



August 19, 2015

CURRENT PRICE: \$54.81
RATING: HOLD
PRICE TARGET: N/A
CURRENT YIELD: 3.8%

EPS Estimates - Non-GAAP

	DEC 14A	DEC 15E
1Q	\$0.59 A	\$0.52A
2Q	\$0.64 A	\$0.74A
3Q	\$0.71 A	\$0.71
4Q	\$0.63 A	\$0.69
	\$2.58	\$2.66

Trading Data

52-WEEK PRICE RANGE: **\$56.69 - \$42.30**
 SHARES OUTSTANDING: **1,962(M)**
 MARKET CAP: **\$107.5(B)**
 AVG. DAILY TRADING VOLUME: **6.8(M)**
 S&P 500: **2,080**

Valuation Data

BOOK VALUE: **\$1.41**
 PRICE TO BOOK: **39.0x**
 DIVIDEND: **\$2.08**

Altria Corp (NYSE: MO)

2Q15 Earnings Results

Highlights

- 2Q15 diluted earnings of \$0.74/share vs. \$0.64/share during 2Q14
- Higher Smokeable OCI & lower interest/debt expense
- Announces new \$1 billion share repurchase program
- 2015 adjusted diluted EPS guidance raised to \$2.76-\$2.81/share
- Maintain HOLD rating

Investment Thesis

Altria Corp (MO-\$54.81), 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 54.8% 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.

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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 (KHC-\$74.78) and Philip Morris Intl (PM-\$83.74).

Recent Earnings

MO reported 2Q15 diluted earnings of \$0.74/share vs. \$0.64/share during 2Q14. The 15.6% increase was due to higher reported OCI in the smokeable products unit and lower interest/debt expense (\$195 million vs. \$230 million). Revenues when comparing the two quarters, rose 5.7% to \$6.61 billion from \$6.26 billion, cost of sales increased to \$2.00 billion from \$1.97 billion, and excise taxes rose to \$1.74 billion from \$1.69 billion. Marketing, administration, and research costs were 2.5% higher at \$578 million. Operating companies' income improved 11.7% to \$2.29 billion and overall operating income increased 12.6% to \$2.22 billion. The SABMiller investment contributed \$225 million towards earnings in 2Q15 vs. \$200 million during 2Q14. MO's adjusted diluted earnings increased 13.8% to \$0.74/share vs. \$0.65/share during 2Q14. The improvement came from higher adjusted OCI in the smokeable products unit and lower interest/debt expense.

SEGMENT RESULTS

SMOKEABLE PRODUCTS: OCI improved 13.1% to \$2.02 billion, from \$1.79 billion, due to higher pricing/volume and lower resolution expenses (mainly due to end of the federal tobacco quota buy-out payments). These positives were partly offset by the impact of NPM adjustments items in 2Q14 and higher costs from pension, benefit costs, SG&A, and increased promotional investments in 2015. Adjusted OCI increased 15.1% to \$2.03 billion, from \$1.75 billion, and adjusted OCI margins improved 3.3 percentage points to 47.5% from 44.2%.

Total domestic shipment volumes grew 3.1% to 33.5 billion sticks from 32.5 billion sticks. Marlboro's and Discounts' shipping volumes increased 3.0% and 8.9%, respectively, while Other's declined 3.4%. PM stated domestic cigarette shipments grew 1% when adjusted for trade inventory movements and other factors.

MO's overall cigarette market share increased 0.5 percentage points to 51.4% from 50.9%. This was driven by higher market share from Marlboro (44.2% vs. 43.9%) and Discount (4.4% vs. 4.1%). Partly offsetting these positives was a decrease in Other Premium's market share (2.8% vs. 2.9%).



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Cigar's shipment volumes rose 0.9% to 334 million sticks from 331 million sticks due to a 1.6% increase from the "Black & Mild" brand (325 million sticks vs. 320 million sticks). The increase was partly offset by a decrease in Other's volumes (9 million sticks vs. 11 million sticks). Total cigar market share declined to 27.9% from 28.7% as both "Black & Mild's" and Other's market share fell to 27.6% from 28.3%, and to 0.3% from 0.4%, respectively.

