vice President, Commercial Transformation	50
Andreas Kurali	Vice President and Controller	53
Marco Mariotti	President, Eastern Europe Region	54
Mario Masseroli	President, Latin America & Canada Region	48
Deepak Mishra	Chief Strategy Officer	47
Jacek Olczak	Chief Operating Officer	54
Paul Riley	President, East Asia and Australia Region	53
Marian Salzman	Senior Vice President, Global Communications	60
Jaime Suarez	Chief Digital Officer	45
Michael Voegele	Chief Technology Officer	46
Jerry E. Whitson	Deputy General Counsel and Corporate Secretary	63
Miroslaw Zielinski	President, Science and Innovation	57

All of the above-mentioned officers, except Mr. Mishra, Ms. Salzman, Mr. Kunst, and Mr. Voegele, have been employed by us in various capacities during the past five years.

Before joining Philip Morris International Inc. in September 2018, Mr. Mishra was Managing Director, Portfolio Operations at Centerbridge Partners, a private equity firm from 2014, where he led commercial, operational and digital transformation in various business sectors. From 2001 to 2014, Mr. Mishra was Partner and part of the Consumer Goods, Retail and Operations leadership team of McKinsey & Co where he supported clients in their transformation projects.

Before joining Philip Morris International Inc. in April 2018, Ms. Salzman headed Havas PR North America, where she had served as Chief Executive Officer from 2011.

Before joining Philip Morris International Inc. in January 2019, Mr. Kunst was Partner at Bain & Company from 2009, most recently working with us on our transformation projects.

Before joining Philip Morris International Inc. in February 2019, Mr. Voegele had served in various senior capacities at Adidas Group from 2011, most recently, as Global CIO and part of the core leadership team at Adidas Group.

Codes of Conduct and Corporate Governance

We have adopted the Philip Morris International Code of Conduct, which complies with requirements set forth in Item 406 of Regulation S-K. This Code of Conduct applies to all of our employees, including our principal executive officer, principal financial officer, principal accounting officer or controller, and persons performing similar functions. We have also adopted a code of business conduct and ethics that applies to the members of our Board of Directors. These documents are available free of charge on our website at www.pmi.com.

In addition, we have adopted corporate governance guidelines and charters for our Audit, Finance, Compensation and Leadership Development, Product Innovation and Regulatory Affairs and Nominating and Corporate Governance committees of the Board of

Directors. All of these documents are available free of charge on our website at www.pmi.com. Any waiver granted by Philip Morris International Inc. to its principal executive officer, principal financial officer or controller or any person performing similar functions under the Code of Conduct, or certain amendments to the Code of Conduct, will be disclosed on our website at www.pmi.com.

The information on our website is not, and shall not be deemed to be, a part of this Report or incorporated into any other filings made with the SEC.

Also refer to *Board Operations and Governance—Committees of the Board*, *Election of Directors—Process for Nominating Directors* and *Election of Directors—Director Nominees* and *Section 16(a) Beneficial Ownership Reporting Compliance* sections of the proxy statement.

Item 11. *Executive Compensation.*

Refer to *Compensation Discussion and Analysis* and *Compensation of Directors* sections of the proxy statement.

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.*

The number of shares to be issued upon exercise or vesting and the number of shares remaining available for future issuance under PMI's equity compensation plans at December 31, 2018, were as follows:

	Number of Securities to be Issued upon Exercise of Outstanding Options and Vesting of RSUs and PSUs (a)	Weighted Average Exercise Price of Outstanding Options (b)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (excluding Securities reflected in column (a)) (c)
Equity compensation plans approved by stockholders	5,708,735 [1]	$ —	23,886,194

[1] Represents 3,318,795 shares of common stock that may be issued upon vesting of the restricted share units and 2,389,940 shares that may be issued upon vesting of the performance share units if maximum performance targets are achieved for each performance cycle. PMI has not granted options since the spin-off from Altria on March 28, 2008.

Also refer to *Stock Ownership Information—Ownership of Equity Securities* section of the proxy statement.

Item 13. *Certain Relationships and Related Transactions, and Director Independence.*

Refer to *Related Person Transactions and Code of Conduct* and *Election of Directors—Independence of Nominees* sections of the proxy statement.

Item 14. *Principal Accounting Fees and Services.*

Refer to *Audit Committee Matters* section of the proxy statement.

PART IV

Item 15. *Exhibits and Financial Statement Schedules.*

(a) Index to Consolidated Financial Statements and Schedules

	Page
Consolidated Statements of Earnings for the years ended December 31, 2018, 2017 and 2016	57
Consolidated Statements of Comprehensive Earnings for the years ended December 31, 2018, 2017 and 2016	58
Consolidated Balance Sheets at December 31, 2018 and 2017	59 - 60
Consolidated Statements of Cash Flows for the years ended December 31, 2018, 2017 and 2016	61 - 62
Consolidated Statements of Stockholders' (Deficit) Equity for the years ended December 31, 2018, 2017 and 2016	63
Notes to Consolidated Financial Statements	64 - 109
Report of Independent Registered Public Accounting Firm	110 - 111
Report of Management on Internal Control Over Financial Reporting	112

Schedules have been omitted either because such schedules are not required or are not applicable.

(b) The following exhibits are filed as part of this Report:

2.1	—	Distribution Agreement between Altria Group, Inc. and Philip Morris International Inc. dated January 30, 2008 (incorporated by reference to Exhibit 2.1 to the Registration Statement on Form 10 filed February 7, 2008).
3.1	—	Amended and Restated Articles of Incorporation of Philip Morris International Inc. (incorporated by reference to Exhibit 3.1 to the Registration Statement on Form 10 filed February 7, 2008).
3.2	—	Amended and Restated By-Laws of Philip Morris International Inc., effective as of March 29, 2018 (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed March 29, 2018).
4.1	—	Specimen Stock Certificate of Philip Morris International Inc. (incorporated by reference to Exhibit 4.1 to the Registration Statement on Form 10 filed February 7, 2008).
4.2	—	Indenture dated as of April 25, 2008, between Philip Morris International Inc. and HSBC Bank USA, National Association, as Trustee (incorporated by reference to Exhibit 4.3 to the Registration Statement on Form S-3, dated April 25, 2008).
4.6	—	The Registrant agrees to furnish copies of any instruments defining the rights of holders of long-term debt of the Registrant and its consolidated subsidiaries that does not exceed 10 percent of the total assets of the Registrant and its consolidated subsidiaries to the Commission upon request.
10.1	—	Employee Matters Agreement between Altria Group, Inc. and Philip Morris International Inc., dated as of March 28, 2008 (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed March 31, 2008).
10.2	—	Intellectual Property Agreement between Philip Morris International Inc. and Philip Morris USA Inc., dated as of January 1, 2008 (incorporated by reference to Exhibit 10.4 to the Registration Statement on Form 10 filed March 5, 2008).

10.3	—	Credit Agreement relating to a US$3,500,000,000 Revolving Credit Facility (including a US$800,000,000 swingline option) dated as of October 25, 2011, among Philip Morris International Inc. and the Initial Lenders named therein and Citibank International plc, as Facility Agent, and Citibank, N.A., as Swingline Agent, and Citigroup Global Markets Limited, Barclays Capital, BNP Paribas, Credit Suisse AG, Cayman Islands Branch, Deutsche Bank Securities Inc., Goldman Sachs International, HSBC Bank PLC, J.P. Morgan Limited, RBS Securities Inc. and Société Générale as Mandated Lead Arrangers and Bookrunners (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed October 26, 2011).
10.4	—	Amendment No. 1, dated as of August 31, 2012, to the Credit Agreement, dated as of October 25, 2011, among Philip Morris International Inc., the lenders named therein and Citibank International plc, as Facility Agent (incorporated by reference to Exhibit 10.6 to the Quarterly Report on Form 10-Q for the quarter ended September 30, 2012).
10.5	—	Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 15, 2013).
10.6	—	Extension Agreement, effective February 7, 2017, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders party thereto, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 30, 2017).
10.7	—	Extension Agreement, effective January 31, 2014, to Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders party thereto and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.3 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2014).
10.8	—	Credit Agreement, dated as of February 28, 2014, among Philip Morris International Inc., the lenders named therein, J.P. Morgan Europe Limited, as Facility Agent, and JPMorgan Chase Bank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed March 3, 2014).
10.9	—	Extension Agreement, effective as of February 10, 2015, to Credit Agreement dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2015).
10.10	—	Extension Agreement, effective as of February 28, 2015, to the Credit Agreement, dated as of February 28, 2014, among Philip Morris International Inc., the lenders named therein, J.P. Morgan Europe Limited, as Facility Agent, and JPMorgan Chase Bank, N.A. as Swingline Agent (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed January 29, 2015).
10.11	—	Amendment No. 1, dated as of July 20, 2015, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, The Royal Bank of Scotland plc, as resigning administrative agent, and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as successor administrative agent (incorporated by reference to Exhibit 10.52 to the Annual Report on Form 10-K for the year ended December 31, 2015).
10.12	—	Credit Agreement, dated as of October 1, 2015, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as Facility Agent, and Citibank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed October 5, 2015).
10.13	—	Amendment No. 2, effective as of February 9, 2016, to the Credit Agreement dated as of February 12, 2013, with the lenders named therein and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 28, 2016).

10.14	—	Extension Agreement, effective as of February 28, 2016, to the Credit Agreement, dated as of February 28, 2014, among Philip Morris International Inc., each lender named therein, J.P. Morgan Europe Limited, as facility agent, and JPMorgan Chase Bank, N.A., as swingline agent (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed January 28, 2016).
10.15	—	Extension Agreement, effective as of October 1, 2016, to the Credit Agreement dated as of October 1, 2015, among Philip Morris International Inc., lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as facility agent, and Citibank, N.A., as swingline agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 31, 2016).
10.16	—	Extension Agreement, effective as of October 1, 2017, to the Credit Agreement, dated as of October 1, 2015, among Philip Morris International Inc., the lenders party thereto and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as facility agent, and Citibank N.A., as swingline agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 29, 2017).
10.17	—	Extension Agreement, effective as of February 6, 2018, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2018).
10.18	—	Philip Morris International Inc. Automobile Policy (incorporated by reference to Exhibit 10.8 to the Registration Statement on Form 10 filed February 7, 2008).*
10.19	—	Philip Morris International Benefit Equalization Plan, as amended and in effect on August 6, 2012 (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended September 30, 2012).*
10.20	—	Philip Morris International Inc. 2012 Performance Incentive Plan, effective May 9, 2012 (incorporated by reference to Exhibit A to the Definitive Proxy Statement filed on March 30, 2012).*
10.21	—	Philip Morris International Inc. 2017 Performance Incentive Plan, effective May 3, 2017 (incorporated by reference to Exhibit B to the Definitive Proxy Statement filed on March 23, 2017).*
10.22	—	Pension Fund of Philip Morris in Switzerland (IC) (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2015).*
10.23	—	Summary of Supplemental Pension Plan of Philip Morris in Switzerland (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).*
10.24	—	Form of Restated Employee Grantor Trust Enrollment Agreement (Executive Trust Arrangement) (incorporated by reference to Exhibit 10.18 to the Registration Statement on Form 10 filed February 7, 2008).*
10.25	—	Form of Restated Employee Grantor Trust Enrollment Agreement (Secular Trust Arrangement) (incorporated by reference to Exhibit 10.19 to the Registration Statement on Form 10 filed February 7, 2008).*
10.26	—	Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors, effective May 3, 2017 (incorporated by reference to Exhibit C to the Definitive Proxy Statement filed on March 23, 2017).*
10.27	—	Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors (as amended and restated as of January 1, 2018) (incorporated by reference to Exhibit 10.26 to the Annual Report on Form 10-K for the year ended December 31, 2017).*
10.28	—	Philip Morris International Inc. 2008 Deferred Fee Plan for Non-Employee Directors (incorporated by reference to Exhibit 10.21 to the Registration Statement on Form 10 filed February 7, 2008).*
10.29	—	Supplemental Letter to the Employment Agreement (as amended) with André Calantzopoulos (incorporated by reference to Exhibit 10.4 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017). The Employment Agreement was previously filed as Exhibit 10.22 to the Registration Statement on Form 10 filed

February 7, 2008 and is incorporated by reference to this Exhibit 10.29. The Amendment to the Employment Agreement was previously filed as Exhibit 10.1 to the Current Report on Form 8-K/A filed June 13, 2013, and is incorporated by reference to this Exhibit 10.29.*

10.30	—	Supplemental Letter to Employment Agreement with Marc S. Firestone (incorporated by reference to Exhibit 10.5 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017). The Employment Agreement was previously filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 and is incorporated by reference to this Exhibit 10.30. The Amendment to the Employment Agreement was previously filed as Exhibit 10.25 to the Annual Report on Form 10-K for the year ended December 31, 2013, and is incorporated by reference to this Exhibit 10.30.*
10.31	—	Employment Agreement as of January 1, 2018 with Martin G. King (incorporated by reference to Exhibit 10.30 to the Annual Report on Form 10-K for the year ended December 31, 2017). The previous Employment Agreement was filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2015, and is incorporated by reference to this Exhibit 10.31. The Amendments to the previous Employment Agreement were filed as Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended September 30, 2015 and as Exhibit 10.6 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017 and are incorporated by reference to this Exhibit 10.31. *
10.32	—	Supplemental Letter to the Employment Agreement (as amended) with Jacek Olczak (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K/A filed December 12, 2017). The Employment Agreement was previously filed as Exhibit 10.4 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, and is incorporated by reference to this Exhibit 10.32. The Amendments to the Employment Agreement were previously filed as Exhibit 10.33 to the Annual Report on Form 10-K for the year ended December 31, 2013 and as Exhibit 10.7 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017 and are incorporated by reference to this Exhibit 10.32.*
10.33	—	Supplemental Letter to the Employment Agreement (as amended) with Miroslaw Zielinski (incorporated by reference to Exhibit 10.3 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2017). The Employment Agreement was previously filed as Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 and is incorporated by reference to this Exhibit 10.33. The Amendments to the Employment Agreement were previously filed as Exhibit 10.28 to the Annual Report on Form 10-K for the year ended December 31, 2013 and as Exhibit 10.8 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017, and are incorporated by reference to this Exhibit 10.33.*
10.34	—	Time Sharing Agreement between PMI Global Services Inc. and Louis C. Camilleri dated August 18, 2010 (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 19, 2010).*
10.35	—	Amendment No. 1 to the Time Sharing Agreement between PMI Global Services Inc. and Louis C. Camilleri, dated August 22, 2012 (incorporated by reference to Exhibit 10.4 to the Quarterly Report on Form 10-Q for the quarter ended September 30, 2012).*
10.36	—	Amendment No. 2 to the Time Sharing Agreement between PMI Global Services Inc. and Louis C. Camilleri, dated October 23, 2012 (incorporated by reference to Exhibit 10.27 to the Annual Report on Form 10-K for the year ended December 31, 2012).*
10.37	—	Amendment No. 3 to the Time Sharing Agreement between PMI Global Services Inc. and Louis C. Camilleri, dated December 31, 2014 (incorporated by reference to Exhibit 10.34 to the Annual Report on Form 10-K for the year ended December 31, 2014).*
10.38	—	Termination of Time Sharing Agreement between PMI Global Services Inc. and Louis C. Camilleri, dated September 12, 2018 (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended September 30, 2018 filed October 25, 2018).*
10.39	—	Time Sharing Agreement between PMI Global Services Inc. and André Calantzopoulos, dated May 8, 2013 (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2013).*
10.40	—	Amendment No. 1 to the Time Sharing Agreement between PMI Global Services Inc. and André Calantzopoulos, dated December 23, 2014 (incorporated by reference to Exhibit 10.36 to the Annual Report on Form 10-K for the year ended December 31, 2014).*
10.41	—	

		Agreement with Louis C. Camilleri (incorporated by reference to Exhibit 10.25 to the Registration Statement on Form 10 filed February 7, 2008).*
10.42	—	Amended and Restated Supplemental Management Employees' Retirement Plan (incorporated by reference to Exhibit 10.27 to the Annual Report on Form 10-K for the year ended December 31, 2008).*

10.43	—	Supplemental Equalization Plan, amended and restated as of June 29, 2015 (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).*
10.44	—	Form of Supplemental Equalization Plan Employee Grantor Trust Enrollment Agreement (Secular Trust) (incorporated by reference to Exhibit 10.31 to the Annual Report on Form 10-K for the year ended December 31, 2008).*
10.45	—	Form of Supplemental Equalization Plan Employee Grantor Trust Enrollment Agreement (Executive Trust) (incorporated by reference to Exhibit 10.32 to the Annual Report on Form 10-K for the year ended December 31, 2008).*
10.46	—	Philip Morris International Inc. Form of Indemnification Agreement with Directors and Executive Officers (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed September 18, 2009).*
10.47	—	Form of Deferred Stock Agreement (2015 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 10, 2015).*
10.48	—	Philip Morris International Inc. Tax Return Preparation Services Policy (incorporated by reference to Exhibit 10.51 to the Annual Report on Form 10-K for the year ended December 31, 2014).*
10.49	—	Form of Restricted Stock Unit Agreement (2016 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 9, 2016).*
10.50	—	Form of Performance Share Unit Agreement (2016 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 9, 2016).*
10.51	—	Form of Restricted Stock Unit Agreement (2017 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 7, 2017).*
10.52	—	Form of Performance Share Unit Agreement (2017 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 7, 2017).*
10.53	—	Form of Restricted Stock Unit Agreement (2018 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 13, 2018).*
10.54	—	Form of Performance Share Unit Agreement (2018 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 13, 2018).*
21	—	Subsidiaries of Philip Morris International Inc.
23	—	Consent of independent registered public accounting firm.
24	—	Powers of attorney.
31.1	—	Certification of the Registrant's Chief Executive Officer pursuant to Rule 13a-14(a)/ 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	—	Certification of the Registrant's Chief Financial Officer pursuant to Rule 13a-14(a)/ 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	—	Certification of the Registrant's Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	—	Certification of the Registrant's Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	—	XBRL Instance Document.
101.SCH	—	XBRL Taxonomy Extension Schema.

101.CAL	—	XBRL Taxonomy Extension Calculation Linkbase.
101.DEF	—	XBRL Taxonomy Extension Definition Linkbase.
101.LAB	—	XBRL Taxonomy Extension Label Linkbase.
101.PRE	—	XBRL Taxonomy Extension Presentation Linkbase.

* Denotes management contract or compensatory plan or arrangement in which directors or executive officers are eligible to participate.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PHILIP MORRIS INTERNATIONAL INC.

By: /s/ ANDRÉ CALANTZOPOULOS
(André Calantzopoulos
Chief Executive Officer)

Date: February 7, 2019

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated:

Signature	Title	Date
/s/ ANDRÉ CALANTZOPOULOS (André Calantzopoulos)	Chief Executive Officer	February 7, 2019
/s/ MARTIN G. KING (Martin G. King)	Chief Financial Officer	February 7, 2019
/s/ ANDREAS KURALI (Andreas Kurali)	Vice President and Controller	February 7, 2019
*LOUIS C. CAMILLERI, MASSIMO FERRAGAMO, WERNER GEISSLER, LISA A. HOOK, JENNIFER LI, JUN MAKIHARA, KALPANA MORPARIA, LUCIO A. NOTO, FREDERIK PAULSEN, ROBERT B. POLET, STEPHEN M. WOLF	Directors	
*By: /s/ ANDRÉ CALANTZOPOULOS (André Calantzopoulos Attorney-in-fact)		February 7, 2019

10-K 1 pm123117form10kwrapinclfsm.htm 10-K

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2017

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

Commission File Number: 001-33708

PHILIP MORRIS INTERNATIONAL INC.

(Exact name of registrant as specified in its charter)

Virginia	**13-3435103**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
120 Park Avenue, New York, New York	**10017**
(Address of principal executive offices)	**(Zip Code)**

917-663-2000

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, no par value	New York Stock Exchange
5.650% Notes due 2018	New York Stock Exchange
1.875% Notes due 2019	New York Stock Exchange
1.625% Notes due 2019	New York Stock Exchange
1.375% Notes due 2019	New York Stock Exchange
1.875% Notes due 2019	New York Stock Exchange
2.125% Notes due 2019	New York Stock Exchange
2.000% Notes due 2020	New York Stock Exchange
Floating Notes due 2020	New York Stock Exchange
1.750% Notes due 2020	New York Stock Exchange
4.500% Notes due 2020	New York Stock Exchange
1.875% Notes due 2021	New York Stock Exchange
1.875% Notes due 2021	New York Stock Exchange
4.125% Notes due 2021	New York Stock Exchange
2.900% Notes due 2021	New York Stock Exchange
2.625% Notes due 2022	New York Stock Exchange
2.375% Notes due 2022	New York Stock Exchange
2.500% Notes due 2022	New York Stock Exchange
2.500% Notes due 2022	New York Stock Exchange
2.625% Notes due 2023	New York Stock Exchange
2.125% Notes due 2023	New York Stock Exchange
3.600% Notes due 2023	New York Stock Exchange

Title of each class	Name of each exchange on which registered
2.875% Notes due 2024	New York Stock Exchange
0.625% Notes due 2024	New York Stock Exchange
3.250% Notes due 2024	New York Stock Exchange
2.750% Notes due 2025	New York Stock Exchange
3.375% Notes due 2025	New York Stock Exchange
2.750% Notes due 2026	New York Stock Exchange
2.875% Notes due 2026	New York Stock Exchange
3.125% Notes due 2027	New York Stock Exchange
3.125% Notes due 2028	New York Stock Exchange
2.875% Notes due 2029	New York Stock Exchange
3.125% Notes due 2033	New York Stock Exchange
2.000% Notes due 2036	New York Stock Exchange
1.875% Notes due 2037	New York Stock Exchange
6.375% Notes due 2038	New York Stock Exchange
4.375% Notes due 2041	New York Stock Exchange
4.500% Notes due 2042	New York Stock Exchange
3.875% Notes due 2042	New York Stock Exchange
4.125% Notes due 2043	New York Stock Exchange
4.875% Notes due 2043	New York Stock Exchange
4.250% Notes due 2044	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☑ No ☐

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☑

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☑ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☑ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☑

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☑ Accelerated filer ☐

Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐

Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ☐ No ☑

As of June 30, 2017, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was approximately $182 billion based on the closing sale price of the common stock as reported on the New York Stock Exchange.

Class	Outstanding at January 31, 2018
Common Stock, no par value	1,553,229,898 shares

DOCUMENTS INCORPORATED BY REFERENCE

Document	Parts Into Which Incorporated
Portions of the registrant's definitive proxy statement for use in connection with its annual meeting of shareholders to be held on May 9, 2018, to be filed with the Securities and Exchange Commission ("SEC") on or about March 29, 2018.	Part III

TABLE OF CONTENTS

		Page
PART I		
Item 1.	Business	1
Item 1A.	Risk Factors	6
Item 1B.	Unresolved Staff Comments	11
Item 2.	Properties	11
Item 3.	Legal Proceedings	12
Item 4.	Mine Safety Disclosures	12
PART II		
Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	12
Item 6.	Selected Financial Data	15
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	16
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	68
Item 8.	Financial Statements and Supplementary Data	69
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	122
Item 9A.	Controls and Procedures	122
Item 9B.	Other Information	122
PART III		
Item 10.	Directors, Executive Officers and Corporate Governance	123
Item 11.	Executive Compensation	123
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	124
Item 13.	Certain Relationships and Related Transactions, and Director Independence	124
Item 14.	Principal Accounting Fees and Services	124
PART IV		
Item 15.	Exhibits and Financial Statement Schedules	124
Signatures		130

In this report, "PMI," "we," "us" and "our" refers to Philip Morris International Inc. and its subsidiaries.

PART I

Item 1. *Business.*

(a) General Development of Business

General

Philip Morris International Inc. is a Virginia holding company incorporated in 1987. Our subsidiaries and affiliates and their licensees are engaged in the manufacture and sale of cigarettes and other nicotine-containing products in markets outside of the United States of America. We are building our future on smoke-free products that are a much better consumer choice than continuing to smoke cigarettes. Through multidisciplinary capabilities in product development, state-of-the-art facilities and scientific substantiation, we aim to ensure that our smoke-free products meet adult consumer preferences and rigorous regulatory requirements. Our vision is that these products ultimately replace cigarettes to the benefit of adult smokers, society, our company and our shareholders.

Our cigarettes are sold in more than 180 markets, and in many of these markets they hold the number one or number two market share position. We have a wide range of premium, mid-price and low-price brands. Our portfolio comprises both international and local brands and is led by *Marlboro*, the world's best-selling international cigarette, which accounted for approximately 35% of our total 2017 cigarette shipment volume. *Marlboro* is complemented in the premium-price category by *Parliament*. Our other leading international cigarette brands are *Bond Street, Chesterfield, L&M*, *Lark* and *Philip Morris.* These seven international cigarette brands contributed approximately 75% of our cigarette shipment volume in 2017. We also own a number of important local cigarette brands, such as *Dji Sam Soe*, *Sampoerna A* and *Sampoerna U* in Indonesia; *Fortune* and *Jackpot* in the Philippines; *Belmont* and *Canadian Classics* in Canada; and *Delicados* in Mexico. While there are a number of markets where local brands remain important, international brands are expanding their share in numerous markets.

In addition to our leading cigarette brand portfolio, we are engaged in the development and commercialization of smoke-free alternatives to cigarettes. Reduced-risk products ("RRPs") is the term we use to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continued smoking. We have a range of RRPs in various stages of development, scientific assessment and commercialization. Because our RRPs do not burn tobacco, they produce an aerosol that contains far lower quantities of harmful and potentially harmful constituents than found in cigarette smoke.

Our leading RRP brand, *IQOS*, is a precisely controlled device into which a specially designed heated tobacco unit is inserted and heated to generate an aerosol. We market our heated tobacco units under the brand names *HEETS*, *HEETS Marlboro* and *HEETS FROM MARLBORO*, defined collectively as *HEETS*, as well as *Marlboro HeatSticks* and *Parliament HeatSticks*. *IQOS* was first introduced in Nagoya, Japan in 2014. To date, *IQOS* is available for sale in key cities in 37 markets and nationwide in Japan.

Source of Funds — Dividends

We are a legal entity separate and distinct from our direct and indirect subsidiaries. Accordingly, our right, and thus the right of our creditors and stockholders, to participate in any distribution of the assets or earnings of any subsidiary is subject to the prior rights of creditors of such subsidiary, except to the extent that claims of our company itself as a creditor may be recognized. As a holding company, our principal sources of funds, including funds to make payment on our debt securities, are from the receipt of dividends and repayment of debt from our subsidiaries. Our principal wholly-owned and majority-owned subsidiaries currently are not limited by long-term debt or other agreements in their ability to pay cash dividends or to make other distributions with respect to their common stock.

(b) Financial Information About Segments

For all periods presented in this report, we divided our markets into four geographic regions, which constitute our segments for financial reporting purposes:

•

The European Union ("EU") Region is headquartered in Lausanne, Switzerland, and covers all the EU countries and also comprises Switzerland, Norway and Iceland, which are linked to the EU through trade agreements;

- The Eastern Europe, Middle East & Africa ("EEMA") Region is also headquartered in Lausanne and includes Eastern Europe, certain Balkan countries, Turkey, the Middle East and Africa and our international duty free business;

- The Asia Region is headquartered in Hong Kong and covers all other Asian markets as well as Australia, New Zealand and the Pacific Islands; and

- The Latin America & Canada Region is headquartered in New York and covers the South American continent, Central America, Mexico, the Caribbean and Canada.

Net revenues and operating companies income* (together with a reconciliation to operating income) attributable to each segment for each of the last three years are set forth in Item 8. *Financial Statements and Supplementary Data* of this Annual Report on Form 10-K ("Item 8") in Note 12. *Segment Reporting* to the consolidated financial statements. See Item 7 of this Annual Report on Form 10-K for a discussion of our operating results by business segment.

The relative percentages of operating companies income attributable to each reportable segment were as follows:

	2017	2016	2015
European Union	**32.0 %**	35.8 %	32.6 %
Eastern Europe, Middle East & Africa	**24.4**	27.1	31.2
Asia	**35.1**	28.7	26.3
Latin America & Canada	**8.5**	8.4	9.9
	100.0 %	100.0 %	100.0 %

* For all periods presented in this report, our management evaluated segment performance and allocated resources based on operating companies income, which we define as operating income, excluding general corporate expenses and amortization of intangibles, plus equity (income)/loss in unconsolidated subsidiaries, net. The accounting policies of the segments are the same as those described in Note 2. *Summary of Significant Accounting Policies* to the consolidated financial statements in Item 8.

We use the term net revenues to refer to our operating revenues from the sale of our products, net of sales and promotion incentives. Our net revenues and operating income are affected by various factors, including the volume of products we sell, the price of our products, changes in currency exchange rates and the mix of products we sell. Mix is a term used to refer to the proportionate value of premium-price brands to mid-price or low-price brands in any given market (product mix). Mix can also refer to the proportion of shipment volume in more profitable markets versus shipment volume in less profitable markets (geographic mix). We often collect excise taxes from our customers and then remit them to local governments, and, in those circumstances, we include excise taxes in our net revenues and excise taxes on products. Our cost of sales consists principally of tobacco leaf, non-tobacco raw materials, labor and manufacturing costs, as well as the cost of the *IQOS* devices produced by third-party electronics manufacturing service providers.

Our marketing, administration and research costs include the costs of marketing and selling our products, other costs generally not related to the manufacture of our products (including general corporate expenses), and costs incurred to develop new products. The most significant components of our marketing, administration and research costs are marketing and sales expenses and general and administrative expenses.

To provide a greater focus on both parts of our business -- combustible and reduced-risk products -- and to support our transformation toward a smoke-free future, effective January 1, 2018, we began managing our business in six reportable segments as follows:

- The European Union Region is headquartered in Lausanne, Switzerland and covers all the European Union countries and also Switzerland, Norway and Iceland, which are linked to the European Union through trade agreements;

- The Eastern Europe Region is also headquartered in Lausanne and includes Southeast Europe, Central Asia, Ukraine, Israel and Russia;

- The Middle East & Africa Region is also headquartered in Lausanne and covers the African continent, the Middle East, Turkey and our international duty free business;

- The South & Southeast Asia Region is headquartered in Hong Kong and includes Indonesia, the Philippines and other markets in this region;

- The East Asia & Australia Region is also headquartered in Hong Kong and includes Australia, Japan, South Korea, the People's Republic of China and other markets in this region, as well as Malaysia and Singapore; and

- The Latin America & Canada Region is headquartered in New York and covers the South American continent, Central America, Mexico, the Caribbean and Canada.

(c) Narrative Description of Business

Our total shipments, including cigarettes and heated tobacco units, decreased by 2.7% in 2017 to 798.2 billion units. We estimate that international industry volumes, including cigarettes and heated tobacco units, were approximately 5.2 trillion units in 2017, a 1.3% decrease over 2016. Excluding the People's Republic of China ("PRC"), we estimate that the international cigarette and heated tobacco unit volume was 2.8 trillion units in 2017, a 2.8% decrease over 2016. We estimate that our reported share of the international market (which is defined as worldwide cigarette and heated tobacco unit volume, excluding the United States of America) was approximately 15.2% in 2017, 15.5% in 2016 and 15.6% in 2015. Excluding the PRC, we estimate that our reported share of the international market was approximately 28.0%, 28.1%, and 28.6% in 2017, 2016 and 2015, respectively.

Shipments of our principal cigarette brand, *Marlboro*, decreased by 4.0% in 2017 and represented approximately 9.7% of the international cigarette market, excluding the PRC, in 2017, 9.6% in 2016 and 9.6% in 2015.

We have a market share of at least 15% and, in a number of instances, substantially more than 15%, in approximately 100 markets, including Algeria, Argentina, Australia, Austria, Belgium, Brazil, Canada, the Czech Republic, Egypt, France, Germany, Hong Kong, Indonesia, Israel, Italy, Japan, Korea, Kuwait, Mexico, the Netherlands, Norway, the Philippines, Poland, Portugal, Russia, Saudi Arabia, Spain, Singapore, Switzerland, Turkey and Ukraine.

Heated tobacco units is the term we use to refer to heated tobacco consumables, which include our *HEETS*, *HEETS Marlboro* and *HEETS FROM MARLBORO*, defined collectively as *HEETS*, as well as *Marlboro HeatSticks* and *Parliament HeatSticks.* Total shipment volume of heated tobacco units reached 36.2 billion units in 2017, up from 7.4 billion units in 2016.

References to total international market, defined as worldwide cigarette and heated tobacco unit volume excluding the United States, total industry, total market and market shares in this Form 10-K are our estimates for tax-paid products based on the latest available data from a number of internal and external sources.

Distribution & Sales

Our main types of distribution are tailored to the characteristics of each market and are often used simultaneously:

- Direct sales and distribution, where we have set up our own distribution selling directly to the retailers (including gas stations and other key accounts);
- Distribution through independent distributors that often distribute other fast-moving consumer goods and are responsible for distribution in a particular market;
- Exclusive zonified distribution, where the distributors are dedicated to us in tobacco products distribution and assigned to exclusive territories within a market;
- Distribution through national or regional wholesalers that then supply the retail trade; and
- Our own brand retail and e-commerce infrastructures for our RRP products and accessories.

Competition

We are subject to highly competitive conditions in all aspects of our business. We compete primarily on the basis of product quality, brand recognition, brand loyalty, taste, R&D, innovation, packaging, customer service, marketing, advertising and retail price and, increasingly, adult smoker willingness to convert to our RRPs. Our competitors include three large international tobacco companies and several regional and local tobacco companies and, in some instances, state-owned tobacco enterprises, principally in Algeria, Egypt, the PRC, Taiwan, Thailand and Vietnam. Industry consolidation and privatizations of state-owned enterprises have led to an overall increase in competitive pressures. Some competitors have different profit and volume objectives, and some international competitors are susceptible to changes in currency exchange rates. In the combustible product category, we predominantly sell American blend cigarette brands, such as *Marlboro*, *L&M*, *Parliament, Philip Morris* and *Chesterfield*, which are the most popular across many of our markets. In the RRP product category, we predominantly sell *IQOS* devices and heated tobacco units. We seek to compete in all profitable retail price categories, although our brand portfolio is weighted towards the premium-price category.

Procurement and Raw Materials

We purchase tobacco leaf of various types, grades and styles throughout the world, mostly through independent tobacco suppliers. We also contract directly with farmers in several countries, including Argentina, Brazil, Colombia, Ecuador, Italy, Kazakhstan, Pakistan, the Philippines and Poland. In 2017, direct sourcing from farmers represented approximately 22% of PMI's global leaf requirements. The largest supplies of tobacco leaf are sourced from Argentina, Brazil, China, India, Indonesia (mostly for domestic use in kretek products), Malawi, Mozambique, Philippines, Turkey and the United States.

We believe that there is an adequate supply of tobacco leaf in the world markets to satisfy our current and anticipated production requirements.

In addition to tobacco leaf, we purchase a wide variety of direct materials from a total of approximately 450 suppliers. In 2017, our top ten suppliers of direct materials combined represented approximately 50% of our total direct materials purchases. The three most significant direct materials that we purchase are printed paper board used in packaging, acetate tow used in filter making and fine paper used in the manufacturing of cigarettes and heated tobacco units. In addition, the adequate supply and procurement of cloves are of particular importance to our Indonesian business.

The adequate supply chain for our RRP portfolio, including the supply of electronic devices, is important to our business. We work with two electronics manufacturing service providers for the supply of our *IQOS* devices and a small number of other providers for other products in our RRP portfolio and related accessories. Although we work closely with these service providers on monitoring their production capability and financial health, the commercialization of our RRPs could be adversely affected if they are unable to meet their commitments. The production of our RRP portfolio requires various metals, and we believe that there is an adequate supply of such metals in the world markets to satisfy our current and anticipated production requirements. However, some components and materials necessary for the production of our RRPs are obtained from single or limited sources, and can be subject to industry-wide shortages and price fluctuations. Our inability to secure an adequate supply of such components and materials could negatively impact the commercialization of our RRPs.

Our *IQOS* devices are subject to product warranties, which are described in more detail in Item 8. Note 5. *Product Warranty* to our consolidated financial statements. We discuss our RRP products in more detail in Item 7. *Business Environment—Reduced Risk Products*.

Business Environment

Information called for by this Item is hereby incorporated by reference to the paragraphs in Item 7, *Business Environment*.

Other Matters

Customers

None of our business segments is dependent upon a single customer or a few customers, the loss of which would have a material adverse effect on our consolidated results of operations.

Employees

At December 31, 2017, we employed approximately 80,600 people worldwide, including full time, temporary and part-time staff. Our businesses are subject to a number of laws and regulations relating to our relationship with our employees. Generally, these laws and regulations are specific to the location of each business. In addition, in accordance with European Union requirements, we have established a European Works Council composed of management and elected members of our workforce. We believe that our relations with our employees and their representative organizations are excellent.

Executive Officers of the Registrant

The disclosure regarding executive officers is set forth under the heading “Executive Officers as of February 9, 2018” in Item 10. *Directors, Executive Officers and Corporate Governance* of this Annual Report on Form 10-K ("Item 10").

Research and Development

Our product development is based on the elimination of combustion via tobacco heating and other innovative systems for aerosol generation, which we believe is the most promising path to providing a better consumer choice for those who would otherwise continue to smoke. We recognize that no single product will appeal to all adult smokers. Therefore, we are developing a portfolio of products intended to appeal to a variety of distinct preferences. Four RRP platforms are in various stages of development and commercialization readiness. We describe each of them in more detail in Item 7, *Business Environment—Reduced-Risk Products.*

The research and development expense for our RRP portfolio accounted for 74%, 72% and 70% of our total research and development expense for the years ended December 31, 2017, 2016 and 2015, respectively.

The research and development expense for the years ended December 31, 2017, 2016 and 2015, is set forth in Item 8, Note 14. *Additional Information* to the consolidated financial statements.

Intellectual Property

Our trademarks are valuable assets, and their protection and reputation are essential to us. We own the trademark rights to all of our principal brands, including *Marlboro*, or have the right to use them in all countries where we use them.

In addition, we have more than 7,800 granted patents worldwide and approximately 7,700 pending patent applications. Our patent portfolio, as a whole, is material to our business. However, no one patent, or group of related patents, is material to us. We also have registered industrial designs, as well as unregistered proprietary trade secrets, technology, know-how, processes and other unregistered intellectual property rights.

Effective January 1, 2008, PMI entered into an Intellectual Property Agreement with Philip Morris USA Inc. ("PM USA"). The Intellectual Property Agreement governs the ownership of intellectual property between PMI and PM USA. Ownership of the jointly funded intellectual property has been allocated as follows:

- PMI owns all rights to the jointly funded intellectual property outside the United States, its territories and possessions; and
- PM USA owns all rights to the jointly funded intellectual property in the United States, its territories and possessions.

Ownership of intellectual property related to patent applications and resulting patents based solely on the jointly funded intellectual property, regardless of when filed or issued, will be exclusive to PM USA in the United States, its territories and possessions and exclusive to PMI everywhere else.

The Intellectual Property Agreement contains provisions concerning intellectual property that is independently developed by us or PM USA following March 28, 2008, the date of the spin-off from Altria Group, Inc. For ten years following that date, independently developed intellectual property may be subject to rights under certain circumstances that would allow either us or PM USA a priority position to obtain the rights to the new intellectual property from the other party, with the price and other commercial terms to be negotiated.

In the event of a dispute between us and PM USA under the Intellectual Property Agreement, we have agreed with PM USA to submit the dispute first to negotiation between our and PM USA's senior executives and then to binding arbitration.

Seasonality

Our business segments are not significantly affected by seasonality, although in certain markets cigarette consumption trends rise during the summer months due to longer daylight time and tourism.

Environmental Regulation

We are subject to international, national and local environmental laws and regulations in the countries in which we do business. We have specific programs across our business units designed to meet applicable environmental compliance requirements and reduce our carbon footprint and wastage as well as water and energy consumption. We report externally about our climate change mitigation strategy, together with associated targets and results in reducing our carbon footprint, through CDP (formerly, the Carbon Disclosure Project), the leading international non-governmental organization assessing the work of thousands of companies worldwide in the area of climate change. We have developed and implemented a consistent environmental and occupational health, safety and security management system ("EHSS"), which involves policies, standard practices and procedures at all our manufacturing centers. We also conduct regular safety assessments at our offices, warehouses and car fleet organizations. Furthermore, we have engaged an external certification body to validate the effectiveness of our EHSS management system at our manufacturing centers around the world, in accordance with internationally recognized standards for safety and environmental management. The environmental performance data we report externally is also verified by a qualified third party. Our subsidiaries expect to continue to make investments in order to drive improved performance and maintain compliance with environmental laws and regulations. We assess and report the compliance status of all our legal entities on a regular basis. Based on the management and controls we have in place and our review of climate change risks (both physical and regulatory), environmental expenditures have not had, and are not expected to have, a material adverse effect on our consolidated results of operations, capital expenditures, financial position, earnings or competitive position.

(d) Financial Information About Geographic Areas

The amounts of net revenues and long-lived assets attributable to each of our geographic segments for each of the last three fiscal years are set forth in Item 8, Note 12. *Segment Reporting* to the consolidated financial statements.

(e) Available Information

We are required to file with the SEC annual, quarterly and current reports, proxy statements and other information required by the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Investors may read and copy any document that we file, including this Annual Report on Form 10-K, at the SEC’s Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. Investors may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an Internet website at http://www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, from which investors can electronically access our SEC filings.

We make available free of charge on, or through, our website at www.pmi.com our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. Investors can access our filings with the SEC by visiting www.pmi.com.

The information on our website is not, and shall not be deemed to be, a part of this report or incorporated into any other filings we make with the SEC.

Item 1A. *Risk Factors.*

The following risk factors should be read carefully in connection with evaluating our business and the forward-looking statements contained in this Annual Report on Form 10-K. Any of the following risks could materially adversely affect our business, our operating results, our financial condition and the actual outcome of matters as to which forward-looking statements are made in this Annual Report on Form 10-K.

Forward-Looking and Cautionary Statements

We may from time to time make written or oral forward-looking statements, including statements contained in this Annual Report on Form 10-K and other filings with the SEC, in reports to stockholders and in press releases and investor webcasts. You can identify these forward-looking statements by use of words such as "strategy," "expects," "continues," "plans," "anticipates," "believes," "will," "estimates," "intends," "projects," "goals," "targets" and other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts.

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from those anticipated,

estimated or projected. Investors should bear this in mind as they consider forward-looking statements and whether to invest in or remain invested in our securities. In connection with the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995, we are identifying important factors that, individually or in the aggregate, could cause actual results and outcomes to differ materially from those contained in any forward-looking statements made by us; any such statement is qualified by reference to the following cautionary statements. We elaborate on these and other risks we face throughout this document, particularly in Item 7, *Business Environment*. You should understand that it is not possible to predict or identify all risk factors. Consequently, you should not consider the following to be a complete discussion of all potential risks or uncertainties. We do not undertake to update any forward-looking statement that we may make from time to time, except in the normal course of our public disclosure obligations.

Risks Related to Our Business and Industry

- **Consumption of tax-paid cigarettes continues to decline in many of our markets.**

This decline is due to multiple factors, including increased taxes and pricing, governmental actions, the diminishing social acceptance of smoking, continuing economic and geopolitical uncertainty, and the continuing prevalence of illicit products. These factors and their potential consequences are discussed more fully below and in Item 7, *Business Environment*.

