Altria

NYSE:MO

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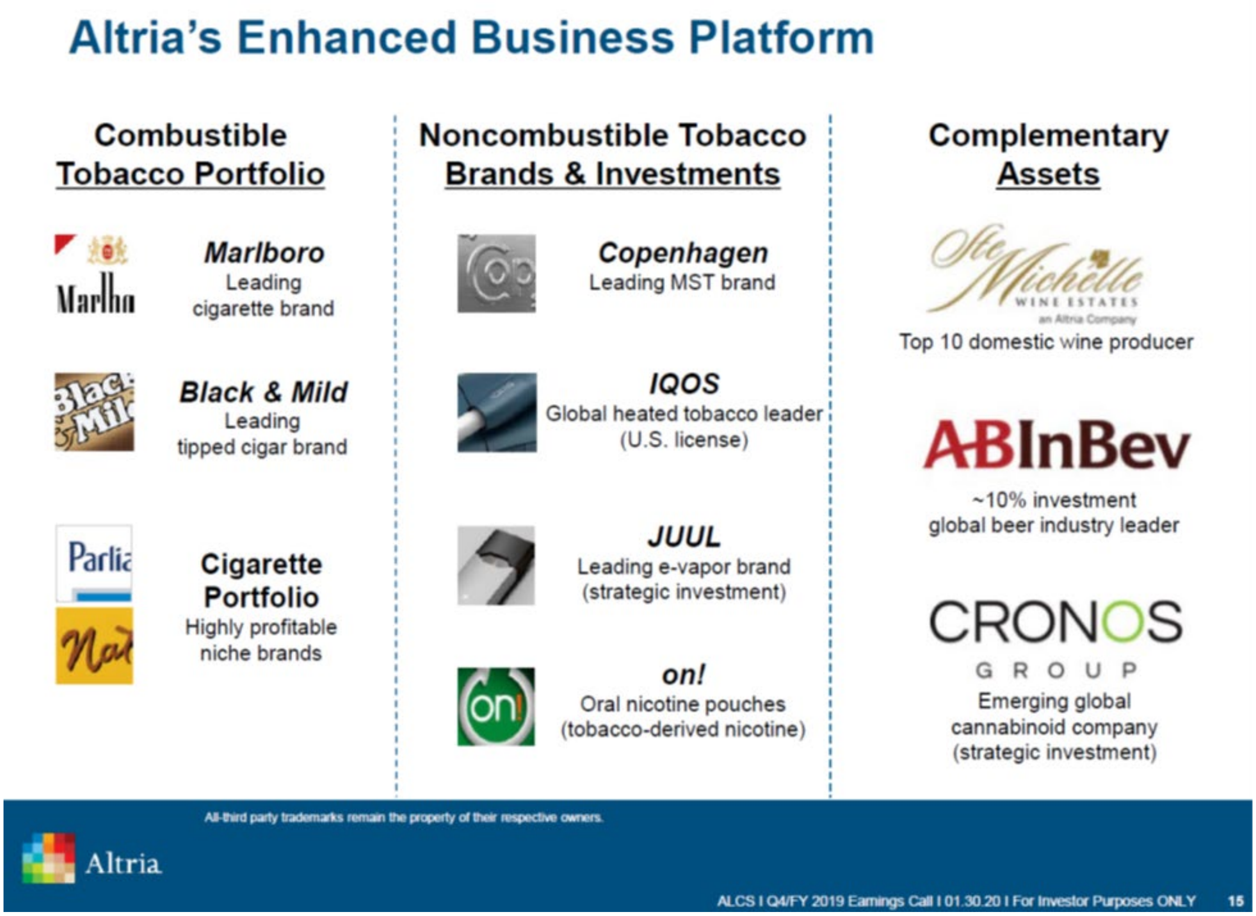
Note: All dollar figures are $US unless stated otherwise.

Introduction

Altria Group Inc. ("Altria" or "MO") is the largest producer of tobacco products in the United States and one of the largest tobacco companies in the world. The company was formed as part of the split of the US and international Philip Morris tobacco businesses in 2008. As a result of the separation, Altria's business activities are confined to the US market. The company is headquartered in Richmond, Virginia and its stock is listed on the NYSE (MO).

Altria's reportable segments are smokeable products, oral tobacco products (formerly called smokeless products) and wine. Through its subsidiaries Philip Morris USA (PM USA), U.S. Smokeless Tobacco Company (USSTC), John Middleton, Nat Sherman, and Helix, Altria offers various tobacco products in the premium and value segments. PM USA is the leading cigarette producer in the United States, with Marlboro its flagship brand. USSTC is the leading producer of moist smokeless tobacco (MST) products. Altria also produces and distributes wine through its Chateau Ste. Michelle subsidiary. Altria currently holds large minority stakes in Anheuser-Busch InBev – a.k.a AB InBev (10.1%), JUUL Labs (35%) and Cronos Group (45%).



The US Tobacco Market

The US tobacco industry is dominated by a handful of major players of which Altria is the clear leader. Industry estimates place Altria's US market share at approximately 50% and Reynolds American at 35%. The ability of tobacco companies to maintain market share depends on quality of product, innovation, price and brand reputation.

Due to the addictive nature of tobacco products and their adverse health impacts, the US government continues to take an active role in managing tobacco products via regulation, bans and other restrictions. The most recent regulatory changes to the US market include increasing the minimum age to legally purchase tobacco products to 21 and requiring packaging to more clearly define health risks. Recent increases in tobacco use by youths have also led the US Food and Drug Administration (FDA) to introduce a comprehensive regulatory plan for e-vapor products.

Tobacco consumers have historically demonstrated habitual consumption and brand loyalty. Due to the highly addictive nature of nicotine, studies show that consumers are more likely to change their method of consuming nicotine — leading to cross-category switching — rather then quitting outright.

