Altria Group, Inc. (MO)

$51.02 (As of 01/17/20)

Price Target (6-12 Months): **$54.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 05/01/19) Prior Recommendation: Underperform	**Neutral**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**3-Hold**
	Zacks Style Scores:	VGM:B
	Value: B | Growth: B	Momentum: F

Summary

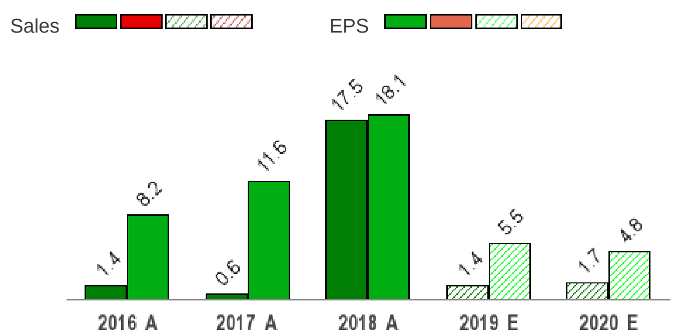
Altria's shares have gained but lagged the industry in the past three months. The company is grappling with headwinds surrounding the cigarette unit. Management expects volumes at the domestic cigarette industry to decline 5-6% in 2019. In this context, tight regulations surrounding sales and marketing of cigarettes along with consumers' rising health awareness are deterrents. Nonetheless, prudent pricing strategies have been aiding Altria to boost revenues in its smokeable and smokeless units as witnessed during the third quarter of 2019. During the quarter, earnings and revenues improved year on year. Further, Altria is on track with the expansion of IQOS in the United States. It has also undertaken several partnerships to widen smokeless offerings. Further, the company is progressing well with cost-reduction plans.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$57.88 - $39.30**
20 Day Average Volume (sh)	**6,955,387**
Market Cap	**$95.3 B**
YTD Price Change	**2.2%**
Beta	**0.44**
Dividend / Div Yld	**$3.36 / 6.6%**
Industry	**Tobacco**
Zacks Industry Rank	**Top 34% (87 out of 254)**
Last EPS Surprise	**-5.3%**
Last Sales Surprise	**2.5%**
EPS F1 Est- 4 week change	**-0.1%**
Expected Report Date	**01/30/2020**
Earnings ESP	**0.3%**
P/E TTM	**12.7**
P/E F1	**11.6**
PEG F1	**1.8**
P/S TTM	**3.8**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2020	4,492 E	5,182 E	5,440 E	4,891 E	20,244 E
2019	4,389 A	5,193 A	5,412 A	4,902 E	19,902 E
2018	4,670 A	4,879 A	5,292 A	4,786 A	19,627 A

EPS Estimates

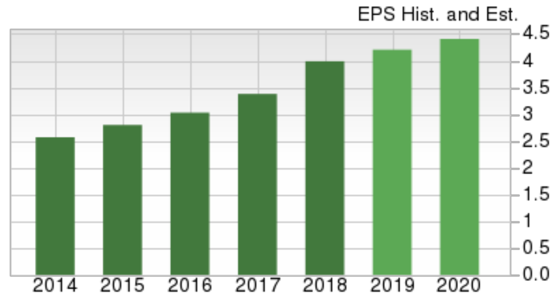
	Q1	Q2	Q3	Q4	Annual*
2020	$0.97 E	$1.14 E	$1.23 E	$1.07 E	$4.41 E
2019	$0.90 A	$1.10 A	$1.08 A	$1.01 E	$4.21 E
2018	$0.95 A	$1.01 A	$1.08 A	$0.95 A	$3.99 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 01/17/2020. The reports text is as of 01/20/2020.

