

Alliance Data(ADS)

\$87.70 (As of 02/27/20)

Price Target (6-12 Months): **\$92.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 12/24/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:C

Value: A

Growth: F

Momentum: A

Summary

Alliance Data's fourth-quarter 2019 earnings of \$4.12 per share missed the Zacks Consensus Estimate by 0.9%. The bottom line declined nearly 29% year over year. The current trend in consumer-based businesses shifting their marketing spend to data-driven marketing strategies should help retain the momentum. Solid receivables growth in Card Services along with strong LoyaltyOne should drive the top line. Shares of Alliance Data have underperformed the industry in the past year. We believe that acquisitions and divestitures will help it grow inorganically and expand the international footprint. However, its rising debt level, leading to higher interest expenses and lower interest coverage ratio, raises financial risk. The company's increased cost of operations, and higher general and administrative expenses put a burden on the margins.

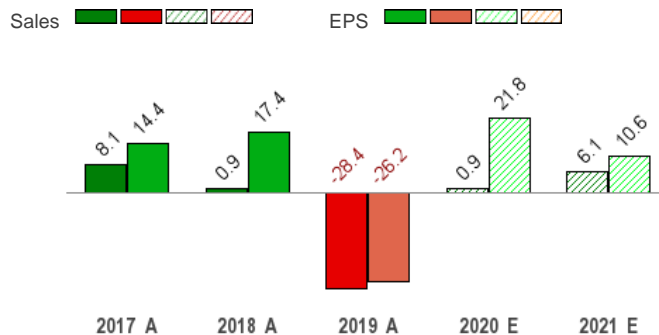
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$182.95 - \$84.62
20 Day Average Volume (sh)	809,735
Market Cap	\$4.0 B
YTD Price Change	-21.8%
Beta	1.73
Dividend / Div Yld	\$2.52 / 2.9%
Industry	Financial Transaction Services
Zacks Industry Rank	Top 45% (114 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-1.0%
Last Sales Surprise	-2.5%
EPS F1 Est- 4 week change	-2.2%
Expected Report Date	04/23/2020
Earnings ESP	2.3%
P/E TTM	5.3
P/E F1	4.3
PEG F1	0.3
P/S TTM	0.7

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,427 E	1,451 E	1,506 E	1,611 E	5,973 E
2020	1,348 E	1,375 E	1,425 E	1,506 E	5,632 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	\$5.22 E	\$5.41 E	\$5.90 E	\$6.15 E	\$22.59 E
2020	\$4.66 E	\$4.75 E	\$5.47 E	\$5.67 E	\$20.42 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 02/27/2020. The reports text is as of 02/28/2020.

Overview

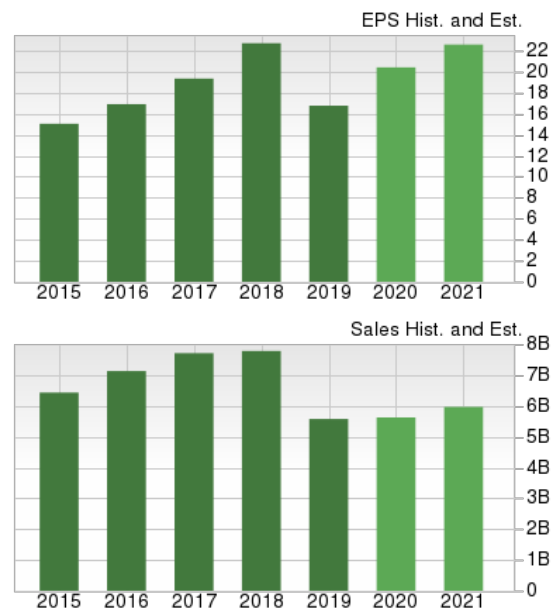
Headquartered in Plano, TX and founded in 1996, Alliance Data Systems Corporation is a private label credit card processing firm for mid-market specialty retail stores in the U.S. It provides transaction, marketing and credit services in the United States, Canada and internationally. Using transaction-rich 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.