SMOKELESS PRODUCTS: OCI increased 2.8% to \$293 million from \$285 million from higher pricing and a rise in "Copenhagen's" and "Skoal's" combined market share. Adjusted OCI improved 4.2% to \$297 million from \$285 million and adjusted OCI margins fell to 66.4% from 66.6%. Net revenues increased 3.7% to \$481 million due to higher pricing and was partly offset by higher promotional investments.

Overall smokeless product shipments grew 2.6% to 209.0 million cans/packs from 203.8 million cans/packs. The increase in shipped volumes of "Skoal" (+5.4%) and "Copenhagen" (+0.1%) was partly offset by a decline in shipments of "Other" (-5.6%). When adjusting for trade inventory movements and other factors, MO estimated its overall domestic smokeless products shipments grew 2.5%.

MO's total domestic smokeless product share declined to 54.8% from 54.9%. This occurred as a gain in "Copenhagen's" market share (31.3% vs. 30.5%) was not enough to counter declines in "Skoal" (19.8% vs. 20.5%) and Other's (3.7% vs. 3.9%).

WINE: Reported and adjusted OCI increased improved 25% to \$35 million from \$28 million and OCI margins grew to 22.4% from 19.9%. The improved results came from higher revenues net of excise taxes (\$156 million vs. \$141 million). Total wine shipments rose 8.9% to 2.05 million cases from 1.89 million cases. These higher shipments came from higher volumes in its brands Chateau Ste. Michele (+9.8%), Columbia Crest (+22.0%), 14 Hands (+4.9%), and Other (+6.0%).

RECENT DEVELOPMENTS

During 2Q15 MO repurchased approximately 5.2 million shares of its common stock at a cost of \$263 million.

While having another \$63 million of stock repurchases remaining in its current repurchase program, the company announced a new \$1 billion repurchase program expected to be completed by mid-2016.

Announced an expansion of its agreement with Philip Morris (PM-\$) to include joint R&D and technology-sharing to develop e-vapor products to be marketed in the US by MO and outside of the US by PM.



Nu Mark LLC continued to increase its US marketing footprint by shipping its MarkTen XL e-vapor products into several larger markets this past April. Additionally, the company expanded the retail distribution of Green Smoke e-vapor products this past June into larger US markets.

MO raised its fully-year adjusted diluted earnings guidance to \$2.76-\$2.81/share, representing a 7.5%-9.5% from 2014's adjusted diluted earnings results.

Our Thoughts

Another good earnings report from MO as the company reported 2Q15 earnings of \$0.74/share vs. \$0.64/share during 2Q14. The 15.6% increase was due to higher reported OCI in all three operating units and lower interest/debt expense (\$195 million vs. \$230 million). Higher product pricing and increased volumes improved OCI results in the smokeable, smokeless, and wind segments. While MO's management stated, during the earnings call, expectations of moderation in its results during 2H15, 2015 earnings guidance was raised to \$2.76-\$2.81/share. Should this materialize, and given the company's efforts to enhance shareholder returns, MO could raise its dividend later this year. We continue to rate this stock 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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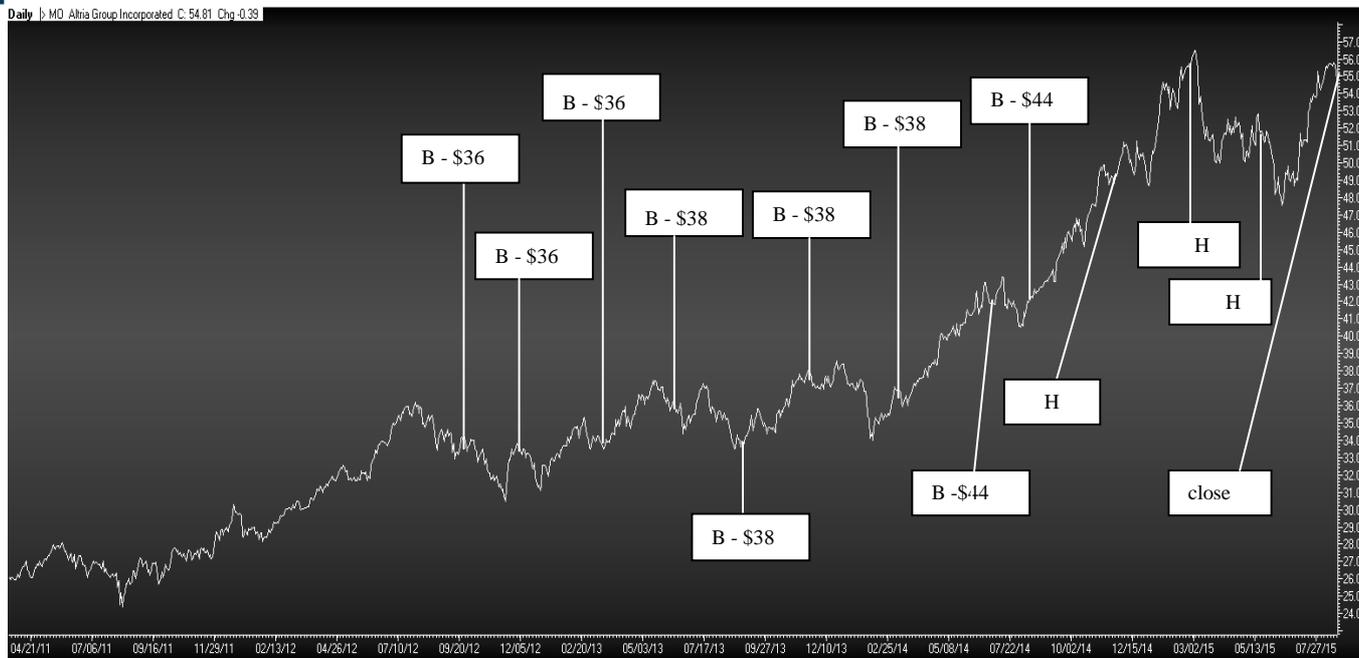