In recent years, consumer behavior has changed due to increasing health concerns and product innovation. Consumers have been more willing to try new nicotine alternatives (e.g. vaping or e-cigarettes) that claim to reduce health risks associated with smokeable products. This recent consumer shift may continue and lead to disruption of traditional combustible tobacco products.

Price is another important factor for many tobacco consumers. Economic uncertainty and price increases can deter consumers from purchasing tobacco products. A 10% increase in price causes a 4% decrease in purchase volume due to price elasticity. Price increases — a common practice in the industry — have led some customers to downgrade to value brands or quit entirely.

Investment Thesis

In its Smokeable Products segment, Altria produces premium and discount cigarettes and cigars. Cigarettes make up 98% of segment revenue by volume. Marlboro is the company's flagship product representing 85% of segment volume and possessing a 43% category market share in the US. The Smokeable Products segment is characterized by declining cigarette volumes, annual price increases and high and expanding margins.

In its Oral Tobacco Products segment, Altria once again owns a portfolio of leading brands spanning products such as moist smokeless tobacco (MST), snus and oral nicotine pouches. The segment is characterized by stable volumes, increasing prices and high and expanding margins. The category is generally more stable than the Smokeable Products segment due to reduced competition and fewer health concerns.

We prefer to value Altria's major investments (AB InBev, JUUL and Cronos) separately from the company's core business of smokeable and oral tobacco products.

We define Altria's core earnings as Operating Income (EBIT) from the Smokeable products and Oral Tobacco Products segments less interest expense and income taxes. Despite the rise of vaping, over the past five years, Altria has grown its core earnings at a compounded rate of 12.6%. The table below summaries our analysis for the periods 2014-2019 and LTM as of Q1 2020.

	2014	2015	2016	2017	2018	2019	LTM
Gross Revenue	24,522.0	25,434.0	25,744.0	25,576.0	25,364.0	25,110.0	25,841.0
Excise Tax incl. in sales	6,577.0	6,580.0	6,407.0	6,082.0	5,737.0	5,314.0	5,388.0
Revenue (net of Excise tax)	17,945.0	18,854.0	19,337.0	19,494.0	19,627.0	19,796.0	20,453.0
COGS	7,785.0	7,740.0	7,746.0	7,531.0	7,373.0	7,085.0	7,286.0
Gross Profit	10,160.0	11,114.0	11,591.0	11,963.0	12,254.0	12,711.0	13,167.0
SG&A	2,539.0	2,708.0	2,650.0	2,338.0	2,756.0	2,226.0	2,230.0
Asset Impairment & Exit Costs	(1.0)	4.0	179.0	32.0	383.0	159.0	119.0
EBIT	7,622.0	8,402.0	8,762.0	9,593.0	9,115.0	10,326.0	10,818.0
Adjustments	20.0	21.0	21.0	21.0	38.0	44.0	55.0
Adj. EBIT	7,642.0	8,423.0	8,783.0	9,614.0	9,153.0	10,370.0	10,873.0
Net Interest Expense	808.0	817.0	747.0	705.0	665.0	1,280.0	1,171.0
Net periodic benefit cost				37.0	(34.0)	(37.0)	(9.0)
EBT	6,834.0	7,606.0	8,036.0	8,872.0	8,522.0	9,127.0	9,711.0
Income Tax	2,704.0	2,835.0	2,812.6	2,972.1	2,374.0	2,064.0	2,227.0
Operating Net Income	**4,130.0**	**4,771.0**	**5,223.4**	**5,899.9**	**6,148.0**	**7,063.0**	**7,484.0**
Shares o/s (f.d.)	1,978.0	1,961.0	1,952.0	1,921.0	1,888.0	1,869.0	1,865.0
Operating EPS	$2.09	$2.43	$2.68	$3.07	$3.26	$3.78	$4.01
Dividends per share	$2.00	$2.17	$2.35	$2.54	$3.00	$3.28	$3.32
Dividend Payout Ratio (on core earnings)	96%	89%	88%	83%	92%	87%	83%
Dividend Payout Ratio (incl. SAB/ABI dividends)	86%	82%	77%	70%	84%	83%	81%
Effective Tax Rate	40%	37%	35%	34%	28%	23%	23%
Operating EPS *	$2.09	$2.43	$2.68	$3.07	$3.26	$3.78	$4.01
Owner EPS ex- SAB/ABI dividends *	$2.10	$2.40	$2.67	$3.19	$3.23	$3.74	$4.00
Dividends received from SAB/ABI (per MO share)	$0.23	$0.25	$0.37	$0.42	$0.35	$0.21	$0.10
Owner EPS + Dividends	$2.33	$2.65	$3.04	$3.61	$3.58	$3.96	$4.10
Management's Adjusted EPS	$2.57	$2.80	$3.03	$3.39	$3.99	$4.22	$4.39
Owner Earnings *	**4,609.0**	**5,205.0**	**5,948.8**	**6,940.0**	**6,756.0**	**7,395.0**	**7,463.0**
Owner EPS *	$2.33	$2.65	$3.05	$3.61	$3.58	$3.96	$4.00
Owner Earnings ex-ABI dividend *	**4,153.0**	**4,710.0**	**5,209.8**	**6,134.0**	**6,099.0**	**6,999.0**	**7,463.0**
Owner EPS - ex ABI dividend *	$2.10	$2.40	$2.67	$3.19	$3.23	$3.74	$4.00

* Per GreensKeeper and company reports

	2014	2015	2016	2017	2018	2019
1998 Master Settlement AMT in COGS	4,600.0	4,500.0	4,600.0	4,500.0	4,200.0	4,200.0
COGS ex- 1998 Master Settlement	3,185.0	3,240.0	3,146.0	3,031.0	3,173.0	2,885.0
Stated Gross Margin	57%	59%	60%	61%	62%	64%
Adjusted Gross Margin	82%	83%	84%	84%	84%	85%

The only adjustments we made to Altria's stated (US GAAP) figures were to add back the minor annual amortization of intangibles and net periodic benefit cost adjustment and to normalize the income tax rate for 2016 and 2017. We also ignore the wine segment as its financial contribution is immaterial (the segment represents a small percentage of revenue and achieves a breakeven contribution).