- **Cigarettes are subject to substantial taxes. Significant increases in cigarette-related taxes have been proposed or enacted and are likely to continue to be proposed or enacted in numerous jurisdictions. These tax increases may disproportionately affect our profitability and make us less competitive versus certain of our competitors.**

Tax regimes, including excise taxes, sales taxes and import duties, can disproportionately affect the retail price of cigarettes versus other combustible tobacco products, or disproportionately affect the relative retail price of our cigarette brands versus cigarette brands manufactured by certain of our competitors. Because our portfolio is weighted toward the premium-price cigarette category, tax regimes based on sales price can place us at a competitive disadvantage in certain markets. As a result, our volume and profitability may be adversely affected in these markets.

Increases in cigarette taxes are expected to continue to have an adverse impact on our sales of cigarettes, due to resulting lower consumption levels, a shift in sales from manufactured cigarettes to other combustible tobacco products and from the premium-price to the mid-price or low-price cigarette categories, where we may be under-represented, from local sales to legal cross-border purchases of lower price products, or to illicit products such as contraband, counterfeit and "illicit whites."

- **Our business faces significant governmental action aimed at increasing regulatory requirements with the goal of reducing or preventing the use of tobacco products.**

Governmental actions, combined with the diminishing social acceptance of smoking and private actions to restrict smoking, have resulted in reduced industry volume in many of our markets, and we expect that such factors will continue to reduce consumption levels and will increase down-trading and the risk of counterfeiting, contraband, "illicit whites" and legal cross-border purchases. Significant regulatory developments will take place over the next few years in most of our markets, driven principally by the World Health Organization's Framework Convention on Tobacco Control (“FCTC”). The FCTC is the first international public health treaty on tobacco, and its objective is to establish a global agenda for tobacco regulation. The FCTC has led to increased efforts by tobacco control advocates and public health organizations to promote increasingly restrictive regulatory measures on the marketing and sale of tobacco products to adult smokers. Regulatory initiatives that have been proposed, introduced or enacted include:

- restrictions on or licensing of outlets permitted to sell cigarettes;
- the levying of substantial and increasing tax and duty charges;
- restrictions or bans on advertising, marketing and sponsorship;

- the display of larger health warnings, graphic health warnings and other labeling requirements;
- restrictions on packaging design, including the use of colors, and plain packaging;
- restrictions on packaging and cigarette formats and dimensions;
- restrictions or bans on the display of tobacco product packaging at the point of sale and restrictions or bans on cigarette vending machines;
- requirements regarding testing, disclosure and performance standards for tar, nicotine, carbon monoxide and other smoke constituents;
- disclosure, restrictions, or bans of tobacco product ingredients;
- increased restrictions on smoking in public and work places and, in some instances, in private places and outdoors;

- restrictions on the sale of novel tobacco or nicotine-containing products;
- elimination of duty free sales and duty free allowances for travelers; and
- encouraging litigation against tobacco companies.

Our operating income could be significantly affected by regulatory initiatives resulting in a significant decrease in demand for our brands, in particular requirements that lead to a commoditization of tobacco products, as well as any significant increase in the cost of complying with new regulatory requirements.

- **Litigation related to tobacco use and exposure to environmental tobacco smoke could substantially reduce our profitability and could severely impair our liquidity.**

There is litigation related to tobacco products pending in certain jurisdictions. Damages claimed in some tobacco-related litigation are significant and, in certain cases in Brazil, Canada and Nigeria, range into the billions of U.S. dollars. We anticipate that new cases will continue to be filed. The FCTC encourages litigation against tobacco product manufacturers. It is possible that our consolidated results of operations, cash flows or financial position could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. See Item 8, Note 18. *Contingencies* ("Note 18. *Contingencies*") for a discussion of pending litigation.

- **We face intense competition, and our failure to compete effectively could have a material adverse effect on our profitability and results of operations.**

We compete primarily on the basis of product quality, brand recognition, brand loyalty, taste, R&D, innovation, packaging, customer service, marketing, advertising and retail price and, increasingly, adult smoker willingness to convert to our RRPs. We are subject to highly competitive conditions in all aspects of our business. The competitive environment and our competitive position can be significantly influenced by weak economic conditions, erosion of consumer confidence, competitors' introduction of lower-price products or innovative products, higher tobacco product taxes, higher absolute prices and larger gaps between retail price categories, and product regulation that diminishes the ability to differentiate tobacco products. Competitors include three large international tobacco companies and several regional and local tobacco companies and, in some instances, state-owned tobacco enterprises, principally in Algeria, Egypt, the PRC, Taiwan, Thailand and Vietnam. Industry consolidation and privatizations of state-owned enterprises have led to an overall increase in competitive pressures. Some competitors have different profit and volume objectives, and some international competitors are susceptible to changes in different currency exchange rates.

- **Because we have operations in numerous countries, our results may be influenced by economic, regulatory and political developments, natural disasters or conflicts.**

Some of the countries in which we operate face the threat of civil unrest and can be subject to regime changes. In others, nationalization, terrorism, conflict and the threat of war may have a significant impact on the business environment. Economic, political, regulatory or other developments or natural disasters could disrupt our supply chain, manufacturing capabilities or distribution capabilities. In addition, such developments could lead to loss of property or equipment that are critical to our business in certain markets and difficulty in staffing and managing our operations, which could reduce our volumes, revenues and net earnings.

In certain markets, we are dependent on governmental approvals of various actions such as price changes, and failure to obtain such approvals could impair growth of our profitability.

In addition, despite our high ethical standards and rigorous control and compliance procedures aimed at preventing and detecting unlawful conduct, given the breadth and scope of our international operations, we may not be able to detect all potential improper or unlawful conduct by our employees and partners.

- **We may be unable to anticipate changes in consumer preferences or to respond to consumer behavior influenced by economic downturns.**

Our business is subject to changes in adult consumer preferences, which may be influenced by local economic conditions. To be successful, we must:

- promote brand equity successfully;
- anticipate and respond to new adult consumer trends;
- develop new products and markets and broaden brand portfolios;
- improve productivity;
- convince adult smokers to convert to our RRPs;
- ensure adequate production capacity to meet demand for our products; and
- be able to protect or enhance margins through price increases.

In periods of economic uncertainty, adult consumers may tend to purchase lower-price brands, and the volume of our premium-price and mid-price brands and our profitability could suffer accordingly. Such down-trading trends may be reinforced by regulation that limits branding, communication and product differentiation.

- **We lose revenues as a result of counterfeiting, contraband, cross-border purchases, "illicit whites" and non-tax-paid volume produced by local manufacturers.**

Large quantities of counterfeit cigarettes are sold in the international market. We believe that *Marlboro* is the most heavily counterfeited international cigarette brand, although we cannot quantify the revenues we lose as a result of this activity. In addition, our revenues are reduced by contraband, legal cross-border purchases, "illicit whites" and non-tax-paid volume produced by local manufacturers.

- **From time to time, we are subject to governmental investigations on a range of matters.**

Investigations include allegations of contraband shipments of cigarettes, allegations of unlawful pricing activities within certain markets, allegations of underpayment of customs duties and/or excise taxes, allegations of false and misleading usage of descriptors and allegations of unlawful advertising. We cannot predict the outcome of those investigations or whether additional investigations may be commenced, and it is possible that our business could be materially affected by an unfavorable outcome of pending or future investigations. See Note 18. *Contingencies—Other Litigation* and Item 7, *Business Environment-Governmental Investigations* for a description of certain governmental investigations to which we are subject.

- **We may be unsuccessful in our attempts to introduce reduced-risk products, and regulators may not permit the commercialization of these products or the communication of scientifically substantiated risk-reduction claims.**

Our key strategic priorities are: to develop and commercialize products that present less risk of harm to adult smokers who switch to those products versus continued smoking; and to convince current adult smokers who would otherwise continue to smoke to switch to those RRPs. For our efforts to be successful, we must: develop RRPs that such adult smokers find acceptable alternatives to smoking; conduct rigorous scientific studies to substantiate that they reduce exposure to harmful and potentially harmful constituents in smoke and, ultimately, that these products present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to them versus continued smoking; and effectively advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs, including communication of scientifically substantiated information to enable adult smokers to make better consumer choices. We might not succeed in our efforts. If we do not succeed, but others do, we may be at a competitive disadvantage. Furthermore, we cannot predict whether regulators will permit the sale and/or marketing of RRPs with scientifically substantiated risk-reduction claims. Such restrictions could limit the success of our RRPs.

- **We may be unsuccessful in our efforts to differentiate reduced-risk products and cigarettes with respect to taxation.**

To date, we have been largely successful in demonstrating to regulators that our RRPs are not cigarettes, and as such they are generally taxed either as a separate category or as other tobacco products, which typically yields more favorable tax rates than cigarettes. If we cease to be successful in these efforts, RRP unit margins may be adversely affected.

- **Our reported results could be adversely affected by unfavorable currency exchange rates, and currency devaluations could impair our competitiveness.**

We conduct our business primarily in local currency and, for purposes of financial reporting, the local currency results are translated into U.S. dollars based on average exchange rates prevailing during a reporting period. During times of a strengthening U.S. dollar, our reported net revenues and operating income will be reduced because the local currency translates into fewer U.S. dollars. During periods of local economic crises, foreign currencies may be devalued significantly against the U.S. dollar, reducing our margins. Actions to recover margins may result in lower volume and a weaker competitive position.

- **Changes in the earnings mix and changes in tax laws may result in significant variability in our effective tax rates. Our ability to receive payments from foreign subsidiaries or to repatriate royalties and dividends could be restricted by local country currency exchange controls.**

The Tax Cuts and Jobs Act that was signed into law in December 2017 constitutes a major change to the U.S. tax system. Our estimated impact of the Tax Cuts and Jobs Act is based on management's current interpretations, and our analysis is ongoing. Our final tax liability may be materially different from current estimates due to developments such as implementing regulations and clarifications. In future periods, our effective tax rate and our ability to recover deferred tax assets could be subject to additional uncertainty as a result of such developments. Furthermore, changes in the earnings mix or applicable foreign tax laws may result in significant variability in our effective tax rates. Because we are a U.S. holding company, our most significant source of funds is distributions from our non-U.S. subsidiaries. Certain countries in which we operate have adopted or could institute currency exchange controls that limit or prohibit our local subsidiaries' ability to convert local currency into U.S. dollars or to make payments outside the country. This could subject us to the risks of local currency devaluation and business disruption.

- **Our ability to grow profitability may be limited by our inability to introduce new products, enter new markets or improve our margins through higher pricing and improvements in our brand and geographic mix.**

Our profit growth may suffer if we are unable to introduce new products or enter new markets successfully, to raise prices or to improve the proportion of our sales of higher margin products and in higher margin geographies.

- **We may be unable to expand our brand portfolio through successful acquisitions or the development of strategic business relationships.**

One element of our growth strategy is to strengthen our brand portfolio and market positions through selective acquisitions and the development of strategic business relationships. Acquisition and strategic business development opportunities are limited and present risks of failing to achieve efficient and effective integration, strategic objectives and anticipated revenue improvements and cost savings. There is no assurance that we will be able to acquire attractive businesses on favorable terms, or that future acquisitions or strategic business developments will be accretive to earnings.

- **Government mandated prices, production control programs, shifts in crops driven by economic conditions and the impact of climate change may increase the cost or reduce the quality of the tobacco and other agricultural products used to manufacture our products.**

As with other agricultural commodities, the price of tobacco leaf and cloves can be influenced by imbalances in supply and demand, and crop quality can be influenced by variations in weather patterns, including those caused by climate change. Tobacco production in certain countries is subject to a variety of controls, including government mandated prices and production control programs. Changes in the patterns of demand for agricultural products could cause farmers to produce less tobacco or cloves. Any significant change in tobacco leaf and clove prices, quality and quantity could affect our profitability and our business.

- **Our ability to implement our strategy of attracting and retaining the best global talent may be impaired by the decreasing social acceptance of cigarette smoking.**

The tobacco industry competes for talent with consumer products and other companies that enjoy greater societal acceptance. As a result, we may be unable to attract and retain the best global talent.

- **The failure of our information systems to function as intended or their penetration by outside parties with the intent to corrupt them or our failure to comply with privacy laws and regulations could result in business disruption, litigation and regulatory action, and loss of revenue, assets or personal or other confidential data.**

We use information systems to help manage business processes, collect and interpret business data and communicate internally and externally with employees, suppliers, customers and others. Some of these information systems are managed by third-party service providers. We have backup systems and business continuity plans in place, and we take care to protect our systems and data from unauthorized access. Nevertheless, failure of our systems to function as intended, or penetration of our systems by outside parties intent on extracting or corrupting information or otherwise disrupting business processes, could place us at a competitive disadvantage, result in a loss of revenue, assets or personal or other sensitive data, litigation and regulatory action, cause damage to our reputation and that of our brands and result in significant remediation and other costs. Failure to protect personal data and respect the rights of data subjects could subject us to substantial fines under regulations such as the EU General Data Protection Regulation.

- **We may be required to replace third-party contract manufacturers or service providers with our own resources.**

In certain instances, we contract with third parties to manufacture some of our products or product parts or to provide other services. We may be unable to renew these agreements on satisfactory terms for numerous reasons, including government regulations. Accordingly, our costs may increase significantly if we must replace such third parties with our own resources.

Item 1B. *Unresolved Staff Comments.*

None.

Item 2. *Properties.*

At December 31, 2017, we operated and owned 46 manufacturing facilities and maintained contract manufacturing relationships with 25 third-party manufacturers across 23 markets. In addition, we work with 38 third-party operators in Indonesia who manufacture our hand-rolled cigarettes.

PMI-Owned Manufacturing Facilities

	EU [1]	EEMA	Asia	Latin America & Canada	TOTAL
Fully integrated	7	8	9	7	31
Make-pack	3	—	1	2	6
Other	3	1	3	2	9
Total	13	9	13	11	46

[1] Includes facilities that produced heated tobacco units in 2017.

In 2017, 23 of our facilities each manufactured over 10 billion cigarettes, of which eight facilities each produced over 30 billion units. Our largest factories are in Karawang and Sukorejo (Indonesia), Izmir (Turkey), Krakow (Poland), St. Petersburg and Krasnodar (Russia), Batangas and Marikina (Philippines), Berlin (Germany), Kharkiv (Ukraine), and Kutna Hora (Czech Republic). Our smallest factories are mostly in Latin America and Asia, where due to tariff and other constraints we have established small manufacturing units in individual markets. We will continue to optimize our manufacturing base, taking into consideration the evolution of trade blocks.

The plants and properties owned or leased and operated by our subsidiaries are maintained in good condition and are believed to be suitable and adequate for our present needs.

We are integrating the production of heated tobacco units into a number of our existing manufacturing facilities and progressing with our plans to build manufacturing capacity for our other RRP platforms.

Item 3. *Legal Proceedings.*

The information called for by this Item is incorporated herein by reference to Item 8. Note 18. *Contingencies*.

Item 4. *Mine Safety Disclosures.*

Not applicable.

PART II

Item 5. *Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.*

The principal stock exchange on which our common stock (no par value) is listed is the New York Stock Exchange. At January 31, 2018, there were approximately 57,300 holders of record of our common stock.

Performance Graph

The graph below compares the cumulative total shareholder return on PMI's common stock with the cumulative total return for the same period of PMI's Peer Group and the S&P 500 Index. The graph assumes the investment of $100 as of December 31, 2012, in PMI common stock (at prices quoted on the New York Stock Exchange) and each of the indices as of the market close and reinvestment of dividends on a quarterly basis.

pm12312014_chart-46538a14.jpg

Date	PMI	PMI Peer Group [1]	S&P 500 Index
December 31, 2012	$100.00	$100.00	$100.00
December 31, 2013	$108.50	$122.80	$132.40
December 31, 2014	$106.20	$132.50	$150.50
December 31, 2015	$120.40	$143.50	$152.60
December 31, 2016	$130.80	$145.60	$170.80
December 31, 2017	$156.80	$172.70	$208.10

[1] The PMI Peer Group presented in this graph is the same as that used in the prior year, except Reynolds American Inc. was removed following the completion of its acquisition by British American Tobacco p.l.c. on July 25, 2017. The PMI Peer Group was established based on a review of four characteristics: global presence; a focus on consumer products; and net revenues and a market capitalization of a similar size to those of PMI. The review also considered the primary international tobacco companies. As a result of this review, the following companies constitute the PMI Peer Group: Altria Group, Inc., Anheuser-Busch InBev SA/NV, British American Tobacco p.l.c., The Coca-Cola Company, Colgate-Palmolive Co., Diageo plc, Heineken N.V., Imperial Brands PLC, Japan Tobacco Inc., Johnson & Johnson, Kimberly-Clark Corporation, The Kraft-Heinz Company, McDonald's Corp., Mondelēz International, Inc., Nestlé S.A., PepsiCo, Inc., The Procter & Gamble Company, Roche Holding AG, and Unilever NV and PLC.

Note: Figures are rounded to the nearest $0.10.

Issuer Purchases of Equity Securities During the Quarter Ended December 31, 2017

Our share repurchase activity for each of the three months in the quarter ended December 31, 2017, was as follows:

Period	Total Number of Shares Repurchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Programs
October 1, 2017 – October 31, 2017 (1)	—	$ —	—	$ —
November 1, 2017 – November 30, 2017 (1)	—	$ —	—	$ —
December 1, 2017 – December 31, 2017 (1)	—	$ —	—	$ —
Pursuant to Publicly Announced Plans or Programs	—	$ —		
October 1, 2017 – October 31, 2017 (2)	672	$ 112.68		
November 1, 2017 – November 30, 2017 (2)	271	$ 104.73		
December 1, 2017 – December 31, 2017 (2)	497	$ 102.99		
For the Quarter Ended December 31, 2017	1,440	$ 107.84		

(1) During this reporting period, we did not have an authorized share repurchase program.

(2) Shares repurchased represent shares tendered to us by employees who vested in restricted share unit awards and used shares to pay all, or a portion of, the related taxes.

The other information called for by this Item is included in Item 8, Note 22. *Quarterly Financial Data (Unaudited)* to the consolidated financial statements.

Item 6. *Selected Financial Data*

(in millions of dollars, except per share data)

	2017	2016	2015	2014	2013
Summary of Operations:					
Net revenues	**$ 78,098**	$ 74,953	$ 73,908	$ 80,106	$ 80,029
Cost of sales	**10,432**	9,391	9,365	10,436	10,410
Excise taxes on products	**49,350**	48,268	47,114	50,339	48,812
Gross profit	**18,316**	17,294	17,429	19,331	20,807
Operating income	**11,503**	10,815	10,623	11,702	13,515
Interest expense, net	**914**	891	1,008	1,052	973
Earnings before income taxes	**10,589**	9,924	9,615	10,650	12,542
Pre-tax profit margin	**13.6 %**	13.2 %	13.0 %	13.3 %	15.7 %
Provision for income taxes	**4,307**	2,768	2,688	3,097	3,670
Net earnings	**6,341**	7,250	7,032	7,658	8,850
Net earnings attributable to noncontrolling interests	**306**	283	159	165	274
Net earnings attributable to PMI	**6,035**	6,967	6,873	7,493	8,576
Basic earnings per share	**3.88**	4.48	4.42	4.76	5.26
Diluted earnings per share	**3.88**	4.48	4.42	4.76	5.26
Dividends declared per share	**4.22**	4.12	4.04	3.88	3.58
Capital expenditures	**1,548**	1,172	960	1,153	1,200
Depreciation and amortization	**875**	743	754	889	882
Property, plant and equipment, net	**7,271**	6,064	5,721	6,071	6,755
Inventories	**8,806**	9,017	8,473	8,592	9,846
Total assets	**42,968**	36,851	33,956	35,187	38,168
Long-term debt	**31,334**	25,851	25,250	26,929	24,023
Total debt	**34,339**	29,067	28,480	29,455	27,678
Stockholders' deficit	**(10,230)**	(10,900)	(11,476)	(11,203)	(6,274)
Common dividends declared as a % of Diluted EPS	**108.8 %**	92.0 %	91.4 %	81.5 %	68.1 %

Market price per common share — high/low	**123.55-89.97**	104.20-84.46	90.27-75.27	91.63-75.28	96.73-82.86
Closing price of common share at year end	**105.65**	91.49	87.91	81.45	87.13
Price/earnings ratio at year end — Diluted	**27**	20	20	17	17
Number of common shares outstanding at year end (millions)	**1,553**	1,551	1,549	1,547	1,589
Number of employees	**80,600**	79,500	80,200	82,500	91,100

This Selected Financial Data should be read in conjunction with Item 7 and Item 8.

Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations.*

The following discussion should be read in conjunction with the other sections of this Annual Report on Form 10-K, including the consolidated financial statements and related notes contained in Item 8, and the discussion of risks and cautionary factors that may affect future results in Item 1A. *Risk Factors*.

Description of Our Company

We are a leading international tobacco company engaged in the manufacture and sale of cigarettes and other nicotine-containing products in markets outside the United States of America. We are building our future on smoke-free products that are a much better consumer choice than continuing to smoke cigarettes. Through multidisciplinary capabilities in product development, state-of-the-art facilities and scientific substantiation, we aim to ensure that our smoke-free products meet adult consumer preferences and rigorous regulatory requirements. Our vision is that these products ultimately replace cigarettes to the benefit of adult smokers, society, our company and our shareholders.

Our cigarettes are sold in more than 180 markets, and in many of these markets they hold the number one or number two market share position. We have a wide range of premium, mid-price and low-price brands. Our portfolio comprises both international and local brands. In addition to the manufacture and sale of cigarettes, we are engaged in the development and commercialization of reduced-risk products ("RRPs"). RRPs is the term we use to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continued smoking. We have a range of RRPs in various stages of development, scientific assessment and commercialization. Because our RRPs do not burn tobacco, they produce an aerosol that contains far lower quantities of harmful and potentially harmful constituents than found in cigarette smoke.

For all periods presented in this report, we managed our business in four segments:

- European Union;
- Eastern Europe, Middle East & Africa ("EEMA");
- Asia;
  and
- Latin America & Canada.

To provide a greater focus on both parts of our business -- combustible and reduced-risk products -- and to support our transformation toward a smoke-free future, effective January 1, 2018, we are managing our business in six reportable segments as follows:

- European Union - Covers all the European Union countries and also Switzerland, Norway and Iceland, which are linked to the European Union through trade agreements;
- Eastern Europe - Includes Southeast Europe, Central Asia, Ukraine, Israel and Russia;
- Middle East & Africa - Covers the African continent, the Middle East, Turkey and PMI Duty Free;
- South & Southeast Asia - Includes Indonesia, the Philippines and other markets in this region;
- East Asia & Australia - Includes Australia, Japan, South Korea, the People's Republic of China and other markets in this region, as well as Malaysia and Singapore; and
- Latin America & Canada - Covers the South American continent, Central America, Mexico, the Caribbean and Canada.

We use the term net revenues to refer to our operating revenues from the sale of our products, net of sales and promotion incentives. Our net revenues and operating income are affected by various factors, including the volume of products we sell, the price of our products, changes in currency exchange rates and the mix of products we sell. Mix is a term used to refer to the proportionate value of premium-price brands to mid-price or low-price brands in any given market (product mix). Mix can also refer to the proportion of shipment volume in more profitable markets versus shipment volume in less profitable markets (geographic mix). We often collect excise taxes from our customers and then remit them to governments, and, in those circumstances, we include the excise taxes in our net revenues and in excise taxes on products. Our cost of sales consists principally of tobacco leaf, non-tobacco raw materials, labor and manufacturing costs, as well as the cost of the *IQOS* devices produced by third-party electronics manufacturing service providers.

Our marketing, administration and research costs include the costs of marketing and selling our products, other costs generally not related to the manufacture of our products (including general corporate expenses), and costs incurred to develop new products. The most

significant components of our marketing, administration and research costs are marketing and sales expenses and general and administrative expenses.

Philip Morris International Inc. is a legal entity separate and distinct from its direct and indirect subsidiaries. Accordingly, our right, and thus the right of our creditors and stockholders, to participate in any distribution of the assets or earnings of any subsidiary is subject to the prior rights of creditors of such subsidiary, except to the extent that claims of our company itself as a creditor may be recognized. As a holding company, our principal sources of funds, including funds to make payment on our debt securities, are from the receipt of dividends and repayment of debt from our subsidiaries. Our principal wholly-owned and majority-owned subsidiaries currently are not limited by long-term debt or other agreements in their ability to pay cash dividends or to make other distributions with respect to their common stock.

Executive Summary

The following executive summary provides significant highlights from the Discussion and Analysis that follows.

Consolidated Operating Results

- **Net Revenues and Net Revenues, Excluding Excise Taxes on Products –** The changes in our net revenues, and net revenues, excluding excise taxes, for the year ended December 31, 2017, from the comparable 2016 amounts, were as follows:

	For the Years Ended December 31,		Variance		Variance due to		
(in millions)	**2017**	**2016**	**$**	**%**	**Currency**	**Volume/ Mix**	**Pricing**
Net revenues	**$ 78,098**	$ 74,953	$ 3,145	4.2 %	$ (2,355)	$ (439)	$ 5,939
Excise taxes on products	**(49,350)**	(48,268)	(1,082)	(2.2%)	1,918	1,553	(4,553)
Net revenues, excluding excise taxes on products	**$ 28,748**	$ 26,685	$ 2,063	7.7 %	$ (437)	$ 1,114	$ 1,386

Net revenues include $3.8 billion in 2017 and $739 million in 2016 related to the sale of RRPs, mainly driven by Japan. These net revenue amounts include excise taxes billed to customers, where we collect and remit the excise tax. Excluding excise taxes, net revenues for RRPs were $3.6 billion in 2017 and $733 million in 2016. In some jurisdictions, including Japan, we are not responsible for collecting excise taxes.

- **Diluted Earnings Per Share –** The changes in our reported diluted earnings per share ("diluted EPS") for the year ended December 31, 2017, from the comparable 2016 amounts, were as follows:

	Diluted EPS	% Growth
For the year ended December 31, 2016	**$ 4.48**	
2016 Asset impairment and exit costs	—	
2016 Tax items	—	
Subtotal of 2016 items	—	
2017 Asset impairment and exit costs	—	
2017 Tax items	**(0.84)**	
Subtotal of 2017 items	**(0.84)**	
Currency	**(0.21)**	
Interest	**0.01**	

Change in tax rate		**(0.03)**	
Operations		**0.47**	
For the year ended December 31, 2017	**$**	**3.88**	**(13.4)%**

Income Taxes – Our effective income tax rate for 2017 increased by 12.8 percentage points to 40.7%. The 2017 tax items that decreased our diluted EPS by $0.84 per share in the table above were primarily due to the impact of the Tax Cuts and Jobs Act, which was signed into law in December 2017.

The principal elements of the Tax Cuts and Jobs Act relevant to our consolidated financial statements for the year ended December 31, 2017, were:

- A reduction of the U.S. federal corporate tax rate from 35% to 21%; and
- The requirement to pay a one-time transition tax on accumulated foreign earnings, including 2017 earnings ("transition tax").

In connection with these elements of the Tax Cuts and Jobs Act, we recognized a provisional expense of $1.6 billion, which was included as a component of income tax expense as follows:

- A provisional charge of $1.4 billion, which represents the transition tax of $2.2 billion, net of a reversal of $0.7 billion of previously recorded deferred tax liabilities on part of the accumulated foreign earnings, and other items of $0.1 billion.

- Re-measurement of U.S. deferred tax assets and liabilities using a rate of 21%, which, under the Tax Cuts and Jobs Act, is expected to be in place when such deferred assets and liabilities reverse in the future. In connection with this re-measurement, we recorded a provisional charge of $0.2 billion.

While the impacts of the Tax Cuts and Jobs Act reduced net earnings by $1.6 billion, there was no net impact on operating cash flows for the year, as the changes in deferred taxes and income taxes payable offset the net earnings impact. At December 31, 2017, we recorded an income tax payable of $1.7 billion representing the transition tax of $2.2 billion, partially offset by foreign tax credits related to foreign withholding taxes previously paid of $0.5 billion. The income tax payable is due over an 8-year period beginning in 2018. For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements.

The change in the effective tax rate that decreased our diluted EPS by $0.03 per share in the table above was primarily due to earnings mix by taxing jurisdiction.

Currency – The unfavorable currency impact during 2017 results from the fluctuations of the U.S. dollar, especially against the Brazilian real, Egyptian pound, Euro, Japanese yen and Turkish lira, partially offset by the Russian ruble. This unfavorable currency movement has impacted our profitability across our primary revenue markets and local currency cost bases.

Interest – The favorable impact of interest was due primarily to higher interest income, partly offset by higher average debt levels.

Operations – The increase in diluted EPS of $0.47 from our operations in the table above was due primarily to the following segments:

- Asia: Favorable volume/mix, higher pricing and lower manufacturing costs, partially offset by higher marketing, administration and research costs; and

- Latin America & Canada: Higher pricing, partially offset by unfavorable volume/mix;

partially offset by

- EEMA: Unfavorable volume/mix and higher marketing, administration and research costs, partially offset by higher pricing; and

- European Union: Unfavorable volume/mix and higher marketing, administration and research costs, partially offset by higher pricing.

For further details, see the *Consolidated Operating Results* and *Operating Results by Business Segment* sections of the following *Discussion and Analysis*.

2018 Forecasted Results – On February 8, 2018, we announced our forecast for 2018 full-year reported diluted EPS to be in a range of $5.20 to $5.35, representing a projected increase of approximately 34% to 38% at prevailing exchange rates, versus $3.88 in 2017. Excluding a favorable currency impact, at then-prevailing exchange rates, of approximately $0.16 per share for the full-year 2018, the forecast range represents a projected increase of approximately 7% to 10% versus adjusted diluted earnings per share of $4.72 in 2017.

This forecast assumes:

- Net revenue growth, excluding excise taxes, of over 8.0%, excluding currency;
- Operating cash flow of over $9.0 billion;
- Capital expenditures of approximately $1.7 billion; and
- No share repurchases.

Following the enactment of the Tax Cuts and Jobs Act, our 2018 full-year diluted earnings per share forecast -- based on the current interpretation of the legislation -- assumes a full-year effective tax rate of approximately 28%, subject to future regulatory developments and earnings mix by taxing jurisdiction. The difference between the 21% statutory rate under the new law and our effective rate reflects the fact that we operate in markets outside the United States and is driven by three main factors: foreign tax rate differences, non-deductibility of interest expense and a partial disallowance of foreign tax credits related to the application of the rules for global intangible low-taxed income.

We calculated 2017 adjusted diluted EPS as reported diluted EPS of $3.88, plus the $0.84 per share charge related to tax items. During 2017, we did not have an EPS impact related to asset impairment and exit costs.

Adjusted diluted EPS is not a measure under accounting principles generally accepted in the United States of America ("U.S. GAAP"). We define adjusted diluted EPS as reported diluted EPS adjusted for asset impairment and exit costs, tax items and unusual items. We believe it is appropriate to disclose this measure as it represents core earnings, improves comparability and helps investors analyze business performance and trends. Adjusted diluted EPS should be considered neither in isolation nor as a substitute for reported diluted EPS prepared in accordance with U.S. GAAP.

This 2018 guidance excludes the impact of any future acquisitions, unanticipated asset impairment and exit cost charges, future changes in currency exchange rates, further developments related to the Tax Cuts and Jobs Act, and any unusual events. The factors described in Item 1A. *Risk Factors* represent continuing risks to these projections.

Discussion and Analysis

Critical Accounting Estimates

Item 8, Note 2. *Summary of Significant Accounting Policies* to our consolidated financial statements includes a summary of the significant accounting policies and methods used in the preparation of our consolidated financial statements. In most instances, we must use a particular accounting policy or method because it is the only one that is permitted under U.S. GAAP.

The preparation of financial statements requires that we use estimates and assumptions that affect the reported amounts of our assets, liabilities, net revenues and expenses, as well as our disclosure of contingencies. If actual amounts differ from previous estimates, we include the revisions in our consolidated results of operations in the period during which we know the actual amounts. Historically, aggregate differences, if any, between our estimates and actual amounts in any year have not had a significant impact on our consolidated financial statements.

The selection and disclosure of our critical accounting estimates have been discussed with our Audit Committee. The following is a discussion of the more significant assumptions, estimates, accounting policies and methods used in the preparation of our consolidated financial statements:

Revenue Recognition - We recognize revenue when persuasive evidence of an arrangement exists, delivery of product has occurred, the sales price is fixed or determinable and collectability is reasonably assured. For our company, this means that revenue is recognized when title and risk of loss is transferred to our customers. Title transfers to our customers upon shipment or upon receipt at the customer's location as determined by the sales terms for each transaction. The company estimates the cost of sales returns based on historical experience, and these estimates are immaterial. Estimated costs associated with warranty programs for *IQOS* devices are generally

provided for in cost of sales in the period the related revenues are recognized, based on a number of factors including historical experience, product failure rates and warranty policies.

Goodwill and Non-Amortizable Intangible Assets Valuation - We test goodwill and non-amortizable intangible assets for impairment annually or more frequently if events occur that would warrant such review. During the second quarter of 2016, we changed the date of

our annual goodwill impairment test from the first quarter to the second quarter. The change was made to more closely align the impairment testing date with our long-range planning and forecasting process. We had determined that this change in accounting principle was preferable under the circumstances and believe that the change in the annual impairment testing date did not delay, accelerate, or avoid an impairment charge. While the company has the option to perform a qualitative assessment for both goodwill and non-amortizable intangible assets to determine if it is more likely than not that an impairment exists, the company elects to perform the quantitative assessment for our annual impairment analysis. The impairment analysis involves comparing the fair value of each reporting unit or non-amortizable intangible asset to the carrying value. If the carrying value exceeds the fair value, goodwill or a non-amortizable intangible asset is considered impaired. To determine the fair value of goodwill, we primarily use a discounted cash flow model, supported by the market approach using earnings multiples of comparable global and local companies within the tobacco industry. At December 31, 2017, the carrying value of our goodwill was $7.7 billion, which is related to ten reporting units, each of which consists of a group of markets with similar economic characteristics. The estimated fair value of each of our ten reporting units exceeded the carrying value as of December 31, 2017. To determine the fair value of non-amortizable intangible assets, we primarily use a discounted cash flow model applying the relief-from-royalty method. We concluded that the fair value of our non-amortizable intangible assets exceeded the carrying value. These discounted cash flow models include management assumptions relevant for forecasting operating cash flows, which are subject to changes in business conditions, such as volumes and prices, costs to produce, discount rates and estimated capital needs. Management considers historical experience and all available information at the time the fair values are estimated, and we believe these assumptions are consistent with the assumptions a hypothetical marketplace participant would use. Since the March 28, 2008, spin-off from Altria Group, Inc., we have not recorded a charge to earnings for an impairment of goodwill or non-amortizable intangible assets.

Marketing and Advertising Costs - We incur certain costs to support our products through programs that include advertising, marketing, consumer engagement and trade promotions. The costs of our advertising and marketing programs are expensed in accordance with U.S. GAAP. Recognition of the cost related to our consumer engagement and trade promotion programs contain uncertainties due to the judgment required in estimating the potential performance and compliance for each program. For volume-based incentives provided to customers, management continually assesses and estimates, by customer, the likelihood of the customer's achieving the specified targets, and records the reduction of revenue as the sales are made. For other trade promotions, management relies on estimated utilization rates that have been developed from historical experience. Changes in the assumptions used in estimating the cost of any individual marketing program would not result in a material change in our financial position, results of operations or operating cash flows.

Employee Benefit Plans - As discussed in Item 8, Note 13. *Benefit Plans* to our consolidated financial statements, we provide a range of benefits to our employees and retired employees, including pensions, postretirement health care and postemployment benefits (primarily severance). We record annual amounts relating to these plans based on calculations specified by U.S. GAAP. These calculations include various actuarial assumptions, such as discount rates, assumed rates of return on plan assets, compensation increases, mortality, turnover rates and health care cost trend rates. We review actuarial assumptions on an annual basis and make modifications to the assumptions based on current rates and trends when it is deemed appropriate to do so. As permitted by U.S. GAAP, any effect of the modifications is generally amortized over future periods. We believe that the assumptions utilized in calculating our obligations under these plans are reasonable based upon our historical experience and advice from our actuaries.

Weighted-average discount rate assumptions for pensions and postretirement plans are as follows:

	2017	2016
Pension plans	**1.51%**	1.52%
Postretirement plans	**3.79%**	3.68%

We anticipate that assumption changes will decrease 2018 pre-tax pension and postretirement expense to approximately $164 million as compared with approximately $199 million in 2017, excluding amounts related to early retirement programs. The anticipated decrease is primarily due to higher expected return on assets of $21 million, coupled with lower amortization out of other comprehensive earnings for prior service cost of $12 million and unrecognized actuarial gains/losses of $10 million, partially offset by other movements of $8 million.

Weighted-average expected rate of return and discount rate assumptions have a significant effect on the amount of expense reported for the employee benefit plans. A fifty-basis-point decrease in our discount rate would increase our 2018 pension and postretirement expense by approximately $38 million, and a fifty-basis-point increase in our

discount rate would decrease our 2018 pension and postretirement expense by approximately $54 million. Similarly, a fifty-basis-point decrease (increase) in the expected return on plan assets would increase (decrease) our 2018 pension expense by approximately $45 million. See Item 8, Note 13. *Benefit Plans* to our consolidated financial statements for a sensitivity discussion of the assumed health care cost trend rates.

Income Taxes - Income tax provisions for jurisdictions outside the United States, as well as state and local income tax provisions, are determined on a separate company basis, and the related assets and liabilities are recorded in our consolidated balance sheets.

The extent of our operations involves dealing with uncertainties and judgments in the application of complex tax regulations in a multitude of jurisdictions. The final taxes paid are dependent upon many factors, including negotiations with taxing authorities in various jurisdictions and resolution of disputes arising from federal, state, and international tax audits. In accordance with the authoritative guidance for income taxes, we evaluate potential tax exposures and record tax liabilities for anticipated tax audit issues based on our estimate of whether, and the extent to which, additional taxes will be due. We adjust these reserves in light of changing facts and circumstances; however, due to the complexity of some of these uncertainties, the ultimate resolution may result in a payment that is materially different from our current estimate of the tax liabilities. If our estimate of tax liabilities proves to be less than the ultimate assessment, an additional charge to expense would result. If payment of these amounts ultimately proves to be less than the recorded amounts, the reversal of the liabilities would result in tax benefits being recognized in the period when we determine the liabilities are no longer necessary.

The effective tax rates used for interim reporting are based on our full-year geographic earnings mix projections. Changes in currency exchange rates or earnings mix by taxing jurisdiction could have an impact on the effective tax rates. Significant judgment is required in determining income tax provisions and in evaluating tax positions.

For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements.

Hedging - As discussed below in "Market Risk," we use derivative financial instruments principally to reduce exposures to market risks resulting from fluctuations in foreign currency exchange and interest rates by creating offsetting exposures. For derivatives to which we have elected to apply hedge accounting, gains and losses on these derivatives are initially deferred in accumulated other comprehensive losses on the consolidated balance sheet and recognized in the consolidated statement of earnings in the periods when the related hedged transactions are also recognized in operating results. If we had elected not to use the hedge accounting provisions, gains (losses) deferred in stockholders' (deficit) equity would have been recorded in our net earnings for these derivatives.

Contingencies - As discussed in Item 8, Note 18. *Contingencies* to our consolidated financial statements, legal proceedings covering a wide range of matters are pending or threatened against us, and/or our subsidiaries, and/or our indemnitees in various jurisdictions. We and our subsidiaries record provisions in the consolidated financial statements for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. The variability in pleadings in multiple jurisdictions, together with the actual experience of management in litigating claims, demonstrate that the monetary relief that may be specified in a lawsuit bears little relevance to the ultimate outcome. Much of the pending tobacco-related litigation is in its early stages, and litigation is subject to uncertainty. At the present time, while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available to it: (i) management has not concluded that it is probable that a loss has been incurred in any of the pending tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any. Legal defense costs are expensed as incurred.

Consolidated Operating Results

Our net revenues, excise taxes on products and operating companies income by segment were as follows:

(in millions)	2017	2016	2015
Net Revenues			
European Union	**$ 27,580**	$ 27,129	$ 26,563
Eastern Europe, Middle East & Africa	**18,045**	18,286	18,328
Asia	**22,635**	20,531	19,469
Latin America & Canada	**9,838**	9,007	9,548
Net Revenues	**$ 78,098**	$ 74,953	$ 73,908

(in millions)	2017	2016	2015
Excise Taxes on Products			
European Union	**$ 19,262**	$ 18,967	$ 18,495
Eastern Europe, Middle East & Africa	**11,346**	11,286	10,964
Asia	**11,845**	11,850	11,266
Latin America & Canada	**6,897**	6,165	6,389
Excise Taxes on Products	**$ 49,350**	$ 48,268	$ 47,114

(in millions)	2017	2016	2015
Operating Income			
Operating companies income:			
European Union	**$ 3,775**	$ 3,994	$ 3,576
Eastern Europe, Middle East & Africa	**2,888**	3,016	3,425
Asia	**4,149**	3,196	2,886
Latin America & Canada	**1,002**	938	1,085
Amortization of intangibles	**(88)**	(74)	(82)
General corporate expenses	**(164)**	(161)	(162)
Less:			
Equity (income)/loss in unconsolidated subsidiaries, net	**(59)**	(94)	(105)
Operating Income	**$ 11,503**	$ 10,815	$ 10,623

As discussed in Item 8, Note 12. *Segment Reporting* to our consolidated financial statements, we evaluate segment performance and allocate resources based on operating companies income, which we define as operating income, excluding general corporate expenses and amortization of intangibles, plus equity (income)/loss in unconsolidated subsidiaries, net. We believe it is appropriate to disclose this measure to help investors analyze the business performance and trends of our various business segments.

Our shipment volume by segment for cigarettes and heated tobacco units was as follows:

PMI Shipment Volume (Million Units)

	2017	2016	2015
Cigarettes			
European Union	**187,293**	193,586	194,589
Eastern Europe, Middle East & Africa	**256,157**	271,393	279,411
Asia	**234,253**	260,029	281,350
Latin America & Canada	**84,223**	87,938	91,920
Total Cigarettes	**761,926**	812,946	847,270
Heated Tobacco Units			
European Union	**1,889**	224	24
Eastern Europe, Middle East & Africa	**1,581**	100	2
Asia	**32,729**	7,070	370
Latin America & Canada	**27**	—	—
Total Heated Tobacco Units	**36,226**	7,394	396
Cigarettes and Heated Tobacco Units			
European Union	**189,182**	193,810	194,613
Eastern Europe, Middle East & Africa	**257,738**	271,493	279,413
Asia	**266,982**	267,099	281,720
Latin America & Canada	**84,250**	87,938	91,920
Total Cigarettes and Heated Tobacco Units	**798,152**	820,340	847,666

Heated tobacco units is the term we use to refer to heated tobacco consumables, which include our *HEETS*, *HEETS Marlboro* and *HEETS FROM MARLBORO*, defined collectively as *HEETS*, as well as *Marlboro HeatSticks* and *Parliament HeatSticks.*

Our net revenues by product category, which include excise taxes billed to customers, were as follows:

PMI Net Revenues by Product Category

(in millions)	2017	2016	2015
Combustible Products			
European Union	**$ 27,261**	$ 27,067	$ 26,533
Eastern Europe, Middle East & Africa	**17,886**	18,276	18,328
Asia	**19,325**	19,865	19,434
Latin America & Canada	**9,833**	9,006	9,547
Total Combustible Products	**$ 74,305**	$ 74,214	$ 73,842
Reduced-Risk Products			
European Union	**$ 320**	$ 62	$ 30
Eastern Europe, Middle East & Africa	**158**	9	—
Asia	**3,310**	666	35
Latin America & Canada	**5**	2	1
Total Reduced-Risk Products	**$ 3,793**	$ 739	$ 66
Total PMI Net Revenues	**$ 78,098**	$ 74,953	$ 73,908

Note: Sum of product categories or Regions might not foot to total PMI due to rounding.

