

American Eagle (AEO)

\$14.30 (As of 02/10/20)

Price Target (6-12 Months): **\$15.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 12/05/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:B

Value: A

Growth: C

Momentum: B

Summary

Shares of American Eagle have declined and underperformed the industry in the past three months. The stock came under pressure due to management's bleak earnings guidance for the fiscal fourth quarter. The company is grappling with persistent challenges in the AE apparel business, which is likely to continue in the fiscal fourth quarter. Moreover, increased promotions and higher SG&A expenses might hurt margins. Nevertheless, the company's third-quarter fiscal 2019 sales beat estimates but earnings were in line. Also, the company witnessed comps growth for the 19th straight quarter, driven by strong performances across AE Jeans, Aerie and the digital channel. Moreover, strength in its AE and Aerie brands as well as solid growth across stores and digital channels have been aiding top and bottom lines.

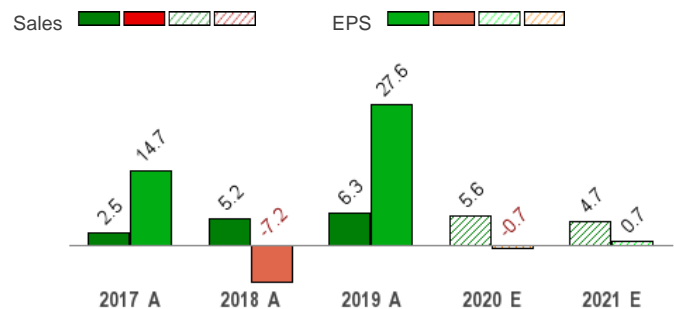
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$24.30 - \$13.66
20 Day Average Volume (sh)	3,143,419
Market Cap	\$2.4 B
YTD Price Change	-2.7%
Beta	0.84
Dividend / Div Yld	\$0.55 / 3.8%
Industry	Retail - Apparel and Shoes
Zacks Industry Rank	Top 27% (68 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	0.0%
Last Sales Surprise	0.2%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	03/04/2020
Earnings ESP	-6.7%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	925 E	1,096 E	1,120 E	1,343 E	4,461 E
2020	886 A	1,041 A	1,066 A	1,267 E	4,261 E
2019	823 A	965 A	1,004 A	1,244 A	4,036 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.24 E	\$0.36 E	\$0.53 E	\$0.44 E	\$1.48 E
2020	\$0.24 A	\$0.39 A	\$0.48 A	\$0.36 E	\$1.47 E
2019	\$0.23 A	\$0.34 A	\$0.48 A	\$0.43 A	\$1.48 A

*Quarterly figures may not add up to annual.

P/E TTM	9.3
P/E F1	9.7
PEG F1	1.4
P/S TTM	0.6

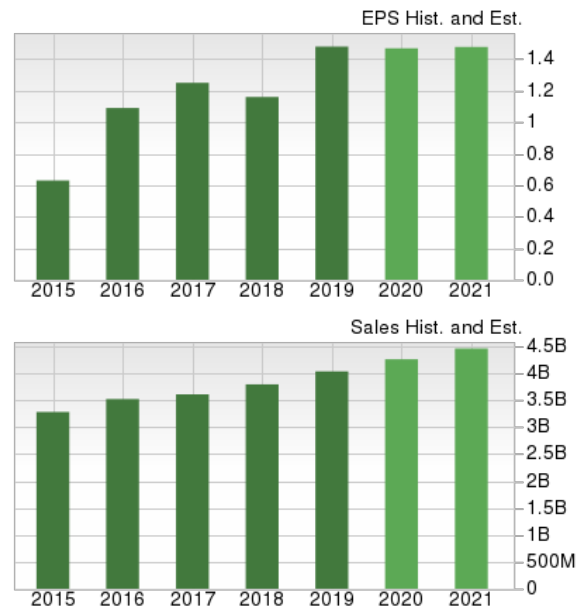
The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 02/10/2020. The reports text is as of 02/11/2020.

