# Alliance Data(ADS)

**$48.91** (As of 08/11/20)

Price Target (6-12 Months): **$51.00**

| Long Term: 6-12 Months | **Zacks Recommendation:** | **Neutral** |
|---|---|---|
| | (Since: 05/25/20) | |
| | Prior Recommendation: Underperform | |
| Short Term: 1-3 Months | **Zacks Rank:** (1-5) | **4-Sell** |
| | Zacks Style Scores: | VGM:B |
| | Value: A \| Growth: D \| Momentum: D | |

## Summary

Alliance Data's second-quarter bottom line beat estimates but declined year over year due to lower volumes. The company continues to benefit from data-driven marketing strategies. Solid receivables growth in Card Services along with strong LoyaltyOne should drive the top line of the firm. Acquisitions and divestitures will help Alliance Data grow inorganically and expand the international footprint. Shares of Alliance Data have underperformed the industry in a year's time. Nevertheless, the company remains focused toward returning value to its shareholders in the form of share buybacks. However, rising debt levels have led to an increase in interest expenses, raising financial risk and straining margin expansion. The company's increased cost of operations, and higher general and administrative expenses have also affected the margins.
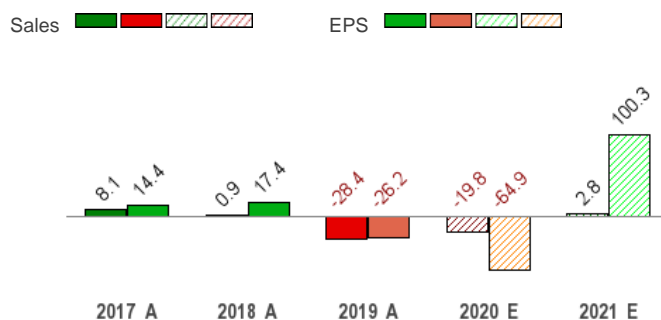
## Price, Consensus & Surprise



## Data Overview

| | |
|---|---|
| 52 Week High-Low | **$154.20 - $20.51** |
| 20 Day Average Volume (sh) | **1,096,232** |
| Market Cap | **$2.3 B** |
| YTD Price Change | **-56.4%** |
| Beta | **2.49** |
| Dividend / Div Yld | **$0.84 / 1.7%** |
| Industry | **Financial Transaction Services** |
| Zacks Industry Rank | **Top 40% (100 out of 253)** |
| | |
| Last EPS Surprise | **1.1%** |
| Last Sales Surprise | **-21.2%** |
| EPS F1 Est- 4 week change | **-22.7%** |
| Expected Report Date | **10/22/2020** |
| Earnings ESP | **0.0%** |
| | |
| P/E TTM | **4.2** |
| P/E F1 | **8.3** |
| PEG F1 | **0.5** |
| P/S TTM | **0.4** |

## Sales and EPS Growth Rates (Y/Y %)



### Sales Estimates (millions of $)

| | Q1 | Q2 | Q3 | Q4 | Annual* |
|---|---|---|---|---|---|
| 2021 | 1,126 E | 1,113 E | 1,150 E | 1,246 E | 4,602 E |
| 2020 | 1,382 A | 979 A | 1,025 E | 1,092 E | 4,478 E |
| 2019 | 1,334 A | 1,349 A | 1,438 A | 1,461 A | 5,581 A |

### EPS Estimates

| | Q1 | Q2 | Q3 | Q4 | Annual* |
|---|---|---|---|---|---|
| 2021 | $2.07 E | $2.21 E | $3.61 E | $3.54 E | $11.78 E |
| 2020 | $0.75 A | $1.86 A | $1.78 E | $1.37 E | $5.88 E |
| 2019 | $3.72 A | $3.83 A | $5.05 A | $4.12 A | $16.77 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 08/11/2020. The reports text is as of 08/12/2020.