Net revenues related to combustible products refer to the operating revenues generated from the sale of these products, net of sales and promotion incentives. These net revenue amounts consist of the sale of our cigarettes and other tobacco products combined. Other tobacco products primarily include roll-your-own and make-your-own cigarettes, pipe tobacco, cigars and cigarillos and do not include reduced-risk products.

Net revenues related to reduced-risk products refer to the operating revenues generated from the sale of these products, net of sales and promotion incentives. These net revenue amounts consist of the sale of our heated tobacco units, *IQOS* devices and related accessories, and other nicotine-containing products, which primarily include our e-vapor products.

References to total international market, defined as worldwide cigarette and heated tobacco unit volume excluding the United States, total industry, total market and market shares throughout this *"Discussion and Analysis"* are our estimates for tax-paid products based on the latest available data from a number of internal and external sources.

2017 compared with 2016

The following discussion compares our consolidated operating results for the year ended December 31, 2017, with the year ended December 31, 2016.

Estimated international cigarette and heated tobacco unit volume, excluding China and the United States, of 2.8 trillion was down by 2.8%.

Our total shipment volume decreased by 2.7%, principally due to:

- European Union, notably reflecting lower cigarette shipment volume in Greece, Italy and Spain, partly offset by higher heated tobacco unit shipment volume;

- EEMA, notably reflecting lower cigarette shipment volume in Russia, Saudi Arabia - where our cigarette shipment volume declined by 35.8%, impacted by the new excise tax implemented in June 2017 that resulted in the doubling of retail prices - and Ukraine; partly offset by higher cigarette shipment volume in North Africa, notably Algeria, and higher heated tobacco unit shipment volume;

- Asia, notably reflecting lower cigarette shipment volume in Indonesia, Japan, Korea, Pakistan - impacted by excise tax-driven price increases and an increase in the prevalence of illicit trade - and the Philippines; fully offset by higher heated tobacco unit shipment volume, mainly in Japan and Korea; and

- Latin America & Canada, notably reflecting lower cigarette shipment volume in Argentina, Brazil, Canada, Colombia and Mexico.

Excluding the favorable net impact of estimated cigarette and heated tobacco unit inventory movements of approximately 3.3 billion units, our total shipment volume decreased by 3.1%. The favorable inventory movements were driven primarily by approximately 8.5 billion units net in Japan reflecting: the increasing demand for *HeatSticks*, anticipated to further increase in the first quarter of 2018 following a planned lifting of the restriction on *IQOS* device sales; the establishment of appropriate distributor inventory levels of heated tobacco units, given the current high dependence on a single manufacturing center; and the transition from air freight to sea freight of heated tobacco units, largely completed in the fourth quarter of 2017. These favorable inventory movements were partly offset by a reduction of combustible product inventory levels, mainly in: the European Union, notably Italy and Spain; EEMA, notably North Africa, Russia and Saudi Arabia.

Our cigarette shipment volume by brand and heated tobacco unit shipment volume are shown in the table below:

PMI Shipment Volume by Brand (Million Units)

	Full-Year		
	2017	**2016**	**Change**
Cigarettes			
Marlboro	**270,366**	281,720	(4.0%)
L&M	**90,817**	96,770	(6.2%)
Chesterfield	**55,075**	46,291	19.0 %
Philip Morris	**48,522**	35,914	35.1 %
Parliament	**43,965**	45,671	(3.7%)
Bond Street	**37,987**	44,567	(14.8%)
Lark	**24,373**	27,571	(11.6%)
Others	**190,821**	234,442	(18.6%)
Total Cigarettes	**761,926**	812,946	(6.3%)
Heated Tobacco Units	**36,226**	7,394	+100.0%
Total Cigarettes and Heated Tobacco Units	**798,152**	820,340	(2.7%)

Cigarette shipment volume of *Marlboro* decreased in: the European Union, mainly due to Greece, Italy and Spain; EEMA, predominantly due to Saudi Arabia, reflecting the impact of the new excise tax implemented in June 2017 that resulted in the doubling of the retail price of *Marlboro* from SAR 12 to SAR 24 per pack, partly offset by North Africa, notably Algeria and Egypt, and Turkey; Asia, mainly due to Japan and Korea, principally reflecting out-switching to heated tobacco products, partly offset by Indonesia and the Philippines; and Latin America & Canada, mainly due to Argentina and Brazil.

Cigarette shipment volume of the following brands decreased: *L&M*, mainly due to Russia, Saudi Arabia and Turkey, partly offset by Algeria, Argentina, Colombia and Kazakhstan; *Parliament*, mainly due to Japan, Russia and Saudi Arabia, partly offset by Kazakhstan; *Bond Street*, mainly due to Kazakhstan, Russia and Ukraine; *Lark*, principally due to Japan; and "Others," mainly due to low-price brands in Indonesia, Pakistan, the Philippines, Russia and Ukraine.

Cigarette shipment volume of the following brands increased: *Chesterfield,* notably driven by Argentina, Brazil, Colombia, Saudi Arabia, Turkey and Venezuela, partly offset by Italy and Russia; and *Philip Morris*, mainly driven by Russia and Ukraine, notably reflecting successful portfolio consolidation of local, low-price brands in "Others," partly offset by Argentina and Italy.

Our net revenues and excise taxes on products were as follows:

	For the Years Ended December 31,		Variance	
(in millions)	**2017**	**2016**	**$**	**%**
Net revenues	**$ 78,098**	$ 74,953	$ 3,145	4.2%
Excise taxes on products	**49,350**	48,268	1,082	2.2%
Net revenues, excluding excise taxes on products	**$ 28,748**	$ 26,685	$ 2,063	7.7%

Net revenues, which include excise taxes billed to customers, increased by $3.1 billion. Excluding excise taxes, net revenues increased by $2.1 billion, due to:

- price increases ($1.4 billion) and
- favorable volume/mix ($1.1 billion), partly offset by
- unfavorable currency ($437 million).

The unfavorable currency was due primarily to the Argentine peso, Egyptian pound, Japanese yen, Philippine peso and Turkish lira, partially offset by the Russian ruble.

Net revenues include $3.8 billion in 2017 and $739 million in 2016 related to the sale of RRPs, mainly driven by Japan. These net revenue amounts include excise taxes billed to customers. Excluding excise taxes, net revenues for RRPs were $3.6 billion in 2017 and $733 million in 2016. In some jurisdictions, including Japan, we are not responsible for collecting excise taxes. In 2017, approximately $0.9 billion of our $3.6 billion in RRP net revenues, excluding excise taxes, were from *IQOS* devices and accessories.

Excise taxes on products increased by $1.1 billion, due to:

- higher excise taxes resulting from changes in retail prices and tax rates ($4.6 billion), partially offset by
- favorable currency ($1.9 billion) and
- lower excise taxes resulting from volume/mix ($1.6 billion).

Our cost of sales; marketing, administration and research costs; and operating income were as follows:

	For the Years Ended December 31,		Variance	
(in millions)	**2017**	**2016**	**$**	**%**
Cost of sales	**$ 10,432**	$ 9,391	$ 1,041	11.1%
Marketing, administration and research costs	**6,725**	6,405	320	5.0%
Operating income	**11,503**	10,815	688	6.4%

Cost of sales increased by $1.0 billion, due to:

- higher cost of sales resulting from volume/mix ($1.1 billion), partly offset by
- lower manufacturing costs ($36 million) and
- favorable currency ($30 million).

Marketing, administration and research costs increased by $320 million, due to:

- higher expenses ($570 million, largely reflecting increased investment behind reduced-risk products, predominately in the European Union and Asia), partly offset by
- favorable currency ($250 million).

Operating income increased by $688 million, due primarily to:

- price increases ($1.4 billion), partly offset by
- higher marketing, administration and research costs ($570 million) and
- unfavorable currency ($157 million).

Interest expense, net, of $914 million increased by $23 million, due primarily to unfavorably currency and higher average debt levels, partly offset by higher interest income.

Our effective tax rate increased by 12.8 percentage points to 40.7%. The 2017 effective tax rate was unfavorably impacted by $1.6 billion due to the Tax Cuts and Jobs Act. For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements. We are continuing to evaluate the impact that the Tax Cuts and Jobs Act will have on our tax liability. Based upon our current interpretation of the Tax Cuts and Jobs Act, we estimate that our 2018 effective tax rate will be approximately 28%, subject to future regulatory developments and earnings mix by taxing jurisdiction.

We are regularly examined by tax authorities around the world, and we are currently under examination in a number of jurisdictions. It is reasonably possible that within the next 12 months certain tax examinations will close, which could result in a change in unrecognized tax benefits along with related interest and penalties. An estimate of any possible change cannot be made at this time.

Net earnings attributable to PMI of $6.0 billion decreased by $932 million (13.4%). This decrease was due primarily to a higher effective tax rate as discussed above, partly offset by higher operating income. Diluted and basic EPS of $3.88 decreased by 13.4%. Excluding

an unfavorable tax impact of $0.84 primarily related to the implementation of the Tax Cuts and Jobs Act and an unfavorable currency impact of $0.21, diluted EPS increased by 10.0%.

2016 compared with 2015

The following discussion compares our consolidated operating results for the year ended December 31, 2016, with the year ended December 31, 2015.

Our cigarette shipment volume decreased by 4.1%, or by 4.7% excluding net estimated inventory movements, due to:

- European Union, principally Italy, Germany and Greece, partly offset by Poland and Spain;
- EEMA, mainly North Africa, primarily Algeria, and Russia, partly offset by Saudi Arabia and Ukraine;
- Asia, principally Indonesia, Pakistan, the Philippines and Thailand, partly offset by Korea; and
- Latin America & Canada, predominantly Argentina, partly offset by Mexico.

Our cigarette market share increased in a number of markets, including Brazil, Canada, Colombia, the Czech Republic, France, Mexico, the Netherlands, Norway, Poland, Saudi Arabia, Spain, Switzerland, Turkey and the United Arab Emirates.

Our cigarette shipment volume by brand is shown in the table below:

PMI Cigarette Shipment Volume by Brand (Million Units)

	Full-Year		
	2016	2015	Change
Marlboro	281,720	285,583	(1.4%)
L&M	96,770	97,884	(1.1%)
Chesterfield	46,291	41,397	11.8 %
Parliament	45,671	44,879	1.8 %
Bond Street	44,567	43,608	2.2 %
Philip Morris	35,914	35,815	0.3 %
Lark	27,571	28,828	(4.4%)
Others	234,442	269,276	(12.9%)
Total PMI	812,946	847,270	(4.1%)

Cigarette shipment volume of *Marlboro* decreased, driven by Algeria, Argentina, Egypt and Vietnam, as well as in-switching to heated tobacco units, partly offset by Korea, Mexico, the Philippines, Saudi Arabia and Spain.

Cigarette shipment volume of *L&M* decreased, notably in Russia, Thailand and Turkey, partly offset by Algeria, Kazakhstan and Ukraine. Cigarette shipment volume of *Chesterfield* increased, mainly driven by Argentina, the Czech Republic, reflecting the morphing of *Red & White,* Turkey and the United Kingdom, partly offset by Russia. Cigarette shipment volume of *Parliament* increased, mainly driven by Korea, Turkey and Ukraine, partly offset by Japan and Russia. Cigarette shipment volume of *Bond Street* increased, mainly driven by Ukraine, partly offset by Kazakhstan. Cigarette shipment volume of *Philip Morris* increased, driven mainly by Italy and Russia, partly offset by Argentina. Cigarette shipment volume of *Lark* decreased, principally due to Japan and Turkey. Cigarette shipment volume of "Others" decreased, mainly due to local, largely low-margin brands in Pakistan, the Philippines, Russia and Ukraine.

Total shipment volume of heated tobacco units reached 7.4 billion units, up from 396 million units in 2015.

Our net revenues and excise taxes on products were as follows:

(in millions)	For the Years Ended December 31,		Variance	
	2016	2015	$	%
Net revenues	$ 74,953	$ 73,908	$ 1,045	1.4 %
Excise taxes on products	48,268	47,114	1,154	2.4 %
Net revenues, excluding excise taxes on products	$ 26,685	$ 26,794	$ (109)	(0.4)%

Net revenues, which include excise taxes billed to customers, increased by $1.0 billion. Excluding excise taxes, net revenues decreased by $109 million, due to:

- unfavorable currency ($1.3 billion) and
- unfavorable volume/mix ($450 million), partly offset by
- price increases ($1.6 billion).

The unfavorable currency was due primarily to the Argentine peso, Canadian dollar, Egyptian pound, Euro, Kazakh tenge, Mexican peso, Philippine peso, Russian ruble and Turkish lira, partially offset by the Japanese yen.

Net revenues include $739 million in 2016 related to sale of RRPs, mainly driven by Japan. This amount includes excise taxes billed to customers. Excluding excise taxes, net revenues for RRPs were $733 million in 2016. In some jurisdictions, including Japan, we are not responsible for collecting excise taxes. Approximately 22% of our $733 million in 2016 RRP net revenues, excluding excise taxes, were from *IQOS* devices.

Excise taxes on products increased by $1.2 billion, due to:

- higher excise taxes resulting from changes in retail prices and tax rates ($5.3 billion), partly offset by
- favorable currency ($3.9 billion) and
- lower excise taxes resulting from volume/mix ($236 million).

Our cost of sales; marketing, administration and research costs; and operating income were as follows:

(in millions)	For the Years Ended December 31,		Variance	
	2016	2015	$	%
Cost of sales	$ 9,391	$ 9,365	$ 26	0.3 %
Marketing, administration and research costs	6,405	6,656	(251)	(3.8)%
Operating income	10,815	10,623	192	1.8 %

Cost of sales increased by $26 million, due to:

- higher cost of sales resulting from volume/mix ($242 million), partly offset by
- favorable currency ($216 million).

Marketing, administration and research costs decreased by $251 million, due to:

- lower expenses ($210 million, driven by a favorable comparison to 2015, notably related to cigarette brand building and business optimization initiatives, partly offset by increased support behind Reduced-Risk Products) and
- favorable currency ($41 million).

Operating income increased by $192 million, due primarily to:

- price increases ($1.6 billion),
- lower marketing, administration and research costs ($210 million) and
- the non-recurrence of the 2015 pre-tax charges for asset impairment and exit costs ($68 million), partly offset by
- unfavorable currency ($1.0 billion) and
- unfavorable volume/mix ($692 million).

Interest expense, net, of $891 million decreased by $117 million, due primarily to lower effective interest rates on debt and higher interest income.

Our effective tax rate decreased by 0.1 percentage point to 27.9%. The 2015 effective tax rate was unfavorably impacted by changes to repatriation assertions on certain foreign subsidiary historical earnings ($58 million), partially offset by a reduction in unrecognized tax benefits of $41 million following the conclusion of the IRS examinations of Altria Group, Inc.'s consolidated tax returns for the years 2007 and 2008 and PMI's consolidated tax returns for the years 2009 through 2011. Prior to March 28, 2008, PMI was a wholly-owned subsidiary of Altria Group, Inc.

Net earnings attributable to PMI of $7.0 billion increased by $94 million (1.4%). This increase was due primarily to higher operating income as discussed above, and lower interest expense, net. Diluted and basic EPS of $4.48 increased by 1.4%. Excluding an unfavorable currency impact of $0.46, diluted EPS increased by 11.8%.

Operating Results by Business Segment

Business Environment

Taxes, Legislation, Regulation and Other Matters Regarding the Manufacture, Marketing, Sale and Use of Tobacco Products

The tobacco industry and our business face a number of challenges that may adversely affect our business, volume, results of operations, cash flows and financial position. These challenges, which are discussed below and in "*Cautionary Factors That May Affect Future Results*," include:

- regulatory restrictions on our products, including restrictions on the packaging, marketing, and sale of tobacco or other nicotine-containing products that could reduce our competitiveness, eliminate our ability to communicate with adult consumers, or even ban certain of our products;
- fiscal challenges, such as excessive excise tax increases and discriminatory tax structures;
- illicit trade in cigarettes and other tobacco products, including counterfeit, contraband and so-called "illicit whites";

- intense competition, including from non-tax paid volume by certain local manufacturers;
- pending and threatened litigation as discussed in Item 8, Note 18. *Contingencies*; and
- governmental investigations.

Regulatory Restrictions: The tobacco industry operates in a highly regulated environment. The well-known risks of smoking have led regulators to impose significant restrictions and high excise taxes on cigarettes.

We support a comprehensive regulatory framework for tobacco products based on the principle of harm reduction, including mandated health warnings, minimum age laws, restrictions on advertising, and public place smoking restrictions. We also support regulatory measures that help reduce illicit trade.

Much of the regulation that shapes the business environment in which we operate is driven by the World Health Organization's ("WHO") Framework Convention on Tobacco Control ("FCTC"), which entered into force in 2005. The FCTC is the first international public health treaty and has as its main objective to establish a global agenda for tobacco regulation, with the purpose of reducing tobacco use. To date, 180 countries and the European Union are Parties to the FCTC. The treaty requires Parties to have in place various tobacco control measures and recommends others. The FCTC governing body, the Conference of the Parties ("CoP"), has also adopted non-binding guidelines and policy recommendations related to certain articles of the FCTC that go beyond the text of the treaty.

We have opposed certain measures and continue to engage in a dialogue with regulators with respect to those measures that we do not believe would protect public health and, if implemented, could disrupt competition, severely limit our ability to market and sell our products to adult smokers, or increase illicit trade. Certain measures are discussed in more detail below. It is not possible to predict whether or to what extent measures recommended in the FCTC guidelines will be implemented.

Fiscal Challenges: Excessive and disruptive excise, sales and other tax increases and discriminatory tax structures are expected to continue to have an adverse impact on our profitability, due to lower consumption and consumer down-trading to non-premium, discount, other low-price or low-taxed combustible tobacco products such as fine cut tobacco and illicit cigarettes. In addition, in certain jurisdictions, some of our combustible products are subject to tax structures that discriminate against premium-price products and manufactured cigarettes. We believe that such tax policies undermine public health by encouraging consumers to turn to illicit trade, and ultimately undercut government revenue objectives, disrupt the competitive environment, and encourage criminal activity. Other jurisdictions have imposed, or are seeking to impose, levies or other taxes specifically on tobacco companies, such as taxes on revenues and/or profits.

EU Tobacco Products Directive: In April 2014, the EU adopted the text of a significantly revised EU Tobacco Products Directive (TPD), which entered into force in May 2016. All 28 Member States and Norway have adopted laws transposing the TPD. The TPD sets forth a comprehensive set of regulatory requirements for tobacco products, including:

- health warnings covering 65% of the front and back panels of cigarette packs, with an option for Member States to further standardize tobacco packaging, including the introduction of plain packaging;
- a ban on characterizing flavors in some tobacco products, with a transition period for menthol expiring in May 2020;
- security features and tracking and tracing measures that will become effective on May 20, 2019, and will increase operational expenses; and
- a framework for the regulation of novel tobacco products and e-cigarettes, including requirements for health warnings and information leaflets, a prohibition on product packaging text related to reduced risk, and the introduction of notification requirements or authorization procedures in advance of commercialization.

Plain Packaging and Other Packaging Restrictions: Plain packaging legislation bans the use of branding, logos and colors on packaging other than the brand name and variant that may be printed only in specified locations and in a uniform font. To date, Australia, France, Georgia, Hungary, Ireland, New Zealand, Norway, Slovenia and the U.K. have adopted plain packaging laws, which are in various degrees of implementation.

Several countries have initiated World Trade Organization ("WTO") dispute settlement proceedings against Australia related to Australia's plain packaging legislation. The matter is still pending before the WTO panel.

Other countries are also considering adopting plain packaging legislation, including, but not limited to, Canada, Singapore, South Africa and Turkey.

Some countries have adopted, or are considering adopting, packaging restrictions that could have an impact similar to plain packaging. Examples of such restrictions include standardizing the shape and size of packages, prohibiting certain colors or the use of certain descriptive phrases on packaging, and requiring very large graphic health warnings that leave little space for branding.

Restrictions and Bans on the Use of Ingredients: The WHO and others in the public health community have recommended restrictions or total bans on the use of some or all ingredients in tobacco products, including menthol. Broad restrictions and ingredient bans would require us to reformulate our American blend tobacco products and could reduce our ability to differentiate these products in the market in the long term. Menthol bans would eliminate the entire category of mentholated tobacco products. The European Union has banned flavored tobacco products, subject to an exemption until May 2020 for menthol. Other countries may follow the EU's approach. For instance, Turkey has banned menthol as of May 2020. Broader ingredient bans have been adopted by Canada and Brazil. While the Canadian ingredient ban initially exempted menthol, amendments to the federal Tobacco Act banned menthol in cigarettes as of October 2017. In addition, the Canadian parliament is considering further amendments to the Act that would extend the menthol ban to all tobacco products. The majority of Canadian provinces have also adopted or are in the process of adopting menthol bans. The Brazil ingredients

ban, which would prohibit the use of virtually all ingredients with flavoring or aromatic properties, is not in force due to a legal challenge by a tobacco industry union, of which our Brazilian subsidiary is a member. Other lawsuits are also pending against the Brazil ingredients ban. It is not possible to predict the outcome of these legal proceedings.

Bans on Display of Tobacco Products at Retail: In a number of our markets, including, but not limited to, Australia, Canada, Norway, Russia, and Singapore, governments have banned the display of tobacco products at the point of sale. Other countries are also considering similar bans.

Bans and Restrictions on Advertising, Marketing, Promotions and Sponsorships: For many years, the FCTC has called for, and countries have imposed, partial or total bans on tobacco advertising, marketing, promotions and sponsorships, including bans and restrictions on advertising on radio and television, in print and on the Internet. The FCTC's non-binding guidelines recommend that governments prohibit all forms of communication with adult smokers.

Restrictions on Product Design: Some members of the public health community are calling for the further standardization of tobacco products by requiring, for example, that cigarettes have a certain minimum diameter, which would amount to a ban on slim cigarettes, or requiring the use of standardized filter and cigarette paper designs. In addition, at its meeting in November 2016, the CoP adopted non-binding guidelines recommending that countries regulate product design features that increase the attractiveness of tobacco products, such as the diameter of cigarettes and the use of flavor capsules.

Restrictions on Public Smoking: The pace and scope of public smoking restrictions have increased significantly in most of our markets. Many countries around the world have adopted, or are likely to adopt, regulations that restrict or ban smoking in public and/or work places, restaurants, bars and nightclubs. Some public health groups have called for, and some countries, regional governments and municipalities have adopted or proposed, bans on smoking in outdoor places, as well as bans on smoking in cars (typically, when minors are present) and private homes.

Other Regulatory Issues: Some regulators are considering, or in some cases have adopted, regulatory measures designed to reduce the supply of tobacco products. These include regulations intended to reduce the number of retailers selling tobacco products by, for example, reducing the overall number of tobacco retail licenses available or banning the sale of tobacco products within arbitrary distances of certain public facilities.

In a limited number of markets, most notably Japan, we are dependent on governmental approvals that may limit our pricing flexibility.

Illicit Trade: The illicit tobacco trade creates a cheap and unregulated supply of tobacco products, undermines efforts to reduce smoking prevalence, especially among youth, damages legitimate businesses, stimulates organized crime, increases corruption and reduces government tax revenue. Illicit trade may account for as much as 10% of global cigarette consumption; this includes counterfeit, contraband and the growing problem of “illicit whites,” which are cigarettes legally produced in one jurisdiction for the sole purpose of being exported and illegally sold in another jurisdiction where they have no legitimate market. We estimate that illicit trade in the European Union accounted for slightly less than 10% of total cigarette consumption in 2016.

A number of jurisdictions are considering actions to prevent illicit trade. In November 2012, the FCTC adopted the Protocol to Eliminate Illicit Trade in Tobacco Products (the “Protocol”), which includes supply chain control measures, such as licensing of manufacturers and distributors, enforcement in free trade zones, controls on duty free and Internet sales and the implementation of tracking and tracing technologies. To date, 54 Parties have signed the Protocol, and 35 Parties, including the European Union, have ratified it. The Protocol will come into force once the fortieth Party ratifies it, after which countries must implement its measures via national legislation. We expect, and welcome, that other Parties will ratify the Protocol.

As discussed in the *EU Tobacco Products Directive* section above, the EU regulations that mandate tracking and tracing of cigarettes and roll-your-own products manufactured or destined for the EU will become effective on May 20, 2019. The effective date for other tobacco-containing products, including some of our RRPs such as the heated tobacco units used with *IQOS*, is May 20, 2024.

In 2009, our Colombian subsidiaries entered into an Investment and Cooperation Agreement with the national and regional governments of Colombia to promote investment in, and cooperation on, anti-contraband and anti-

counterfeit efforts. The agreement provides $200 million in funding over a 20-year period to address issues such as combating the illegal cigarette trade and increasing the quality and quantity of locally-grown tobacco.

In May 2016, PMI launched PMI IMPACT, a global initiative that supports third-party projects dedicated to fighting illegal trade and related crimes such as corruption, organized criminal networks and money laundering. The centerpiece of PMI IMPACT is a council of external independent experts with impeccable credentials in the fields of law, anti-corruption and law enforcement. The experts are

responsible for evaluating and approving funding proposals for PMI IMPACT grants. PMI has pledged $100 million to fund projects within PMI IMPACT over three funding rounds. Substantially all grants under the first funding round were awarded in 2017. The second funding round began in September 2017.

In November 2016, PMI signed a joint Declaration of Intent to Prevent the Maritime Transportation of Counterfeit Goods together with eight other global brand owners and five of the world's largest shipping companies. This commitment was a result of a dialogue with the International Chamber of Commerce's Business Action to Stop Counterfeiting and Piracy. The signatories aim to tackle the infiltration of shipping services by criminal networks that exploit vessels to transport counterfeit goods, including "illicit whites," across the oceans.

Reduced-Risk Products (RRPs)

Our Approach to RRPs: We recognize that smoking cigarettes causes serious diseases and that the best way to avoid the harms of smoking is never to start or to quit. Nevertheless, it is predicted that over the next decade the number of smokers will remain largely unchanged from the current estimate of 1.1 billion, despite the considerable efforts to discourage smoking.

Cigarettes burn tobacco, which produces smoke. As a result of the combustion process, the smoker inhales various toxic substances. In contrast, RRPs do not burn tobacco and produce an aerosol that contains significantly lower levels of harmful and potentially harmful constituents ("HPHCs") than found in cigarette smoke.

For smokers who would otherwise continue to smoke, we believe that RRPs offer a much better consumer choice. Accordingly, our key strategic priorities are: to develop and commercialize products that present less risk of harm to adult smokers who switch to those products versus continued smoking; and to convince current adult smokers who would otherwise continue to smoke to switch to those products.

We recognize that this transformation from cigarettes to RRPs will take time and that the speed of transformation will depend in part upon factors beyond our control, such as the willingness of governments, regulators and other policy groups to embrace RRPs as a desired alternative to continued cigarette smoking. We also recognize that our part in this transformation must be funded from our existing cigarette business. For as long as a significant number of adult smokers continues to smoke, it is critical that the industry be led by responsible and ethical manufacturers. Therefore, during the transformation, we intend to remain a leading international cigarette manufacturer.

We have a range of RRPs in various stages of development, scientific assessment and commercialization. We conduct rigorous scientific assessments of our RRP platforms to substantiate that they reduce exposure to HPHCs and, ultimately, that these products present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to them versus continued smoking. We draw upon a team of expert scientists and engineers from a broad spectrum of scientific disciplines and our extensive learnings of adult consumer preferences to develop and assess our RRPs. Our efforts are guided by the following key objectives:

- to develop RRPs that adult smokers who would otherwise continue to smoke find to be satisfying alternatives to smoking;
- for those adult smokers, our goal is to offer RRPs with a scientifically substantiated risk-reduction profile that approaches as closely as possible that associated with smoking cessation;
- to substantiate the reduction of risk for the individual adult smoker and the reduction of harm to the population as a whole, based on scientific evidence of the highest standard that is made available for scrutiny and review by external independent scientists and relevant regulatory bodies; and
- to advocate for the development of science-based regulatory frameworks for the development and commercialization of RRPs, including the communication of scientifically substantiated information to enable adult smokers to make better consumer choices.

Our RRP Platforms: Our product development is based on the elimination of combustion via tobacco heating and other innovative systems for aerosol generation, which we believe is the most promising path to providing a better consumer choice for those who would otherwise continue to smoke. We recognize that no single product will appeal

to all adult smokers. Therefore, we are developing a portfolio of products intended to appeal to a variety of distinct adult consumer preferences.

Four RRP platforms are in various stages of development and commercialization readiness:

Platform 1 uses a precisely controlled heating device that we are commercializing under the *IQOS* brand name, into which a specially designed and proprietary tobacco unit is inserted and heated to generate an aerosol. We have conducted a series of clinical studies for this platform, the results of which were included in our submission to the U.S. Food and Drug Administration ("FDA") described below. As anticipated, the results of the first six-month term of the 6+6 month exposure response study were received at the

end of 2017, and the related report is under preparation. We expect to submit the final report for these results to the FDA in May of 2018. We expect to receive the results of the second six-month term of the study for analysis in the second quarter of 2018.

Platform 2 uses a pressed carbon heat source which, when ignited, generates an aerosol by heating tobacco. The results of our pharmacokinetic study (that measured the nicotine pharmacokinetic profile and subjective effects) and of our five-day reduced exposure study with *Platform 2* indicate that this platform could be an acceptable substitute for adult smokers who seek an alternative to cigarettes. Furthermore, the reduced exposure study showed a substantial reduction in relevant biomarkers of exposure to HPHCs in those who switched to *Platform 2* compared to those who continued to smoke cigarettes over a five-day period. The sustainability of this reduction as well as changes in clinical risk markers were assessed in a 3-month reduced exposure study. As anticipated, the results of this study were received at the end of 2017, and the related report is under preparation. We expect the report to be finalized in the second quarter of 2018. Subsequently, in accordance with standard scientific practices, we intend to share the conclusions in scientific forums and to submit them for inclusion in peer-reviewed publications.

Platform 3 provides an aerosol of nicotine salt formed by the chemical reaction of nicotine with a weak organic acid. We have explored two routes for this platform, one with electronics and one without, and have initiated a new nicotine pharmacokinetic study. We expect to receive the results for analysis in the second quarter of 2018.

Platform 4 covers e-vapor products, which are battery-powered devices that produce an aerosol by vaporizing a nicotine-containing liquid solution. Our e-vapor products comprise devices using current generation technology, and we are well advanced in the development and commercialization of our new e-vapor mesh technology that addresses certain challenges presented by some e-vapor products currently on the market. Our *MESH* products are designed to ensure the consistency and quality of the generated aerosol. We have initiated a nicotine pharmacokinetic study for which we expect to receive the results for analysis in the second quarter of 2018; the results of this study are expected to contribute to further developments of *Platform 4* products.

Commercialization of RRPs: We are building a new product category and tailor our commercialization strategy to the characteristics of each specific market. We focus our commercialization efforts on retail experience, guided consumer trials and customer care, as well as digital communication programs. In order to accelerate switching to *IQOS*, our initial market introductions typically entail one-on-one consumer engagement and introductory device discounts. These initial commercialization efforts require substantial investment.

In 2014, we introduced the *IQOS* system in pilot city launches in Nagoya, Japan, and in Milan, Italy. Since then, we have expanded our commercialization activities to include all of Japan, as well as multiple cities in Italy. To date, *IQOS* is available for sale in key cities in 37 markets and nationwide in Japan.

On the basis of our experience in Japan and Italy, we estimate that only a very small percentage of adult smokers who convert to *IQOS* switch back to cigarettes.

In the first quarter of 2016, we started the large scale commercial production of heated tobacco units. During 2017, we experienced supply shortages resulting from stronger-than-anticipated demand, primarily in Japan. Currently, we are no longer experiencing capacity limitations. We are integrating the production of our heated tobacco units into a number of our existing manufacturing facilities and progressing with our plans to build manufacturing capacity for our other RRP platforms.

In 2017, we secured a second supplier of *IQOS* devices. We are no longer experiencing supply constraints on the *IQOS* devices and, based on demand forecasts, we expect to be able to fully supply our current and planned launch markets with such devices.

The adequate supply chain for our RRP portfolio, including the supply of electronic devices, is important to our business. We work with two electronics manufacturing service providers for the supply of our *IQOS* devices and a small number of other providers for other products in our RRP portfolio and related accessories. Although we work closely with these service providers on monitoring their production capability and financial health, the commercialization of our RRPs could be adversely affected if they are unable to meet their commitments. The production of our RRP portfolio requires various metals, and we believe that there is an adequate supply of such metals in the world markets to satisfy our current and anticipated production requirements. However, some components and materials necessary for the production of our RRPs, including those for the electronic devices, are obtained from single or limited sources, and can be subject to industry-wide shortages and price fluctuations. Our

inability to secure an adequate supply of such components and materials could negatively impact the commercialization of our RRPs.

Our *IQOS* devices are subject to standard product warranties generally for a period of 12 months from the date of purchase or such other periods as required by law. We discuss product warranties in more detail in Note 5. *Product Warranty*. The significance of warranty claims is dependent on a number of factors including warranty policies and product failure rates and may increase with the number of devices sold.

To further improve the consumer experience, we introduced a new version of the *IQOS* device in the first quarter of 2017 and continue to develop product improvements.

We are also progressing with our commercialization efforts for the other platforms:

- We currently market our e-vapor products in several markets, including Ireland, Israel, Spain and the U.K. A city test of *MESH*, one of our Platform 4 products, is ongoing in Birmingham, U.K., and we expect to initiate a pilot launch of a next-generation version of this product in 2018.

- In December 2017, we initiated a small-scale city test of *TEEPS*, our Platform 2 product, in Santo Domingo, the Dominican Republic.

- In 2018, we plan to conduct a consumer test of our Platform 3 product.

RRP Regulation and Taxation: RRPs contain nicotine and are not risk-free. We therefore support science-based regulation and taxation of RRPs. Regulation and taxation should differentiate between cigarettes and products that present, are likely to present, or have the potential to present less risk of harm to adult smokers who switch to these products versus continued smoking. Regulation should provide minimum standards for RRPs and specific rules for product assessment methodologies, ingredients, labelling and consumer communication, and should ensure that the public is informed about the health risks of all combustible and non-combustible tobacco and nicotine-containing products. Regulation, as well as tobacco industry activities, should reflect the fact that youth should not consume nicotine in any form.

Some governments have banned or are seeking to ban or severely restrict emerging tobacco and nicotine-containing products such as our RRPs. These regulations might foreclose or unreasonably restrict adult consumer access even to products that might be shown to be a better consumer choice than continuing to smoke. We oppose such blanket bans and unreasonable restrictions of products that have the potential to present less risk of harm compared to continued smoking. By contrast, we support regulation that sets clear standards and propels innovation to benefit adult smokers who would otherwise continue to smoke.

In the United States, an established regulatory framework for assessing "Modified Risk Tobacco Products" and "New Tobacco Products" exists under the jurisdiction of the FDA. We submitted to the FDA a Modified Risk Tobacco Product Application ("MRTPA") for *IQOS* in December 2016, and a Premarket Tobacco Product Application ("PMTA") for *IQOS* in March 2017. In May 2017, the FDA formally accepted and filed our MRTPA for substantive scientific review and, in June 2017, the FDA opened the period for the public to provide comments on our application. In August 2017, the FDA completed a preliminary review of our PMTA and accepted our application for substantive review. The FDA referred our MRTPA to the Tobacco Product Scientific Advisory Committee ("TPSAC"). TPSAC held a meeting on January 24 and January 25, 2018 on our MRTPA. The recommendations and votes of TPSAC are not binding on the FDA. By regulation, the FDA's decision on our MRTPA will take into account, in addition to the views of TPSAC, scientific evidence as well as comments, data and information submitted by interested persons.

Separately, on July 28, 2017, the FDA issued a policy announcement aiming to explore the potential of nicotine reduction in cigarettes in conjunction with less harmful products that deliver nicotine for adults who choose to use such products.

Future FDA actions may influence the regulatory approach of other governments.

In the EU, all EU Member States and Norway have transposed the EU Tobacco Products Directive, including the provisions on novel tobacco products, such as heated tobacco units, and e-cigarettes. Most of the EU Member States require a notification submitted six months before the intended placing on the market of a novel tobacco product, while some require pre-market authorizations for the introduction of such products. To date, we have filed a comprehensive dossier summarizing our scientific assessment of *IQOS* in 22 Member States.

On December 12, 2017, at the request of the U.K. Department of Health and Public Health England, the U.K. Committee on Toxicity published its assessment of the risk of heated tobacco products relative to cigarette smoking.

This assessment included analysis of scientific data for two heated tobacco products, one of which was *IQOS*. The assessment concluded that, while still harmful to health, compared with the known risks from cigarettes, heated tobacco products are probably less harmful. Subsequently, on February 6, 2018, Public Health England published a report stating that the available evidence suggests that heated tobacco products may be considerably less harmful than cigarettes and more harmful than e-cigarettes.

We make our scientific findings publicly available for scrutiny and peer review through several channels, including our websites. From time to time, adult consumers, competitors, members of the scientific community, and others inquire into our scientific methodologies, challenge our scientific conclusions or request further study of certain aspects of our RRPs and their health effects. We are committed to a robust and open scientific debate but believe that such debate should be based on accurate and reliable scientific information. We seek to provide accurate and reliable scientific information about our RRPs; nonetheless, we may not be able to prevent third-party dissemination of false, misleading or unsubstantiated information about these products.

To date, we have been largely successful in demonstrating to regulators that our RRPs are not cigarettes, and as such they are generally taxed either as a separate category or as other tobacco products, which typically yields more favorable tax rates than cigarettes. Although we believe that this is sensible from the public health perspective, we cannot guarantee that regulators will continue this approach.

There can be no assurance that we will succeed in our efforts to replace cigarettes with RRPs or that regulation will allow us to commercialize RRPs in all markets, to communicate scientifically substantiated risk-reduction claims, or to treat RRPs differently from cigarettes.

Our RRP Business Development Initiatives: In December 2013, we established a strategic framework with Altria Group, Inc. ("Altria") under which Altria will make available its e-vapor products exclusively to us for commercialization outside the United States, and we will make available two of our RRPs exclusively to Altria for commercialization in the United States. In March 2015, we launched *Solaris*, a Platform 4 e-vapor product licensed from Altria, in Spain. In December 2015, we introduced *Solaris* in Israel.

In July 2015, we extended the strategic framework with Altria to include a Joint Research, Development and Technology Sharing Agreement. The additional agreement provides the framework under which PMI and Altria will collaborate to develop the next generation of e-vapor products for commercialization in the United States by Altria and in markets outside the United States by PMI. The collaboration between PMI and Altria in this endeavor is enabled by exclusive technology cross licenses and technical information sharing. The agreements also provide for cooperation on the scientific assessment of, and for the sharing of improvements to, the existing generation of licensed products.

Other Developments: On September 12, 2017, we announced our support of the Foundation for a Smoke-Free World. We agreed to contribute $80 million per year over the next 12 years, as specified in the agreement. We made an initial contribution of $4.5 million in 2017 and the first annual contribution of $80 million in the beginning of 2018. The Foundation is an independent body and is governed by its independent Board of Directors. The Foundation's role, as set out in its corporate charter, includes funding research in the field of tobacco harm reduction, encouraging measures that reduce the harm caused by smoking, and assessing the effect of reduced cigarette consumption on the industry value chain.

Governmental Investigations

From time to time, we are subject to governmental investigations on a range of matters. We describe certain matters pending in Thailand and South Korea in Item 8, Note 18. *Contingencies*.

In November 2010, a WTO panel issued its decision in a dispute relating to facts that arose from August 2006 between the Philippines and Thailand concerning a series of Thai customs and tax measures affecting cigarettes imported by PM Thailand into Thailand (see Item 8, Note 18. *Contingencies* for additional information). The WTO panel decision, which was upheld by the WTO Appellate Body, concluded that Thailand had no basis to find that PM Thailand's declared customs values and taxes paid were too low, as alleged by the DSI in 2009. The decision also created obligations for Thailand to revise its laws, regulations, or practices affecting the customs valuation and tax treatment of future cigarette imports. Thailand agreed in September 2011 to fully comply with the decision by October 2012. The Philippines asserts that to date Thailand has not fully complied with the WTO panel decision. The Philippines has repeatedly expressed concerns with ongoing investigations by Thailand of PM Thailand, including those that led to the criminal charges described in Item 8, Note 18. *Contingencies*, and has commenced two formal proceedings at the WTO to challenge criminal charges against PM Thailand arguing that the criminal charges appear to be based on grounds not supported by WTO customs valuation rules and inconsistent with several decisions already taken by Thai Customs and other Thai governmental agencies.

Acquisitions and Other Business Arrangements

We discuss our acquisitions and other business arrangements in Item 8, Note 6. *Acquisitions and Other Business Arrangements* to our consolidated financial statements.

Investments in Unconsolidated Subsidiaries

We discuss our investments in unconsolidated subsidiaries in Item 8, Note 4. *Investments in Unconsolidated Subsidiaries* to our consolidated financial statements.

Trade Policy

We are subject to various trade restrictions imposed by the United States of America and countries in which we do business ("Trade Sanctions"), including the trade and economic sanctions administered by the U.S. Department of the Treasury's Office of Foreign Assets Control and the U.S. Department of State. It is our policy to comply fully with these Trade Sanctions.

Tobacco products are agricultural products under U.S. law and are not technological or strategic in nature. From time to time we make sales in countries subject to Trade Sanctions, either where such sanctions do not apply to our business or pursuant to exemptions or licenses.

To our knowledge, none of our commercial arrangements results in the governments of any country identified by the U.S. government as a state sponsor of terrorism, nor entities controlled by those governments, receiving cash or acting as intermediaries in violation of U.S. laws.

We do not sell products in Iran, Sudan, North Korea and Syria. From time to time, we explore opportunities to sell our products in one or more of these countries, as permitted by law.

In January 2018, we commenced sales of cigarettes in Cuba, as permitted by law.

Certain states within the U.S. have enacted legislation permitting state pension funds to divest or abstain from future investment in stocks of companies that do business with certain countries that are sanctioned by the U.S. We do not believe such legislation has had a material effect on the price of our shares.

2017 compared with 2016

The following discussion compares operating results within each of our reportable segments for 2017 with 2016.

Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance reflect cigarettes and heated tobacco units.

European Union:

European Union	**For the Years Ended December 31,**		**Variance**	
(in millions)	**2017**	**2016**	**$**	**%**
Net revenues	**$ 27,580**	$ 27,129	$ 451	1.7 %
Excise taxes on products	**19,262**	18,967	295	1.6 %
Net revenues, excluding excise taxes on products	**8,318**	8,162	156	1.9 %
Operating companies income	**3,775**	3,994	(219)	(5.5%)

Net revenues increased by $451 million. Excluding excise taxes, net revenues increased by $156 million, due to:

- price increases ($156 million) and
- favorable currency ($45 million), partially offset by
- unfavorable volume/mix ($45 million).

The net revenues of the European Union segment include $320 million in 2017 and $62 million in 2016 related to the sale of RRPs. Excluding excise taxes, net revenues for RRPs were $269 million in 2017 and $57 million in 2016.

Operating companies income decreased by $219 million during 2017. This decrease was due primarily to:

- higher marketing, administration and research costs ($223 million, primarily related to increased investment behind reduced-risked products),
- unfavorable volume/mix ($119 million) and
- unfavorable currency ($43 million), partly offset by
- price increases ($156 million) and
- lower manufacturing costs ($14 million).