Management typically guides analysts and the market to an "adjusted EPS" figure which includes the contribution from AB InBev and backs out restructuring and other charges. We present the management Adjusted EPS figure in the table above for reference. But given the recurring nature of restructuring and other expenses we view them as true expenses that should be deducted to derive a more accurate view of the profitability of the core business.

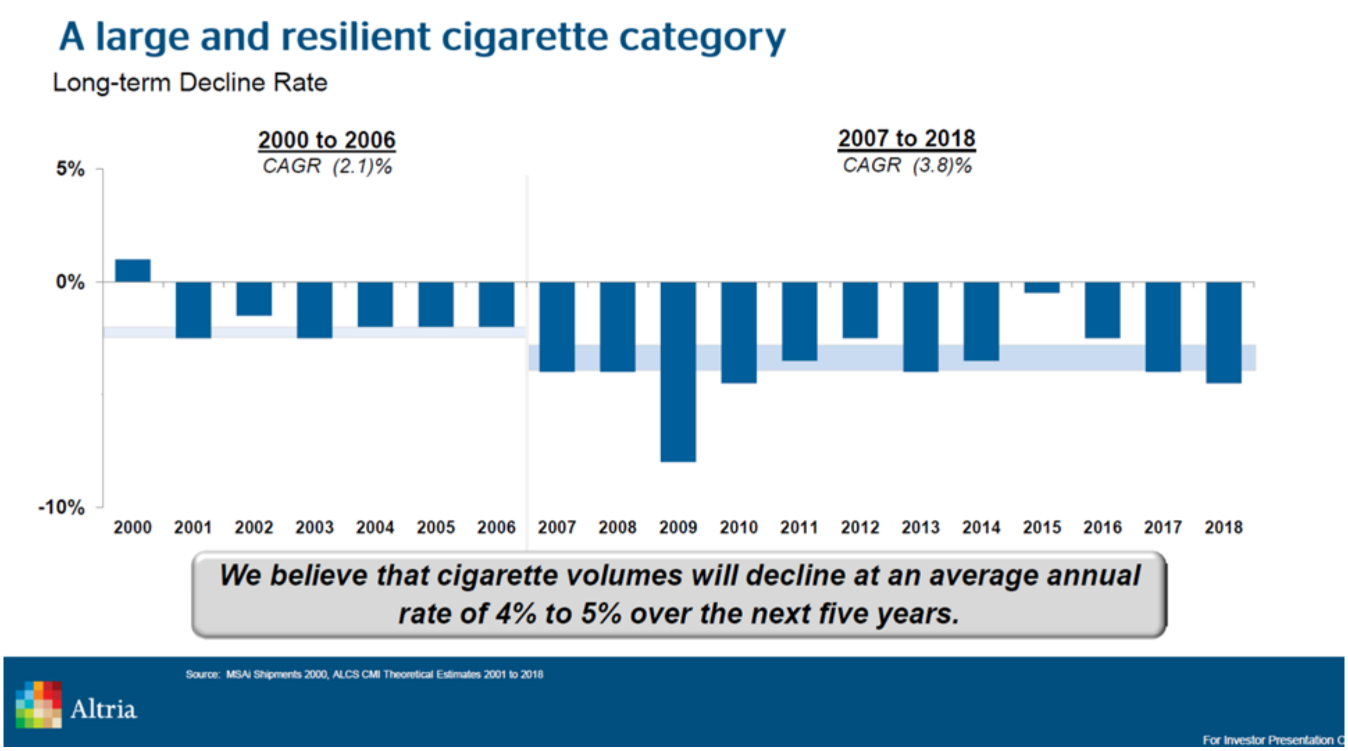
As a check on our core EPS calculations, we also calculated the Owner Earnings for each year during the period using similar methodology. Our results under both methods were consistent.

Altria has compounded its Core EPS and Owner EPS at approximately 12.6% over this period. We would also highlight that Core EPS and Owner EPS were both sufficient each year to cover the company's dividend payments without relying on any dividend receipts from SABMiller /AB InBev.

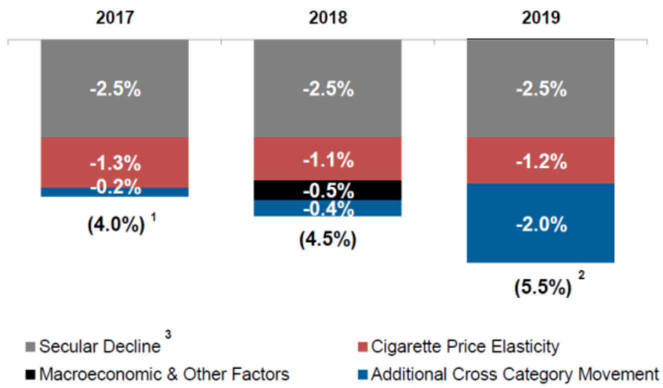
Key Value Drivers

In our experience, many investment theses turn on just a few key variables that truly matter. We believe that Altria is no exception. The crux of our investment case for Altria rests on future volume decline rates for smokeable products and Altria's continued ability to raise prices to offset that decline. The bear case for MO seems to rest on the argument that the growth of e-vapor and e-cigarettes will permanently impair Altria's smokeables business and accelerate the historical rate of secular decline.

The health risks associated with cigarettes have been known for decades, yet the industry continues to not only survive, but thrive. Decline rates vary year to year but over the long-term, appear to be in the mid-to-low-single-digit range. Altria management has recently commented that they expect US cigarette industry volumes to decline annually at a rate of 4-6% going forward.



