

Carters, Inc. (CRI)

\$67.39 (As of 04/02/20)

Price Target (6-12 Months): **\$71.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 05/01/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:A

Value: B

Growth: A

Momentum: B

Summary

Shares of Carter's have lagged the industry in the past three months. The stock remains under pressure due to the ongoing global COVID-19 crisis. It expects the coronavirus outbreak to significantly affect the results. It has closed all stores across the United States and Canada and withdrew its first quarter and 2020 view. Further, the company's top and bottom lines lagged the Zacks Consensus Estimate during fourth-quarter 2019. Results were impacted by soft wholesale businesses along with higher expenses. Moreover, soft margins remained a drag. However, the company's omni-channel efforts bode well, as e-commerce continues to be its highest margin business. Also, it is gaining from momentum in the international business, driven by growth in markets outside North America, especially Canada.

Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$112.46 - \$60.17
20 Day Average Volume (sh)	878,441
Market Cap	\$3.0 B
YTD Price Change	-38.4%
Beta	1.19
Dividend / Div Yld	\$2.40 / 3.6%
Industry	Shoes and Retail Apparel
Zacks Industry Rank	Bottom 28% (182 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-2.8%
Last Sales Surprise	0.3%
EPS F1 Est- 4 week change	-8.2%
Expected Report Date	05/05/2020
Earnings ESP	-8.8%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					3,611 E
2020	719 E	723 E	971 E	1,156 E	3,570 E
2019	741 A	734 A	943 A	1,101 A	3,519 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$6.96 E
2020	\$0.49 E	\$0.84 E	\$2.00 E	\$3.20 E	\$6.22 E
2019	\$0.87 A	\$0.95 A	\$1.87 A	\$2.81 A	\$6.46 A

*Quarterly figures may not add up to annual.

P/E TTM	10.4
P/E F1	10.8
PEG F1	1.4
P/S TTM	0.8

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 04/02/2020. The reports text is as of 04/03/2020.

Overview

Headquartered in Atlanta, GA, Carter's Inc. is the largest marketer of branded apparel and related products for babies, and young children in North America.

Notably, the company has a portfolio of popular brands, including Carter's, OshKoshB'gosh, Just One You, Child of Mine, Simple Joys, Skip Hop, and Precious Firsts. It sells the products through leading department stores, national chains and specialty retailers, both domestically and internationally. Additionally, Carter's showcases its products through company-operated stores in the United States, Canada and Mexico, and its websites namely www.carters.com, www.oshkoshbgosh.com and www.cartersoshkosh.ca.

The company generated \$3.5 billion in net sales in 2019. As of Dec 28, 2019, it operated 862 stores in the United States, 201 in Canada and 46 in Mexico. Additionally, it had a solid wholesale presence in the United States (including department stores, national chain stores, specialty stores and discount retailers). It also operates through e-commerce sites in the United States, Canada and China as well as other international wholesale, licensing and online channels.

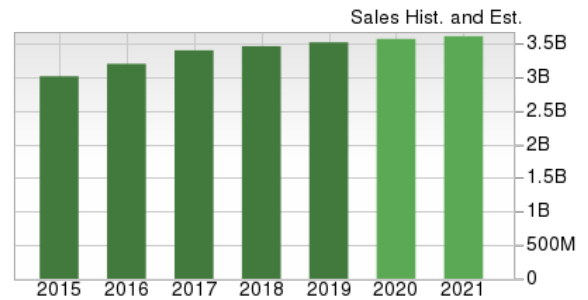
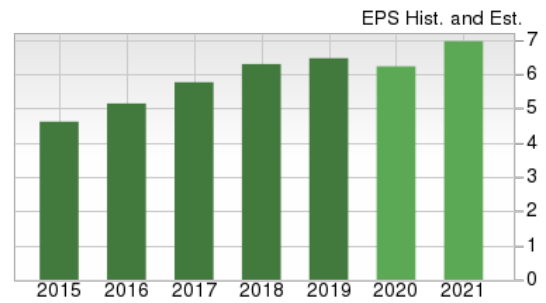
Of all the brands, Carter's and OshKoshB'gosh are the two most recognized and trusted names for young children's apparel. Among the rest, its Genuine Kids and Just One You brands are sold at Target, Child of Mine brand is sold at Walmart and Simple Joys brand is available on Amazon. The company's Skip Hop brand is a fast-growing global lifestyle brand and innovative leader in the children's durables product category.

