



Target Corporation (TGT)

Updated March 7th, 2021 by Josh Arnold

Key Metrics

| | | | | | |
|-----------------------------|-------|--|-------|----------------------------------|-----------------------|
| Current Price: | \$173 | 5 Year CAGR Estimate: | 5.5% | Market Cap: | \$86 B |
| Fair Value Price: | \$157 | 5 Year Growth Estimate: | 6.0% | Ex-Dividend Date: | 05/18/21 ¹ |
| % Fair Value: | 110% | 5 Year Valuation Multiple Estimate: | -2.0% | Dividend Payment Date: | 05/10/21 ¹ |
| Dividend Yield: | 1.6% | 5 Year Price Target | \$210 | Years Of Dividend Growth: | 53 |
| Dividend Risk Score: | A | Retirement Suitability Score: | B | Last Dividend Increase: | 3.0% |

Overview & Current Events

Target was founded in 1902 and after a failed bid to expand into Canada, has operations solely in the U.S. market. Its business consists of about 1,850 big box stores, which offer general merchandise and food. Target has a market capitalization of \$86 billion and should produce about \$91 billion in total revenue this year.

Target reported fourth quarter and full year earnings on March 2nd, 2021 with results easily beating estimates on both the top and bottom lines, as Target capped what ended up being a blockbuster 2020 with another very strong performance in the critical fourth quarter. Adjusted earnings-per-share came to \$2.67 in Q4, which was two-thirds higher than in was in the same period a year ago. Revenue soared as well, adding 21% to end the quarter at \$28.3 billion, beating expectations by nearly a billion dollars.

Comparable sales were up a staggering 20.5% in Q4, reflecting traffic growth of 6.5% and average ticket size of +13.1%. Store comparable sales were up 6.9%, while digital comparable sales more than doubled year-over-year. Q4 was the last comparable quarter before COVID hit, and we therefore see significant headwinds in terms of comparable sales for this year now that COVID is being lapped starting in Q1. Same-day services, which include Order Pick Up, Drive Up, and Shipt, grew 212% during Q4 with Drive Up growing more than 500%.

Target declined to give guidance for this year, but we see the lack of an extraordinary tailwind like COVID as producing somewhat lower earnings this year off of 2020's enormously high earnings total. Our initial estimate is for \$8.70 in earnings-per-share as Target begins to lap its most difficult comparables in its history.

Growth on a Per-Share Basis

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2026 |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|----------------|
| EPS | \$4.28 | \$4.38 | \$3.21 | \$4.27 | \$4.69 | \$5.01 | \$4.65 | \$5.39 | \$6.39 | \$9.42 | \$8.70 | \$11.64 |
| DPS | \$1.10 | \$1.32 | \$1.58 | \$1.90 | \$2.16 | \$2.32 | \$2.44 | \$2.52 | \$2.60 | \$2.68 | \$2.72 | \$3.64 |
| Shares² | 679 | 657 | 635 | 640 | 633 | 583 | 546 | 524 | 512 | 506 | 495 | 455 |

Target has grown its earnings-per-share at an average annual rate of 8.2% during the last decade. Due to fierce competition and the failed attempt to expand to Canada, Target's earnings-per-share remained almost flat from 2012 to 2017. However, turnaround efforts have borne fruit and as a result, Target has significantly improved its performance in recent quarters. The company has reduced its share count by about -2.8% per year in the last five years, although the pace of buybacks has slowed materially as the share price has risen. Overall, we expect 6% annualized growth.

We see continued comparable sales growth as driving results, along with a small measure of margin expansion, and a tailwind from the buyback. Target's digital efforts are also working extremely nicely, as we saw again in Q4 results, and the company's small-format stores are performing very well, opening up a new avenue of growth for the company in the coming years. SG&A costs were leveraged down in the second half of 2020, which is a positive development from prior quarters. Target lifted its share repurchase suspension during the Q3 report, so we expect to see significant shareholder

¹ Estimated date

² Share count in millions

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returns via this medium in the near future. However, we note that Target remains committed to investing in its digital capabilities, as well as its 50+ year streak of dividend increases.