The large 9.2% decline in 2009 in the above chart stands out and led us to investigate further. Our analysis revealed that it was partially due to the economic impacts of the Great Recession. However, it was also exacerbated by the massive April 2009 increase in the Federal Excise Tax on cigarettes (from $0.39 per pack to $1.01 per pack or an increase of 159%) imposed by the Obama Administration.



1 Macroeconomic & Other Factors had little to no impact to the cigarette industry volume decline rate for 2017
2 Macroeconomic & Other Factors were a 0.2% tailwind to the cigarette industry volume decline rate for 2019
3 Includes approximately 1% historical movement across tobacco categories

Source: 2019 Altria Q4 conference call slides

Our view is that the present decline rate remains steady at around 5% which is consistent with management's forecast. The recent uptick in the rate from prior periods has been attributed to the rise of e-vapor products and is discussed further below.

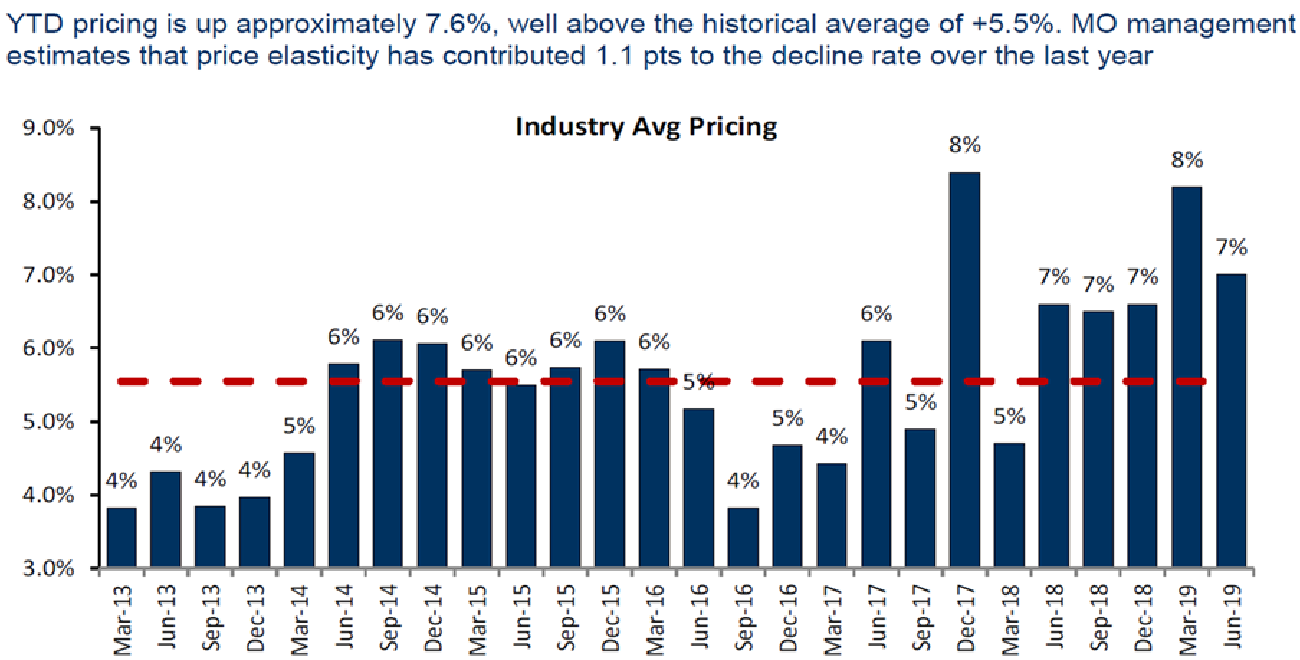
Pricing

Declining cigarette volumes have been a feature of the US market since 1981. Despite that relentless headwind, the tobacco industry has continued to deliver exceptional shareholder returns.

The business strategy to manage the secular decline is straightforward. Altria's long-term growth algorithm relies on implementing price increases several times a year to offset lost volume. The quantum of the price increases are tweaked based on experienced volume declines. In the latest earnings conference call, the company's CEO referred to their "continued use of revenue growth management". Price elasticity has remained steady for decades and so the company uses its pricing power as needed to offset the volume declines as they occur.

> *"So we don't go into the year with a pricing plan and just stick to it. We evaluate that as we progress through the year. But we certainly feel very confident about the tools we have available and now supported by the advanced analytics."*

CEO William Gifford – Q1 2020 Earnings Call



Source: https://twitter.com/ChrisPavese/status/1169707375202373633

Due to price elasticity, management uses price increases as sparingly as possible in order to achieve their financial objectives. The fixed nature of a large portion of the federal excise taxes blunts the impact of wholesale price increases on consumer retail prices.

Altria's pricing power comes from the strength of its brands — especially the iconic Marlboro brand — and the oligopolistic structure of the industry. Increasing prices and lower product volumes leads to continued margin expansion over time. The company's revenues generally grow at a low-to-mid-single digit annual rates.

Regulations now essentially prohibit advertising which make it nearly impossible for new entrants to enter the market, further widening Altria's moat.(1) Standardized packaging and advertising restrictions also thwart new brand creation which benefits the incumbents. In additional to creating barriers to entry and reinforcing pricing power, these regulations also lower marketing costs for manufacturers.

Declining volumes and lowered advertising costs lead to lower operating expenses. Altria has continued to consolidate its manufacturing facilities over the years and trimmed its employee workforce thereby lowering operating costs. These moves have further increased operating margins. Over the past 20 years, pricing actions and reduced operating costs have driven operating margins from 25% to over 55%. They continue to increase.

