



Kohl's Corporation (KSS)

Updated August 28th, 2023, by Josh Arnold

Key Metrics

Current Price:	\$24	5 Year CAGR Estimate:	8.5%	Market Cap:	\$2.6 B
Fair Value Price:	\$23	5 Year Growth Estimate:	3.0%	Ex-Dividend Date:	09/05/2023
% Fair Value:	107%	5 Year Valuation Multiple Estimate:	-1.3%	Dividend Payment Date:	09/20/2023
Dividend Yield:	8.3%	5 Year Price Target	\$26	Years Of Dividend Growth:	2
Dividend Risk Score:	F	Retirement Suitability Score:	C	Rating:	Hold

Overview & Current Events

Wisconsin-based retailer Kohl's traces its roots back to a single store: Kohl's Department Store in 1962. Since then, it has grown into a leader in the space – offering women's, men's and children's apparel, housewares, accessories, and footwear in more than 1,100 stores in 49 states. The \$2.6 billion market capitalization company should generate about \$17 billion in sales this year.

Kohl's reported second quarter earnings on August 23rd, 2023, and results were better than expected for both revenue and profits. The company posted earnings-per-share of 52 cents, which was 30 cents better than expected. Revenue was off 5% year-over-year at \$3.9 billion, but was \$190 million better than expected. Comparable sales fell 5%, driving the entirety of the revenue decline.

Gross margin was down 61 basis points to 39% of revenue. SG&A costs were up 1.6% year-over-year to \$1.3 billion, or up 208 basis points as a percentage of revenue to 33.5%. The combination of these factors drove lower operating income of \$163 million from \$266 million. As a percentage of revenue, operating income declined sharply, falling from 6.5% to 4.2%.

Net income was \$58 million, down from \$143 million a year ago. Inventory declined 14% year-over-year to \$3.5 billion, while operating cash flow was \$430 million.

The company reiterated its outlook for the year of a net sales decline of 2% to 4%, operating margin of 4.0% of revenue, and diluted earnings-per-share of \$2.10 to \$2.70. We've updated our earnings estimate to \$2.50 per share for this year.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	\$4.05	\$4.24	\$3.46	\$3.11	\$4.19	\$5.60	\$4.86	(\$1.21)	\$7.33	(\$0.15)	\$2.50	\$2.90
DPS	\$1.40	\$1.56	\$1.80	\$2.00	\$2.20	\$2.44	\$2.68	\$0.70	\$1.00	\$2.00	\$2.00	\$2.00
Shares¹	211	201	186	174	168	165	154	154	134	110	100	85

From 2007 through 2018, Kohl's was able to grow earnings-per-share by about 4.7% annually. However, it should be noted that this was driven by the company's extensive share repurchase program. Over that period the share count was nearly halved, a reduction rate of -5.6% per annum. After a sizable uptick in earnings in 2018 (in large part due to a lower tax rate), Kohl's produced a -13% decline in 2019, and earnings declined enormously in 2020 to a sizable loss. We saw the same sort of thing in 2022.

With the share repurchase program back on, and in a big way, we've reduced our share count forecast accordingly. Fears of struggling margins have proven to be right, as 2022 was awful from a margin perspective. We note that 2021's earnings has the potential to be the top for some time. We forecast earnings-per-share at \$2.50 this year as the company is seeing weakened demand come to fruition, and significant margin headwinds. Kohl's capital return program is back in terms of being a sizable draw for the stock. We believe the dividend will remain at its current level of \$2 per

¹ Share count in millions

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share annually for the foreseeable future. We note the sizable reduction in the share count makes it easier for Kohl's to raise the dividend per share, as the number of shares receiving the dividend declines.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	12.7	13.2	17.1	14.1	10.4	11.9	11.3	---	7.4	---	9.6	9.0
Avg. Yld.	2.7%	2.8%	3.1%	4.6%	5.1%	3.7%	4.9%	2.7%	1.9%	7.9%	8.3%	7.7%

Over the past decade, shares of Kohl's have routinely traded hands with an average multiple of nearly 13 times earnings. However, given weak 2022 results and disappointing 2023 guidance, along with declining valuations in the sector, we believe investors will be less willing to pay 13 times earnings or more in the near term. Our fair value estimate stands at 9 times earnings, which is lower than the current multiple of 9.6. The yield is currently 8.3%, and we expect it will decline as the dividend is flat, with a higher share price.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	34%	37%	52%	64%	64%	44%	55%	---	14%	---	80%	69%

We forecast the payout ratio to be 80% of earnings for this year given the level of earnings that we are currently expecting. With modest earnings gains projected from this year's base, the payout ratio should move lower assuming the company doesn't raise the dividend.