European Union - Total Market, PMI Shipment & Market Share Commentaries

The estimated total market in the European Union decreased by 1.9% to 492.1 billion units. Our Regional market share was flat at 38.3%, with gains in France, Germany and Poland offset by declines in Italy and Spain.

Shipment volume and market share performance by brand for cigarettes and heated tobacco units are shown in the tables below:

European Union Shipment Volume by Brand (Million Units)

	Full-Year		
	2017	**2016**	**Change**
Cigarettes			
Marlboro	**93,088**	96,245	(3.3 %)
L&M	**34,261**	34,691	(1.2 %)
Chesterfield	**29,087**	30,140	(3.5 %)
Philip Morris	**15,158**	16,290	(6.9 %)
Others	**15,699**	16,220	(3.2 %)
Total Cigarettes	**187,293**	193,586	(3.3 %)
Heated Tobacco Units	**1,889**	224	+100.0%
Total European Union	**189,182**	193,810	(2.4 %)

European Union Market Shares by Brand

	Full-Year		
	2017	**2016**	**Change p.p.**
Marlboro	**18.8 %**	19.0 %	(0.2)
L&M	**6.9 %**	6.9 %	—
Chesterfield	**6.0 %**	5.9 %	0.1
Philip Morris	**3.1 %**	3.2 %	(0.1)
HEETS	**0.3 %**	— %	0.3
Others	**3.2 %**	3.3 %	(0.1)

Total European Union	**38.3 %**	38.3 %	—

Our total shipment volume decreased by 2.4% to 189.2 billion units, or by 1.9% excluding estimated net inventory movements, notably in Italy and Spain. The decrease in cigarette shipment volume of *Marlboro* was mainly due to Greece, Italy and Spain. The decrease in cigarette shipment volume of *L&M* was mainly due to Germany, Romania and Spain, partly offset by France. The decrease in cigarette shipment volume of *Chesterfield* was mainly due to Italy, Portugal and Spain, partly offset by Poland. The decrease in cigarette shipment volume of *Philip Morris* was mainly due to Italy. The decrease in cigarette shipment volume of "Others" was due notably to *Muratti* in Italy.

European Union - Key Market Commentaries

In **France**, estimated industry size, our shipment volume and market share performance, shown in the table below, include cigarettes and our heated tobacco units.

France Key Market Data

	Full-Year		
	2017	**2016**	**Change % / p.p.**
Total Market (billion units)	**44.4**	44.9	(1.2%)
PMI Shipments (million units)	**19,264**	19,247	0.1 %
PMI Market Share			
Marlboro	**27.1 %**	26.4%	0.7
Philip Morris	**10.3 %**	10.2%	0.1
Chesterfield	**3.0 %**	3.1%	(0.1)
Others*	**2.8 %**	2.7%	0.1
Total	**43.2 %**	42.4%	0.8

**Includes heated tobacco units.*

The estimated total market decreased by 1.2%. The increase in our shipment volume was driven by higher market share, notably of *Marlboro*, reflecting the growth of both *Marlboro* Red and Gold in 30s packs launched in March 2017.

In **Germany**, estimated industry size, our shipment volume and market share performance, shown in the table below, include cigarettes and our heated tobacco units.

Germany Key Market Data

	Full-Year		
	2017	**2016**	**Change % / p.p.**
Total Market (billion units)	**76.9**	78.1	(1.6%)
PMI Shipments (million units)	**28,575**	28,958	(1.3%)
PMI Market Share			
Marlboro	**22.7 %**	22.5%	0.2
L&M	**11.5 %**	11.6%	(0.1)
Chesterfield	**1.5 %**	1.6%	(0.1)
Others*	**1.5 %**	1.4%	0.1
Total	**37.2 %**	37.1%	0.1

**Includes heated tobacco units.*

The estimated total market decreased by 1.6%, or by 2.7% excluding the net impact of estimated trade inventory movements, mainly reflecting the impact of price increases in March 2017. The decrease in our shipment volume was mainly due to the lower total market, partly offset by higher market share.

In **Italy**, estimated industry size, our shipment volume and market share performance, shown in the table below, include cigarettes and our heated tobacco units.

	Italy Key Market Data		
	Full-Year		
	2017	2016	Change % / p.p.
Total Market (billion units)	**69.8**	72.1	(3.2 %)
PMI Shipments (million units)	**36,767**	38,744	(5.1 %)
PMI Market Share			
Marlboro	**23.9 %**	24.3 %	(0.4)
Chesterfield	**11.3 %**	11.5 %	(0.2)
Philip Morris	**7.7 %**	8.5 %	(0.8)
HEETS	**0.7 %**	0.1 %	0.6
Others	**8.6 %**	8.1 %	0.5
Total	**52.2 %**	52.5 %	(0.3)

The estimated total market decreased by 3.2%, partly reflecting the implementation of the Tobacco Product Directive's ban on pack sizes of ten cigarettes at the end of 2016. The decline of our shipments, down by 3.6% excluding the net impact of distributor inventory movements, mainly reflected the lower total market, as well as lower cigarette market share, principally due to *Marlboro*, partly reflecting the ban on pack sizes of ten cigarettes, and low-price *Philip Morris*, impacted by the growth of the super-low price segment, partly offset by *HEETS* and *Merit* in "Others."

In **Poland**, estimated industry size, our shipment volume and market share performance, shown in the table below, include cigarettes and our heated tobacco units.

	Poland Key Market Data		
	Full-Year		
	2017	2016	Change % / p.p.
Total Market (billion units)	**41.7**	41.3	0.9 %
PMI Shipments (million units)	**17,784**	17,485	1.7 %
PMI Market Share			
Marlboro	**10.7 %**	11.6 %	(0.9)
L&M	**18.4 %**	18.5 %	(0.1)
Chesterfield	**10.4 %**	9.1 %	1.3
HEETS	**0.2 %**	— %	0.2
Others	**3.0 %**	3.1 %	(0.1)
Total	**42.7 %**	42.3 %	0.4

The estimated total market increased by 0.9%. The increase in our shipment volume was primarily driven by the higher total market and higher market share, driven by *Chesterfield*, benefiting from brand support, partly offset by *Marlboro*, reflecting pressure from competitive brands in the below premium segment.

In **Spain**, estimated industry size, our shipment volume and market share performance, shown in the table below, include cigarettes and our heated tobacco units.

	Spain Key Market Data		
	Full-Year		
	2017	2016	Change % / p.p.
Total Market (billion units)	**45.0**	46.7	(3.5%)
PMI Shipments (million units)	**14,456**	16,374	(11.7%)
PMI Market Share			
Marlboro	**16.5%**	18.0%	(1.5)
L&M	**5.3%**	5.4%	(0.1)
Chesterfield	**8.6%**	8.6%	—
Others*	**1.9%**	1.9%	—
Total	**32.3%**	33.9%	(1.6)

**Includes heated tobacco units.*

The estimated total market decreased by 3.5%, or by 2.5% excluding the net impact of estimated trade inventory movements. The decline of our shipment volume, down by 8.0% excluding the net impact of distributor inventory movements, mainly reflected the lower total market, and lower market share, due to *Marlboro*, reflecting the impact of price increases, particularly above the round €5.00 per pack price point in the vending channel, as well as a challenging comparison with 2016 in which the market share of *Marlboro* grew by 1.0 point.

Eastern Europe, Middle East & Africa:

Eastern Europe, Middle East & Africa (in millions)	For the Years Ended December 31, 2017	2016	Variance $	%
Net revenues	**$ 18,045**	$ 18,286	$ (241)	(1.3%)
Excise taxes on products	**11,346**	11,286	60	0.5 %
Net revenues, excluding excise taxes on products	**6,699**	7,000	(301)	(4.3%)
Operating companies income	**2,888**	3,016	(128)	(4.2%)

Net revenues decreased by $241 million. Excluding excise taxes, net revenues decreased by $301 million, due to:

- unfavorable volume/mix ($374 million) and
- unfavorable currency ($291 million), partly offset by
- price increases ($364 million).

The net revenues of the Eastern Europe, Middle East & Africa segment include $158 million in 2017 and $9 million in 2016 related to the sale of RRPs. Excluding excise taxes, net revenues for RRPs were $149 million in 2017 and $9 million in 2016.

Operating companies income decreased by $128 million during 2017. This decrease was due primarily to:

- unfavorable volume/mix ($344 million) and
- higher marketing, administration and research costs ($201 million), partly offset by
- price increases ($364 million) and
- favorable currency ($81 million).

Eastern Europe, Middle East & Africa - Total Market, PMI Shipment & Market Share Commentaries

EEMA PMI Shipment Volume by Brand (Million Units)

	Full-Year		
	2017	**2016**	**Change**
Cigarettes			
Marlboro	**70,122**	73,818	(5.0%)
L&M	**46,923**	52,183	(10.1%)
Bond Street	**36,336**	42,553	(14.6%)
Parliament	**33,299**	33,940	(1.9%)
Philip Morris	**19,086**	2,058	+100.0%
Others	**50,391**	66,841	(24.6%)
Total Cigarettes	**256,157**	271,393	(5.6%)
Heated Tobacco Units	**1,581**	100	+100.0%
Total EEMA	**257,738**	271,493	(5.1%)

The estimated total market in EEMA decreased by 2.8% to 1.0 trillion units. Our Regional market share decreased by 0.3 points to 24.9%.

Our total shipment volume decreased by 5.1% to 257.7 billion units, mainly reflecting: lower cigarette shipment volume in Russia, Saudi Arabia - where our cigarette shipment volume declined by 35.8%, impacted by the new excise tax implemented in June 2017 that resulted in the doubling of retail prices - and Ukraine; partly offset by higher cigarette shipment volume in North Africa, notably Algeria, and higher heated tobacco unit shipment volume. The decrease in cigarette shipment volume of *Marlboro* was predominantly due to Saudi Arabia, reflecting the impact of the excise tax that resulted in the doubling of the brand's retail price from SAR 12 to SAR 24 per pack, partly offset by North Africa, mainly Algeria and Egypt, and Turkey. The decrease in cigarette shipment volume of *L&M* was mainly due to Russia, Saudi Arabia and Turkey, partly offset by Algeria and Kazakhstan. The decrease in cigarette shipment volume of *Bond Street* was mainly due to Kazakhstan, Russia and Ukraine. The decrease in cigarette shipment volume of *Parliament* was mainly due to Russia and Saudi Arabia, partly offset by Kazakhstan. The increase in cigarette shipment volume of *Philip Morris* was driven mainly by Russia and Ukraine, largely reflecting successful portfolio consolidation of local, low-price brands in "Others."

Eastern Europe, Middle East & Africa - Key Market Commentaries

In **North Africa** (defined as Algeria, Egypt, Libya, Morocco and Tunisia), estimated cigarette industry size, our cigarette shipment volume and cigarette market share performance are shown in the table below.

	North Africa Key Market Data		
	Full-Year		
	2017	2016	Change % / p.p.
Total Cigarette Market (billion units)	**144.9**	142.3	1.9 %
PMI Cigarette Shipments (million units)	**35,085**	34,035	3.1 %
PMI Cigarette Market Share			
Marlboro	**9.3 %**	8.3 %	1.0
L&M	**11.8 %**	12.2 %	(0.4)
Others	**2.9 %**	2.7 %	0.2
Total	**24.0 %**	23.2 %	0.8

The estimated total cigarette market increased by 1.9%, mainly driven by Egypt, partially offset by Tunisia. The increase in our cigarette shipment volume was mainly driven by the higher cigarette market, as well as higher cigarette market share, notably of *Marlboro* in Algeria, partly offset by *L&M* in Egypt.

In **Russia**, estimated industry size and our shipment volume, shown in the table below, include cigarettes and our heated tobacco units. Our market share performance, as measured by Nielsen and shown in the table below, reflects that of cigarettes.

	Russia Key Market Data		
	Full-Year		
	2017	2016	Change % / p.p.
Total Market (billion units)	**260.0**	280.0	(7.2 %)
PMI Shipments (million units)	**72,417**	79,706	(9.1 %)
PMI Cigarette Market Share			
Marlboro	**1.5 %**	1.4 %	0.1
Parliament	**3.5 %**	3.8 %	(0.3)
Bond Street	**8.6 %**	8.4 %	0.2
Philip Morris	**4.3 %**	0.2 %	4.1
Others	**9.2 %**	13.4 %	(4.2)
Total	**27.1 %**	27.2 %	(0.1)

The estimated total market decreased by 7.2%, reflecting the impact of excise tax-driven price increases and an increase in the prevalence of illicit trade. The decline of our shipment volume was mainly due to the lower total market. Our market share decreased by 0.1 point. The decline of "Others" largely reflected the successful portfolio consolidation of local, low-price brands into *Philip Morris*.

In **Turkey**, estimated cigarette industry size, our cigarette shipment volume and cigarette market share performance, as measured by Nielsen, are shown in the table below.

Turkey Key Market Data

	Full-Year		
	2017	2016	Change % / p.p.
Total Cigarette Market (billion units)	**106.2**	105.5	0.7 %
PMI Cigarette Shipments (million units)	**49,649**	49,624	0.1 %
PMI Cigarette Market Share			
Marlboro	**10.2 %**	10.2 %	—
Parliament	**11.5 %**	11.7 %	(0.2)
Lark	**6.9 %**	7.4 %	(0.5)
Others	**14.7 %**	15.0 %	(0.3)
Total	**43.3 %**	44.3 %	(1.0)

The estimated total cigarette market increased by 0.7%. Excluding the net impact of estimated trade inventory movements, the estimated total cigarette market declined by 1.6%. The decrease in our cigarette market share, as measured by Nielsen, was mainly due to *Lark,* and *L&M* and *Muratti* in "Others," partly offset by *Chesterfield*, principally reflecting competitive pressure from super-low price alternatives.

In **Ukraine**, estimated industry size and our shipment volume, shown in the table below, include cigarettes and our heated tobacco units. Our market share performance, as measured by Nielsen and shown in the table below, reflects that of cigarettes.

Ukraine Key Market Data

	Full-Year		
	2017	2016	Change % / p.p.
Total Market (billion units)	**67.1**	73.1	) (8.2 %
PMI Shipments (million units)	**19,356**	22,022	) (12.1 %
PMI Cigarette Market Share			
Marlboro	**3.0 %**	3.1 %	(0.1)
Parliament	**3.2 %**	2.9 %	0.3
Bond Street	**8.4 %**	10.0 %	(1.6)
Philip Morris	**3.1 %**	— %	3.1
Others	**9.6 %**	13.2 %	(3.6)
Total	**27.3 %**	29.2 %	(1.9)

The estimated total market decreased by 8.2%, mainly due to the impact of price increases and an increase in the prevalence of illicit trade. The decrease in our shipment volume was primarily due to the lower total market, as well as lower cigarette market share, as measured by Nielsen, notably of low-price *Bond Street*, reflecting competitive pressure from lower-priced alternatives, partly offset by *Parliament* and *Philip Morris*, following the successful portfolio consolidation of a local, low-price brand in "Others."

Asia:

Asia (in millions)	For the Years Ended December 31, 2017	2016	Variance $	%
Net revenues	**$ 22,635**	$ 20,531	$ 2,104	10.2 %
Excise taxes on products	**11,845**	11,850	(5)	— %
Net revenues, excluding excise taxes on products	**10,790**	8,681	2,109	24.3 %
Operating companies income	**4,149**	3,196	953	29.8 %

Net revenues increased by $2.1 billion. Excluding excise taxes, net revenues increased by $2.1 billion, due to:

- favorable volume/mix ($1.7 billion) and
- price increases ($559 million), partly offset by
- unfavorable currency ($137 million).

The net revenues of the Asia segment include $3.3 billion in 2017 and $666 million in 2016 related to the sale of RRPs, mainly driven by Japan and Korea in 2017 and Japan in 2016. Excluding excise taxes, net revenues for RRPs were $3.2 billion in 2017 and $666 million in 2016. In some jurisdictions, including Japan, we are not responsible for collecting excise taxes.

Operating companies income increased by $953 million during 2017. This increase was due primarily to:

- favorable volume/mix ($622 million),
- price increases ($559 million) and
- lower manufacturing costs ($40 million), partly offset by
- higher marketing, administration and research costs ($141 million, principally related to increased investment behind reduced-risk products) and
- unfavorable currency ($123 million).

Asia - Total Market, PMI Shipment & Market Share Commentaries

Asia PMI Shipment Volume by Brand (Million Units)

	Full-Year 2017	2016	Change
Cigarettes			
Marlboro	**73,446**	76,463	(3.9%)
Lark	**14,474**	17,600	(17.8%)
Parliament	**9,224**	10,142	(9.1%)
Others	**137,109**	155,824	(12.0%)
Total Cigarettes	**234,253**	260,029	(9.9%)
Heated Tobacco Units	**32,729**	7,070	+100.0%

Total Asia	**266,982**	267,099	— %

The estimated total market in Asia, excluding China, decreased by 3.1% to 1.1 trillion units. Our Regional market share, excluding China, was flat at 23.8%.

Our total shipment volume of 267.0 billion units was flat, mainly reflecting: lower cigarette shipment volume in Indonesia, Japan, Korea, Pakistan - impacted by excise tax-driven price increases in 2017 and an increase in the prevalence of illicit trade - and the Philippines, fully offset by higher heated tobacco unit shipment volume, mainly in Japan and Korea. The decrease in cigarette shipment volume of *Marlboro* was mainly due to Japan and Korea, primarily reflecting out-switching to heated tobacco products, partly offset by Indonesia and the Philippines. The decrease in cigarette shipment volume of *Lark* was principally due to Japan. The decrease in cigarette shipment

volume of *Parliament* was mainly due to Japan and Korea. The decrease in cigarette shipment volume of "Others" was mainly due to local, low-price brands in Indonesia, Pakistan and the Philippines.

Our total shipment volume benefited from the favorable net impact of estimated combustible and heated tobacco unit inventory movements, which were driven by approximately 8.5 billion units net in Japan, reflecting: the increasing demand for *HeatSticks*, anticipated to further increase in the first quarter of 2018 following a planned lifting of the restriction on *IQOS* device sales; the establishment of appropriate distributor inventory levels of heated tobacco units, given the current high dependence on a single manufacturing center; and the transition from air freight to sea freight of heated tobacco units, largely completed in the fourth quarter of 2017. Excluding the impact of total estimated net inventory movements, our total shipment volume decreased by 3.1%.

Asia - Key Market Commentaries

In **Indonesia**, estimated cigarette industry size, our cigarette shipment volume, cigarette market share and segmentation performance are shown in the tables below.

	Indonesia Key Market Data		
	Full-Year		
	2017	**2016**	**Change % / p.p.**
Total Cigarette Market (billion units)	**307.4**	315.6	(2.6%)
PMI Cigarette Shipments (million units)	**101,324**	105,524	(4.0%)
PMI Cigarette Market Share			
Sampoerna A	**13.8%**	14.0%	(0.2)
Dji Sam Soe	**7.4%**	6.5%	0.9
Sampoerna U	**4.1%**	5.2%	(1.1)
Others	**7.7%**	7.7%	—
Total	**33.0%**	33.4%	(0.4)

	Indonesia Segmentation Data		
	Full-Year		
	2017	**2016**	**Change p.p.**
Segment % of Total Market			
Hand-Rolled Kretek (SKT)	**17.6%**	18.2%	(0.6)
Machine-Made Kretek (SKM)	**77.2%**	75.8%	1.4
Whites (SPM)	**5.2%**	6.0%	(0.8)
Total	**100.0%**	**100.0%**	—
PMI % Share of Segment			
Hand-Rolled Kretek (SKT)	**37.5%**	37.3%	0.2
Machine-Made Kretek (SKM)	**29.4%**	28.9%	0.5
Whites (SPM)	**70.2%**	79.5%	(9.3)

The estimated total cigarette market decreased by 2.6%, reflecting a soft economic environment and the impact of above-inflation excise tax-driven price increases. The decrease in our shipments was mainly due to the lower total market and lower cigarette market share, notably due to a decline of *Sampoerna U*, reflecting the impact of price increases, partly offset by a growth of *Dji Sam Soe*, driven by the variant *Magnum Mild*.

In **Japan**, our shipments reflect cigarette and heated tobacco unit volume. The estimated total market and our market share reflect total industry cigarette and heated tobacco unit volume.

Japan Key Market Data

	Full-Year		
	2017	**2016**	**Change % / p.p.**
Total Market (billion units)	**171.5**	179.0	(4.2%)
PMI Shipments (million units)			
Cigarettes	**34,853**	43,915	(20.6%)
Heated Tobacco Units	**31,291**	7,069	+100%
Total	**66,144**	50,985	29.7 %
PMI Market Share			
Marlboro	**9.3%**	10.6%	(1.3)
HeatSticks	**10.8%**	2.9%	7.9
Parliament	**2.1%**	2.3%	(0.2)
Lark	**8.6%**	9.6%	(1.0)
Others	**1.3%**	1.7%	(0.4)
Total	**32.1%**	27.1%	5.0

The estimated total market decreased by 4.2%. Our shipment volume increased by 13.1%, excluding the net impact of estimated cigarette and heated tobacco unit distributor inventory movements, driven by higher market share of *HeatSticks*.

In **Korea**, our shipments reflect cigarette and heated tobacco unit volume. The estimated total market and our market share reflect total industry cigarette and heated tobacco unit volume.

Korea Key Market Data

	Full-Year		
	2017	**2016**	**Change % / p.p.**
Total Market (billion units)	**70.6**	73.6	(4.1%)
PMI Shipments (million units)			
Cigarettes	**13,499**	15,490	(12.9%)
Heated Tobacco Units	**1,438**	—	— %
Total	**14,937**	15,490	(3.6%)
PMI Market Share			
Marlboro	**8.7%**	9.6%	(0.9)
Parliament	**8.0%**	7.9%	0.1
HEETS	**2.0%**	—%	2.0
Virginia S.	**2.0%**	3.0%	(1.0)
Others	**0.5%**	0.5%	—

Total	**21.2 %**	21.0 %	0.2

The estimated total market decreased by 4.1%, or by 3.3% excluding the net impact of estimated cigarette trade inventory movements. The decrease in our shipment volume was due to the lower total market, partly offset by higher market share driven by the May 2017 launch of *HEETS*.

In the **Philippines**, estimated cigarette industry size, our cigarette shipment volume and cigarette market share performance are shown in the table below.

	Philippines Key Market Data		
	Full-Year		
	2017	2016	Change % / p.p.
Total Cigarette Market (billion units)	**74.9**	79.3	(5.6%)
PMI Cigarette Shipments (million units)	**50,618**	56,611	(10.6%)
PMI Cigarette Market Share			
Marlboro	**33.0%**	28.4%	4.6
Fortune	**18.0%**	23.4%	(5.4)
Jackpot	**6.1%**	7.9%	(1.8)
Others	**10.5%**	11.6%	(1.1)
Total	**67.6%**	71.3%	(3.7)

The decline of the estimated total cigarette market of 6.7% excluding the net impact of estimated trade inventory movements, was mainly due to the impact of excise tax-driven price increases. The decline in our cigarette shipment volume was due to the lower total cigarette market, as well as lower cigarette market share, particularly of our low and super-low price brands as a result of the timing of competitors' price increases, which initially widened the price gaps to our principal competitor's discounted brands, partly offset by *Marlboro*, which benefited from in-switching from lower-priced brands.

Latin America & Canada:

Latin America & Canada (in millions)	For the Years Ended December 31, 2017	2016	Variance $	%
Net revenues	**$ 9,838**	$ 9,007	$ 831	9.2%
Excise taxes on products	**6,897**	6,165	732	11.9%
Net revenues, excluding excise taxes on products	**2,941**	2,842	99	3.5%
Operating companies income	**1,002**	938	64	6.8%

Net revenues increased by $831 million. Excluding excise taxes, net revenues increased by $99 million, due to:

- price increases ($307 million), partly offset by
- unfavorable volume/mix ($154 million) and
- unfavorable currency ($54 million).

The net revenues of the Latin America & Canada segment include $5 million in 2017 related to the sale of RRPs. Excluding excise taxes, net revenues for RRPs were $4 million in 2017.

Operating companies income increased by $64 million during 2017. This increase was due primarily to:

- price increases ($307 million), partly offset by
- unfavorable volume/mix ($152 million),
- unfavorable currency ($70 million) and
- higher manufacturing costs ($17 million).

Latin America & Canada - Total Market, PMI Shipment & Market Share Commentaries

Latin America & Canada PMI Shipment Volume by Brand (Million Units)

	Full-Year		
	2017	**2016**	**Change**
Cigarettes			
Marlboro	**33,711**	35,194	(4.2%)
Philip Morris	**13,320**	16,463	(19.1%)
Chesterfield	**9,852**	2,626	+100.0%
Others	**27,340**	33,655	(18.8%)
Total Cigarettes	**84,223**	87,938	(4.2%)
Heated Tobacco Units	**27**	—	— %
Total Latin America & Canada	**84,250**	87,938	(4.2%)

The estimated total market in Latin America & Canada decreased by 3.8% to 213.0 billion units. Our Regional market share decreased by 0.1 point to 39.6%.

Our total shipment volume decreased by 4.2% to 84.3 billion units, mainly due to lower cigarette shipment volume in Argentina, Brazil, Canada, Colombia and Mexico. The decrease in cigarette shipment volume of *Marlboro* was mainly due to Argentina and Brazil. The decrease in cigarette shipment volume of *Philip Morris* was mainly due to Argentina. The increase in cigarette shipment volume of *Chesterfield* was driven by Argentina, Brazil, Colombia and Venezuela, partly offset by Mexico. The decrease in cigarette shipment volume of "Others" was principally due to mainly local brands in Argentina, Brazil, Colombia and Venezuela, largely reflecting successful brand portfolio consolidation, Canada and Mexico.

Latin America & Canada - Key Market Commentaries

In **Argentina**, estimated cigarette industry size, our cigarette shipment volume and cigarette market share performance are shown in the table below.

	Argentina Key Market Data		
	Full-Year		
	2017	2016	Change % / p.p.
Total Cigarette Market (billion units)	**36.2**	36.1	0.2 %
PMI Cigarette Shipments (million units)	**27,002**	27,512	(1.9 %)
PMI Cigarette Market Share			
Marlboro	**20.0 %**	22.4 %	(2.4)
Chesterfield	**15.9 %**	5.5 %	10.4
Philip Morris	**33.0 %**	41.6 %	(8.6)
Others	**5.8 %**	6.8 %	(1.0)
Total	**74.7 %**	76.3 %	(1.6)

The estimated total cigarette market increased by 0.2%, reflecting higher tax declarations by local manufacturers, as well as a favorable comparison to the full year 2016, which declined by 11.6% mainly due to the impact of tax-driven price increases. The decrease in our cigarette shipment volume was mainly due to lower cigarette market share, reflecting the growth of the low price segment, where local manufacturers are exempt from paying minimum excise tax, resulting in widened price gaps with premium *Marlboro* and mid-price *Philip Morris*, partly offset by low-price *Chesterfield* that benefited from successful brand portfolio consolidation of a low-price brand in "Others."

In **Canada**, estimated industry size, our shipment volume and market share performance, shown in the table below, include cigarettes and our heated tobacco units.

	Canada Key Market Data		
	Full-Year		
	2017	2016	Change % / p.p.
Total Market (billion units)	**24.6**	26.3	(6.3 %)
PMI Shipments (million units)	**9,259**	10,049	(7.9 %)
PMI Market Share			
Belmont	**4.1 %**	3.7 %	0.4
Canadian Classics	**9.5 %**	10.2 %	(0.7)
Next	**11.5 %**	11.3 %	0.2
Others*	**12.2 %**	13.2 %	(1.0)
Total	**37.3 %**	38.4 %	(1.1)

**Includes heated tobacco units*

The estimated total market decreased by 6.3%, mainly due to the impact of price increases. The decrease in our shipment volume mainly reflected the lower total market, as well as lower cigarette market share, unfavorably impacted by estimated net trade inventory movements.

In **Mexico**, estimated cigarette industry size, our cigarette shipment volume and cigarette market share performance are shown in the table below.

	Mexico Key Market Data		
	Full-Year		
	2017	2016	Change % / p.p.
Total Cigarette Market (billion units)	**35.8**	36.2	(1.1 %)
PMI Cigarette Shipments (million units)	**24,351**	25,080	(2.9 %)
PMI Cigarette Market Share			
Marlboro	**49.4 %**	49.0 %	0.4
Delicados	**8.3 %**	9.7 %	(1.4)
Benson & Hedges	**5.0 %**	4.7 %	0.3
Others	**5.4 %**	5.9 %	(0.5)
Total	**68.1 %**	69.3 %	(1.2)

The estimated total cigarette market decreased by 1.1%, or increased by 1.2% excluding the net impact of estimated trade inventory movements. The decrease in our cigarette shipment volume mainly reflected the lower total cigarette market, as well as lower cigarette market share. The decrease of our cigarette market share largely reflected the net impact of the estimated trade inventory movements, as well as lower share of *Delicados*, impacted by competitive pressure in the low price segment.

2016 compared with 2015

The following discussion compares operating results within each of our reportable segments for 2016 with 2015.

Unless otherwise stated, references to total industry, total market, our shipment volume and our market share performance in the following discussion reflect cigarettes only.

European Union:

European Union (in millions)	For the Years Ended December 31, 2016	2015	Variance $	%
Net revenues	$ 27,129	$ 26,563	$ 566	2.1 %
Excise taxes on products	18,967	18,495	472	2.6 %
Net revenues, excluding excise taxes on products	8,162	8,068	94	1.2 %
Operating companies income	3,994	3,576	418	11.7 %

Net revenues increased by $566 million. Excluding excise taxes, net revenues increased by $94 million, due to:

- price increases ($390 million), partly offset by
- unfavorable volume/mix ($149 million) and
- unfavorable currency ($147 million).

Operating companies income increased by $418 million during 2016. This increase was due primarily to:

- price increases ($390 million),
- the non-recurrence of the 2015 pre-tax charges for asset impairment and exit costs ($68 million),
- lower manufacturing costs ($49 million),

- lower marketing, administration and research costs ($47 million) and
- favorable currency ($34 million), partly offset by
- unfavorable volume/mix ($168 million).

European Union - Industry Volume

The estimated total cigarette market decreased by 1.4% to 501.6 billion units. The moderate decline of the estimated total cigarette market reflected improved macroeconomics, a lower prevalence of illicit trade and, in certain geographies, the estimated positive impact of immigration, which was concentrated in the first half of 2016.

European Union - PMI Shipment Volume and Market Share Commentaries

Cigarette shipment volume and market share performance by brand are shown in the tables below:

European Union Cigarette Shipment Volume by Brand (Million Units)

	Full-Year		
	2016	**2015**	**Change**
Marlboro	96,245	95,588	0.7 %
L&M	34,691	35,010	(0.9 %)
Chesterfield	30,140	28,278	6.6 %
Philip Morris	16,290	14,205	14.7 %
Others	16,220	21,508	(24.6 %)
Total European Union	193,586	194,589	(0.5 %)

European Union Cigarette Market Shares by Brand

	Full-Year		
	2016	**2015**	**Change p.p.**
Marlboro	19.0 %	18.8 %	0.2
L&M	6.9 %	6.9 %	—
Chesterfield	5.9 %	5.6 %	0.3
Philip Morris	3.2 %	3.2 %	—
Others	3.3 %	3.8 %	(0.5)
Total European Union	38.3 %	38.3 %	—

Our cigarette shipment volume decreased by 0.5% to 193.6 billion units, mainly due to Italy, Germany and Greece, partly offset by Poland and Spain. Cigarette shipment volume of *Marlboro* increased by 0.7%, mainly driven by Spain, partly offset by Greece. Our total cigarette market share was flat at 38.3%, with gains, notably in the Czech Republic, France, Poland and Spain, offset by declines, mainly in Greece and Italy. Cigarette shipment volume of "Others" decreased, mainly due the morphing of various trademarks in the Czech Republic and Italy into international brands.

European Union - Key Market Commentaries

In **France**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

	France Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	44.9	45.5	(1.2 %)
PMI Cigarette Shipments (million units)	19,243	18,943	1.6 %
PMI Cigarette Market Share			
Marlboro	26.4 %	25.9 %	0.5
Philip Morris	10.2 %	9.5 %	0.7
Chesterfield	3.1 %	3.3 %	(0.2)
Others	2.7 %	2.9 %	(0.2)
Total	42.4 %	41.6 %	0.8

The estimated total cigarette market decreased moderately by 1.2%, partly reflecting a lower prevalence of illicit trade and e-vapor products. The increase in our cigarette shipment volume mainly reflected market share growth, driven by *Marlboro*, as well as the launch of certain *Philip Morris* variants in January 2016.

In **Germany**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

	Germany Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	78.1	80.0	(2.4 %)
PMI Cigarette Shipments (million units)	28,950	29,778	(2.8 %)
PMI Cigarette Market Share			
Marlboro	22.5 %	22.1 %	0.4
L&M	11.6 %	11.9 %	(0.3)
Chesterfield	1.6 %	1.5 %	0.1
Others	1.4 %	1.7 %	(0.3)
Total	37.1 %	37.2 %	(0.1)

The estimated total cigarette market decreased by 2.4%, primarily reflecting the impact of price increases. The decrease in our cigarette shipment volume primarily reflected the lower total market.

In **Italy**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

Italy Key Market Data

	Full-Year		
	2016	**2015**	**Change % / p.p.**
Total Cigarette Market (billion units)	72.1	73.8	(2.4%)
PMI Cigarette Shipments (million units)	38,624	39,717	(2.8%)
PMI Cigarette Market Share			
Marlboro	24.3%	24.7%	(0.4)
Chesterfield	11.5%	11.0%	0.5
Philip Morris	8.5%	9.2%	(0.7)
Others	8.1%	8.8%	(0.7)
Total	52.4%	53.7%	(1.3)

The estimated total cigarette market decreased by 2.4%, primarily reflecting the impact of price increases. The decline of our cigarette shipments, down by 4.8% excluding the net impact of distributor inventory movements, reflected the lower total market, and lower cigarette market share, notably due to *Marlboro* as a result of its price increase in the second quarter of 2016, and low-price *Philip Morris*, impacted by the growth of the super-low price segment, partly offset by super-low price *Chesterfield.*

In **Poland**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

Poland Key Market Data

	Full-Year		
	2016	**2015**	**Change % / p.p.**
Total Cigarette Market (billion units)	41.3	41.1	0.5%
PMI Cigarette Shipments (million units)	17,485	16,763	4.3%
PMI Cigarette Market Share			
Marlboro	11.6%	11.4%	0.2
L&M	18.5%	18.1%	0.4
Chesterfield	9.1%	8.6%	0.5
Others	3.1%	2.7%	0.4
Total	42.3%	40.8%	1.5

The estimated total cigarette market increased by 0.5%, primarily reflecting a lower prevalence of non-duty paid products. The increase in our cigarette shipment volume was mainly driven by higher cigarette market share, principally *L&M*, reflecting the positive impact of brand support, *Chesterfield*, benefiting from its 100s and super-slims variants, and *RGD* in "Others," up by 0.4 points to 2.6%.

In **Spain**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

	Spain Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	46.7	46.7	(0.1%)
PMI Cigarette Shipments (million units)	16,365	15,435	6.0 %
PMI Cigarette Market Share			
Marlboro	18.0%	17.0%	1.0
Chesterfield	8.6%	9.1%	(0.5)
L&M	5.4%	5.8%	(0.4)
Others	1.9%	1.5%	0.4
Total	33.9%	33.4%	0.5

The estimated total cigarette market decreased by 0.1%, reflecting an improved economy and the favorable estimated impact of in-switching from other tobacco products. Excluding the net impact of distributor inventory movements, our cigarette shipment volume increased by 1.6%, driven by higher market share reflecting the strong performance of *Marlboro*, benefiting from its round price point in the vending channel and the new Architecture 2.0.

Eastern Europe, Middle East & Africa:

Eastern Europe, Middle East & Africa (in millions)	For the Years Ended December 31, 2016	2015	Variance $	%
Net revenues	$ 18,286	$ 18,328	$ (42)	(0.2%)
Excise taxes on products	11,286	10,964	322	2.9 %
Net revenues, excluding excise taxes on products	7,000	7,364	(364)	(4.9%)
Operating companies income	3,016	3,425	(409)	(11.9%)

Net revenues decreased by $42 million. Excluding excise taxes, net revenues decreased by $364 million, due to:

- unfavorable currency ($600 million) and
- unfavorable volume/mix ($348 million), partly offset by
- price increases ($584 million).

Operating companies income decreased by $409 million during 2016. This decrease was due primarily to:

- unfavorable currency ($839 million) and
- unfavorable volume/mix ($333 million), partly offset by
- price increases ($584 million) and

- lower marketing, administration and research costs ($170 million).

Eastern Europe, Middle East & Africa - PMI Cigarette Shipment Volume Commentaries

Our cigarette shipment volume decreased by 2.9% to 271.4 billion units, mainly due to North Africa, primarily Algeria, and Russia, partially offset by Saudi Arabia and Ukraine. Cigarette shipment volume of *Marlboro* decreased by 8.5% to 73.8 billion units, principally due to Algeria and Egypt, partly offset by Saudi Arabia. Cigarette shipment volume of *Parliament* increased by 1.0% to 33.9 billion

units, driven by Saudi Arabia, Turkey and Ukraine, partly offset by Russia. Cigarette shipment volume of *L&M* increased by 1.9% to 52.2 billion units, driven notably by Algeria, Kazakhstan and Ukraine, partly offset by Russia and Turkey.

Eastern Europe, Middle East & Africa - Key Market Commentaries

In **North Africa**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

	North Africa Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	142.3	139.7	1.9 %
PMI Cigarette Shipments (million units)	34,035	38,111	(10.7 %)
PMI Cigarette Market Share			
Marlboro	8.3 %	13.6 %	(5.3)
L&M	12.2 %	11.8 %	0.4
Others	2.7 %	2.2 %	0.5
Total	23.2 %	27.6 %	(4.4)

The estimated total cigarette market increased by 1.9%, driven by Egypt, Morocco and Tunisia, partly offset by Algeria. The decrease in our cigarette shipment volume reflected lower market share, mainly due to *Marlboro* in Algeria, principally resulting from the impact of excise tax-driven price increases, as well as lower-than-anticipated acceptance of Architecture 2.0 for *Marlboro Round Taste.*

In **Russia**, estimated industry size, our cigarette shipment volume and market share performance, as measured by Nielsen, are shown in the table below.

	Russia Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	280.0	294.1	(4.8 %)
PMI Cigarette Shipments (million units)	79,651	84,422	(5.7 %)
PMI Cigarette Market Share			
Marlboro	1.4 %	1.4 %	—
Parliament	3.8 %	3.9 %	(0.1)
Bond Street	8.4 %	8.4 %	—
Others	13.6 %	14.7 %	(1.1)
Total	27.2 %	28.4 %	(1.2)

The estimated total cigarette market decreased by 4.8%, mainly due to the impact of excise tax-driven price increases. The decrease in our cigarette shipment volume, down by 8.3% excluding the impact of estimated distributor inventory movements, mainly reflected the lower total market, and lower cigarette market share primarily due to a decline in "Others" of mid-price *L&M* and *Chesterfield* and super-low *Optima*, resulting from the timing of retail price increases compared to competition.

In **Turkey**, estimated industry size, our cigarette shipment volume and market share performance, as measured by Nielsen, are shown in the table below.

	Turkey Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	105.5	103.2	2.2 %
PMI Cigarette Shipments (million units)	49,624	49,014	1.2 %
PMI Cigarette Market Share			
Marlboro	10.2 %	9.5 %	0.7
Parliament	11.7 %	11.6 %	0.1
Lark	7.4 %	7.6 %	(0.2)
Others	15.0 %	15.1 %	(0.1)
Total	44.3 %	43.8 %	0.5

The estimated total cigarette market increased by 2.2%, primarily reflecting a lower prevalence of illicit trade. The increase in our cigarette shipment volume was mainly driven by the higher total market. Our higher market share, led by *Marlboro*, primarily reflecting the growth of its slimmer *Touch* variant, and *Chesterfield*, partly offset by *L&M* in "Others."

In **Ukraine**, estimated industry size, our cigarette shipment volume and market share performance, as measured by Nielsen, are shown in the table below.

	Ukraine Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	73.1	70.6	3.5 %
PMI Cigarette Shipments (million units)	22,014	19,195	14.7 %
PMI Cigarette Market Share			
Marlboro	3.1 %	3.8 %	(0.7)
Parliament	2.9 %	2.8 %	0.1
Bond Street	10.0 %	8.2 %	1.8
Others	13.2 %	14.9 %	(1.7)
Total	29.2 %	29.7 %	(0.5)

The estimated total cigarette market increased by 3.5%, mainly driven by a lower prevalence of illicit trade. The increase in our cigarette shipment volume reflected the higher total cigarette market. The decrease in our market share was primarily due to *Marlboro*, reflecting the impact of widened price gaps, and mid-price *Chesterfield* and super-low *President* in "Others," mainly resulting from competitive price pressure in the low price segment, partly offset by *Bond Street* and *L&M* in "Others."

Asia:

Asia (in millions)	For the Years Ended December 31, 2016	2015	Variance $	%
Net revenues	$ 20,531	$ 19,469	$ 1,062	5.5%
Excise taxes on products	11,850	11,266	584	5.2%
Net revenues, excluding excise taxes on products	8,681	8,203	478	5.8%
Operating companies income	3,196	2,886	310	10.7%

Net revenues increased by $1.1 billion. Excluding excise taxes, net revenues increased by $478 million, due primarily to:

- price increases ($335 million) and
- favorable volume/mix ($151 million).

Net revenues include $666 million in 2016 related to sale of RRPs, mainly driven by Japan. Excluding excise taxes, net revenues for RRPs were $666 million in 2016. In some jurisdictions, including Japan, we are not responsible for collecting excise taxes.

Operating companies income increased by $310 million during 2016. This increase was due primarily to:

- price increases ($335 million),
- favorable currency ($52 million) and
- lower marketing, administration and research costs ($28 million), partly offset by
- unfavorable volume/mix ($106 million).

Asia - PMI Cigarette Shipment Volume Commentaries

Our cigarette shipment volume decreased by 7.6% to 260.0 billion units, mainly due to: Indonesia; Pakistan, reflecting a lower total estimated cigarette market resulting from excise tax-driven price increases and the growth of illicit trade; the Philippines; and Thailand, primarily reflecting the impact of excise tax-driven price increases in the first quarter of 2016, as well as lower market share; and in-switching from our cigarette brands to heated tobacco units; partly offset by Korea, reflecting a normalization of the total estimated cigarette market following the disruptive excise tax increase in January 2015.

Cigarette shipment volume of *Marlboro* increased by 4.0% to 76.5 billion units, mainly driven by Korea and the Philippines, partly offset by Vietnam, as well as in-switching from that brand to heated tobacco units. Cigarette shipment volume of *Parliament* increased by 7.5% to 10.1 billion units, driven by Korea. Cigarette shipment volume of *Lark* decreased by 3.8% to 17.6 billion units, principally due to Japan.

Asia - Key Market Commentaries

In **Indonesia**, estimated industry size, our cigarette shipment volume, market share and segmentation performance are shown in the tables below.

