

# Target Corp.

CONSUMER DISCRETIONARY | NATHAN SCHOMBERG AND RYAN DAVID

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Ticker: TGT

Stock Exchange: NYSE

Sector: Consumer Discretionary

Current Price: \$123.98

Industry: Retailer

Valuation Date: 12/1/2019

## COMPANY OVERVIEW

Target Corporation was founded in 1902 in Minneapolis, Minnesota by George Draper Dayton. Originally known as Dayton Dry Goods Company, Target has seen a lot of changes over the past century but Dayton's core concepts of dependable merchandise, fair business practices and a generous spirit of giving have stayed instilled in the company. Target has over 1,800 stores across the United States and has even made international expansion as they have built stores in Canada and India. Target Corporation is the eighth-largest retailer in the United States and is a top S&P 500 company who sells a wide variety of items from household goods and food to electronics and décor. The average shopper found at Target is female between the ages of 18 and 44 with an average income of \$65,000.

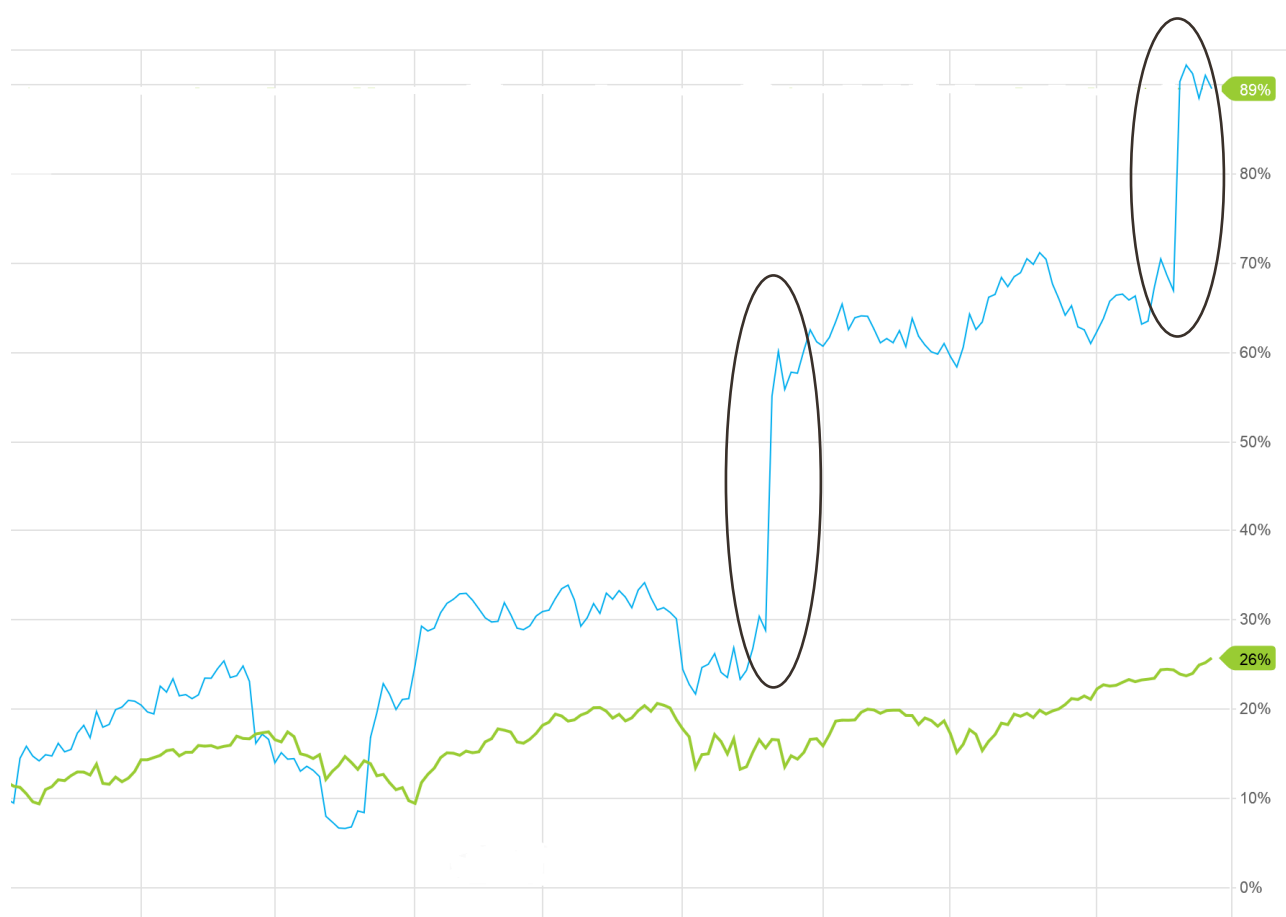
## MANAGEMENT

Target Corporation's management team is led by Chief Executive Officer Brian Cornell. Mr. Cornell joined the Target team in August of 2014 after over 30 years leadership positions at leading retail and global consumer product companies. Since taking over in 2014 the Target stock price has seen an increase of over 106% jumping from \$60 to \$124. Next in line is Chief Financial Officer Michael Fiddelke. Mr. Fiddelke is responsible for financial planning and analysis, financial operations, internal audit, accounting, investor relations, treasury, tax and risk. Throughout Michael Fiddelke's 15-year Target tenure he has moved throughout the company in leadership positions from merchandising to human resources and store operations. Mr. Fiddelke is a key member of the Target team and his experience across multiple fields gives him an advantage in his leadership position. The last member of the Target team we wanted to highlight is Janna Potts Chief Stores Officer. Ms. Potts is responsible for leading more than 300,000 team members and operating more than 1,800 stores. With a large portion of profits from brick and mortar stores Janna Potts remains a key cog on the Target team and is an important role in the continual growth of the company.

**PRICE PERFORMANCE**

Target's stock has been publicly traded since 1967. Since it went public, it has had a 14306% return compared to the S&P 500 index which has had a 2934% return. The stock currently has a price of 125.90 and a 5 year beta of 0.75.

Below is shown the YTD of Target's stock price compared to the S&P 500 index. There is a 63% spread between the two giving an 89% return of Target to 26% return of the S&P 500. The two large increases on the graph are two big jumps in price. This is mostly correlated with their two earning report at the end of summer and end of November where Target exceed sales and net income projections in both reports causing investors to buy.

