Aarons, Inc. (AAN)

$59.20 (As of 08/12/20)

Price Target (6-12 Months): **$68.00**

Long Term: 6-12 Months | **Zacks Recommendation:** **Outperform**

(Since: 07/13/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months | **Zacks Rank:** (1-5) **1-Strong Buy**

Zacks Style Scores: VGM:A

Value: A | Growth: B | Momentum: D

Summary

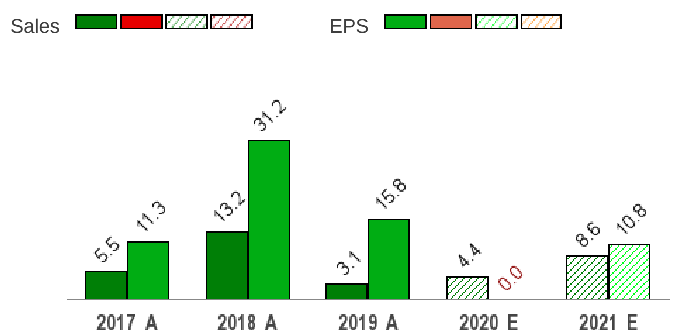
Shares of Aaron's outpaced the industry in the past three months, following its solid second-quarter 2020 results. Notably, the company's earnings surpassed the Zacks Consensus Estimate for the third straight quarter. Solid performance of the Progressive segment, driven by strong invoice growth, operating cost management and sturdy customer payment activity, also contributed to quarterly results. Further, it continued to witness robust e-commerce growth in the second quarter. Also, transformation initiatives, including store fleet optimization, omni-channel expansion and investment in loyalty program bode well. However, management withdrew its guidance for 2020, citing the unprecedented impacts of the coronavirus outbreak. Also, weakness in Aaron's business unit and soft revenues from its franchisee stores remain concerns.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$78.59 - $13.01**
20 Day Average Volume (sh)	**964,841**
Market Cap	**$4.0 B**
YTD Price Change	**3.7%**
Beta	**1.64**
Dividend / Div Yld	**$0.16 / 0.3%**
Industry	**Retail - Consumer Electronics**
Zacks Industry Rank	**Top 38% (97 out of 253)**
Last EPS Surprise	**43.9%**
Last Sales Surprise	**4.7%**
EPS F1 Est- 4 week change	**19.0%**
Expected Report Date	**11/02/2020**
Earnings ESP	**5.3%**
P/E TTM	**15.1**
P/E F1	**15.3**
PEG F1	**0.9**
P/S TTM	**1.0**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2021	1,182 E	1,134 E	1,067 E	1,121 E	4,478 E
2020	1,101 A	1,030 A	965 E	1,023 E	4,122 E
2019	1,012 A	968 A	964 A	1,004 A	3,948 A

EPS Estimates

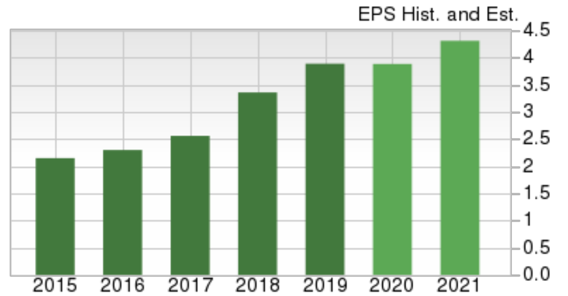
	Q1	Q2	Q3	Q4	Annual*
2021	$1.05 E	$1.08 E	$0.87 E	$1.18 E	$4.31 E
2020	$0.85 A	$1.18 A	$0.82 E	$1.05 E	$3.89 E
2019	$1.08 A	$0.93 A	$0.73 A	$1.15 A	$3.89 A

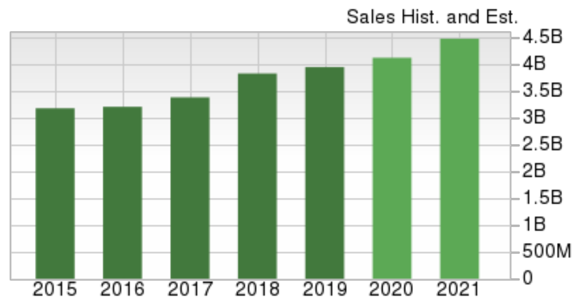
*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/12/2020. The reports text is as of 08/13/2020.

Overview

Based in Atlanta, GA, Aaron's, Inc. is a major omni-channel provider of lease-purchase solutions, mainly to underserved and credit-challenged customers. Through its various business segments, the company primarily deals in sales and lease ownership, apart from specialty retailing in furniture, home appliances, consumer electronics, as well as accessories.





