Carter's, Inc. (CRI)

Updated August 12th, 2023 by Felix Martinez

Key Metrics

Current Price:	$73	**5 Year CAGR Estimate:**	7.3%	**Market Cap:**	$2.73 B
Fair Value Price:	$72	**5 Year Growth Estimate:**	4.0%	**Ex-Dividend Date:**	09/02/2023[1]
% Fair Value:	103%	**5 Year Valuation Multiple Estimate:**	-0.5%	**Dividend Payment Date:**	09/16/2023[2]
Dividend Yield:	4.1%	**5 Year Price Target**	$87	**Years Of Dividend Growth:**	2
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Rating:**	Hold

Overview & Current Events

Carter's, Inc. is the largest branded retailer of apparel exclusively for babies and young children in North America. It was founded in 1865 by William Carter. The company owns the Carter's and OshKosh B'gosh brands, two of the most known brands in the children's apparel space. Carter's acquired competitor OshKosh B'gosh for $312 million in 2005. Now, these brands are sold in leading department stores, national chains, and specialty retailers domestically and internationally. They are also sold through nearly 1,000 company-operated stores in the United States, Canada, and Mexico and on its online websites. The company trades on the stock exchange under the ticker "CRI." Before the COVID-19 pandemic, the company had a dividend growth history of six consecutive years. The company had to cut its dividend by 70% because of the COVID-19 lockdowns. However, the dividend is now higher than the pre-COVID-19 levels. The company trades with a market cap of $2.73 billion.

On July 28th, 2023, the company reported second-quarter results for Fiscal Year (FY)2023. The company witnessed a decline in net sales by $100.5 million, marking a substantial 14.3% decrease from the second quarter of fiscal 2022, largely attributed to adverse macroeconomic factors like inflation, rising interest rates, elevated consumer debt levels, and recession concerns. This unfavorable economic backdrop led to reduced consumer and wholesale demand, resulting in a 15%, 17%, and 8% dip in U.S. Retail, U.S. Wholesale, and international segment net sales, respectively. The adverse effect of foreign currency exchange rates further impacted consolidated net sales by approximately $1.2 million, accounting for a 0.2% decrease.

The operational performance also bore the brunt of these economic challenges. Operating income contracted by $37.9 million, depicting a 50.2% decrease from the second quarter of fiscal 2022. Consequently, the operating margin stood at 6.3%, down from 10.8% in the prior-year period, largely due to lower sales and amplified performance-based compensation. Adjusted operating income mirrored this trend, plummeting by $37.5 million, marking a 49.7% decline, resulting in an adjusted operating margin of 6.3%. Net income for the quarter amounted to $23.9 million, corresponding to an earnings per diluted share of $0.64, down from $37.0 million and $0.93, respectively, in the same quarter of fiscal 2022. Amidst this challenging landscape, the company remains committed to fortifying its market position, enhancing operational efficiencies, and sustaining robust cash flow.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	$3.37	$3.93	$4.61	$5.14	$5.76	$6.29	$6.46	$4.16	$7.87	$6.90	***$5.96***	***$7.25***
DPS	$0.48	$0.76	$0.88	$1.32	$1.48	$1.80	$2.00	$0.60	$1.40	$3.00	***$3.10***	***$3.77***
Shares[3]	54.5	52.7	51.8	48.9	47.2	45.6	43.9	43.8	41.2	37.6	***37.0***	***37.0***

Some of the growth prospects that will drive higher revenue and earnings will be that the company continues to lead in eCommerce. Over the next five years, the company expects eCommerce sales to grow to nearly 50% of its total U.S retail

[1] Ex-Dividend and Dividend Payment dates are estimates.
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[3] Share count is in millions.

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sales. Another growth driver will come from the company's "Age Up" initiative. This initiative focuses on apparel sales for children ages four to 10 years old. This older age apparel market is larger than the combined baby and toddler apparel markets. Over the past ten years, earnings have had a compound annual growth rate of 8.3%. However, we think that a 4% yearly growth rate over the next five years is on the low end but conservative. We also expect that the dividend will grow at the 4% rate over the next five years as well.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	21.1	21.9	19.3	16.8	20.4	13.0	17.1	22.6	12.9	10.8	***12.3***	***12.0***
Avg. Yld.	0.7%	0.9%	1.0%	1.5%	1.3%	2.2%	1.8%	0.6%	1.4%	4.0%	***4.1%***	***4.3%***

The company looks to be slightly overvalued, with a current PE of 12.3x earnings. Over the past ten years, the company's PE has an average of 17.6x earnings; over the past five years, the PE has an average of 15.3x. However, we think that a PE of 12.0x earnings is fair. This would provide an investor with a (0.5)% valuation multiple headwind if the company were to trade at a 12.0x multiple.

