



Target Corporation (TGT)

Updated May 23rd, 2019 by Josh Arnold

Key Metrics

Current Price:	\$78	5 Year CAGR Estimate:	12.0%	Volatility Percentile:	78.7%
Fair Value Price:	\$89	5 Year Growth Estimate:	6.0%	Momentum Percentile:	38.6%
% Fair Value:	88%	5 Year Valuation Multiple Estimate:	2.7%	Growth Percentile:	52.6%
Dividend Yield:	3.3%	5 Year Price Target	\$119	Valuation Percentile:	75.4%
Dividend Risk Score:	A	Retirement Suitability Score:	A	Total Return Percentile:	74.3%

Overview & Current Events

Target was founded in 1902 and after a failed bid to expand into Canada, has operations solely in the U.S. market. Its business consists of about 1,850 big box stores, which offer general merchandise and food. Target has a market capitalization of \$40 billion and should produce about \$78 billion in total revenue this year.

Target has been able to withstand the ongoing price war in the retail sector. The acquisition of Whole Foods by Amazon caused shockwaves for traditional retailers, but the dire forecasts on pricing and market share have not materialized. Moreover, Target has moved in the right direction to address its challenges. It has invested heavily in the remodeling of its stores and has expanded the same-day delivery option to about 65% of U.S. households.

Target reported Q1 earnings on 5/22/19 and results were very strong, sending the stock up 8% on the day as investors cheered the report. Total revenue was up 5% year-over-year, coming in at \$17.6 billion in Q1. The gain consisted of comparable sales growth of 4.8% with the balance from stores that aren't yet part of the comparable base. Digital sales also soared 42%, adding 2.1% to the comparable sales growth number, implying a +2.7% gain for the retail stores. The top line gain produced in Q1 was excellent and well ahead of expectations as it appears Target is picking up significant revenue momentum once again.

Margins were strong as well as operating income rose 9% on a dollar basis to \$1.135 billion in Q1, up from \$1.041 billion in last year's Q1. Target's operating margin rate was 6.4%, a gain over the 6.2% in the comparable period last year. Gross margins declined 20bps to 29.6% as higher digital fulfillment and supply chain costs weighed, but were partially offset by the benefit of the company's merchandising strategies. SG&A costs were 20.8% in Q1, down 30bps and helping to offset the loss of gross margin, reflecting the savings in technology and lower market expenses. Wage growth continues to be a problem, but Target has implemented offsetting cost controls.

Target continues to expect low to mid-single digit gains in comparable sales for this year and an earnings-per-share range of \$5.75 to \$6.05. As a result, we are reiterating our guidance of \$5.90 for this year.

Separately, Target returned \$608 million to shareholders in Q1, including dividends of \$330 million and share repurchases of \$278 million in repurchases. The company has \$1 billion left on its current buyback authorization.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$3.30	\$3.88	\$4.28	\$4.38	\$3.21	\$4.27	\$4.69	\$5.01	\$4.65	\$5.39	\$5.90	\$7.90
DPS	\$0.66	\$0.84	\$1.10	\$1.32	\$1.58	\$1.90	\$2.16	\$2.32	\$2.44	\$2.52	\$2.56	\$3.30
Shares	754.8	729.4	679.1	656.7	635.1	640.1	632.9	582.5	545.9	524.3	510.0	420.0

Target has grown its earnings-per-share at an average annual rate of 6.5% during the last decade. Due to fierce competition and the failed attempt to expand to Canada, Target's earnings-per-share remained almost flat from 2012 to 2017. However, turnaround efforts have borne fruit and as a result, Target has significantly improved its performance in recent quarters. The company has reduced its share count by about 4% per year in the last five years and is likely to maintain a similar buyback rate ahead. Overall, it is reasonable to expect 6% annualized growth beyond this year. We see continued comparable sales growth as driving results, along with a small measure of margin expansion.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	12.8	13.9	11.9	13.7	20.7	14.7	16.6	14.6	14.2	14.2	13.1	15.0
Avg. Yld.	1.6%	1.6%	2.2%	2.2%	2.4%	3.0%	2.8%	3.2%	4.0%	3.3%	3.3%	2.8%

After the sizable post-earnings gain, shares are near where they were at the time of our last update. Thus, the valuation is still quite attractive in our view. Target is trading at a price-to-earnings ratio of 13.1, which is lower than its 10-year average of 14.7, and our fair value estimate of 15 times earnings. If the stock reverts to fair value over the next five years, it will enjoy a 2.7% annualized gain.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	20.0%	21.6%	25.7%	30.1%	49.2%	44.5%	46.1%	46.3%	52.5%	46.8%	43.4%	41.8%

