Target Corporation (TGT)

Updated April 13th, 2018 by Aristofanis Papadatos

Key Metrics

Current Price:	$73	**5 Year CAGR Estimate:**	10.8%	**Quality Percentile:**	N/A
Fair Value Price:	$78	**5 Year Growth Estimate:**	6.0%	**Momentum Percentile:**	N/A
% Fair Value:	93%	**5 Year Valuation Multiple Estimate:**	1.4%	**Total Return Percentile:**	N/A
Dividend Yield:	3.4%	**5 Year Price Target**	$105	**Valuation Percentile:**	N/A

Overview & Current Events

Target was founded in 1902 and has operations only in the U.S. It consists of about 1800 discount stores, which offer general merchandize and food, and has a market cap of $39 billion.

Target has been greatly affected by the ongoing price war in the retail sector, which has heated more than ever. The stock lost almost 40% in the 12 months leading to last summer due to fierce competition and the acquisition of Whole Foods by Amazon, which caused panic in the market over its potential repercussions to conventional retailers. However, Target moved in the right direction to address its challenges. It invested heavily in remodeling its stores while it also improved its e-commerce segment in order to compete more efficiently with its peers, particularly Amazon.

The success of the strategy of Target was prominent in its last earnings report, in March. The company achieved 3.6% growth in its same-store sales. Half of this growth came from online sales, which rose more than 25% for the 4th consecutive year. The management of Target confirmed that it will continue to heavily invest in its business. Target will remodel more than 300 stores this year while it will expand its online order pickup service to approximately 1,000 stores this year. All these positive developments have led the stock to retrieve its losses, with a 46% rally in the last 9 months.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$2.86	$3.30	$3.88	$4.28	$4.38	$3.21	$4.27	$4.69	$5.01	$4.65	***$5.27***	***$7.05***
DPS	$0.60	$0.66	$0.84	$1.10	$1.32	$1.58	$1.90	$2.16	$2.32	$2.44	***$2.60***	***$3.60***

Due to the fierce competition and the failed attempt to expand to Canada, the earnings per share [EPS] of Target remained almost flat from 2012 to 2017. However, the turnaround efforts have eventually begun to bear fruit. In addition, the company will greatly benefit from the recent tax reform, as its tax rate will drop from about 30% to the low 20s. As a result, the analysts and the management expect the EPS to climb 13% this year, to approximately $5.27.

Target grew its EPS at an average annual rate of 5.5% from 2008 to 2017. While its EPS have remained almost flat in the last five years, Target has significantly improved its performance in the last three 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. It is reasonable to expect 6% annualized EPS growth, from $5.27 this year to $7.05 in 2023.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	16.2	12.8	13.9	11.9	13.7	20.7	14.7	16.6	14.6	14.2	***13.9***	***14.9***
Avg. Yld.	1.3%	1.6%	1.6%	2.2%	2.2%	2.4%	3.0%	2.8%	3.2%	4.0%	***3.4%***	***3.4%***

It is critical to note that Target has dramatically outperformed the market in the last nine months, having rallied 46% while S&P has gained only 9%. Consequently, most of the stock appreciation potential from a valuation point of view has disappeared.

Target has traded at a 10-year average P/E of 14.9. The stock is now trading at a somewhat lower P/E of13.9, partly due to the intense competition in its sector. Nevertheless, as the company seems to be moving in the right direction and its turnaround efforts have begun to bear fruit, it is reasonable to expect the stock to revert towards its average P/E in the future. If this occurs in 2023, the stock will enjoy an average annualized 1.4% return from the expansion of its P/E ratio.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	46.3%	43.5%	44.4%	47.6%	47.2%	47.2%	47.7%	51.8%	53.5%	54.4%	***53.2%***	***54.0%***
Debt/A	65.6%	68.9%	65.5%	64.6%	66.1%	65.6%	63.6%	66.0%	67.8%	70.7%	***70.0%***	***70.0%***
Int. Cov.	8.1	5.1	5.8	6.9	6.1	8.4	4.6	5.1	9.1	4.9	***6.5***	***6.5***
Payout	21.0%	20.0%	21.6%	25.7%	30.1%	49.2%	44.5%	46.1%	46.3%	52.5%	***49.3%***	***51.1%***
Std. Dev.	60.0%	39.2%	20.4%	23.4%	15.1%	16.2%	20.6%	20.7%	22.8%	30.3%	***28.0%***	***25.0%***

Target is a dividend aristocrat that has grown its dividend for 49 consecutive years. However, as it has grown its dividend much faster than its earnings, it has markedly increased its payout ratio, from 20% in 2009 to 49.3% this year. Moreover, the company is heavily investing in its business in order to navigate through the changing landscape in the retail sector. Therefore, the company is likely to raise its dividend at a slow pace in the upcoming years. Last year, it raised its dividend by only 3%.

Given the price war in the retail sector, Target does not have a moat. In addition, as consumers tend to curtail their consumption during recessions, the company is vulnerable in such periods. To be sure, its EPS fell 14% in 2008. 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 to the EPS 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

After a rough year, Target has markedly improved its performance in the last nine months. As a result, its stock has rallied 46% during this period and hence most of the capital appreciation potential of the stock from expansion of its P/E ratio has disappeared. Nevertheless, the stock can still offer a 10.8% average annual return over the next five years thanks to its 3.4% dividend, a 1.4% annual expansion of its P/E ratio and a reasonable 6% annual EPS growth. This potential return is certainly attractive and is much higher than the upside potential of most stocks at the current phase of the ongoing 9-year bull market.

Total Return Breakdown by Year