## Overview

Headquartered in Plano, TX and founded in 1996, Alliance Data Systems Corporation is a private label credit card processing firm for mid-market specialty retail stores in the U.S. It provides transaction, marketing and credit services in the United States, Canada and internationally. Using transaction-rich data, Alliance Data creates and manages customized solutions that change consumer behavior and enable its clients to create and enhance customer loyalty to build stronger, mutually beneficial relationships with their customers. The company is a leading player among its competitors. Alliance Data is one of the largest third party payment processors in the United States and the second largest third party private label card issuer as measured by accounts. In Canada, it owns and operates the premier coalition loyalty-marketing program (AIR MILES).

On Jul 1, 2019, Alliance Data sold its Epsilon business to Publicis Groupe. Therefore, the company operates in two reportable segments: LoyaltyOne and Card Services.

**Card Services (81.5% of 2019 revenues)** provides risk management solutions, account origination, funding, transaction processing, customer care and collections services for the company's private label retail credit card programs.

**LoyaltyOne (18.5%)** uses information gathered through loyalty programs to help clients in designing and implementing marketing programs. Clients include financial services providers, grocers, drug stores, petroleum retailers and specialty retailers.

The company derives revenues primarily from the company's coalition and short-term loyalty programs through its AIR MILES Reward Program and BrandLoyalty.



EPS Hist. and Est.



Sales Hist. and Est.
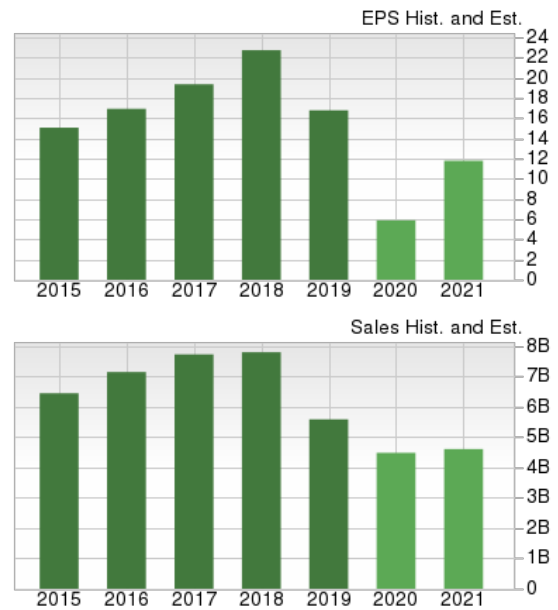
## Reasons To Buy:

▲ Shares of Alliance Data have lost 67.9% in the past year against the industry's growth of 6.7%. Nevertheless, strong fundamentals of the company will help shares bounce back.

▲ Organic growth has been a key strength at Alliance Data. We believe the company to retain its revenue momentum in the coming quarters with ample opportunities from the current trend in consumer-based businesses shifting their marketing spend to data-driven marketing strategies.

▲ Alliance Data divested Epsilon to Publicis Groupe for $4.4 billion in July 2019. The business has been witnessing declining sales for some time. The divestiture will help the company focus more on market-leading high-growth, high-ROI Card Service segment, which contributes the lion's share of Alliance Data's total revenues. Also, the company estimates the divestiture to provide significant liquidity to return capital to shareholders and improve capital structure.

▲ Alliance Data has made several strategic acquisitions to grow inorganically. Acquisitions have helped the company expand international footprint, consolidate its position in digital agency, boost the LoyaltyOne business, strengthen position in the digital marketing channels, expand its Omni-Channel distribution capabilities and widen presence in Brazil. With solid financial strength and flexibility, we expect Alliance Data to pursue strategic acquisitions that supports international expansion, with solid growth opportunities.

▲ Alliance Data remains focused toward returning value to its shareholders. It uses share repurchases as a tool to mitigate the adverse impact of foreign exchange and intends to focus more into share buybacks and then into mergers and acquisitions. Though the company has a new share buyback authorization of $1.1 billion, it has suspended the same in the wake of the pandemic.

▲ Alliance Data has a strong balance sheet by virtue of its solid cash position. The company had long-term and other debt amounting to $3.2 billion as of Jun 30, 2020. Cash and cash equivalents came in at nearly $5 billion for the same period. This suggests that the company has sufficient cash reserves to meet debt obligations. The company also extended the timeline for further debt reduction of $2 billion from Jun 2021 till Dec 2022, and extended an additional debt of $850 million from Jun 2021 to Dec 2024.