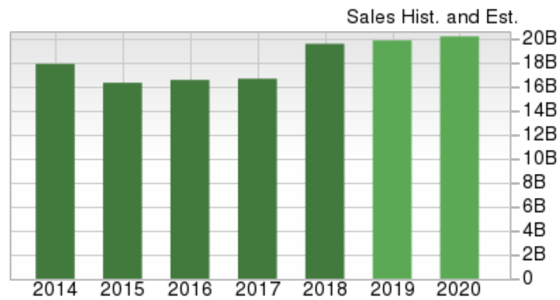
Overview

Altria Group, Inc. was founded in 1919 and is headquartered at Richmond, VA. The company specializes in cigarettes, smokeless products and wine. It is the holding company for Philip Morris USA, Inc. (PM USA), U.S. Smokeless Tobacco Company LLC (UST), John Middleton Inc., Sherman Group Holdings, LLC and its subsidiaries — Ste. Michelle Wine Estates Ltd. (Ste. Michelle) and Philip Morris Capital Corporation (PMCC).



At the end of Mar 31, 2019, Altria had an approximate 10.1% ownership in Anheuser-Busch InBev SA/NV (AB InBev). It also holds investments in JUUL, Cronos Group Inc. (CRON) and Burger Sohne Holding AG.

Altria reports under the following segments on the basis of products:



- **Smokeable Products (87.9% of 2018 Sales)**: The segment, which comprises mainly of PM USA, sells major brands like Marlboro cigarettes, Virginia Slims cigarettes and Parliament cigarettes.

- **Smokeless Tobacco (8.9% of 2018 Sales)**: The segment was formed after the acquisition of UST and its smokeless tobacco business in Jan 2009. The smokeless products segment includes brands like Copenhagen, Skoal, Red Seal, Husky and Marlboro Snus, a PM USA spit-less smokeless tobacco product.

- **Wine (2.7% of 2018 Sales)**: The segment was formed after the acquisition of UST and its premium wine business — Ste. Michelle. The main brands are Chateau Ste. Michelle and Columbia Crest. The company also owns wineries or distributes wines from several other wine regions and foreign countries.

- **All Other (0.5% of 2018 sales)**: Altria holds investments in finance leases, principally in transportation (including aircraft), power generation and manufacturing equipment and facilities.

Products of the company are mainly sold through distributors, wholesalers and large retail chains.

Reasons To Buy:

> The company gains from strategic pricing for its smokeable and smokeless products. Moreover, it is striving to expand in the reduced risk tobacco products space.

▲ **Strong Q3 Results:** Altria delivered robust third-quarter performance, with the top and the bottom line improving year on year. The upside can be attributed to higher revenues in the smokeable and smokeless products categories. Moreover, the bottom line in the reported quarter was supported by increased adjusted operating companies income ("OCI") in the smokeable and smokeless products segments, higher adjusted earnings from Altria's equity investment in AB InBev and lower spending.

Management is on track with growth plans. This, combined with a strong portfolio of owned and acquired products makes the company optimistic about achieving set targets. That said, management reiterated its earnings guidance for 2019. It continues to expect adjusted earnings in the range of $4.19-$4.27, which indicates 5-7% year-over-year growth. Further, the company expects to achieve compounded annual adjusted earnings growth of 5% to 8% during 2020-2022. Shares of the company have gained 13.8% in the past three months, compared with the industry's growth of 16.8%.

▲ **Strong Pricing is the Growth Driver:** Altria's strong pricing has helped it stay afloat in the industry even in the face of declining cigarette volumes. Though higher pricing might lead to possible decline in cigarette consumption, it is seen that smokers tend to absorb price increases owing to the addictive quality of cigarettes. In third-quarter 2019, higher pricing aided performance of the smokeable and smokeless segments. In fact, high pricing was a prime catalyst for top line and adjusted OCI growth in the quarter. Going ahead, product pricing is expected to boost the company's performance.

▲ **Efforts to Expand Smokeless Tobacco & Other Categories:** There has been a general shift among consumers toward low-risk, smokeless tobacco products due to serious health hazards of smoking cigarettes. Altria has been responding to the changing market scenario by offering several reduced risk tobacco products (RRPs). We note that revenues from the Smokeless product category have been steadily rising. During the second and the third quarter of 2019, revenues in the unit advanced 4% and 5.8% year over year, respectively.