(1) The 1998 Net Master Settlement has also been criticized for creating additional barriers to entry and locking in the market position of the current oligopoly. See e.g. A Tobacco Cartel Is Born, Paid For by Smokers, The Wall Street Journal, May 1, 2000.

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We modeled the future price of a pack of Marlboros in the US a decade from today under the following assumptions:

- Annual volume declines of 5% in 2020 and 2022-2030
- A more severe volume decline of 7% in 2021 due to COVID and its impact on the economy and market share losses due to down trading
- Targeting a 1% annual revenue increase in this segment

The result: the average retail price of a pack of Marlboros would go from $7.68 to $14.47 in the next decade with an annual increase of approximately 6.3%. We believe that this is manageable and unlikely to disrupt the company's long-term growth algorithm. In fact, many developed economies already have higher per-pack pricing due to higher excise taxes. We suspect that American values of liberty and individual freedoms should continue to result in modest excise taxes relative to other countries.

Price - 20 Pack (Marlboro)	
Australia	$20.90
New Zealand	$18.36
Ireland	$14.10
United Kingdom	$13.63
Norway	$11.96
France	$10.84
Canada	$10.76
Israel	$9.96
Iceland	$9.91
Singapore	$9.91
Switzerland	$8.74
Finland	$8.30
United States	$8.00

Source: https://www.numbeo.com/cost-of-living/prices_by_country.jsp?displayCurrency=USD&itemId=17

Oral Tobacco Products

While Altria's cigarette brand lineup is unmatched, its oral tobacco brands are equally as impressive. Altria owns the Copenhagen and Skoal brands and has a broad product lineup with a 50.4% share of the US market. In 2019 the company also purchased an 80% interest in the on! nicotine pouch brand.

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Our Unmatched Oral Tobacco Portfolio

Altria's Oral Tobacco Products segment revenues have been growing at a mid-single-digit rate. Stable volumes, annual price increases and a strong brand lineup have led to segment operating margins of 70% and rising. This growing segment contributes about 11% of Altria's tobacco revenues and 15% of the company's operating profit. The strength of this segment provides stability and helps to offset some of the pressures on the traditional smokeable business.

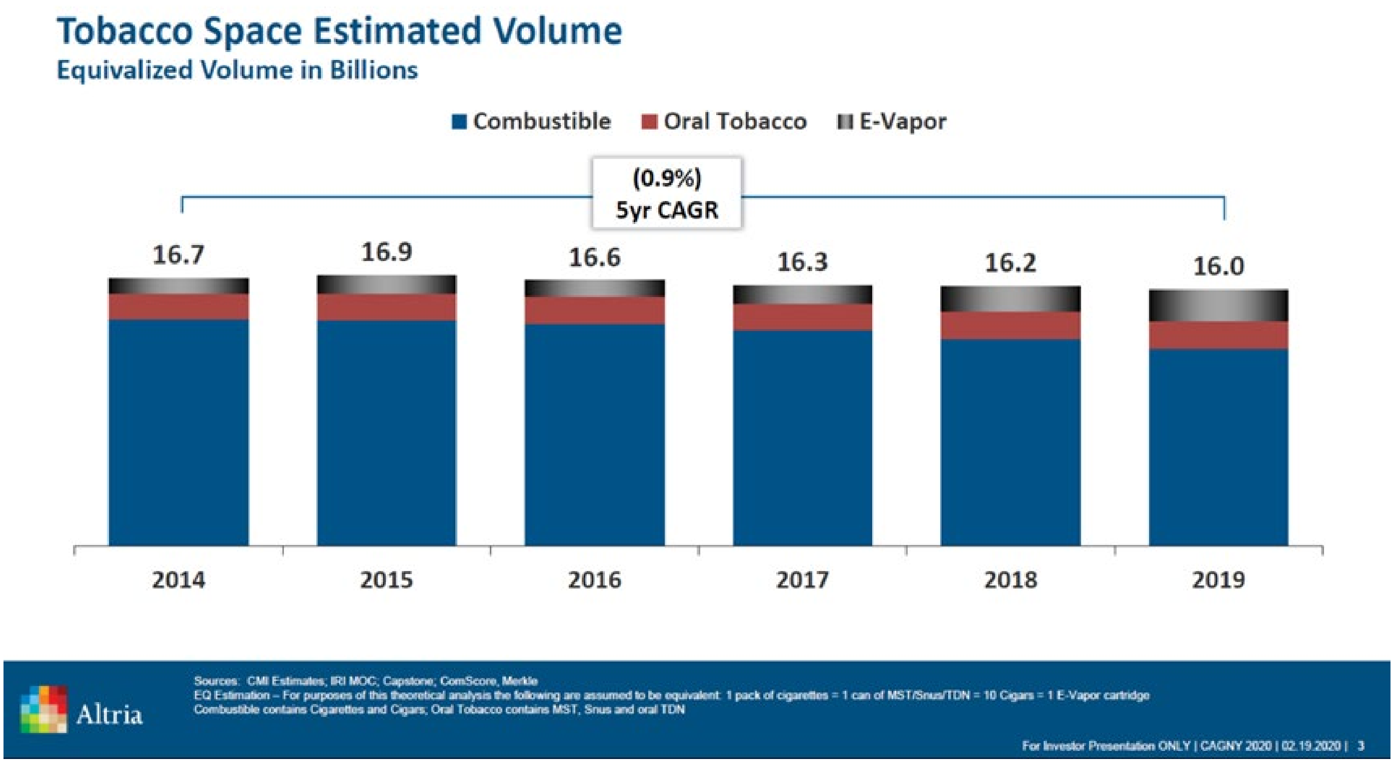
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Smokeable Products										
Revenue	$14,843	$14,917	$15,232	$15,217	$15,523	$16,369	$16,604	$16,709	$16,712	$16,830
EBIT	$5,618	$5,737	$6,239	$7,063	$6,873	$7,569	$7,766	$8,426	$8,408	$9,009
Revenue Growth (y/y)		*0.5%*	*2.1%*	*-0.1%*	*2.0%*	*5.4%*	*1.4%*	*0.6%*	*0.0%*	*0.7%*
EBIT Margin	*37.8%*	*38.5%*	*41.0%*	*46.4%*	*44.3%*	*46.2%*	*46.8%*	*50.4%*	*50.3%*	*53.5%*

