Aarons, Inc. (AAN)

$42.70 (As of 02/25/20)

Price Target (6-12 Months): **$36.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 02/24/20) Prior Recommendation: Neutral	**Underperform**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**4-Sell**
	Zacks Style Scores:	VGM:B
	Value: B | Growth: C | Momentum: D	

Summary

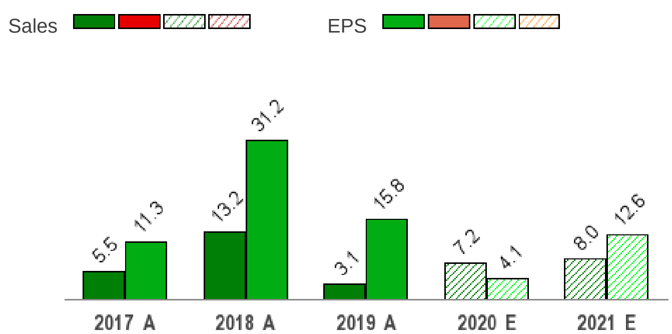
Shares of Aaron's have underperformed the industry in the past three months. Aaron's Business segment has been grappling with soft conditions for a while now. Also, the company has been witnessing a decline in franchisee revenues. Further, management provided muted view for 2020. It expects EBITDA margin in 2020 to be lower than 2019. The company expects the business to face challenges due to lower portfolio size and continued pressure from consumer electronics. Moreover, stiff competition remains a concern. Nevertheless, its top and bottom lines improved year over year in the fourth quarter. Strength in the Progressive segment on robust invoice volume and solid customer base is aiding top-line growth. In addition, the company is on track with transformational initiatives to bring Aaron's business back on sustainable growth track.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$78.59 - $40.79**
20 Day Average Volume (sh)	**1,171,132**
Market Cap	**$2.9 B**
YTD Price Change	**-25.2%**
Beta	**0.39**
Dividend / Div Yld	**$0.16 / 0.4%**
Industry	**Retail - Consumer Electronics**
Zacks Industry Rank	**Bottom 9% (232 out of 255)**
Last EPS Surprise	**8.5%**
Last Sales Surprise	**-0.4%**
EPS F1 Est- 4 week change	**-12.3%**
Expected Report Date	**04/23/2020**
Earnings ESP	**-5.1%**
P/E TTM	**11.0**
P/E F1	**10.5**
PEG F1	**0.6**
P/S TTM	**0.7**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2021	1,155 E	1,135 E	1,142 E	1,175 E	4,572 E
2020	1,053 E	1,055 E	1,061 E	1,091 E	4,233 E
2019	1,012 A	968 A	964 A	1,004 A	3,948 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	$1.08 E	$0.96 E	$1.09 E	$1.36 E	$4.56 E
2020	$0.85 E	$0.92 E	$0.94 E	$1.27 E	$4.05 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 02/25/2020. The reports text is as of 02/26/2020.

Overview

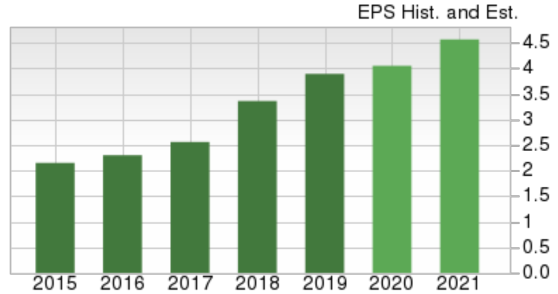
Based in Atlanta, GA, Aaron's, Inc. is a major omni-channel provider of lease-purchase solutions, mainly to underserved and credit-challenged customers. Through its various business segments, the company primarily deals in sales and lease ownership, apart from specialty retailing in furniture, home appliances,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

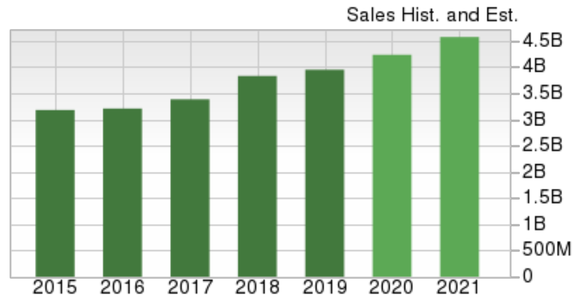
Additionally, Aaron's stores offers products from popular brands like Philips, Samsung, Whirlpool, Hewlett-Packard, LG, Simmons, and Ashley, among others.