Overview

Based in Pittsburgh, PA, American Eagle Outfitters Inc. is a specialty retailer of casual apparel, accessories and footwear for men and women aged 15–25 years. American Eagle, along with its subsidiaries, engages in the designing and marketing of casual clothing. The company's assortment includes jeans, cargo pants, graphic T-shirts as well as a range of accessories, outerwear and footwear.

American Eagle currently operates under the American Eagle (AE) Brand, Aerie by American Eagle and an online retailing channel – AEO Direct.

- **AE Brand:** Under this brand, the company sells latest fashion apparel and accessories for men and women in the age group of 15–25 years, including sweaters, graphic T-shirts, fleece, outerwear and accessories.
- **Aerie by American Eagle:** Launched in 2006, Aerie is a lifestyle brand providing simple and stylish apparel, especially for young girls. The company sells apparel through its standalone Aerie stores across the United States and Canada, and globally through its online channel, aerie.com.
- **AEO Direct:** AEO Direct is American Eagle's online retailing channel, through which it sells a wide range of apparel and accessories from its different brands. The company merchandises its products through e-commerce websites, ae.com and aerie.com.



As of Nov 2, 2019, the company operated 1,094 stores, comprising 945 AE (including 170 Aerie side-by-side locations), 142 Aerie stand-alone, five Tailgate and two Todd Snyder stores. Additionally, it operated 241 international licensed outlets.



Reasons To Buy:

- ▲ **Solid Comps Trend:** American Eagle reported strong holiday season results, which can be attributed to strong momentum in American Eagle's (AE) brand's signature jeans range and the Aerie brand. Management stated that fourth-quarter fiscal 2019 comparable sales (comps) till Jan 13, 2020 were nearly flat compared with 6% increase in the year-ago quarter.

Overall, the company boasts a solid comparable sales (comps) trend, which continued in third-quarter fiscal 2019. Comps growth of 5% in the third quarter marked the company's 19th straight quarter of positive comps. Comps gained from strong performances across AE Jeans, Aerie and the digital channel. Comps also benefited from increased number of transactions, partly offset by a fall in average transaction size on account of lower average unit retail price. Brand-wise, comps rose 20% at Aerie and 2% for the AE brand. AE Jeans recorded 25th consecutive quarter of robust top-line growth. Further, the company witnessed positive comps across stores and digital channels.

Going forward, management remains optimistic about continued strength in the Aerie brand, which will boost growth. Also, the AE brand's jeans and bottoms businesses remain strong. Moreover, the company's efforts to improve product assortments and inventory management remain encouraging. For the fiscal fourth quarter, management projects comps to remain flat year over year.

- ▲ **Strengthening Omni-Channel Capabilities:** American Eagle is striving to develop its omni-channel platform by enhancing its digital portals while also investing in store fleet. Backed by its investments in omni-channel capabilities, store and digital channels have been witnessing strong growth over several quarters. In the fiscal third quarter, in-store comps rose 2% after witnessing a decline in the second quarter. Also, the company's digital business continued to exhibit solid growth, contributing about 28% to total revenues. Digital sales rose in low double digits, up 100 basis points (bps) from the year-ago period. In the recent quarters, American Eagle saw significant increase in its app and mobile channels, which together represent more than half of its digital business.

Moreover, its investments in store fleet are highlighted by its store optimization efforts. In fiscal 2019, management intends to open 25 to 30 AE outlets and 35 to 40 Aerie stand-alone stores. Also, it expects to remodel 15 to 20 AE stores. Further, American Eagle expects to shut down 10 to 15 AE and 5 to 10 Aerie stand-alone stores in the fiscal year. This makes it clear that a winning marketing strategy in retail is providing the best combination of digital and physical store experiences.

