Tapestry Inc. (TPR)

Updated January 5th, 2021 by Felix Martinez

Key Metrics

Current Price:	$33	**5 Year CAGR Estimate:**	2.8%	**Market Cap:**	$9.2 B
Fair Value Price:	$28	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date:**	N/A
% Fair Value:	116%	**5 Year Valuation Multiple Estimate:**	-3.0%	**Dividend Payment Date:**	N/A
Dividend Yield:	N/A	**5 Year Price Target**	$24	**Years of Dividend Growth:**	0
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	N/A

Overview & Current Events

Tapestry Inc. (TPR) was founded in 2017 as a transformation from Coach IP Holdings LLC (founded in 1941) and is a leading American multinational luxury fashion holding company. The Company is based in New York and is the parent company of three brands: Coach, Kate Spade, and Stuart Weitzman. The Company's renaming came after Coach acquired Stuart Weitzman and Kate Spade and expanded from making Coach-brand handbags to producing a wider variety of products through their three primary brands. These products include various leather goods, footwear, accessories, clothes, fragrances, and jewelry. Tapestry has a market capitalization of approximately $4.4 billion, over 20,000 employees, and $4.9 billion in annual revenue. Coach continues to make up 70% of company sales, Kate Spade represents about a quarter of sales, and Stuart Weitzman is a small but growing segment in the overall business. The Company sells products worldwide from its 1,500+ branded retail locations, brand websites, and through thousands of distributor retail locations.

Tapestry reported Fiscal year (FY)2021 first-quarter results on October 29, 2020. For the quarter, sales were down (14)% Year over Year (YoY) from $1.36 billion to $1.17 billion; however, it improved from last quarter. Operating income was $202 million versus $52 million in the prior year, which increased by 288%. The Company had a net profit of $232 million in the quarter, giving earnings per diluted share of $0.83. Compared to $20 million's net income with earnings per diluted share of $0.07 in the prior-year period. CEO Ms. Crevoiserat said that the Company has multiple initiatives that are designed to create a strong foundation for profitable expansion. She and management expect to "…return to sustained topline growth in the second half of fiscal 2021, with bottom-line growth in each of fiscal 2021, 2022 and 2023."

The Company is not providing an FY2021 outlook because of the dynamic nature of the COVID-19 pandemic. However, consensus estimate that the Company will make $2.34 per share for the full year of 2021. This is an improvement from the last quarter report of $1.87 per share for FY2021. Thus, we will use $2.34 per share as fair value and an annual return calculation rate.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$2.92	$3.53	$3.72	$3.10	$1.92	$1.98	$2.15	$2.63	$2.57	$0.97	***$2.34***	***$2.99***
DPS	$0.68	$0.98	$1.24	$1.35	$1.35	$1.35	$1.35	$1.35	$1.35	$1.02	***$0.34***	---
Shares[1]	255.5	285.1	281.9	274.4	276.6	278.5	281.9	288.0	286.8	278.0	***278.0***	***278.0***

Tapestry had experienced negative earnings growth of (11.5)% since 2011, when it earned $2.98 per share, but has had (13.3)% annual growth over the past five years. Revenue has continued to grow at a CAGR of 9.5% for the past five years, while operating margins have deteriorated, resulting in flat and choppy earnings in recent years. We expect stabilization and 5.0% forward earnings growth, primarily due to share buybacks at low valuations and continued slow revenue growth. Still, the outcome is highly dependent on Tapestry's ability to maintain margins and sustain at least mild topline growth.

[1] Share count is in millions.

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Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	17.3	18.4	14.9	16.2	19.4	17.4	18.3	17.4	15.2	13.7	***14.0***	***12.0***
Avg. Yld.	1.3%	1.5%	2.2%	2.7%	3.6%	3.9%	3.4%	3.0%	3.5%	0.0%	***0.0%***	***0.0%***

Over the past decade, Tapestry has averaged a P/E ratio of 16.8. However, for most of that period, the Company consisted entirely of the Coach brand and enjoyed higher returns on invested capital. With slowing sales and declining margins in a competitive environment of online competition and slower global growth, we consider a P/E ratio of 12 to be fair until the Company can demonstrate a resumption of growth and stabilized margins. The Company has upside valuation potential even with a partial reversion towards the mean of a P/E ratio of 12 or 13, but likely only if the Company demonstrates improvement.