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.

  As of Dec 31, 2019, the division had 1,072,000 customers, reflecting 22.4% year-over-year growth.





- **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 Dec 31, 2019, the Aaron's Business segment had 1,167 company-operated stores and 335 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 Sell:

Soft Aaron's Business: The Aaron's Business segment has been grappling with soft conditions for a while now. This segment's total revenues fell 5.4% in the fourth quarter on lack of revenues from net closure of 145 stores in 2019, and revenue attrition from prior-year store mergers and lower collections. This was partly offset by gains from contributions from the buyout of 152 franchised locations. Customer count declined 4.8% year over year. Non-retail sales tumbled 30.8% on a year-over-year basis. Also, lease revenues and fees in the fourth quarter decreased 1.2% from the year-ago quarter. At the quarter-end, company-operated Aaron's stores had 946,000 customers, reflecting an 8.9% year-over-year decrease. Persistent decline in this segment may be a threat to the company's top line. Shares of Aaron's have lost 28.3% in the past three months, wider than the industry's 12.1% decline.

Although Aaron's business is progressing well with its transformational initiatives, it continues to grapple with soft trends. Revenues for the segment declined 5.4% in the fourth quarter.

Decline Franchised Stores: Aaron's franchisee revenues declined 13.5% from the prior-year quarter to $101.2 million. Also, same-store revenues for franchised stores decreased 1.2% year over year and same-store customer counts dipped 4.9% in the reported quarter. Notably, the company's franchisees had a customer base of 239,000 at the end of the quarter.

Muted Projection: Management provided guidance for 2020, which was lower than analyst expectations. The company projects 2020 total revenues within $4,150-$4,300 million and adjusted earnings in the range of $3.80-$4.00 per share. Although sales and earnings indicate year-over-year improvement, the projections are lower than analysts' expectation. Aaron's expects EBITDA margin in 2020 to be lower than 2019 but within the long-term annual targeted range of 11-13% of revenues. The decline in EBITDA margin can be primarily due to pressure on gross margin from a rapid acceleration in invoice growth and the resulting younger portfolio, which is expected to increase 90-day buyout activity in first-half 2020. For 2020, the company projects adjusted EBITDA within $430-$458 million. It expects the business to be challenged by lower portfolio size and continued pressure from consumer electronics.

Intense Competition to Weigh on Results: 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.

Risks

- **Solid Q4 Results:** Aaron's reported robust fourth-quarter 2019 results, wherein both the top and bottom lines improved year over year. The company's earnings surpassed the Zacks Consensus Estimate, after missing the same in the preceding quarter. Also, the top line registered growth, when calculated on the basis of the 2019 adoption of ASC 842 associated with lease accounting. Revenue growth was backed by an increase in Progressive revenues and contributions from franchised stores acquired by the Aaron's Business segment. Moreover, the company's adjusted EBITDA rose 11.1% year over year, owing to robust growth at the Progressive segment. Adjusted EBITDA margin was up 30 basis points (bps) to 12.5%, when calculated on the basis of the 2019 adoption of ASC 842.

- **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 fourth-quarter 2019, the segment's revenues increased 6.7% year over year. Invoice volume rose 34.4%, owing to a 23.3% rise in invoice volume per active door and 9% increase in active doors to roughly 22,000. As of Dec 31, 2019, the division had 1,072,000 customers, reflecting 22.4% year-over-year growth. Further, the segment's EBITDA grew 17.6% in the reported quarter. For 2020, the company expects revenues within $2,540-$2,635 million and adjusted EBITDA in the range of $310-$325 million for the segment.