Reasons To Buy:

- ▲ Shares of Alliance Data have lost 49.5% in the past year against the industry's growth of 24.6%. Nonetheless, its solid fundamentals should help its shares gain momentum. The company carries a Value Score of A. The stock has seen the Zacks Consensus Estimate for current-quarter earnings being revised 0.4% upward over the past 30 days.
- ▲ 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. For 2020, Alliance Data estimates core EPS of \$20.50. The estimated figure indicates a year-over-year increase of 22%.
- ▲ 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. As such, the board approved a new share buyback program of \$1.1 billion in July 2019. Its ROE of 49% compares favorably with the industry average of 42.6%.
- ▲ In 2019, the company retired debt levels of \$2.9 billion. 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 2019, operating expenses increased 9.3% to \$4.3 billion. The company must strive to improve revenues else margin will be dented.
- ▼ Alliance Data's long-term debt has increased 43% in five years' time. As a result interest expenses have more than doubled over the same time frame. Its debt-to-equity ratio of 644.5% compares unfavorably with the industry average of 52.8%. An increase in leverage thus might lead to heightened financial risk for the company and burden on margins. The company must continue to service its debt uninterruptedly, else creditworthiness will be dented.
- ▼ With more than 60% of the Canadian households collecting reward miles, the AIR MILES Reward Program has positioned itself as Canada's premier coalition loyalty program. In the event of actual redemptions by AIR MILES Reward Program being more than expected or if there is an increase in costs related to redemption of AIR MILES reward miles, profitability will likely be affected. In addition, AIR MILES reward miles issued is directly proportional to AIR MILES reward miles available for redemption in the future. This in turn, might affect revenues.

Alliance Data's increasing expenses due to higher cost of operations and an increased general and administrative expense and high leverage with low times interest earned raise concern.

Last Earnings Report

Alliance Data Q4 Earnings & Revenues Miss Estimates

Alliance Data Systems' fourth-quarter 2019 operating earnings of \$4.12 per share missed the Zacks Consensus Estimate by 0.9%. The bottom line declined nearly 29% year over year.

Earnings were weighed down by restructuring and strategic transaction costs.

Shares of the company lost 0.61% in the pre-market trading session owing to lower-than-expected results.

Quarter Ending **12/2019**

Report Date	Jan 30, 2020
Sales Surprise	-2.52%
EPS Surprise	-0.96%
Quarterly EPS	4.12
Annual EPS (TTM)	16.72

Behind the Headlines

Alliance Data reported total revenues of \$1.46 billion, flat year over year. The top line missed the Zacks Consensus Estimate by 2.7%.

Operating expenses increased 20.5% year over year to \$1.15 billion. Adjusted EBITDA (net of funding costs) declined 39% year over year to \$278 million.

Full Year Results

The company reported earnings per share of \$16.77, down 14% year over year. Revenues of \$5.58 billion declined 2% year over year.

Segment Update

Card Services revenues were \$1.13 billion, flat year over year. Adjusted EBITDA was \$209.6 million, down 51% year over year.

LoyaltyOne revenues totaled \$332 million, flat year over year. Adjusted EBITDA increased 19% to \$80.3 million. AIR MILES reward miles issued was up 1% year over year.

The company incurred \$33 million in restructuring and other charges.

Financial Update

As of Dec 31, 2019, cash and cash equivalents was \$3.9 billion, up 1.5% from Dec 31, 2018-level.

At quarter end, debt level dropped 50.2% from 2018-end to \$2.85 billion.

For the full year, the company generated cash from operations of \$1.2 billion, down 24.4% year over year. Capital expenditure at Alliance Data declined 28.8% year over year to \$142.3 million in the same period.

2020 Guidance

Alliance Data estimates core EPS of \$20.5, indicating growth of 22% year over year. Revenues are expected to remain unchanged year over year at \$5.6 billion.

Business Update

Alliance Data shifted its client base in Card Services toward faster growing companies and verticals by selling approximately \$2.1 billion in non-strategic receivables. It divested Epsilon and Precima units. The company extended the debt maturity ladder providing liquidity that can be used to re-invest in the business. A seasoned industry veteran, Ralph Andretta, was hired from Citigroup to lead the company.

Valuation

Alliance Data's shares are down 21.8% and 49.5% 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 0.1% and down 0.2% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are up 24.6% and 11.1%, respectively.

The S&P 500 index is down 3.3% in the year-to-date period and up 10.3% in the past year.

The stock is currently trading at 4.2x forward 12-month earnings, which compares to 26.3x for the Zacks sub-industry, 24.1x for the Zacks sector and 17.8x for the S&P 500 index.

