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Altria Group, Inc. (MO) CEO Howard Willard on Q3 2019 Results - Earnings Call Transcript

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Q3: 10-31-19 Earnings Summary

Press Release *Slides*

EPS of $1.19 beats by $0.04 | Revenue of $5.41B (2.27% Y/Y) beats by $68.73M

Earning Call Audio

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Altria Group, Inc. (NYSE:MO) Q3 2019 Results Earnings Conference Call October 31, 2019 9:00 AM ET

Company Participants

Mac Livingston - Vice President, Investor Relations

Howard Willard - Chief Executive Officer

Billy Gifford - Chief Financial Officer

Conference Call Participants

Chris Growe - Stifel

Michael Lavery - Piper Jaffray

Robert Rampton - UBS

Steve Powers - Deutsche Bank

Owen Bennett - Jefferies

Pam Kaufman - Morgan Stanley

Nik Modi - RBC

Gaurav Jain - Barclays

Vivien Azer - Cowen

Michael Lavery - Piper Jaffray

Robert Rampton - UBS

Adam Spielman - Citi

Steve Powers - Deutsche Bank

Petros Voulgaris - Goldman Sachs

Angelica LaVito - CNBC

Jennifer Maloney - Wall Street Journal

Operator

Good day, and welcome to the Altria Group 2019 Third Quarter Earnings Conference Call. Today's call is scheduled to last about one hour including remarks by Altria's management and a question-and-answer session. [Operator Instructions]

I would now like to turn the call over to Mr. Mac Livingston, Vice President of Investor Relations for Altria Client Services. Please go ahead sir.

Mac Livingston

Good morning, and thank you for joining us. We're here this morning with Howard Willard, Altria's CEO; and Billy Gifford, our CFO to discuss Altria's 2019 third quarter and first half business results.

Earlier today, we issued a press release providing these results. We're also including slides to accompany our remarks. And all of this information is available on our website at altria.com and through the Altria Investor App.

During our call today, unless otherwise stated, we're comparing results to the same period in 2018. Our remarks contain forward-looking and cautionary statements and projections of future results. Please review the forward-looking and cautionary statement section at the end of today's earnings release for various factors that could cause actual results to differ materially from projections. Future dividend payments and share repurchases remain subject to the discretion of Altria's board. Share repurchases also depends on marketplace conditions and other factors.

Altria reports its financial results in accordance with U.S., Generally Accepted Accounting Principles. Today's call will contain various operating results on both the reported and adjusted basis. Adjusted results exclude special items that affect comparisons with reported results. Descriptions of these non-GAAP financial measures and reconciliations are included in today's earnings release and on our website at altria.com.

With that, I'll turn the call over to Howard.

Howard Willard

Thanks Mac and good morning everyone. We are in the midst of a remarkable transformation within the tobacco industry. Once predictable the industry has become increasingly dynamic and complex and while this evolution may pose short-term challenges we believe tobacco harm reduction is a significant opportunity for the industry and adult tobacco consumers. We believe that in the next decade, non-combustible products can surpass combustibles as the preferred choice among adult tobacco consumers. We intend to lead this historic transformation with our unmatched portfolio of non-combustible products and investments. Before moving to our strong third quarter performance I'd like to provide you with our perspective on Altria's strategy and the key non combustible platforms.

Over the last two years we believe we built a business platform with the ability to deliver strong long-term results across a variety of future industry scenarios. We understood that no single product would likely satisfy all adult smokers looking for alternatives and that the regulatory environment for non-combustible products would continue to evolve.

We assessed our portfolio and believe that we have addressed gaps with investments in e-vapor and oral nicotine pouches as well as an adjacent investment in cannabis. Today we believe we have the strongest portfolio across multiple tobacco platforms and are well positioned for future growth in a rapidly evolving U.S. tobacco industry.

Turning to the key non-combustible platforms the e-vapor category faces a critical inflection point. We must address underage use while also preserving options for the more than 20 million adult smokers who are interested in less harmful tobacco products. We continue to believe that raising the legal minimum age to purchase all tobacco products to 21 at the Federal and state levels is the most effective action to reverse the rise in youth vaping.

Today, more than 50% of the U.S. population is governed by Tobacco 21 Laws. And while there is strong momentum behind this change, more activity is required from the federal government and remaining states to enact Tobacco 21 Laws nationally. We also want swift action from the FDA and other public health authorities to take the appropriate actions regarding flavored e-vapor products and to identify the sources of the recent vaping injuries. We believe that these actions could reset the course for the e-vapor category and preserve its long-term potential for harm reduction. We are also excited about the opportunity that heated tobacco presents to adult smokers.

Based on third-party research, approximately 40% of U.S. adult smokers have tried, but ultimately rejected e-vapor products. We believe heated tobacco could be an appealing alternative for these adult smokers. Unlike e-vapor products, these systems contain real tobacco and offer a sensorial experience closer to that of traditional cigarettes.

The IQOS Heated Tobacco System is the first and only heated tobacco product that's received pre-market authorization from the FDA and it also has a pending MRTP application. We believe that heated tobacco systems and IQOS specifically are well positioned to meet the preferences of adult smokers who are looking for, but had not found a satisfying alternative to cigarettes.

Finally, we believe that oral tobacco can provide a compelling alternative for adult smokers. In moist smokeless tobacco, we filed a modified risk application with the FDA for Copenhagen snuff based on decades of available science. Additionally, we have invested in the rapidly growing oral nicotine pouch segment which offers adult tobacco consumers convenient nicotine satisfaction. Ultimately, the adult tobacco consumer and the regulatory framework will dictate which categories grow and at what pace. We believe our broad portfolio, investments and leading capabilities position us to win in multiple future scenarios.

Turning to third quarter performance, Altria continued to deliver excellent results driven by our core tobacco businesses. We grew adjusted diluted earnings per share over 10% in the third quarter with both of our core tobacco segments delivering double-digit adjusted operating company's income growth. Expanding their adjusted operating companies income margins and maintaining momentum on their leading premium brands.