- **Solid Cash Position & Shareholder-Friendly Moves:** Aaron's boasts a healthy balance sheet, which enables it to invest in the business and reward shareholders. As of Dec 31, 2019, the company had cash and cash equivalents of $57.8 million compared with $15.3 million in the corresponding period of 2018. As of Dec 31, 2019, it generated cash from operations of $317.2 million. In 2019, the company returned $78.7 million related to the purchase of 1,156,000 common shares at $59.90 per share and $9.4 million in dividends. It ended fourth-quarter 2019 with available liquidity of $444 million and net debt to adjusted EBITDA ratio of 0.65. In 2019, Aaron's repurchased 513,900 shares for $29.8 million. Moreover, the company expects capital expenditure within $90-$100 million for 2020.

- **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.

Last Earnings Report

Aaron's Q4 Earnings & Sales Beat, Muted View

Quarter Ending	12/2019
Report Date	**Feb 20, 2020**
Sales Surprise	**-0.44%**
EPS Surprise	**8.49%**
Quarterly EPS	**1.15**
Annual EPS (TTM)	**3.89**

Aaron's reported robust fourth-quarter 2019 results, wherein both the top and bottom lines improved year over year. The company's earnings surpassed the Zacks Consensus Estimate, after missing the same in the preceding quarter. Meanwhile, sales marginally missed the consensus mark. However, the solid performance was not enough to appease investors, who seem to be let down by the 2020 outlook, which was lower than analysts' expectations.

Q4 Highlights

Aaron's reported adjusted earnings of $1.15 per share, which surpassed the Zacks Consensus Estimate of $1.06. Moreover, the metric rose 12.7% from the prior-year quarter.

Including one-time items, the company reported loss per share of $1.60 on a GAAP basis against earnings of 89 cents reported in the year-ago quarter.

Consolidated revenues inched up 1% year over year to $1003.6 million but missed the Zacks Consensus Estimate of $1008 million. The top line grew 8.4% when calculated on the basis of the 2019 adoption of ASC 842 associated with lease accounting. The revenue growth was backed by an increase in Progressive revenues and contributions from franchised stores acquired by the Aaron's Business segment. This was partly offset by the company's store closures in 2019.

Aaron's franchisee revenues declined 13.5% from the year-ago quarter to $101.2 million. However, same-store revenues for franchised stores decreased 1.2% and same-store customer counts dipped 4.9% in the reported quarter. Notably, the company's franchisees had a customer base of 239,000 at the end of the quarter.

Adjusted EBITDA rose 11.1% year over year to $125.2 million, owing to robust growth at the Progressive segment. Adjusted EBITDA margin was up 30 bps to 12.5%, when calculated on the basis of the 2019 adoption of ASC 842.

Segment Details

Progressive Leasing

Revenues at the segment grew 6.7% year over year to $559.5 million in the reported quarter. Invoice volume rose 34.4% from the prior-year period, owing to a 23.3% rise in invoice volume per active door and a 9% increase in active doors to roughly 22,000. As of Dec 31, 2019, the division had 1,072,000 customers, reflecting 22.4% year-over-year growth.

The segment's EBITDA was $77.1 million, up 17.6% from the year-ago quarter. Further, EBITDA margin contracted 50 bps to 13.8%.

Aaron's Business

Total revenues at the Aaron's Business segment fell 5.4% from the year-ago period to $435 million, thanks to lack of revenues from net closure of 145 stores in 2019, and revenue attrition from prior-year store mergers and lower collections. This was partly offset by gains from contributions from the buyout of 152 franchised locations. Moreover, same-store revenues inched up 0.4%, while customer count declined 4.8% from the prior-year level.