- ▲ **Accelerating Aerie Growth:** American Eagle continues to witness spectacular growth in its Aerie brand, with comps growth of 20% in the fiscal third quarter. This marked the 20th straight quarter (five years) of double-digit comps growth for the brand, reflecting a significant momentum in all areas of the business. Aerie has evolved into a lifestyle brand, and remains focused on expanding market share and rapidly growing customer base. After the success of its core intimates offerings, the brand is rapidly gaining share in the innovative apparel market with the body positivity movement. The Aerie brand is a key growth engine for American Eagle and is on track to reach the next brand milestone of \$1 billion in sales. The company sees store expansion as an essential tool for building the Aerie brand. Consequently, American Eagle plans to accelerate the Aerie store footprint, with the opening of 35 to 40 Aerie stand-alone stores in fiscal 2019.

- ▲ **Robust Capital Plan & Shareholder-Friendly Moves:** American Eagle enjoys a strong financial status. As of Nov 2, 2019, the company had a debt-free balance sheet, with total cash and investments of \$265 million. These help it to make capital investments alongside returning excess cash to shareholders via dividends and share buybacks. Notably, the company returned nearly \$55 million to its shareholders via dividends and share buybacks. It paid out dividends of \$23 million and bought back nearly 2 million shares for \$32 million. Year to date, the company has repurchased about 6.3 million shares for \$112 million, following which it had 35.4 million shares remaining under its current authorization. This clearly underscores the company's commitment toward boosting shareholder value. Moreover, the company spent \$58 million as capital expenditure in the reported quarter. For fiscal 2019, management continues to anticipate capital expenditures of \$200-\$215 million, of which more than half will be allocated to store openings and refurbishment. The balance will be invested in omni-channel and digital projects as well as general corporate maintenance.

Aerie brand reported the 20th straight quarter of double-digit comps growth in third-quarter fiscal 2019. The brand is on track to reach its next milestone of \$1 billion in sales.

Reasons To Sell:

▼ **Soft AE Apparel Business Hurts View:** In the fiscal third quarter conference call, the company stated that it witnessed a softer-than-expected start to the holiday season on account of persistent challenges in the AE apparel business. We note that American Eagle witnessed weaker demand in some AE apparel categories in the fiscal third quarter, which resulted in increased markdowns. This downturn continued in the fiscal fourth quarter as well. Consequently, the company provided a soft earnings view for fiscal fourth quarter. It envisions adjusted earnings of 34-36 cents in fourth-quarter fiscal 2019, down from 43 cents recorded in the year-ago quarter. Driven by the soft outlook, shares of the company have decreased 10.6% in the past three months against the industry's growth of 1.4%.

American Eagle witnessed weaker demand in some AE apparel categories in the fiscal third quarter, which resulted in increased markdowns. This downturn continued in the fiscal fourth quarter as well.

▼ **Higher Expenses Weigh on Margins:** American Eagle's gross margin contracted 160 bps in third-quarter fiscal 2019 mainly due to higher markdowns. Meanwhile, operating margin declined 110 bps on gross margin contraction, somewhat mitigated with lower SG&A, as a rate of sales. However, in dollar terms, SG&A expenses rose 4% to \$259 million, thanks to increased store salaries and professional fees, somewhat offset by lower incentive expense.

In fourth-quarter fiscal 2019, the company expects gross margin to be hurt more than the fiscal third quarter, due to increased promotional activity. SG&A is expected to be roughly flat.

▼ **High Dependence on Outside Suppliers:** American Eagle does not own or operate any manufacturing facility and therefore, depends on third-party manufacturers for all its merchandise. The company's operations may be adversely affected in case of any import disruptions, like manufacturers' failure to ship orders on time or meet its standards.

▼ **Macroeconomic Challenges & Seasonality of Business:** The apparel retail industry is consumer driven and hence, very sensitive to the health of the economy. Spending on apparel and accessories is heavily dependent on the personal disposable income of consumers. The current macroeconomic challenges such as high household debt and unemployment levels may restrain consumers from spending on these items. Further, the seasonal and cyclical nature of the company's business puts it at risk as failure to perform well during the peak season might hurt its annual performance.