**INVESTMENT THESIS**

There are three main areas we decided to focus on for this stock:

1. We fully invest in opportunities to profitably grow our business, create sustainable long-term value, and maintain our current operations and assets
2. We maintain a competitive quarterly dividend and seek to grow it annually
3. We return any excess cash to shareholders by repurchasing shares within the limits of our credit rating goals

On the tangible side of things, there have been three recent areas which Target has invested in opportunities to grow their business. The first being their increase in private labels which contribute to more than a third of Target's annual revenue. Target has also remodeled current locations as well as expanded into more rural areas and has seen a 4.8% increase in same store sales from it. Additionally, they turned their store locations into mini warehouse pick-ups offering same day shipping to their stores after acquiring the "Shipt" service (which in turn equated to half of total sales in Q1 in 2019). By having same day store pick up, it lowers their shipping expenses and creates incentive for shoppers to buy more in person.

On the non-tangible side, Target has done a lot creating long term value and growing their business. The first by making themselves an icon in culture. This has been mentioned in Books such as "Power of Habit". By doing this, they have created loyalty and an image that is apparent in our American culture. Our studies show that people actually enjoy going to Target just to spend more money than they intended compared to places like Walmart. Additionally, Target has been strategic by making their following and use on Instagram profitable. Not only is Instagram the fastest growing social media, and not only does Target have the largest following to its competitors on Instagram, but it has made its online shopping experience transfer to Instagram extremely user friendly (within 3 clicks I could have bought an item).

Target Corporation has maintained a competitive quarterly dividend and seek to continue to grow it annually. Target has recently declared a \$.66 dividend that will be paid in early December. The company has been able to increase its dividend for 51 consecutive years making it a "dividend king" in the consumer discretionary market. Target has also announced a plan to repurchase \$5 billion in shares which is expected to occur in the 2020 fiscal year. The company's plan to repurchase stock is an investment in themselves as they plan to increase their financial position. We feel this is promising information based on their current performance with their current plan's track record (in the second quarter of 2019, Target repurchased shares worth \$341 million and still paid out dividends of \$328 million). Since they have shown they are able to capture growth opportunities and still pay a dividend, we believe they will continue to follow through with their plan in a profitable manner for shareholders.