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Oral Tobacco										
Revenue	$1,447	$1,519	$1,578	$1,648	$1,671	$1,746	$1,916	$2,023	$2,131	$2,240
EBIT	$803	$859	$931	$1,023	$1,061	$1,108	$1,172	$1,306	$1,431	$1,580
Revenue Growth (y/y)		*5.0%*	*3.9%*	*4.4%*	*1.4%*	*4.5%*	*9.7%*	*5.6%*	*5.3%*	*5.1%*
EBIT Margin	*55.5%*	*56.6%*	*59.0%*	*62.1%*	*63.5%*	*63.5%*	*61.2%*	*64.6%*	*67.2%*	*70.5%*

The Rise (and fall?) of e-vapor

The major challenge facing Altria and all combustible cigarette manufacturers at present is the rise of e-vapor / e-cigarette consumption. In recent years, there has been a slight uptick in the secular decline rate of smokeable products which has been attributed to this consumer shift. We believe the threat of a major disruption by the e-vapor category is overstated. Big tobacco has successfully managed through many quandaries over the decades. Perhaps our investment thesis should be called "this time it isn't different".

The e-vapor category is currently about 10% of the size of the smokeable market (by volume) and the oral tobacco segment represents another 10%. The e-vapor category in the United States is dominated by the JUUL brand with an estimated market share of 70%+. JUUL sales grew rapidly in recent years and attracted interest from Altria which culminated in its purchase of a 35% stake in JUUL in 2018 for $13.5 billion.

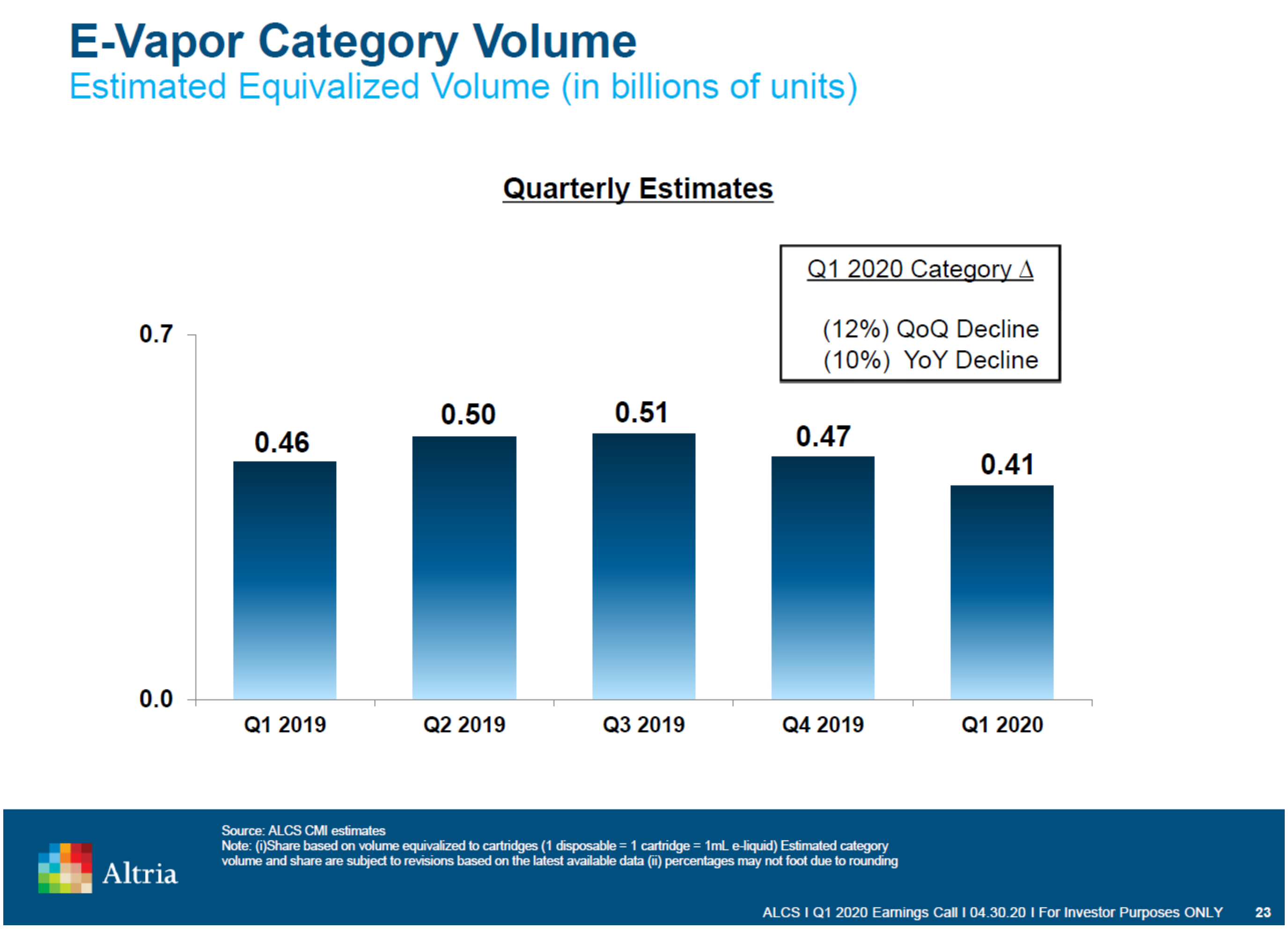


JUUL's rise and its popularity with teens and young adults has also attracted the attention of regulators and legislators. Adding to the increasing scrutiny of this new segment was an outbreak of e-cigarette or E-vapor Product Use Associated Lung Injury (EVALI) which sickened thousands of youths in the United States and led to dozens of deaths. The culprit is likely the use of Vitamin E acetate being used by illicit manufacturers in THC vape products (JUUL does not sell products containing THC).