The smokeable products segment delivered another remarkable quarter growing its third quarter adjusted operating companies income 12.6% and increasing its year-to-date adjusted operating companies income growth to 8.1%. Higher pricing and the impact of our cost reduction efforts more than offset lower cigarette volumes to drive income growth in both the third quarter and in the first nine months.

PM USA is pleased with Marlboro's performance with eight consecutive quarters of stability, since the end of 2017. In discount, L&M is performing in line with expectations and we are pleased with its increased profitability over time. We believe discount category dynamics continue to primarily reflect a churn between branded discount and deep discount offerings. Overall discount category retail share was flat sequentially in the quarter at 24.2% and remains in line with historical share levels.

We estimate that U.S. cigarette industry volumes declined by 5.5% in the third quarter and first nine months when adjusted for trade inventory movements, calendar differences and other factors. We continue to believe that increased adult smoker movement to e-vapor and high levels of exclusive e-vapor category usage were the primary drivers of the accelerated decline rate over the past year.

Based on our 12-month moving data, we estimate there are now 12.6 million adult vapers 21-plus as of September 2019, up from 10.3 million at the end of 2018. Importantly that growth trend coincides with the trend toward more exclusive usage in the category. According to our adult consumer tracking data, we estimate that 6 million adults 21-plus vape and do not smoke as of September 2019, which is the highest number of exclusive users since our study began in 2014.

Adult tobacco consumer movement across tobacco spaces remains highly dynamic and we will continue to monitor these trends. Over the past 12 months, U.S. cigarette industry volumes declined by an estimated 5.5% when adjusted for trade inventory movements, calendar differences, and other factors. We reaffirm our full-year 2019 U.S. cigarette industry adjusted volume decline estimates of 5% to 6%. We also maintain our 4% to 6% adjusted decline rate estimates through 2023 until more information is known about how adult tobacco consumers will respond to e-vapor category dynamics, including regulation and legislative developments.

Turning to our smokeless product segment results, USSTC is successfully executing against its strategy of maximizing income while maintaining momentum on Copenhagen over time. The smokeless product segment continued its strong 2019 performance, growing its adjusted operating companies income by 10.2% in the third quarter and 9.7% for the first nine months of 2019. Copenhagen's category-leading retail share was 24.7% for the third quarter, up one-tenth sequentially and up two-tenth versus the year ago quarter.

USSTC's smokeless volumes decreased an estimated 3% in the first nine months of the year when adjusted for trade inventory movements and calendar differences. In the last six months smokeless industry volume decreased by an estimated 1.5%. We believe these declines reflect increasing adult tobacco consumer interests in both e-vapor products and oral nicotine pouches.

In e-vapor, we participate in the category through our 35% economic investment in JUUL. We made the investment based on our belief that JUUL's product development strength, early signs of brand equity and potential to convert adult smokers set it apart from all other e-vapor products in the market. We also believe that the investment would enhance Altria's growing portfolio of noncombustible product offering.

Given the dramatic shifts in the current e-vapor regulatory and marketplace environments, we have revised our transaction assumptions. In preparing our financials this quarter, we performed a valuation analysis on our JUUL investment, which considered multiple regulatory and marketplace scenarios. In aggregate, we're now projecting lower e-vapor category volumes in the U.S. versus our original estimates, which resulted in a third quarter non-cash impairment charge of $4.5 billion related to our JUUL investment. Also factoring into this determination where other changes to our original assumptions. For example, we expect it may take longer for JUUL to realize the strong margin performance that we previously communicated.

We've also revised our estimates of JUUL's international business due to recent market development. Despite this impairment charge, we remain committed to JUUL's success. We are pleased with the recent decisions by JUUL to change leadership and we are optimistic about JUUL's focus and prioritization in key areas such as establishing industry-leading responsible practices and pursuing regulatory authorization of their products. Finally, regarding antitrust clearance, we've certified substantial compliance with the FTC's second request and we expect a resolution in the first quarter of next year.

Turning to the heated tobacco, PM USA is executing a robust marketing strategy for IQOS in the Atlanta lead market. The first US IQOS store opened in September, and has since been supplemented by additional retail touch points, including a mobile pop up unit and IQOS Corners located within select stores. We've also recently opened a second IQOS boutique in the Mall of Georgia.

Of course responsible marketing is the foundation for all our consumer interactions. IQOS is intended only for adult smokers and IQOS boutique entrants must be 21 or older. The performance of IQOS in Atlanta and other lead markets will be an important input to our future commercialization plan for the brand. The primary goals of the lead markets are to determine how best to communicate with adult smokers and how to scale our efforts. PMI's MRTP application for IQOS remains pending with the FDA and we are optimistic about the prospects of IQOS receiving this modified risk authorization. Additionally, we are encouraged that the FDA's draft PMTA rules, include a special pathway for technological changes to previously authorized products, which could support bringing newer versions of the IQOS device market.

Finally, we are excited to announce that IQOS will be expanding to Richmond, Virginia beginning next month. With an IQOS store opening in the Carytown district. Altria has a sizable employee base enrichment and deep connections with the community that could accelerate early adoption of IQOS. We also anticipate distributing heat sticks to approximately 150 retail outlets within the area and deploying a similar marketing strategy as the Atlanta lead market.

We are pleased to expand IQOS availability as an alternative to adult smokers and look forward to sharing more details in the future. In oral nicotine pouches, we are pleased to announce that the on! transaction closed during the third quarter. Now that the transaction is complete, we'd like to update you on our plans to pursue leadership in this new and fast growing category. We are focused on engaging adult tobacco consumers through both traditional retail and digital experiences. We launched a premium branded website for on! where age restricted adult tobacco consumers can explore the brand and will soon be able to purchase the product online.

We expect to begin production of on! in our Richmond manufacturing center beginning first quarter next year. In 2020, we are targeting annualized capacity of 50 million cans by mid-year and 75 million cans by year-end with additional capacity available if necessary. In addition, our strong regulatory affairs team is preparing PMTAs for the on! portfolio for the May 2020 deadline.

