Kontoor Brands Inc. (KTB)

Updated November 17th, 2020 by Jonathan Weber

Key Metrics

Current Price:	$40	**5 Year CAGR Estimate:**	2.0%	**Market Cap:**	$2.3B
Fair Value Price:	$31	**5 Year Growth Estimate:**	3.0%	**Ex-Dividend Date:**	12/09/20
% Fair Value:	130%	**5 Year Valuation Multiple Estimate:**	-5.1%	**Dividend Payment Date:**	12/18/20
Dividend Yield:	4.0%	**5 Year Price Target**	$36	**Years Of Dividend Growth:**	-
Dividend Risk Score:	N/A	**Retirement Suitability Score:**	N/A	**Last Dividend Increase:**	-

Overview & Current Events

Kontoor Brands is an apparel company that focuses on what it calls "lifestyle apparel". The company, which was spun off from V.F. Corporation (VFC) in 2019, owns some of the world's most iconic denim brands, including *Wrangler, Lee,* and *Rock & Republic.* Kontoor Brands is a US-focused company, just around 30% of its revenues are generated outside of the United States. Kontoor is headquartered in Greensboro, North Carolina.

Kontoor Brands reported its third quarter financial results on October 29. The company reported that its revenue declined by 9% compared to the previous year's quarter, to $580 million. Revenues came in $34 million higher than what the analyst community had forecasted. Kontoor Brands' revenues declined primarily due to the current pandemic impact, as consumers spending less hurt Kontoor's ability to sell merchandise during the quarter.

Kontoor Brands' earnings-per-share totaled $1.33 during the third quarter, beating the analyst consensus estimate by a very large $0.75. Kontoor Brands' lower revenue generation did not hurt its profitability too much, as Kontoor Brand was able to increase its gross profit margin by a meaningful 240 basis points, which came as a surprise to the analyst community. 2020 will be less profitable than 2019, but management's current guidance of $2.25 to $2.35 in earnings-per-share is better compared to what the analyst community had expected. As the coronavirus crisis will not be in place forever, we try to calculate fair value using an earnings power figure that adjusts for the crisis. In Kontoor Brands' case, we see earnings power at $2.80, which is around the guidance midpoint at the beginning of the year, i.e. before the pandemic. Kontoor Brands has reinstated its dividend, but at a lower level of $0.40 per share per quarter.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	$3.84	***$2.30***	***$3.25***
DPS	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	$2.24	***$1.60***	***$1.77***
Shares[1]	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	57.9	***57.6***	***57.0***

Kontoor Brands was spun off not too long ago, thus there is no long-term data available. Due to the nature of the industry Kontoor Brands is active in, it has to be expected that this is a vulnerable business during recessions.

For 2020, Kontoor Brands forecasted solid results before the coronavirus emerged, with this statement being based on the fact that one-time separation costs have passed, although the divestment of some business lines was seen as a headwind to revenues and profits. Management had previously forecasted revenue growth in the low-single-digits for 2020 and 2021, before the current pandemic emerged. The further spread of the virus in the US and Europe during the last couple of months hurt Kontoor Brands' first half results badly, but thanks to reopening efforts, the back half of the year will likely not be as bad, which is why we, and the analyst community, still forecast positive net profits for the current year. Once the pandemic has fully passed, Kontoor Brands will, we believe, recover to a substantially higher profitability once again, although the exit of some business lines will likely prevent Kontoor Brands from getting close to $4 in earnings-per-share in the foreseeable future.

[1] In Millions

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	10.9	***14.3***	***11.0***
Avg. Yld.	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	5.3	***4.0%***	***4.9%***

Finding a fair value for Kontoor Brands is difficult because it does not have any history as a standalone company. We can, however, look at the historical valuation of its prior parent company. V.F. Corporation has traded at an average price-to-earnings ratio of 17. Given that Kontoor Brands was created to separate V.F. Corporation's slow-growing legacy brands from its faster-growing core businesses, Kontoor Brands should trade at a discount to that. Based on our current earnings power estimate, we feel that shares are trading above fair value, following huge gains since our last update.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	58.3%	***57.1%***	***54.4%***

Kontoor Brands' investment case was primarily centered on a high dividend yield that looked like it was covered in a solid way before the current crisis, which has devastated the industry. The dividend has been reinstated following a suspension during the peak of the pandemic, but the new payout is lower compared to pre-crisis dividend levels.

Kontoor Brands' competitive advantage lies in its ownership of some of the world's most popular denim brands, *Lee's* and *Wrangler* in particular control a large amount of market share in the denim category. The company is vulnerable to economic downturns, which is being showcased during the current pandemic.

Final Thoughts & Recommendation

Kontoor Brands is a consumer goods company that was created through a spin-off of some low-growth businesses. We believe that the company's earnings and revenues will recover meaningfully once the pandemic has passed, and the recent dividend reinstatement is a positive. Following sizeable share price gains since our last update, shares are now trading above our fair value estimate, however, which is why we rate the stock a sell for now.

Total Return Breakdown by Year