The company's reportable segments include U.S. Retail, U.S. Wholesale and International.

The **U.S. Retail** segment includes the sale of its products through its U.S. retail and e-commerce websites.

The **U.S. Wholesale** segment consists of revenues, primarily from the sale of products to its U.S. wholesale partners.

The **International** segment comprises the sale of products outside the United States through its company and franchisee-operated retail stores in Canada and Mexico, e-commerce sites in Canada and China, and sales to its international wholesale customers.



Reasons To Buy:

- ▲ **Retail Strategy — Co-branded Stores:** Carter's Retail strategy remains focused on improving store productivity, strengthening e-commerce business and enhancing product offerings by introducing extended sizes for the Carter's brand and expanding Skip Hop brand offerings. The company had estimated net sales for Skip Hop to increase nearly 20% globally in 2019, contributing to total profitability. Additionally, the company is witnessing a positive response for its co-branded stores, which is a one-stop shop for families with young children. These stores have been the most productive lately, receiving the maximum return on investment. In the third quarter, co-branded stores were one of the best performing store types. The company opened four co-branded stores in Mexico during 2019. Moreover, it launched e-commerce operations in Mexico during the fourth quarter. Backed by the success of this store type, management plans to open more than 100 co-branded stores through 2024. Additionally, it earlier envisioned over 80% of its stores to be co-branded by 2021.
 - ▲ **E-commerce Growth:** Carter's is seeking opportunities to strengthen e-commerce capabilities through investments to speed up deliveries. The company's e-commerce operations performed well in the fourth quarter. Notably, e-commerce sales grew 36% in the fourth quarter, with e-commerce penetration improving to 32% in 2019. Carter's move to relaunch its website led to a significant rise in conversion and sales growth. Additionally, the company is making investments to strengthen its mobile app, which is likely to be re-launched in 2020. Further, the company's brands are sold online at sites of its wholesale customers. Going ahead, management anticipates e-commerce penetration to surge to 42% by 2024.
 - ▲ **Omni-Channel Capabilities:** Carter's has been making efforts to enhance omni-channel capabilities. In this regard, the company is gaining from its same-day pickup service for online orders, easy access to a broad array of online products when shopping in stores and easy access to its new credit card program. This has led to an increase of 44% in multi-channel customers, driven by improved experiences. The company's same day buy online, pick up in store facility gained momentum during the holiday season. Further, shift in consumer preferences to the pick-up in store option over online home delivery led to a rise in store traffic. Following successful testing of its pick-up in store service from certain store locations, the company now intends to expand this facility to all the stores within the second half of 2020.
 - ▲ **International Segment Gets Back on Track:** After reporting sluggish performances for a while, Carter's international segment has been experiencing decent growth for the past two quarters. Notably, sales in this segment witnessed nearly a 2.4% rise in revenues to \$131.7 million in the fourth quarter, following a 1% rise in the third quarter. The uptick was driven by growth in markets outside North America and favorable impact of currency fluctuations, partly offset by the change in business model in China. Also, solid performance in Canada coupled with comparable retail sales growth of 8% contributed to the segment sales. Further, management expects its international business to account for 14% of total sales by 2024. The company's multichannel operations in Canada and Mexico are anticipated to drive 70% of international sales growth, in the next five years.
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Carter's Retail strategy is focused on improving store productivity, strengthening e-commerce business and enhancing product offerings for the Carter's and Skip Hop brands.

Reasons To Sell:

- ▼ **COVID-19 Compels to Withdraw Outlook, Stock Underperforms:** The crippling effect of the coronavirus outbreak has been leading to supply-chain disruptions, slowdown in production activities and reduced demand for several commodities. In the view of implementation of safety measures and a drop in store footfall, companies are temporarily shutting down their brick-and-mortar stores, curtailing work hours and operating in shifts, or permitting employees to work remotely. In response, Carter's temporarily closed all stores in the United States and Canada starting from Mar 19. The clothing retailer has also chosen to withdraw its first quarter and 2020 guidance. Also, it withdrew \$750 million from its revolving credit facility to add to its cash balance. Given this tough situation, shares of the company have plunged 38.9% in the past three months compared with the industry's decline of 24.5%.