As a reminder, Altria owns 80% of the Helix Innovations joint venture that will commercialize on! globally. On! has a product portfolio consisting of 35 unique SKUs; seven flavor varieties across five nicotine strengths. We believe the breadth of nicotine strengths and flavors is a tremendous competitive advantage as both adult smokers and dippers can find satisfying options within the on! portfolio.

As I mentioned at the beginning of the call, we continue to believe the evolution of the tobacco industry represents a significant opportunity for Altria. We marked major milestones in our transformation journey this year, including launching IQOS and completing the on! transaction. We believe that with current adult smoker trends and e-vapor disruption it's an opportune time to expand the availability of these options.

We believe that incremental investment behind our noncombustible portfolio will best position Altria for long-term industry leadership. In light of these considerations, we are replacing our long-term adjusted diluted EPS growth aspiration of 7% to 9% with a compounded annual adjusted diluted EPS growth objective of 5% to 8% for the years 2020 through 2022.

We believe this new growth objective provides us the flexibility to make investments in noncombustible offerings for the long term, generate sustainable income growth in our core tobacco businesses and return cash to shareholders through a strong dividend. We also expect to maintain our dividend payout ratio target of approximately 80% of adjusted diluted EPS during this period. We will provide specific full-year 2020 adjusted diluted EPS guidance in January when we announce our fourth quarter 2019 results.

Turning to 2019 earnings, we reaffirm our guidance for full-year adjusted diluted EPS to be in a range of $4.19 to $4.27, representing a growth rate of 5% to 7% from an adjusted diluted EPS base of $3.99 in 2018. Altria's 2019 success to date can be attributed to our resilient core tobacco businesses and our talented employees. Our employee base has embraced industry disruption with focus and dedication. Our business results show what I see every day that our people propel our success and I thank them for that.

I'll now turn it over to Billy to provide more detail on our performance and other investments.

Billy Gifford

Thanks, Howard, and good morning everyone. We'll begin with additional color on our smokeable products segment. Reported domestic cigarette volume decreased 6.6% in the third quarter, primarily due to the industry's rate of decline, retail share losses and trade inventory movements, partially offset by one extra shipping day. When adjusted for calendar differences, trade inventory movements, and other factors, smokeable products segment cigarette volumes declined by an estimated 7% for the third quarter and 7.5% for the first nine months.

In the third quarter, the smokeable products segment expanded adjusted OCI margins by 4.9 percentage points to 55.3%, driven by higher pricing and lower controllable costs. In the smokeable products segment, excellent price realization reflects both pricing actions and greater efficiency and use of promotional resources, thanks to investments made in trade programs, data analytics and consumer data.

Net price realization was 9.6% in the third quarter and 8.4% for the first nine months of 2019. Marlboro's performance continues to be supported by its leading brand equity bolstered by investments in product expansion, packaging innovation, digital loyalty and trade programs. Specifically, the Marlboro's rewards program continues to resonate well with adult smokers and drive visits to Marlboro.com. Enrollment continue to grow in the third quarter and the program now has 2.5 million participants and 150 million pack codes have been entered since the program launched in January.

In cigars, volume grew 4.1% in the third quarter, outpacing the industry and Black & Mild continued its strength in the premium tip cigar segment. In the smokeless products segment, adjusted OCI margins expanded by 2.5 percentage points to 71.9% in the third quarter, primarily driven by higher pricing, lower promotional investments and lower controllable costs. USSTC's third quarter retail share was 53.9%, up 0.1% sequentially and down 0.4% versus the prior year.

Turning to our alcohol assets, in wine, the premium segment continues to be highly competitive. Ste. Michelle delivered adjusted operating companies income of $16 million, down nearly 45% in the third quarter, primarily due to higher promotional investments and lower shipment volume. And in beer, adjusted earnings from our equity investment in ABI were $238 million in the third quarter, up more than 6% year-over-year, reflecting Altria's share of ABI's second quarter results.

The cannabis space remains very active and Cronos is making progress and executing against its growth strategy. Cronos closed on its acquisition of Redwood Holdings during the third quarter, which provides Cronos with a leading U.S. hemp-based products platform. Redwood manufactures and sells hemp-derived CBD and few skincare and other consumer products under the Lord Jones luxury brand name. We believe the acquisition fits well into Cronos' strategy of building differentiated brands and disruptive intellectual property. We're very excited about the future prospects of the cannabis industry and the opportunity for Cronos to position itself for long-term leadership.

Moving to our capital allocation, we continue to return a significant amount of cash to shareholders in the form of dividends and share buybacks. In August, we marked a 50th year of dividend increases. We are proud of our dividend growth history and remain focused on providing long-term value to shareholders through dividends. With the recent increase Altria's current annualized dividend rate is $3.36 per share, which represents an annual dividend yield of 7.3% as of October 28, 2019.

We paid $1.5 billion in dividends in the third quarter, and we still expect to complete our previously announced $1 billion share repurchase program by the end of 2020. Altria's businesses generate significant cash flow. In fact, we've generally produced about $1 billion of cash annually in excess of our dividend payments, which provides flexibility to repurchase shares, finance debt maturities, and invest strategically in the business.

Our cost reduction program remains on track and we still expect to realize approximately $575 million and annualized cost savings by the end of 2019. Our savings continue to build from the second quarter into the third. And as the year progresses this offering is more -- this is offsetting more of the incremental interest expense we incurred in connection with our investments in Cronos and JUUL. As a reminder, the program includes savings from workforce reductions, third-party spending reductions, and closure of our Nu Mark operations.

With that we'll wrap up. And Howard and I will be happy to take your questions. While the calls are being compiled, I'll remind you that today's earnings release and our non-GAAP reconciliations are available in Altria.com. We've also posted our usual quarterly metrics, which include pricing, inventory and other housekeeping items.

With that, I'll open up the question-and-answer period. Operator, do we have any questions?

Question-and-Answer Session

Operator

Thank you. [Operator Instructions] We will take questions from the investment community first. our first question comes from the line of Chris Growe with Stifel.

Chris Growe

Hi, good morning.