Non-retail sales tumbled 30.8% on a year-over-year basis. Lease revenues and fees for the three months ended Dec 31, 2019 decreased 1.2% from the comparable year-ago period. At the quarter-end, company-operated Aaron's stores had 946,000 customers, reflecting an 8.9% year-over-year decrease.

The segment's adjusted EBITDA was $49.3 million, up 3.6% year over year, driven by recovery in collections performance, expense management and gains from real estate sales. Also, adjusted EBITDA margin expanded 90 bps to 11.3%.

As of Dec 31, 2019, the Aaron's Business segment had 1,167 company-operated stores and 335 franchised stores.

Vive

Sales at the Vive segment, formerly known was Dent-A-Med, Inc. (DAMI), amounted to $9.1 million, in line with the year-ago period.

Financial Position

The company ended the quarter with cash and cash equivalents of $57.8 million, debt of $341 million, and shareholders' equity of $1,737.3 million. As of Dec 31, 2019, the company generated cash from operations of $317.2 million.

Moreover, it repurchased 513,900 shares for $29.8 million in 2019. The company expects capital expenditure within $90-$100 million for 2020.

Guidance

Management provided guidance for 2020, which was lower than analyst expectations. The company projects total revenues in the band of $4,150-$4,300 million for 2020. Adjusted EBITDA is anticipated in the range of $430-$458 million.

Total Revenues at the Aaron's Business segment are projected within $1,575-$1,625 million, while revenues at the Progressive segment are envisioned in the $2,540-$2,635 million range. However, revenues at the Vive segment are expected within $35-$40 million.

Adjusted EBITDA is anticipated within $125-$135 million for the Aaron's Business and $310-$325 million for the Progressive division. For the

Vive segment, management projects adjusted EBITDA of negative $2-$5 million.

For 2020, management expects adjusted earnings in the range of $3.80-$4.00 per share.

Recent News

Aaron's Hikes Dividend – Nov 5, 2019

Aaron's hiked its quarterly cash dividend by 14.3% to 4 cents per share, from the prior payout of 3.5 cents per share. The raised dividend is payable Jan 6, 2020 to shareholders of record as on Dec 19.

Valuation

Aaron's shares are up 25.2% in the year-to-date period and 21.5% for the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Retail-Wholesale sector are down 4.9% and 0.3%, respectively in the year-to-date period. Over the past year, the Zacks sub-industry and the sector is up 0.7% and 10.1%, respectively.

The S&P 500 index is down 2.9% in the year-to-date period and up 11.2% in the past year.

The stock is currently trading at 10.44X forward 12-month earnings, which compares to 16.7X for the Zacks sub-industry, 24.48X for the Zacks sector and 17.88X for the S&P 500 index.

Over the past five years, the stock has traded as high as 18.17X and as low as 8.74X, with a 5-year median of 13.1X. Our Underperform recommendation indicates that the stock will perform worst than the market. Our $36 price target reflects 8.80X 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	10.44	16.7	24.48	17.88
	5-Year High	18.17	21.77	26.2	19.34
	5-Year Low	8.74	8.32	19.07	15.18
	5-Year Median	13.1	11.52	23	17.47
P/S F12M	Current	0.64	0.37	1.02	3.29
	5-Year High	1.21	0.5	1.11	3.43
	5-Year Low	0.42	0.21	0.8	2.54
	5-Year Median	0.77	0.3	0.92	3
EV/EBITDA TTM	Current	1.32	5.43	15.1	12
	5-Year High	2.3	6.61	15.28	12.87
	5-Year Low	1.09	2.78	10.79	8.48
	5-Year Median	1.76	4.24	12.41	10.77

As of 02/25/2020

Industry Analysis **Zacks Industry Rank:** Bottom 9% (232 out of 255)

Top Peers

Best Buy Co., Inc. **(BBY)**	Neutral
Big Lots, Inc. **(BIG)**	Neutral
Rent-A-Center, Inc. **(RCII)**	Neutral
RH **(RH)**	Neutral
Systemax Inc. **(SYX)**	Neutral
Walmart Inc. **(WMT)**	Neutral
Conns, Inc. **(CONN)**	Underperform
GameStop Corp. **(GME)**	Underperform