As a result of growing youth usage and EVALI, a regulatory crackdown ensued and remains in progress. Changes have included an increase in the minimum age required to purchase tobacco products to 21, the banning of many flavored products and the requirement for alternative tobacco delivery systems to submit a pre-market tobacco application (PMTA) to the FDA by September, 2020 in order to be permitted to remain on the market.

Altria is providing regulatory assistance to JUUL in order to prepare their FDA PMTA submission. The cost to compile a PMTA has been estimated at over $1 million per SKU. Smaller competitors will likely be acquired or driven out of business given the expense and expertise required to ensure continued market access. In addition, as with the traditional cigarette market, restrictions on promotion will create barriers to entry and favor established brands like JUUL. Complicated and expensive PMTA submissions and increasing regulatory and legal challenges play to big tobacco's strengths.

We believe that this recent negative publicity will inevitably lead to slowing e-vapor use and possibly reverse the recent gains that e-vapor products have made on traditional tobacco products. There are early signs that this is in fact already happening as shown in the chart below.



The future potential of the e-vapor market is uncertain. It is also unclear if vaping will accelerate the long-term secular decline rate of traditional tobacco products. If vaping is here to stay, we like JUUL's market position but recognize that the company will need to clean up its act. We believe that they are already taking positive steps in that direction.

Due to the potential threat that vaping poses to smokeable tobacco products, we understand the strategic rationale of Altria's investment in JUUL. A strategic investment in the leading player seems like a smart way to hedge against the risk of future disruption.

However, the purchase price paid by Altria was unforgivable. JUUL was unprofitable at the time of Altria's investment and remains so today. The $36.5 billion valuation placed on the business at the time represented 50x revenue and a sharp increase from a recent JUUL financing round according to industry reports. Altria appeared to be desperate to make the investment at any price. The result? Altria has since written down the value of its investment in JUUL by $8.6 billion (67%) in just two short years.

The silver lining in Altria's value-destroying capital allocation decision is that the resulting stock selloff provided us with an opportunity to acquire MO shares at an attractive price for clients who are comfortable with tobacco investments.

Altria's former CEO responsible for the acquisition recently "retired" and the roles of board Chairman and CEO recently separated. We believe that the new CEO and the board have been sufficiently chastened to exercise greater financial discipline going forward. The importance of the company's dividend to shareholders and the company's high payout ratio will impose further capital allocation discipline on management and the board going forward.

In addition to its stake in JUUL, Altria also has the exclusive rights to commercialize Philip Morris International's IQOS electronically-heated tobacco product. IQOS received FDA approval in April 2019 and Altria is just starting its rollout of the product in selected US markets.

Whether e-vapor and e-cigarette delivery systems will accelerate the secular decline rate for smokeable products is far from clear. We suspect that traditional tobacco products will prove to be more resilient than the market is currently pricing into Altria's stock. If we are wrong and the traditional market is disrupted, Altria is well positioned in these segments by way of its relationships with both JUUL and IQOS.(2)

Balance Sheet

As a testament to the strength of Altria's core business, despite issuing debt to fund the $15 billion of cash paid for its stakes in JUUL, Cronos and on! in just the past few years, Altria's balance sheet remains in decent shape.

Net debt to EBITDA is currently below 2.3x and Interest Coverage (EBIT/Interest) is approximately 8.6x. Both figures are appropriate for a stable business with minimal capital expenditures. Moody's and Standard & Poor's rate the company's debt A3 and BBB respectively. Debt is prudently termed out over 40 years and the overall financial leverage of the business is appropriate.

(2) As an interesting side note to the transaction, the Federal Trade Commission (FTC) is now suing Altria for anti-competitive behavior relating to its investment in JUUL and is seeking to unwind the transaction. Altria has stated that it disagrees with the FTC's position and plans to vigorously defend the lawsuit. We can not predict the ultimate outcome of this lawsuit.

AB InBev Position

Altria currently owns a 10.1% stake in Anheuser-Busch AB InBev SA/NV (NYSE:BUD). Most of its stake was received as part of Altria's sale of its interest in SABMiller plc to AB InBev in 2016. Altria's entire stake in AB InBev becomes freely tradeable in October 2021.

Based on the current trading price of AB InBev, Altria's holding is currently worth $8.55 billion. We estimate that Altria would pay approximately $1.1 billion in taxes if it were to dispose of the entire holding. Accordingly, Altria's position in AB InBev would generate net proceeds of $7.4 billion or $3.99 per MO share at AB InBev's current trading price. Stated differently, the AB InBev stake is currently worth 10.8% of Altria's current market cap. It is also worth noting that AB InBev's stock is currently trading 57% below its 52-week high.

The sizable proceeds from a sale of this stake could be used to trim debt (if necessary) and/or repurchase MO shares. We do not view the AB InBev holding as strategic and it provides Altria management with welcome financial flexibility.

Dividends

Altria has increased its dividend payments in each of the past ten years by an average of 9.6% per annum. We estimate that the current dividend rate of $3.32 represents 83% of Altria's Core EPS. Our view is that the dividend is not only safe, but that it will continue to increase.

Given management's past capital allocation transgressions, we prefer a high payout ratio in order to impose fiscal discipline and deter them from venturing outside of their core business of tobacco. At the current share price of $36.74, MO's current annual dividend yield is 9.1%.