Carter's is reeling under the COVID-19 impact, which has compelled it to withdraw first quarter and 2020 guidance. Also, high costs and soft margins remain concerns.
 - ▼ **Elevated Expenses Weigh on Q4 Earnings:** Carter's reported fourth-quarter 2019 results, wherein top and bottom lines lagged the Zacks Consensus Estimate. Moreover, adjusted earnings declined 1.1% year over year owing to higher expenses and interest expenses. Notably, SG&A expenses rose 1.5% to roughly \$312 million. Also, interest expenses increased 1.9% to \$8.9 million during the reported quarter. Moreover, the impact of lower traffic to its U.S. retail stores also hurt the bottom line to some extent.
 - ▼ **Dismal Margin Trend:** After gross margin expansion in the third quarter, Carter's gross margin contracted 70 basis points (bps) to 42.5% in fourth-quarter 2019 due to an increase in inventory and higher tariffs on products from China. Earlier, the metric contracted 50 basis points (bps) 140 bps and 170 bps contraction in the second and first quarter 2019, as well as fourth-quarter 2018, respectively. Further, adjusted operating income decreased 4.6% to \$162.8 million in the fourth quarter. Adjusted operating margin contracted 100 bps to 14.7%, due to decline in gross margin. Persistence of this trend may weigh on the company's profitability in the near term.
 - ▼ **Macroeconomic Factors May Impact Discretionary Sales:** The company's customers remain sensitive to macroeconomic factors including interest rate hikes, increase in fuel and energy costs, credit availability, unemployment levels, and high household debt levels, which may negatively impact their discretionary spending, and in turn the company's growth and profitability.
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Last Earnings Report

Carter's Q4 Earnings & Sales Miss Estimates

Carter's reported fourth-quarter 2019 results, wherein top and bottom lines lagged the Zacks Consensus Estimate. Moreover, earnings declined on a year-over-year basis, while sales improved. Results were impacted by soft wholesale businesses along with higher expenses.

Q4 Highlights

Carter's fourth-quarter 2019 adjusted earnings of \$2.81 per share decreased 1.1% year over year and missed the Zacks Consensus Estimate of \$2.89. This might be attributed to higher SG&A expenses and interest expenses. On a GAAP basis, the company reported earnings per share of \$2.82 compared with \$2.83 earned in the year-ago quarter.

Net sales grew 1.3% to \$1,100.5 million but marginally missed the Zacks Consensus Estimate of \$1,102 million, owing to growth in retail and international segments. Also, favorable foreign currency aided the top line by \$0.3 million.

Segmental Sales

Sales at the U.S. Retail segment rose 2.2% year over year to \$619.9 million. Comparable sales (comps) increased 1.6%, driven by growth in e-commerce sales.

The U.S. Wholesale segment witnessed decrease in sales of 0.7% to \$348.9 million, owing to decrease in off-price channel sales and increased demand for the exclusive Carter's brand.

The International segment witnessed nearly 2.4% rise in revenues to \$131.7 million in the fourth quarter due to growth in markets outside North America, partly offset by the change in business model in China and favorable impact of currency fluctuations. Currency-neutral revenues for the segment increased \$0.3 million.

Margins

Gross profit was almost flat on a year-over-year basis, at \$467.5 million and gross margin contracted 70 basis points (bps) to 42.5%. Adjusted operating income decreased 4.6% to \$162.8 million. Adjusted operating margin contracted 100 bps to 14.7%, due to decline in gross margin.

Balance Sheet & Shareholder-Friendly Moves

The company ended the quarter with cash and cash equivalents of \$214.3 million, net long-term debt of \$594.7 million, and shareholders' equity of \$880.1 million. Inventories as of Dec 28, 2019, increased 3.4% to \$594 million.

In 2019, the company generated \$387,215 million in operating cash flow. Capital expenditure in the quarter totaled \$61.4 million.