Last Earnings Report

American Eagle Q3 Earnings In Line, Revenues Beat Estimates

American Eagle Outfitters, Inc. reported in-line earnings in third-quarter fiscal 2019. Revenue-wise, the company marginally outpaced the Zacks Consensus Estimate and the metric grew on a year-over-year basis. However, management's bleak earnings guidance for the fiscal fourth quarter fell shy of the analysts' expectations.

The company stated that it witnessed a softer-than-expected start to the holiday season on account of persistent challenges in the AE apparel business. We note that American Eagle witnessed weaker demand in some AE apparel categories in the fiscal third quarter, which resulted in increased markdowns. This downturn continued in the fiscal fourth quarter as well.

For fourth-quarter fiscal 2019, American Eagle envisions adjusted earnings to come in at 34-36 cents, down from 43 cents recorded in the year-ago quarter.

Q3 Highlights

Adjusted earnings of 48 cents per share in the fiscal third quarter matched the Zacks Consensus Estimate. The bottom line also remained flat with the prior-year quarter's figure.

Total net revenues grew 6% year over year to \$1,066.4 million and beat the Zacks Consensus Estimate of \$1,064 million. The upside was backed by consolidated comparable sales (comps) growth of 5% year over year. This marked the company's 19th straight quarter of positive comps, with strong performances across AE Jeans, Aerie and the digital channel.

Comps gained from increased number of transactions, partly offset by a fall in average transaction size on account of lower average unit retail price. Brand-wise, comps rose 20% at Aerie and 2% for the AE brand. This marked the Aerie brand's 20th straight quarter of double-digit comps improvement, reflecting a significant momentum in all areas of the business and significant market share gains. Meanwhile, the AE jeans business recorded the 25th consecutive quarter of robust top-line growth.

Furthermore, the company witnessed positive comps across stores and digital channels. On a consolidated basis, in-store comps rose 2% in the reported quarter, after a decline in the previous quarter.

Additionally, American Eagle's digital business continued to exhibit solid growth, contributing about 28% to total revenues. Further, digital sales rose in low double digits, up 100 basis points (bps) from the year-ago period. In the recent quarters, American Eagle saw significant increases in its app and mobile channels, which together represents more than half of its digital business.

Quarter in Detail

Gross profit grew 2% to \$407.1 million in the reported quarter. However, gross margin contracted 160 bps to 38.2%, mainly due to higher markdowns.

SG&A expenses were up 4% to \$259 million, thanks to increased store salaries and professional fees, somewhat offset by lower incentive expense. As a rate of sales, SG&A declined 50 bps to 24.3%.

Further, operating income of \$103.1 million decreased 5% from \$108.6 million recorded in the prior-year quarter. Also, operating margin declined 110 bps to 9.7% due to gross margin contraction, somewhat mitigated with lower SG&A as a rate of sales.

Other Financial Details

American Eagle ended the fiscal third quarter with cash and investments of \$265 million. Further, total shareholders' equity as of Nov 2, 2019, was \$1,260.4 million.

Moreover, the company spent \$58 million as capital expenditure in the quarter under review. For fiscal 2019, management continues to anticipate capital expenditure of \$200-\$215 million. More than half of this spending will be allocated to store openings and refurbishment while the remaining is likely to be invested in omni-channel and digital projects as well as general corporate maintenance.

As of Nov 2, American Eagle's merchandise inventory was roughly \$647.3 million, up 9% from the comparable year-ago period number.

During the reported quarter, the company returned nearly \$55 million to its shareholders via dividends and share buybacks. It paid out dividends of \$23 million and bought back nearly 2 million shares for \$32 million. Year to date, the company has repurchased about 6.3 million shares for \$112 million, following which it had 35.4 million shares remaining under its current authorization.

Store Update

American Eagle inaugurated six AE stores and 12 Aerie stand-alone stores, while closed one Aerie stand-alone outlet in third-quarter fiscal 2019.

