CAPITOL SECURITIES MANAGEMENT, INC.

EQUITY RESEARCH

March 29, 2021

CURRENT PRICE:	**$52.30**
RATING:	**BUY**
PRICE TARGET:	**$56**
CURRENT YIELD:	**6.6%**

EPS Estimates - Non-GAAP

	DEC 20A	DEC 21E
1Q	$0.83	$1.03
2Q	$1.04	$0.90
3Q	($0.51)	$1.11
4Q	$1.03	$1.19
	$2.40	**$4.56**

Trading Data

52-WEEK PRICE RANGE:	**$52.59 - $30.95**
SHARES OUTSTANDING:	**1,859(M)**
MARKET CAP:	**$97.2(B)**
AVG. DAILY TRADING VOLUME:	**9.4(M)**
S&P 500:	**3,971**

Valuation Data

BOOK VALUE:	**$1.49**
PRICE TO BOOK:	**35.1x**
DIVIDEND:	**$3.44**

Altria Corp (NYSE: MO)

Maintain BUY rating & Raising price target

Highlights

- 4Q20 earnings of $1.03/share vs. ($1.00)/share during 4Q19
- Increasing marketing of non-combustible products
- Announces $2 billion share repurchase program
- Management gives 2021 earnings guidance of $4.49-$4.62
- Maintain BUY rating & raising price target to $56

Investment Thesis

Altria Corp (MO-$52.30), 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. After a recent drop in MO’s shares, from the recent stock market declined sparked by the US spread of Covid pandemic, and investor disappointment over the company’s JUUL investment, its shares may be poised for a rebound, in addition to offering investors a dividend yield of 6.6%. These shares are recommended for moderate-to-aggressive risk-tolerant investors.

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% market share of the US cigarette market. Through 12/31/20 Philip Morris USA generated approximately 88.3% of overall revenues, or $23.1 billion.

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.

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. The Smokeable business unit (includes cigarettes/cigars) generated 87.5% of MO's revenues, or $22.0 billion during FY19. PMCC owns a portfolio of leveraged/direct finance leases and produced lees than 1% of revenues. MO also owns approximately a 10.2% economic equity interest, with voting rights, in Anheuser-Busch InBev (BUD-$64.10). 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 few years the company spun-off Kraft Foods (KHC-$40.78) and Philip Morris Intl (PM-$90.99). In 2009 MO completed its purchase of US Tobacco (Skoal/Copenhagen brands & Ste. Michele Wines) currently giving MO 49% of the smokeless tobacco market share. To reduce its dependence on tobacco revenue streams, MO recently acquired equity stakes in JUUL Labs and Cronos (CRON-$9.16).

Recent Earnings

MO reported 4Q20 diluted earnings of $1.03/share vs. ($1.00)/share during 4Q19. The improvement came mainly from the absence of a 4Q19 $4.1 billion impairment charge for MO’s JUUL investment. When comparing the two quarters, 4Q20’s OCI increased for the smokeable and oral products units, experienced a lower loss from the wine unit, and benefitted from a higher estimated value in the investment in JUUL during 2020. These positives were partly offset by higher taxes, lower ABI (BUD-$64.10) investment returns, reduced net income from Cronos-related special items, and higher losses from all other categories resulting from reductions in estimated residual value of some PMCC assets. 4Q20’s adjusted earnings declined to $0.99/share from $1.01/share during 4Q19. FY20’s operating earnings $2.40/share vs. ($0.70)/share during FY19 and adjusted earnings rose to $4.36/share from $4.21/share.

SEGMENT RESULTS

SMOKEABLE PRODUCTS: 4Q20’s OCI rose 10.8% to $2.38 billion from $2.15 billion during 4Q19. The increase came from higher pricing, lower costs, absence of 2019 impairment charges and exit/implementation costs. These were partly offset by higher resolution expenses, increased promotional investments, Covid related expenses, and lower volumes. Overall net revenues improved 5.0% due to higher product pricing and was partially offset by higher promotional investments
.

Adjusted OCI grew 10.2% to $2.39 billion benefiting from higher product pricing and lower costs, after being partly offset by higher resolution expenses, higher promotional investments, and lower sales volumes. Adjusted OCI margins were flat at 54.8%.