During the fourth quarter and 2019, Carter's returned nearly \$71.5 million and \$286.5 million, respectively, to its shareholders through dividend payout and share buybacks. In the quarter, the company bought back 499,552 shares for \$49.4 million, the average price being \$98.98 per share. It paid out a dividend of 50 cents per share in the reported quarter. Year-to-date through Feb 21, 2020, the company has repurchased 220,943 shares for \$24.1 million at an average price of \$108.94 per share.

The company approved a new incremental \$500 million share repurchase authorization and increased quarterly dividend by 20% to 60 cents per share effective with the dividend to be paid out next month.

Store Update

In the fourth quarter, Carter's opened 20 retail stores and shut three in the United States. As of Dec 28, 2019, the company operated 862 retail stores in the United States alongside 201 in Canada and 46 in Mexico.

Outlook

Management issued guidance for 2020. The company anticipates top-line growth of roughly 2-3% in 2020. Adjusted earnings are expected to improve nearly 4-6% from \$6.46 reported in 2019. Earnings view excludes anticipated expenses of around \$10-\$12 million related to organizational restructurings.

For the first quarter of 2020, the company projects net sales to be comparable to the first quarter of 2019. Adjusted diluted earnings per share are expected to be around 60 cents compared with 87 cents earned in the first quarter of 2019.

The outbreak of coronavirus in China has given rise to a tough situation for companies operating in the region. The virus has affected several industries within China, including textile production and manufacturing. The company plans to source around 15% of its products from China in 2020. However, its first-quarter and 2020 guidance do not include any adjustments for potential effects of the coronavirus situation.

Quarter Ending **12/2019**

Report Date	Feb 24, 2020
Sales Surprise	0.34%
EPS Surprise	-2.77%
Quarterly EPS	2.81
Annual EPS (TTM)	6.50

Recent News

Carter's Withdraws Guidance on COVID-19 Impact – Mar 26, 2020

Carter's withdrew its first quarter and 2020 outlook due to the unprecedented impact of COVID-19. Also, management has withdrawn \$750 million available from its revolving credit facility in a bid to strengthen financial stability. Keeping in these lines, the company has decided to cut on its capital spending and other expenses along with inventory. Further, it has suspended its share repurchase program.

Prior to this, the company closed stores in United States and Canada starting from Mar 19 in order to curb the spread of COVID-19. During this time, all employees will be paid salaries and other benefits till early April. Moreover, employees are entitled to additional assistance if store closures are extended beyond April.

Valuation

Carter's shares are down 38.4% in the year-to-date period and 34.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Discretionary sector are down 24.1% and 31%, respectively, in the year-to-date period. Over the past year, the Zacks sub-industry and the sector are down 10.6% and 24.4%, respectively.

The S&P 500 index is down 21.5% in the year-to-date period and 12.4% in the past year.

The stock is currently trading at 9.75X forward 12-month earnings, which compares to 22.64X for the Zacks sub-industry, 16.11X for the Zacks sector and 15.78X for the S&P 500 index.

Over the past five years, the stock has traded as high as 22.05X and as low as 9.31X, with a 5-year median of 16.11X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$71 price target reflects 10.27X forward 12-month earnings.

The table below shows summary valuation data for CRI

Valuation Multiples - CRI					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	9.75	22.64	16.11	15.78
	5-Year High	22.05	26.48	23.23	19.34
	5-Year Low	9.31	18.63	16.11	15.18
	5-Year Median	15.85	23.21	19.88	17.44
P/S F12M	Current	0.84	2.59	1.86	2.74
	5-Year High	1.96	3.5	3.67	3.69
	5-Year Low	0.79	2.07	1.72	2.43
	5-Year Median	1.41	2.85	2.95	3.19
EV/EBITDA TTM	Current	8.41	17.85	8.73	9.36
	5-Year High	14.34	24.5	17.6	12.88
	5-Year Low	8	12.4	8.26	8.27
	5-Year Median	11.06	16.01	12.26	10.78

As of 04/02/2020

Industry Analysis Zacks Industry Rank: Bottom 28% (182 out of 254)



