



February 18, 2015

CURRENT PRICE: \$55.24
RATING: HOLD
PRICE TARGET: N/A
CURRENT YIELD: 3.8%

EPS Estimates - Non-GAAP

	DEC 14A	DEC 15E
1Q	\$0.59 A	\$0.66
2Q	\$0.43 A	\$0.65
3Q	\$0.71 A	\$0.71
4Q	\$0.63 A	\$0.69
	\$2.58	\$2.71

Trading Data

52-WEEK PRICE RANGE: **\$55.58 - \$35.10**
SHARES OUTSTANDING: **1,970(M)**
MARKET CAP: **\$108.8(B)**
AVG. DAILY TRADING VOLUME: **7.0(M)**
S&P 500: **2,099**

Valuation Data

BOOK VALUE: **\$1.54**
PRICE TO BOOK: **35.9x**
DIVIDEND: **\$2.08**

Altria Corp (NYSE: MO)

4Q14 Earnings Results

Highlights

- 4Q14 diluted earnings of \$0.63/share vs. \$0.59/share during 4Q13
- Higher OCI in 3 operating units
- E-cig marketing now covers continental US
- Potential dividend increase in 2015
- Maintain HOLD rating

Investment Thesis

Altria Corp (MO-\$55.24), formerly known as Philip Morris, is the largest US tobacco company. MO is focused on the US domestic tobacco business and has seen year-over-year revenue growth, on a pro-forma basis. Going forward management intends to grow earnings through revenue/cash flow growth, share repurchases, and cost reductions. Earnings growth may generate dividend increases in the future. MO's stock pays a current dividend yield of 3.8%.

Company Summary

Altria Group, headquartered in Richmond VA, is the parent company of Philip Morris USA, US Smokeless Tobacco, John Middleton, Ste. Michelle Estate Wineries, and Philip Morris Capital Corp (PMCC). The company operates five segments: domestic cigarettes, smokeless tobacco products, machine made cigars, wineries, and financial services/real estate. The company has 9,900 employees located throughout the US. Philip Morris USA manufactures and sells cigarettes, and other tobacco products, in the US. This unit's cigarette brands include "Marlboro" (#1 in US market share), "Benson & Hedges", "Parliament", "Basic" and "Virginia Slims". This business gives MO approximately a 50.9% market share of the US cigarette market. Through 12/31/14 Philip Morris USA generated approximately 89.4% of overall revenues, or \$21.9 billion. During 2009 MO completed its purchase of US Tobacco (Skool/Copenhagen brands & Ste. Michele Wines) and currently gives MO 55.3% of the smokeless tobacco market share.

For Important Disclosure information regarding the Firm's rating system, valuation methods and potential conflicts of interest, please refer to the last two pages of this report.



EQUITY RESEARCH

Business Overview

MO is the largest cigarette manufacturer in the US. In 2007 the company purchased the John Middleton Co which sells and manufactures machine-made cigars (Black & Mild)/pipe tobacco and has 29.4% current market share. The Smokeable business unit (includes cigarettes/cigars) generated 89.4% of MO's revenues, or \$21.9 billion during FY14. PMCC owns a portfolio of leveraged/direct finance leases and produced less than 1% of revenues. MO also owns approximately a 26%-27% economic equity interest, with voting rights, in the SABMiller beer company. Over the past twenty years MO at one time owned, or acquired, Miller Brewing, Nabisco, Kraft, and Jacobs Suchard AG. These businesses were subsequently either sold or spun-off. During the past three years the company spun-off Kraft Foods (KRFT-\$64.75) and Philip Morris Intl (PM-\$83.00).

Recent Earnings

MO reported 4Q14 diluted earnings of \$0.63/share vs. \$0.24/share during 4Q13. The improvement was due to higher revenues in all operating segments, increased gains on PMCC's asset sales, and the absence of losses from early debt extinguishment incurred during 4Q13. Net revenues improved 2.9% to \$6.26 billion from \$6.10 billion and overall operating income grew 6.3% to \$1.92 million from \$1.80 million. MO's SAB Miller investment contributed \$253 million during the quarter, equaling the same amount contributed during 4Q13. 4Q14's adjusted diluted earnings rose 15.8% to \$0.66/share vs. \$0.57/share during 4Q13. The improvement came from higher adjustable OCI in the smokeable products segment, a lower tax rate resulting from the 2013 debt offer, lower interest/other debt expense, increased earnings from SAB Miller, larger gains on PMCC asset sales, and fewer shares outstanding. MO's FY14 diluted earnings grew 13.3% to \$2.56/share from \$2.26/share during FY13, and adjusted diluted earnings increased 8.0% to \$2.57/share from \$2.38/share.