	Indonesia Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	315.6	320.0	(1.4%)
PMI Cigarette Shipments (million units)	105,524	109,840	(3.9%)
PMI Cigarette Market Share			
Sampoerna A	14.0%	14.6%	(0.6)
Dji Sam Soe	6.5%	6.9%	(0.4)
U Mild	4.2%	4.7%	(0.5)
Others	8.7%	8.1%	0.6
Total	33.4%	34.3%	(0.9)

	Indonesia Segmentation Data		
	Full-Year		
	2016	2015	Change p.p.
Segment % of Total Market			
Hand-Rolled Kretek (SKT)	18.2%	19.1%	(0.9)
Machine-Made Kretek (SKM)	75.8%	74.7%	1.1
Whites (SPM)	6.0%	6.2%	(0.2)
Total	100.0%	100.0%	—
PMI % Share of Segment			
Hand-Rolled Kretek (SKT)	37.3%	37.7%	(0.4)
Machine-Made Kretek (SKM)	28.9%	29.7%	(0.8)
Whites (SPM)	79.5%	80.3%	(0.8)

The estimated total cigarette market decreased by 1.4%, mainly reflecting a soft economic environment and the impact of excise tax-driven price increases. The decrease in our cigarette shipments was mainly due to lower market share, reflecting the soft performance of our SKM portfolio, due to competitors' discounted product offerings, and our SKT portfolio, broadly in line with industry trends, as well as a lower estimated total market.

In **Japan**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

	Japan Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	173.8	182.3	(4.6%)
PMI Cigarette Shipments (million units)	43,915	45,690	(3.9%)
PMI Cigarette Market Share			
Marlboro	10.9%	11.3%	(0.4)
Parliament	2.4%	2.3%	0.1
Lark	9.9%	9.9%	—
Others	1.7%	1.8%	(0.1)
Total	24.9%	25.3%	(0.4)

The estimated total cigarette market decreased by 4.6%, reflecting the continued underlying cigarette consumption decline, the growth of reduced-risk products, and the impact of the April price increases of certain brands of our key competitor. Excluding the net impact of distributor inventory movements, our cigarette shipment volume decreased by 6.5%. The decline was mainly due to a lower total cigarette market, as well as lower cigarette market share, reflecting the impact of competitors' retail pricing, competitors' differentiated menthol taste product offerings and in-switching from our cigarette brands to heated tobacco units.

The estimated national market share of heated tobacco units was 2.9%, bringing our total combined national market share to 27.1%, up by 1.7 points. We calculate national market share for heated tobacco units in Japan as the total sales volume for heated tobacco units as a percentage of the total estimated sales volume for cigarettes and heated tobacco units.

In **Korea**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

	Korea Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	73.6	67.3	9.4%
PMI Cigarette Shipments (million units)	15,490	14,201	9.1%
PMI Cigarette Market Share			
Marlboro	9.6%	9.6%	—
Parliament	7.9%	7.2%	0.7
Virginia S.	3.0%	3.8%	(0.8)
Others	0.5%	0.6%	(0.1)
Total	21.0%	21.2%	(0.2)

Excluding a favorable comparison with the prior year driven by estimated trade inventory movements, the estimated total cigarette market increased by 4.3%, reflecting the normalization of the market following the disruptive excise

tax increase of 120% in January 2015. The growth in our cigarette shipment volume primarily reflected the higher estimated total market.

In the **Philippines**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

	Philippines Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	79.3	90.2	(12.0%)
PMI Cigarette Shipments (million units)	56,611	66,236	(14.5%)
PMI Cigarette Market Share			
Marlboro	28.4%	20.0%	8.4
Fortune	23.4%	29.2%	(5.8)
Jackpot	7.9%	12.4%	(4.5)
Others	11.6%	11.8%	(0.2)
Total	71.3%	73.4%	(2.1)

The estimated total cigarette market decreased by 12.0%, mainly due to the impact of excise tax-driven price increases. The decline in our cigarette shipment volume reflected the lower total market, as well as the impact of these price increases on market share, particularly on our low and super-low price brands, *Fortune* and *Jackpot,* partly offset by an increase in market share of *Marlboro*, benefiting from its narrowed price gap with lower-priced brands as a result of the price increases.

Latin America & Canada:

Latin America & Canada (in millions)	For the Years Ended December 31, 2016	2015	Variance $	%
Net revenues	$ 9,007	$ 9,548	$ (541)	(5.7%)
Excise taxes on products	6,165	6,389	(224)	(3.5%)
Net revenues, excluding excise taxes on products	2,842	3,159	(317)	(10.0%)
Operating companies income	938	1,085	(147)	(13.5%)

Net revenues decreased by $541 million. Excluding excise taxes, net revenues decreased by $317 million, due to:

- unfavorable currency ($525 million) and
- unfavorable volume/mix ($104 million), partly offset by
- price increases ($312 million).

Operating companies income decreased by $147 million during 2016. This decrease was due to:

- unfavorable currency ($282 million),

- unfavorable volume/mix ($85 million),
- higher manufacturing costs ($57 million) and
- higher marketing, administration and research costs ($35 million), partly offset by
- price increases ($312 million).

Latin America & Canada - PMI Cigarette Shipment Volume Commentaries

Our cigarette shipment volume decreased by 4.3% to 87.9 billion units, mainly due to Argentina, partly offset by Mexico. While cigarette shipment volume of *Marlboro* decreased by 1.8% to 35.2 billion units, its market share increased by 0.6 points to an estimated 15.8%,

primarily driven by Brazil, up by 0.6 points to 10.3%, Colombia, up by 0.3 points to 9.3%, and Mexico, up by 1.2 points to 49.0%, partly offset by Argentina, down by 1.9 points to 22.4%. Cigarette shipment volume of *Philip Morris* decreased by 15.3% to 16.5 billion units, mainly due to Argentina.

Latin America & Canada - Key Market Commentaries

In **Argentina**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

	Argentina Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	36.1	40.8	(11.6%)
PMI Cigarette Shipments (million units)	27,512	31,910	(13.8%)
PMI Cigarette Market Share			
Marlboro	22.4%	24.3%	(1.9)
Parliament	1.9%	2.1%	(0.2)
Philip Morris	41.6%	44.7%	(3.1)
Others	10.4%	7.1%	3.3
Total	76.3%	78.2%	(1.9)

The decline of the estimated total cigarette market of 11.6% mainly reflected a soft economic environment and the impact of the May 2016 excise tax increase that drove a more than 50% increase in average industry retail prices. The decrease in our cigarette shipment volume was principally due to the lower total market. Our lower cigarette market share primarily reflected growth in competitors' super-low priced products benefiting from down-trading, partly offset by low-price *Chesterfield* in "Others." The capsule segment was up by 1.0 point to 17.4% of the total market; our share of the segment increased by 0.4 points to 73.9%.

In **Canada**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

	Canada Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	26.3	26.7	(1.6%)
PMI Cigarette Shipments (million units)	10,049	9,926	1.2 %
PMI Cigarette Market Share			
Belmont	3.7%	3.3%	0.4
Canadian Classics	10.2%	10.3%	(0.1)
Next	11.3%	10.6%	0.7
Others	13.2%	13.1%	0.1
Total	38.4%	37.3%	1.1

The estimated total cigarette market decreased by 1.6%. The increase in our cigarette shipment volume was principally driven by higher cigarette market share, favorably impacted by estimated trade inventory movements, partly offset by a lower total market.

In **Mexico**, estimated industry size, our cigarette shipment volume and market share performance are shown in the table below.

	Mexico Key Market Data		
	Full-Year		
	2016	2015	Change % / p.p.
Total Cigarette Market (billion units)	36.2	33.8	7.0%
PMI Cigarette Shipments (million units)	25,080	23,246	7.9%
PMI Cigarette Market Share			
Marlboro	49.0%	47.8%	1.2
Delicados	9.7%	10.7%	(1.0)
Benson & Hedges	4.7%	4.5%	0.2
Others	5.9%	5.8%	0.1
Total	69.3%	68.8%	0.5

The estimated total cigarette market increased by 7.0%, or by 2.2% excluding the net impact of estimated trade inventory movements, primarily reflecting improved market conditions and a lower prevalence of illicit trade. The increase in our cigarette shipment volume reflected the higher total market. Our cigarette market share, benefiting from the impact of estimated inventory movements, was up by 0.5 points, with growth of *Marlboro* and *Benson & Hedges*, reflecting the impact of new product launches, partly offset by low-price *Delicados*. Our share of the premium segment, representing 56.9% of the total market, increased by 1.0 point to 93.5%.

Financial Review

Ÿ Net Cash Provided by Operating Activities

Net cash provided by operating activities of $8.9 billion for the year ended December 31, 2017, increased by $0.8 billion from the comparable 2016 period. While the impacts of the Tax Cuts and Jobs Act reduced net earnings by $1.6 billion, there was no net impact on operating cash flows for the year, as the changes in deferred taxes and income taxes payable offset the net earnings impact. Excluding the impact of the Tax Cuts and Jobs Act as well as favorable currency movements of $0.4 billion, the increase in cash flows provided by operating activities can be attributed to higher net earnings offset by working capital and other movements.

At December 31, 2017, PMI recorded an income tax payable of $1.7 billion representing the transition tax of $2.2 billion, partially offset by foreign tax credits related to foreign withholding taxes previously paid of $0.5 billion. The income tax payable is due over an 8-year period beginning in 2018. For further details, see Item 8, Note 11. *Income Taxes* to our consolidated financial statements.

Net cash provided by operating activities of $8.1 billion for the year ended December 31, 2016, increased by $212 million from the comparable 2015 period. Excluding unfavorable currency movements of $409 million, the change was due primarily to net earnings growth and lower cash payments related to exit costs, partly offset by higher working capital requirements and 2016 installment payments of security into a court trust pertaining to the *Létourneau* and *Blais* cases as well as a 2016 payment to the South Korean tax authorities (see Item 8, Note 18. *Contingencies* for additional information).

Excluding currency, the unfavorable variance in working capital was due primarily to the following:

- more cash used for accounts receivable, primarily due to the timing of sales and cash collections (including unfavorable comparisons to the cash flows provided for accounts receivable in 2015 following the expansion of arrangements to sell accounts receivable to unaffiliated financial institutions as disclosed in Item 8, Note 20. *Sale of Accounts Receivable*), partly offset by

- more cash provided by accrued liabilities and other current assets, primarily due to the timing of payments for excise taxes.

Ÿ Net Cash Used in Investing Activities

Net cash used in investing activities of $3.0 billion for the year ended December 31, 2017, increased by $2.0 billion from the comparable 2016 period. This increase in net cash used of $2.0 billion was due principally to cash collateral posted to secure derivatives designated as net investment hedges of Euro assets following the strengthening of the Euro versus the U.S. dollar, and higher capital expenditures. For further details on our derivatives designated as net investment hedges, see Item 8, Note 15. *Financial Instruments*.

Net cash used in investing activities of $968 million for the year ended December 31, 2016, increased by $260 million from the comparable 2015 period, due primarily to higher capital expenditures.

Our capital expenditures were $1.5 billion in 2017, $1.2 billion in 2016 and $1.0 billion in 2015. The 2017 expenditures were primarily related to our ongoing investments in RRPs to support capacity expansion (notably for heated tobacco units). We expect total capital expenditures in 2018 of approximately $1.7 billion (including additional capital expenditures related to our ongoing investment in RRPs to support capacity expansion), to be funded by operating cash flows.

Ÿ Net Cash Used in Financing Activities

During 2017, net cash used in financing activities was $2.8 billion, compared with net cash used in financing activities of $5.4 billion during 2016 and $4.7 billion in 2015.

The 2017 change was due primarily to higher proceeds from long-term debt issuances (primarily the $6.9 billion proceeds in 2017 from our U.S. dollar and Euro debt issuances versus the $3.5 billion proceeds in 2016 from our U.S. dollar and Euro debt issuances).

The 2016 change was due primarily to lower net proceeds received from the sale of subsidiary shares to noncontrolling interests, partially offset by higher proceeds from long-term debt issuances. For further details on the proceeds from the sale of subsidiary shares in 2015, see Item 8, Note 6. *Acquisitions and Other Business Arrangements* to our consolidated financial statements.

Dividends paid in 2017, 2016 and 2015 were $6.5 billion, $6.4 billion and $6.3 billion, respectively.

Ÿ Debt and Liquidity

We define cash and cash equivalents as short-term, highly liquid investments, readily convertible to known amounts of cash that mature within a maximum of three months and have an insignificant risk of change in value due to interest rate or credit risk changes. As a policy, we do not hold any investments in structured or equity-linked products. Our cash and cash equivalents are predominantly held in demand deposits with institutions that have investment-grade long-term credit rating. As part of our cash management strategy and in order to manage counterparty exposure, we also enter into reverse repurchase agreements. Such agreements are collateralized with government or corporate securities held by a custodial bank and, at maturity, cash is paid back to PMI and the collateral is returned to the bank. While we entered into these agreements during the periods and had an average balance during 2017 and 2016 of $0.9 billion and $0.2 billion, respectively, we had a zero balance both at December 31, 2017 and December 31, 2016.

We utilize long-term and short-term debt financing, including a commercial paper program that is regularly used to finance ongoing liquidity requirements, as part of our overall cash management strategy. Our ability to access the capital and credit markets as well as overall dynamics of these markets may impact borrowing costs. We expect that the combination of our long-term and short-term debt financing, the commercial paper program and the committed credit facilities, coupled with our operating cash flows, will enable us to meet our liquidity requirements.

Credit Ratings – The cost and terms of our financing arrangements as well as our access to commercial paper markets may be affected by applicable credit ratings. At February 9, 2018, our credit ratings and outlook by major credit rating agencies were as follows:

	Short-term	Long-term	Outlook
Moody's	P-1	A2	Stable

Standard & Poor's	A-1	A	Negative
Fitch	F1	A	Negative

Credit Facilities – On January 29, 2018, we entered into an agreement to extend the term of our $2.0 billion 364-day revolving credit facility from February 6, 2018, to February 5, 2019. On August 29, 2017, we entered into an agreement, effective October 1, 2017, to

extend the term of our $3.5 billion multi-year revolving credit facility, for an additional year covering the period October 1, 2021 to October 1, 2022.

At February 9, 2018, our committed credit facilities were as follows:

(in billions)

Type	Committed Credit Facilities
364-day revolving credit, expiring February 5, 2019	**$ 2.0**
Multi-year revolving credit, expiring February 28, 2021	**2.5**
Multi-year revolving credit, expiring October 1, 2022	**3.5**
Total facilities	**$ 8.0**

At February 9, 2018, there were no borrowings under the committed credit facilities, and the entire committed amounts were available for borrowing.

All banks participating in our committed credit facilities have an investment-grade long-term credit rating from the credit rating agencies. We continuously monitor the credit quality of our banking group, and at this time we are not aware of any potential non-performing credit provider.

Each of these facilities requires us to maintain a ratio of consolidated earnings before interest, taxes, depreciation and amortization ("consolidated EBITDA") to consolidated interest expense of not less than 3.5 to 1.0 on a rolling four-quarter basis. At December 31, 2017, our ratio calculated in accordance with the agreements was 10.6 to 1.0. These facilities do not include any credit rating triggers, material adverse change clauses or any provisions that could require us to post collateral. We expect to continue to meet our covenants. The terms "consolidated EBITDA" and "consolidated interest expense," both of which include certain adjustments, are defined in the facility agreements previously filed with the U.S. Securities and Exchange Commission.

In addition to the committed credit facilities discussed above, certain of our subsidiaries maintain short-term credit arrangements to meet their respective working capital needs. These credit arrangements, which amounted to approximately $2.8 billion at December 31, 2017 and $2.9 billion at December 31, 2016, are for the sole use of our subsidiaries. Borrowings under these arrangements amounted to $499 million at December 31, 2017, and $643 million at December 31, 2016.

Commercial Paper Program – We continue to have access to liquidity in the commercial paper market through programs in place in the U.S. and in Europe having an aggregate issuance capacity of $8.0 billion. At December 31, 2017 and December 31, 2016, we had no commercial paper outstanding. The average commercial paper balance outstanding during 2017 and 2016 was $5.2 billion and $4.2 billion, respectively.

Sale of Accounts Receivable – To mitigate credit risk and enhance cash and liquidity management we sell trade receivables to unaffiliated financial institutions. These arrangements allow us to sell, on an ongoing basis, certain trade receivables without recourse. The trade receivables sold are generally short-term in nature and are removed from the consolidated balance sheets. We sell trade receivables under two types of arrangements, servicing and nonservicing.

Our operating cash flows were positively impacted by the amount of the trade receivables sold and derecognized from the consolidated balance sheets, which remained outstanding with the unaffiliated financial institutions. The trade receivables sold that remained outstanding under these arrangements as of December 31, 2017, 2016 and 2015 were $1,092 million, $729 million and $888 million, respectively. The net proceeds received are included in cash provided by operating activities in the consolidated statements of cash flows.

For further details, see Item 8, Note 20. *Sale of Accounts Receivable* to our consolidated financial statements.

Debt – Our total debt was $34.3 billion at December 31, 2017, and $29.1 billion at December 31, 2016. Our total debt is primarily fixed rate in nature. For further details, see Item 8, Note 7. *Indebtedness*. The weighted-average all-

in financing cost of our total debt was 2.6% in 2017, compared to 2.8% in 2016. See Item 8, Note 16. *Fair Value Measurements* to our consolidated financial statements for a discussion of our disclosures related to the fair value of debt. The amount of debt that we can issue is subject to approval by our Board of Directors.

On February 14, 2017, we filed a shelf registration statement with the U.S. Securities and Exchange Commission, under which we may from time to time sell debt securities and/or warrants to purchase debt securities over a three-year period.

Our debt issuances in 2017 were as follows:

(in millions)

Type		Face Value	Interest Rate	Issuance	Maturity
U.S. dollar notes	(a)	$700	1.625%	February 2017	February 2019
U.S. dollar notes	(b)	$300	Floating	February 2017	February 2020
U.S. dollar notes	(a)	$1,000	2.000%	February 2017	February 2020
U.S. dollar notes	(a)	$500	2.625%	February 2017	February 2022
U.S. dollar notes	(c)	$750	2.375%	August 2017	August 2022
U.S. dollar notes	(c)	$500	3.125%	August 2017	August 2027
U.S. dollar notes	(d)	$750	1.875%	November 2017	November 2019
U.S. dollar notes	(d)	$750	2.500%	November 2017	November 2022
U.S. dollar notes	(e)	$500	3.125%	November 2017	March 2028
EURO notes	(f)	€500 (approximately $582)	0.625%	November 2017	November 2024
EURO notes	(f)	€500 (approximately $582)	1.875%	November 2017	November 2037

(a) Interest on these notes is payable semi-annually in arrears beginning in August 2017.
(b) Interest on these notes is payable quarterly in arrears beginning in May 2017.
(c) Interest on these notes is payable semi-annually in arrears beginning in February 2018.
(d) Interest on these notes is payable semi-annually in arrears beginning May 2018.
(e) Interest on these notes is payable semi-annually in arrears beginning March 2018.
(f) Interest on these notes is payable annually in arrears beginning November 2018.

The net proceeds from the sale of the securities listed in the table above were used for general corporate purposes.

The weighted-average time to maturity of our long-term debt was 9.4 years at the end of 2017 and 10.6 years at the end of 2016.

- **Off-Balance Sheet Arrangements and Aggregate Contractual Obligations**

We have no off-balance sheet arrangements, including special purpose entities, other than guarantees and contractual obligations discussed below.

Guarantees – At December 31, 2017, we were contingently liable for $0.9 billion of guarantees of our own performance, which were primarily related to excise taxes on the shipment of our products. There is no liability in the consolidated financial statements associated with these guarantees. At December 31, 2017, our third-party guarantees were insignificant.

Aggregate Contractual Obligations – The following table summarizes our contractual obligations at December 31, 2017:

		Payments Due			
(in millions)	**Total**	**2018**	**2019-2020**	**2021-2022**	**2023 and Thereafter**
Long-term debt [1]	$34,120	$2,506	$8,221	$5,811	$17,582
Interest on borrowings [2]	11,131	981	1,656	1,372	7,122
Operating leases [3]	849	179	219	95	356
Purchase obligations [4]:					
Inventory and production costs	5,040	2,696	1,255	687	402
Other	2,230	1,437	588	194	11
	7,270	4,133	1,843	881	413
Other long-term liabilities [5]	468	58	60	42	308
	$53,838	$7,857	$11,999	$8,201	$25,781

[1] Amounts represent the expected cash payments of our long-term debt and capital lease obligations.

[2] Amounts represent the expected cash payments of our interest expense on our long-term debt, including the current portion of long-term debt. Interest on our fixed-rate debt is presented using the stated interest rate. Interest on our variable debt is estimated using the rate in effect at December 31, 2017. Amounts exclude the amortization of debt discounts, the amortization of loan fees and fees for lines of credit that would be included in interest expense in the consolidated statements of earnings.

[3] Amounts represent the minimum rental commitments under non-cancelable operating leases.

[4] Purchase obligations for inventory and production costs (such as raw materials, indirect materials and supplies, packaging, co-manufacturing arrangements, storage and distribution) are commitments for projected needs to be utilized in the normal course of business. Other purchase obligations include commitments for marketing, advertising, capital expenditures, information technology and professional services. Arrangements are considered purchase obligations if a contract specifies all significant terms, including fixed or minimum quantities to be purchased, a pricing structure and approximate timing of the transaction. Amounts represent the minimum commitments under non-cancelable contracts. Any amounts reflected on the consolidated balance sheet as accounts payable and accrued liabilities are excluded from the table above.

[5] Other long-term liabilities consist primarily of postretirement health care costs and accruals established for employment costs. The following long-term liabilities included on the consolidated balance sheet are excluded from the table above: accrued pension and postemployment costs, tax contingencies, insurance accruals and other accruals. We are unable to estimate the timing of payments (or contributions in the case of accrued pension costs) for these items. Currently, we anticipate making pension contributions of approximately $53 million in 2018, based on current tax and benefit laws (as discussed in Item 8, Note 13. *Benefit Plans* to our consolidated financial statements).

Ÿ **Equity and Dividends**

We discuss our stock awards as of December 31, 2017, in Item 8, Note 9. *Stock Plans* to our consolidated financial statements.

During 2017, 2016 and 2015, we did not repurchase any shares under a share repurchase program and we do not presently intend to repurchase shares of our common stock in 2018.

Dividends paid in 2017 were $6.5 billion. During the third quarter of 2017, our Board of Directors approved a 2.9% increase in the quarterly dividend to $1.07 per common share. As a result, the present annualized dividend rate is $4.28 per common share.

Market Risk

Ÿ ***Counterparty Risk -*** We predominantly work with financial institutions with strong short- and long-term credit ratings as assigned by Standard & Poor's and Moody's. These banks are also part of a defined group of relationship banks. Non-investment grade institutions are only used in certain emerging markets to the extent required by local business needs. We have a conservative approach when it comes to choosing financial counterparties and financial instruments. As such we do not invest or hold investments in any structured or equity-linked products. The majority of our cash and cash equivalents is currently invested in demand deposits maturing within less than 30 days.

We continuously monitor and assess the credit worthiness of all our counterparties.

Ÿ ***Derivative Financial Instruments -*** We operate in markets outside of the U.S., with manufacturing and sales facilities in various locations throughout the world. Consequently, we use certain financial instruments to manage our foreign currency and interest rate exposure. We use derivative financial instruments principally to reduce our exposure to market risks resulting from fluctuations in foreign

exchange rates by creating offsetting exposures. We are not a party to leveraged derivatives and, by policy, do not use derivative financial instruments for speculative purposes.

See Item 8, Note 15. *Financial Instruments,* Item 8, Note 16. *Fair Value Measurements* and Item 8, Note 19. *Balance Sheet Offsetting* to our consolidated financial statements for further details on our derivative financial instruments and the related collateral arrangements.

Ÿ ***Value at Risk*** **-** We use a value at risk computation to estimate the potential one-day loss in the fair value of our interest-rate-sensitive financial instruments and to estimate the potential one-day loss in pre-tax earnings of our foreign currency price-sensitive derivative financial instruments. This computation includes our debt, short-term investments, and foreign currency forwards, swaps and options. Anticipated transactions, foreign currency trade payables and receivables, and net investments in foreign subsidiaries, which the foregoing instruments are intended to hedge, were excluded from the computation.

The computation estimates were made assuming normal market conditions, using a 95% confidence interval. We use a "variance/co-variance" model to determine the observed interrelationships between movements in interest rates and various currencies. These interrelationships were determined by observing interest rate and forward currency rate movements over the preceding quarter for determining value at risk at December 31, 2017 and 2016, and over each of the four preceding quarters for the calculation of average value at risk amounts during each year. The values of foreign currency options do not change on a one-to-one basis with the underlying currency and were valued accordingly in the computation.

The estimated potential one-day loss in fair value of our interest-rate-sensitive instruments, primarily debt, under normal market conditions and the estimated potential one-day loss in pre-tax earnings from foreign currency instruments under normal market conditions, as calculated in the value at risk model, were as follows:

	Pre-Tax Earnings Impact			
(in millions)	**At 12/31/17**	**Average**	**High**	**Low**
Instruments sensitive to:				
Foreign currency rates	**$27**	**$49**	**$58**	**$27**

	Fair Value Impact			
(in millions)	**At 12/31/17**	**Average**	**High**	**Low**
Instruments sensitive to:				
Interest rates	**$118**	**$150**	**$173**	**$118**

	Pre-Tax Earnings Impact			
(in millions)	**At 12/31/16**	**Average**	**High**	**Low**
Instruments sensitive to:				
Foreign currency rates	$63	$58	$87	$34

	Fair Value Impact			
(in millions)	**At 12/31/16**	**Average**	**High**	**Low**
Instruments sensitive to:				
Interest rates	$143	$147	$217	$112

The value at risk computation is a risk analysis tool designed to statistically estimate the maximum probable daily loss from adverse movements in interest and foreign currency rates under normal market conditions. The computation does not purport to represent actual losses in fair value or earnings to be incurred by us, nor does it consider the effect of favorable changes in market rates. We cannot predict actual future movements in such market rates and do not present these results to be indicative of future movements in market rates or to be representative of any actual impact that future changes in market rates may have on our future results of operations or financial position.

Contingencies

See Item 3 and Item 8, Note 18. *Contingencies* to our consolidated financial statements for a discussion of contingencies.

Cautionary Factors That May Affect Future Results

Forward-Looking and Cautionary Statements

We may from time to time make written or oral forward-looking statements, including statements contained in filings with the SEC, in reports to stockholders and in press releases and investor webcasts. You can identify these forward-looking statements by use of words such as "strategy," "expects," "continues," "plans," "anticipates," "believes," "will," "estimates," "intends," "projects," "goals," "targets" and other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts.

We cannot guarantee that any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from those anticipated, estimated or projected. Investors should bear this in mind as they consider forward-looking statements and whether to invest in or remain invested in our securities. In connection with the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995, we are identifying important factors that, individually or in the aggregate, could cause actual results and outcomes to differ materially from those contained in any forward-looking statements made by us; any such statement is qualified by reference to the following cautionary statements. We elaborate on these and other risks we face throughout this document, particularly in Item 1A. *Risk Factors* and *Business Environment* of this section. You should understand that it is not possible to predict or identify all risk factors. Consequently, you should not consider the following to be a complete discussion of all potential risks or uncertainties. We do not undertake to update any forward-looking statement that we may make from time to time, except in the normal course of our public disclosure obligations.

Item 7A. *Quantitative and Qualitative Disclosures About Market Risk.*

The information called for by this Item is included in Item 7, *Market Risk*.

Item 8. *Financial Statements and Supplementary Data.*

Consolidated Balance Sheets
(in millions of dollars, except share data)

at December 31,	2017	2016
Assets		
Cash and cash equivalents	**$ 8,447**	$ 4,239
Receivables (less allowances of $30 in 2017 and $42 in 2016)	**3,738**	3,499
Inventories:		
Leaf tobacco	**2,606**	2,498
Other raw materials	**1,563**	1,569
Finished product	**4,637**	4,950
	8,806	9,017
Other current assets	**603**	853
Total current assets	**21,594**	17,608
Property, plant and equipment, at cost:		
Land and land improvements	**639**	590
Buildings and building equipment	**3,989**	3,474
Machinery and equipment	**8,976**	7,366
Construction in progress	**962**	930
	14,566	12,360
Less: accumulated depreciation	**7,295**	6,296
	7,271	6,064
Goodwill (Note 3)	**7,666**	7,324
Other intangible assets, net (Note 3)	**2,432**	2,470
Investments in unconsolidated subsidiaries (Note 4)	**1,074**	1,011
Deferred income taxes	**1,007**	859
Other assets	**1,924**	1,515
Total Assets	**$ 42,968**	$ 36,851

See notes to consolidated financial statements.

at December 31,	2017	2016
Liabilities		
Short-term borrowings (Note 7)	**$ 499**	$ 643
Current portion of long-term debt (Note 7)	**2,506**	2,573
Accounts payable	**2,242**	1,666
Accrued liabilities:		
Marketing and selling	**708**	575
Taxes, except income taxes	**5,324**	6,204
Employment costs	**856**	800
Dividends payable	**1,669**	1,621
Other	**1,346**	1,553
Income taxes (Note 11)	**812**	832
Total current liabilities	**15,962**	16,467
Long-term debt (Note 7)	**31,334**	25,851
Deferred income taxes	**799**	1,897
Employment costs	**2,271**	2,800
Income taxes and other liabilities (Note 11)	**2,832**	736
Total liabilities	**53,198**	47,751
Contingencies (Note 18)		
Stockholders' (Deficit) Equity		
Common stock, no par value (2,109,316,331 shares issued in 2017 and 2016)	**—**	—
Additional paid-in capital	**1,972**	1,964
Earnings reinvested in the business	**29,859**	30,397
Accumulated other comprehensive losses	**(8,535)**	(9,559)
	23,296	22,802
Less: cost of repurchased stock (556,098,569 and 557,930,784 shares in 2017 and 2016, respectively)	**35,382**	35,490
Total PMI stockholders' deficit	**(12,086)**	(12,688)
Noncontrolling interests	**1,856**	1,788
Total stockholders' deficit	**(10,230)**	(10,900)
Total Liabilities and Stockholders' (Deficit) Equity	**$ 42,968**	$ 36,851

See notes to consolidated financial statements.

Consolidated Statements of Earnings
(in millions of dollars, except per share data)

for the years ended December 31,	2017	2016	2015
Net revenues	**$ 78,098**	$ 74,953	$ 73,908
Cost of sales	**10,432**	9,391	9,365
Excise taxes on products	**49,350**	48,268	47,114
Gross profit	**18,316**	17,294	17,429
Marketing, administration and research costs	**6,725**	6,405	6,656
Asset impairment and exit costs	**—**	—	68
Amortization of intangibles	**88**	74	82
Operating income	**11,503**	10,815	10,623
Interest expense, net (Note 14)	**914**	891	1,008
Earnings before income taxes	**10,589**	9,924	9,615
Provision for income taxes (Note 11)	**4,307**	2,768	2,688
Equity (income)/loss in unconsolidated subsidiaries, net	**(59)**	(94)	(105)
Net earnings	**6,341**	7,250	7,032
Net earnings attributable to noncontrolling interests	**306**	283	159
Net earnings attributable to PMI	**$ 6,035**	$ 6,967	$ 6,873
Per share data (Note 10):			
Basic earnings per share	**$ 3.88**	$ 4.48	$ 4.42
Diluted earnings per share	**$ 3.88**	$ 4.48	$ 4.42

See notes to consolidated financial statements.

Consolidated Statements of Comprehensive Earnings
(in millions of dollars)

for the years ended December 31,	2017	2016	2015
Net earnings	**$ 6,341**	$ 7,250	$ 7,032
Other comprehensive earnings (losses), net of income taxes:			
Change in currency translation adjustments:			
Unrealized gains (losses), net of income taxes of $620 in 2017, ($101) in 2016 and ($143) in 2015	**330**	(14)	(2,248)
(Gains)/losses transferred to earnings, net of income taxes of $- in 2017, 2016 and 2015	**(2)**	5	(1)
Change in net loss and prior service cost:			
Net gains (losses) and prior service costs, net of income taxes of ($17) in 2017, $78 in 2016 and $17 in 2015	**523**	(460)	(536)
Amortization of net losses, prior service costs and net transition costs, net of income taxes of ($31) in 2017, ($43) in 2016 and ($48) in 2015	**228**	224	227
Change in fair value of derivatives accounted for as hedges:			
Gains (losses) recognized, net of income taxes of $8 in 2017, ($4) in 2016 and ($5) in 2015	**(44)**	8	38
(Gains) losses transferred to earnings, net of income taxes of $2 in 2017, ($3) in 2016 and $14 in 2015	**(11)**	30	(102)
Total other comprehensive earnings (losses)	**1,024**	(207)	(2,622)
Total comprehensive earnings	**7,365**	7,043	4,410
Less comprehensive earnings attributable to:			
Noncontrolling interests	**306**	233	113
Comprehensive earnings attributable to PMI	**$ 7,059**	$ 6,810	$ 4,297

See notes to consolidated financial statements.

Consolidated Statements of Stockholders' (Deficit) Equity

(in millions of dollars, except per share data)

	PMI Stockholders' (Deficit) Equity						
	Common Stock	Additional Paid-in Capital	Earnings Reinvested in the Business	Accumulated Other Comprehensive Losses	Cost of Repurchased Stock	Noncontrolling Interests	Total
Balances, January 1, 2015	$ —	$ 710	$ 29,249	$ (6,826)	$ (35,762)	$ 1,426	$ (11,203)
Net earnings			6,873			159	7,032
Other comprehensive earnings (losses), net of income taxes				(2,576)		(46)	(2,622)
Issuance of stock awards		(3)			149		146
Dividends declared ($4.04 per share)			(6,280)				(6,280)
Payments to noncontrolling interests						(171)	(171)
Sale (purchase) of subsidiary shares to/(from) noncontrolling interests (Note 6)		1,222				400	1,622
Balances, December 31, 2015	—	1,929	29,842	(9,402)	(35,613)	1,768	(11,476)
Net earnings			6,967			283	7,250
Other comprehensive earnings (losses), net of income taxes				(157)		(50)	(207)
Issuance of stock awards		37			123		160
Dividends declared ($4.12 per share)			(6,412)				(6,412)
Payments to noncontrolling interests						(219)	(219)
Other		(2)				6	4
Balances, December 31, 2016	—	1,964	30,397	(9,559)	(35,490)	1,788	(10,900)
Net earnings			**6,035**			**306**	**6,341**
Other comprehensive earnings (losses), net of income taxes				**1,024**		**—**	**1,024**
Issuance of stock awards		**20**			**108**		**128**
Dividends declared ($4.22 per share)			**(6,573)**				**(6,573)**
Payments to noncontrolling interests						**(255)**	**(255)**
Other		**(12)**				**17**	**5**
Balances, December 31, 2017	**$ —**	**$ 1,972**	**$ 29,859**	**$ (8,535)**	**$ (35,382)**	**$ 1,856**	**$ (10,230)**

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(in millions of dollars)

for the years ended December 31,	2017	2016	2015
CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES			
Net earnings	**$ 6,341**	$ 7,250	$ 7,032
Adjustments to reconcile net earnings to operating cash flows:			
Depreciation and amortization	**875**	743	754
Deferred income tax (benefit) provision	**(501)**	182	(18)
Asset impairment and exit costs, net of cash paid	**(10)**	(31)	(164)
Cash effects of changes in:			
Receivables, net	**(92)**	(1,009)	647
Inventories	**730**	(695)	(841)
Accounts payable	**425**	373	310
Accrued liabilities and other current assets	**(554)**	1,477	(8)
Income taxes	**1,370**	(209)	(42)
Pension plan contributions	**(66)**	(191)	(154)
Other	**394**	187	349
Net cash provided by operating activities	**8,912**	8,077	7,865
CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES			
Capital expenditures	**(1,548)**	(1,172)	(960)
Investments in unconsolidated subsidiaries	**(111)**	(41)	(55)
Net investment hedges	**(1,527)**	295	239
Other	**172**	(50)	68
Net cash used in investing activities	**(3,014)**	(968)	(708)

See notes to consolidated financial statements.

for the years ended December 31,	2017	2016	2015
CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES			
Short-term borrowing activity by original maturity:			
Net repayments - maturities of 90 days or less	**$ (127)**	$ (12)	$ (266)
Issuances - maturities longer than 90 days	**1,634**	—	—
Repayments - maturities longer than 90 days	**(1,634)**	—	—
Long-term debt proceeds	**6,850**	3,536	1,539
Long-term debt repaid	**(2,551)**	(2,393)	(1,229)
Repurchases of common stock	**—**	—	(48)
Dividends paid	**(6,520)**	(6,378)	(6,250)
Sale (purchase) of subsidiary shares to/(from) noncontrolling interests (Note 6)	**5**	7	1,622
Other	**(426)**	(173)	(104)
Net cash used in financing activities	**(2,769)**	(5,413)	(4,736)
Effect of exchange rate changes on cash and cash equivalents	**1,079**	(874)	(686)
Cash and cash equivalents:			
Increase	**4,208**	822	1,735
Balance at beginning of year	**4,239**	3,417	1,682
Balance at end of year	**$ 8,447**	$ 4,239	$ 3,417
Cash Paid:			
Interest	**$ 1,050**	$ 1,052	$ 1,045
Income taxes	**$ 3,403**	$ 2,829	$ 2,771

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Note 1.

Background and Basis of Presentation:

Background

Philip Morris International Inc. is a holding company incorporated in Virginia, U.S.A., whose subsidiaries and affiliates and their licensees are engaged in the manufacture and sale of cigarettes and other nicotine-containing products, including reduced-risk products, in markets outside of the United States of America. Throughout these financial statements, the term "PMI" refers to Philip Morris International Inc. and its subsidiaries.

Reduced-risk products ("RRPs") is the term PMI uses to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continued smoking. PMI has a range of RRPs in various stages of development, scientific assessment and commercialization.

Basis of presentation

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities at the dates of the financial statements and the reported amounts of net revenues and expenses during the reporting periods. Significant estimates and assumptions include, among other things: pension and benefit plan assumptions; useful lives and valuation assumptions of goodwill and other intangible assets; marketing programs, and income taxes. Actual results could differ from those estimates.

The consolidated financial statements include PMI, as well as its wholly-owned and majority-owned subsidiaries. Investments in which PMI exercises significant influence (generally 20%-50% ownership interest) are accounted for under the equity method of accounting. Investments in which PMI has an ownership interest of less than 20%, or does not exercise significant influence, are accounted for under the cost method of accounting. All intercompany transactions and balances have been eliminated.

Certain prior years' amounts have been reclassified to conform with the current year's presentation, due primarily to the aggregation of the U.S. and non-U.S. pension plans in Note 13. *Benefit Plans*.

Note 2.

Summary of Significant Accounting Policies:

Cash and cash equivalents

Cash equivalents include demand deposits with banks and all highly liquid investments with original maturities of three months or less.

Depreciation

Property, plant and equipment are stated at historical cost and depreciated by the straight-line method over the estimated useful lives of the assets. Machinery and equipment are depreciated over periods ranging from 3 to 15 years, and buildings and building improvements over periods up to 40 years.

Employee benefit plans

PMI provides a range of benefits to its employees and retired employees, including pensions, postretirement health care and postemployment benefits (primarily severance). PMI records annual amounts relating to these plans based on calculations specified under U.S. GAAP. PMI recognizes the funded status of its defined pension and postretirement plans on the consolidated balance sheets. The funded status is measured as the difference between the fair value of the plans assets and the benefit obligation. PMI measures the plan assets and liabilities at the end of the fiscal year. For defined benefit pension plans, the benefit obligation is the projected benefit obligation. For the postretirement health care plans, the benefit obligation is the accumulated postretirement benefit obligation. Any plan with an overfunded status is recognized as an asset, and any plan with an underfunded status is recognized as a liability. Any gains or losses and prior service costs or credits that have not been recognized as a component of net periodic benefit costs are recorded as a component of other comprehensive earnings (losses), net of deferred taxes. PMI elects to recognize actuarial gains/(losses) using the corridor approach.

Foreign currency translation

PMI translates the results of operations of its subsidiaries and affiliates using average exchange rates during each period, whereas balance sheet accounts are translated using exchange rates at the end of each period. Currency translation adjustments are recorded as a component of stockholders' (deficit) equity. In addition, some of PMI's subsidiaries have assets and liabilities denominated in currencies other than their functional currencies, and to the extent those are not designated as net investment hedges, these assets and liabilities generate transaction gains and losses when translated into their respective functional currencies.

Goodwill and non-amortizable intangible assets valuation

PMI tests goodwill and non-amortizable intangible assets for impairment annually or more frequently if events occur that would warrant such review. PMI performs its annual impairment analysis in the second quarter of each year. The impairment analysis involves comparing the fair value of each reporting unit or non-amortizable intangible asset to the carrying value. If the carrying value exceeds the fair value, goodwill or a non-amortizable intangible asset is considered impaired.

Hedging instruments

Derivative financial instruments are recorded at fair value on the consolidated balance sheets as either assets or liabilities. Changes in the fair value of derivatives are recorded each period either in accumulated other comprehensive losses on the consolidated balance sheet, or in earnings, depending on whether a derivative is designated and effective as part of a hedge transaction and, if it is, the type of hedge transaction. Gains and losses on derivative instruments reported in accumulated other comprehensive losses are reclassified to the consolidated statements of earnings in the periods in which operating results are affected by the hedged item. Cash flows from hedging instruments are classified in the same manner as the affected hedged item in the consolidated statements of cash flows.

Impairment of long-lived assets

PMI reviews long-lived assets, including amortizable intangible assets, for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable. PMI performs undiscounted operating cash flow analyses to determine if an impairment exists. For purposes of recognition and measurement of an impairment for assets held for use, PMI groups assets and liabilities at the lowest level for which cash flows are separately identifiable. If an impairment is determined to exist, any related impairment loss is calculated based on fair value. Impairment losses on assets to be disposed of, if any, are based on the estimated proceeds to be received, less costs of disposal.

Impairment of investments in unconsolidated subsidiaries

Investments in unconsolidated subsidiaries are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of the investments may not be recoverable. An impairment loss would be recorded whenever a decline in value of an equity investment below its carrying amount is determined to be other than temporary. PMI determines whether a loss is other than temporary by considering the length of time and extent to which the fair value of the equity investment has been less than the carrying amount, the financial

condition of the equity investment, and the intent to retain the investment for a period of time is sufficient to allow for any anticipated recovery in market value.

Income taxes

Income taxes are provided on all earnings for jurisdictions outside the United States. These provisions, as well as state and local income tax provisions, are determined on a separate company basis, and the related assets and liabilities are recorded in PMI's consolidated balance sheets. Significant judgment is required in determining income tax provisions and in evaluating tax positions. PMI recognizes

accrued interest and penalties associated with uncertain tax positions as part of the provision for income taxes on the consolidated statements of earnings.

Inventories

Inventories are stated at the lower of cost or market. The first-in, first-out and average cost methods are used to cost substantially all inventories. It is a generally recognized industry practice to classify leaf tobacco inventory as a current asset, although part of such inventory, because of the duration of the aging process, ordinarily would not be utilized within one year.

Marketing costs

PMI supports its products with advertising, adult consumer engagement and trade promotions. Such programs include, but are not limited to, discounts, rebates, in-store display incentives, e-commerce, mobile and other digital platforms, adult consumer activation and promotion activities, as well as costs associated with adult consumer experience outlets and other adult consumer touchpoints and volume-based incentives. Advertising, as well as certain consumer engagement and trade activities costs, are expensed as incurred. Trade promotions are recorded as a reduction of revenues based on amounts estimated as being due to customers at the end of a period, based principally on historical utilization. For interim reporting purposes, advertising and certain consumer engagement expenses are charged to earnings based on estimated sales and related expenses for the full year.

Revenue recognition

PMI recognizes revenues, net of sales incentives and including shipping and handling charges billed to customers, either upon shipment or delivery of goods when title and risk of loss pass to customers. Excise taxes billed by PMI to customers are reported in net revenues. Shipping and handling costs are classified as part of cost of sales. Estimated costs associated with warranty programs are generally provided for in cost of sales in the period the related revenues are recognized.