Howard Willard

Hi Chris.

Chris Growe

Hi. I just wanted to lead out with a question in relation to your new medium-term, if I can call that EPS growth outlook, and I just wanted to better understand the basis for that change and you gave some color on the call. I guess, I would just ask is your -- I assume does your 4% to 6% volume growth outlook remains the same? And then embedded within that EPS growth outlook, how much of this is about -- obviously it's become a pretty fast-changing environment in this category, a lot of new products, obviously the IQOS and on! How much of it's about investment as opposed to some varying outlook in volume or that kind of thing for your business?

Howard Willard

Sure. I think first of all, our current mid-term cigarette volume decline estimate remains the same at 4% to 6%. Although certainly, as we indicated before, if the environment changes our view of that we would update you on that in the future. I think there are a variety of reasons why we replaced our 7% to 9% EPS growth with a 5% to 8% EPS growth through 2022.

Two, that I think are worthy of calling out. First of all, I think it gives us flexibility to increase our investments over the next couple of years in expanding both IQOS and on! at a time that I think that adult tobacco consumers would be particularly interested in those products, and we could build a strong business that would contribute to EPS growth over the long term.

The second thing is that while we don't yet have the final FDA guidance on e-vapor there is certainly the possibility that the e-vapor category could see its growth rate significantly slowed down or even see the category contract in relation to that FDA guidance. And the 5% to 8% EPS growth gives us the opportunity, if necessary, to push out some of the contributions from JUUL that we expected on our equity income line beyond next year.

Chris Growe

Okay, that's helpful. Thank you for that. And then, just another question in relation to IQOS, obviously you're adding Richmond, should we expect you to continue to just methodically add new locations, or is there an idea that you have to establish some learnings in these markets and then think about expanding this to other markets. I'm just trying to get an idea of the phasing, I know we can't get exactly, but the phasing how to think about incremental locations for IQOS?

Billy Gifford

Yes, it's a great question, Chris. The way we're thinking about IQOS as we certainly want to get the learnings of the U.S. consumer and their interaction, what really resonates with them as far as the learning the product and engaging with the product. We are excited about the launch that we had in Atlanta.

We're excited about being able to expand it to Richmond. I think the pace will really matter from a standpoint of, we want to go as quick as we can. But we want to be disciplined about it and we want to garner those learning so that we're efficient when we have future expansions.

Chris Growe

Okay, thanks so much for your time.

Howard Willard

Thank you.

Operator

Your next question comes from the line of Owen Bennett with Jefferies.

Owen Bennett

Good morning, guys.

Howard Willard

Good morning.

Owen Bennett

And yes, just a couple of questions please. First one, I was just wondering on your volume guidance industry wise for this year, it seems as we've seen a slowdown in industry vapor volumes recently, I was just wondering, why you've not upgraded the industry guidance? And then secondly, you mentioned that you've revised some of your international growth expectations around JUUL. I was just hoping you could give a few more specifics on what has changed in terms of your international outlook for JUUL exactly? Thank you.

Howard Willard

Sure, I'll take the first question and then I'll ask Billy to comment on the second one. Our expectations for cigarette industry volume declines this year are between 5% and 6% and we're right at the midpoint of that nine months through the year. So we remain confident that the decline rate will fall within that range. I think as you pointed out the year-over-year growth rate of the e-vapor category in the third quarter slowed down a bit from the second quarter, but we don't think any impact that might have on the cigarette category is going to move us outside that range. Billy you wanted to comment on JUUL.

Billy Gifford

Sure. When you think about the international markets, I think you've seen that several countries take action on e-vapor based on what they were seeing take place in the U.S. and so we make sure we -- we make sure we factored that into the scenarios, as we were looking at the revising the assumptions.

Owen Bennett

Okay, thanks very much guys. I appreciate it.

Howard Willard

Thank you.

Operator

Next question is from the line of Pam Kaufman with Morgan Stanley.

Pam Kaufman

Hi, good morning.

Howard Willard

Good morning Pam.

Pam Kaufman

Earlier this year you laid out key assumptions around JUUL's five-year outlook. Can you elaborate on how these assumptions have changed? I mean, previously, we believe that the return would exceed your 8% lock within five years. So how long do you think it will now take for JUUL to exceed this hurdle? And when do you think that JUUL can approach U.S. and international cigarette margins, and is this still a realistic target?

Billy Gifford

Yes, I think, Pamela, it's too early to update those. I think we tried to revise the assumptions. Remember, we ran a range of scenarios because we're still waiting on the FDA to issue final guidance. You'll recall that JUUL took unilateral action in the marketplace, but all of these products are still available.

So we're waiting to see what that final guidance is and see what -- how the consumer is going to be playing and what restrictions around product availability there will be, and then we can refresh those. So what we did is we ran a range of scenarios, so that we would make sure that we had accounted for the various assumptions and changes in those assumptions that could take place across a range of outcomes.

Howard Willard

And Pam, the primary drivers of the change in value of our investment in JUUL, as we laid out in the release was that we reduced our expectations for overall e-vapor category volume growth over the next several years. And obviously that impacted JUUL's volume. And we also expect that that JUUL response to slowing volume in the e-vapor category and the likely impact of the FDA final guidance, it could push out a year or two their ability to achieve the kind of margins that we talked about here in the U.S.. I think probably the most important next set of information we're looking for is to see the FDA's final guidance and how consumers react to that.

Pam Kaufman

And how do you feel about having to so materially reduce your estimate of such a large investment so quickly after being completed, and how will this experience impact your future approach to M&A versus internal investment?

Howard Willard

Sure of course, we're not pleased to have to take an impairment charge on JUUL investment. And certainly while we had a range of scenarios when we made our investment in JUUL, we did not anticipate this dramatic a change in the e-vapor category. Certainly the lung injury I think was something we had not predicted, and in the pretty dramatic potential regulatory change that may occur next year, I think it was on the extreme end of what we might have expected.

