Altria Group (MO)

Updated May 4th, 2018 by Bob Ciura

Key Metrics

Current Price:	$57	**5 Year CAGR Estimate:**	14.6%	**Quality Percentile:**	N/A
Fair Value Price:	$65	**5 Year Growth Estimate:**	7.0%	**Momentum Percentile:**	N/A
% Fair Value:	88%	**5 Year Valuation Multiple Estimate:**	2.7%	**Total Return Percentile:**	N/A
Dividend Yield:	4.9%	**5 Year Price Target**	$90	**Valuation Percentile:**	N/A

Overview & Current Events

Altria Group was founded by Philip Morris in 1847. Today, it is a consumer staples giant. It sells the Marlboro cigarette brand in the U.S., and a number of other non-smokeable brands, including Skoal, Copenhagen, and Ste. Michelle. Altria also has a 10% ownership stake in global beer giant Anheuser Busch Inbev.

On 4/26/18, Altria released strong first-quarter earnings. Quarterly revenue of $4.67 billion increased 1.7%, and earnings-per-share of $0.95 rose 30% year-over-year. Revenue and earnings-per-share both beat analyst expectations, by $40 million and $0.03 per share, respectively. Revenue in Altria's smoke-able products declined 0.8% for the quarter. Elsewhere, Ste. Michelle grew volume and revenue with wine shipment volume up 6.1%. In beer, equity earnings from its Anheuser Busch InBev investment were $225 million in the first quarter.

Per-Share Growth

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$1.66	$1.76	$1.87	$1.64	$2.06	$2.26	$2.56	$2.67	$2.73	$3.39	***$3.96***	***$5.55***
DPS	$1.68	$1.32	$1.46	$1.58	$1.70	$1.84	$2.08	$2.17	$2.35	$2.54	***$2.90***	***$4.07***

Altria has generated steady earnings growth for many years. Dividends have also grown consistently, after taking account for various spin-offs of Kraft Foods and Philip Morris International. Going forward, Altria's growth will be fueled by price increases and new products. Altria enjoys strong brands across its product portfolio, including the No. 1 cigarette brand. As a result, it has pricing power over the consumer, and typically increases prices each year. In addition, Altria is innovating new products to help offset the declining smoking rate. Altria's non-combustible product portfolio includes e-vapor and e-cigarettes. The company is awaiting regulatory approval from the Food & Drug Administration for its new reduced-risk product line called IQOS. Altria's reduced-risk products heat tobacco rather than burn it, which Altria believes results in fewer harmful side effects.

In the past 10 years, Altria increased earnings-per-share by 9.1% per year, on average. As a result, a forecast of 7% annual earnings growth through 2023 seems achievable. Altria has increased its dividend 52 times in the past 49 years. Going forward, dividend growth is expected to mimic the rate of earnings growth over the next five years.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	11.9	9.9	11.8	16.2	15.7	15.7	16.5	20.1	23.4	20.6	***14.2***	***16.2***
Avg. Yld.	8.5%	7.6%	6.6%	6.0%	5.3%	5.2%	4.9%	4.0%	3.7%	3.6%	***4.9%***	***4.5%***

At the midpoint of Altria's 2018 guidance, the company expects earnings-per-share of approximately $3.96. As a result, Altria stock trades for a price-to-earnings ratio of 14.2. In the past 10 years, Altria stock traded for an average price-to-earnings ratio of 16.2. The 10-year average price-to-earnings ratio is a reasonable estimate of fair value for Altria. As a result, the stock appears to be undervalued. If Altria stock returned to a price-to-earnings ratio of 16.2 by 2023, the expanding valuation would boost annual returns by approximately 3%. In addition to earnings growth and dividends, Altria stock has total return potential of nearly 15% per year, which is a highly attractive rate of return.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	28.2%	24.1%	24.6%	24.3%	27.1%	30.0%	29.5%	35.3%	25.2%	27.7%	***28.0%***	***28.0%***
Int. Cov.	30.1	5.1	6.0	5.6	6.7	7.6	10.7	10.9	30.3	15.0	***12.8***	***12.8***
Payout	101%	75.0%	78.1%	96.3%	82.5%	81.4%	81.2%	81.3%	86.1%	74.9%	***73.2%***	***73.3%***
Std. Dev.	21.8%	18.0%	15.0%	12.9%	15.4%	13.5%	13.9%	19.6%	12.5%	20.6%	***16.3%***	***16.3%***
Debt/A	89.6%	88.8%	86.0%	89.9%	90.9%	88.1%	91.2%	90.7%	72.2%	64.4%	***65.0%***	***65.0%***

Altria has tremendous competitive advantages. It operates in a highly regulated industry, which helps insulate Altria from any competition. In addition, it has the most valuable cigarette brand in the U.S., with a number of other category-leading brands. This gives the company the ability to raise prices over time. Lastly, Altria's manufacturing and distribution costs are very low, thanks to its economies of scale. Altria spent just $199 million in capital expenditures last year, and it generated $4.9 billion of operating cash flow. Altria also has a highly secure dividend payout. The company has a target dividend payout ratio of 80%.

Another benefit of Altria's business model is that it is highly resistant to recessions. Altria's product line includes cigarettes and alcohol, sales of which generally do not decline when the economy enters a recession. Altria's earnings rose steadily throughout the Great Recession, and investors can expect Altria's earnings to hold up very well when the next recession occurs.

Final Thoughts & Recommendation

Altria stock has declined to start 2018, due to falling cigarette sales volume in the U.S. This has highlighted concerns of declining smoking rates. Since cigarettes still represent over 80% of Altria's revenue and profit, this is a potential risk factor for investors. However, Altria is investing in new products that will meet the changing consumer demands. In the meantime, investors have the opportunity to invest in a high-quality business trading at a significant discount to fair value. With a low valuation and high dividend yield, Altria could deliver double-digit annual returns, which makes the stock a buy for value and income investors.

Total Return Breakdown by Year