Alliance Data's high-ROI Card Service segment, solid inorganic background, strengthening its balance sheet to gain financial flexibility and effective capital deployment bodes well for growth.

## Reasons To Sell:

▼ Alliance Data has been witnessing a rise in operating expenses for the past few years due to higher cost of operations and an increased general and administrative expense. Total operating expenses have escalated 40.2% in the last five years. In first-half 2020, operating expenses increased 1.7% year over year to $1.2 billion, primarily due to rise in provision expense.

Nonetheless, Alliance Data's  expense reduction programs achieved about $140 million in cost savings in the first half of 2020. The company estimates additional cost savings of more than $100 million in second half of 2020 ($50 million for each of the next two quarters) on operating efficiencies.

▼ Alliance Data is exposed to fluctuations in exchange rate between the U.S. and the Canadian dollar and between the U.S. dollar and euro. This is a major concern. In 2019, foreign currency movements relative to the U.S. dollar negatively impacted its revenues by approximately $45 million and income from operations before income taxes by approximately $1 million.

▼ The company's ROA of 2.3% compares unfavorably with the prior quarter's  figure of 2.5%. This implies inefficient utilization of assets of the company.

Alliance Data's increasing expenses due to higher cost of operations and an increased general and administrative expense and poor return on asset raise concern.

## Last Earnings Report

**Alliance Data Q2 Earnings Beat Estimates, Decline Y/Y**

Alliance Data's operating earnings of $1.86 per share for the second quarter of 2020 beat the Zacks Consensus Estimate of $1.84. However, the bottom line plunged 51% year over year.

The soft performance was attributable to lower revenues as a result of a decline in volumes due to the COVID-19 pandemic. However, lower expense limited the downside.

| Quarter Ending | 06/2020 |
|---|---|
| Report Date | **Jul 23, 2020** |
| Sales Surprise | **-21.23%** |
| EPS Surprise | **1.09%** |
| Quarterly EPS | **1.86** |
| Annual EPS (TTM) | **11.78** |

### Behind the Headlines

Alliance Data reported total revenues of $979 million, down 27% year over year. The downside was due to lower revenues from Card Services as well as LoyaltyOne segment. The top line missed the Zacks Consensus Estimate by 21.2%.

Operating expenses decreased 20.4% year over year to $804.6 million. Operating income decreased 48.2% year over year to $174.7 million largely due to lower revenues.

Adjusted EBITDA (net of funding costs) declined 50% year over year to $156 million.

### Segment Update

**LoyaltyOne**: Revenues totaled $151 million, down 40% year over year attributable to fewer short-term loyalty programs due to the impact of COVID-19 as well as divestment of Precima. Adjusted EBITDA decreased 11% to $45 million.

AIR MILES reward miles issued decreased 26% reflecting a decline in discretionary spending, including credit card spend and delays in promotions by sponsors. AIR MILES reward miles redeemed declined 42%, reflecting the impact of the pandemic on travel-related categories, partially offset by strength from merchandise redemptions.

BrandLoyalty revenues decreased 44% or $70 million due to a decline in programs.

**Card Services**: Revenues were $828 million, down 24% year over year attributable to lower sales volumes and increased fee waivers due to COVID-19. Adjusted EBITDA was $127 million, down 56% year over year, attributable to lower revenues. However, decline in operating expenses and the $7 million year-over-year decrease in the provision for loan loss limited the downside.

### Expense Reduction Programs Update

Expense reduction programs achieved about $140 million in cost savings in the first half of 2020. The company estimates additional cost savings of more than $100 million in second half of 2020.

### Financial Update

As of Jun 30, 2020, cash and cash equivalents was $4.9 billion, up 28% from Dec 31, 2019-level.

At quarter end, the debt level was up 12.3% from 2019-end to $3.2 billion.

