

Target Corporation (TGT)

Rating	NEUTRAL
Price (24-Feb-16,US\$)	76.94
Target price (US\$)	72.00
52-week price range	85.01 - 67.59
Market cap (US\$ m)	47,399.01
Enterprise value (US\$ m)	56,113.01

*Stock ratings are relative to the coverage universe in each analyst's or each team's respective sector.

¹Target price is for 12 months.

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EARNINGS

"We Made Progress, but We Have a Lot More to Do."

CS View. TGT announced results moderately better than our expectations, as the company showed strength in their "signature categories" while benefiting from aggressive share repurchase activity. Comps rose +1.9%, driven by traffic growth of +1.3%. Segment operating margins deleveraged 9 bps, driven by lower gross margins. The company's strategy is to aggressively close the gap between digital/e-commerce and brick-and-mortar through investment and promotion. Target is attempting to improve in-store execution through remerchandising efforts in "signature categories" and improve store presentations through visual merchandizing, all aimed at regaining momentum and being viewed as differentiated by the consumer.

Comps up +1.9%, driven by traffic growth of +1.3%. AUR increased +2.0%, and traffic increased +1.3%, offsetting a -1.3% decline in units per transaction. "Signature categories" (apparel, beauty, baby, kids, wellness) outperformed the company with comps of +5.7%. Strongest sub-categories were: toys in kids (+10%), ready-to-wear in apparel (double-digit increase), wearable electronics and food in wellness. E-commerce grew +34% and contributed +130 bps to the comp, while brick & mortar comps rose +0.6%. Inventory growth of +3.9% exceeded sales growth of -0.6%, in part driven by efforts to improve in-stock position. REDcard penetration grew +190 bps y/y to +23.0% from +21.1% in 4Q14. Payables/inventory deleveraged modestly at 86.2% vs. 88.3% in 4Q14.

Share price performance



On 24-Feb-2016 the S&P 500 INDEX closed at 1921.72
Daily Feb24, 2015 - Feb24, 2016, 02/24/15 = US\$76.95

Quarterly EPS	Q1	Q2	Q3	Q4
2015A	0.66	0.76	0.55	1.49
2016E	1.01	1.21	0.76	2.31
2017E	1.21	1.33	0.92	1.76

Financial and valuation metrics

Year	1/14A	1/15A	1/16E	1/17E
EPS (CS adj.) (US\$)	3.07	3.46	5.25	5.21
Prev. EPS (US\$)	-	-	5.22	5.06
P/E (x)	25.0	22.2	14.7	14.8
P/E rel. (%)		134.7	91.2	104.1
Revenue (US\$ m)	72,596.4	73,940.0	73,785.0	70,244.3
EBITDA (US\$ m)	6,062.7	6,227.0	7,123.0	7,645.5
OCFPS (US\$)	7.08	1.80	9.21	10.48
P/OCF (x)	8.0	40.9	8.4	7.3
EV/EBITDA (current)	9.6	9.3	8.1	7.6
Net debt (US\$ m)	13,087	10,586	8,714	8,714
ROIC (%)	7.63	10.53	14.22	15.93
Number of shares (m)	616.05	IC (current, US\$ m)		24,583.00
Net debt (Next Qtr., US\$ m)	9,998.0	EV/IC (x)		2.4
Net debt/tot eq (Next Qtr.,%)	70.5	Dividend (current, US\$)		8.43

Source: Company data, Thomson Reuters, Credit Suisse estimates

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Operating margins deleveraged 10 bps, driven by lower gross margins. Gross margins deleveraged -56 bps y/y, with the benefit from divesting the lower margin pharmacy business, offset by increased promotions. TGT no longer faces easier year-on-year gross margin comparisons from the promotions necessary to generate sales following the 4Q13 data breach. This was partially offset by better SG&A, which decreased \$137 mn in part due to programs put in practice at the beginning of the year as well as partial impact of the pharmacy sale to CVS. SG&A also included \$1 mn incremental contribution from credit card profit-sharing income.

Estimates. We adjust our FY16 EPS estimate to \$5.21 from \$5.03. We maintain our target price of \$72.

Companies Mentioned (Price as of 24-Feb-2016)

CVS Health (CVS.N, \$96.88)
Target Corporation (TGT.N, \$76.94, NEUTRAL, TP \$72.0)

Disclosure Appendix

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3-Year Price and Rating History for Target Corporation (TGT.N)

TGT.N	Closing Price	Target Price	
Date	(US\$)	(US\$)	Rating
27-Feb-13	63.12	62.00	N
23-Jan-14	58.65	55.00	
19-Nov-14	72.50	63.00	
16-Jan-15	74.94	72.00	

* Asterisk signifies initiation or assumption of coverage.



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Target Price and Rating

Valuation Methodology and Risks: (12 months) for Target Corporation (TGT.N)

Method: Our \$72 price target for Target is based on an 8.5x EV/EBITDA multiple on our 2015 estimate. This reflects TGT's historical slight discount to WMT, which trades at 8.8x our '15 EV/EBITDA. We believe a discount is warranted given the significant time and resources necessary for Target's operational turnaround. The stock is trading within a narrow range of its price target, and accordingly, we have a Neutral rating.

Risk: Risks to our \$72 target price for Target include pressure on selling and administrative costs including payroll and healthcare costs, mix shift towards lower margin e-commerce business, and Wal-Mart's aggressive pricing strategy. All of these risks could imply further downside to the stock, which would negatively impact our price target and/or Neutral rating.

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