We expect such trends to continue fueling Altria in the forthcoming periods. Moreover, the company is undertaking dedicated endeavors to bolster presence in the RRPs space. In this respect, the marketing and technology sharing agreement between Altria and Philip Morris, pertaining to the sale of IQOS in the United States, has been approved by the FDA. IQOS, which has been faring well internationally, is expected to boost Altria's performance in the United States as well. In September, 2019, Altria through its subsidiary — PM USA — commenced the commercialization of IQOS in Atlanta, Georgia. The company is on track with the expansion of IQOS in Richmond, Virginia. Moreover, Altria has acquired 35% stake in JUUL Labs Inc. Additionally, Altria, through its subsidiary Helix Innovations LLC, completed the acquisition of 80% stake in certain companies of Burger Group (Burger Sohne Holding AG). Burger Group is engaged in the commercialization the oral tobacco-derived nicotine (TDN) pouch product — on! Management believes that on! is a worthwhile addition to Altria's smokeless portfolio, as oral TDN products are gaining popularity in the United States owing to their low risk claims.

Further, Altria is undertaking efforts to expand in the cannabis industry. This is evident from the acquisition of stakes of the Canadian cannabis company, Cronos Group, for nearly $1.8 billion. We expect Altria's efforts to strengthen presence in the nascent but booming cannabis space is likely to boost growth in the forthcoming periods.

▲ **Cost Reduction Efforts:** The company is progressing well with its cost-reduction initiatives to deliver annualized cost savings of nearly $575 million by the end of 2019. The program includes savings generated through reductions in workforce and third-party spending as well as the closure of Nu Mark operations. Savings generated from this initiative will be mainly utilized for lowering interests' expenses associated with investments in JUUL and Cronos.

▲ **Enhances Shareholders' Value:** Altria has been consistently returning value to shareholders through dividend payouts and share buybacks. During 2018, the company paid dividends worth almost $5.4 billion. During the third quarter of 2019, the company paid out dividends worth almost $1.5 billion. We note that in August 2019, the company raised its dividend from 80 cents per share to 84 cents. This marks the company's 54th dividend hike in the past 50 years. As a result, the company's annualized dividend rate is now pegged at $3.36 per share. Management is on track to maintain a payout ratio of 80% of the bottom line. Further, the company expects to complete its current 1-billion share repurchase program by the end of 2020.

Reasons To Sell:

Management expects domestic cigarette industry volume to decline in 2019. This is most likely to be triggered by consumers growing health awareness and regulatory barriers.

- **Soft Cigarette Volumes for 2019:** The company struggles with weak shipment volumes in the smokeables unit. During the third quarter of 2019, total smokeable products shipment volume declined 6.5% from the prior-year quarter's number. Reported domestic cigarette shipment volumes slipped 6.6% year over year due to adverse trade inventory movements, cigarette industry's rate of decline and retail share losses. Also, the company's total cigarette retail share dipped 0.6 percentage point. Cigarette shipment volumes are being adeversley impacted by anti-tobacco campaigns and increased consumer awareness regarding the harmful impacts of tobacco consumption. Regulatory hurdles (discussed below) are also a vital factor limiting the marketing of cigarettes, thereby adversely impacting its sales volumes. This has been hurting Altria's smokeable product category. Such industry-wide headwinds are likely to persist in the forthcoming periods. Altria expects domestic cigarette industry volume to decline 5-6% in 2019. .

- **Regulatory Restrictions on Tobacco Consumption:** Government bodies across different nations are imposing restrictions on tobacco companies. The U.S. Food and Drug Administration (FDA) has made it mandatory for tobacco companies to use precautionary labels on cigarette packets to dissuade customers from smoking. Also, per court orders, Altria and other cigarette manufacturers have been directed to put up self-critical advertisements on television and newspapers to dissuade customers from smoking.