However, all that said, in the third quarter JUUL had a [48%] [ph] share of the e-vapor category in the U.S., the category, at least through the nine months to this year was growing quite dramatically with JUUL as the primary driver of that growth. And so we continue to believe, first of all, that bold action to address usage of e-vapor products is appropriate. And we encouraged bold action by FDA. But we also believe that JUUL is set up in the longer term to continue to be the winner in e-vapor.

And because of that we continue to be supportive of JUUL's business and look forward to them working through the changes in the e-vapor category and being a contributor to our equity income line going forward.

Pam Kaufman

Thanks.

Operator

Your next question is from the line of Nik Modi with RBC.

Nik Modi

Yes, thanks. Good morning, everyone.

Howard Willard

Good morning Nik.

Nik Modi

Two questions from -- good morning, Howard. Two questions. First, when you talk about the 2020 to 2022 earnings CAGR, can you help us understand the kind of the puts and takes in terms of how consistent that number will be like? Should we expect some really heavy investment period in the upfront as you kind of invest behind on! and IQOS national expansion. So any clarity around that. I'm not asking for 2020 guidance. I'm just trying to get a better sense of kind of how you think about it philosophically.

And then the second question is really helping to understand the Marlboro franchise and my understanding is that the non-promoted portion of Marlboro is actually doing very well, helped by that rewards program. So I was just hoping you can give us some context around how the Marlboro trademark is performing.

Howard Willard

Sure. Let me first answer the question around the expected consistency we would have for our annual EPS growth between 2020 and 2022. When we replaced our long-term objective with this three year objective, you'll notice we widened the range of EPS growth a bit and I think that was by design. When we established our 7% to 9% EPS growth objective it was at a time when volumes across the various tobacco categories in the U.S. were quite predictable. And there wasn't as much movement between categories and it was also at a time when our SABMiller investment didn't have near the volatility that we have with the ABI Investment.

And so I think we really felt better having a 3% range for that mid-term EPS growth objective. And I would also say that I think many of you that have invested for a long time know that we had a 7% to 9% growth aspiration, but we tended to deliver about 8% each year. I think that we purposely, I think, want the flexibility to make higher or lower investments over each of the three years based on market conditions in the U.S. market. So you might see a little bit more movement within that range and we were really looking to create that level of flexibility. I'll turn it over to Billy for the Marlboro question.

Billy Gifford

Yes. Nick. We appreciate you recognizing the strength of the Marlboro brand. First, I would applaud both the Marlboro team and data analytics team. The Marlboro team put together a great Marlboro rewards program really based on analyzing the data we have on our consumer to drive higher interaction of our Marlboro consumer with at the brand itself. And what that has allowed is with the data that we're capturing in the data analytics to be much more efficient around the use of -- and targeted with the use of promotions in the marketplace.

Nik Modi

Thank you.

Operator

Your next question is from Gaurav Jain with Barclays.

Gaurav Jain

Hi, good morning. Thank you. Yes, I had a couple of questions, one was on the recent discussions with Philip Morris and why they were called off. And in particular, the value of your core tobacco business was around eight times PE, which would suggest that the business is on decline. So, can you help us triangulate the multiple that you put on your own tobacco business and the growth outlook that you are now offering, which is still quite a healthy growth outlook? Thank you.

Howard Willard

Thank you. I'll comment first on our breaking off negotiations for a merger with PMI. I think as we communicated at the time we thought that merger between PMI and Altria had the potential to generate significant revenue and cost synergies under the right terms. We did negotiate to try and come to terms and ultimately we were unsuccessful. And so as we communicated recently we're now very focused on our stand-alone business prospects and continue to have a partnership with PMI that we're very excited about to commercialize IQOS in the U.S.

With regard to the multiple that we ascribe to our core tobacco business, certainly people on the call are aware that the multiple that the stock prices ascribe to our overall business has come down quite dramatically over the last three years, I think partially driven by concern about the regulatory pressures here in the U.S.

We continue to believe that that our stock is undervalued. And when we look at -- when we look at the 5% to 8% mid-term EPS growth guidance, the ability to build a strong platform of noncombustible tobacco products to continue to generate income over the long term and our strong core combustible and smokeless tobacco business. We think that the stock price has significant upside. Thank you.

Gaurav Jain

Sure. And a follow-up on that. So you have valuable stakes, and particularly in ABI, which are probably not accurately reflected in the current stock price. So this discrepancy were to persist. Would you think of taking any actions to unlock the value?

Billy Gifford

Yes, thank you for the question. I think you recall, as part of that transaction, we had a lock-up. That was a five year lock up that would expire in 2021. And then after that you can expect us to go through the same analysis we did with SAB, which is to look at that capital that's allocated toward the investment, make sure it's the right choice to keep it locked up in that investment and then make decisions, the appropriate decisions at the time.

Our position on the ABI investment is that it was a great investment. It put two powerhouse breweries together. It's the first really global platform for beer in the world and we feel good about the investment, but you can expect us to go through the analysis when the lock-up expires.

Howard Willard

One thing I might add here -- one thing I might add to that is back when we were debating what to do with the SABMiller stake, one of the concerns we had was the given its low tax basis any sale at that time would have resulted in quite a significant tax bill. And as you may recall with the federal tax reform here in the U.S., I think that while we still continue to have a relatively low basis on that asset, I think that we're facing a much lower tax rate, if we ever did decide to sell that in the future.

Gaurav Jain

That's very helpful. Thanks a lot.

Operator

Your next question is from the line of Vivien Azer with Cowen.

Vivien Azer

Hi, good morning.

Howard Willard

Hi, Vivien.

Vivien Azer

So Howard, I was hoping that we could just revisit the cigarette volume outlook for the U.S. please. While I appreciate that year-to-date you're at the midpoint of your 2019 guidance, the year-to-date trends are skewing toward the more unfavorable end of your longer-term guidance. And when I look at slide 13, very helpful in your presentation. And look at the fact that the cross category movement impact has increased 5x in less than 12 months. Holding of 4% to 6% outlook suggests that not only does that not get worse, in theory, it gets a little bit better. Is that how you guys are thinking about it? Any color there would be very helpful? Thank you.