EQUITY RESEARCH

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

	1Q14	2Q14	3Q14	4Q14	FY14	1Q15	2Q15	3Q15e	4Q15e	FY15e
Net revenues	\$5,517	\$6,256	\$6,491	\$6,258	\$24,522	\$5,804	\$6,613	\$6,527	\$6,598	\$25,542
Cost of sales	1,752	1,968	2,079	1,986	7,785	1,797	2,004	2,069	2,091	7,961
Excise taxes on products	1,509	1,685	1,738	1,645	6,577	1,532	1,738	1,762	1,782	6,814
Gross profit	2,256	2,603	2,674	2,627	10,160	2,475	2,871	2,696	2,725	10,767
Marketing, administration, & research costs	463	564	605	646	2,278	552	578	612	632	2,374
Exit cost/asset impairment	2	10	7		1		4			
Operating companies income	1,791	2,049	2,062	1,981	7,883	1,923	2,289	2,084	2,093	8,389
Amortization of intangibles	-5	-5	-5	-5	-20	-5	-5	-5	-5	-20
General corporate expenses	-52	-69	-53	-67	-241	-53	-60	-66	-62	-241
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	1,865	2,224	2,013	2,026	8,128
Restructuring charge										
Interest & other debt expense, net	153	230	213	212	808	209	195	223	223	850
Loss on early debt extinguishment				-44	-44	-228				-228
Earnings from SABMiller equity investment	225	200	328	253	1,006	134	225	348	273	980
Earnings before income taxes	1,806	1,945	2,114	1,909	7,774	1,562	2,254	2,138	2,076	8,030
Income taxes	631	683	717	673	2,704	544	805	748	726	2,823
Net earnings (continuing ops.)	1,175	1,262	1,397	1,236	5,070	1,018	1,449	1,390	1,350	5,207
Earnings from discontinued ops.										
Earnings attributable to non-controlling interests							1			
Net earnings	\$1,175	\$1,262	\$1,397	\$1,236	\$5,070	\$1,018	\$1,448	\$1,390	\$1,350.00	\$5,207
Net earnings attributable to Altria	\$0.59	\$0.64	\$0.71	\$0.63	\$2.56	\$0.52	\$0.74	\$0.71	\$0.69	\$2.66
Earnings per share	\$0.57	\$0.65	\$0.69	\$0.66	\$2.57	\$0.63	\$0.74	\$0.71	\$0.73	\$2.81
Continuing operations earnings per share	\$0.59	\$0.64	\$0.71	\$0.63	\$2.56	\$0.52	\$0.74	\$0.71	\$0.69	\$2.66

Important Disclosures



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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