On a quarter-to-quarter comparison, cigarette shipment volumes improved 3.1% because of trade inventory movements while being partially offset by losses in MO's retail share. After adjusting for inventory movements, management believes shipment volumes decreased 1.0% and total industry cigarette volumes fell 0.5%. MO's reported cigar shipments grew 1%.

MO's overall cigarette market share decreased to 49.6% from 49.9%. This occurred as Marlboro's market share rose to 43.3% from 43.1%, while Discounts fell to 3.7% from 4.1%, and Other Premiums declined to 2.3% from 2.4%.

ORAL TOBACCO PRODUCTS: During 4Q20, OCI improved 9.4% to $421 million from $385 million during 4Q19 as results were driven by higher product pricing and favorable asset impairment/exit/implementation/acquisition-related costs. These were partially offset by higher promotional investments and increased costs. Net revenues increased 4.5% to $632 million due to increased product pricing and was partly offset by higher promotional investments.

Adjusted OCI rose 4.3% to $412 million because of higher pricing which was partly offset by larger promotional investments and increased costs. Adjusted OCI margins fell slightly to 68.7% from 68.8%.

Product shipments increased 0.5% resulting from the industry's growth rate, calendar differences, and other factors. These positives were partially offset by retail share loss (from oral nicotine pouch sale growth), and trade inventory movements. After adjustments for calendar differences, trade inventory movements, and other shipments, overall shipments increased approximately 0.5%. Copenhagen volumes fell 1.3% to 127.4 million cans/packs, Skoal declined 4.3% to 51.3 million cans/packs, while Other rose 27.4% to 23.7 million cans/packs.

MO's oral product market share decreased to 49.0% from 51.4% due mainly to the growth of oral nicotine pouches. Copenhagen's market share fell to 31.2% from 33.2%, Skoal's dropped to 13.3% from 14.6%, and Other's rose to 4.5% from 3.6%.

WINE: Reported OCI during 4Q20 rose to ($13 million) from ($53 million) in 4Q19 due to the absence of a 2019 impairment charge. This was partially offset by 2020 inventory-related charges, lower shipment volume, and higher costs. The Wine unit was severely impacted by the Covid economic slowdown causing lower on-premise and direct-to-consumer sales. Net revenues fell 12.6% from lower shipments as shipments decreased 13.3% to approximately 2.1 million cases. Adjusted OCI, affected by lower shipments and higher costs declined 87% to $3 million.

MO'S NONCOMBUSTIBLE PRODUCTS BUSINESS PLATFORM

During 2020 MO began selling IQOS in Charlotte NC and "Heatsticks" in approximately 1000 US retail locations in Charlotte, Richmond VA, and Atlanta GA. The company plans to expand the marketing of these two products into four new metro markets in the US. Packaging for "Heatsticks" was recently changed and are now offered as "Amber", "Blue Menthol", and "Green Menthol". During this past December, the US Food & Drug Administration (FDA) authorized the sale of IQOS 3 devices in the US. This product features a longer duration battery and faster recharging time which MO will begin to market to the public.

MO expanded Helix's "on!" product distribution by 22,000 stores during 4Q20 and is currently available in 78,000 US retail locations. This product has attained retail share of approximately 2.4% of the US oral tobacco category. Annual manufacturing production capacity of "on!" is now 50 million cans and MO believes capacity can grow to meet increasing demand by mid-2021.

RECENT DEVELOPMENTS

Independent Chairman of the Board and Board Director, Thomas F. Farrell II, announced his retirement from MO's Board following the conclusion of his current term, anticipated to be around 5/20/21.

MO announced the pricing of its previously announced cash tender offer for certain senior unsecured notes with maturities ranging from 2022-2049. The total maximum tender offer is expected to be approximately $4.6 billion.

Management announced it will convert its non-voting shares in JUUL Labs to voting shares per its 2018 minority purchase agreement.

The FDA authorized sale of the IQOS 3 Tobacco heating systems in the US. This product is viewed as an enhancement to the IQOS 2.4 product currently being sold throughout the country by MO.

EARNINGS CONFERENCE CALL TAKEAWAYS: Following the 4Q20 earnings release, MO held an earnings conference call. Below are some of the key points made during the presentation.

-Management gave FY21 adjusted earnings guidance of $4.49-44.62/share, equating to a 3%-6% improvement over FY20, with earnings growth expected during the last three quarters of 2021.