Billy Gifford

Yes, thank you for the question, Vivien. I think when you look at that, that's certainly a 12-month moving and you'll recall that when you look at the e-vapor category going from second to third, it's virtually flat. And then we have the proposed regulation that's going to hit the marketplace. So at this point, we still feel very comfortable with the 4% to 6% on that mid-term volume. And so we will certainly monitor it and keep track of it as we move forward. But this period that we're showing you on slide 13 is the period that you saw the huge growth in the e-vapor category.

Howard Willard

And Vivien, this is Howard. What I might add is that certainly we don't have the final FDA guidance and its impact on e-vapor, but I think that there is a reasonable possibility that that's going to cause a slowdown in the e-vapor category growth. And of course that will cause some of the adult cigarette smokers that otherwise might have gone to e-vapor to evaluate that decision probably differently.

We'd like to have quite robust offerings on IQOS and on! available for them. But certainly that could have an impact on the historical decline rate for cigarettes. And then I would also point out that we've had quite rapid growth in the e-vapor category starting in the third and fourth quarter of last year and through the first three quarters of this year. But that growth rate, on a year-over-year basis, had been slowing down. And I think given that there are not new e-vapor products coming into the marketplace, at least until FDA authorizations take place. We would expect that there would be a natural slowing down in the growth of e-vapor here over the next year or two. And certainly that's what happened when IQOS was introduced in Japan, and so I think you also have to factor that into the calculation.

Vivien Azer

Okay, that's helpful. Certainly the slowdown is apparent in the scanner data as well. May I -- second question is on IQOS. So have you guys established a target on when you might achieve profitability on that platform in the U.S. And the second question to that. In the near term it seems like the promotional spending is aggressive, perhaps appropriately. So, given the bundle is priced at $80, it would imply that the device itself is going for about $25. Are you guys funding that promotional investment independently? Thanks.

Speaker

Sure. So we have not communicated a timeline for when IQOS would be profit positive. And we really feel like at this point, it's a bit premature. I think we are going to learn a lot about the most efficient way to scale IQOS in markets across the country. And I think based on that learning we'll have a much better understanding of what the cost structure would be going forward.

And I would say that you are right that our level of spending in the Atlanta market is probably higher than it will be on a market basis going forward, but Atlanta is really designed for us to try a broad spectrum of tools to create awareness trial and purchase of IQOS. And then based on that learnings, we will design a more efficient less costly plan to expand it around the country. And I think that that means that it may take us few more months to start expanding it, but we think that the benefit will get an efficiency and ability to scale winning platform is well worth it.

Vivien Azer

Terrific. Thanks very much.

Operator

Your next question is from the line of Michael Lavery with Piper Jaffray.

Michael Lavery

Good morning.

Howard Willard

Hi Michael.

Michael Lavery

Can you just talk about your approach to how you think about the IQOS rollout? And obviously, now you've already announced a second city. But as you look ahead, how much did your learnings from Atlanta and now Richmond determine how you might adjust or update the tactics and the go-to-market approach, or does it all subscribe your thinking on the magnitude and timing of the push that you might like?

Howard Willard

Yes, I think the primary driver of our ultimate national rollout strategy and the tactics we use to cost effectively drive consumer trial awareness and purchase. The primary driver of that is going to be the results in Atlanta and now Richmond. We had enough time to revisit revised and improve the Atlanta promotional plan several times. So we feel quite good about it.

But we have no doubt that we're going to learn things in Atlanta that allow us to be much more efficient as we roll out nationally. But I would say also that given the likelihood that there is going to be some disruption in the e-vapor market we also wanted to step up the speed with which we would expand IQOS. So while we are going to learn how to best expand it nationally, we have also set aside the resources now with our 5% to 8% EPS guidance to ramp that up much more quickly on a national basis once we do learn from Atlanta.

Michael Lavery

That's helpful. And on the outlook for next year just at a very high level in broad strokes, is there some uncertainty around the speed of traction, just given that it's so earlier on the IQOS launch such that you might have several scenarios potentially in mind for how next year unfolds and could the guidance for next year possibly even be wider than your growth objective?

Howard Willard

Yes, I won't get ahead of ourselves on guidance for next year. Certainly, as I said, I think that our learnings in the Atlanta test market are going to inform the plan we have for expanding IQOS and we'll have similar learnings on which will also inform it. Although I have to tell you that that we think that the new mid-term EPS growth guidance range gives us a lot of flexibility for a variety of scenarios. But ultimately I'll leave that for January.

I do want to follow-up. I think I failed to answer one part of your question earlier, Michael, which is you are right that in Atlanta in order to encourage adult cigarette smokers to purchase the device, we are offering quite a competitive price on a bundle that includes the device and heat sticks. And that is a promotion that we're incurring the cost for. But when you look at somebody who purchases that bundle and then converts to IQOS over the course of the year, it's a relatively small investment for the significant income stream that creates.

Michael Lavery

That's helpful. Thank you. And just one last one on obviously your smokeless segment operating margins are extremely high. How does this compare and how do you see it evolving over time, if it's different already today.

Howard Willard

Yes, one of the real benefits of our participation in the nicotine pouch category with on! is that we think after a period of initial investment to build the business we think that the margins on! are likely to be similar to the kind of margins we have in the smokeless tobacco business. It shares many of the same manufacturing characteristics that we've developed on smokeless tobacco, so that could be a very high profit business going forward.

Michael Lavery

Okay. Thank you very much.

Howard Willard

Thank you.

Operator

Your next question is from the line of Robert Rampton with UBS.

Robert Rampton

Good morning. Probably just three questions from me. Sorry to just labor a point, but just to be clear, when you say a 5% to 8% CAGR over three years, do you mean in any given year 5% is the floor?

Howard Willard

So our intention with that is that the base year would be 2019. And the CAGR between 2019 and 2022 would be between 5% and 8%.

Robert Rampton

Okay, that's very clear. Thank you. And then, sorry, my second question. Could you give me more color on how that underlying 5.5% evolved over the course of the quarter. Obviously the press around FDA in terms was more toward the tail-end. But we are interested to hear that how that evolved.

