



Ross Stores (ROST)

Updated August 23rd, 2019 by Aristofanis Papadatos

Key Metrics

Current Price:	\$103	5 Year CAGR Estimate:	5.4%	Volatility Percentile:	60.1%
Fair Value Price:	\$77	5 Year Growth Estimate:	10.0%	Momentum Percentile:	74.2%
% Fair Value:	133%	5 Year Valuation Multiple Estimate:	-5.6%	Growth Percentile:	91.9%
Dividend Yield:	1.0%	5 Year Price Target	\$124	Valuation Percentile:	14.0%
Dividend Risk Score:	A	Retirement Suitability Score:	C	Total Return Percentile:	24.4%

Overview & Current Events

Ross Stores operates 1,523 stores with off-price apparel and home fashion in 38 states. It also operates 249 dd's DISCOUNTS stores in 18 states and has a market cap of \$37 billion. The retailer offers attractive merchandize at a 20%-60% discount compared to the regular prices of department and specialty stores. Ross Stores has grown its revenue and its earnings-per-share every single year for more than a decade. This record is a testament to the strength of its business model and the quality of its management, which executes its growth plan in an exemplary way.

In late August, Ross Stores reported (8/22/19) financial results for the second quarter of fiscal 2019. The retailer grew its sales by 6% thanks to its new stores and 3% same-store sales growth. The latter exceeded the analysts' consensus of 2.1%. Operating margin of 13.7% was better than expected but only thanks to favorable timing of expenses, which are expected to reverse in the second half of the year. Earnings-per-share rose 10%, from \$1.04 in last year's quarter to \$1.14, and exceeded analysts' consensus by \$0.03.

While the Ladies segment continued to trail the total performance of Ross Stores, it has shown signs of improvement. Management tightened its guidance for this year's earnings-per-share from \$4.38-\$4.52 to \$4.41-\$4.50. It also plans to open about 100 new stores and continues to expect 1%-2% same-store sales growth. Guidance would have been better but it was affected by the recent announcement of 10% tariffs on goods sourced from China.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$0.89	\$1.16	\$1.43	\$1.77	\$1.94	\$2.21	\$2.51	\$2.83	\$3.55	\$4.26	\$4.52	\$7.28
DPS	\$0.12	\$0.18	\$0.24	\$0.30	\$0.36	\$0.40	\$0.47	\$0.54	\$0.64	\$0.90	\$1.02	\$1.80
Shares¹	491.7	472.3	451.8	440.0	426.8	414.9	402.3	391.9	379.7	368.4	355.0	310.0

Ross Stores has grown its earnings-per-share by a multiple of 7 in the last decade, from \$0.58 in 2008 to \$4.26 in 2018. Moreover, it still has growth prospects ahead. The company currently has 1,772 stores while management is confident for a potential of 2,500 to 3,000 stores in the U.S. Thus, the company can still grow its store count meaningfully. As the retailer opens about 100 new stores per year, it is evident that it has at least a decade of growth ahead.

Ross Stores has missed the analysts' estimates only once in the last 22 quarters. As it tends to be conservative in its guidance, we expect earnings-per-share to be around \$4.52 this year. Moreover, the company has grown its earnings-per-share by 22.1% and 14.0% per year on average in the last 10 and 5 years, respectively. As the retailer will find it increasingly difficult to keep growing at its historical pace, particularly amid heating competition, we assume 10.0% average annual earnings-per-share growth for the next five years.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	11.6	12.0	14.1	17.2	17.4	17.0	20.3	21.4	19.7	20.1	22.8	17.1
Avg. Yld.	1.2%	1.3%	1.2%	1.0%	1.0%	1.1%	0.9%	0.9%	1.0%	1.0%	1.0%	1.5%

1. In millions.

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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Ross Stores is trading at a price-to-earnings ratio of 22.8, which is higher than its 10-year average price-to-earnings ratio of 17.1. If the stock reverts to its average valuation level in the next five years, it will incur a -5.6% annualized drag due to the contraction of its valuation level during this period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	13.5%	15.5%	16.8%	16.9%	18.6%	18.1%	18.7%	19.1%	19.2%	21.1%	22.6%	24.7%