On May 28, 2014, the Financial Accounting Standards Board issued Accounting Standards Update ASU 2014-09, "Revenue from Contracts with Customers." For further details, see Note 21. *New Accounting Standards*.

Stock-based compensation

PMI measures compensation cost for all stock-based awards at fair value on date of grant and recognizes the compensation costs over the service periods for awards expected to vest. PMI's accounting policy is to estimate the number of awards expected to be forfeited and adjust the expense when it is no longer probable that the employee will fulfill the service condition. For further details, see Note 9. *Stock Plans*.

Note 3.

Goodwill and Other Intangible Assets, net:

Goodwill and other intangible assets, net, by segment were as follows:

	Goodwill		Other Intangible Assets, net	
(in millions)	**December 31, 2017**	**December 31, 2016**	**December 31, 2017**	**December 31, 2016**
European Union	**$ 1,419**	$ 1,238	**$ 458**	$ 479
Eastern Europe, Middle East & Africa	**423**	372	**194**	200
Asia	**3,577**	3,596	**1,048**	1,074
Latin America & Canada	**2,247**	2,118	**732**	717

Total	**$ 7,666**	$ 7,324	**$ 2,432**	$ 2,470

Goodwill primarily reflects PMI's acquisitions in Canada, Colombia, Greece, Indonesia, Mexico, Pakistan and Serbia, as well as the business combination in the Philippines.

The movements in goodwill were as follows:

(in millions)	European Union	Eastern Europe, Middle East & Africa	Asia	Latin America & Canada	Total
Balance at January 1, 2016	$ 1,310	$ 374	$ 3,581	$ 2,150	$ 7,415
Changes due to:					
Currency	(72)	(2)	15	(32)	(91)
Balance at December 31, 2016	1,238	372	3,596	2,118	7,324
Changes due to:					
Currency	**181**	**51**	**(19)**	**129**	**342**
Balance at December 31, 2017	**$ 1,419**	**$ 423**	**$ 3,577**	**$ 2,247**	**$ 7,666**

Additional details of other intangible assets were as follows:

	December 31, 2017		December 31, 2016	
(in millions)	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Non-amortizable intangible assets	**$ 1,323**		$ 1,455	
Amortizable intangible assets	**1,798**	**$ 689**	1,598	$ 583
Total other intangible assets	**$ 3,121**	**$ 689**	$ 3,053	$ 583

Non-amortizable intangible assets substantially consist of trademarks from PMI's acquisitions in Indonesia in 2005 and Mexico in 2007. Amortizable intangible assets primarily consist of certain trademarks and distribution networks associated with business combinations. During the first quarter of 2017, PMI reclassified three trademarks with a gross carrying amount of $153 million from non-amortizable intangible assets to amortizable intangible assets. The gross carrying amount, the range of useful lives as well as the weighted-average remaining useful life of amortizable intangible assets at December 31, 2017, were as follows:

Description (dollars in millions)	Gross Carrying Amount	Initial Estimated Useful Lives	Weighted-Average Remaining Useful Life
Trademarks	**$ 1,559**	2 - 40 years	19 years
Distribution networks	**152**	5 - 30 years	9 years
Other (including farmer contracts and intellectual property rights)	**87**	4 - 17 years	9 years

	$ 1,798

Pre-tax amortization expense for intangible assets during the years ended December 31, 2017, 2016 and 2015, was $88 million, $74 million and $82 million, respectively. Amortization expense for each of the next five years is estimated to be $84 million or less, assuming no additional transactions occur that require the amortization of intangible assets.

The increase in the gross carrying amount of other intangible assets from December 31, 2016, was primarily due to currency movements.

During the second quarter of 2017, PMI completed its annual review of goodwill and non-amortizable intangible assets for potential impairment, and no impairment charges were required as a result of this review. Additionally, PMI elected to early adopt Accounting

Standards Update ASU 2017-04 “Intangibles-Goodwill and Other (Topic 350) Simplifying the Test for Goodwill Impairment,” which had no impact on PMI's impairment review or conclusion.

Note 4.

Investments in Unconsolidated Subsidiaries:

At December 31, 2017 and 2016, PMI had total investments in unconsolidated subsidiaries of $1,074 million and $1,011 million, respectively, which were accounted for under the equity method of accounting. Equity method investments are initially recorded at cost. Under the equity method of accounting, the investment is adjusted for PMI's proportionate share of earnings or losses and movements in currency translation adjustments. The carrying value of our equity method investments at December 31, 2017 and 2016 exceeded our share of the unconsolidated subsidiaries' book value by $927 million and $867 million, respectively. The difference between the investment carrying value and the amount of underlying equity in net assets, excluding $873 million and $810 million attributable to goodwill as of December 31, 2017 and 2016, respectively, is being amortized on a straight-line basis over the underlying assets' estimated useful lives of 10 to 20 years. At December 31, 2017 and 2016, PMI received year-to-date dividends from unconsolidated subsidiaries of $120 million and $117 million, respectively.

PMI holds a 49% equity interest in United Arab Emirates-based Emirati Investors-TA (FZC) (“EITA”). PMI holds an approximate 25% economic interest in Société des Tabacs Algéro-Emiratie (“STAEM”), an Algerian joint venture that is 51% owned by EITA and 49% by the Algerian state-owned enterprise Société Nationale des Tabacs et Allumettes SpA. STAEM manufactures and distributes under license some of PMI’s brands.

PMI holds a 23% equity interest in Megapolis Distribution BV, the holding company of CJSC TK Megapolis, PMI's distributor in Russia.

The initial investments in EITA and Megapolis Distribution BV were recorded at cost and are included in investments in unconsolidated subsidiaries on the consolidated balance sheets.

PMI’s earnings activity from unconsolidated subsidiaries was as follows:

	For the Years Ended December 31,	
(in millions)	**2017**	**2016**
Net revenues	**$ 4,425**	$ 3,985

PMI’s balance sheet activity related to unconsolidated subsidiaries was as follows:

	At December 31,	
(in millions)	**2017**	**2016**
Receivables	**$ 293**	$ 289

The activity primarily related to agreements with PMI’s unconsolidated subsidiaries within the Eastern Europe, Middle East & Africa segment. These agreements, which are in the ordinary course of business, are primarily for distribution, contract manufacturing and licenses. PMI eliminated its respective share of all significant intercompany transactions with the equity method investees.

Note 5.

Product Warranty:

PMI's *IQOS* devices are subject to standard product warranties generally for a period of 12 months from the date of purchase or such other periods as required by law. Estimated costs associated with warranty programs are generally provided for in cost of sales in the period the related revenue is recognized, and during 2017, PMI recorded $168 million associated with these product warranty programs. PMI assesses the adequacy of its accrued warranty liabilities and adjusts the amounts as necessary based on actual experience and changes in future estimates. Factors

that affect warranty obligations may vary across markets but typically include product failure rates, logistics and service delivery costs, and warranty policies. At December 31, 2017, $71 million was accrued related to these warranty obligations within other accrued liabilities.

Note 6.

Acquisitions and Other Business Arrangements:

As announced in June 2015, PMI's subsidiary PT HM Sampoerna Tbk. ("Sampoerna"), of which PMI held a 98.18% interest, was required to comply with the January 30, 2014, Indonesian Stock Exchange ("IDX") regulation requiring all listed public companies to have at least a 7.5% public shareholding by January 30, 2016. In order to comply with this requirement, Sampoerna conducted a rights issue (the "Rights Issue"). The exercise price for the rights was set at Rp. 77,000 per share, a 1.349% premium to the closing price on the IDX as of September 30, 2015. In connection with the Rights Issue, PT Philip Morris Indonesia ("PMID"), a fully consolidated subsidiary of PMI, sold 264,209,711 of the rights to third-party investors. Delivery of the rights sold took place on October 26, 2015. The total net proceeds from the Rights Issue were $1.5 billion at prevailing exchange rates on the closing date. The sale of the rights resulted in an increase to PMI's additional paid-in capital of $1.1 billion.

Note 7.

Indebtedness:

Short-Term Borrowings

At December 31, 2017 and 2016, PMI's short-term borrowings and related average interest rates consisted of the following:

	December 31, 2017		December 31, 2016	
(in millions)	Amount Outstanding	Average Year-End Rate	Amount Outstanding	Average Year-End Rate
Commercial paper	**$ —**	**— %**	$ —	— %
Bank loans	**499**	**5.7**	643	5.0
	$ 499		$ 643	

Given the mix of subsidiaries and their respective local economic environments, the average interest rate for bank loans above can vary significantly from day to day and country to country.

The fair values of PMI's short-term borrowings at December 31, 2017 and 2016, based upon current market interest rates, approximate the amounts disclosed above.

Long-Term Debt

At December 31, 2017 and 2016, PMI's long-term debt consisted of the following:

	December 31,	
(in millions)	2017	2016
U.S. dollar notes, 1.375% to 6.375% (average interest rate 3.560%), due through 2044	**$ 23,291**	$ 19,857
Foreign currency obligations:		
Euro notes, 0.625% to 3.125% (average interest rate 2.250%), due through 2037	**8,997**	6,828
	1,376	1,312

Swiss franc notes, 0.750% to 2.000% (average interest rate 1.269%), due through 2024		
Other (average interest rate 3.421%), due through 2024	**176**	427
	33,840	28,424
Less current portion of long-term debt	**2,506**	2,573
	$ 31,334	$ 25,851

Other debt:

Other foreign currency debt above includes mortgage debt in Switzerland and capital lease obligations at December 31, 2017 and December 31, 2016. Other foreign currency debt above also includes a bank loan in the Philippines at December 31, 2016.

Debt Issuances Outstanding:

PMI's debt issuances outstanding at December 31, 2017, were as follows:

(in millions)

Type	Face Value	Interest Rate	Issuance	Maturity
U.S. dollar notes	**$2,500**	**5.650%**	May 2008	May 2018
U.S. dollar notes	**$750**	**1.875%**	November 2013	January 2019
U.S. dollar notes	**$700**	**1.625%**	February 2017	February 2019
U.S. dollar notes	**$500**	**1.375%**	February 2016	February 2019
U.S. dollar notes	**$750**	**1.875%**	November 2017	November 2019
U.S. dollar notes	**$300**	**Floating**	February 2017	February 2020
U.S. dollar notes	**$1,000**	**2.000%**	February 2017	February 2020
U.S. dollar notes	**$1,000**	**4.500%**	March 2010	March 2020
U.S. dollar notes	**$750**	**1.875%**	February 2016	February 2021
U.S. dollar notes	**$350**	**4.125%**	May 2011	May 2021
U.S. dollar notes	**$750**	**2.900%**	November 2011	November 2021
U.S. dollar notes	**$500**	**2.625%**	February 2017	February 2022
U.S. dollar notes	**$750**	**2.375%**	August 2017	August 2022
U.S. dollar notes	**$750**	**2.500%**	August 2012	August 2022
U.S. dollar notes	**$750**	**2.500%**	November 2017	November 2022
U.S. dollar notes	**$600**	**2.625%**	March 2013	March 2023
U.S. dollar notes	**$500**	**2.125%**	May 2016	May 2023
U.S. dollar notes	**$500**	**3.600%**	November 2013	November 2023
U.S. dollar notes	**$750**	**3.250%**	November 2014	November 2024
U.S. dollar notes	**$750**	**3.375%**	August 2015	August 2025
U.S. dollar notes	**$750**	**2.750%**	February 2016	February 2026
U.S. dollar notes	**$500**	**3.125%**	August 2017	August 2027
U.S. dollar notes	**$500**	**3.125%**	November 2017	March 2028
U.S. dollar notes	**$1,500**	**6.375%**	May 2008	May 2038
U.S. dollar notes	**$750**	**4.375%**	November 2011	November 2041
	$700	**4.500%**	March 2012	March 2042

U.S. dollar notes					
U.S. dollar notes		**$750**	**3.875%**	August 2012	August 2042
U.S. dollar notes		**$850**	**4.125%**	March 2013	March 2043
U.S. dollar notes		**$750**	**4.875%**	November 2013	November 2043
U.S. dollar notes		**$750**	**4.250%**	November 2014	November 2044
U.S. dollar notes	(a)	**$500**	**4.250%**	May 2016	November 2044
EURO notes	(b)	**€750 (approximately $951)**	**2.125%**	May 2012	May 2019
EURO notes	(b)	**€1,250 (approximately $1,621)**	**1.750%**	March 2013	March 2020
EURO notes	(b)	**€750 (approximately $1,029)**	**1.875%**	March 2014	March 2021
EURO notes	(b)	**€600 (approximately $761)**	**2.875%**	May 2012	May 2024
EURO notes	(b)	**€500 (approximately $582)**	**0.625%**	November 2017	November 2024
EURO notes	(b)	**€750 (approximately $972)**	**2.750%**	March 2013	March 2025
EURO notes	(b)	**€1,000 (approximately $1,372)**	**2.875%**	March 2014	March 2026
EURO notes	(b)	**€500 (approximately $697)**	**2.875%**	May 2014	May 2029

(in millions)

Type		Face Value	Interest Rate	Issuance	Maturity
EURO notes	(b)	**€500 (approximately $648)**	**3.125%**	June 2013	June 2033
EURO notes	(b)	**€500 (approximately $578)**	**2.000%**	May 2016	May 2036
EURO notes	(b)	**€500 (approximately $582)**	**1.875%**	November 2017	November 2037
Swiss franc notes	(b)	**CHF200 (approximately $217)**	**0.875%**	March 2013	March 2019
Swiss franc notes	(b)	**CHF275 (approximately $311)**	**0.750%**	May 2014	December 2019
Swiss franc notes	(b)	**CHF325 (approximately $334)**	**1.000%**	September 2012	September 2020
Swiss franc notes	(b)	**CHF300 (approximately $335)**	**2.000%**	December 2011	December 2021
Swiss franc notes	(b)	**CHF250 (approximately $283)**	**1.625%**	May 2014	May 2024

(a) These notes are a further issuance of the 4.250% notes issued by PMI in November 2014.
(b) USD equivalents for foreign currency notes were calculated based on exchange rates on the date of issuance.

The net proceeds from the sale of the securities listed in the table above were used for general corporate purposes, including working capital requirements and repurchase of PMI's common stock until 2015.

Aggregate maturities:

Aggregate maturities of long-term debt are as follows:

(in millions)

2018	$ 2,506
2019	4,091
2020	4,130
2021	3,056
2022	2,755
2023-2027	8,144
2028-2032	1,097
Thereafter	8,341
	34,120
Debt discounts	(280)

Total long-term debt	$ 33,840

See Note 16. *Fair Value Measurements* for additional disclosures related to the fair value of PMI's debt.

Credit Facilities

On January 27, 2017, PMI entered into an agreement to extend the term of its $2.0 billion 364-day revolving credit facility from February 7, 2017 to February 6, 2018. On August 29, 2017, PMI entered into an agreement, effective October 1, 2017, to extend the term of its $3.5 billion multi-year revolving credit facility, for an additional year covering the period October 1, 2021 to October 1, 2022.

At December 31, 2017, PMI's total committed credit facilities and commercial paper outstanding were as follows:

Type (in billions of dollars)	Committed Credit Facilities	Commercial Paper
364-day revolving credit, expiring February 6, 2018	**$ 2.0**	
Multi-year revolving credit, expiring February 28, 2021	**2.5**	
Multi-year revolving credit, expiring October 1, 2022	**3.5**	
Total facilities	**$ 8.0**	
Commercial paper outstanding		**$ —**

At December 31, 2017, there were no borrowings under these committed credit facilities, and the entire committed amounts were available for borrowing.

On January 29, 2018, PMI entered into an agreement to extend the term of its $2.0 billion 364-day revolving credit facility from February 6, 2018, to February 5, 2019.

Each of these facilities requires PMI to maintain a ratio of consolidated earnings before interest, taxes, depreciation and amortization ("consolidated EBITDA") to consolidated interest expense of not less than 3.5 to 1.0 on a rolling four-quarter basis. At December 31, 2017, PMI's ratio calculated in accordance with the agreements was 10.6 to 1.0. These facilities do not include any credit rating triggers, material adverse change clauses or any provisions that could require PMI to post collateral. The terms "consolidated EBITDA" and "consolidated interest expense," both of which include certain adjustments, are defined in the facility agreements previously filed with the Securities and Exchange Commission.

In addition to the committed credit facilities discussed above, certain subsidiaries maintain short-term credit arrangements to meet their respective working capital needs. These credit arrangements, which amounted to approximately $2.8 billion at December 31, 2017 and $2.9 billion at December 31, 2016, are for the sole use of the subsidiaries. Borrowings under these arrangements amounted to $499 million at December 31, 2017, and $643 million at December 31, 2016.

Note 8.

Capital Stock:

Shares of authorized common stock are 6.0 billion; issued, repurchased and outstanding shares were as follows:

	Shares Issued	Shares Repurchased	Shares Outstanding
Balances, January 1, 2015	2,109,316,331	(562,416,635)	1,546,899,696
Issuance of stock awards		2,444,373	2,444,373
Balances, December 31, 2015	2,109,316,331	(559,972,262)	1,549,344,069
Issuance of stock awards		2,041,478	2,041,478
Balances, December 31, 2016	2,109,316,331	(557,930,784)	1,551,385,547
Issuance of stock awards		**1,832,215**	**1,832,215**
Balances, December 31, 2017	**2,109,316,331**	**(556,098,569)**	**1,553,217,762**

At December 31, 2017, 31,246,310 shares of common stock were reserved for stock awards under PMI's stock plans, and 250 million shares of preferred stock, without par value, were authorized but unissued. PMI currently has no plans to issue any shares of preferred stock.

Note 9.

Stock Plans:

In May 2017, PMI's shareholders approved the Philip Morris International Inc. 2017 Performance Incentive Plan (the "2017 Plan"). The 2017 Plan replaced the 2012 Performance Incentive Plan, and there will be no additional grants under the replaced plan. Under the 2017 Plan, PMI may grant to eligible employees restricted shares and restricted share units, performance-based cash incentive awards and performance-based equity awards. Up to 25 million shares of PMI's common stock may be issued under the 2017 Plan. At December 31, 2017, shares available for grant under the 2017 Plan were 24,991,850.

In May 2017, PMI's shareholders also approved the Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors (the "2017 Non-Employee Directors Plan"). The 2017 Non-Employee Directors Plan replaced the 2008 Stock Compensation Plan for Non-Employee Directors, and there will be no additional grants under the replaced plan. A non-employee director is defined as a member of the PMI Board of Directors who is not a full-time employee of PMI or of any corporation in which PMI owns, directly or indirectly, stock possessing at least 50% of the total combined voting power of all classes of stock entitled to vote in the election of directors in such corporation. Up to 1 million shares of PMI common stock may be awarded under the 2017 Non-Employee Directors Plan. As of December 31, 2017, shares available for grant under the plan were 1,000,000.

Restricted share unit (RSU) awards

PMI may grant RSU awards to eligible employees; recipients may not sell, assign, pledge or otherwise encumber such awards. Such awards are subject to forfeiture if certain employment conditions are not met. RSU awards generally vest on the third anniversary of the grant date. RSU awards do not carry voting rights, although they do earn dividend equivalents.

During 2017, the activity for RSU awards was as follows:

	Number of Shares	Weighted-Average Grant Date Fair Value Per Share
Balance at January 1, 2017	**4,500,990**	**$ 82.08**
Granted	**1,210,210**	**98.59**
Vested	**(2,022,856)**	**78.19**
Forfeited	**(75,944)**	**88.82**
Balance at December 31, 2017	**3,612,400**	**$ 89.65**

During the years ended December 31, 2017, 2016 and 2015, the weighted-average grant date fair value of the RSU awards granted to PMI employees and the recorded compensation expense related to RSU awards were as follows:

(in millions, except per RSU award granted)	Total Weighted-Average Grant Date Fair Value of RSU Awards Granted	Weighted-Average Grant Date Fair Value Per RSU Award Granted	Compensation Expense related to RSU Awards
2017	**$ 119**	**$ 98.59**	**$ 111**
2016	$ 108	$ 89.03	$ 126

2015	$ 126	$ 82.28	$ 166

The fair value of the RSU awards at the date of grant is amortized to expense over the restriction period, typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2017, PMI had $108 million of total unrecognized compensation costs related to non-vested RSU awards. These costs are expected to be recognized over a weighted-average period of two years, or upon death, disability or reaching the age of 58.

During the years ended December 31, 2017, 2016 and 2015, share and fair value information for PMI RSU awards that vested were as follows:

(dollars in millions)	Shares of RSU Awards that Vested	Grant Date Fair Value of Vested Shares of RSU Awards	Total Fair Value of RSU Awards that Vested
2017	**2,022,856**	**$ 158**	**$ 208**
2016	2,302,525	$ 202	$ 210
2015	2,711,974	$ 217	$ 224

Performance share unit (PSU) awards

PMI may grant PSU awards to certain executives; recipients may not sell, assign, pledge or otherwise encumber such awards. The PSU awards require the achievement of certain performance factors, which are predetermined at the time of grant, over a three-year performance cycle. PMI's performance metrics consist of PMI's Total Shareholder Return (TSR) relative to a predetermined peer group and on an absolute basis, PMI's currency-neutral compound annual adjusted operating companies income growth rate, excluding acquisitions, and PMI's performance against specific measures of PMI's innovation and transformation. The aggregate of the weighted performance factors for the three metrics determines the percentage of PSUs that will vest at the end of the three-year performance cycle. The minimum percentage of PSUs that can vest is zero, with a target percentage of 100 and a maximum percentage of 200. Each vested PSU entitles the participant to one share of common stock. An aggregate weighted PSU performance factor of 100 will result in the targeted number of PSUs being vested. At the end of the performance cycle, participants are entitled to an amount equivalent to the accumulated dividends paid on common stock during the performance cycle for the number of shares earned. PSU awards do not carry voting rights.

During 2017, the activity for PSU awards was as follows:

	Number of Shares	Grant Date Fair Value Subject to TSR Performance Factor Per Share[a]	Grant Date Fair Value Subject to Other Performance Factors Per Share[b]
Balance at January 1, 2017	**427,570**	**$ 104.60**	**$ 89.02**
Granted	**393,460**	**128.72**	**98.29**
Vested	—	—	—
Forfeited	—	—	—
Balance at December 31, 2017	**821,030**	**$ 116.16**	**$ 93.46**

[a] The grant date fair value of the PSU market based awards subject to the TSR performance factor was determined by using the Monte Carlo simulation model.

[b] The grant date fair value of the PSU awards subject to the other performance factors was determined by using the average of the high and low market price of PMI's stock at the date of grant.

During the years ended December 31, 2017 and 2016, the grant date fair value of the PSU awards granted to PMI employees and the recorded compensation expense related to PSU awards were as follows:

(in millions, except per PSU award granted)	PSU Grant Date Fair Value Subject to TSR Performance Factor[a]	PSU Grant Date Fair Value Subject to Other Performance Factors[b]	Compensation Expense related to PSU Awards
	Total	**Total**	**Total**

		Per PSU Award		Per PSU Award	
2017	**$ 25**	**$ 128.72**	**$ 19**	**$ 98.29**	**$ 37**
2016	$ 22	$ 104.60	$ 19	$ 89.02	$ 27

(a) The grant date fair value of the PSU market based awards subject to the TSR performance factor was determined by using the Monte Carlo simulation model.

(b) The grant date fair value of the PSU awards subject to the other performance factors was determined by using the average of the high and low market price of PMI's stock at the date of grant.

The fair value of the PSU award at the date of grant is amortized to expense over the performance period, which is typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2017, PMI had $34 million of total unrecognized compensation cost related to non-vested PSU awards. This cost is recognized over a weighted-average performance cycle period of two years, or upon death, disability or reaching the age of 58.

During the years ended December 31, 2017, and 2016, there were no PSU awards that vested. PMI did not grant any PSU awards during 2015.

Note 10.

Earnings per Share:

Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are participating securities and therefore are included in PMI's earnings per share calculation pursuant to the two-class method.

Basic and diluted earnings per share ("EPS") were calculated using the following:

	For the Years Ended December 31,		
(in millions)	**2017**	**2016**	**2015**
Net earnings attributable to PMI	**$ 6,035**	$ 6,967	$ 6,873
Less distributed and undistributed earnings attributable to share-based payment awards	**14**	19	24
Net earnings for basic and diluted EPS	**$ 6,021**	$ 6,948	$ 6,849
Weighted-average shares for basic EPS	**1,552**	1,551	1,549
Plus contingently	**1**	—	—

issuable performance stock units (PSUs)			
Weighted-average shares for diluted EPS	**1,553**	1,551	1,549

For the 2017, 2016 and 2015 computations, there were no antidilutive stock options.

Note 11.

Income Taxes:

Earnings before income taxes and provision for income taxes consisted of the following for the years ended December 31, 2017, 2016 and 2015:

(in millions)	2017	2016	2015
Earnings before income taxes	**$ 10,589**	$ 9,924	$ 9,615
Provision for income taxes:			
United States federal and state:			
Current	**$ 1,662**	$ (39)	$ (56)
Deferred	**(384)**	293	117
Total United States	**1,278**	254	61
Outside United States:			
Current	**3,146**	2,625	2,762
Deferred	**(117)**	(111)	(135)
Total outside United States	**3,029**	2,514	2,627
Total provision for income taxes	**$ 4,307**	$ 2,768	$ 2,688

United States income tax is primarily attributable to repatriation costs.

In December 2017, the Tax Cuts and Jobs Act was signed into law. The principal elements of the Tax Cuts and Jobs Act relevant to PMI's consolidated financial statements for the year ended December 31, 2017, were:

- A reduction of the U.S. federal corporate tax rate from 35% to 21%; and

- The requirement to pay a one-time transition tax on accumulated foreign earnings, including 2017 earnings ("transition tax").

In connection with these elements of the Tax Cuts and Jobs Act, PMI recognized a provisional expense of $1.6 billion, which was included as a component of income tax expense as follows:

- A provisional charge of $1.4 billion, which represents the transition tax of $2.2 billion, net of a reversal of $0.7 billion of previously recorded deferred tax liabilities on part of the accumulated foreign earnings, and other items of $0.1 billion.

- Re-measurement of U.S. deferred tax assets and liabilities using a rate of 21%, which, under the Tax Cuts and Jobs Act, is expected to be in place when such deferred assets and liabilities reverse in the future. In connection with this re-measurement, PMI recorded a provisional charge of $0.2 billion.

Other provisions of the Tax Cuts and Jobs Act did not have a significant impact on PMI’s consolidated financial statements for the year ended December 31, 2017, but may impact the effective tax rate in subsequent periods.

The Tax Cuts and Jobs Act has significant complexity and our final tax liability may materially differ from these estimates, due to, among other things, changes in PMI's assumptions, guidance that may be issued by the U.S. Treasury Department and the Internal Revenue Service and related interpretations and clarifications of tax law. For the transition tax, further information is required to finalize the estimated amount of accumulated foreign earnings as well as to validate the amount of earnings represented by the aggregate foreign cash position as defined in the Tax Cuts and Jobs Act. For the re-measurement of the deferred tax assets and liabilities, further analysis will be required to refine PMI's calculations and related account balances.

PMI will complete the remaining elements of its analysis during 2018, and any adjustments to the provisional charges will be included in income tax expense or benefit in the appropriate period, in accordance with guidance provided by Staff Accounting Bulletin No. 118 (SAB 118).

At December 31, 2017, U.S. federal and foreign deferred income taxes have been provisionally provided on all accumulated earnings of PMI's foreign subsidiaries.

At December 31, 2017, PMI recorded an income tax payable of $1.7 billion attributable to the Tax Cuts and Jobs Act, of which $1.6 billion was recorded in "income taxes and other liabilities" on PMI's consolidated balance sheet. The income tax payable of $1.7 billion represented the transition tax of $2.2 billion, partially offset by foreign tax credits related to foreign withholding taxes previously paid of $0.5 billion. The income tax payable is due over an 8-year period beginning in 2018.

A reconciliation of the beginning and ending amount of unrecognized tax benefits was as follows:

(in millions)	2017	2016	2015
Balance at January 1,	**$ 79**	$ 88	$ 123
Additions based on tax positions related to the current year	**71**	13	17
Additions for tax positions of previous years	**5**	1	6
Reductions for tax positions of prior years	**—**	(7)	(42)
Reductions due to lapse of statute of limitations	**(7)**	(14)	(7)
Settlements	**(4)**	(2)	(1)
Other	**1**	—	(8)
Balance at December 31,	**$ 145**	$ 79	$ 88

Unrecognized tax benefits and PMI's liability for contingent income taxes, interest and penalties were as follows:

(in millions)	December 31, 2017	December 31, 2016	December 31, 2015
Unrecognized tax benefits	**$ 145**	$ 79	$ 88
Accrued interest and penalties	**23**	15	28
Tax credits and other indirect benefits	**(35)**	(31)	(40)
Liability for tax contingencies	**$ 133**	$ 63	$ 76

The amount of unrecognized tax benefits that, if recognized, would impact the effective tax rate was $110 million at December 31, 2017. The remainder, if recognized, would principally affect deferred taxes.

For the years ended December 31, 2017, 2016 and 2015, PMI recognized income (expense) in its consolidated statements of earnings of $(11) million, $13 million and $3 million, respectively, related to interest and penalties.

PMI is regularly examined by tax authorities around the world and is currently under examination in a number of jurisdictions. The U.S. federal statute of limitations remains open for the years 2013 and onward. Foreign and U.S. state jurisdictions have statutes of limitations generally ranging from three to five years. Years still open to examination by foreign tax authorities in major jurisdictions include Germany (2015 onward), Indonesia (2014 onward), Russia (2015 onward) and Switzerland (2017 onward).

It is reasonably possible that within the next 12 months certain tax examinations will close, which could result in a change in unrecognized tax benefits, along with related interest and penalties. An estimate of any possible change cannot be made at this time.

The effective income tax rate on pre-tax earnings differed from the U.S. federal statutory rate for the following reasons for the years ended December 31, 2017, 2016 and 2015:

	2017	2016	2015

U.S. federal statutory rate	**35.0 %**	35.0 %	35.0 %
Increase (decrease) resulting from:			
Foreign rate differences	**(12.2)**	(12.6)	(12.3)
Dividend repatriation cost	**16.4**	5.8	5.7
Other	**1.5**	(0.3)	(0.4)
Effective tax rate	**40.7 %**	27.9 %	28.0 %

The 2017 effective tax rate increased 12.8 percentage points to 40.7%. The change in the effective tax rate for 2017, as compared to 2016, was primarily due to the Tax Cuts and Jobs Act. In addition to the transition tax, which resulted in a net tax charge of $1.4 billion, the Tax Cuts and Jobs Act also included a reduction in the U.S. income tax rate from 35% to 21%, as of January 1, 2018. This change in income tax rate required a re-measurement of PMI's U.S. deferred tax assets and liabilities at December 31, 2017, resulting in a tax charge of $0.2 billion.

The 2016 effective tax rate decreased 0.1 percentage point to 27.9%. The change in the effective tax rate for 2016, as compared to 2015, was primarily due to earnings mix by taxing jurisdiction and repatriation cost differences.

The 2015 effective tax rate decreased 1.1 percentage points to 28.0%. The effective tax rate for 2015 was unfavorably impacted by changes to repatriation assertions on certain foreign subsidiary historical earnings ($58 million), partially offset by the recognition of tax benefits of $41 million following the conclusion of the IRS examinations of Altria's consolidated tax returns for the years 2007 and 2008 and PMI's consolidated tax returns for the years 2009 through 2011. Prior to March 28, 2008, PMI was a wholly-owned subsidiary of Altria. Excluding the effect of these items, the change in the effective tax rate for 2015, as compared to 2014, was primarily due to earnings mix by taxing jurisdiction and repatriation cost differences.

The tax effects of temporary differences that gave rise to deferred income tax assets and liabilities consisted of the following:

(in millions)	At December 31, 2017	At December 31, 2016
Deferred income tax assets:		
Accrued postretirement and postemployment benefits	**$ 239**	$ 287
Accrued pension costs	**334**	256
Inventory	**131**	241
Accrued liabilities	**117**	137
Foreign exchange	**91**	—
Other	**114**	173
Total deferred income tax assets	**1,026**	1,094
Deferred income tax liabilities:		
Trade names	**(546)**	(554)
Property, plant and equipment	**(223)**	(217)
Unremitted earnings	**(49)**	(636)
Foreign exchange	**—**	(725)
Total deferred income tax liabilities	**(818)**	(2,132)
Net deferred income tax assets (liabilities)	**$ 208**	$ (1,038)

Note 12.

Segment Reporting:

PMI's subsidiaries and affiliates are engaged in the manufacture and sale of cigarettes and other nicotine-containing products, including RRPs, in markets outside of the United States of America. Reportable segments for PMI are organized by geographic region and managed by segment managers who are responsible for the operating and financial results of the regions inclusive of all product categories sold in the region. PMI's reportable segments are the European Union; Eastern Europe, Middle East & Africa; Asia; and Latin America & Canada for all periods presented in these financial statements. PMI records net revenues and operating companies income to its segments based upon the geographic area in which the customer resides.

PMI's chief operating decision maker evaluates segment performance and allocates resources based on regional operating companies income, which includes results from all product categories sold in each region. PMI defines operating companies income as operating income, excluding general corporate expenses and amortization of intangibles, plus equity (income)/loss in unconsolidated subsidiaries, net. General corporate expenses include amounts relating to central functions that provide strategic direction and support for activities including new product and market launches across the product portfolio. Interest expense, net, and provision for income taxes are centrally managed and, accordingly, such items are not presented by segment since they are excluded from the measure of segment profitability

reviewed by management. Information about total assets by segment is not disclosed because such information is not reported to or used by PMI's chief operating decision maker. Segment goodwill and other intangible assets, net, are disclosed in Note 3. *Goodwill and Other Intangible Assets, net.* The accounting policies of the segments are the same as those described in Note 2. *Summary of Significant Accounting Policies.*

Segment data were as follows:

(in millions)	For the Years Ended December 31,		
	2017	**2016**	**2015**
Net revenues:			
European Union	**$ 27,580**	$ 27,129	$ 26,563
Eastern Europe, Middle East & Africa	**18,045**	18,286	18,328
Asia	**22,635**	20,531	19,469
Latin America & Canada	**9,838**	9,007	9,548
Net revenues[1]	**$ 78,098**	$ 74,953	$ 73,908

[1] Total net revenues attributable to customers located in Indonesia, PMI's largest market in terms of net revenues, were $8.0 billion, $7.7 billion and $7.1 billion for the years ended December 31, 2017, 2016 and 2015, respectively. Total net revenues attributable to customers located in Germany were $7.2 billion, $7.1 billion and $7.2 billion for the years ended December 31, 2017, 2016 and 2015, respectively.

(in millions)	For the Years Ended December 31,		
	2017	**2016**	**2015**
Earnings before income taxes:			
Operating companies income:			
European Union	**$ 3,775**	$ 3,994	$ 3,576
Eastern Europe, Middle East & Africa	**2,888**	3,016	3,425
Asia	**4,149**	3,196	2,886
Latin America & Canada	**1,002**	938	1,085
Amortization of intangibles	**(88)**	(74)	(82)
General corporate expenses	**(164)**	(161)	(162)
Less:			
Equity (income)/loss in unconsolidated subsidiaries, net	**(59)**	(94)	(105)
Operating income	**11,503**	10,815	10,623
Interest expense, net	**(914)**	(891)	(1,008)
Earnings before income taxes	**$ 10,589**	$ 9,924	$ 9,615

(in millions)	For the Years Ended December 31,		
	2017	**2016**	**2015**
Depreciation expense:			

European Union	**$ 213**	$ 184	$ 184
Eastern Europe, Middle East & Africa	**164**	150	163
Asia	**313**	247	230
Latin America & Canada	**85**	79	85
	775	660	662
Other	**12**	9	10
Total depreciation expense	**$ 787**	$ 669	$ 672

(in millions)	For the Years Ended December 31, 2017	2016	2015
Capital expenditures:			
European Union	**$ 956**	$ 665	$ 497
Eastern Europe, Middle East & Africa	**182**	223	147
Asia	**227**	180	185
Latin America & Canada	**175**	103	130
	1,540	1,171	959
Other	**8**	1	1
Total capital expenditures	**$ 1,548**	$ 1,172	$ 960

(in millions)	At December 31, 2017	2016	2015
Long-lived assets:			
European Union	**$ 4,130**	$ 3,282	$ 3,129
Eastern Europe, Middle East & Africa	**976**	866	743
Asia	**2,078**	1,916	1,743
Latin America & Canada	**885**	765	605
Total long-lived assets	**8,069**	6,829	6,220
Other	**1,126**	750	644
Total property, plant and equipment, net and Other assets	**$ 9,195**	$ 7,579	$ 6,864

Long-lived assets consist of non-current assets other than goodwill; other intangible assets, net; deferred tax assets, investments in unconsolidated subsidiaries, and financial instruments. PMI's largest markets in terms of long-lived assets are Italy, Switzerland and Indonesia. Total long-lived assets located in Italy, which is reflected in the European Union segment above, were $1.2 billion, $0.7 billion and $0.4 billion at December 31, 2017, 2016 and 2015, respectively. Total long-lived assets located in Switzerland, which is reflected in the European Union segment above, were $0.9 billion, $0.9 billion and $0.9 billion at December 31, 2017, 2016 and 2015, respectively. Total long-lived assets located in Indonesia, which is reflected in the Asia segment above, were $0.8 billion, $0.8 billion and $0.7 billion at December 31, 2017, 2016 and 2015, respectively.

Note 13.

Benefit Plans:

Pension coverage for employees of PMI's subsidiaries is provided, to the extent deemed appropriate, through separate plans, many of which are plans outside of the U.S., which are governed by local statutory requirements, and to a lesser extent U.S. plans that are closed to new participants. In addition, PMI provides health care and other

benefits to substantially all U.S. retired employees and certain non-U.S. retired employees. In general, health care benefits for non-U.S. retired employees are covered through local government plans.

Pension and Postretirement Benefit Plans

Obligations and Funded Status

The postretirement health care plans are not funded. The projected benefit obligations, plan assets and funded status of PMI's pension plans, and the accumulated benefit obligation and net amount accrued for PMI's postretirement health care plans, at December 31, 2017 and 2016, were as follows:

	Pension[1]		Postretirement	
(in millions)	**2017**	**2016**	**2017**	**2016**
Benefit obligation at January 1,	**$ 8,387**	$ 8,086	**$ 227**	$ 211
Service cost	**208**	207	**4**	3
Interest cost	**108**	146	**8**	9
Benefits paid	**(226)**	(240)	**(10)**	(10)
Settlement and curtailment	**—**	(1)	**—**	—
Actuarial losses (gains)	**(93)**	427	**12**	15
Currency	**621**	(329)	**7**	(2)
Other	**23**	91	**—**	1
Benefit obligation at December 31,	**9,028**	8,387	**248**	227
Fair value of plan assets at January 1,	**6,457**	6,404		
Actual return on plan assets	**742**	322		
Employer contributions	**66**	191		
Employee contributions	**40**	39		
Benefits paid	**(226)**	(240)		
Settlement and curtailment	**—**	—		
Currency	**519**	(259)		
Fair value of plan assets at December 31,	**7,598**	6,457		
Net pension and postretirement liability recognized at December 31,	**$ (1,430)**	$ (1,930)	**$ (248)**	$ (227)

(1) Primarily non-U.S. based defined benefit retirement plans.

At December 31, 2017 and 2016, the Swiss pension plan represented 57% and 57% of the benefit obligation, respectively, and approximately 57% of the fair value of plan assets for each of the years. At December 31, 2017 and 2016, the U.S. pension plan represented 5% and 5% of the benefit obligation, respectively, and approximately 4% and 5% of the fair value of plan assets at December 31, 2017 and 2016, respectively.

At December 31, 2017 and 2016, the amounts recognized on PMI's consolidated balance sheets for the pension and postretirement plans were as follows:

	Pension	Postretirement

(in millions)	2017	2016	2017	2016
Other assets	**$ 47**	$ 33		
Accrued liabilities — employment costs	**(26)**	(23)	**$ (10)**	$ (10)
Long-term employment costs	**(1,451)**	(1,940)	**(238)**	(217)
	$ (1,430)	$ (1,930)	**$ (248)**	$ (227)

The accumulated benefit obligation, which represents benefits earned to date, for the pension plans was $8,496 million and $7,931 million at December 31, 2017 and 2016, respectively.

For pension plans with accumulated benefit obligations in excess of plan assets, the projected benefit obligation, accumulated benefit obligation and fair value of plan assets were $7,287 million, $6,953 million and $5,835 million, respectively, as of December 31, 2017. The projected benefit obligation, accumulated benefit obligation and fair value of plan assets were $6,934 million, $6,622 million and $5,009 million, respectively, as of December 31, 2016.

The following weighted-average assumptions were used to determine PMI's pension and postretirement benefit obligations at December 31:

	Pension		Postretirement	
	2017	**2016**	**2017**	**2016**
Discount rate	**1.51 %**	1.52 %	**3.79 %**	3.68 %
Rate of compensation increase	**1.65**	1.68		
Health care cost trend rate assumed for next year			**6.17**	7.15
Ultimate trend rate			**4.62**	5.08
Year that rate reaches the ultimate trend rate			**2029**	2029

The discount rate for the largest pension plans is based on a yield curve constructed from a portfolio of high quality corporate bonds that produces a cash flow pattern equivalent to each plan's expected benefit payments. The discount rate for the remaining plans is developed from local bond indices that match local benefit obligations as closely as possible.

Components of Net Periodic Benefit Cost

Net periodic pension and postretirement health care costs consisted of the following for the years ended December 31, 2017, 2016 and 2015:

	Pension			Postretirement		
(in millions)	**2017**	**2016**	**2015**	**2017**	**2016**	**2015**
Service cost	**$ 208**	$ 207	$ 205	**$ 4**	$ 3	$ 4
Interest cost	**108**	146	156	**8**	9	9
Expected return on plan assets	**(326)**	(346)	(340)	**—**	—	—
Amortization:						
Net losses	**186**	186	194	**5**	2	4
Prior service cost	**6**	4	4	**—**	—	—
Settlement and curtailment	**6**	4	3	**—**	—	—
Net periodic pension and postretirement costs	**$ 188**	$ 201	$ 222	**$ 17**	$ 14	$ 17

As of December 31, 2016, PMI elected to change the method used to calculate the service and interest cost components of the net periodic pension benefit costs. Historically, these costs were determined utilizing a single weighted-average discount rate based on a yield curve used to measure the benefit obligation at the beginning of the period. As of January 1, 2017, PMI utilized a full yield curve approach in the estimation of the service and interest costs by applying the specific spot rates along the yield curve to the relevant projected cash flows. Specifically, service costs were determined based on duration-specific spot rates applied to service cost cash flows, and interest costs were determined by applying duration-specific spot rates to the year-by-year projected benefit payments. PMI

changed to the new method to provide a more precise measurement of service and interest costs by improving the correlation between the projected benefit cash flows to the corresponding spot rates along the yield curve. PMI accounted for this change as a change in accounting estimate on a prospective basis. This change did not affect the measurement of PMI's pension plan obligations and did not have a material impact on PMI's consolidated results of operations, financial position or cash flows.

Settlement and curtailment charges were due primarily to early retirement programs.

For the pension plans, the estimated net loss and prior service cost that are expected to be amortized from accumulated other comprehensive earnings into net periodic benefit cost during 2018 are $171 million and $2 million, respectively.