Howard Willard

Sure. I won't get into the details within the quarter, but I think, as you looked at that trend, obviously we had a 5.5% cigarette category decline rate, down from 6% in the second quarter. And certainly when you look at the sequential growth of e-vapor instead of picking up sequentially in the third quarter, it was largely flat from the second quarter. So I think, we'll see what happens in the fourth quarter, but I think the fourth quarter impact on e-vapor which might have some impact on cigarettes is likely to be based on what happens in the regulatory environment.

Robert Rampton

Very clear thank you. I'm sorry, my final question is so certain states have taken action on flavors earlier than [indiscernible] by the FDA. Any early indications about what that's doing to cigarette volumes and so on and so forth?

Howard Willard

I think it's fairly early days on some of those state actions and some of them I think had been held up with court challenges. So I think we'll have a much better read on that in the fourth quarter.

Robert Rampton

All right. Thank you very much.

Speaker

Thank you.

Operator

Your next question comes from the line of Adam Spielman with Citi.

Adam Spielman

Hello. Thank you.

Howard Willard

Hi Adam.

Adam Spielman

Hi. So you said that you've already revised some of your marketing strategies in Atlanta for IQOS. I think, clearly you've already got some learnings there. And I was just wondering if you could, at a very high level, share what you have learned so far and what those changes have been in your marketing strategy? Thank you.

Howard Willard

Sure. When I referenced the fact that we had changed and improved our IQOS marketing strategy, I was really referring to the fact that we were ready to launch more than a year ago. And because the authorization of the product took longer than we had expected, our marketing team had been meeting with PMI and learning from their experiences overseas and making adjustments to improve the marketing plan. I would say that we really haven't made significant changes versus our original launch plan since the product was placed in the market.

Adam Spielman

Okay, thank you. Thank you. I'm sorry to have misunderstood, but I guess following from that when we get to the 4Q results, will you be able to give us I guess what PM has always done, which is some indication of market share for IQOS in the relevant geography. And any discussion about what you're learning. I'm quite intrigued about whether I'd like you to be able to say that you will update us on frankly how it's going in Atlanta?

Howard Willard

Certainly we're going to provide what we think is appropriate to fill you in on how we think it's improving and where we're going to go from there. We'll decide what those appropriate metrics are as we move along, but certainly we're going to give you some insight into how it's performing.

Billy Gifford

I think probably our biggest focus for the next three months or so is to measure our ability to drive awareness of the product in Atlanta to drive trial and then ultimately to deliver purchase and conversion. I think at this stage we're less focused on market share and we're more focused on some of those earlier precursors to generating market share in the market.

Adam Spielman

In a year’s time what sort of market share would you say will represents a success for IQOS in Atlanta? Talking about December 2020, what would you hope to achieve by that?

Howard Willard

Yes, I'm going to hesitate to comment on that. I think that's really what we're interested in learning from the Atlanta market. What I would say is that certainly the biggest success that IQOS has had is in Japan, and I don't expect that we will achieve those levels, although that's what we're going to try and learn in Atlanta. But I do believe that when you compare to some of the PMI experiences in Western Europe, I do think we have an advantage in that we have fairly large convenience stores with modern retail and it really provides a platform to billboard the product. And we also have quite good database resources to reach out to adult tobacco consumers. So, I would say we are optimistic about the progress we can make in the U.S. versus some of PMI's markets but I'll hesitate to make a speculation.

Adam Spielman

And one final question from me and changing the subject completely, coming back to your comments about JUUL overseas, outside the U.S., you said one of the reasons you took down your assumptions overseas because -- is because some markets, let's say, India have just said we're not going to allow e-vapor. But I was wondering also if there was any evidence that in the markets where JUUL is being available, let's say Western Europe, Korea. The sales performance had been as good as you'd hoped or worse than you had sort of originally hoped, or better than you had hoped. And whether that performance in the markets where it's actually been launched affected your assumptions about -- or scenarios for international rollout of JUUL.

Howard Willard

Sure. The primary driver of the adjustment we made in the JUUL international business valuation was more driven by the overall e-vapor category situation in various countries. It was not related to individual country performance based on JUUL's early launch results.

And I have to say that it's now in many, many countries, but I would say it's still quite early to assess which countries it's going to have a real success in. So it was more driven by the overall e-vapor category environment than it was specific to JUUL's performance.

Adam Spielman

Thank you very much. Thank you for my answering all my questions.

Howard Willard

Thank you.

Operator

Your next question comes from Steve Powers with Deutsche Bank.

Steve Powers

Hey, good morning. Thanks. Howard, I just wanted to take a moment and maybe revisit your opening comments surrounding the notion that the industry used to be predictable but now has become more dynamic and complex. I think we all realize that there has been significant volatility, especially in the last couple of years and that similar rate of volatility is likely to continue for some time, but is long term predictability no longer Altria's base case to the degree it might have ones been? And then how is that changing your approach to the market and the company's strategic considerations going forward? Maybe you could just elaborate a bit on that, that'll be helpful.

Howard Willard

Sure. If you go back 10 years and think about the first five-year period of the last 10 years, we had very predictable and quite high EPS growth. And the primary driver of that was with strong operating companies income growth from our MST business and from our combustible cigarette business. And the volume decline rates in cigarettes was quite consistent and while we were making some investments in other categories, they really weren't having much of an impact on the decline rate of cigarettes and that generated quite a predictable and quite a satisfying level of EPS growth.

I think that we believe that at least over the next three or four years, you could have some variability in the decline rate of the cigarette category as some of these non-combustible tobacco-product categories are launched, are invested in and start to build a larger base business. And it could take over the next three years it could take some time for the volume switching between categories to become more predictable.

And certainly, we saw an accelerated decline in the cigarette category this year. But I would point out that it was the step up in that decline was almost wholly driven by more rapid e-vapor category growth. So the good news for the long-term success of the cigarette industry in the U.S. is consumers in the U.S. are still interested in satisfying nicotine products, they are just finding a variety of different ways to satisfy -- their desire for satisfying nicotine products.