As of Nov 2, the company operated 1,094 stores, comprising 945 AE (including 170 Aerie side-by-side locations), 142 Aerie stand-alone, five Tailgate and two Todd Snyder stores. Additionally, it operated 241 international licensed outlets.

In fiscal 2019, management intends to open 25-30 AE outlets and 35-40 Aerie stand-alone stores. Also, it expects to remodel 15-20 AE stores. Further, American Eagle expects to shut down 10-15 AE and 5-10 Aerie stand-alone stores in the fiscal year.

Quarter Ending **10/2019**

Report Date	Dec 11, 2019
Sales Surprise	0.23%
EPS Surprise	0.00%
Quarterly EPS	0.48
Annual EPS (TTM)	1.54

Looking Ahead

Management remains optimistic about continued strength in the Aerie brand, which will continue delivering growth. Also, the AE brand's jeans and bottoms businesses remain strong. Moreover, the company's efforts to improve product assortments and inventory management are encouraging.

For the fiscal fourth quarter, management projects comps to remain flat year over year. Further, gross margin is expected to be hurt more than the fiscal third quarter, due to increased promotional activity. SG&A is expected to be roughly flat and the effective tax rate is projected to be 20-22% for the fiscal fourth quarter.

Recent News

American Eagle Reports Impressive Holiday Sales – Jan 13

American Eagle announced impressive holiday sales numbers, which can be attributed to strong momentum in American Eagle's (AE) brand's signature jeans range and the Aerie brand. Management stated that fourth-quarter fiscal 2019 comparable sales (comps) till date were nearly flat compared with 6% increase in the year-ago quarter.

Moreover, the company reiterated the previously issued fiscal fourth-quarter earnings guidance. It continues to anticipate earnings per share of 34-36 cents, which indicates a decline from 43 cents recorded in the year-ago quarter. Also, the Zacks Consensus Estimate for the current quarter is pegged at 37 cents per share, which is higher than the company's guidance. Markedly, the aforementioned earnings guidance does not include the impacts of tax reform as well as potential asset impairment and restructuring charges.

American Eagle Announces Quarterly Dividend – Dec 18, 2019

American Eagle declared a quarterly cash dividend of 13.75 cents per share, payable on Dec 17, 2019 to shareholders with record as of Jan 3, 2020.

Valuation

American Eagle shares are down 2.7% in the year-to-date period and 31.5% over the trailing 12-month period. Stocks in the Zacks sub-industry are down 1.8% but the Zacks Retail-Wholesale sector is up 3.5% in the year-to-date period. Over the past year, the Zacks sub-industry is down 27% while the sector is up 17.7%.

The S&P 500 index is up 3.3% in the year-to-date period and 20.2% in the past year.

The stock is currently trading at 9.64X forward 12-month earnings, which compares to 12.02X for the Zacks sub-industry, 25.41X for the Zacks sector and 19.12X for the S&P 500 index.

Over the past five years, the stock has traded as high as 20.88X and as low as 8.62X, with a 5-year median of 12.86X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$15 price target reflects 10.1X forward 12-month earnings.

The table below shows summary valuation data for AEO

Valuation Multiples - AEO					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	9.64	12.02	25.41	19.12
	5-Year High	20.88	18.38	26.2	19.34
	5-Year Low	8.62	10.23	19.07	15.18
	5-Year Median	12.86	14.24	23	17.47
P/S F12M	Current	0.53	0.6	1.07	3.53
	5-Year High	1.26	1.34	1.1	3.53
	5-Year Low	0.51	0.54	0.8	2.54
	5-Year Median	0.82	0.81	0.92	3
EV/EBITDA TTM	Current	7.33	8.65	15.71	11.36
	5-Year High	10.58	8.9	15.71	12.85
	5-Year Low	3.46	4.71	10.79	8.47
	5-Year Median	6.34	6.74	12.39	10.7

As of 02/10/2020

Industry Analysis Zacks Industry Rank: Top 27% (68 out of 255)