Valuation Analysis

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | Now | 2026 |
|-----------|------|------|------|------|------|------|------|------|------|------|------|------|
| Avg. P/E | 11.9 | 13.7 | 20.7 | 14.7 | 16.6 | 14.6 | 14.2 | 14.2 | 14.4 | 14.0 | 19.9 | 18.0 |
| Avg. Yld. | 2.2% | 2.2% | 2.4% | 3.0% | 2.8% | 3.2% | 4.0% | 3.3% | 2.8% | 2.0% | 1.6% | 1.7% |

Target shares trade for 19.9 times our earnings estimate for this year, slightly ahead of our raised estimate of fair value at 18 times earnings. We note that the 1.6% yield is the lowest yield the stock has traded with for several years. If the stock reverts to our estimate of fair value over the next five years, it will produce a small headwind to total returns. Target's recent above-trend growth is already reflected in our fair value estimate.

Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2026 |
|--------|------|------|------|------|------|------|------|------|------|------|------|------|
| Payout | 26% | 30% | 49% | 45% | 46% | 46% | 53% | 47% | 41% | 28% | 31% | 31% |

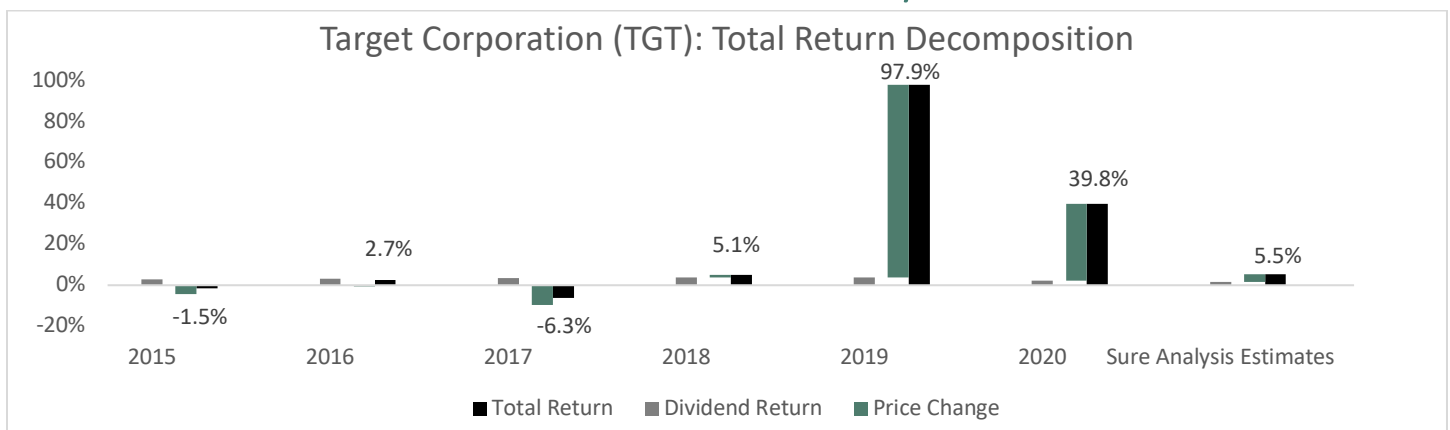
Target has grown its dividend for more than five decades. However, as it had grown its dividend more quickly than its earnings, the company has increased its payout ratio, from 20% in 2009 to 30% this year. Moreover, the company is heavily investing in its business in order to navigate through the changing landscape in the retail sector. Therefore, Target is likely to raise its dividend at a slower pace in the upcoming years, but we see no dividend risk at this point.

Target's competitive advantage comes from its everyday low prices on attractive merchandise in its guest-friendly stores. However, given the price war in the retail sector, Target's moat faces decline. In addition, as consumers tend to curtail their consumption during recessions, the company is vulnerable in such periods. In 2008, its earnings-per-share fell -14%. 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 for the earnings 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. Target is combatting this in part with its massive push towards digital sales channels, which is working.

Final Thoughts & Recommendation

We see Target as modestly overvalued, but given explosive earnings growth in 2020, we see earnings lower for this year. We forecast total returns at 5.5% annually moving forward, and rate Target a hold as a result.