SEGMENT RESULTS

SMOKEABLE PRODUCTS: Reported OCI rose 7.6% to \$1.71 billion from \$1.60 billion primarily due to higher product pricing and the end of federal tobacco quota buy-out payments. These positives were partly offset by higher SG&A expenses and lower reported shipment volumes. Adjusted OCI increased 7.8% to \$1.72 billion from \$1.60 billion and adjusted OCI margins improved 1.8 percentage points to 43.9% from 42.1%. Total domestic shipment volumes declined 1.7% to 31.3 billion sticks reflecting the industry's overall decline, which was partly offset by retail share gains.

Malboro's shipment volume decreased 1.9% to 26.95 billion from 27.47 billion, Other Premium's fell 7.5% to 1.74 billion from 1.88 billion, and Discount's rose 5.2% to 2.65 billion from 2.52 billion. When adjusted for trade inventory changes, and other factors, MO estimates domestic cigarette shipment volumes decreased 3.0%. In terms of retail market share, MO's total cigarette market share increased 0.1 percentage points to 50.9% from 50.8%. In this category, Marlboro's market share was flat at 43.8%, Discount's rose 0.2 percentage points (4.2% vs. 4.0%), and Other Premium's decreased 0.1 percentage points (2.9% vs. 3.0%).



EQUITY RESEARCH

MO's total cigar shipments rose 3.9% to 319 million from 307 million driven by a 4% increase in "Black & Mild" shipments, which rose to 315 million from 303 million. Other cigars' shipments were flat at 4 million. MO's total cigar retail market share declined 0.4 percentage points (28.8% vs. 29.2%) as "Black & Mild's" fell 0.4 percentage points (28.4% vs. 28.8%) and Other's was flat a 0.4%.

SMOKELESS PRODUCTS: Reported OCI increased 1.2% to \$257 million from \$254 million due to higher pricing and volume shipments. These were partly offset by a rise in promotional investments and the timing of general/administrative expenses. Adjusted OCI was flat at \$257 million and adjusted OCI margins decreased to 60% from 62.5%. This segment's revenues and revenues net of excise taxes rose 4.3% and 4.1%, respectively. These increases were the result of higher pricing/volumes while being partly offset by higher promotional investments.

Overall smokeless products shipment volumes rose 1.0% to 200.4 million cans/packs from 198.5 million cans/packs due to the timing of inventory movements. Copenhagen's shipment volumes rose 4.0% to 113.9 million cans/packs, Skoal's decreased 2.9% to 68.0 million cans/packs, and Other's fell 2.6% to 18.5 million cans/packs. After adjusting for trade inventory changes and other factors, MO estimates smokeless product shipment volumes improved 2.5%.

Retail market share for MO's smokeless products increased 0.3 percentage points (55.3% from 55.0%). Copenhagen's market share rose 1.1 percentage points (31.1% vs. 30.0%), Skoal's declined 0.7 percentage points (20.2% from 20.9%), and Other's decreased 0.1 percentage points (4.0% vs. 4.1%).

WINE SEGMENT: Reported and adjusted OCI increased 17.8% to \$53 million from \$45 million due to higher shipment volumes. OCI margins grew 2.0% percentage points to 25.6% from 23.6%. Net revenues improved 8.6% to \$215 million, from \$198 million, because of higher product shipments. Total wine shipments grew 9.6% to 2.81 million cases from 2.56 million cases. This was driven by increased shipments of Chateau Ste. Michelle (+15.5%), Columbia Crest (+28.5%), 14 Hands (+26.1%). Partly offsetting these gains was a decrease in shipments of Other wines (-10.5%).