Furthermore, the company has three operating and reportable segments: Progressive Leasing, Aaron's Business, and DAMI.

- **Progressive Leasing (accounting for 53.9% of total revenues in 2019):** This segment includes the virtual lease-to-own business. It partners with various retailers, mainly in the furniture and bedding; electronics and accessories; mobile; jewelry; consumer electronics; automobile; as well as appliance industries to provide a lease-purchase option for credit-challenged customers. Progressive Leasing had retail partners across 46 states and the District of Columbia.

- **Aaron's Business (45.2%):** This segment centers on around Aaron's branded company-owned and franchised lease-to-own stores, Aarons.com and Woodhaven, the company's furniture manufacturing facilities. Additionally, this operating unit supports franchisees of its Aaron's stores.

As of Jun 30, 2020, the Aaron's Business segment had 1,098 company-operated stores and 316 franchised stores.

- **Dent-A-Med, Inc. — DAMI** (0.9%): Acquired in 2015, the DAMI segment mainly serves customers that are not eligible for traditional prime lending. It operates as a wholly-owned subsidiary of Progressive Leasing and provides customized programs including revolving loans, private label cards and access to the processing platform.

Reasons To Buy:

Aaron's Q2 results were driven by strong invoice growth, operating cost management and sturdy customer payment activity. Revenues grew 14.2% year over year in second-quarter 2020.

- **Solid Q2 Results**: Shares of Aaron's surged 82.4% in the past three months outperforming the industry's growth of 41.4%. The stock received a boost following its better-than-expected results for second-quarter 2020, wherein both the top and bottom lines grew year over year. Solid performance of the Progressive segment, driven by strong invoice growth, operating cost management and sturdy customer payment activity, also contributed to quarterly results. Further, the company's earnings surpassed the Zacks Consensus Estimate for the third straight quarter. Going ahead, management issued a third-quarter view, wherein it anticipates revenues of $950-$975 million and adjusted earnings of 80-90 cents per share. However, Aaron's withdrew its 2020 guidance, citing unprecedented impacts ofthe outbreak.

- **Robust Progressive Business Performance**: Aaron's has been experiencing continued strength in its Progressive segment, which covers the virtual lease-to-own business. The segment has been performing exceedingly well for quite some time now, backed by robust growth in invoice volume and a solid customer base. In second-quarter 2020, the segment's revenues increased 14.2% year over year. Although invoice volumes fell 2.2%, invoice volume per active door rose 1.7%. Further, the segment's EBITDA was $70.7 million, up 3.7% from the year-ago quarter.

- **Financial Flexibility**:Aaron's boasts a healthy balance sheet, which enables it to invest in the business and reward shareholders. As of Jun 30, 2020, the company had cash and cash equivalents of $313.1 million compared with $57.8 million as of Dec 31, 2019. Aaron's total debt of $285.8 million as of Jun 30 grew 6.2% on a sequential basis. Its debt-to-capitalization ratio of 0.16 represents a significant sequential decrease from 0.31. Moreover, the debt-to-capitalization ratio compares favorably with the industry's ratio of 0.56. Also, management boasts $800-million liquidity as of Jun 30, which is likely to help it stay afloat amid this crisis.

- **Shareholder Returns**: Aaron's financial position helps it to make capital investments alongside returning excess cash to shareholders via dividends and share buybacks. During the second quarter, the company did not repurchase shares but paid out dividends worth $5.4 million. This clearly underscores the company's commitment toward rewarding shareholders. Moreover, management declared quarterly cash dividend of 4 cents, payable on Jul 7. Notably, Aaron's has a dividend payout ratio of 0.3%, annualized dividend yield of 14.3% and free cash flow yield of 12.1%.

- **Aaron's Business Transformation on Track**: The Aaron's business is progressing well with its transformational initiatives over the past few years. These initiatives are likely to bring the segment back to sustainable long-term growth in revenue and earnings, through investments in activities to improve customer experience, operating efficiencies, compliance and employee engagement. Additionally, the company's e-commerce site (Aarons.com) has witnessed significant growth in the past few years and is attracting new and younger customers. The company continued to witness e-commerce growth in the second quarter, as only online business remained operational amid the coronavirus outbreak.