  The FDA had also announced that tobacco makers must seek marketing authorization for any tobacco product introduced after Feb 15, 2007. In May 2016, the FDA expanded this restriction to include e-cigarettes, pipe tobacco, cigars and hookah alongside traditional tobacco products. Moreover, the European Union and the FDA proposed a ban on menthol in accordance with the Tobacco Control Act which essentially states that menthol cigarettes have an adverse impact on public health. In recent developments, the FDA raised concerns surrounding the consumption of e-cigarettes. Regulatory authorities are particularly concerned about the high use of these products among the youth.

- **Challenging Industry Landscape & Limited Suppliers:** The tobacco industry witnesses high volatility due to consumers changing preferences, as evident from the rising demand for reduced risk and flavored tobacco offerings. As a result, it is essential for Altria to frequently update its offerings to match consumer's needs. Failure to do so might radically impact the company's market share. Moreover, changes in consumer preferences and regulatory hurdles may cause the company to recall products, which may drastically impact financial strength. Additionally, Altria depends on a limited number of suppliers and facilities to manufacture tobacco products. Any hindrance emerging from the supply end can lead to adverse business impacts.

- **Weak Wine Segment:** Altria's wine segment has been weak for a while. During the third quarter, net revenues in the unit dipped 7.7% year on year, due to increased promotional investments and reduced shipment volumes. The segment's revenues, net of excise taxes, dropped 7.4%. Wine shipment volume declined 9.6% to about 2 million cases.

Last Earnings Report

Altria's Q3 Earnings & Revenues Up Y/Y on Solid Pricing

Quarter Ending	09/2019
Report Date	Oct 31, 2019
Sales Surprise	2.49%
EPS Surprise	-5.26%
Quarterly EPS	1.08
Annual EPS (TTM)	4.03

Altria posted third-quarter 2019 results, wherein adjusted earnings came in at $1.19 per share, which rose 10.2% year over year. The uptick can be attributed to increased adjusted operating companies income (OCI) in the smokeable and smokeless products segments, higher adjusted earnings from Altria's equity investment in AB InBev and lower spending. These were partly offset by higher interest expenses.

Net revenues inched up 0.3% year over year to $6,856 million. Higher revenues in the smokeless and smokeable units drove the top line. Revenues net of excise taxes rose 2.3% to $5,412 million.

Gross profit in the reported quarter improved 7.4% to $3,497 million from the prior-year quarter's number. Notably, reported OCI increased 13.8% to 3,002 million and reported operating income rose 15.1% to $2,944 million.

Segment Details

Smokeable Products: Net revenues in the category inched up 0.2% year over year to $6,049 million, owing to higher pricing and lower spending on promotions. The upsides were countered by lower shipment volumes. Revenues, net of excise taxes, rose 2.5% year over year to $4,643 million. Total smokeable Products shipment volume declined 6.5% from the prior-year quarter's number. Reported domestic cigarette shipment volumes slipped 6.6% year over year due to adverse trade inventory movements, cigarette industry's rate of decline and retail share losses. Adjusting for the aforementioned items, domestic cigarette shipment volume declined nearly 7%. During the quarter, the company's total cigarette retail share dipped 0.6 percentage point to 49.6%. Meanwhile, reported cigar shipment volume rose 4.1%.

Adjusted OCI in the segment improved 12.6% to $2,568 million, owing to better pricing as well as reduced costs and promotional spending. Adjusted OCI margins rose 4.9 percentage points to 55.3%.

Smokeless Products: Net revenues in the segment improved 5.8% from the year-ago quarter's figure to $620 million, driven by higher pricing and reduced promotional investments. These were partially countered by low shipment volume. Revenues, net of excise taxes, increased 6.3% to $587 million in the quarter. Domestic shipment volume for the segment fell 2.5% due to the industry's rate of decline and retail share losses. Total smokeless products retail share went down 0.4 percentage points to 53.9%.

Adjusted OCI rose 10.2% to $422 million, owing to improved pricing as well as reduced promotional investments and costs. These were partially offset by lower shipment volume. Adjusted OCI margin expanded 2.5 percentage points to 71.9%.