Top Peers

Buckle, Inc. (The) (BKE)	Outperform
Guess?, Inc. (GES)	Outperform
Abercrombie & Fitch Company (ANF)	Neutral
Foot Locker, Inc. (FL)	Neutral
The Gap, Inc. (GPS)	Neutral
PVH Corp. (PVH)	Neutral
L Brands, Inc. (LB)	Underperform
Urban Outfitters, Inc. (URBN)	Underperform

Industry Comparison Industry: Retail - Apparel And Shoes				Industry Peers		
	AEO Neutral	X Industry	S&P 500	ANF Neutral	BKE Outperform	URBN Underperform
VGM Score	B	-	-	C	A	B
Market Cap	2.39 B	828.79 M	24.17 B	1.06 B	1.27 B	2.58 B
# of Analysts	9	3	13	10	1	12
Dividend Yield	3.85%	0.00%	1.77%	4.75%	4.64%	0.00%
Value Score	A	-	-	A	A	A
Cash/Price	0.11	0.13	0.04	0.39	0.20	0.13
EV/EBITDA	6.74	7.65	13.89	7.47	8.34	6.69
PEG Ratio	1.36	1.30	2.05	0.90	NA	1.12
Price/Book (P/B)	1.92	1.68	3.27	1.07	3.05	1.81
Price/Cash Flow (P/CF)	5.82	5.87	13.60	4.69	10.01	6.76
P/E (F1)	9.76	12.43	19.00	13.79	13.14	11.45
Price/Sales (P/S)	0.56	0.49	2.66	0.29	1.43	0.66
Earnings Yield	10.35%	7.82%	5.26%	7.24%	7.61%	8.72%
Debt/Equity	1.07	1.05	0.71	1.48	0.69	0.78
Cash Flow (\$/share)	2.46	1.51	6.89	3.59	2.59	3.90
Growth Score	C	-	-	F	B	D
Hist. EPS Growth (3-5 yrs)	14.64%	-0.69%	10.85%	-3.52%	-12.87%	9.20%
Proj. EPS Growth (F1/F0)	0.61%	8.69%	7.22%	81.58%	-4.37%	8.69%
Curr. Cash Flow Growth	14.78%	9.92%	8.88%	8.78%	1.12%	33.74%
Hist. Cash Flow Growth (3-5 yrs)	9.35%	-0.29%	8.36%	-7.00%	-8.74%	0.23%
Current Ratio	1.33	1.50	1.22	1.41	2.33	1.57
Debt/Capital	51.79%	51.44%	42.90%	59.75%	40.72%	43.91%
Net Margin	6.20%	2.74%	11.81%	1.52%	11.03%	5.96%
Return on Equity	21.25%	10.96%	16.98%	5.30%	24.46%	16.67%
Sales/Assets	1.42	1.33	0.54	1.13	1.12	1.33
Proj. Sales Growth (F1/F0)	4.68%	2.46%	4.06%	1.98%	-0.93%	4.00%
Momentum Score	B	-	-	D	B	B
Daily Price Chg	0.35%	0.00%	0.45%	1.44%	1.81%	1.74%
1 Week Price Chg	-1.04%	0.84%	2.47%	1.53%	4.18%	1.29%
4 Week Price Chg	-2.05%	-2.05%	0.95%	-6.34%	-0.35%	1.11%
12 Week Price Chg	-9.26%	-2.67%	5.05%	-1.35%	10.17%	-12.53%
52 Week Price Chg	-33.15%	-13.66%	16.18%	-23.83%	45.21%	-15.31%
20 Day Average Volume	3,143,419	235,503	1,999,386	1,720,367	436,228	1,160,057
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.51%	0.00%
(F1) EPS Est 4 week change	0.00%	0.00%	0.00%	0.41%	0.51%	-0.11%
(F1) EPS Est 12 week change	-9.65%	0.00%	-0.18%	-3.40%	10.06%	-9.28%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.00%	0.00%	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	A
Growth Score	C
Momentum Score	B
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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