Macy's (M)

Updated May 4th, 2018 by Jonathan Weber

Key Metrics

Current Price:	$31	**5 Year CAGR Estimate:**	11.7%	**Quality Percentile:**	N/A
Fair Value Price:	$38	**5 Year Growth Estimate:**	2.6%	**Momentum Percentile:**	N/A
% Fair Value:	81%	**5 Year Valuation Multiple Estimate:**	4.3%	**Total Return Percentile:**	N/A
Dividend Yield:	4.8%	**5 Year Price Target**	$44	**Valuation Percentile:**	

Overview & Current Events

Macy's is a department store company that operates brick and mortar stores as well as online stores under the Macy's, Bloomingdale's and Bluemercury brands. Macy's was founded in 1929, is headquartered in Cincinnati, Ohio, and currently has a market cap of $10 billion.

Macy's reported its most recent quarterly results on February 27. The company earned $2.82 per share, an increase of 40% over 2016's Q4 EPS of $2.02. During all of 2017 Macy's has earned $3.77 per share (profits are very seasonal, Q4 earnings are always the highest due to holiday spending). During the fourth quarter Macy's revenues grew by 1.8%, the important comps sales metric was positive as well (up 1.4% year-over-year). Macy's expects 2018's earnings-per-share (EPS) of $3.55 to $3.75, with revenues being down slightly year over year (due to store closures, asset sales and the impact of a 53rd week in fiscal year 2017).

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$1.29	$1.41	$2.03	$2.88	$3.45	$4.00	$4.40	$3.77	$3.13	$3.77	***$3.65***	***$4.15***
DPS	$0.35	$0.20	$0.20	$0.35	$0.70	$0.90	$1.13	$1.35	$1.48	$1.51	***$1.55***	***$1.75***

Macy's EPS grew every year coming out of the Great Recession up to 2014. After EPS peaked in 2014 they declined considerably, though, which is primarily due to the struggles the brick-and-mortar retail industry has seen since. Online competition from companies such as Amazon has made many retailers struggle to generate rising comparable store sales, especially those whose business is easily impacted by online competition (groceries, home improvement retailers, etc. are less affected than clothing retailers, for example).

This has led to earnings declines for department stores such as Macy's, but more recently things are pointing upwards again. During 2017 Macy's grew its profits considerably, and the company is making strategic moves to stabilize its business. Expanding its own online business and moving towards an omni-channel approach (coupling online and brick-and-mortar sales). Macy's has been successful in this approach (compared to other brick-and-mortar focused retailers), which was one of the reasons why Macy's has been able to grow its revenues during 2017 despite closing down some stores and selling assets.

With the economy doing well and disposable incomes rising significantly Macy's also benefits from a macro tailwind going forward, as this should push sales up for most retailers. Macy's has stated that it will continue to close down the least profitable stores to focus on the most profitable locations, which will help increase margins going forward. At the same time the sale of less profitable assets produces additional cash flows that Macy's is currently using to reduce its debt, which, in turn, is also beneficial for its earnings due to lower interest expenses.

Macy's recent dividend growth rate has been in the low single digits.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	13.9	9.9	10.7	9.7	11.1	11.7	13.4	15.2	11.9	6.6	***8.5***	***10.5***
Avg. Yld.	2.9%	1.4%	0.9%	1.3%	1.8%	1.9%	1.9%	2.4%	4.0%	6.1%	***4.8%***	***4.3%***

Macy’s has never traded at an especially high valuation, but over the last two years shares got even less expensive. This is primarily due to the earnings decline Macy’s suffered during 2016 and due to investors worrying about the retail industry. During 2018 shares performed well so far, which has lifted the company’s multiples somewhat, but shares continue to trade at a discount to the 10-year median PE ratio of 11.0.

The same selling pressure that has made Macy’s valuation decline has also led to a dividend yield that is substantially higher than it usually was over the last decade. At 4.8% Macy’s offers a lot of income for investors, and the dividend looks safe for the foreseeable future.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	44.6%	44.7%	49.3%	48.3%	53.1%	51.9%	52.7%	51.4%	51.2%	49.9%	***50.0%***	***50.0%***
Debt/A	78.8%	77.9%	73.3%	73.2%	70.9%	71.3%	75.1%	79.1%	77.9%	70.6%	***68.0%***	***61.0%***
Int. Cov.	-	1.9	3.3	5.5	4.8	6.9	6.8	5.7	3.6	6.1	***6.5***	***7.0***
Payout	27.3%	14.2%	9.9%	12.2%	20.3%	22.5%	25.7%	35.8%	47.3%	40.1%	***42.5%***	***42.2%***
Std. Dev.	70.2%	36.8%	32.1%	23.4%	21.3%	17.4%	28.4%	38.3%	47.1%	45.6%	***36.0%***	***32.0%***

Macy’s produces a high amount of gross profits relative to the assets it owns, which is, at least partially, due to the fact that its assets (which the company has owned for a long time) are significantly depreciated on its balance sheet. Debt to assets are at a relatively high level, but Macy’s has started reducing its debt in 2016 and has made a lot of progress in this regard during 2017. Since Macy’s produces very high cash flows ($1.9 billion during 2017), and only pays out ~$460 million in dividends each year, Macy’s has a lot of surplus cash flows that can be used for share repurchases or debt reduction. Recently Macy’s has not bought back a lot of shares and has instead chosen to lower its debt levels, which is opportune in a rising rates environment, as this means significantly lower interest expenses in the coming years.

Macy’s has a renowned brand, 50% of Americans shop at Macy’s at least once a year. There is a Macy’s store in the majority of grade A malls, and macys.com gets more than 1.5 billion visits annually. This shows that Macy’s has a strong position in the brick-and-mortar department store industry, competitors therefore will have a hard time getting market share from Macy’s. Online competition is another issue, but Macy’s own e-commerce presence and omni-channel strategy should help soften the impact Amazon and others will have on Macy’s going forward. From 2007 to 2009 Macy’s earnings declined by 35%, but the company remained highly profitable and cash flow positive.

Final Thoughts & Recommendation

Macy’s has to find a strategy versus online retailers (like all of its peers), but it seems Macy’s is making a lot of progress in that regard. With lower debt levels, rising comparable store sales, a focus on its most profitable stores, and macro tailwinds, Macy’s has a good chance of growing its profits going forward. Coupled with a low valuation and a high dividend yield Macy’s could deliver compelling total returns in the coming years.

Total Return Breakdown by Year