Wine: Net revenues declined 7.7% year on year to $167 million, due to increased promotional investments and reduced shipment volumes. The segment's revenues, net of excise taxes, dropped 7.4% to $162 million. Wine shipment volume declined 9.6% to about 2 million cases. Adjusted OCI in the category declined 44.8% to $16 million as a result of increased promotional investment and reduced shipment volumes. Adjusted OCI margin contracted 6.7 percentage points to 9.9%.

Financial Updates

During the third quarter, the company paid out dividends worth almost $1.5 billion. We note that in August, the company raised its dividends from 80 cents per share to 84 cents. This marks the company's 54th dividend hike in the past 50 years. As a result, the company's annualized dividend rate is now pegged at $3.36 per share. The raised dividend were paid on Oct 10, 2019 to shareholders of record as on Sep 16. The company expects to complete its current 1-billion share repurchase program by the end of 2020.

Other Developments

In August, the company completed the buyout of Burger Sohne Holding (Burger Group) to commercialize on! oral nicotine pouches. In September, Altria through its subsidiary — PM USA — commenced the commercialization of IQOS in Atlanta, Georgia. In respect of JUUL, Altria recorded pre-tax impairment charge worth $4.5 billion, during the third quarter.

Further, the company is on track with its savings initiatives. It continues to expect annualized cost savings of nearly $575 million by the end of 2019. The program includes savings generated through reductions in workforce and third-party spending as well as the closure of Nu Mark operations.

Outlook

Management reiterated its guidance for 2019, wherein it expects adjusted earnings in the range of $4.19-$4.27 that suggests 5-7% year-over-year growth. Further, Altria expects domestic cigarette industry volume to decline 5-6% in 2019. Also, it continues to expect 2019 adjusted effective tax rate of 23.5-24.5%. Further the company expects to achieve compounded annual adjusted earnings growth of 5% to 8% during 2020-2022.

Recent News

Altria Announces Dividend - Dec 11, 2019

Altria announced a quarterly dividend of 84 cents a share, payable on Jan 10, 2020 to shareholders of record as on Dec 24.

Altria Ends Merger Talks, Makes Changes in JUUL & 2019 View - Sep 25, 2019

Altria ended talks of a potential merger with Philip Morris International, Inc. as the companies were unable to come to terms. Altria also issued a verdict regarding CEO transition for JUUL Labs Inc. K.C. Crosthwaite has been appointed as the new CEO of JUUL. Further, Altria raised the lower end of its earnings guidance for 2019. It now expects adjusted earnings in the range of $4.19- $4.27 compared with the previous view of $4.15-$4.27.

Valuation

Altria shares are up 12.9% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Staples sector are up 27.5% and 20.3%, respectively over the past year.

The S&P 500 index is up 26.6% in the past year.

The stock is currently trading at 11.55X forward 12-month earnings, which compares to 12.5X for the Zacks sub-industry, 19.96X for the Zacks sector and 19.2X for the S&P 500 index.

Over the past five years, the stock has traded as high as 22.81X and as low as 9.12X, with a 5-year median of 18.27X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our $54 price target reflects 12.22X forward 12-month earnings.

The table below shows summary valuation data for MO

Valuation Multiples - MO

		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	11.55	12.5	19.96	19.2
	5-Year High	22.81	21.23	22.38	19.34
	5-Year Low	9.12	10.54	16.66	15.17
	5-Year Median	18.27	17.47	19.76	17.44
P/S F12M	Current	4.7	3.78	10.26	3.57
	5-Year High	7.56	6.8	11.13	3.57
	5-Year Low	3.78	3.13	8.09	2.54
	5-Year Median	5.91	4.9	9.88	3
EV/EBITDA F12M	Current	9.32	9.41	34.39	12.66
	5-Year High	15.63	17.13	37.23	12.66
	5-Year Low	7.8	8.03	29.38	9.08
	5-Year Median	13.03	12.9	33.53	10.78

As of 01/17/2020

Industry Analysis **Zacks Industry Rank:** Top 34% (87 out of 254)