Risks

- **Soft Aaron's Business**: The Aaron's Business segment has been grappling with soft conditions for a while now. Total revenues at the Aaron's Business segment fell 2.8% to $431 million, mainly due to a net reduction of 185 outlets in the 15 months ended Jun 30, and a lower lease portfolio balance impact and temporary store closures stemming from the COVID-19 pandemic. This was somewhat offset by robust customer payment activities. Moreover, same-store revenues rose 1.4%, while customer count on a same-store basis dropped 6.5%. Non-retail sales decreased 3.2% on a year-over-year basis. Lease revenues and fees for the three months ended Jun 30 declined 2.8% from the year-ago quarter. At the quarter-end, the company-operated Aaron's stores had 898,000 customers, reflecting an 8.7% year-over-year drop. Persistent decline in this segment may be a threat to the company's top line.

- **Decline in Franchisee Revenues**: During second-quarter 2020, Aaron's franchisee revenues declined 3.5% to $104.2 million. Same-store revenues for franchised stores increased 6.6% and same-store customer counts dropped 7.6% in the reported quarter. Notably, the company's franchisees had a customer base of 216,000 at the end of the quarter.

- **Intense Competition**: Aaron's faces stiff competition from a diverse group of competitors including national, regional and local providers of lease-to-own stores, virtual lease-to-own operators, traditional and e-commerce players, as well as consumer finance companies. In addition, the company competes with retail stores for customers purchasing merchandise for cash or on credit. A challenging retail landscape, aggressive promotional strategies and waning store traffic might hurt Aaron's performance. This may adversely affect both top and bottom-line performances.

- **Dropping Consumer Sentiment May Impact Sales**: Any dropping consumer confidence – a key determinant of the economy's health – may have serious bearing on spending. The company's customers remain sensitive to macroeconomic factors, including unemployment levels and high household debt levels, which may negatively impact their sentiments. For now, the novel coronavirus has wreaked havoc. The retail sector, in particular, remains under pressure. Again, job losses as well as lower disposable income due to this catastrophe are making things worse. Consumers are avoiding discretionary spending and focusing on necessities for the time being.

Last Earnings Report

Aaron's Earnings & Revenues Surpass Estimates in Q2

Quarter Ending	06/2020
Report Date	**Jul 29, 2020**
Sales Surprise	**4.67%**
EPS Surprise	**43.90%**
Quarterly EPS	**1.18**
Annual EPS (TTM)	**3.91**

Aaron's better-than-expected results for second-quarter 2020. Both top and bottom lines grew year over year. Solid performance of the Progressive segment, driven by strong invoice growth, operating cost management and sturdy customer payment activity, also contributed to quarterly results.

Q2 Highlights

Aaron's delivered adjusted earnings of $1.18 per share, which surpassed the Zacks Consensus Estimate of 82 cents. Further, the metric advanced 26.9% from the prior-year quarter's reported figure.

Reported earnings per share were $1.01 on a GAAP basis, up 62.9% year over year from 62 cents reported in the year-ago quarter.

Consolidated revenues rose 6.4% to $1,030.1 million and surpassed the Zacks Consensus Estimate of $984 million. Revenue growth was mainly backed by an increase in Progressive revenues, partly offset by soft revenues at the Aaron's Business segment.

Aaron's franchisee revenues declined 3.5% to $104.2 million. Same-store revenues for franchised stores increased 6.6% and same-store customer counts dropped 7.6% in the reported quarter. Notably, the company's franchisees had a customer base of 216,000 at the end of the quarter.

Adjusted EBITDA grew 20.9% year over year to $129.8 million, with adjusted EBITDA margin expanding 150 basis points (bps) to 12.6% in the reported quarter.

Segment Details

Progressive Leasing

Revenues at the segment grew 14.2% to $589.7 million in the reported quarter. Moreover, invoice volumes fell 2.2% due to a 1.7% rise in invoice volume per active door and a 3.9% decrease in active doors to roughly 19,000. As of Jun 30, 2020, the division had 902,000 customers, reflecting a 0.8% decline year over year.

The segment's EBITDA was $70.7 million, up 3.7% from the year-ago quarter. However, EBITDA margin contracted 120 bps to 12%.

Aaron's Business

Total revenues at the Aaron's Business segment fell 2.8% to $431 million, mainly due to net reduction of 185 outlets in the 15 months ended Jun 30, and lower lease portfolio balance impact and temporary store closures stemming from the COVID-19 pandemic. This was somewhat offset by robust customer payment activities. Moreover, same-store revenues rose 1.4%, while customer count on a same-store basis dropped 6.5%.

Non-retail sales decreased 3.2% on a year-over-year basis. Lease revenues and fees for the three months ended Jun 30 declined 2.8% from the year-ago quarter. At the quarter-end, the company-operated Aaron's stores had 898,000 customers, reflecting an 8.7% year-over-year drop.