The following weighted-average assumptions were used to determine PMI's net pension and postretirement health care costs:

	Pension			Postretirement		
	2017	**2016**	**2015**	**2017**	**2016**	**2015**
Discount rate - service cost	**1.68 %**	1.81 %	2.04 %	**3.68 %**	4.45 %	4.20 %
Discount rate - interest cost	**1.27**	1.81	2.04	**3.68**	4.45	4.20
Expected rate of return on plan assets	**4.80**	5.36	5.38			
Rate of compensation increase	**1.68**	2.03	2.12			
Health care cost trend rate				**7.15**	6.23	6.62

PMI's expected rate of return on pension plan assets is determined by the plan assets' historical long-term investment performance, current asset allocation and estimates of future long-term returns by asset class.

PMI and certain of its subsidiaries sponsor defined contribution plans. Amounts charged to expense for defined contribution plans totaled $58 million, $56 million and $52 million for the years ended December 31, 2017, 2016 and 2015, respectively.

Plan Assets

PMI's investment strategy for pension plans is based on an expectation that equity securities will outperform debt securities over the long term. Accordingly, the target allocation of PMI's plan assets is broadly characterized as approximately a 60%/40% split between equity and debt securities. The strategy primarily utilizes indexed U.S. equity securities, international equity securities and investment-grade debt securities. PMI's plans have no investments in hedge funds, private equity or derivatives. PMI attempts to mitigate investment risk by rebalancing between equity and debt asset classes once a year or as PMI's contributions and benefit payments are made.

The fair value of PMI's pension plan assets at December 31, 2017 and 2016, by asset category was as follows:

Asset Category (in millions)	**At December 31, 2017**	**Quoted Prices In Active Markets for Identical Assets/ Liabilities (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Cash and cash equivalents	**$ 17**	**$ 17**		
Equity securities:				
U.S. securities	**146**	**146**		
International securities	**518**	**518**		
Investment funds[(a)]	**6,219**	**4,191**	**$ 2,028**	
International government bonds	**119**	**119**		
Corporate bonds	**247**	**247**		
	22	**22**		

Other				
Total assets in the fair value hierarchy	**$ 7,288**	**$ 5,260**	**$ 2,028**	**$ —**
Investment funds measured at net asset value[b]	**310**			
Total assets	**$ 7,598**			

[a] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and Barclays Capital U.S. for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 60% are invested in U.S. and international equities; 20% are invested in U.S. and international government bonds; 10% are invested in real estate and other money markets, and 10% are invested in corporate bonds.

[b] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Asset Category (in millions)	At December 31, 2016	Quoted Prices In Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$ 8	$ 8		
Equity securities:				
U.S. securities	131	131		
International securities	432	432		
Investment funds[a]	5,270	3,530	$ 1,740	
International government bonds	309	309		
Other	10	10		
Total assets in the fair value hierarchy	$ 6,160	$ 4,420	$ 1,740	$ —
Investment funds measured at net asset value[b]	297			
Total assets	$ 6,457			

[a] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and Barclays Capital U.S. for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 60% were invested in U.S. and international equities; 19% were invested in U.S. and international government bonds; 11% were invested in real estate and other money markets, and 10% were invested in corporate bonds.

[b] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

See Note 16. *Fair Value Measurements* for a discussion of the fair value of pension plan assets.

PMI makes, and plans to make, contributions to the extent that they are tax deductible and to meet specific funding requirements of its funded pension plans. Currently, PMI anticipates making contributions of approximately $53 million in 2018 to its pension plans, based on current tax and benefit laws. However, this estimate is subject to change as a result of changes in tax and other benefit laws, as well as asset performance significantly above or below the assumed long-term rate of return on pension assets, or changes in interest and currency rates.

The estimated future benefit payments from PMI pension plans at December 31, 2017, are as follows:

(in millions)	
2018	$ 295
	290

2019	
2020	309
2021	318
2022	330
2023 - 2027	1,879

PMI's expected future annual benefit payments for its postretirement health care plans are estimated to be not material through 2027.

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care trend rates would have the following effects as of December 31, 2017:

	One-Percentage-Point Increase	One-Percentage-Point Decrease
Effect on total service and interest cost	**21.7 %**	**(16.7 %)**
Effect on postretirement benefit obligation	**16.3**	**(13.0)**

Postemployment Benefit Plans

PMI and certain of its subsidiaries sponsor postemployment benefit plans covering substantially all salaried and certain hourly employees. The cost of these plans is charged to expense over the working life of the covered employees. Net postemployment costs were $144 million, $166 million and $187 million for the years ended December 31, 2017, 2016 and 2015, respectively.

The estimated net loss for the postemployment benefit plans that will be amortized from accumulated other comprehensive losses into net postemployment costs during 2018 is approximately $60 million.

The amounts recognized in accrued postemployment costs on PMI's consolidated balance sheets at December 31, 2017 and 2016, were $671 million and $727 million, respectively.

The accrued postemployment costs were determined using a weighted-average discount rate of 3.0% and 2.8% in 2017 and 2016, respectively; an assumed ultimate annual weighted-average turnover rate of 2.6% and 2.8% in 2017 and 2016, respectively; assumed compensation cost increases of 2.3% in 2017 and 2.6% in 2016, and assumed benefits as defined in the respective plans. In accordance with local regulations, certain postemployment plans are funded. As a result, the accrued postemployment costs disclosed above are presented net of the related assets of $33 million and $25 million at December 31, 2017 and 2016, respectively. Postemployment costs arising from actions that offer employees benefits in excess of those specified in the respective plans are charged to expense when incurred.

Comprehensive Earnings (Losses)

The amounts recorded in accumulated other comprehensive losses at December 31, 2017, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	**$ (2,624)**	**$ (80)**	**$ (617)**	**$ (3,321)**
Prior service cost	**(35)**	**4**	**—**	**(31)**
Net transition obligation	**(5)**	**—**	**—**	**(5)**
Deferred income taxes	**327**	**28**	**186**	**541**
Losses to be amortized	**$ (2,337)**	**$ (48)**	**$ (431)**	**$ (2,816)**

The amounts recorded in accumulated other comprehensive losses at December 31, 2016, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total

Net losses	$ (3,314)	$ (73)	$ (713)	$ (4,100)
Prior service cost	(53)	4	—	(49)
Net transition obligation	(5)	—	—	(5)
Deferred income taxes	350	24	215	589
Losses to be amortized	$ (3,022)	$ (45)	$ (498)	$ (3,565)

The amounts recorded in accumulated other comprehensive losses at December 31, 2015, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (3,074)	$ (61)	$ (710)	$ (3,845)
Prior service cost	(40)	5	—	(35)
Net transition obligation	(5)	—	—	(5)
Deferred income taxes	320	20	213	553
Losses to be amortized	$ (2,799)	$ (36)	$ (497)	$ (3,332)

The movements in other comprehensive earnings (losses) during the year ended December 31, 2017, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	**$ 175**	**$ 5**	**$ 68**	**$ 248**
Prior service cost	**5**	**—**	**—**	**5**
Other income/expense:				
Net losses	**6**	**—**	**—**	**6**
Prior service cost	**—**	**—**	**—**	**—**
Deferred income taxes	**(10)**	**(1)**	**(20)**	**(31)**
	176	**4**	**48**	**228**
Other movements during the year:				
Net losses	**509**	**(12)**	**28**	**525**
Prior service cost	**13**	**—**	**—**	**13**
Deferred income taxes	**(13)**	**5**	**(9)**	**(17)**
	509	**(7)**	**19**	**521**
Total movements in other comprehensive earnings (losses)	**$ 685**	**$ (3)**	**$ 67**	**$ 749**

The movements in other comprehensive earnings (losses) during the year ended December 31, 2016, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	$ 193	$ 2	$ 62	$ 257
Prior service cost	6	—	—	6
Other income/expense:				
Net losses	4	—	—	4
Prior service cost	—	—	—	—
Deferred income taxes	(26)	—	(17)	(43)
	177	2	45	224
Other movements during the year:				
Net losses	(437)	(15)	(65)	(517)
Prior service cost	(18)	—	—	(18)
Deferred income taxes	55	4	19	78
	(400)	(11)	(46)	(457)
Total movements in other comprehensive earnings (losses)	$ (223)	$ (9)	$ (1)	$ (233)

The movements in other comprehensive earnings (losses) during the year ended December 31, 2015, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	$ 194	$ 4	$ 69	$ 267
Prior service cost	4	—	—	4
Other income/expense:				
Net losses	3	—	—	3
Prior service cost	1	—	—	1
Deferred income taxes	(26)	(2)	(20)	(48)
	176	2	49	227
Other movements during the year:				
Net losses	(510)	12	(58)	(556)
Deferred income taxes	4	(4)	17	17
	(506)	8	(41)	(539)
Total movements in other comprehensive earnings (losses)	$ (330)	$ 10	$ 8	$ (312)

Note 14.

Additional Information:

(in millions)	For the Years Ended December 31, 2017	2016	2015
Research and development expense	**$ 453**	$ 429	$ 423
Advertising expense	**$ 830**	$ 405	$ 448
Foreign currency net transaction losses	**$ 49**	$ 272	$ 102
Interest expense	**$ 1,096**	$ 1,069	$ 1,132
Interest income	**(182)**	(178)	(124)
Interest expense, net	**$ 914**	$ 891	$ 1,008
Rent expense	**$ 313**	$ 284	$ 286

Minimum rental commitments under non-cancelable operating leases in effect at December 31, 2017, were as follows:

(in millions)	
2018	$ 179
2019	125
2020	94
2021	58
2022	37
Thereafter	356
	$ 849

Note 15.

Financial Instruments:

Overview

PMI operates in markets outside of the United States of America, with manufacturing and sales facilities in various locations around the world. PMI utilizes certain financial instruments to manage foreign currency and interest rate exposure. Derivative financial instruments are used by PMI principally to reduce exposures to market risks resulting from fluctuations in foreign currency exchange and interest rates by creating offsetting exposures. PMI is not a party to leveraged derivatives and, by policy, does not use derivative financial instruments for speculative purposes. Financial instruments qualifying for hedge accounting must maintain a specified level of effectiveness between the hedging instrument and the item being hedged, both at inception and throughout the hedged period. PMI formally

documents the nature and relationships between the hedging instruments and hedged items, as well as its risk-management objectives, strategies for undertaking the various hedge transactions and method of assessing hedge effectiveness. Additionally, for hedges of forecasted transactions, the significant characteristics and expected terms of the forecasted transaction must be specifically identified, and it must be probable that each forecasted transaction will occur. If it were deemed probable that the forecasted transaction would not occur, the gain or loss would be recognized in earnings. PMI reports its net transaction gains or losses in marketing, administration and research costs on the consolidated statements of earnings.

PMI uses deliverable and non-deliverable forward foreign exchange contracts, foreign currency swaps and foreign currency options, collectively referred to as foreign exchange contracts ("foreign exchange contracts"), and interest rate contracts to mitigate its exposure to changes in exchange and interest rates from third-party and intercompany actual and forecasted transactions. The primary currencies

to which PMI is exposed include the Australian dollar, Canadian dollar, Euro, Indonesian rupiah, Japanese yen, Mexican peso, Philippine peso, Russian ruble, Swiss franc and Turkish lira. At December 31, 2017 and 2016, PMI had contracts with aggregate notional amounts of $26.1 billion and $29.2 billion, respectively. Of the $26.1 billion aggregate notional amount at December 31, 2017, $3.4 billion related to cash flow hedges, $11.3 billion related to hedges of net investments in foreign operations and $11.4 billion related to other derivatives that primarily offset currency exposures on intercompany financing. Of the $29.2 billion aggregate notional amount at December 31, 2016, $5.0 billion related to cash flow hedges, $10.6 billion related to hedges of net investments in foreign operations and $13.6 billion related to other derivatives that primarily offset currency exposures on intercompany financing.

The fair value of PMI's foreign exchange contracts included in the consolidated balance sheet as of December 31, 2017 and 2016, were as follows:

	Asset Derivatives			Liability Derivatives		
		Fair Value			Fair Value	
(in millions)	**Balance Sheet Classification**	**2017**	**2016**	**Balance Sheet Classification**	**2017**	**2016**
Foreign exchange contracts designated as hedging instruments	Other current assets	**$ 84**	$ 207	Other accrued liabilities	**$ 197**	$ 66
	Other assets	**34**	436	Other liabilities	**880**	36
Foreign exchange contracts not designated as hedging instruments	Other current assets	**22**	161	Other accrued liabilities	**37**	61
	Other assets	**—**	9	Other liabilities	**14**	—
Total derivatives		**$ 140**	$ 813		**$ 1,128**	$ 163

For the years ended December 31, 2017, 2016 and 2015, PMI's cash flow and net investment hedging instruments impacted the consolidated statements of earnings and comprehensive earnings as follows:

(pre-tax, millions)	**For the Year Ended December 31,**								
	Amount of Gain/(Loss) Recognized in Other Comprehensive Earnings/ (Losses) on Derivatives			**Statement of Earnings Classification of Gain/ (Loss) Reclassified from Other Comprehensive Earnings/(Losses) into Earnings**	**Amount of Gain/(Loss) Reclassified from Other Comprehensive Earnings/ (Losses) into Earnings**		
	2017	**2016**	**2015**		**2017**	**2016**	**2015**
Derivatives in Cash Flow Hedging Relationship							
Foreign exchange contracts	**$ (52)**	$ 12	$ 43				
				Net revenues	**$ 60**	$ (38)	$ 149
				Cost of sales	**1**	46	(3)
					(7)	(11)	1

				Marketing, administration and research costs			
				Interest expense, net	**(41)**	(30)	(31)
Derivatives in Net Investment Hedging Relationship							
Foreign exchange contracts	**(1,644)**	296	253				
Total	**$ (1,696)**	$ 308	$ 296		**$ 13**	$ (33)	$ 116

Cash Flow Hedges

PMI has entered into foreign exchange contracts to hedge the foreign currency exchange and interest rate risks related to certain forecasted transactions. The effective portion of gains and losses associated with qualifying cash flow hedge contracts is deferred as a component of accumulated other comprehensive losses until the underlying hedged transactions are reported in PMI's consolidated statements of earnings. During the years ended December 31, 2017, 2016 and 2015, ineffectiveness related to cash flow hedges was not material. As

of December 31, 2017, PMI has hedged forecasted transactions for periods not exceeding the next twelve months, with the exception of one foreign exchange contract that expires in May 2024. The impact of these hedges is primarily included in operating cash flows on PMI's consolidated statements of cash flows.

Hedges of Net Investments in Foreign Operations

PMI designates certain foreign currency denominated debt and foreign exchange contracts as net investment hedges, primarily of its Euro net assets. For the years ended December 31, 2017, 2016 and 2015, these hedges of net investments resulted in gains/(losses), net of income taxes, of $(1,725) million, $430 million and $761 million, respectively, principally related to changes in the exchange rates between the Euro and U.S. dollar. These gains/(losses) were reported as a component of accumulated other comprehensive losses within currency translation adjustments, and were substantially offset by the losses and gains generated on the underlying assets. For the years ended December 31, 2017, 2016 and 2015, ineffectiveness related to net investment hedges was not material. The premiums paid for, and settlements of, net investment hedges are included in investing cash flows on PMI's consolidated statements of cash flows.

Other Derivatives

PMI has entered into foreign exchange contracts to hedge the foreign currency exchange and interest rate risks related to intercompany loans between certain subsidiaries, and third-party loans. While effective as economic hedges, no hedge accounting is applied for these contracts; therefore, the unrealized gains (losses) relating to these contracts are reported in PMI's consolidated statements of earnings. For the years ended December 31, 2017, 2016 and 2015, the gains/(losses) from contracts for which PMI did not apply hedge accounting were $382 million, $(85) million and $(587) million, respectively. The gains/(losses) from these contracts substantially offset the losses and gains generated by the underlying intercompany and third-party loans being hedged.

As a result, for the years ended December 31, 2017, 2016 and 2015, these items impacted the consolidated statement of earnings as follows:

(pre-tax, in millions)

Derivatives not Designated as Hedging Instruments	Statement of Earnings Classification of Gain/(Loss)	Amount of Gain/(Loss) Recognized in Earnings		
		2017	2016	2015
Foreign exchange contracts				
	Interest expense, net	**$ (60)**	$ (24)	$ (1)
Total		**$ (60)**	$ (24)	$ (1)

Qualifying Hedging Activities Reported in Accumulated Other Comprehensive Losses

Derivative gains or losses reported in accumulated other comprehensive losses are a result of qualifying hedging activity. Transfers of these gains or losses to earnings are offset by the corresponding gains or losses on the underlying hedged item. Hedging activity affected accumulated other comprehensive losses, net of income taxes, as follows:

(in millions)	For the Years Ended December 31,		
	2017	2016	2015
Gain as of January 1,	**$ 97**	$ 59	$ 123
Derivative (gains)/losses transferred to earnings	**(11)**	30	(102)
	(44)	8	38

Change in fair value			
Gain as of December 31,	**$ 42**	$ 97	$ 59

At December 31, 2017, PMI expects $36 million of derivative gains that are included in accumulated other comprehensive losses to be reclassified to the consolidated statement of earnings within the next 12 months. These gains are expected to be substantially offset by the statement of earnings impact of the respective hedged transactions.

Contingent Features

PMI's derivative instruments do not contain contingent features.

Credit Exposure and Credit Risk

PMI is exposed to credit loss in the event of non-performance by counterparties. While PMI does not anticipate non-performance, its risk is limited to the fair value of the financial instruments less any cash collateral received or pledged. PMI actively monitors its exposure to credit risk through the use of credit approvals and credit limits and by selecting and continuously monitoring a diverse group of major international banks and financial institutions as counterparties.

Fair Value

See Note 16. *Fair Value Measurements* and Note 19. *Balance Sheet Offsetting* for additional discussion of derivative financial instruments.

Note 16.

Fair Value Measurements:

The authoritative guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The guidance also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of input that may be used to measure fair value, which are as follows:

Level 1 — Quoted prices in active markets for identical assets or liabilities;

Level 2 — Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

PMI's policy is to reflect transfers between hierarchy levels at the end of the reporting period.

Derivative Financial Instruments

PMI assesses the fair value of its foreign exchange contracts and interest rate contracts using standard valuation models that use, as their basis, readily observable market inputs. The fair value of PMI's foreign exchange forward contracts is determined by using the prevailing foreign exchange spot rates and interest rate differentials, and the respective maturity dates of the instruments. The fair value of PMI's currency options is determined by using a Black-Scholes methodology based on foreign exchange spot rates and interest rate differentials, currency volatilities and maturity dates. PMI's derivative financial instruments have been classified within Level 2 at December 31, 2017 and 2016. See Note 15. *Financial Instruments* for additional discussion of derivative financial instruments.

Pension Plan Assets

The fair value of pension plan assets determined by using readily available quoted market prices in active markets has been classified within Level 1 of the fair value hierarchy at December 31, 2017 and 2016. The fair value of pension plan assets determined by using quoted prices in markets that are not active has been classified within Level 2 at December 31, 2017 and 2016. See Note 13. *Benefit Plans* for additional discussion of pension plan assets.

Debt

The fair value of PMI's outstanding debt, which is utilized solely for disclosure purposes, is determined using quotes and market interest rates currently available to PMI for issuances of debt with similar terms and remaining maturities. The aggregate carrying value of PMI's debt, excluding short-term borrowings and $28 million of capital lease obligations, was $33,812 million at December 31, 2017. The aggregate carrying value of PMI's debt, excluding short-term borrowings and $13 million of capital lease obligations, was $28,411 million

at December 31, 2016. The fair value of PMI's outstanding debt, excluding the aforementioned short-term borrowings and capital lease obligations, was classified within Level 1 and Level 2 at December 31, 2017 and 2016.

The aggregate fair values of PMI's derivative financial instruments, pension plan assets and debt as of December 31, 2017 and 2016, were as follows:

(in millions)	Fair Value At December 31, 2017	Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Foreign exchange contracts	**$ 140**	**$ —**	**$ 140**	**$ —**
Pension plan assets	**7,288**	**5,260**	**2,028**	**—**
Total assets in fair value hierarchy	**$ 7,428**	**$ 5,260**	**$ 2,168**	**$ —**
Pension plan assets measured at net asset value[(a)]	**310**			
Total assets	**$ 7,738**			
Liabilities:				
Debt	**$ 35,856**	**$ 35,685**	**$ 171**	**$ —**
Foreign exchange contracts	**1,128**	**—**	**1,128**	**—**
Total liabilities	**$ 36,984**	**$ 35,685**	**$ 1,299**	**$ —**

(in millions)	Fair Value At December 31, 2016	Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Foreign exchange contracts	$ 813	$ —	$ 813	$ —
Pension plan assets	6,160	4,420	1,740	—
Total assets in fair value hierarchy	$ 6,973	$ 4,420	$ 2,553	$ —
Pension plan assets measured at net asset value[(a)]	297			
Total assets	$ 7,270			

Liabilities:				
Debt	$ 30,192	$ 29,756	$ 436	$ —
Foreign exchange contracts	163	—	163	—
Total liabilities	$ 30,355	$ 29,756	$ 599	$ —

[a] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in these tables are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Note 17.

Accumulated Other Comprehensive Losses:

PMI's accumulated other comprehensive losses, net of taxes, consisted of the following:

(Losses) Earnings (in millions)	At December 31,		
	2017	**2016**	**2015**
Currency translation adjustments	**$ (5,761)**	$ (6,091)	$ (6,129)
Pension and other benefits	**(2,816)**	(3,565)	(3,332)
Derivatives accounted for as hedges	**42**	97	59
Total accumulated other comprehensive losses	**$ (8,535)**	$ (9,559)	$ (9,402)

Reclassifications from Other Comprehensive Earnings

The movements in accumulated other comprehensive losses and the related tax impact, for each of the components above, that are due to current period activity and reclassifications to the income statement are shown on the consolidated statements of comprehensive earnings for the years ended December 31, 2017, 2016, and 2015. For the years ended December 31, 2017, 2016, and 2015, $2 million, $(5) million and $1 million of net currency translation adjustment gains/(losses) were transferred from other comprehensive earnings to marketing, administration and research costs in the consolidated statements of earnings, respectively, upon liquidation of subsidiaries. For additional information, see Note 13. *Benefit Plans* and Note 15. *Financial Instruments* for disclosures related to PMI's pension and other benefits and derivative financial instruments.

Note 18.

Contingencies:

Tobacco-Related Litigation

Legal proceedings covering a wide range of matters are pending or threatened against us, and/or our subsidiaries, and/or our indemnitees in various jurisdictions. Our indemnitees include distributors, licensees and others that have been named as parties in certain cases and that we have agreed to defend, as well as to pay costs and some or all of judgments, if any, that may be entered against them. Pursuant to the terms of the Distribution Agreement between Altria Group, Inc. ("Altria") and PMI, PMI will indemnify Altria and Philip Morris USA Inc. ("PM USA"), a U.S. tobacco subsidiary of Altria, for tobacco product claims based in substantial part on products manufactured by PMI or contract manufactured for PMI by PM USA, and PM USA will indemnify PMI for tobacco product claims based in substantial part on products manufactured by PM USA, excluding tobacco products contract manufactured for PMI.

It is possible that there could be adverse developments in pending cases against us and our subsidiaries. An unfavorable outcome or settlement of pending tobacco-related litigation could encourage the commencement of additional litigation.

Damages claimed in some of the tobacco-related litigation are significant and, in certain cases in Brazil, Canada and Nigeria, range into the billions of U.S. dollars. The variability in pleadings in multiple jurisdictions, together with the actual experience of management in litigating claims, demonstrate that the monetary relief that may be specified in a lawsuit bears little relevance to the ultimate outcome. Much of the tobacco-related litigation is in its early stages, and

litigation is subject to uncertainty. However, as discussed below, we have to date been largely successful in defending tobacco-related litigation.

We and our subsidiaries record provisions in the consolidated financial statements for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. At the present time, while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available to it (i) management has not concluded that it is probable that a loss has been incurred in any of the pending tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss for any of the pending tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any. Legal defense costs are expensed as incurred.

It is possible that our consolidated results of operations, cash flows or financial position could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. Nevertheless, although litigation is subject to uncertainty, we and each of our subsidiaries named as a defendant believe, and each has been so advised by counsel handling the respective cases, that we have valid defenses to the litigation pending against us, as well as valid bases for appeal of adverse verdicts. All such cases are, and will continue to be, vigorously defended. However, we and our subsidiaries may enter into settlement discussions in particular cases if we believe it is in our best interests to do so.

To date, no tobacco-related case has been finally resolved in favor of a plaintiff against us, our subsidiaries or indemnitees.

The table below lists the number of tobacco-related cases pending against us and/or our subsidiaries or indemnitees as of February 9, 2018, December 31, 2016 and December 31, 2015:

Type of Case	Number of Cases Pending as of February 9, 2018	Number of Cases Pending as of December 31, 2016	Number of Cases Pending as of December 31, 2015
Individual Smoking and Health Cases	**57**	64	68
Smoking and Health Class Actions	**11**	11	11
Health Care Cost Recovery Actions	**16**	16	16
Label-Related Class Actions	**1**	—	—
Individual Label-Related Cases	**1**	3	3
Public Civil Actions	**2**	2	3

Since 1995, when the first tobacco-related litigation was filed against a PMI entity, 476 Smoking and Health, Label-Related, Health Care Cost Recovery, and Public Civil Actions in which we and/or one of our subsidiaries and/or indemnitees were a defendant have been terminated in our favor. Thirteen cases have had decisions in favor of plaintiffs. Nine of these cases have subsequently reached final resolution in our favor and four remain on appeal.

The table below lists the verdict and significant post-trial developments in the four pending cases where a verdict was returned in favor of the plaintiff:

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
February 2004	Brazil/The Smoker Health Defense Association	Class Action	The Civil Court of São Paulo found defendants liable without hearing evidence. In April 2004, the court awarded "moral damages" of R$1,000 (approximately $305) per smoker per full year of smoking plus interest at the rate of 1% per month, as of the date of the ruling. The court did not assess actual damages, which were to be assessed in a second phase of the case. The size of the class was not defined in the ruling.	Defendants appealed to the São Paulo Court of Appeals, which annulled the ruling in November 2008, finding that the trial court had inappropriately ruled without hearing evidence and returned the case to the trial court for further proceedings. In May 2011, the trial court dismissed the claim. Plaintiff appealed the decision. In February 2015, the appellate court unanimously dismissed plaintiff's appeal. In September 2015, plaintiff appealed to the Superior Court of Justice. In addition, the defendants filed a constitutional appeal to the Federal Supreme Tribunal on the basis that plaintiff did not have standing to bring the lawsuit. This appeal is still pending.

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
May 27, 2015	Canada/Cecilia Létourneau	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec ruled in favor of the *Létourneau* class on liability and awarded a total of CAD 131 million (approximately $104 million) in punitive damages, allocating CAD 46 million (approximately $37 million) to our subsidiary. The trial court ordered defendants to pay the full punitive damage award into a trust within 60 days. The court did not order the payment of compensatory damages.	In June 2015, our subsidiary commenced the appellate process with the Court of Appeal of Quebec. Our subsidiary also filed a motion to cancel the trial court's order for payment into a trust notwithstanding appeal. In July 2015, the Court of Appeal granted the motion to cancel and overturned the trial court's ruling that our subsidiary make the payment into a trust. In August 2015, plaintiffs filed a motion for security with the Court of Appeal covering both the *Létourneau* case and the *Blais* case described below. In October 2015, the Court of Appeal granted the motion and ordered our subsidiary to furnish security totaling CAD 226 million (approximately $180 million) to cover both

the *Létourneau* and *Blais* cases. The hearing for the merits appeal took place in November 2016. (See below for further detail.)

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
May 27, 2015	Canada/Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec ruled in favor of the *Blais* class on liability and found the class members' compensatory damages totaled approximately CAD 15.5 billion (approximately $12.3 billion), including pre-judgment interest. The trial court awarded compensatory damages on a joint and several liability basis, allocating 20% to our subsidiary (approximately CAD 3.1 billion including pre-judgment interest (approximately $2.5 billion)). The trial court awarded CAD 90,000 (approximately $71,500) in punitive damages, allocating CAD 30,000 (approximately $23,900) to our subsidiary. The trial court ordered defendants to pay CAD 1 billion (approximately $795 million) of the compensatory damage award, CAD 200 million (approximately $159 million) of which is our subsidiary's portion, into a trust within 60 days.	In June 2015, our subsidiary commenced the appellate process with the Court of Appeal of Quebec. Our subsidiary also filed a motion to cancel the trial court's order for payment into a trust notwithstanding appeal. In July 2015, the Court of Appeal granted the motion to cancel and overturned the trial court's ruling that our subsidiary make the payment into a trust. In August 2015, plaintiffs filed a motion for security with the Court of Appeal. In October 2015, the Court of Appeal granted the motion and ordered our subsidiary to furnish security totaling, together with the *Létourneau* case, CAD 226 million (approximately $180 million). The hearing for the merits appeal took place in November 2016. (See below for further detail.)

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
August 5, 2016	Argentina/Hugo Lespada	Individual Action	On August 5, 2016, the Civil Court No. 14 - Mar del Plata, issued a verdict in favor of plaintiff, an individual smoker, and awarded him ARS 110,000	On August 23, 2016, our subsidiary filed its notice of appeal. On October 31, 2017, the Civil and Commercial Court of Appeals of Mar del Plata ruled that plaintiff's claim

	(approximately $5,558), plus interest, in compensatory and moral damages. The trial court found that our subsidiary failed to warn plaintiff of the risk of becoming addicted to cigarettes.	was barred by the statute of limitations and it reversed the trial court's decision. On November 28, 2017, plaintiff filed an extraordinary appeal of the reversal of the trial court's decision to the Supreme Court of the Province of Buenos Aires.

Pending claims related to tobacco products generally fall within the following categories:

Smoking and Health Litigation: These cases primarily allege personal injury and are brought by individual plaintiffs or on behalf of a class or purported class of individual plaintiffs. Plaintiffs' allegations of liability in these cases are based on various theories of recovery, including negligence, gross negligence, strict liability, fraud, misrepresentation, design defect, failure to warn, breach of express and implied warranties, violations of deceptive trade practice laws and consumer protection statutes. Plaintiffs in these cases seek various forms of relief, including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include licit activity, failure to state a claim, lack of defect, lack of proximate cause, assumption of the risk, contributory negligence, and statute of limitations.

As of February 9, 2018, there were a number of smoking and health cases pending against us, our subsidiaries or indemnitees, as follows:

- 57 cases brought by individual plaintiffs in Argentina (30), Brazil (10), Canada (4), Chile (5), Costa Rica (1), Italy (3), the Philippines (1), Russia (1), Turkey (1) and Scotland (1), compared with 64 such cases on December 31, 2016, and 68 cases on December 31, 2015; and

- 11 cases brought on behalf of classes of individual plaintiffs in Brazil (2) and Canada (9), compared with 11 such cases on December 31, 2016, and 11 such cases on December 31, 2015.

In the first class action pending in Brazil, *The Smoker Health Defense Association (ADESF) v. Souza Cruz, S.A. and Philip Morris Marketing, S.A., Nineteenth Lower Civil Court of the Central Courts of the Judiciary District of São Paulo, Brazil*, filed July 25, 1995, our subsidiary and another member of the industry are defendants. The plaintiff, a consumer organization, is seeking damages for all addicted smokers and former smokers, and injunctive relief. In 2004, the trial court found defendants liable without hearing evidence and awarded “moral damages” of R$1,000 (approximately $305) per smoker per full year of smoking plus interest at the rate of 1% per month, as of the date of the ruling. The court did not award actual damages, which were to be assessed in the second phase of the case. The size of the class was not estimated. Defendants appealed to the São Paulo Court of Appeals, which annulled the ruling in November 2008, finding that the trial court had inappropriately ruled without hearing evidence and returned the case to the trial court for further proceedings. In May 2011, the trial court dismissed the claim. In February 2015, the appellate court unanimously dismissed plaintiff's appeal. In September 2015, plaintiff appealed to the Superior Court of Justice. In February 2017, the Chief Justice of the Supreme Court of Justice denied plaintiff's appeal. In March 2017, plaintiff filed an *en banc* appeal to the Supreme Court of Justice. In addition, the defendants filed a constitutional appeal to the Federal Supreme Tribunal on the basis that plaintiff did not have standing to bring the lawsuit. Both appeals are still pending.

In the second class action pending in Brazil*, Public Prosecutor of São Paulo v. Philip Morris Brasil Industria e Comercio Ltda., Civil Court of the City of São Paulo, Brazil,* filed August 6, 2007, our subsidiary is a defendant. The plaintiff, the Public Prosecutor of the State of São Paulo, is seeking (i) damages on behalf of all smokers nationwide, former smokers, and their relatives; (ii) damages on behalf of people exposed to environmental tobacco smoke nationwide, and their relatives; and (iii) reimbursement of the health care costs allegedly incurred for the treatment of tobacco-related diseases by all Brazilian States and Municipalities, and the Federal District. In an interim ruling issued in December 2007, the trial court limited the scope of this claim to the State of São Paulo only. In December 2008, the Seventh Civil Court of São Paulo issued a decision declaring that it lacked jurisdiction because the case involved issues similar to the *ADESF* case discussed above and should be transferred to the Nineteenth Lower Civil Court in São Paulo where the *ADESF* case is pending. The court further stated that these cases should be consolidated for the purposes of judgment. In April 2010, the São Paulo Court of Appeals reversed the Seventh Civil Court's decision that consolidated the cases, finding that they are based on different legal claims and are progressing at different stages of proceedings. This case was returned to the Seventh Civil Court of São Paulo, and our subsidiary filed its closing arguments in December 2010. In March 2012, the trial court dismissed the case on the merits. In January 2014, the São Paulo Court of Appeals rejected plaintiff’s appeal and affirmed the trial court decision. In July 2014, plaintiff appealed to the Superior Court of Justice.

In the first class action pending in Canada, *Cecilia Létourneau v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI Macdonald Corp., Quebec Superior Court, Canada,* filed in September 1998, our subsidiary and

other Canadian manufacturers (Imperial Tobacco Canada Ltd. and JTI-MacDonald Corp.) are defendants. The plaintiff, an individual smoker, sought compensatory and punitive damages for each member of the class who is deemed addicted to smoking. The class was certified in 2005. Trial began in March 2012 and concluded in December 2014. The trial court issued its judgment on May 27, 2015. The trial court found our subsidiary and two other Canadian manufacturers liable and awarded a total of CAD 131 million (approximately $104 million) in punitive damages, allocating CAD 46 million (approximately $37 million) to our subsidiary. The trial court found that defendants violated the Civil Code of Quebec, the Quebec Charter of Human Rights and Freedoms, and the Quebec Consumer Protection Act by failing to warn adequately of the dangers of smoking. The trial court also found that defendants conspired to prevent consumers from learning the dangers of smoking. The trial court further held that these civil faults were a cause of the class members' addiction. The trial court rejected other grounds of

fault advanced by the class, holding that: (i) the evidence was insufficient to show that defendants marketed to youth, (ii) defendants' advertising did not convey false information about the characteristics of cigarettes, and (iii) defendants did not commit a fault by using the descriptors light or mild for cigarettes with a lower tar delivery. The trial court estimated the size of the addiction class at 918,000 members but declined to award compensatory damages to the addiction class because the evidence did not establish the claims with sufficient accuracy. The trial court ordered defendants to pay the full punitive damage award into a trust within 60 days and found that a claims process to allocate the awarded damages to individual class members would be too expensive and difficult to administer. The trial court ordered a briefing on the proposed process for the distribution of sums remaining from the punitive damage award after payment of attorneys' fees and legal costs. In June 2015, our subsidiary commenced the appellate process by filing its inscription of appeal of the trial court's judgment with the Court of Appeal of Quebec. Our subsidiary also filed a motion to cancel the trial court's order for payment into a trust within 60 days notwithstanding appeal. In July 2015, the Court of Appeal granted the motion to cancel and overturned the trial court's ruling that our subsidiary make the payment into a trust within 60 days. In August 2015, plaintiffs filed a motion with the Court of Appeal seeking security in both the *Létourneau* case and the *Blais* case described below. In October 2015, the Court of Appeal granted the motion and ordered our subsidiary to furnish security totaling CAD 226 million (approximately $180 million), in the form of cash into a court trust or letters of credit, in six equal consecutive quarterly installments of approximately CAD 37.6 million (approximately $29.9 million) beginning in December 2015 through March 2017. See the *Blais* description for further detail concerning the security order. The Court of Appeal heard oral arguments on the merits appeal in November 2016. Our subsidiary and PMI believe that the findings of liability and damages were incorrect and should ultimately be set aside on any one of many grounds, including the following: (i) holding that defendants violated Quebec law by failing to warn class members of the risks of smoking even after the court found that class members knew, or should have known, of the risks, (ii) finding that plaintiffs were not required to prove that defendants' alleged misconduct caused injury to each class member in direct contravention of binding precedent, (iii) creating a factual presumption, without any evidence from class members or otherwise, that defendants' alleged misconduct caused all smoking by all class members, (iv) holding that the addiction class members' claims for punitive damages were not time-barred even though the case was filed more than three years after a prominent addiction warning appeared on all packages, and (v) awarding punitive damages to punish defendants without proper consideration as to whether punitive damages were necessary to deter future misconduct.

In the second class action pending in Canada, *Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI Macdonald Corp., Quebec Superior Court, Canada*, filed in November 1998, our subsidiary and other Canadian manufacturers (Imperial Tobacco Canada Ltd. and JTI-MacDonald Corp.) are defendants. The plaintiffs, an anti-smoking organization and an individual smoker, sought compensatory and punitive damages for each member of the class who allegedly suffers from certain smoking-related diseases. The class was certified in 2005. Trial began in March 2012 and concluded in December 2014. The trial court issued its judgment on May 27, 2015. The trial court found our subsidiary and two other Canadian manufacturers liable and found that the class members' compensatory damages totaled approximately CAD 15.5 billion, including pre-judgment interest (approximately $12.3 billion). The trial court awarded compensatory damages on a joint and several liability basis, allocating 20% to our subsidiary (approximately CAD 3.1 billion, including pre-judgment interest (approximately $2.5 billion)). In addition, the trial court awarded CAD 90,000 (approximately $71,500) in punitive damages, allocating CAD 30,000 (approximately $23,900) to our subsidiary and found that defendants violated the Civil Code of Quebec, the Quebec Charter of Human Rights and Freedoms, and the Quebec Consumer Protection Act by failing to warn adequately of the dangers of smoking. The trial court also found that defendants conspired to prevent consumers from learning the dangers of smoking. The trial court further held that these civil faults were a cause of the class members' diseases. The trial court rejected other grounds of fault advanced by the class, holding that: (i) the evidence was insufficient to show that defendants marketed to youth, (ii) defendants' advertising did not convey false information about the characteristics of cigarettes, and (iii) defendants did not commit a fault by using the descriptors light or mild for cigarettes with a lower tar delivery. The trial court estimated the disease class at 99,957 members. The trial court ordered defendants to pay CAD 1 billion (approximately $795 million) of the compensatory damage award into a trust within 60 days, CAD 200 million (approximately $159 million) of which is our subsidiary's portion and ordered briefing on a proposed claims process for the distribution of damages to individual class members and for payment of attorneys' fees and legal costs. In June 2015, our subsidiary commenced the appellate process by filing its inscription of appeal of the trial court's judgment with the Court of Appeal of Quebec. Our subsidiary also filed a motion to cancel the trial court's order for payment into a trust within 60 days notwithstanding appeal. In July 2015, the Court of Appeal granted the motion to cancel and overturned the trial court's ruling that our subsidiary make an initial payment within 60 days. In August 2015, plaintiffs filed a motion with the Court of Appeal seeking an order that defendants place irrevocable letters of credit totaling CAD 5 billion (approximately $3.97 billion) into trust, to secure the judgments in both the *Létourneau*

and *Blais* cases. Plaintiffs subsequently withdrew their motion for security against JTI-MacDonald Corp. and proceeded only against our subsidiary and Imperial Tobacco Canada Ltd. In October 2015, the Court of Appeal granted the motion and ordered our subsidiary to furnish security totaling CAD 226 million (approximately $180 million) to cover both the *Létourneau* and *Blais* cases. Such security may take the form of cash into a court trust or letters of credit, in six equal consecutive quarterly installments of approximately CAD 37.6 million (approximately $29.9 million) beginning in December 2015 through March 2017. The Court of Appeal ordered Imperial Tobacco Canada Ltd. to furnish security totaling CAD 758 million (approximately $603 million) in seven equal consecutive quarterly installments of approximately CAD 108 million (approximately $85.9 million) beginning in December 2015 through June 2017. In March 2017, our subsidiary made its sixth and final quarterly installment of security for approximately CAD 37.6 million (approximately $29.9 million) into a court trust. This payment is included in other assets on the consolidated balance sheets and in cash used in operating activities in the consolidated statements of cash flows. The Court of Appeal ordered that the security is payable upon a final judgment of the Court of Appeal affirming the trial court's judgment or upon

further order of the Court of Appeal. The Court of Appeal heard oral arguments on the merits appeal in November 2016. Our subsidiary and PMI believe that the findings of liability and damages were incorrect and should ultimately be set aside on any one of many grounds, including the following: (i) holding that defendants violated Quebec law by failing to warn class members of the risks of smoking even after the court found that class members knew, or should have known, of the risks, (ii) finding that plaintiffs were not required to prove that defendants' alleged misconduct caused injury to each class member in direct contravention of binding precedent, (iii) creating a factual presumption, without any evidence from class members or otherwise, that defendants' alleged misconduct caused all smoking by all class members, (iv) relying on epidemiological evidence that did not meet recognized scientific standards, and (v) awarding punitive damages to punish defendants without proper consideration as to whether punitive damages were necessary to deter future misconduct.

In the third class action pending in Canada, *Kunta v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Winnipeg, Canada*, filed June 12, 2009, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic obstructive pulmonary disease ("COPD"), severe asthma, and mild reversible lung disease resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products. In September 2009, plaintiff's counsel informed defendants that he did not anticipate taking any action in this case while he pursues the class action filed in Saskatchewan (see description of *Adams*, below).

In the fourth class action pending in Canada, *Adams v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Saskatchewan, Canada*, filed July 10, 2009, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, emphysema, heart disease, or cancer, as well as restitution of profits. Preliminary motions are pending.

In the fifth class action pending in Canada, *Semple v. Canadian Tobacco Manufacturers' Council, et al., The Supreme Court (trial court), Nova Scotia, Canada*, filed June 18, 2009, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and COPD resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products. No activity in this case is anticipated while plaintiff's counsel pursues the class action filed in Saskatchewan (see description of *Adams*, above).

In the sixth class action pending in Canada, *Dorion v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Alberta, Canada,* filed June 15, 2009, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic bronchitis and severe sinus infections resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products. To date, we, our subsidiaries, and our indemnitees have not been properly served with the complaint. No activity in this case is anticipated while plaintiff's counsel pursues the class action filed in Saskatchewan (see description of *Adams*, above).

In the seventh class action pending in Canada, *McDermid v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and heart disease resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from heart disease allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed.

In the eighth class action pending in Canada, *Bourassa v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, the heir to a deceased smoker, alleges that the decedent

was addicted to tobacco products and suffered from emphysema resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from chronic respiratory diseases allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed. In December 2014, plaintiff filed an amended statement of claim.

In the ninth class action pending in Canada, *Suzanne Jacklin v. Canadian Tobacco Manufacturers' Council, et al., Ontario Superior Court of Justice,* filed June 20, 2012, we, our subsidiaries, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of

tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, heart disease, or cancer, as well as restitution of profits. Plaintiff's counsel has indicated that he does not intend to take any action in this case in the near future.