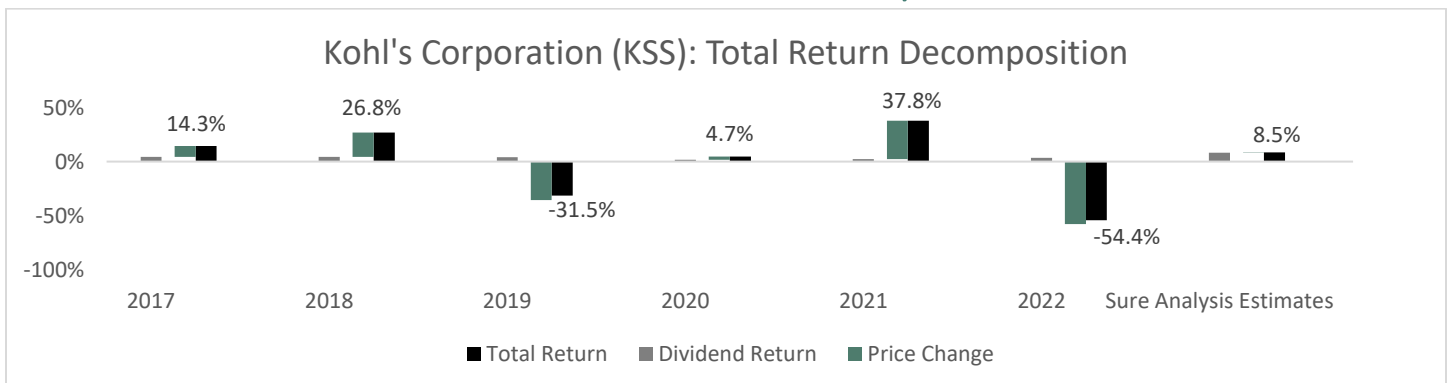
Compared to other retailers we believe Kohl's has a competitive advantage in the way of a well-entrenched store footprint outside of large malls, private-label brands, a large loyalty program, and an Amazon return service. This is offset somewhat by the competitive nature of the business, but it still allows Kohl's to stand out. This focus was a headwind during the COVID recession, but that appears to no longer be the case.

During the Great Recession Kohl's held up quite well, with earnings-per-share of \$3.39, \$2.89, and \$3.23 during the 2007 through 2009 period – representing a decline of just -15% when competitors were faring much worse. Damage was much worse in 2020 as Kohl's posted a sizable loss but the company's earnings recovered quickly.

Final Thoughts & Recommendation

Kohl's projected total returns now stand at 8.5% given updated earnings estimates, so the stock appears attractive still. Returns could be from the 8.3% yield, 1.3% valuation headwind, and 3% growth. We like that Kohl's has reinstated the dividend and share repurchases, but margins remain a significant headwind despite lower inventory balances. Given this, we're downgrading from buy to hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	19,031	19,023	19,204	19,681	20,229	19,974	19,974	15,955	19,433	18,098
Gross Profit	6,944	6,925	6,939	7,737	8,030	7,834	7,834	5,595	7,996	6,641
Gross Margin	36.5%	36.4%	36.1%	39.3%	39.7%	39.2%	39.2%	35.1%	41.1%	36.7%
SG&A Exp.	4,313	4,350	4,452	5,430	5,601	5,705	5,705	5,021	5,478	5,587
D&A Exp.	889	886	934	938	964	917	917	874	838	808
Operating Profit	1,742	1,689	1,553	1,369	1,465	1,212	1,212	(300)	1,680	246
Op. Margin	9.2%	8.9%	8.1%	7.0%	7.2%	6.1%	6.1%	-1.9%	8.6%	1.4%
Net Profit	889	867	673	556	801	691	691	(163)	938	(19)
Net Margin	4.7%	4.6%	3.5%	2.8%	4.0%	3.5%	3.5%	-1.0%	4.8%	-0.1%
Free Cash Flow	1,241	1,342	794	1,385	1,529	802	802	1,004	1,666	(544)
Income Tax	515	482	384	319	241	210	210	(383)	281	(39)

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	14,357	14,333	13,606	13,574	13,389	12,469	14,555	15,337	15,054	14,345
Cash & Equivalents	971	1,407	707	1,074	1,308	934	723	2,271	1,587	153
Inventories	3,874	3,814	4,038	3,795	3,542	3,475	3,537	2,590	3,067	3,189
Total Liabilities	8,379	8,342	8,115	8,397	7,970	6,942	9,105	10,141	10,393	10,582
Accounts Payable	1,365	1,511	1,251	1,507	1,271	1,187	1,206	1,476	1,683	1,330
Long-Term Debt	2,792	2,780	2,792	2,795	2,797	1,861	1,856	2,451	1,910	1,997
Total Equity	5,978	5,991	5,491	5,177	5,419	5,527	5,450	5,196	4,661	3,763
LTD/E Ratio	0.47	0.46	0.51	0.54	0.52	0.34	0.34	0.47	0.41	0.53

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	6.3%	6.0%	4.8%	4.1%	5.9%	5.3%	5.1%	-1.1%	6.2%	-0.1%
Return on Equity	14.8%	14.5%	11.7%	10.4%	15.1%	12.6%	12.6%	-3.1%	19.0%	-0.5%
ROIC	10.3%	9.9%	7.9%	6.8%	9.9%	8.9%	9.4%	-2.2%	13.2%	-0.3%
Shares Out.	211	201	186	174	168	165	154	154	134	120
Revenue/Share	86.50	93.25	98.48	109.95	122.60	126.42	126.42	103.60	131.30	150.82
FCF/Share	5.64	6.58	4.07	7.74	9.27	5.08	5.08	6.52	11.26	-4.53

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

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