RECENT DEVELOPMENTS

There were several announced changes in MO's management team. Altria's President/CEO announced his retirement effective 3/1/15. Howard Willard, Altria's CFO, will become the Chief Operating Officer. William Gifford, Altria's Senior VP of Strategy/Business Development, will become CFO. These changes will occur on 3/1/15.

During 4Q14 MO had repurchased approximately 3.5 million shares of its common stock in its current \$1 billion share repurchase program authorized by its Board of Directors. MO still has another \$518 million worth of shares to repurchase, under this program, by year-end 2015.

MO issued \$1 billion of 2.65% senior unsecured long-term notes due 2020 during 4Q14.

MO's e-cig marketing efforts continued as the company completed the national expansion of its "MarkTen" e-vapor products. The product is now offered in over 130,000 retail stores throughout the US.

Our Thoughts

Another good earnings quarter for MO as the company reported 4Q14 diluted earnings of \$0.63/share vs. \$0.24/share during 4Q13. The improvement was due to higher revenues in all operating segments, increased gains on PMCC's asset sales, and the absence of losses from early extinguishment of debt incurred during 4Q13. The profitability of the e-cig business remains unclear given none of the major US domestic companies, offering these products, have revealed profit margins surrounding this new endeavor. Our expectations are clarity for e-cigarette margins will not develop for another 12-24 months as e-cig providers compete for market share and could face competition in product pricing. Going forward, we expect MO's overall earnings to increase in 2015 given management's 2015 adjusted diluted earnings guidance of \$2.75-\$2.80/share, representing a potential 7%-9% increase over 2014. Under such a scenario, we expect the company to increase its dividend in 2015. Our 2015 diluted earnings estimate is \$2.71/share. We continue to rate MO a HOLD



Risks

There is no guarantee MO will improve earnings/cash flow. Declining US cigarette volumes may hurt the company's revenues and profits. Litigation risks surround cigarette manufacturers. Rising interest rates, higher tobacco prices, tax issues, or rising operating costs could negatively impact MO's earnings. MO's stock may be adversely impacted by negative equity/credit markets, terrorist attacks, and failure to comply with Sarbanes Oxley guidelines.

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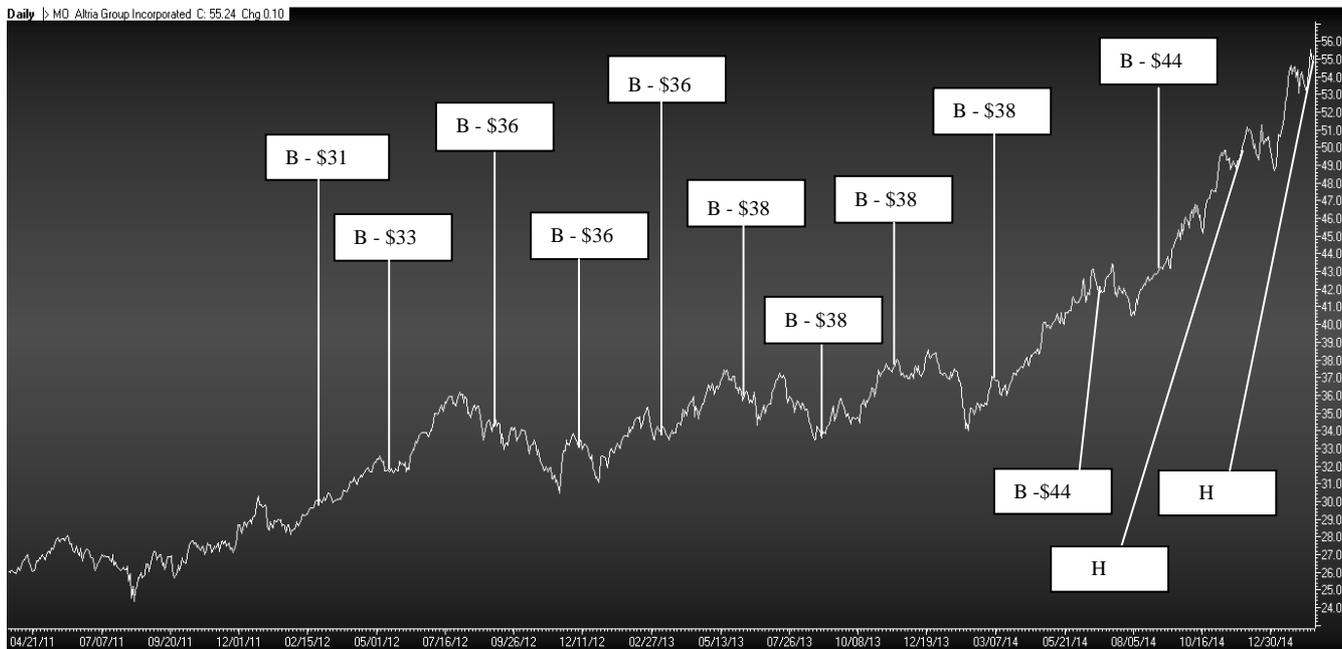
EQUITY RESEARCH