The segment's adjusted EBITDA was $57.1 million, up 44% year over year on the back of enhanced merchandise write-offs, reduced SG&A expenses and solid customer payment activity, which somewhat offset adverse impacts from lower portfolio balance and temporary store closures as a result of coronavirus. Also, adjusted EBITDA margin expanded 420 bps to 13.2%.

As of Jun 30, 2020, Aaron's Business had 1,098 company-operated stores and 316 franchised stores.

Vive

Sales at the Vive segment, formerly known as Dent-A-Med, Inc., amounted to $9.4 million in the quarter under review.

Financial Position

The company ended the quarter with cash and cash equivalents of $313.1 million, debt of $285.8 million and shareholders' equity of $1,521.2 million. As of Jun 30, 2020, the company generated cash from operations of $360.8 million.

During the quarter, the company did not repurchase shares but paid out dividends of $5.4 million. Also, the company has roughly $800-million liquidity as of Jun 30, which is likely to help it stay afloat amid this crisis.

Outlook

Going ahead, management issued a third-quarter view. Notably, it anticipates revenues of $950-$975 million and adjusted earnings of 80-90 cents per share.

Recent News

Aaron's Approve Quarterly Dividend - Aug 6, 2020

Aaron's board has approved a dividend of 4 cents per share to be payable on Oct 6, 2020 as of shareholders record on Sep 17.

Aaron’s Plans to Split Into Two Public Companies – Jul 29, 2020

Aaron’s announced plans to split into two independent, publicly-traded companies namely Progressive Leasing and the Aaron's Business. This deal is anticipated to be concluded by the end of this year provided certain closing conditions are fulfilled.

Aaron's Issues Upbeat Second-Quarter View Amid Coronavirus - Jun 8, 2020

Aaron’s announced encouraging second-quarter 2020 guidance, which includes the disruptions caused by the pandemic. Notably, revenues are forecasted between $975 million and $1 billion in the second quarter. Adjusted earnings are also envisioned to be 80-85 cents per share, whose midpoint of 82.5 cents comes way above the Zacks Consensus Estimate of 43 cents. Management expects revenues and earnings in the third and fourth quarters to be significantly better sequentially, driven by the improving trajectory of its lease origination activity.

With Progressive's retail partners reopening their stores, invoice volumes are showing signs of improvement. Going ahead, management expects this trend to continue. In fact, invoice volumes are envisioned to be flat to down low-single digits during the second quarter. The company also noted that the segment will not incur any costs related to COVID-19 in the said quarter.

Further, revenues in the Aaron’s segment are projected to decline 15% year over year due to COVID-19 impacts realized in April 2020. Same-store revenues are anticipated to be down 1.5-2.5%. Also, it highlighted that write-offs related to COVID-19 are likely to improve by almost 100 basis points (bps) year over year in the second quarter. This reflects a significant rise on a sequential basis. Apart from these, no charges associated with COVID-19 will be incurred in the second quarter.

Aaron's Join Hands With Rooms To Go to Offer PPE Amid Coronavirus Crisis - May 28, 2020

Aaron's has partnered with Rooms To Go for offering Personal Protective Equipment (PPE) to Grady Health System given the recent cornavirus outbreak. These PPEs will be used by the Atlanta medical facilities which have been affected by the ongoing pandemic.

Valuation

Aaron's shares are up 2.5% in the year-to-date period but down 8.4% for the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Retail-Wholesale sector are up 27.9% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and the sector are up 26.5% and 42.4%, respectively.

The S&P 500 index is up 4.8% in the year-to-date period and 19.1% in the past year.

The stock is currently trading at 14.27X forward 12-month earnings, which compares to 23.03X for the Zacks sub-industry, 33.03X for the Zacks sector and 22.6X for the S&P 500 index.

Over the past five years, the stock has traded as high as 18.17X and as low as 3.79X, with a 5-year median of 12.87X. Our Outperform recommendation indicates that the stock will perform better than the market. Our $68 price target reflects 16.39X forward 12-month earnings.

