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Tobacco Bondholders Shrug Off FDA News While Cigarette Stocks Are Hit Hard.

- **Government seeks to cut nicotine to non-addictive levels**
- **Shares in Altria, BAT and Imperial Brands hit hardest**

Tobacco shares tumbled after the Food and Drug Administration said it will seek tougher regulations on nicotine levels to curb addiction, threatening to further winnow the customer base for an American industry that's been shrinking for decades.

Marlboro maker Altria Group Inc. sank the most since 2008, Imperial Brands closed in London at the lowest since November, and U.S.-listed shares of British American Tobacco Group headed for the worst day in three years. Together, the three purveyors of tobacco products shed almost $30 billion in market cap after the FDA announcement.

"Concern among investors is clear and not misplaced if the strictest reading of this announcement proves accurate," Cowen analyst Vivien Azer wrote in a note to clients.

She also cautioned that there remain "unknowns," joining a handful of other investment banks advising clients that the share slump is likely overdone.

The selling came as the proposal caught investors in the $130 billion American tobacco industry off guard. If enacted, the rules would represent one of the most sweeping federal efforts to reduce smoking since Congress required cigarette packages to carry health warnings in 1965.

Judging by the reaction in the corporate and municipal bond markets, the chances that cash flows will be interrupted seem relatively thin — at least for now.

There were only a handful of trades on Friday in the $86.5 billion market for debt backed by payments from tobacco companies, in junk-rated issues. The largest, a $2.5 million block of Buckeye Ohio Tobacco Settlement bonds with a 5.875 percent coupon and maturing in 2047, saw its yield climb four basis points to 6.11 percent.

Debt backed by the leading cigarette makers showed little reaction, with some of Altria's bonds, which are rated A-, posting small gains at midday.

"A lot of these guys are investment grade," said Ken Shea, a Bloomberg Intelligence analyst who follows tobacco companies. "I doubt immediate cash flows will be impacted by today's news."

Research departments at leading banks suggested the stock selloff presented a chance to buy. Jefferies analyst Owen Bennett says the proposal is a "positive" for future growth as it could lead to more demand for vapor cigarettes and potentially induce cities to lower tax rates from current levels.

Sales of cigarettes have already been in decline, even as taxes on the products rise. The industry's cigarette sales volume dropped an estimated 4.5 percent last quarter, Altria reported earlier this week. The average state excise tax was $1.74 per pack last quarter, compared with 19 cents for the same time last year, according to Altria.

“We do not believe these moves are justified,” Citigroup analyst Adam Spielman said in a note to clients Friday. “The FDA’s track record is of moving extremely slowly. So far these are proposals for discussion only. There is no time line for implementation. Equally we find it hard to believe the Trump administration or the current Congress would be supportive, given their public record on regulation.”

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