Top Peers

Vector Group Ltd. **(VGR)**	Outperform
British American Tobacco p.l.c. **(BTI)**	Neutral
Anheuser-Busch InBev SA/NV **(BUD)**	Neutral
Imperial Tobacco Group PLC **(IMBBY)**	Neutral
JAPAN TOB INC **(JAPAY)**	Neutral
Constellation Brands Inc **(STZ)**	Neutral
Schweitzer-Mauduit International, Inc. **(SWM)**	Neutral
Turning Point Brands, Inc. **(TPB)**	Neutral

Industry Comparison Industry: Tobacco

Industry Peers

	MO Neutral	X Industry	S&P 500	BTI Neutral	IMBBY Neutral	JAPAY Neutral
VGM Score	B	-	-	C	A	B
Market Cap	95.31 B	1.69 B	24.65 B	96.13 B	25.60 B	38.70 B
# of Analysts	8	1	13	4	4	2
Dividend Yield	6.59%	4.85%	1.73%	5.94%	14.16%	4.85%
Value Score	B	-	-	B	A	B
Cash/Price	0.02	0.08	0.04	0.05	0.13	0.08
EV/EBITDA	11.79	8.93	14.11	NA	NA	NA
PEG Ratio	1.81	1.81	2.08	1.31	1.09	2.36
Price/Book (P/B)	8.96	2.59	3.39	1.14	3.59	1.56
Price/Cash Flow (P/CF)	12.34	9.33	13.81	9.19	5.23	7.89
P/E (F1)	11.57	11.92	19.19	10.33	7.51	12.26
Price/Sales (P/S)	3.78	1.77	2.69	NA	NA	1.96
Earnings Yield	8.64%	8.40%	5.21%	9.69%	13.34%	8.16%
Debt/Equity	2.53	0.29	0.72	0.63	2.09	0.26
Cash Flow ($/share)	4.13	3.04	6.94	4.91	5.11	1.38
Growth Score	B	-	-	D	A	C
Hist. EPS Growth (3-5 yrs)	10.91%	5.36%	10.56%	NA	NA	-1.70%
Proj. EPS Growth (F1/F0)	4.78%	5.04%	7.57%	5.30%	6.10%	4.09%
Curr. Cash Flow Growth	15.41%	4.57%	14.73%	20.53%	-3.71%	3.28%
Hist. Cash Flow Growth (3-5 yrs)	9.32%	1.95%	9.00%	8.12%	1.08%	NA
Current Ratio	0.56	1.20	1.24	0.73	0.90	1.29
Debt/Capital	71.69%	38.82%	42.99%	38.82%	67.69%	20.76%
Net Margin	7.00%	7.00%	11.14%	NA	NA	17.02%
Return on Equity	56.17%	10.82%	17.16%	NA	NA	13.70%
Sales/Assets	0.45	0.95	0.55	NA	NA	0.40
Proj. Sales Growth (F1/F0)	1.72%	1.90%	4.16%	3.02%	-69.63%	2.09%
Momentum Score	F	-	-	D	F	C
Daily Price Chg	-0.14%	0.00%	0.27%	-0.02%	0.75%	0.00%
1 Week Price Chg	1.19%	0.00%	0.39%	3.57%	1.96%	-2.33%
4 Week Price Chg	0.45%	4.25%	2.95%	6.87%	13.08%	-5.05%
12 Week Price Chg	8.65%	8.65%	7.76%	27.29%	11.97%	-3.71%
52 Week Price Chg	8.41%	-11.19%	22.29%	37.78%	-14.83%	-11.19%
20 Day Average Volume	6,955,387	318,345	1,536,375	1,277,215	318,345	37,753
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	-0.06%	0.00%	0.00%
(F1) EPS Est 4 week change	-0.11%	0.00%	0.00%	-0.06%	0.00%	1.14%
(F1) EPS Est 12 week change	-1.32%	-0.49%	-0.40%	1.62%	-3.32%	-2.20%
(Q1) EPS Est Mthly Chg	-1.28%	0.00%	0.00%	NA	NA	NA

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	B
Growth Score	B
Momentum Score	F
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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