Top Peers

Deckers Outdoor Corporation (DECK)	Neutral
The Gap, Inc. (GPS)	Neutral
Ralph Lauren Corporation (RL)	Neutral
Abercrombie & Fitch Company (ANF)	Underperform
Caleres, Inc. (CAL)	Underperform
Delta Apparel, Inc. (DLA)	Underperform
NIKE, Inc. (NKE)	Underperform
Steven Madden, Ltd. (SHOO)	Underperform

Industry Comparison Industry: Shoes And Retail Apparel				Industry Peers		
	CRI Neutral	X Industry	S&P 500	ANF Underperform	GPS Neutral	RL Neutral
VGM Score	A	-	-	D	A	A
Market Cap	2.96 B	1.17 B	17.16 B	500.10 M	2.04 B	4.86 B
# of Analysts	4	4	13	10	11	6
Dividend Yield	3.56%	1.26%	2.5%	10.04%	17.64%	4.17%
Value Score	B	-	-	A	A	A
Cash/Price	0.07	0.15	0.06	1.08	0.57	0.38
EV/EBITDA	8.65	7.41	10.80	4.62	6.15	5.64
PEG Ratio	1.40	0.84	1.74	1.08	0.37	1.00
Price/Book (P/B)	3.38	1.38	2.33	0.47	0.62	1.56
Price/Cash Flow (P/CF)	7.65	7.65	9.11	2.26	1.58	5.93
P/E (F1)	10.71	12.03	14.73	19.39	4.44	9.37
Price/Sales (P/S)	0.84	0.57	1.81	0.14	0.12	0.76
Earnings Yield	9.23%	8.33%	6.71%	5.14%	22.55%	10.67%
Debt/Equity	1.43	0.40	0.70	1.39	2.04	0.65
Cash Flow (\$/share)	8.81	2.97	7.01	3.53	3.49	11.12
Growth Score	A	-	-	D	B	B
Hist. EPS Growth (3-5 yrs)	10.03%	9.27%	10.92%	-0.50%	-2.19%	1.80%
Proj. EPS Growth (F1/F0)	-3.68%	2.78%	1.02%	-43.70%	-37.06%	-5.21%
Curr. Cash Flow Growth	0.60%	0.43%	5.93%	-6.25%	-14.41%	9.60%
Hist. Cash Flow Growth (3-5 yrs)	6.40%	6.04%	8.55%	-7.00%	-5.36%	-3.42%
Current Ratio	2.33	1.90	1.24	1.55	1.41	1.94
Debt/Capital	58.86%	34.67%	42.33%	58.09%	67.08%	39.49%
Net Margin	7.50%	6.55%	11.67%	1.09%	2.14%	10.40%
Return on Equity	34.62%	17.13%	16.70%	4.61%	21.04%	20.83%
Sales/Assets	1.27	1.20	0.54	1.05	1.18	0.91
Proj. Sales Growth (F1/F0)	1.45%	1.34%	1.54%	-2.64%	-5.66%	-0.34%
Momentum Score	B	-	-	F	C	B
Daily Price Chg	7.31%	0.24%	1.45%	-2.45%	-6.62%	0.43%
1 Week Price Chg	4.74%	16.99%	12.29%	14.04%	7.89%	2.07%
4 Week Price Chg	-22.98%	-27.24%	-21.33%	-31.71%	-58.83%	-39.02%
12 Week Price Chg	-37.27%	-38.70%	-28.56%	-54.06%	-68.45%	-44.06%
52 Week Price Chg	-34.18%	-35.82%	-22.55%	-70.08%	-79.42%	-48.61%
20 Day Average Volume	878,441	170,202	4,257,668	3,647,356	12,425,589	1,635,143
(F1) EPS Est 1 week change	0.00%	0.00%	-0.04%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-8.22%	-7.19%	-4.30%	-66.14%	-26.98%	-18.84%
(F1) EPS Est 12 week change	-10.21%	-10.79%	-5.47%	-65.89%	-25.66%	-15.51%
(Q1) EPS Est Mthly Chg	-15.23%	-19.25%	-5.91%	-82.51%	-171.62%	-17.24%

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	A
Momentum Score	B
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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