-The Board of Directors approved a new $2 billion share repurchase program with expectations of completion by mid-2022.

-MO plans to maintain its long-term objective of an 80% dividend payout ratio of adjusted diluted earnings

-Management noted overall tobacco revenues remained fairly stable given that total tobacco volumes have only fallen 1% annually during the past five years.

-The company's smokeable products (89% of revenues) generates cash which is being invested in non-combustible products
.
-Helix is ramping up its manufacturing of "on!" and currently has manufacturing capacity of 50 million cans. Company estimates its manufacturing capacity can be ramped-up to meet expected increased consumer demand as the product is placed in additional US retail spaces. During 2020 "on!" was sold in 78,000 stores. The "Heatstix" product is sold in 1,000 stores. These two products, along with IQOS and the JUUL products, are part of MO's "Moving Beyond Smoking" campaign geared to offer smokers non-combustible alternative products to cigarettes.

-MO plans to expand IQOS and "Heatstix" products into 4 new metropolitan markets and surrounding geographic areas in 2021.

-During 4Q20, management believes consumer stay-at-home habits, created by the pandemic, "contributed to more tobacco usage occasions and higher discretionary spending." While consumer trips to retail stores were lower than earlier periods, more money is being spent on tobacco products per visit.

-MO did not give 2021 cigarette industry volume guidance due to the following variables: smokers stay-at-home habits, unemployment rates, fiscal stimulus, cross category movement between tobacco and non-tobacco products, the timing and breadth of covid vaccine programs, and post-vaccine consumer purchasing trends.

-Management intends to continue promotional spending and investing programs for its products.

-4Q20's adjusted earnings contributions from InBev (BUD-$64.10) was $157 million, a decrease of 19% from 4Q19. For FY20, InBev contributed $540 million in adjusted earnings, a 36% decrease from FY19.

-Many states experienced tax revenue decreases during the Covid pandemic. Thus, there is a possibility that going forward, some states may attempt to raise tobacco excise taxes.

Our Thoughts

Given MO's high dividend yield of 6.6%, we continue to rate MO a BUY for income/growth investors. These shares have rebounded since our last report given a good 4Q20 earnings report and lowered Wall Street concerns over the company's large write-off of its JUUL investment and the recently announced $2 billion share repurchase program. These developments appear to be improving investor expectations of MO. This emerging positive view, in our opinion, was helped by the company providing more transparency and description about its tobacco alternative products (IQOS, HeatStix, "on!"). Potentially, MO could move higher assuming continued FY21 earnings growth, success with its new tobacco alternative products, possible FDA approval of JUUL products during the next 12-24 months, positive Cronos investment returns, and the potential of future dividend increases. We are raising our price target to $56/share, equating to 12.3x our FY21 adjusted earnings estimate of $4.56/share.

RISKS TO OUR PRICE TARGET:
Decreasing earnings/cash flow at MO. Decreasing US cigarette consumption, oral tobacco products, consumption volumes may also hurt the company's revenues/profits. Declining earnings for MO's three operating units poses a risk to the company. Ownership stakes in Cronos & JUUL may not produce profits to pay higher interest payments on subsequent debt incurred for these investments. Additionally, there is no guarantee non-combustible product sales will occur and be able to offset declining sales of traditional tobacco revenues. This sotck could decline in value if MO reduces/eliminates the common stock dividend or is unable to pay its debt. Litigation/regulation risks and excise taxes are a threat to MO. Rising interest rates/inflation, corporate taxes, economic recessions, higher tobacco prices, increased gasoline prices, rising operating costs/debt expense, or tax issues could negatively impact MO's future earnings. This stock may be adversely impacted by negative equity/credit markets, credit ratings agencies downgrading of MO's debt, geopolitical events, wars, cyber hacking, supply chain issues, black swan events, terrorist attacks, and failure to comply with Sarbanes Oxley and generally accepted accounting guidelines. All factors mentioned above could cause a decline in MO's stock or its ability to maintain its common stock dividend.