Over the past five years, the stock has traded as high as 21.1x and as low as 4.2x, with a 5-year median of 11.7x. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$92 price target reflects 4.4x 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	4.21	26.32	24.13	17.81
	5-Year High	21.06	28	25.26	19.34
	5-Year Low	4.21	20.78	18.78	15.18
	5-Year Median	11.74	23	20.58	17.46
P/S F12M	Current	0.71	10.01	3.88	3.28
	5-Year High	2.85	11.65	5.14	3.43
	5-Year Low	0.71	7.19	3.09	2.54
	5-Year Median	1.56	8.69	3.63	3
P/B TTM	Current	2.49	7.77	4.75	4.51
	5-Year High	10.78	12.79	6.71	4.9
	5-Year Low	2.49	5.34	4.13	2.85
	5-Year Median	7.11	8.12	5.25	3.62

As of 02/27/2020

Industry Analysis Zacks Industry Rank: Top 45% (114 out of 254)



Top Peers

Diebold Nixdorf, Incorporated (DBD)	Neutral
Equifax, Inc. (EFX)	Neutral
Fidelity National Information Services, Inc. (FIS)	Neutral
Fiserv, Inc. (FISV)	Neutral
Global Payments Inc. (GPN)	Neutral
MarketAxess Holdings Inc. (MKT)	Neutral
Synchrony Financial (SYF)	Neutral
The Western Union Company (WU)	Neutral

Industry Comparison Industry: Financial Transaction Services				Industry Peers		
	ADS Neutral	X Industry	S&P 500	FIS Neutral	FISV Neutral	WU Neutral
VGM Score	C	-	-	D	B	A
Market Cap	4.04 B	2.51 B	21.35 B	85.59 B	73.80 B	9.38 B
# of Analysts	7	6	13	15	16	8
Dividend Yield	2.87%	0.00%	2.02%	1.01%	0.00%	3.52%
Value Score	A	-	-	D	D	B
Cash/Price	0.82	0.07	0.04	0.01	0.01	0.14
EV/EBITDA	6.63	16.37	12.70	31.09	28.35	6.45
PEG Ratio	0.25	1.54	1.84	2.47	1.54	0.74
Price/Book (P/B)	2.49	4.21	2.92	1.73	2.13	NA
Price/Cash Flow (P/CF)	3.58	17.08	11.89	17.08	16.21	9.49
P/E (F1)	4.18	21.08	16.90	22.06	21.87	11.42
Price/Sales (P/S)	0.72	4.53	2.39	8.28	7.24	1.77
Earnings Yield	23.28%	4.66%	5.90%	4.53%	4.57%	8.76%
Debt/Equity	6.44	0.35	0.70	0.35	0.62	-81.75
Cash Flow (\$/share)	24.48	2.86	6.94	8.13	6.70	2.39
Growth Score	F	-	-	C	A	B
Hist. EPS Growth (3-5 yrs)	10.76%	17.05%	10.85%	18.44%	17.05%	2.99%
Proj. EPS Growth (F1/F0)	21.77%	15.10%	6.79%	12.20%	24.09%	14.96%
Curr. Cash Flow Growth	-34.53%	8.28%	5.92%	57.47%	147.85%	-11.92%
Hist. Cash Flow Growth (3-5 yrs)	0.58%	10.92%	8.38%	26.53%	29.38%	-2.25%
Current Ratio	1.77	1.15	1.23	0.84	1.08	0.97
Debt/Capital	86.57%	36.09%	42.53%	25.84%	38.74%	99.03%
Net Margin	5.57%	8.29%	11.57%	2.88%	8.77%	20.00%
Return on Equity	42.81%	19.79%	16.80%	9.60%	11.78%	-737.30%
Sales/Assets	0.20	0.46	0.54	0.18	0.22	0.59
Proj. Sales Growth (F1/F0)	0.90%	10.17%	4.07%	31.92%	50.36%	-0.88%
Momentum Score	A	-	-	B	A	A
Daily Price Chg	-3.56%	-3.41%	-3.99%	-3.50%	-3.84%	-4.62%
1 Week Price Chg	-0.65%	-0.20%	-0.94%	-1.59%	-2.31%	-1.79%
4 Week Price Chg	-18.18%	-9.31%	-9.83%	-5.85%	-10.47%	-17.72%
12 Week Price Chg	-15.33%	-1.21%	-6.79%	1.42%	-5.44%	-15.39%
52 Week Price Chg	-49.31%	15.14%	2.79%	28.41%	28.16%	27.08%
20 Day Average Volume	809,735	508,130	2,169,477	3,390,877	3,524,236	8,026,139
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-2.17%	0.00%	-0.09%	-0.36%	0.14%	1.02%
(F1) EPS Est 12 week change	-1.71%	-0.23%	-0.24%	-0.01%	0.35%	0.57%
(Q1) EPS Est Mthly Chg	0.83%	0.00%	-0.72%	-3.72%	-2.89%	0.66%

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	F
Momentum Score	A
VGM Score	C

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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