The table below shows summary valuation data for AAN

Valuation Multiples - AAN

		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	14.27	23.03	33.03	22.6
	5-Year High	18.17	23.03	34.76	22.62
	5-Year Low	3.79	8.32	19.08	15.25
	5-Year Median	12.87	11.53	23.46	17.58
P/S F12M	Current	0.92	0.48	1.23	3.65
	5-Year High	1.21	0.48	1.24	3.65
	5-Year Low	0.23	0.21	0.82	2.53
	5-Year Median	0.77	0.31	0.97	3.05
EV/EBITDA TTM	Current	1.61	5.87	19.36	12.55
	5-Year High	2.32	5.87	19.75	12.84
	5-Year Low	0.53	2.72	11.13	8.24
	5-Year Median	1.71	4.13	12.94	10.9

As of 08/12/2020

Industry Analysis **Zacks Industry Rank:** Top 38% (97 out of 253)

Top Peers

Company (Ticker)	Rec	Rank
Best Buy Co., Inc. **(BBY)**	Outperform	2
RentACenter, Inc. **(RCII)**	Outperform	1
Systemax Inc. **(SYX)**	Outperform	2
Conns, Inc. **(CONN)**	Neutral	4
GameStop Corp. **(GME)**	Neutral	4
RH **(RH)**	Neutral	3
Vivint Smart Home, Inc. **(VVNT)**	Neutral	4
Walmart Inc. **(WMT)**	Neutral	4

Industry Comparison Industry: Retail - Consumer Electronics

	AAN	X Industry	S&P 500	CONN	GME	SYX
				Industry Peers		
Zacks Recommendation (Long Term)	Outperform	-	-	Neutral	Neutral	Outperform
Zacks Rank (Short Term)	1	-	-	4	4	2
VGM Score	A	-	-	A	F	A
Market Cap	3.97 B	873.03 M	23.75 B	325.32 M	292.71 M	873.03 M
# of Analysts	6	4.5	14	4	5	1
Dividend Yield	0.27%	0.00%	1.68%	0.00%	0.00%	2.40%
Value Score	A	-	-	B	F	A
Cash/Price	0.09	0.25	0.07	1.13	2.12	0.07
EV/EBITDA	1.80	7.73	13.35	7.19	-0.74	12.42
PEG Ratio	0.91	1.67	2.98	NA	NA	NA
Price/Book (P/B)	2.61	1.43	3.20	0.66	0.67	5.87
Price/Cash Flow (P/CF)	1.68	9.81	12.97	2.41	2.58	16.16
P/E (F1)	15.06	17.38	22.17	NA	NA	17.38
Price/Sales (P/S)	0.97	0.78	2.54	0.22	0.05	0.93
Earnings Yield	6.55%	-4.12%	4.31%	-19.00%	-33.19%	5.75%
Debt/Equity	0.19	0.29	0.77	3.08	1.14	0.39
Cash Flow ($/share)	35.14	1.44	6.94	4.65	1.75	1.44
Growth Score	B	-	-	B	C	B
Hist. EPS Growth (3-5 yrs)	16.56%	21.61%	10.41%	35.73%	-26.21%	40.36%
Proj. EPS Growth (F1/F0)	-0.13%	2.16%	-6.32%	-211.07%	-783.64%	-3.60%
Curr. Cash Flow Growth	13.84%	-20.22%	5.22%	8.16%	-66.61%	5.05%
Hist. Cash Flow Growth (3-5 yrs)	15.48%	10.50%	8.55%	9.76%	-26.81%	49.91%
Current Ratio	3.04	1.34	1.33	6.46	0.93	1.65
Debt/Capital	15.82%	21.82%	44.59%	75.51%	53.17%	27.82%
Net Margin	-6.80%	1.14%	10.13%	-1.06%	-10.83%	5.22%
Return on Equity	16.23%	5.24%	14.59%	-1.78%	-14.93%	31.03%
Sales/Assets	1.32	1.70	0.51	0.69	2.08	2.41
Proj. Sales Growth (F1/F0)	4.43%	0.00%	-1.40%	-6.13%	-11.04%	2.55%
Momentum Score	D	-	-	D	B	B
Daily Price Chg	3.39%	0.43%	0.67%	-3.98%	3.91%	0.43%
1 Week Price Chg	4.68%	4.60%	2.30%	10.74%	3.74%	4.60%
4 Week Price Chg	31.85%	9.39%	4.87%	9.58%	7.88%	17.57%
12 Week Price Chg	75.36%	22.92%	13.54%	79.36%	2.03%	17.09%
52 Week Price Chg	-7.28%	-7.28%	6.06%	-43.21%	36.15%	16.22%
20 Day Average Volume	964,841	145,050	2,006,991	323,456	3,354,877	86,922
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	18.99%	8.44%	1.95%	-5.78%	0.00%	21.82%
(F1) EPS Est 12 week change	49.14%	13.92%	2.72%	-344.27%	-125.15%	21.82%
(Q1) EPS Est Mthly Chg	50.09%	15.13%	0.84%	-52.38%	0.00%	37.93%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	A
Growth Score	B
Momentum Score	D
VGM Score	A

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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