Risks

There is no guarantee MO will improve earnings/cash flow. Declining US cigarette consumption/volumes may hurt the company's revenues and profits. Declining earnings from MO’s three operating units pose a risk to the company. Additonally, there is no guarantee non-combustible product sales growth will occur and offset declining traditional tobacco product revenues. Ownership stakes in Cronos and JUUL may not produce profits to pay higher interest payments on subsequent debt incurred for these investments. This stock could decline in value if MO reduces/eliminates the common stock dividend. Litigation/regulation risks and excise taxes are a threat to MO. Rising interest rates/inflation, corporate tax rates, economic recessions, higher tobacco prices, increased gasoline prices, rising operating costs/debt expense, or tax issues could negatively impact MO's future earnings. This stock may be adversely impacted by negative equity/credit markets, credit ratings agencies downgrades of MO’s debt, geopolitical events, wars, cyber hacking, supply chain issues, black swan events, terrorist attacks, and failure to comply with Sarbanes Oxley and generally accepted accounting guidelines. All factors mentioned above could cause a decrease or elimination of MO’s common stock dividend.

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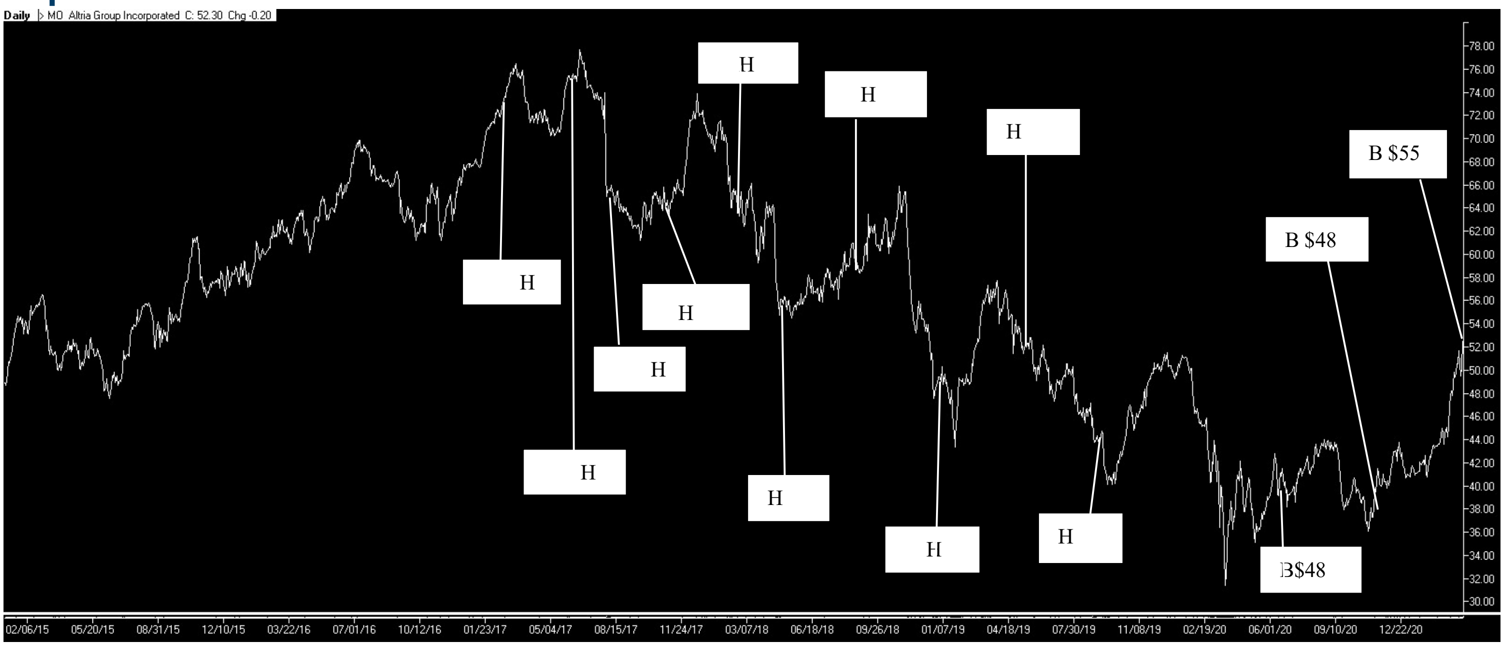
Altria Group, Inc.
(dollars in millions, except per share data