Cash from operations decreased 2% year over year to $1.1 billion in the first six months of the year. Capital expenditure at Alliance Data declined 71.7% year over year to $26.1 million in the same period.

### Dividend Update

The board of directors approved quarterly dividend of 21 cents to be paid out on Sep 18 to stockholders of record as of Aug 14, 2020.

## Recent News

**Alliance Data's May Average Receivables Down Y/Y** - Jun 15, 2020

Alliance Data's May average receivables declines 4% year over year. Delinquency rate of 4.8% compares with 5% in year ago month.

## Valuation

Alliance Data's shares are down 56.4% and 67.9% in the year-to-date period and over the trailing 12-month period, respectively. Stocks in the Zacks sub-industry and the Zacks Finance sector are up 2.9% and 1.7% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are up 6.7% and 3.4%, respectively.

The S&P 500 index is up 3.3% in the year-to-date period and 14% in the past year.

The stock is currently trading at 4.74x forward 12-month earnings, which compares to 31.21x for the Zacks sub-industry, 29.96x for the Zacks sector and 22.62x for the S&P 500 index.

Over the past five years, the stock has traded as high as 19.13x and as low as 1.09x, with a 5-year median of 11.06x. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our $51 price target reflects 4.94x forward 12-month earnings.

The table below shows summary valuation data for ADS

| Valuation Multiples - ADS | | Stock | Sub-Industry | Sector | S&P 500 |
|---|---|---|---|---|---|
| P/E F12M | Current | 4.74 | 31.21 | 29.96 | 22.62 |
| | 5-Year High | 19.13 | 31.68 | 29.96 | 22.62 |
| | 5-Year Low | 1.09 | 20.78 | 18.68 | 15.25 |
| | 5-Year Median | 11.06 | 23.31 | 20.96 | 17.58 |
| P/S F12M | Current | 0.51 | 11.31 | 4.18 | 3.62 |
| | 5-Year High | 2.6 | 11.31 | 4.18 | 3.65 |
| | 5-Year Low | 0.19 | 7.18 | 3.07 | 2.53 |
| | 5-Year Median | 1.5 | 8.78 | 3.6 | 3.05 |
| P/B TTM | Current | 2.02 | 7.02 | 4.78 | 4.64 |
| | 5-Year High | 10.78 | 12.78 | 6.72 | 4.68 |
| | 5-Year Low | 0.66 | 5.22 | 3.28 | 2.83 |
| | 5-Year Median | 6.47 | 8.07 | 5.22 | 3.74 |

As of 08/11/2020

## Industry Analysis Zacks Industry Rank: Top 40% (100 out of 253)



### Top Peers

| Company (Ticker) | Rec | Rank |
|---|---|---|
| MarketAxess Holdings Inc. (MKTX) | Outperform | 2 |
| Diebold Nixdorf, Incorporated (DBD) | Neutral | 3 |
| Equifax, Inc. (EFX) | Neutral | 3 |
| Fidelity National Information Services, Inc. (FIS) | Neutral | 3 |
| Fiserv, Inc. (FISV) | Neutral | 3 |
| Global Payments Inc. (GPN) | Neutral | 3 |
| Synchrony Financial (SYF) | Neutral | 3 |
| The Western Union Company (WU) | Neutral | 3 |