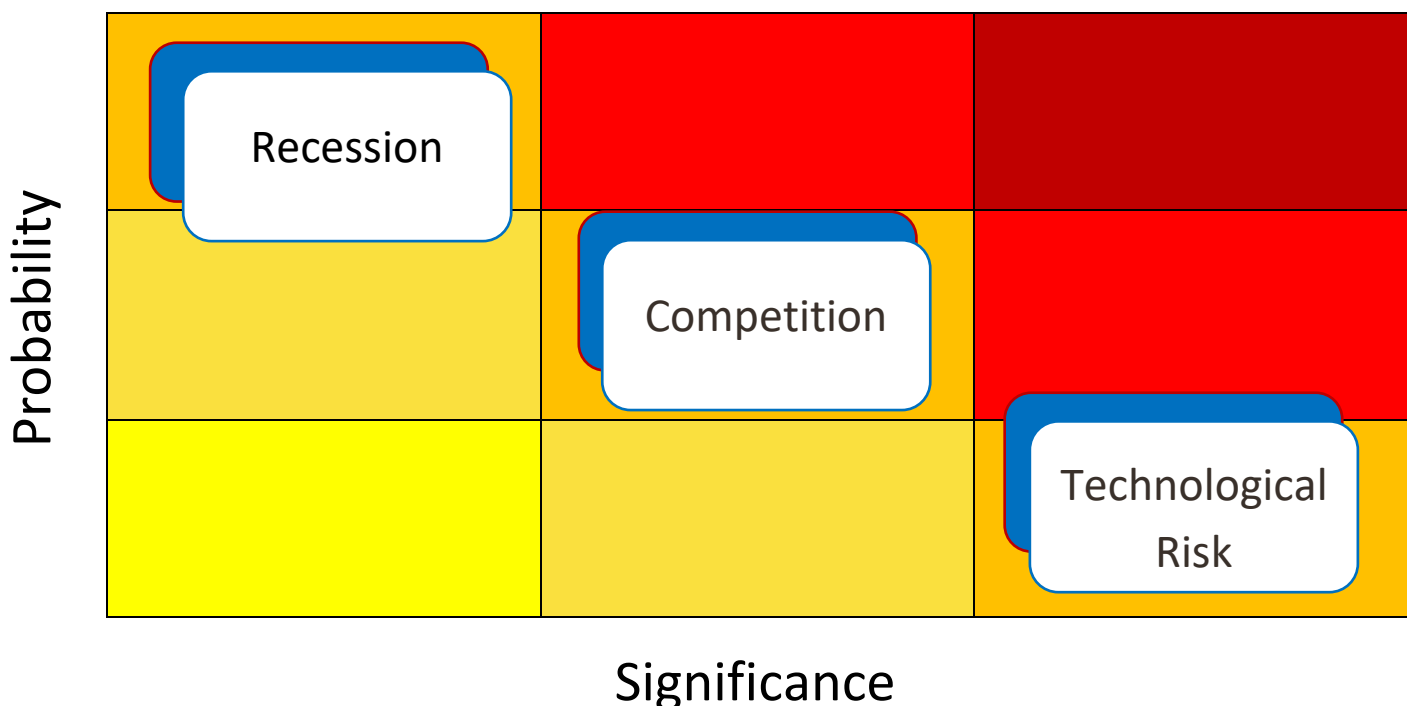
## RISKS

Target Corporation faces many risks as all companies do. The three most important risks we decided to focus on are recession, competition, and technological risks. The risk that has the highest probability but the lowest risk to the company is the possibility of a recession. Target is not completely recession proof but have the tools in place to overcome any future bear market. With Target selling essential products from food to home necessities sales will continue to see growth no matter the market.