	1Q20	2Q20	3Q20	4Q20	FY20	1Q21e	2Q21e	3Q21e	4Q21e	FY21e
Net revenues	$6,359	$6,367	$7,123	$6,304	$26,153	$6,382	$6,423	$6,745	$6,594	$26,144
Cost of sales	2,173	1,775	1,961	1,909	7,818	1,793	1,805	1,884	1,846	7,328
Excise taxes on products	1,313	1,305	1,445	1,249	5,312	1,295	1,317	1,366	1,358	5,336
Gross profit	2,873	3,287	3,717	3,146	13,023	3,294	3,301	3,495	3,390	13,480
Marketing, administration, & research costs	473	428	480	473	1,855	492	494	491	492	1,969
Exit cost/asset impairment				3	3					
Operating companies income	2,400	2,859	3,237	2,675	11,171	2,802	2,807	3,004	2,898	11,511
Amortization of intangibles	19	18	17	18	72	18	19	18	16	71
General corporate expenses	45	45	60	77	227	54	65	65	72	256
Changes to MDLZ/PM tax-related receivables										
Adjustment to 3rd party guarantee accrual										
Corporate asset impairment/exit costs				1	1					
Corporate exit cost										
Operating income	2,336	2,796	3,160	2,581	10,873	2,730	2,723	2,921	2,810	11,184
Restructuring charege										
Interest & other debt expense,net	275	308	310	316	1,209	318	319	319	319	1,275
Loss on early debt extinguishment										
Earnings from equity investments	157	9	-472	195	111	114	111	122	132	479
Other Income	27	28	3	19	77	12	15	14	18	49
Loss on AB InBev/SAB Miller business combination										
Gain/loss on Cronos-related financial instruments	137	40	105	62	140	35	28	36	39	138
Impairment on JUUL investment			2,600		2,600					
Earnings before income taxes	2,108	2,565	-324	2,541	6,890	2,573	2,239	2,774	2,968	10,554
Income taxes	558	627	632	619	2,436	656	571	707	757	2,691
Net earnings (continuing ops.)	1,550	1,938	-956	1,922	4,454	1,917	1,668	2,067	2,211	7,863
Earningns from discontinued ops.										
Earnings attributable to non-controlling interests	2	5	4	2	13	2	6	2	4	14
Net earnings	$1,552	$1,943	($952)	$1,924	$4,467	$1,919	$1,674	$2,069	$2,215	$7,877
Net earnings attributable to Altria	$0.83	$1.04	($0.51)	$1.03	$2.40	$1.03	$0.90	$1.11	$1.19	$3.23
Earnings per share	$1.09	$1.09	$1.19	$0.99	$4.36	$1.04	$1.10	$1.22	$1.20	$4.56
Continuing operations earnings per share	$0.83	$1.04	($0.51)	$1.03	$2.40	$1.03	$0.90	$1.11	$1.19	$3.23

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
6/12/20 Raise rating to BUY with a $48 price target
3/29/21 Raised price target to $56/share
Ratings:
Buy: B
Hold: H
Sell: S

$56 price target equates to 12.3x our 2021 adjusted earnings estimate of $4.56/share

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Steven Marascia certifies, with respect to the companies or securities that he analyzes, that (1) the views expressed in this report accurately reflect his personal views about all of the subject companies and securities and (2) no part of his compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this report.

Analyst Steven Marascia owns shares of Altria Corp.

Stock ratings used in this report are defined as follows:

(1) Buy – The stock's total return including dividends is expected to exceed the industry or market average by at least 10% over the next twelve months.
(2) Hold – The stock's total return including dividends is expected to be in line with the industry or market average of +/- 10% over the next twelve months.
(3) Sell – The Stock's total return including dividends is expected to be below the industry or market average by 10% or more over the next twelve months.

The distribution of investment ratings for all companies in our coverage universe are as follows: (1) 50%, (2) 50%, (3) 0%

The distribution of investment ratings used for companies whom we have performed banking services in the last 12 months are (1)100%, (2) 0%, (3) 0%

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The subject company is not, or during the past 12 months, was not, a client of Capitol Securities Management's Investment Banking/Public Finance unit.

Other Disclosures

For more information on this report, please contact us at 800.612.1484 or write to Capitol Securities, 100 Concourse Boulevard, Suite 101, Glen Allen, Virginia 23059