I do believe that we will enter probably a more predictable phase here, maybe in the later part of the next 10 years because I do think eventually we're going to get to the point where you've got larger and pretty well marketed on non-combustible tobacco product platforms that would include heated tobacco. I think e-vapor will get through this short-term disruption and return to a more predictable path. And then of course, oral tobacco including oral tobacco drive nicotine pouches are likely to also end up with a larger base business.

So we think in the long term, the predictability and the profit growth that was provided largely by combustible cigarettes, that can be provided in the future, but it's likely to be from a portfolio products that provide nicotine satisfaction and we believe we've built a very compelling set of brands in each of those key categories that should generate nice EPS growth over the longer term.

Steve Powers

Okay, great, thank you for that. Maybe sort of related and maybe to build on some of the earlier questions as e-vapor has come under increasing public scrutiny these past few months, I think everyone is looking for a noticeable change in trend in adjacent categories, and you've spoken a bit about that regarding smokeable demand, but do you anticipate any potential impact on smokeless as well as we think about what may or may not transpire over the next couple of quarters?

Howard Willard

Sure. I think if changes in the e-vapor growth rate are going to have an impact on other categories. I think we're more likely to see it probably in the first quarter or second quarter of next year. And I think you are right to point out that there is that growth rate changes or if the category goes through a decline next year, I would expect to see it potentially reflected in change in growth rates in combustible cigarettes, also moist smokeless tobacco.

And you might also see a more favorable volume trend for IQOS and tobacco drive nicotine pouches, are driven by two things. If there is some e-vapor consumers that find their product of choice is no longer available, they may look to other product alternatives, and then a big driver of the growth of e-vapor this year was cigarette -- adult cigarette smokers, dual using and then moving to that category. If they're not moving to vapor anymore, they're likely stay in cigarettes or move somewhere else.

Steve Powers

Thanks a lot. I appreciate it.

Howard Willard

All right, thank you.

Operator

Your next question is from the line of Petros Voulgaris with Goldman Sachs.

Petros Voulgaris

Good morning, everyone.

Howard Willard

Good morning.

Petros Voulgaris

Two questions from me. Can you give some color into how you think about the continuum of risk with respect to how you weigh the differences and the probability of removal of menthol in e-cigs versus the probability of removal of menthol in cigarettes? And I guess as a follow up, could you shed a little light into what cohorts in terms of demographics might be exhibiting a slower rate of decline with respect to cigarette shipment volumes?

Howard Willard

Sure. Let me try and address your first question, and I'll have Billy comment on your second one. I think that our expectation is that the FDA is going to provide further information on their final guidance in the e-vapor category. And I think our expectation is that that is going to impact flavored products in the e-vapor category.

We don't have any indication that that FDA is going to communicate in the near term here any further perspective on removing menthol cigarettes from the market and that would require a completely different process. It's really not under way at this point in order to support that. I really think our expectation is that in the next couple of months we're going to hear really about flavors in e-vapor.

Billy Gifford

Could I ask you to just clarify the second part of the question? I'm not sure, I completely understood it.

Petros Voulgaris

Yes, I mean I know you look at the market at 21 and over. I don't know if there is like the age group from 20 to 30 is exhibiting a different rate of decline with respect to some of the older cohorts, or how you cut it. I was wondering if you could just shed a little light into the demographics and how like there is changing dynamics within the -- and how that's impacting cigarette shipment volumes?

Billy Gifford

Yes, I don't think there is any significant skew in age cohorts for cigarette shipment volume. You'll recall, as we talk about the e-vapor category, it has certainly been more attractive to that younger age cohort, call it 21 to 39. So they are more interested in the alternative product categories to a little bit higher extent than the older adult smoker above that 39 age group. But as far as overall decline, absent and moving to other categories, we don't see any significant skew by age cohort.

Operator

Ladies and gentleman, we will now invite the media to participate in questions. [Operator Instructions] Your first question is from the line of Angelica LaVito with CNBC.

Angelica LaVito

Good morning, thanks for taking the question. I just wanted to ask have you considered the possibility that the FDA does not authorize JUUL's PMTA?

Howard Willard

Sure. I think that with the filing date for the PMTAs moved from 2022 to May of next year, I think that creates a more challenging situation on both filing and -- filing approvable applications for all the e-vapor companies. However, I believe that JUUL is highly likely to end up filing a successful application and ultimately having their products authorized because they have a significant amount of resources applied against that task.

And I think that one of the benefits they have going for them is that within the e-vapor category the JUUL product, I think, is distinguished itself compared to other e-vapor products as having quite a significant success at convincing adult cigarette smokers to convert ultimately to exclusive use of e-vapor. And I think that's one of the things that the FDA is going to consider in debating whether or not to approve an application.

Operator

And your final question is from the line of Jennifer Maloney with Wall Street Journal.

Jennifer Maloney

Good morning. I wonder if you could share your understanding of JUUL consumers' willingness to switch flavors. The company did get to observe on how consumers reacted when they pulled many of their flavors out of retail stores last year, a lot of people switched from Mango to mint. So, based on those observations and others, what is your best projection of what may happen if their flavors are limited to tobacco only.

Howard Willard

Jennifer, thanks for the question. I have to tell you that I'm probably the wrong person to answer that question. I'm aware of the same trends that you referenced when some of their flavors, other than tobacco, menthol and mint were restricted in the marketplace. But given that we don't operate the JUUL business, I don't really have access to that kind of research. That's probably best directed toward JUUL management.

Operator

Thank you. At this time, I would like to turn the call back to management for closing comments.

Howard Willard

Thank you. To close, we believe we are the best positioned company to successfully navigate through the current tobacco environment. We have excellent profit growth and cash generation from our core tobacco businesses and we have built a diversified business platform of noncombustible products that can satisfy adult tobacco consumers and provide future profitability under many different future marketplace scenarios. Thanks again for joining us and please contact our Investor Relations team, if you have further questions.

Operator

Thank you for participating in today's conference call. You may now disconnect your lines.