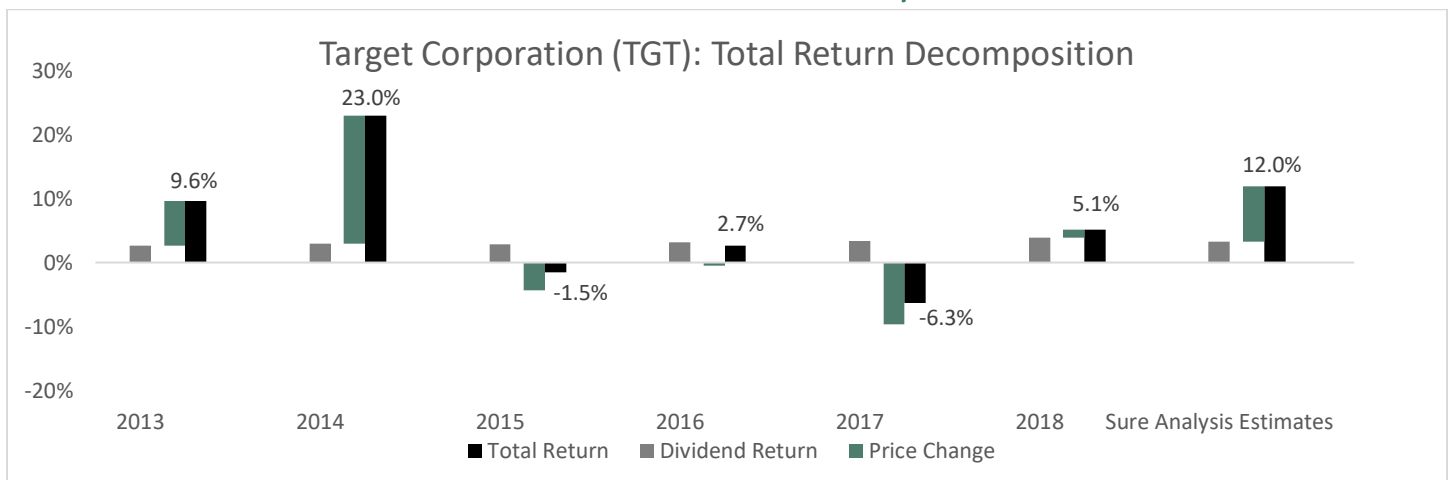
Target is a Dividend Aristocrat that has grown its dividend for 49 consecutive years. However, as it has grown its dividend much more quickly than its earnings, the company has markedly increased its payout ratio, from 20% in 2009 to 43% this year. Moreover, the company is heavily investing in its business in order to navigate through the changing landscape in the retail sector. Therefore, Target is likely to raise its dividend at a slower pace in the upcoming years.

Target's competitive advantage comes from its discounted prices on attractive merchandise in its guest-friendly stores. However, given the price war in the retail sector, Target's moat is declining. In addition, as consumers tend to curtail their consumption during recessions, the company is vulnerable in such periods. In 2008, its earnings-per-share fell 14%. Nevertheless, that performance was much better than that of most companies, which saw their earnings collapse during the Great Recession. Moreover, it took only one year for the earnings of Target to return to their pre-crisis level. Therefore, while Target is vulnerable to economic downturns, it is much more resilient than most stocks in such periods.

Final Thoughts & Recommendation

We see Target as undervalued and as possessing a reasonably strong growth outlook. In addition, the company's dividend history is outstanding as it should become a Dividend King next year. We see total annual returns at 12% in the coming years, consisting of 6% earnings growth, the 3.3% dividend yield, and a 2.7% tailwind from a rising valuation. Target offers a good mix of growth, value, and yield that we find attractive. Target earns a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	65357	67390	69865	73301	71279	72618	73785	69495	71879	75356
Gross Profit	19774	20805	21559	22266	21240	21340	21544	20350	20754	22057
Gross Margin	30.3%	30.9%	30.9%	30.4%	29.8%	29.4%	29.2%	29.3%	28.9%	29.3%
SG&A Exp.	13078	13469	14106	14643	14465	14676	14665	13356	14248	15723
D&A Exp.	2023	2084	2131	2044	1996	2129	2213	2298	2445	2474
Operating Profit	4673	5252	5322	5579	4779	4535	4910	4969	4312	4110
Op. Margin	7.1%	7.8%	7.6%	7.6%	6.7%	6.2%	6.7%	7.2%	6.0%	5.5%
Net Profit	2488	2920	2929	2999	1971	-1636	3363	2737	2934	2937
Net Margin	3.8%	4.3%	4.2%	4.1%	2.8%	-2.3%	4.6%	3.9%	4.1%	3.9%
Free Cash Flow	4152	3142	1066	2979	4634	2679	4520	3889	4390	2457
Income Tax	1384	1575	1527	1741	1427	1204	1602	1296	718	746

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	44533	43705	46630	48163	44553	41172	40262	37431	38999	41290
Cash & Equivalents	583	583	794	784	670	2210	4046	2512	2643	1556
Acc. Receivable	6966	6153	5927	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Inventories	7179	7596	7918	7903	8278	8282	8601	8309	8657	9497
Goodwill & Int.	N/A	N/A	242	224	331	298	277	259	782	N/A
Total Liabilities	29186	28218	30809	31605	28322	27175	27305	26478	27290	29993
Accounts Payable	6511	6625	6857	7056	7335	7759	7418	7252	8677	9761
Long-Term Debt	16814	15726	16483	17648	12572	12725	12760	12749	11587	11275
Total Equity	15347	15487	15821	16558	16231	13997	12957	10953	11709	11297
D/E Ratio	1.10	1.02	1.04	1.07	0.77	0.91	0.98	1.16	0.99	1.00

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	5.6%	6.6%	6.5%	6.3%	4.3%	-3.8%	8.3%	7.0%	7.7%	7.3%
Return on Equity	17.1%	18.9%	18.7%	18.5%	12.0%	-10.8%	25.0%	22.9%	25.9%	25.5%
ROIC	7.7%	9.2%	9.2%	9.0%	6.3%	-5.9%	12.8%	11.1%	12.5%	12.8%
Shares Out.	754.8	729.4	679.1	656.7	635.1	640.1	632.9	582.5	545.9	524.3
Revenue/Share	86.59	92.39	102.16	110.51	111.06	113.45	116.58	119.30	130.62	141.33
FCF/Share	5.50	4.31	1.56	4.49	7.22	4.19	7.14	6.68	7.98	4.61

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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