Safety, Quality, Competitive Advantage, & Recession Resiliency

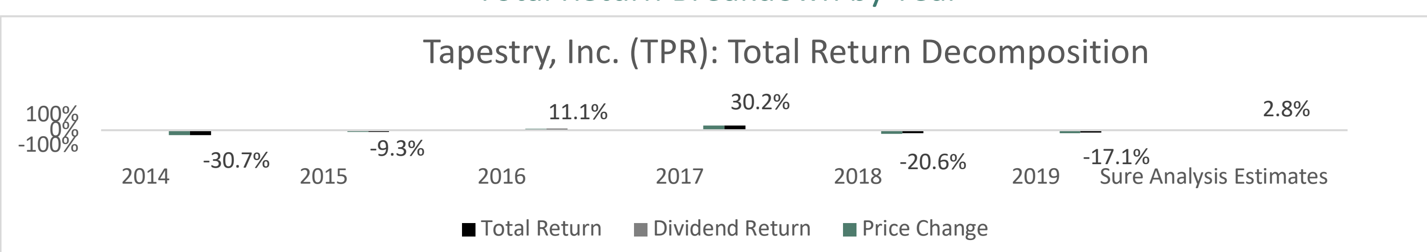
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	23.3%	27.8%	33.3%	43.5%	70.3%	68.2%	62.8%	51.3%	52.5%	105.2%	---	---

Tapestry's luxury brands, especially Coach, give the company at least a small economic moat. This is evidenced by its historically high returns on invested capital and considerable market outperformance since Coach went public in the early 2000s. However, the company's returns on invested capital have been declining in recent years, indicating a deterioration in brand strength or cyclical as online retail puts margin pressure on all physical retailers. Overall, their investment returns and profitability remain above average but diminishing. The ongoing trade dispute between the United States and China puts further pressure on Tapestry, as a small portion of its products is made in China, but a significant amount of its sales are earned from China. Tapestry currently has a BBB- credit rating, which puts them on the low side of investment grade. The company's balance has gotten better, with a Debt/Equity ratio of 1.7 compared to last reported 2. Still, the inconsistency of their earnings and the company's economic vulnerability appears to be driving lower overall credit quality from the rating agencies. The security does not necessarily offer growth or stability that many retirees rely on. The company did remain highly profitable during the previous two recessions as the primary Coach brand, but the expanded Tapestry company is untested by a downturn in its current form.

Final Thoughts & Recommendation

Tapestry has decent brands but faces stiff competition, global tariff uncertainty, coronavirus outbreak, diminishing profitability, and the rest of the retail sector. The good news is that Tapestry is a producer of its products, rather than just a middleman, and has various online platforms from which to grow. We expect moderate forward returns of 2.8% per annum from Tapestry as a baseline case, but the result is expected to be highly variable. The dividend has been suspended, and we do not know when it will be restarted and how much. Overall, business uncertainty remains high. We consider Tapestry to be a Sell after its recent run-up.

Total Return Breakdown by Year



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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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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	4159	4763	5075	4806	4192	4492	4488	5880	6027	4961
Gross Profit	3024	3466	3698	3297	2909	3051	3081	3849	4054	3239
Gross Margin	72.7%	72.8%	72.9%	68.6%	69.4%	67.9%	68.6%	65.5%	67.3%	65.3%
SG&A Exp.	1719	1954	2174	2177	2291	2398	2294	3178	3240	3312
D&A Exp.	125	133	163	189	192	211	213	260	268	248
Operating Profit	1305	1512	1525	1120	618	654	787	671	814	-73
Operating Margin	31.4%	31.7%	30.0%	23.3%	14.7%	14.5%	17.5%	11.4%	13.5%	-1.5%
Net Profit	881	1039	1034	781	402	461	591	398	643	-652
Net Margin	21.2%	21.8%	20.4%	16.3%	9.6%	10.3%	13.2%	6.8%	10.7%	-13.1%
Free Cash Flow	886	1037	1173	766	728	353	571	729	518	202
Income Tax	420	467	486	341	209	166	168	199	123	28

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	2635	3104	3532	3663	4667	4893	5832	6678	6877	7924
Cash & Equivalents	700	917	1063	592	1292	859	2673	1243	969	1426
Accounts Receivable	143	174	175	199	220	245	268	314	298	193
Inventories	422	504	525	526	485	459	470	674	778	737
Goodwill & Int. Ass.	341	386	355	371	794	849	821	3217	3228	2681
Total Liabilities	1023	1111	1123	1243	2177	2210	2830	3434	3364	5648
Accounts Payable	119	155	179	154	223	187	195	264	244	131
Long-Term Debt	24	23	1	141	890	876	1580	1594	1597	2299
Shareholder's Equity	1613	1993	2409	2421	2490	2683	3002	3245	3513	2276
D/E Ratio	0.02	0.01	0.00	0.06	0.36	0.33	0.53	0.49	0.45	1.01

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	34.5%	36.2%	31.2%	21.7%	9.7%	9.6%	11.0%	6.4%	9.5%	-8.8%
Return on Equity	56.5%	57.6%	47.0%	32.4%	16.4%	17.8%	20.8%	12.7%	19.0%	-22.5%
ROIC	55.6%	56.9%	46.7%	31.4%	13.5%	13.3%	14.5%	8.4%	12.9%	-13.5%
Shares Out.	288.5	285.1	281.9	274.4	276.6	278.5	281.9	288.0	286.8	278.0
Revenue/Share	13.79	16.19	17.73	17.14	15.12	16.08	15.87	20.37	20.73	17.81
FCF/Share	2.94	3.53	4.10	2.73	2.62	1.26	2.02	2.53	1.78	0.72

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