Competition is another risk that Target Corporation faces is it goes against other retail and ecommerce giants Walmart and Amazon. We placed this risk right in the middle of the heat map as something with medium significance and medium probability. Target Corporation competes with internet retailers, apparel retailers, wholesale clubs, drug stores, supermarkets, and other forms of retail commerce. Target's ability to positively

differentiate themselves from these other competitors is what provides them with the competitive position within the consumer discretionary field. Target has taken three main steps to create this separation the first step is narrowing its market focus to its core customers of young families. The next step in their plan is investing heavily in technology and store improvements, with the recent acquisition of the \$550-million grocery delivery startup Shipt, Target has taken steps to offer consumers the option to order online and pick up the item in store. The last step they have taken to continually improve their company is constantly innovating. Target Corporation has released many new product lines from sleepwear and household essentials to pool products. These initiatives are making the retailer stand out comparing to competitors.

The last risk we focused on was the technological risks that the Target Corporation faces. Target has already faced the full effects of a technological risk in 2013 as they reported a data breach where more than 41 million customer's payment card accounts were compromised. As a result of this cyber-attack Target was forced to pay an \$18.5 million multistate settlement, the largest ever for a data breach at the time. In order to try and compensate for the situation Target provided free credit monitoring for consumers as well as offering \$10,000 to any consumers that held evidence that they had suffered losses from the breach. We placed this risk with low probability but high significance. If this event does happen again Target will face immense media backlash and lose the loyalty of devoted customers. We placed low probability of this event happening as ever since the data breach in 2013 Target has spent millions of dollars to upgrade protective systems to help assure this event doesn't happen again.



## VALUATION

For Valuation we used two separate methods giving them each a 75% and 25% weighting – EVA Income Statement Valuation and Multiples. (price used 126.85)

**EVA Income Statement Valuation:** For the EVA Income Statement Valuation, we gave a range of ‘worst case’ and ‘best case’ to give an accurate range of estimates. Using multiple different sources (Bloomberg, Yahoo Finance, Factset) we were able to come up with a different WACC of 5.00%. By only changing the WACC to 5.00% (was at 5.46%), we have a target price of 136.00. If we keep it at 5.00% for the WACC and then give them a more accurate growth rate (past two years has been about 4.15%) for the next 5 years we have a target price of 141.00. We account this into our calculation with a 75% weighting.

**Multiples Method:** The multiple we chose was Price to Earnings. We compared them to their biggest competitors which included Walmart, Amazon, Kroger, Home Depot, Costco, Macy’s, and Best Buy. We chose these companies since Amazon and Walmart have similar platforms, and the others are the top of their retail specialties that have product selection like Target in some capacity. Target currently has a P/E of 20.02x, and the average P/E with this grouping was 28.21x. With this method, we have a price of 170.39. We account this into our final calculation with a 25% weighting.

When using these two methods together and our weighting (25% with multiples, 75% with EVA) we come out to a range as low as 144.60 and as high as 148.35. This gives us an upside of 12.9% to 15.1%.

## PEER ANALYSIS

Target corporation has a wide variety of competition in many different fields from grocery stores to consumer electronics. The four companies we thought were most comparable to Target were Walmart, Costco, Kroger, and Best Buy. The six categories we wanted to compare between the companies were the following: sales increase, net income increase, stores increase, PE ratio, and dividend per share. One feature that was extremely appealing to Target that separates it from its competitors is their PE ratio. Target Corporation PE ratio is currently 20.02x which is lower when compared to the peer group average of 28.21x. Additionally, they give a higher dividend and have more top line growth than their competitors. Below we have created a chart to showcase Target’s performance compared to the average of their top competitors.

Name	Sales Increase %	Net Income Increase %	Stores Increase %	PE Ratio	Dividend per share
Target	3.4%	0.07%	1.42%	20.02x	2.60
Average	1.5%	-5.07%	0.96%	28.21x	1.18

## RECOMMENDATION

We Recommend a Buy for Target stock. We see them to be a company that will make a large impact in culture, they continuously beat earnings expectations, they are actively taking steps to increase shareholder value, they have manageable risks, and have a decent upside with conservative measurements in their valuation. We understand that we are already consumer discretionary heavy, but we feel this is a defensive stock that would still

do well in a bull or bear market. To keep weight under control, we'd even recommend a partial sell of another consumer discretionary stock in order to make room for Target to be a part of our portfolio.