Health Care Cost Recovery Litigation: These cases, brought by governmental and non-governmental plaintiffs, seek reimbursement of health care cost expenditures allegedly caused by tobacco products. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including unjust enrichment, negligence, negligent design, strict liability, breach of express and implied warranties, violation of a voluntary undertaking or special duty, fraud, negligent misrepresentation, conspiracy, public nuisance, defective product, failure to warn, sale of cigarettes to minors, and claims under statutes governing competition and deceptive trade practices. Plaintiffs in these cases seek various forms of relief including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include lack of proximate cause, remoteness of injury, failure to state a claim, adequate remedy at law, "unclean hands" (namely, that plaintiffs cannot obtain equitable relief because they participated in, and benefited from, the sale of cigarettes), and statute of limitations.

As of February 9, 2018, there were 16 health care cost recovery cases pending against us, our subsidiaries or indemnitees in Canada (10), Korea (1) and Nigeria (5), compared with 16 such cases on December 31, 2016 and 16 such cases on December 31, 2015.

In the first health care cost recovery case pending in Canada, *Her Majesty the Queen in Right of British Columbia v. Imperial Tobacco Limited, et al., Supreme Court, British Columbia, Vancouver Registry, Canada,* filed January 24, 2001, we, our subsidiaries, our indemnitee (PM USA), and other members of the industry are defendants. The plaintiff, the government of the province of British Columbia, brought a claim based upon legislation enacted by the province authorizing the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, resulting from a "tobacco related wrong." The Supreme Court of Canada has held that the statute is constitutional. We and certain other non-Canadian defendants challenged the jurisdiction of the court. The court rejected the jurisdictional challenge. Pre-trial discovery is ongoing.

In the second health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of New Brunswick v. Rothmans Inc., et al., Court of Queen's Bench of New Brunswick, Trial Court, New Brunswick, Fredericton, Canada,* filed March 13, 2008, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of New Brunswick based on legislation enacted in the province. This legislation is similar to the law introduced in British Columbia that authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Pre-trial discovery is ongoing. In June 2017, the trial court set a trial date for November 4, 2019.

In the third health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of Ontario v. Rothmans Inc., et al., Ontario Superior Court of Justice, Toronto, Canada*, filed September 29, 2009, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Ontario based on legislation enacted in the province. This legislation is similar to the laws introduced in British Columbia and New Brunswick that authorize the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Pre-trial discovery is ongoing.

In the fourth health care cost recovery case filed in Canada, *Attorney General of Newfoundland and Labrador v. Rothmans Inc., et al., Supreme Court of Newfoundland and Labrador, St. Johns, Canada*, filed February 8, 2011, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Newfoundland and Labrador based on legislation enacted in the province that is similar to the laws introduced in British Columbia, New Brunswick and Ontario. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Pre-trial discovery is ongoing.

In the fifth health care cost recovery case filed in Canada, *Attorney General of Quebec v. Imperial Tobacco Limited, et al., Superior Court of Quebec, Canada*, filed June 8, 2012, we, our subsidiary, our indemnitee (PM USA), and other members of the industry are defendants. The claim was filed by the government of the province of Quebec based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces.

The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a “tobacco related wrong.” Pre-trial discovery is ongoing.

In the sixth health care cost recovery case filed in Canada, *Her Majesty in Right of Alberta v. Altria Group, Inc., et al., Supreme Court of Queen's Bench Alberta, Canada*, filed June 8, 2012, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Alberta based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a “tobacco related wrong.” Pre-trial discovery is ongoing.

In the seventh health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Manitoba v. Rothmans, Benson & Hedges, Inc., et al., The Queen's Bench, Winnipeg Judicial Centre, Canada*, filed May 31, 2012, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Manitoba based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Defendants filed their defenses in September 2014. Pre-trial discovery is ongoing.

In the eighth health care cost recovery case filed in Canada, *The Government of Saskatchewan v. Rothmans, Benson & Hedges Inc., et al., Queen's Bench, Judicial Centre of Saskatchewan, Canada*, filed June 8, 2012, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Saskatchewan based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Defendants filed their defenses in February 2015. While discovery initially was scheduled to begin in 2017 by agreement of the parties, to date, the discovery process has not started.

In the ninth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Prince Edward Island v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Prince Edward Island (General Section), Canada*, filed September 10, 2012, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Prince Edward Island based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Defendants filed their defenses in February 2015. While discovery initially was scheduled to begin in 2017 by agreement of the parties, to date, the discovery process has not started.

In the tenth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Nova Scotia v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Nova Scotia, Canada*, filed January 2, 2015, we, our subsidiaries, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Nova Scotia based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong." Defendants filed their defenses in July 2015. While discovery initially was scheduled to begin in 2017 by agreement of the parties, to date, the discovery process has not started.

In the first health care cost recovery case in Nigeria, *The Attorney General of Lagos State v. British American Tobacco (Nigeria) Limited, et al., High Court of Lagos State, Lagos, Nigeria,* filed March 13, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of making challenges to service and the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the second health care cost recovery case in Nigeria, *The Attorney General of Kano State v. British American Tobacco (Nigeria) Limited, et al., High Court of Kano State, Kano, Nigeria,* filed May 9, 2007, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of making challenges to service and the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the third health care cost recovery case in Nigeria, *The Attorney General of Gombe State v. British American Tobacco (Nigeria) Limited, et al., High Court of Gombe State, Gombe, Nigeria,* filed October 17, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In February 2011, the court ruled that the

plaintiff had not complied with the procedural steps necessary to serve us. As a result of this ruling, plaintiff must re-serve its claim. We have not yet been re-served.

In the fourth health care cost recovery case in Nigeria, *The Attorney General of Oyo State, et al., v. British American Tobacco (Nigeria) Limited, et al., High Court of Oyo State, Ibadan, Nigeria,* filed May 25, 2007, we and other members of the industry are defendants. Plaintiffs seek reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We challenged service as improper. In June 2010, the court ruled that plaintiffs did not have leave to serve the writ of summons on the defendants and that they must re-serve the writ. We have not yet been re-served.

In the fifth health care cost recovery case in Nigeria, *The Attorney General of Ogun State v. British American Tobacco (Nigeria) Limited, et al., High Court of Ogun State, Abeokuta, Nigeria*, filed February 26, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In May 2010, the trial court rejected our service objections. We have appealed.

In the health care cost recovery case in Korea, the *National Health Insurance Service v. KT&G, et. al.,* filed April 14, 2014, our subsidiary and other Korean manufacturers are defendants. Plaintiff alleges that defendants concealed the health hazards of smoking, marketed to youth, added ingredients to make their products more harmful and addictive, and misled consumers into believing that *Lights* cigarettes are safer than regular cigarettes. The National Health Insurance Service seeks to recover approximately $53.7 million allegedly incurred in treating 3,484 patients with small cell lung cancer, squamous cell lung cancer, and squamous cell laryngeal cancer from 2003 to 2012. The case is now in the evidentiary phase.

Label-Related Cases: These cases, brought by individual plaintiffs, or on behalf of a class or purported class of individual plaintiffs, allege that the use of the descriptor "Lights" or other alleged misrepresentations or omissions of labeling information constitute fraudulent and misleading conduct. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including misrepresentation, deception, and breach of consumer protection laws. Plaintiffs seek various forms of relief including restitution, injunctive relief, and compensatory and other damages. Defenses raised include lack of causation, lack of reliance, assumption of the risk, and statute of limitations.

As of February 9, 2018, there was 1 case brought by an individual plaintiff in Italy (1) pending against our subsidiaries, compared with 3 such cases on December 31, 2016, and 3 such cases on December 31, 2015, and one purported class action in Israel (1).

An individual plaintiff filed the purported class action, *Aharon Ringer v. Philip Morris Ltd. and Globrands Ltd.,* on July 18, 2017, in the Central District Court of Israel. Our Israeli affiliate and an Israeli importer and distributor for other multinational tobacco companies are defendants. Plaintiff seeks to represent a class of smokers in Israel who have purchased cigarettes imported by defendants since July 18, 2010. Plaintiff estimates the class size to be 7,000,000 smokers. Plaintiff alleges that defendants misled consumers by not disclosing sufficient information about carbon monoxide, tar, and nicotine yields of, and tobacco contained in, the imported cigarettes. Plaintiff seeks various forms of relief, including an order for defendants to label cigarette packs in accordance with plaintiff's demands, and damages for misleading consumers, breach of autonomy and unjust enrichment.

Public Civil Actions: Claims have been filed either by an individual, or a public or private entity, seeking to protect collective or individual rights, such as the right to health, the right to information or the right to safety. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including product defect, concealment, and misrepresentation. Plaintiffs in these cases seek various forms of relief including injunctive relief such as banning cigarettes, descriptors, smoking in certain places and advertising, as well as implementing communication campaigns and reimbursement of medical expenses incurred by public or private institutions.

As of February 9, 2018, there were 2 public civil actions pending against our subsidiaries in Argentina (1) and Venezuela (1), compared with 2 such cases on December 31, 2016, and 3 such cases on December 31, 2015.

In the public civil action in Argentina, *Asociación Argentina de Derecho de Danos v. Massalin Particulares S.A., et al., Civil Court of Buenos Aires, Argentina,* filed February 26, 2007, our subsidiary and another member of the industry are defendants. The plaintiff, a consumer association, seeks the establishment of a relief fund for reimbursement of medical costs associated with diseases allegedly caused by smoking. Our subsidiary filed its answer in September 2007. In March 2010, the case file was transferred to the Federal Court on Administrative Matters after the Civil Court granted plaintiff's request to add the national government as a co-plaintiff in the case. The case is currently in the evidentiary stage.

In the public civil action in Venezuela, *Federation of Consumers and Users Associations ("FEVACU"), et al. v. National Assembly of Venezuela and the Venezuelan Ministry of Health, Constitutional Chamber of the Venezuelan Supreme Court*, filed April 29, 2008, we were not named as a defendant, but the plaintiffs published a notice pursuant to court order, notifying all interested parties to appear in the case. In January 2009, our subsidiary appeared in the

case in response to this notice. The plaintiffs purport to represent the right to health of the citizens of Venezuela and claim that the government failed to protect adequately its citizens' right to health. The claim asks the court to order the government to enact stricter regulations on the manufacture and sale of tobacco products. In addition, the plaintiffs ask the court to order companies involved in the tobacco industry to allocate a percentage of their “sales or benefits” to establish a fund to pay for the health care costs of treating smoking-related diseases. In October 2008, the court ruled that plaintiffs have standing to file the claim and that the claim meets the threshold admissibility requirements. In December 2012, the court admitted our subsidiary and BAT's subsidiary as interested third parties. In February 2013, our subsidiary answered the complaint.

Other Litigation

The Department of Special Investigations of the government of Thailand ("DSI") conducted an investigation into alleged underpayment by our subsidiary, Philip Morris (Thailand) Limited ("PM Thailand"), of customs duties and excise taxes relating to imports from the Philippines covering the period 2003-2007. On January 18, 2016, the Public Prosecutor filed charges against our subsidiary and seven former and current employees in the Bangkok Criminal Court alleging that PM Thailand and the individual defendants jointly and with the intention to defraud the Thai government, under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries of cigarettes from the Philippines during the period of July 2003 to June 2006. The government is seeking a fine of approximately THB 80.8 billion (approximately $2.54 billion). In May 2017, the King of Thailand signed a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. Trial in the case began in November 2017 and is presently expected to conclude in April 2018. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and other Thai governmental agencies.

The DSI also conducted an investigation into alleged underpayment by PM Thailand of customs duties and excise taxes relating to imports from Indonesia covering the period 2000-2003. On January 26, 2017, the Public Prosecutor filed charges against PM Thailand and its former Thai employee in the Bangkok Criminal Court alleging that PM Thailand and its former employee jointly and with the intention to defraud the Thai government under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries during the period from January 2002 to July 2003. The government is seeking a fine of approximately THB 19.8 billion (approximately $621 million). The case is in pre-trial proceedings. The trial is scheduled to begin in the last quarter of 2018. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law, and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and a Thai court. In May 2017, the King of Thailand signed a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. On November 29, 2017, PM Thailand received notices of assessment in the aggregate amount of approximately THB 25.6 billion (approximately $803 million) from the Thai Customs Department alleging that PM Thailand under-declared customs values for the imports from Indonesia covering the period 2001-2003. The notices include the Indonesian import entries subject to the proceedings discussed above and are in addition to the fine sought by the government in the criminal proceedings. PM Thailand filed its appeal against the notices in December 2017. We believe that all of the notices of assessment are barred by the applicable statutes of limitations and are otherwise without merit.

The South Korean Board of Audit and Inspection ("BAI") conducted an audit of certain Korean government agencies and the tobacco industry into whether inventory movements ahead of the January 1, 2015 increase of cigarette-related taxes by tobacco companies, including Philip Morris Korea Inc. ("PM Korea"), our South Korean affiliate, were in compliance with South Korean tax laws. In November 2016, the tax authorities completed their audit and assessed allegedly underpaid taxes and penalties. In order to avoid nonpayment financial costs, PM Korea paid approximately KRW 272 billion (approximately $249 million), of which KRW 100 billion (approximately $92 million) was paid in 2016 and KRW 172 billion (approximately $157 million) was paid in the first quarter of 2017. These amounts are included in other assets in the consolidated balance sheets and in cash used in operating activities in the consolidated statements of cash flows. PM Korea is appealing the assessments. The tax authorities have also referred the matter to the Public Prosecutor, who will further investigate and decide whether to file criminal charges against PM Korea and/or other alleged co-offenders. If the Public Prosecutor decides to prosecute, it may seek up to three times the underpaid tax for company criminal penalties and up to five times the underpaid tax for individual criminal penalties. PM Korea believes that it has paid cigarette-related taxes in compliance with the South Korean tax laws. In addition, the South Korean Ministry of Strategy and Finance ("MOSF") filed a criminal complaint with the Public Prosecutor against PM Korea and its managing director. In its criminal complaint, the MOSF alleged that PM Korea exceeded the monthly product withdrawal limits that the MOSF had set in its notice. The Public Prosecutor will investigate the MOSF's criminal complaint and decide whether to prosecute. PM Korea disagrees with the MOSF's allegations.

We are also involved in additional litigation arising in the ordinary course of our business. While the outcomes of these proceedings are uncertain, management does not expect that the ultimate outcomes of other litigation, including any reasonably possible losses in excess of current accruals, will have a material adverse effect on our consolidated results of operations, cash flows or financial position.

Note 19.

Balance Sheet Offsetting:

Derivative Financial Instruments

PMI uses foreign exchange contracts and interest rate contracts to mitigate its exposure to changes in exchange and interest rates from third-party and intercompany actual and forecasted transactions. Substantially all of PMI's derivative financial instruments are subject to master netting arrangements, whereby the right to offset occurs in the event of default by a participating party. While these contracts contain the enforceable right to offset through close-out netting rights, PMI elects to present them on a gross basis in the consolidated balance sheets. Collateral associated with these arrangements is in the form of cash and is unrestricted. See Note 15. *Financial Instruments* for disclosures related to PMI's derivative financial instruments.

The effects of these derivative financial instrument assets and liabilities on PMI's consolidated balance sheets were as follows:

				Gross Amounts Not Offset in the Consolidated Balance Sheet		
(in millions)	**Gross Amounts Recognized**	**Gross Amount Offset in the Consolidated Balance Sheet**	**Net Amounts Presented in the Consolidated Balance Sheet**	**Financial Instruments**	**Cash Collateral Received/ Pledged**	**Net Amount**
At December 31, 2017						
Assets						
Foreign exchange contracts	**$ 140**	**$ —**	**$ 140**	**$ (50)**	**$ (78)**	**$ 12**
Liabilities						
Foreign exchange contracts	**$ 1,128**	**$ —**	**$ 1,128**	**$ (50)**	**$ (1,004)**	**$ 74**
At December 31, 2016						
Assets						
Foreign exchange contracts	$ 813	$ —	$ 813	$ (126)	$ (607)	$ 80
Liabilities						
Foreign exchange contracts	$ 163	$ —	$ 163	$ (126)	$ (31)	$ 6

Note 20.

Sale of Accounts Receivable:

To mitigate risk and enhance cash and liquidity management PMI sells trade receivables to unaffiliated financial institutions. These arrangements allow PMI to sell, on an ongoing basis, certain trade receivables without recourse. The trade receivables sold are generally short-term in nature and are removed from the consolidated balance sheets. PMI sells trade receivables under two types of arrangements, servicing and non-servicing. For servicing arrangements, PMI continues to service the sold trade receivables on an administrative basis and does not act on behalf of the unaffiliated financial institutions. When applicable, a servicing liability is recorded for the estimated fair value of the servicing. The amounts associated with the servicing liability were not material for the years ended December 31, 2017 and 2016. Under the non-servicing arrangements, PMI does not provide any administrative support or servicing after the trade receivables have been sold to the unaffiliated financial institutions.

Cumulative trade receivables sold, including excise taxes, for the years ended December 31, 2017 and 2016, were $10,003 million and $9,447 million, respectively. PMI’s operating cash flows were positively impacted by the

amount of the trade receivables sold and derecognized from the consolidated balance sheets, which remained outstanding with the unaffiliated financial institutions. The trade receivables sold that remained outstanding under these arrangements as of December 31, 2017, 2016 and 2015, were $1,092 million, $729 million and $888 million, respectively. The net proceeds received are included in cash provided by operating activities in the consolidated statements of cash flows. The difference between the carrying amount of the trade receivables sold and the sum of the cash received is recorded as a loss on sale of trade receivables within marketing, administration and research costs in the consolidated statements of earnings. For the years ended December 31, 2017, 2016 and 2015 the loss on sale of trade receivables was immaterial.

Note 21.

New Accounting Standards:

On February 25, 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ASU 2016-02, "Leases" ("ASU 2016-02"). ASU 2016-02 requires organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases. Additionally, ASU 2016-02 modifies current guidance for lessors' accounting. ASU 2016-02 is effective for interim and annual reporting periods beginning on or after January 1, 2019, with early adoption permitted. PMI has identified its lease management system and is in the process of identifying and evaluating the applicable leases. PMI is currently assessing the impact that the adoption of ASU 2016-02 will have on its financial position and results of operations.

On January 5, 2016, the FASB issued Accounting Standard Update ASU 2016-01, "Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities" ("ASU 2016-01"). ASU 2016-01 will require equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. Additionally, ASU 2016-01 also changes certain disclosure requirements and other aspects of current U.S. GAAP. ASU 2016-01 is effective for interim and annual reporting periods beginning on or after January 1, 2018. PMI has identified certain cost investments which are applicable to ASU 2016-01. At January 1, 2018, the cumulative effect of this change to PMI's Earnings Reinvested in the Business is an increase of $238 million, which is net of $63 million in taxes.

On May 28, 2014, the FASB issued Accounting Standards Update ASU 2014-09, "Revenue from Contracts with Customers" ("ASU 2014-09"). ASU 2014-09 contains principles that an entity will need to apply to determine the measurement of revenue and timing of when it is recognized. The underlying principle is that an entity will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

ASU 2014-09 is effective for interim and annual reporting periods beginning on or after January 1, 2017. In July 2015, the FASB approved a proposal which allows for a deferral of the implementation until January 1, 2018, and permits early application, but not before the original effective date of January 1, 2017. In addition to the guidance in ASU 2014-09, PMI has evaluated ASU 2016-12, which was issued in May 2016 and provides some practical expedients to the original standard. As a result of this evaluation, PMI made an accounting policy election to exclude excise taxes collected from customers from the measurement of the transaction price, thereby presenting revenues, net of excise taxes. PMI has adopted ASU 2014-09 on January 1, 2018 retrospectively to each prior period presented. PMI has elected this transition method solely to reflect the change in excise tax presentation in all prior periods. Based on PMI's assessment to date, the underlying principles of the new standard, relating to the measurement of revenue and the timing of recognition, are closely aligned with PMI's current business model and practices. As a result, other than excise tax presentation, the adoption of ASU 2014-09 will not have any other material impact on the consolidated financial position or results of operations.

Note 22.

Quarterly Financial Data (Unaudited):

(in millions, except per share data)	2017 Quarters			
	1st	2nd	3rd	4th
Net revenues	**$ 16,556**	**$ 19,319**	**$ 20,638**	**$ 21,585**
Gross profit	**$ 3,887**	**$ 4,398**	**$ 4,738**	**$ 5,293**
Net earnings attributable to PMI	**$ 1,590**	**$ 1,781**	**$ 1,970**	**$ 694**
Per share data:				
Basic EPS	**$ 1.02**	**$ 1.14**	**$ 1.27**	**$ 0.44**
Diluted EPS	**$ 1.02**	**$ 1.14**	**$ 1.27**	**$ 0.44**
Dividends declared	**$ 1.04**	**$ 1.04**	**$ 1.07**	**$ 1.07**
Market price:				
— High	**$ 114.65**	**$ 123.55**	**$ 121.69**	**$ 115.28**
— Low	**$ 89.97**	**$ 108.56**	**$ 109.31**	**$ 101.58**

(in millions, except per share data)	2016 Quarters			
	1st	2nd	3rd	4th
Net revenues	$ 16,788	$ 19,041	$ 19,935	$ 19,189
Gross profit	$ 3,987	$ 4,285	$ 4,550	$ 4,472
Net earnings attributable to PMI	$ 1,530	$ 1,788	$ 1,938	$ 1,711
Per share data:				
Basic EPS	$ 0.98	$ 1.15	$ 1.25	$ 1.10
Diluted EPS	$ 0.98	$ 1.15	$ 1.25	$ 1.10
Dividends declared	$ 1.02	$ 1.02	$ 1.04	$ 1.04
Market price:				
— High	$ 99.53	$ 102.55	$ 104.20	$ 98.21
— Low	$ 84.46	$ 95.91	$ 96.95	$ 86.78

Basic and diluted EPS are computed independently for each of the periods presented. Accordingly, the sum of the quarterly EPS amounts may not agree to the total for the year.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of
Philip Morris International Inc. and Subsidiaries:

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Philip Morris International Inc. and its subsidiaries (PMI) as of December 31, 2017 and 2016, and the related consolidated statements of earnings, comprehensive earnings, stockholders' (deficit) equity and of cash flows for each of the three years in the periods ended December 31, 2017, including the related notes (collectively referred to as the "consolidated financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2017, based on criteria established in *Internal Control - Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of PMI as of December 31, 2017 and 2016, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2017 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, PMI maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Basis for Opinions

PMI's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Report of Management on Internal Control over Financial Reporting. Our responsibility is to express opinions on PMI's consolidated financial statements and on PMI's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly

reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PricewaterhouseCoopers SA

/S/ BARRY J. MISTHAL	/S/ DR. MICHAEL ABRESCH
Barry J. Misthal	Dr. Michael Abresch

Lausanne, Switzerland
February 13, 2018

PricewaterhouseCoopers SA has served as the Company's auditor since 2008.

Report of Management on Internal Control Over Financial Reporting

Management of Philip Morris International Inc. ("PMI") is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended. PMI's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes those written policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of PMI;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America;
- provide reasonable assurance that receipts and expenditures of PMI are being made only in accordance with the authorization of management and directors of PMI; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets that could have a material effect on the consolidated financial statements.

Internal control over financial reporting includes the controls themselves, monitoring and internal auditing practices and actions taken to correct deficiencies as identified.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of PMI's internal control over financial reporting as of December 31, 2017. Management based this assessment on criteria for effective internal control over financial reporting described in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management's assessment included an evaluation of the design of PMI's internal control over financial reporting and testing of the operational effectiveness of its internal control over financial reporting. Management reviewed the results of its assessment with the Audit Committee of our Board of Directors.

Based on this assessment, management determined that, as of December 31, 2017, PMI maintained effective internal control over financial reporting.

PricewaterhouseCoopers SA, an independent registered public accounting firm, who audited and reported on the consolidated financial statements of PMI included in this report, has audited the effectiveness of PMI's internal control over financial reporting as of December 31, 2017, as stated in their report herein.

February 13, 2018

Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.*

None.

Item 9A. *Controls and Procedures.*

PMI carried out an evaluation, with the participation of PMI's management, including PMI's Chief Executive Officer and Chief Financial Officer, of the effectiveness of PMI's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based upon that evaluation, PMI's Chief Executive Officer and Chief Financial Officer concluded that PMI's disclosure controls and procedures are effective. There have been no changes in PMI's internal control over financial reporting during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, PMI's internal control over financial reporting.

The Report of Management on Internal Control over Financial Reporting and the Report of Independent Registered Public Accounting Firm are included in Item 8.

Item 9B. *Other Information.*

None.

PART III

Except for the information relating to the executive officers set forth in Item 10 and the information relating to equity compensation plans set forth in Item 12, the information called for by Items 10-14 is hereby incorporated by reference to PMI's definitive proxy statement for use in connection with its annual meeting of stockholders to be held on May 9, 2018, that will be filed with the SEC on or about March 29, 2018 (the "proxy statement"), and, except as indicated therein, made a part hereof.

Item 10. *Directors, Executive Officers and Corporate Governance.*

Executive Officers as of February 9, 2018:

Name	Office	Age
André Calantzopoulos	Chief Executive Officer	60
Massimo Andolina	Senior Vice President, Operations	49
Drago Azinovic	President, Middle East & Africa Region and PMI Duty Free	55
Werner Barth	Senior Vice President, Commercial	53
Charles Bendotti	Senior Vice President, People and Culture	45
Patrick Brunel	Chief Information Officer	52
Frank de Rooij	Vice President, Treasury and Corporate Finance	52
Frederic de Wilde	President, European Union Region	50
Marc S. Firestone	President, External Affairs and General Counsel	58
Paul Janelle	Vice President, Corporate Planning and Business Development	52
Stacey Kennedy	President, South and Southeast Asia Region	45
Martin G. King	Chief Financial Officer	53
Andreas Kurali	Vice President and Controller	52
Marco Mariotti	President, Eastern Europe Region	53
Jacek Olczak	Chief Operating Officer	53
Jeanne Pollès	President, Latin America & Canada Region	52
Paul Riley	President, East Asia and Australia Region	52
Jaime Suarez	Chief Digital Officer	44
Jerry E. Whitson	Deputy General Counsel and Corporate Secretary	62
Miroslaw Zielinski	President, Science and Innovation	56

All of the above-mentioned officers have been employed by us in various capacities during the past five years.

Codes of Conduct and Corporate Governance

We have adopted the Philip Morris International Code of Conduct, which complies with requirements set forth in Item 406 of Regulation S-K. This Code of Conduct applies to all of our employees, including our principal executive officer, principal financial officer, principal accounting officer or controller, and persons performing similar functions. We have also adopted a code of business conduct and ethics that applies to the members of our Board of Directors. These documents are available free of charge on our website at www.pmi.com.

In addition, we have adopted corporate governance guidelines and charters for our Audit, Finance, Compensation and Leadership Development, Product Innovation and Regulatory Affairs and Nominating and Corporate Governance committees of the Board of Directors. All of these documents are available free of charge on our website at www.pmi.com. Any waiver granted by Philip Morris International Inc. to its principal executive officer, principal financial officer or controller or any person performing similar functions under the Code of Conduct, or certain amendments to the Code of Conduct, will be disclosed on our website at www.pmi.com.

The information on our website is not, and shall not be deemed to be, a part of this Report or incorporated into any other filings made with the SEC.

Also refer to *Board Operations and Governance - Committees of the Board*, *Election of Directors - Process for Nominating Directors* and *Election of Directors - Director Nominees* and *Section 16(a) Beneficial Ownership Reporting Compliance* sections of the proxy statement.

Item 11. *Executive Compensation.*

Refer to *Compensation Discussion and Analysis* and *Compensation of Directors* sections of the proxy statement.

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.*

The number of shares to be issued upon exercise or vesting and the number of shares remaining available for future issuance under PMI's equity compensation plans at December 31, 2017, were as follows:

	Number of Securities to be Issued upon Exercise of Outstanding Options and Vesting of RSUs (a)	Weighted Average Exercise Price of Outstanding Options (b)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (excluding Securities reflected in column (a)) (c)
Equity compensation plans approved by stockholders	5,254,460[1]	$ —	25,991,850

[1] Represents 3,612,400 shares of common stock that may be issued upon vesting of the restricted share units and 1,642,060 shares that may be issued upon vesting of the performance share units if maximum performance targets are achieved for each performance cycle. PMI has not granted options since the spin-off from Altria on March 28, 2008.

Item 13. *Certain Relationships and Related Transactions, and Director Independence.*

Refer to *Related Person Transactions and Code of Conduct* and *Election of Directors - Independence of Nominees* sections of the proxy statement.

Item 14. *Principal Accounting Fees and Services.*

Refer to *Audit Committee Matters* section of the proxy statement.

PART IV

Item 15. *Exhibits and Financial Statement Schedules.*

(a) Index to Consolidated Financial Statements and Schedules

	Page
Consolidated Balance Sheets at December 31, 2017 and 2016	69 - 70
Consolidated Statements of Earnings for the years ended December 31, 2017, 2016 and 2015	71
Consolidated Statements of Comprehensive Earnings for the years ended December 31, 2017, 2016 and 2015	72
Consolidated Statements of Stockholders' (Deficit) Equity for the years ended December 31, 2017, 2016 and 2015	73
Consolidated Statements of Cash Flows for the years ended December 31, 2017, 2016 and 2015	74 - 75
Notes to Consolidated Financial Statements	76 - 118
Report of Independent Registered Public Accounting Firm	119 - 120
Report of Management on Internal Control Over Financial Reporting	121

Schedules have been omitted either because such schedules are not required or are not applicable.

(b) The following exhibits are filed as part of this Report:

2.1	—	Distribution Agreement between Altria Group, Inc. and Philip Morris International Inc. dated January 30, 2008 (incorporated by reference to Exhibit 2.1 to the Registration Statement on Form 10 filed February 7, 2008).
3.1	—	Amended and Restated Articles of Incorporation of Philip Morris International Inc. (incorporated by reference to Exhibit 3.1 to the Registration Statement on Form 10 filed February 7, 2008).
3.2	—	Amended and Restated By-laws of Philip Morris International Inc., effective as of January 1, 2018 (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed September 28, 2017).
4.1	—	Specimen Stock Certificate of Philip Morris International Inc. (incorporated by reference to Exhibit 4.1 to the Registration Statement on Form 10 filed February 7, 2008).
4.2	—	Indenture dated as of April 25, 2008, between Philip Morris International Inc. and HSBC Bank USA, National Association, as Trustee (incorporated by reference to Exhibit 4.3 to the Registration Statement on Form S-3, dated April 25, 2008).
4.6	—	The Registrant agrees to furnish copies of any instruments defining the rights of holders of long-term debt of the Registrant and its consolidated subsidiaries that does not exceed 10 percent of the total assets of the Registrant and its consolidated subsidiaries to the Commission upon request.
10.1	—	Employee Matters Agreement between Altria Group, Inc. and Philip Morris International Inc., dated as of March 28, 2008 (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed March 31, 2008).
10.2	—	Intellectual Property Agreement between Philip Morris International Inc. and Philip Morris USA Inc., dated as of January 1, 2008 (incorporated by reference to Exhibit 10.4 to the Registration Statement on Form 10 filed March 5, 2008).
10.3	—	Credit Agreement relating to a US$3,500,000,000 Revolving Credit Facility (including a US$800,000,000 swingline option) dated as of October 25, 2011, among Philip Morris International Inc. and the Initial Lenders named therein and Citibank International plc, as Facility Agent, and Citibank, N.A., as Swingline Agent, and Citigroup Global Markets Limited, Barclays Capital, BNP Paribas, Credit Suisse AG, Cayman Islands Branch, Deutsche Bank Securities Inc., Goldman Sachs International, HSBC Bank PLC, J.P. Morgan Limited, RBS Securities Inc. and Société Générale as Mandated Lead Arrangers and Bookrunners (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed October 26, 2011).
10.4	—	Amendment No. 1, dated as of August 31, 2012, to the Credit Agreement, dated as of October 25, 2011, among Philip Morris International Inc., the lenders named therein and Citibank International plc, as Facility Agent (incorporated by reference to Exhibit 10.6 to the Quarterly Report on Form 10-Q for the quarter ended September 30, 2012).
10.5	—	Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 15, 2013).
10.6	—	Extension Agreement, effective February 7, 2017, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders party thereto, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 30, 2017).
10.7	—	Extension Agreement, effective January 31, 2014, to Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders party thereto and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.3 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2014).

10.8	—	Credit Agreement, dated as of February 28, 2014, among Philip Morris International Inc., the lenders named therein, J.P. Morgan Europe Limited, as Facility Agent, and JPMorgan Chase Bank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed March 3, 2014).
10.9	—	Extension Agreement, effective as of February 10, 2015, to Credit Agreement dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein and Citibank Europe PLC, UK Branch (formerly, The Royal Bank of Scotland plc), as Administrative Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 29, 2015).
10.10	—	Extension Agreement, effective as of February 28, 2015, to the Credit Agreement, dated as of February 28, 2014, among Philip Morris International Inc., the lenders named therein, J.P. Morgan Europe Limited, as Facility Agent, and JPMorgan Chase Bank, N.A. as Swingline Agent (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed January 29, 2015).
10.11	—	Amendment No. 1, dated as of July 20, 2015, to the Credit Agreement, dated as of February 12, 2013, among Philip Morris International Inc., the lenders named therein, The Royal Bank of Scotland plc, as resigning administrative agent, and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as successor administrative agent (incorporated by reference to Exhibit 10.52 to the Annual Report on Form 10-K for the year ended December 31, 2015).
10.12	—	Credit Agreement, dated as of October 1, 2015, among Philip Morris International Inc., the lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as Facility Agent, and Citibank, N.A., as Swingline Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed October 5, 2015).
10.13	—	Amendment No. 2, effective as of February 9, 2016, to the Credit Agreement dated as of February 12, 2013, with the lenders named therein and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed January 28, 2016).
10.14	—	Extension Agreement, effective February 28, 2016, to the Credit Agreement, dated as of February 28, 2014, among Philip Morris International Inc., each lender named therein, J.P. Morgan Europe Limited, as facility agent, and JPMorgan Chase Bank, N.A., as swingline agent (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed January 28, 2016).
10.15	—	Extension Agreement, effective as of October 1, 2016, to the Credit Agreement dated as of October 1, 2015, among Philip Morris International Inc., lenders named therein, Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as facility agent, and Citibank, N.A., as swingline agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 31, 2016).
10.16	—	Extension Agreement, effective October 1, 2017, to the Credit Agreement, dated as of October 1, 2015, among Philip Morris International Inc., the lenders party thereto and Citibank Europe PLC, UK Branch (formerly, Citibank International Limited), as facility agent, and Citibank N.A., as swingline agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 29, 2017).
10.17	—	Philip Morris International Inc. Automobile Policy (incorporated by reference to Exhibit 10.8 to the Registration Statement on Form 10 filed February 7, 2008).*
10.18	—	Philip Morris International Benefit Equalization Plan, as amended and in effect on August 6, 2012 (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended September 30, 2012).*
10.19	—	Philip Morris International Inc. 2012 Performance Incentive Plan, effective May 9, 2012 (incorporated by reference to Exhibit A to the Definitive Proxy Statement filed on March 30, 2012).*
10.20	—	

Philip Morris International Inc. 2017 Performance Incentive Plan, effective May 3, 2017 (incorporated by reference to Exhibit B to the Definitive Proxy Statement filed on March 23, 2017).*

10.21	—	Pension Fund of Philip Morris in Switzerland (IC) (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2015).*
10.22	—	Summary of Supplemental Pension Plan of Philip Morris in Switzerland (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).*
10.23	—	Form of Restated Employee Grantor Trust Enrollment Agreement (Executive Trust Arrangement) (incorporated by reference to Exhibit 10.18 to the Registration Statement on Form 10 filed February 7, 2008).*
10.24	—	Form of Restated Employee Grantor Trust Enrollment Agreement (Secular Trust Arrangement) (incorporated by reference to Exhibit 10.19 to the Registration Statement on Form 10 filed February 7, 2008).*
10.25	—	Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors, effective May 3, 2017 (incorporated by reference to Exhibit C to the Definitive Proxy Statement filed on March 23, 2017).*
10.26	—	Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors (as amended and restated as of January 1, 2018).*
10.27	—	Philip Morris International Inc. 2008 Deferred Fee Plan for Non-Employee Directors (incorporated by reference to Exhibit 10.21 to the Registration Statement on Form 10 filed February 7, 2008).*
10.28	—	Supplemental Letter to the Employment Agreement (as amended) with André Calantzopoulos (incorporated by reference to Exhibit 10.4 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017). The Employment Agreement was previously filed as Exhibit 10.22 to the Registration Statement on Form 10 filed February 7, 2008 and is incorporated by reference to this Exhibit 10.28. The Amendment to the Employment Agreement was previously filed as Exhibit 10.1 to the Current Report on Form 8-K/A filed June 13, 2013, and is incorporated by reference to this Exhibit 10.28.*
10.29	—	Supplemental Letter to Employment Agreement with Marc S. Firestone (incorporated by reference to Exhibit 10.5 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017). The Employment Agreement was previously filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 and is incorporated by reference to this Exhibit 10.29. The Amendment to the Employment Agreement was previously filed as Exhibit 10.25 to the Annual Report on Form 10-K for the year ended December 31, 2013, and is incorporated by reference to this Exhibit 10.29.*
10.30	—	Employment Agreement as of January 1, 2018 with Martin G. King. The previous Employment Agreement was filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2015, and is incorporated by reference to this Exhibit 10.30. The Amendments to the previous Employment Agreement were filed as Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended September 30, 2015 and as Exhibit 10.6 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017 and are incorporated by reference to this Exhibit 10.30. *
10.31	—	Supplemental Letter to the Employment Agreement (as amended) with Jacek Olczak (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K/A filed December 12, 2017). The Employment Agreement was previously filed as Exhibit 10.4 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, and is incorporated by reference to this Exhibit 10.31. The Amendments to the Employment Agreement were previously filed as Exhibit 10.33 to the Annual Report on Form 10-K for the year ended December 31, 2013 and as Exhibit 10.7 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017 and are incorporated by reference to this Exhibit 10.31.*
10.32	—	Supplemental Letter to the Employment Agreement (as amended) with Miroslaw Zielinski (incorporated by reference to Exhibit 10.3 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2017). The Employment Agreement was previously filed as Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 and is incorporated by reference to this Exhibit 10.32. The Amendments to the Employment Agreement were previously filed as Exhibit 10.28 to the Annual Report on Form 10-K for the year ended December 31, 2013 and as Exhibit

		10.8 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2017, and are incorporated by reference to this Exhibit 10.32.*
10.33	—	Time Sharing Agreement between PMI Global Services Inc. and Louis C. Camilleri dated August 18, 2010 (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed August 19, 2010).*

10.34	—	Amendment No. 1 to the Time Sharing Agreement between PMI Global Services Inc. and Louis C. Camilleri, dated August 22, 2012 (incorporated by reference to Exhibit 10.4 to the Quarterly Report on Form 10-Q for the quarter ended September 30, 2012).*
10.35	—	Amendment No. 2 to the Time Sharing Agreement between PMI Global Services Inc. and Louis C. Camilleri, dated October 23, 2012 (incorporated by reference to Exhibit 10.27 to the Annual Report on Form 10-K for the year ended December 31, 2012).*
10.36	—	Amendment No. 3 to the Time Sharing Agreement between PMI Global Services Inc. and Louis C. Camilleri, dated December 31, 2014 (incorporated by reference to Exhibit 10.34 to the Annual Report on Form 10-K for the year ended December 31, 2014).*
10.37	—	Time Sharing Agreement between PMI Global Services Inc. and André Calantzopoulos, dated May 8, 2013 (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2013).*
10.38	—	Amendment No. 1 to the Time Sharing Agreement between PMI Global Services Inc. and André Calantzopoulos, dated December 23, 2014 (incorporated by reference to Exhibit 10.36 to the Annual Report on Form 10-K for the year ended December 31, 2014).*
10.39	—	Agreement with Louis C. Camilleri (incorporated by reference to Exhibit 10.25 to the Registration Statement on Form 10 filed February 7, 2008).*
10.40	—	Amended and Restated Supplemental Management Employees' Retirement Plan (incorporated by reference to Exhibit 10.27 to the Annual Report on Form 10-K for the year ended December 31, 2008).*
10.41	—	Supplemental Equalization Plan, amended and restated as of June 29, 2015 (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2015).*
10.42	—	Form of Supplemental Equalization Plan Employee Grantor Trust Enrollment Agreement (Secular Trust) (incorporated by reference to Exhibit 10.31 to the Annual Report on Form 10-K for the year ended December 31, 2008).*
10.43	—	Form of Supplemental Equalization Plan Employee Grantor Trust Enrollment Agreement (Executive Trust) (incorporated by reference to Exhibit 10.32 to the Annual Report on Form 10-K for the year ended December 31, 2008).*
10.44	—	Philip Morris International Inc. Form of Indemnification Agreement with Directors and Executive Officers (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed September 18, 2009).*
10.45	—	Form of Deferred Stock Agreement (2014 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 7, 2014).*
10.46	—	Form of Deferred Stock Agreement (2015 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 10, 2015).*
10.47	—	Philip Morris International Inc. Tax Return Preparation Services Policy (incorporated by reference to Exhibit 10.51 to the Annual Report on Form 10-K for the year ended December 31, 2014).*
10.48	—	Form of Restricted Stock Unit Agreement (2016 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 9, 2016).*
10.49	—	Form of Performance Share Unit Agreement (2016 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 9, 2016).*
10.50	—	Form of Restricted Stock Unit Agreement (2017 Grants) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed February 7, 2017).*
10.51	—	Form of Performance Share Unit Agreement (2017 Grants) (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed February 7, 2017).*

10.52	—	Philip Morris International Inc. 2008 Stock Compensation Plan for Non-Employee Directors (amended and restated as of January 1, 2015) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed December 15, 2014).*
12	—	Statement regarding computation of ratios of earnings to fixed charges.
21	—	Subsidiaries of Philip Morris International Inc.
23	—	Consent of independent registered public accounting firm.
24	—	Powers of attorney.
31.1	—	Certification of the Registrant's Chief Executive Officer pursuant to Rule 13a-14(a)/ 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	—	Certification of the Registrant's Chief Financial Officer pursuant to Rule 13a-14(a)/ 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	—	Certification of the Registrant's Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	—	Certification of the Registrant's Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	—	XBRL Instance Document.
101.SCH	—	XBRL Taxonomy Extension Schema.
101.CAL	—	XBRL Taxonomy Extension Calculation Linkbase.
101.DEF	—	XBRL Taxonomy Extension Definition Linkbase.
101.LAB	—	XBRL Taxonomy Extension Label Linkbase.
101.PRE	—	XBRL Taxonomy Extension Presentation Linkbase.

* Denotes management contract or compensatory plan or arrangement in which directors or executive officers are eligible to participate.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PHILIP MORRIS INTERNATIONAL INC.

By: /s/ ANDRÉ CALANTZOPOULOS

(André Calantzopoulos
Chief Executive Officer)

Date: February 13, 2018

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated:

Signature	Title	Date
/s/ ANDRÉ CALANTZOPOULOS (André Calantzopoulos)	Chief Executive Officer	February 13, 2018
/s/ MARTIN G. KING (Martin G. King)	Chief Financial Officer	February 13, 2018
/s/ ANDREAS KURALI (Andreas Kurali)	Vice President and Controller	February 13, 2018
*HAROLD BROWN, LOUIS C. CAMILLERI, MASSIMO FERRAGAMO, WERNER GEISSLER, JENNIFER LI, JUN MAKIHARA, SERGIO MARCHIONNE, KALPANA MORPARIA, LUCIO A. NOTO, FREDERIK PAULSEN, ROBERT B. POLET, STEPHEN M. WOLF	Directors	
*By: /s/ ANDRÉ CALANTZOPOULOS (André Calantzopoulos Attorney-in-fact)		February 13, 2018