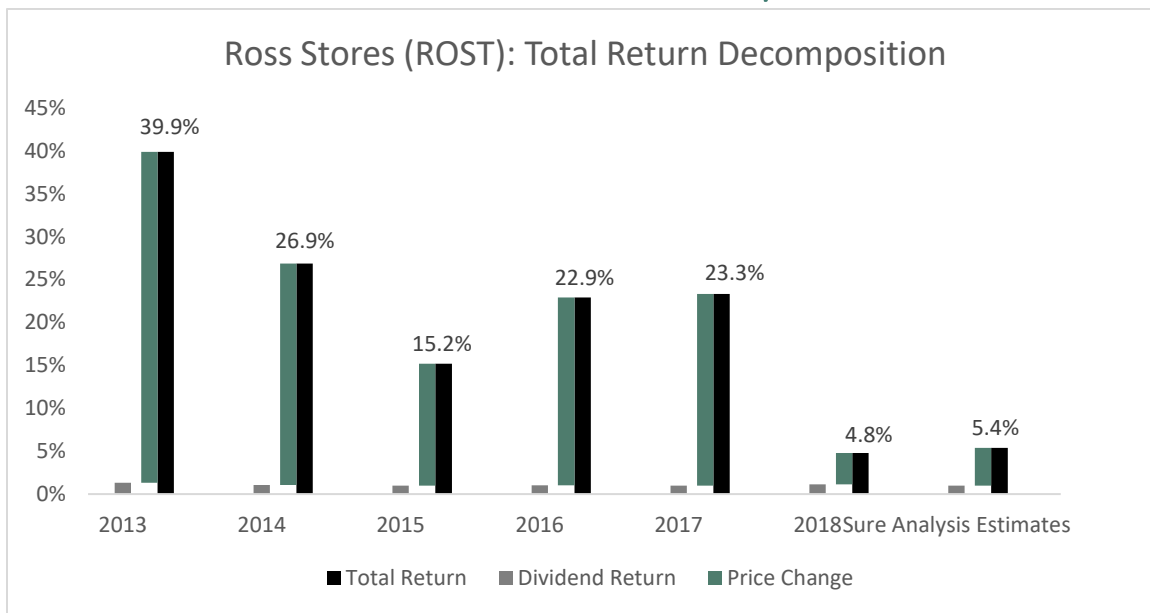
The key behind the exceptional growth record of Ross Stores is the fact that it offers great discounts on popular brands. It creates a treasure-hunting experience, which is appealing to consumers and constitutes a moat. This unique shopping experience helps explain why Ross Stores is one of the few retailers that have not been affected by Amazon. Moreover, while the U.S. economy has been growing for a whole decade, consumers have become increasingly price-conscious in recent years. Therefore, Ross Stores appeals to a wide range of consumers. With that said, competition has become increasingly heated in the retail sector.

Ross Stores offers a low dividend yield (1.0%) but has raised its dividend for 25 consecutive years. It has raised its dividend at a 24% average annual rate since 2001 and yet still has a low payout ratio and a strong balance sheet. Furthermore, its capital expenses have remained below half of its operating cash flows every year in the last decade, resulting in high free cash flows. Ross Stores will likely keep growing its dividend at a double-digit pace for years. Ross Stores is also resilient during recessions, as consumers become particularly price-sensitive.

Final Thoughts & Recommendation

Ross Stores has a somewhat rich valuation and may offer just a 5.4% average annual return over the next five years. It is a high quality discount retailer with a wide moat and solid growth prospects over the next several years. However, due to its valuation, the stock could be sensitive to any negative news. For instance, shares fell 10% after a previous earnings report due to a mild downward revision of its guidance. Overall the stock earns a hold rating due to its rich valuation.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	7184	7866	8608	9721	10230	11042	11940	12867	14135	14984
Gross Profit	1857	2136	2368	2710	2869	3104	3363	3693	4092	4257
Gross Margin	25.8%	27.2%	27.5%	27.9%	28.0%	28.1%	28.2%	28.7%	29.0%	28.4%
SG&A Exp.	1131	1230	1304	1438	1526	1615	1739	1890	2044	2217
D&A Exp.	159	161	160	185	206	233	275	303	313	330
Operating Profit	726	907	1063	1272	1343	1488	1624	1803	2048	2041
Operating Margin	10.1%	11.5%	12.4%	13.1%	13.1%	13.5%	13.6%	14.0%	14.5%	13.6%
Net Profit	443	555	657	787	837	925	1021	1118	1363	1587
Net Margin	6.2%	7.1%	7.6%	8.1%	8.2%	8.4%	8.5%	8.7%	9.6%	10.6%
Free Cash Flow	730	474	404	555	471	726	959	1261	1310	1653
Income Tax	276	342	396	478	506	561	591	669	678	463

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	2769	3116	3301	3671	3897	4687	4869	5309	5722	6074
Cash & Equivalents	768	834	650	647	423	697	762	1112	1290	1413
Accounts Receivable	44	45	51	60	63	73	74	75	88	97
Inventories	872	1087	1130	1209	1257	1373	1419	1513	1642	1750
Total Liabilities	1611	1784	1808	1904	1889	2408	2397	2561	2673	2768
Accounts Payable	658	767	762	808	779	1001	946	1022	1060	1177
Long-Term Debt	150	150	150	150	150	396	396	396	397	312
Shareholder's Equity	1157	1333	1493	1767	2007	2279	2472	2748	3049	3306
D/E Ratio	0.13	0.11	0.10	0.08	0.07	0.17	0.16	0.14	0.13	0.09

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	17.3%	18.9%	20.5%	22.6%	22.1%	21.5%	21.4%	22.0%	24.7%	26.9%
Return on Equity	41.1%	44.6%	46.5%	48.3%	44.4%	43.1%	43.0%	42.8%	47.0%	50.0%
ROIC	36.1%	39.8%	42.0%	44.2%	41.1%	38.3%	36.8%	37.2%	41.4%	44.9%
Shares Out.	491.7	472.3	451.8	440.0	426.8	414.9	402.3	391.9	379.7	368.4
Revenue/Share	14.37	16.40	18.72	21.82	23.70	26.41	29.38	32.58	36.78	40.21
FCF/Share	1.46	0.99	0.88	1.25	1.09	1.74	2.36	3.19	3.41	4.43

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

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