Philip Morris International Inc.
Form 10-K
February 13, 2018

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

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 þ 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 þ 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. þ

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 þ		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 þ

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

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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.

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)%

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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:

(in millions)	For the Years Ended December 31, 2017	2016	Variance $	%
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, 2016	2015	Variance $	%
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, 2016	2015	Variance $	%
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		
			Change
	2017	2016	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.

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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.

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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	For the Years Ended December 31,		Variance	
(in millions)	2017	2016	$	%
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.

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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	For the Years Ended December 31,		Variance	
(in millions)	2017	2016	$	%
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.

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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	For the Years Ended December 31,		Variance	
(in millions)	2017	2016	$	%
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.

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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	For the Years Ended December 31,		Variance	
(in millions)	2016	2015	$	%
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	For the Years Ended December 31,		Variance	
(in millions)	2016	2015	$	%
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	For the Years Ended December 31,		Variance	
(in millions)	2016	2015	$	%
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	For the Years Ended December 31,		Variance	
(in millions)	2016	2015	$	%
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

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.

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.

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.

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).

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

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.

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.

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	