Altria Group, Inc.
(dollars in millions, except per share data)

	1Q14	2Q14	3Q14	4Q14	FY14	1Q15e	2Q15e	3Q15e	4Q15e	FY15e
Net revenues	\$5,517	\$6,256	\$6,491	\$6,258	\$24,522	\$6,289	\$6,452	\$6,527	\$6,598	\$25,866
Cost of sales	1,752	1,968	2,079	1,986	7,785	1,993	2,045	2,069	2,091	8,198
Excise taxes on products	1,509	1,685	1,738	1,645	6,577	1,698	1,742	1,762	1,782	6,984
Gross profit	2,256	2,603	2,674	2,627	10,160	2,598	2,665	2,696	2,725	10,684
Marketing, administration, & research costs	463	564	605	646	2,278	562	661	612	632	2,467
Exit cost/asset impairment	2	10	7		1					
Operating companies income	1,791	2,049	2,062	1,981	7,883	2,036	2,004	2,084	2,093	8,217
Amortization of intangibles	-5	-5	-5	-5	-20	-5	-6	-5	-5	-21
General corporate expenses	-52	-69	-53	-67	-241	-64	-68	-66	-62	-260
Changes to MDLZ/PM tax-related receivables			-5	3	-2					
Reduction of Kraft & PMI receivables										
Corporate asset impairment/exit costs										
Corporate exit cost										
Operating income	1,734	1,975	1,999	1,912	7,620	1,967	1,930	2,013	2,026	7,936
Restructuring charge										
Interest & other debt expense, net	153	230	213	212	808	221	222	223	223	889
Loss on early debt extinguishment				-44	-44					
Earnings from SABMiller equity investment	225	200	328	253	1,006	246	267	348	273	1,134
Earnings before income taxes	1,806	1,945	2,114	1,909	7,774	1,992	1,975	2,138	2,076	8,181
Income taxes	631	683	717	673	2,704	697	691	748	726	2,862
Net earnings (continuing ops.)	1,175	1,262	1,397	1,236	5,070	1,295	1,284	1,390	1,350	5,319
Earnings from discontinued ops.										
Net earnings	\$1,175	\$1,262	\$1,397	\$1,236	\$5,070	\$1,295	\$1,284	\$1,390	\$1,350.00	\$5,319
Net earnings attributable to Altria	\$0.59	\$0.64	\$0.71	\$0.63	\$2.56	\$0.66	\$0.65	\$0.71	\$0.69	\$2.71
Earnings per share	\$0.57	\$0.65	\$0.69	\$0.66	\$2.57	\$0.68	\$0.66	\$0.73	\$0.73	\$2.80
Continuing operations earnings per share	\$0.59	\$0.64	\$0.71	\$0.63	\$2.56	\$0.66	\$0.65	\$0.71	\$0.69	\$2.71

Important Disclosures

Daily | MQ Altria Group Incorporated C: 55.24 Chg 0.10



9/14/09 \$17.99 Initiate BUY
 5/18/10 Raised price target to \$23/share
 8/17/10 Raised price target to \$24/share
 11/16/10 Raised price target to \$26/share
 5/10/11 Raised price target to \$29/share
 2/28/12 Raised price target to \$31/share
 5/16/12 Raised price target to \$33/share
 8/31/12 Raised price target to \$36/share
 6/07/13 Raised price target to \$38/share
 6/24/14 Raised price target to \$44/share
 11/26/14 Reduced rating to HOLD
 Ratings:
 Buy: B
 Hold: H
 Sell: S

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