Industry Comparison Industry: Retail - Consumer Electronics

Industry Peers

	AAN Underperform	X Industry	S&P 500	BBY Neutral	CONN Underperform	SYX Neutral
VGM Score	B	-	-	A	B	B
Market Cap	2.87 B	529.50 M	22.56 B	21.19 B	247.95 M	811.05 M
# of Analysts	8	4	13	10	5	1
Dividend Yield	0.37%	0.00%	1.88%	2.44%	0.00%	2.22%
Value Score	B	-	-	A	A	C
Cash/Price	0.02	0.16	0.04	0.05	0.20	0.11
EV/EBITDA	1.44	6.75	13.36	8.58	7.34	11.47
PEG Ratio	0.63	0.66	1.94	1.42	0.18	NA
Price/Book (P/B)	1.65	1.46	3.09	6.91	0.40	4.89
Price/Cash Flow (P/CF)	1.22	5.81	12.57	9.72	2.22	15.64
P/E (F1)	10.47	13.10	17.93	13.10	4.22	14.50
Price/Sales (P/S)	0.73	0.61	2.51	0.49	0.16	0.86
Earnings Yield	9.48%	7.26%	5.55%	7.63%	23.73%	6.89%
Debt/Equity	0.20	0.28	0.70	1.10	2.04	0.36
Cash Flow ($/share)	34.91	3.39	7.02	8.43	3.89	1.38
Growth Score	C	-	-	C	C	B
Hist. EPS Growth (3-5 yrs)	15.99%	20.38%	10.85%	21.97%	20.38%	70.69%
Proj. EPS Growth (F1/F0)	4.08%	5.20%	6.86%	5.20%	-4.74%	7.19%
Curr. Cash Flow Growth	13.84%	12.48%	6.53%	11.12%	58.97%	-3.38%
Hist. Cash Flow Growth (3-5 yrs)	15.48%	13.36%	8.38%	9.54%	2.04%	61.41%
Current Ratio	2.12	1.95	1.22	1.05	4.92	1.77
Debt/Capital	16.41%	26.53%	42.37%	52.39%	67.13%	26.53%
Net Margin	0.80%	4.33%	11.57%	3.54%	5.37%	5.12%
Return on Equity	14.70%	14.70%	16.80%	49.43%	13.89%	33.73%
Sales/Assets	1.22	1.67	0.54	2.91	0.76	2.48
Proj. Sales Growth (F1/F0)	7.92%	4.88%	4.03%	1.72%	4.57%	5.19%
Momentum Score	D	-	-	A	F	D
Daily Price Chg	-1.34%	-1.84%	-3.36%	-4.22%	-4.42%	-4.93%
1 Week Price Chg	-25.55%	0.03%	-0.94%	0.06%	-0.43%	0.57%
4 Week Price Chg	-31.97%	-7.87%	-5.65%	-7.87%	-6.19%	-10.67%
12 Week Price Chg	-24.55%	-19.51%	-1.04%	4.84%	-57.98%	-5.72%
52 Week Price Chg	-22.36%	-21.18%	8.00%	35.78%	-63.06%	-13.39%
20 Day Average Volume	1,171,132	40,044	2,073,853	1,963,827	723,672	34,338
(F1) EPS Est 1 week change	-13.80%	-0.01%	0.00%	-0.02%	-9.46%	0.00%
(F1) EPS Est 4 week change	-12.32%	-4.32%	-0.06%	0.27%	-9.46%	0.00%
(F1) EPS Est 12 week change	-12.52%	-23.29%	-0.19%	1.59%	-34.06%	0.00%
(Q1) EPS Est Mthly Chg	-23.57%	0.00%	-0.61%	0.41%	-22.22%	0.00%

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	B
Growth Score	C
Momentum Score	D
VGM Score	B

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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