Total Return Breakdown by Year



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Income Statement Metrics

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|-------------------------|--------|--------|--------|---------|--------|--------|--------|--------|--------|--------|
| Revenue | 69,865 | 73,301 | 71,279 | 72,618 | 73,785 | 70,271 | 72,714 | 75,356 | 78,112 | 93,561 |
| Gross Profit | 21,559 | 22,266 | 21,240 | 21,340 | 21,544 | 21,126 | 21,589 | 22,057 | 23,248 | 27,384 |
| Gross Margin | 30.9% | 30.4% | 29.8% | 29.4% | 29.2% | 30.1% | 29.7% | 29.3% | 29.8% | 29.3% |
| SG&A Exp. | 14,106 | 14,643 | 14,465 | 14,676 | 14,665 | 14,217 | 15,140 | 15,723 | 16,233 | 18,615 |
| D&A Exp. | 2,131 | 2,044 | 1,996 | 2,129 | 2,213 | 2,318 | 2,476 | 2,474 | 2,604 | 2,485 |
| Operating Profit | 5,322 | 5,579 | 4,779 | 4,535 | 4,910 | 4,864 | 4,224 | 4,110 | 4,658 | 6,539 |
| Op. Margin | 7.6% | 7.6% | 6.7% | 6.2% | 6.7% | 6.9% | 5.8% | 5.5% | 6.0% | 7.0% |
| Net Profit | 2,929 | 2,999 | 1,971 | (1,636) | 3,363 | 2,734 | 2,914 | 2,937 | 3,281 | 4,368 |
| Net Margin | 4.2% | 4.1% | 2.8% | -2.3% | 4.6% | 3.9% | 4.0% | 3.9% | 4.2% | 4.7% |
| Free Cash Flow | 1,066 | 2,979 | 4,634 | 2,679 | 4,520 | 3,897 | 4,402 | 2,457 | 4,090 | 7,876 |
| Income Tax | 1,527 | 1,741 | 1,427 | 1,204 | 1,602 | 1,295 | 722 | 746 | 921 | 1,178 |

Balance Sheet Metrics

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|-------------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Total Assets | 46,630 | 48,163 | 44,553 | 41,172 | 40,262 | 37,431 | 40,303 | 41,290 | 42,779 | 51,248 |
| Cash & Equivalents | 794 | 784 | 670 | 2,210 | 1,038 | 2,512 | 737 | 787 | 2,577 | 8,511 |
| Acc. Receivable | 5,927 | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Inventories | 7,918 | 7,903 | 8,278 | 8,282 | 8,601 | 8,309 | 8,597 | 9,497 | 8,992 | 10,653 |
| Goodwill & Int. | 242 | 224 | 331 | 298 | 277 | 259 | 709 | 699 | 686 | --- |
| Total Liabilities | 30,809 | 31,605 | 28,322 | 27,175 | 27,305 | 26,478 | 28,652 | 29,993 | 30,946 | 36,808 |
| Accounts Payable | 6,857 | 7,056 | 7,335 | 7,759 | 7,418 | 7,252 | 8,677 | 9,761 | 9,920 | 12,859 |
| Long-Term Debt | 16,483 | 17,648 | 12,572 | 12,725 | 12,760 | 12,749 | 11,398 | 11,275 | 11,499 | 12,680 |
| Total Equity | 15,821 | 16,558 | 16,231 | 13,997 | 12,957 | 10,953 | 11,651 | 11,297 | 11,833 | 14,440 |
| D/E Ratio | 1.04 | 1.07 | 0.77 | 0.91 | 0.98 | 1.16 | 0.98 | 1.00 | 0.97 | 0.88 |

Profitability & Per Share Metrics

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|-------------------------|-------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Return on Assets | 6.5% | 6.3% | 4.3% | -3.8% | 8.3% | 7.0% | 7.5% | 7.2% | 7.8% | 9.3% |
| Return on Equity | 18.7% | 18.5% | 12.0% | -10.8% | 25.0% | 22.9% | 25.8% | 25.6% | 28.4% | 33.3% |
| ROIC | 9.2% | 9.0% | 6.3% | -5.9% | 12.8% | 11.1% | 12.5% | 12.9% | 14.3% | 17.3% |
| Shares Out. | 679 | 657 | 635 | 640 | 633 | 583 | 546 | 524 | 512 | 506 |
| Revenue/Share | 102.2 | 110.51 | 111.06 | 113.45 | 116.58 | 120.64 | 132.14 | 141.33 | 151.50 | 185.12 |
| FCF/Share | 1.56 | 4.49 | 7.22 | 4.19 | 7.14 | 6.69 | 8.00 | 4.61 | 7.93 | 15.58 |

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

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