Valuation

Our base case assumes that Altria will continue to grow revenues at low single-digits and that the secular decline rate of cigarette volumes remains mid-single-digits. We also assume modest margin expansion due to increased pricing and the reduced cost of goods sold and operating expenses.

We further assume a slower pace of share repurchases and dividend increases going forward. Ignoring the investment in AB InBev for the time being, we derive core EPS growth of low to mid-single-digits.

For a company with a high ROIC, ROE in excess of 100%, an appropriate level of financial leverage and an 80-90% payout ratio, we believe that MO is conservatively worth at least 11-12x earnings (probably more).

Altria's LTM core EPS of $4.01 suggests an intrinsic value range of $44 to $48 per share. Using the current trading price of AB InBev and fully accounting for the taxes that Altria would pay on a disposition, Altria's stake in AB InBev is currently worth US$7.43 billion or $4 per MO share.

We assume no contribution from JUUL or Cronos and value both investments at $0. If Cronos were valued at its current FMV and JUUL were valued at Altria's current carrying value of $4.2 billion, they would add $0.43 and $2.25 per MO share of value respectively ($2.68 per MO share in total).

LTM Core EPS	$4.01	
Conservative Multiples	11x	12x
Fair Value Range (core business)	$44.11	$48.12
ABI Stake per MO Share	$3.99	
Intrinsic Value	**$48.10**	**$52.11**
Dividend Discount Model		
Current Dividend	$3.36	
Intrinsic Value (g=3%, r=10%)	$49.44	
Other Investments (Ignored)		
JUUL @ Carrying Value per MO share	$2.25	
Cronos @ FMV per MO share	$0.43	
	$2.68	

As a check, we calculated the value of the company's dividend stream (Dividend Discount Model) using an assumed 3% annual increase and a 10% discount rate. Under these assumptions, the core business is worth $49.44 and adding in the value of the AB InBev stake results in an overall value of $53.43.

We should point out that Altria and its predecessors have increased their dividend 54 times in the company's 51-year history, usually at rates well in excess of our 3% assumption. Unless the company's smokeable business has truly been disrupted, we like our odds of a satisfactory outcome. With a 9.1% dividend yield and EPS growth of 3% we expect a low double-digit annual return without the benefit of any multiple expansion.

In sum, our intrinsic value estimate for MO is between $48-$53 per share and is based on what we believe to be conservative assumptions. Compared with a trading price of $36.74 and a dividend yield of 9.1%, we believe the shares of this high-quality company are undervalued at present.

In addition to the margin of safety provided by the current trading price, investors in Altria also have optionality from Altria's investments in JUUL and Cronos which we value at $0. We are not counting on them to justify our investment decision but will benefit if they work out. Potential upside also comes from the fact that AB InBev is trading at historically low multiples. Once again, we aren't counting on it, but believe that the stake could increase in value in time.

Finally, if our assumptions prove to be conservative, there is a possibility of multiple expansion if market sentiment on the company eventually changes. Based on historical trading multiples, MO is currently trading at depressed levels suggesting that the market is questioning the sustainability of both the dividend and the company's business model. Altria is also trading at a material discount to other comparable companies.

GreensKeeper
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Company Name	Last Trade	Market Cap	Enterprise Value	TEV/EBITDA (LTM)	Forward P/E	Dividend Yield	LTM EBIT Margin %	LTM EBIT Growth %	LTM Total Debt/EBITDA
Philip Morris International Inc.	$72.00	$112,113	$138,618	10.7x	14.72x	6.50%	38%	5.6%	2.2x
British American Tobacco p.l.c.	$37.02	$84,620	$138,168	9.2x	8.89x	7.10%	41%	5%	3.9x
Altria Group, Inc.	$36.74	$68,276	$92,763	7.0x	8.67x	9.10%	55%	15%	2.6x
Japan Tobacco Inc.	$18.50	$32,817	$41,096	7.1x	12.07x	7.80%	20%	-26%	1.9x
Imperial Brands PLC	$20.23	$18,976	$33,893	7.2x	6.23x	12.70%	17%	8%	3.6x

Source: S&P Capital IQ

COVID-19

The pandemic is having minimal impact on Altria's business. Retail outlets selling the company's products remain open. Production at Altria's manufacturing facilities in Richmond, Virginia was disrupted for a short period of time when several employees tested positive. Altria retains several months' worth of finished goods inventory on hand which ensures continued market supply.

Q1 2020 sales were robust with management citing some pantry loading by consumers which is likely to unwind in the coming months. The major potential COVID impact on Altria's business is likely to be due to unemployment. Tobacco is a resilient and defensive business, but unemployment usually leads to down trading which hurts the company disproportionately given its strength in the premium segment of the market. Unemployment also lowers overall demand due to consumer budgetary constraints. Overall the impact from the coronavirus is likely to be short-lived and modest on the company's overall prospects.

The company did draw down $3 billion on its revolving line and has stated that the company will continue to carry excess liquidity in the current environment. Commercial paper markets have been disrupted recently and we view the move as prudent. Last week the company raised $2 billion in term debt which we believe will eventually be used to repay existing debt.

Risks

In addition to the risks cited in this report, the tobacco industry and Altria specifically are both subject to numerous risks including increasing regulation, increased excise taxes, litigation, changing consumer preferences, etc. Please read the company's latest 10K and other SEC filings for additional risk factors and conduct your own research before making any investment decisions.

Conclusion / Summary

The opportunity to purchase shares in a high-quality business at an attractive valuation (< 10x P/E, 9.1% yield) comes along infrequently.

Provided that investors are comfortable investing in the tobacco sector and share our view that the disruption to the smokeable products (cigarettes) is overstated, and in any case, can be managed via Altria's investments in emerging products, an investment in Altria at current market prices should deliver attractive financial returns.

Disclosure: Certain accounts managed by GreensKeeper Asset Management Inc. may own shares of Altria and other securities mentioned in this report.

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