Safety, Quality, Competitive Advantage, & Recession Resiliency

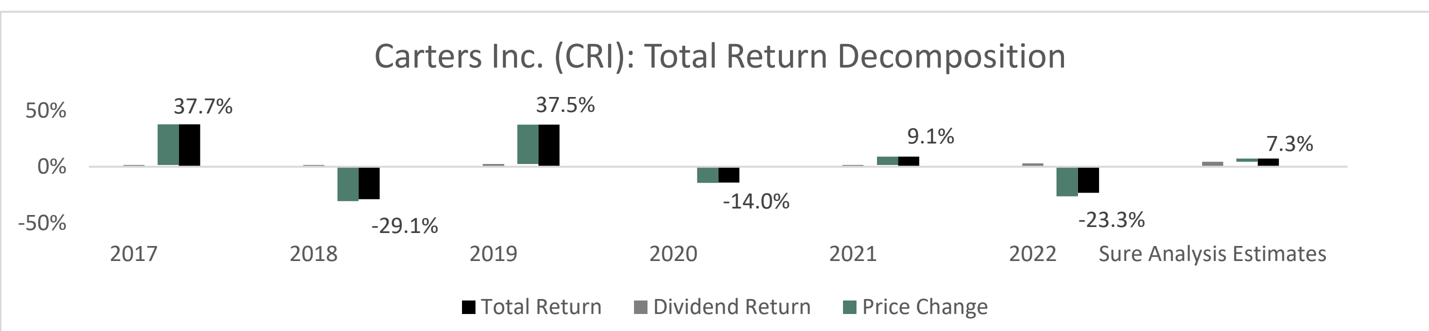
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	14.2%	19.3%	19.1%	25.7%	25.7%	28.6%	31.0%	14.4%	17.8%	43.5%	***52%***	***52%***

Carter's, Inc has a competitive advantage in its brand and its agreement with Target, Walmart, and Amazon to sell exclusive brands in those companies. This allows the company to reach a broad range of consumers worldwide. During the Great Recession, the company's stock price lost about 53% from the end of 2007 to mid-2008. However, earnings fared much better. For example, earnings grew 2% in 2008 and increased 57% in 2009. However, during the COVID-19 pandemic, the company's earnings declined by (36)% in 2020 compared to 2019. However, it rebounded substantially in 2021 by 89%. The company has an S&P credit rating of BB+, not an investment-grade rating. However, the company does have a healthy balance sheet. The company's debt-to-equity ratio is 1.4 and has an interest coverage ratio of 8.4. The dividend is well covered with a current payout ratio of 52%. This gives the company a lot of flexibility for future capital allocation.

Final Thoughts & Recommendation

Carter's, Inc is a well-run company with a history of growing earnings by over 8.3% over the last ten years. The current dividend is attractive and well covered by earnings and free cash flow. We expect the company to have a 7.3% annual rate of return over the next five years at the current price. This will come from the fair valuation and the dividend yield. Thus, we rate the company as a hold at the current price.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	2,639	2,894	3,014	3,199	3,401	3,462	3,519	3,024	3,486	3213
Gross Profit	1,095	1,184	1,258	1,379	1,483	1,497	1,509	1,313	1,662	1472
Gross Margin	41.5%	40.9%	41.7%	43.1%	43.6%	43.3%	42.9%	43.4%	47.7%	45.8%
SG&A Exp.	868	890	909	995	1,107	1,145	1,141	1,106	1,194	1110
D&A Exp.	69	75	68	73	84	90	96	94	94	65
Operating Profit	264	333	393	426	420	391	403	234	497	388
Operating Margin	10.0%	11.5%	13.0%	13.3%	12.3%	11.3%	11.4%	7.7%	14.3%	12.1%
Net Profit	160	195	238	258	303	282	264	110	340	250
Net Margin	6.1%	6.7%	7.9%	8.1%	8.9%	8.1%	7.5%	3.6%	9.7%	7.8%
Free Cash Flow	-11	175	204	281	260	292	326	556	231	48
Income Tax	89	108	130	138	88	74	64	25	99	67

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	1,812	1,893	2,004	1,947	2,071	2,059	2,753	3,393	3,202	2440
Cash & Equivalents	287	341	381	299	178	170	214	1,102	984	212
Accounts Receivable	170	174	185	182	230	244	251	181	234	188
Inventories	418	445	470	488	549	574	594	599	648	745
Goodwill & Int. Ass.	516	499	486	485	644	637	605	557	554	538
Total Liabilities	1,112	1,106	1,129	1,158	1,214	1,189	1,873	2,455	2,252	1643
Accounts Payable	164	150	158	158	182	199	184	472	407	264
Long-Term Debt	586	586	579	580	617	593	595	990	991	617
Shareholder's Equity	701	787	875	788	857	869	880	938	950	796
LTD/E Ratio	0.84	0.74	0.66	0.74	0.72	0.68	0.68	1.05	1.04	0.77

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	9.3%	10.5%	12.2%	13.0%	15.1%	13.7%	11.0%	3.6%	10.3%	8.9%
Return on Equity	19.0%	26.2%	28.6%	31.0%	36.8%	32.7%	30.2%	12.1%	36.0%	28.6%
ROIC	13.1%	14.6%	16.8%	18.3%	21.3%	19.2%	18.0%	6.4%	17.6%	14.9%
Shares Out.	54.5	52.7	51.8	48.9	47.2	45.6	43.9	43.8	41.2	38.85
Revenue/Share	45.87	54.51	57.59	63.49	70.63	74.22	78.72	69.67	81.36	82.69
FCF/Share	-0.19	3.30	3.91	5.57	5.40	6.27	7.29	12.80	5.39	1.24

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