## Industry Comparison Industry: Financial Transaction Services

| | ADS | X Industry | S&P 500 | | FIS | FISV | WU |
|---|---|---|---|---|---|---|---|
| | | | | Industry Peers | | | |
| Zacks Recommendation (Long Term) | Neutral | - | - | | Neutral | Neutral | Neutral |
| Zacks Rank (Short Term) | 4 | - | - | | 3 | 3 | 3 |
| VGM Score | B | - | - | | C | B | A |
| Market Cap | 2.33 B | 2.50 B | 23.61 B | | 88.63 B | 65.77 B | 9.55 B |
| # of Analysts | 7 | 6 | 14 | | 14 | 14 | 8 |
| Dividend Yield | 1.72% | 0.00% | 1.69% | | 0.98% | 0.00% | 3.87% |
| Value Score | A | - | - | | C | C | A |
| Cash/Price | 2.25 | 0.07 | 0.07 | | 0.01 | 0.01 | 0.12 |
| EV/EBITDA | 4.54 | 15.40 | 13.32 | | 31.29 | 25.92 | 6.62 |
| PEG Ratio | 0.49 | 1.67 | 2.95 | | 1.54 | 1.37 | 0.51 |
| Price/Book (P/B) | 2.02 | 4.42 | 3.22 | | 1.80 | 1.99 | NA |
| Price/Cash Flow (P/CF) | 2.00 | 14.79 | 12.79 | | 17.59 | 14.67 | 9.71 |
| P/E (F1) | 8.11 | 26.35 | 22.02 | | 26.32 | 22.25 | 13.02 |
| Price/Sales (P/S) | 0.44 | 4.66 | 2.57 | | 7.26 | 4.57 | 1.94 |
| Earnings Yield | 12.02% | 3.80% | 4.29% | | 3.80% | 4.49% | 7.66% |
| Debt/Equity | 8.56 | 0.43 | 0.77 | | 0.30 | 0.65 | -42.04 |
| Cash Flow ($/share) | 24.48 | 2.39 | 6.94 | | 8.13 | 6.70 | 2.39 |
| Growth Score | D | - | - | | C | B | B |
| Hist. EPS Growth (3-5 yrs) | 3.50% | 17.88% | 10.41% | | 16.96% | 17.88% | 1.96% |
| Proj. EPS Growth (F1/F0) | -64.94% | -7.56% | -6.51% | | -3.13% | 10.36% | 3.11% |
| Curr. Cash Flow Growth | -34.53% | 13.06% | 5.22% | | 57.47% | 147.85% | -11.92% |
| Hist. Cash Flow Growth (3-5 yrs) | 0.58% | 14.80% | 8.55% | | 26.53% | 29.38% | -2.25% |
| Current Ratio | 1.81 | 1.26 | 1.34 | | 0.71 | 1.04 | 0.94 |
| Debt/Capital | 89.54% | 34.80% | 44.59% | | 23.27% | 39.73% | NA |
| Net Margin | 1.73% | 6.22% | 10.13% | | 0.25% | 5.82% | 12.38% |
| Return on Equity | 42.34% | 16.87% | 14.59% | | 6.60% | 8.34% | -1,029.12% |
| Sales/Assets | 0.21 | 0.47 | 0.51 | | 0.15 | 0.19 | 0.57 |
| Proj. Sales Growth (F1/F0) | -19.76% | -3.07% | -1.45% | | 22.02% | 36.91% | -9.34% |
| Momentum Score | D | - | - | | C | B | A |
| Daily Price Chg | 3.43% | -0.67% | -0.17% | | -2.13% | -1.13% | -0.64% |
| 1 Week Price Chg | 4.04% | 3.57% | 2.30% | | 1.00% | 4.13% | -4.16% |
| 4 Week Price Chg | 20.68% | 6.12% | 6.41% | | 4.86% | 0.70% | 7.75% |
| 12 Week Price Chg | 14.68% | 18.21% | 15.42% | | 5.62% | -4.16% | 23.83% |
| 52 Week Price Chg | -67.92% | 3.75% | 2.88% | | 6.08% | -7.15% | 8.50% |
| 20 Day Average Volume | 1,096,232 | 562,170 | 2,007,486 | | 3,303,826 | 4,517,666 | 5,986,739 |
| (F1) EPS Est 1 week change | 0.00% | 0.00% | 0.00% | | -1.36% | -0.31% | 5.47% |
| (F1) EPS Est 4 week change | -22.66% | 2.07% | 1.84% | | 1.06% | 0.27% | 6.02% |
| (F1) EPS Est 12 week change | -22.66% | 2.84% | 2.40% | | -0.05% | 0.50% | 6.89% |
| (Q1) EPS Est Mthly Chg | -39.07% | 2.44% | 0.72% | | 1.69% | 2.44% | 8.64% |

## 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.

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

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.

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.

## Disclosures

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