

Dillards Inc. (DDS)

\$69.91 (As of 01/10/20)

Price Target (6-12 Months): **\$73.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 11/01/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:B

Value: A

Growth: C

Momentum: F

Summary

Shares of Dillard's have outpaced the industry in the past year. The stock also recently received a boost from the strong third-quarter fiscal 2019 results. Earnings beat the Zacks Consensus Estimate in the quarter on sequential gains in comps and retail gross margin. Further, reduced inventory levels aided results. Moreover, the company has been benefiting from growth opportunities in physical stores and e-commerce. Also, it is gaining from initiatives to enhance brand relations, focus on in-trend categories, store remodels and increased rewards to store personnel. Furthermore, its focus on boosting productivity as well as enhancing domestic and omni-channel capabilities should strengthen the customer base. However, elevated SG&A expenses and soft revenues in the fiscal third quarter hurt the bottom line on a year-over-year basis.

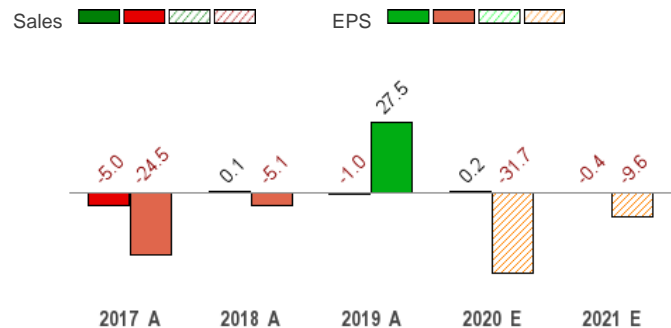
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$86.71 - \$47.95
20 Day Average Volume (sh)	199,753
Market Cap	\$1.7 B
YTD Price Change	-4.8%
Beta	1.14
Dividend / Div Yld	\$0.60 / 0.9%
Industry	Retail - Regional Department Stores
Zacks Industry Rank	Bottom 20% (204 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	179.3%
Last Sales Surprise	-1.1%
EPS F1 Est- 4 week change	-0.2%
Expected Report Date	02/24/2020
Earnings ESP	14.7%
P/E TTM	15.6
P/E F1	16.7
PEG F1	1.7
P/S TTM	0.3

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,473 E	1,429 E	1,375 E	1,991 E	6,348 E
2020	1,465 A	1,459 A	1,388 A	2,024 E	6,371 E
2019	1,491 A	1,501 A	1,455 A	2,011 A	6,356 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.66 E	-\$1.32 E	-\$0.36 E	\$2.67 E	\$3.78 E
2020	\$2.77 A	-\$1.74 A	\$0.23 A	\$2.97 E	\$4.18 E
2019	\$2.89 A	-\$0.10 A	\$0.27 A	\$3.22 A	\$6.12 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 01/10/2020. The reports text is as of 01/13/2020.

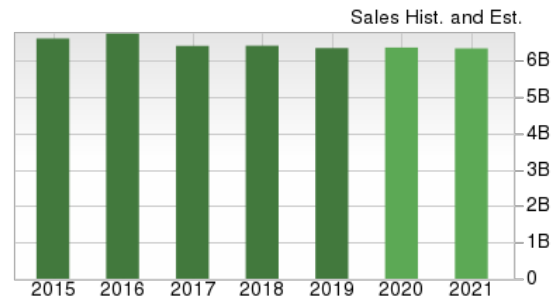
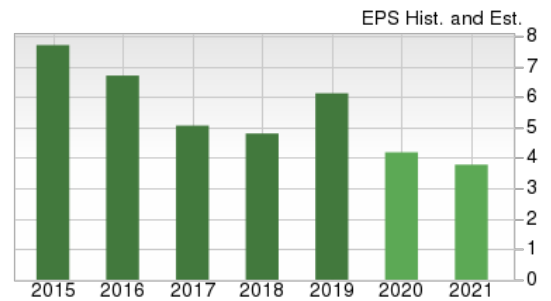
Overview

Dillard's Inc. is a large departmental store chain featuring fashion apparel and home furnishings. As of Nov 2, 2019, Dillard's had about 259 namesake outlets and 30 clearance centers operating in 29 states. The company also sells its merchandise through the Internet at www.dillards.com. Stores are mainly located in the Southwest, Southeast, and Midwest regions of the United States.

The company's primary product categories comprise women's and children's apparel, shoes, accessories and lingerie, men's clothing and accessories, cosmetics, home, and children's clothing. Its merchandise mix consists of both branded and private-label items. The company's strategy is to offer more fashion-forward and trendy products in order to attract customers.

Dillard's also owns a real estate investment trust (REIT), which helps it to enhance its liquidity position. Revenues of a REIT company mostly come from either rent or mortgage payments. The company has an obligation to distribute at least 90% of its taxable income to investors in the form of dividends. A REIT company does not have to pay taxes at the corporate level.

Moreover, Dillard's has a wholly owned captive insurance company, which enables it to manage its risks more efficiently and provide access to more reinsurance markets. A captive insurance company is an 'in-house' insurance company with limited purpose, which insures the risks of its parent company. The captive insurance company may reinsure some or all risks, or may retain such risks of its parent company. The primary goal of forming a captive insurance company is to retain the profit that would have been made by an outside third-party insurance company or in a situation where the coverage is not available for business risks.



Reasons To Buy:

- ▲ **Q3 Strong, Stock Outperforms:** Shares of Dillard's have witnessed momentum lately, following the better-than-expected earnings in third-quarter fiscal 2019. Earnings benefited from sequential gains in comparable sales (comps) as well as retail gross margin. Further, reduced inventory levels boosted performance. Notably, the company's shares have gained 9% in the past year against the industry's decline of 28.9%.
- ▲ **Sequential Comps and Gross Margin Gains:** In third-quarter fiscal 2019, Dillard's reported flat comps compared with a 3% increase in the year-ago quarter. However, comps for the quarter under review reflected an improvement on a sequential basis from a 2% decline reported in second-quarter fiscal 2019. Notably, the eastern region performed exceedingly well, followed by western and central regions. Further, the company's consolidated gross margin expanded 53 basis points (bps) in the fiscal third quarter. Gross margin from retail operations rose 13 bps mainly due to lower inventory levels. Notably, gross margin from retail stores reflected significant gain on a sequential basis from a decline of 319 bps reported in second-quarter fiscal 2019. Notably, merchandise inventories declined nearly 4% as of Nov 2, 2019, favorable compared with flat inventories at the end of second-quarter fiscal 2019.
- ▲ **Growth Initiatives to Boost Customer Base:** Though the department store industry is facing headwinds related to increased competition from specialty retailers and inability to catch up with growing e-commerce. However, Dillard's is shielded by its efforts to capture growth opportunities in brick-and-mortar stores and e-commerce business, which will likely help in retaining existing customers and attract new ones. On the store front, the company is gaining from initiatives to enhance brand relations, focus on in-trend categories, store remodels and increased rewards to store personnel. Moreover, its e-commerce business is catching pace with strategies like enhancement of merchandise assortments and effective inventory management. We expect the company to gain from its focus on increasing productivity at existing stores, developing a leading omni-channel platform and enhancing domestic operations in the years ahead.
- ▲ **Fashionable and Trendy Merchandise Offerings:** Dillard's is a leading player among fashion apparel, cosmetics and home furnishing retailers. The company offers a broad array of merchandise in its stores, featuring products from both national and exclusive brands. The company has created a niche for itself through stringent focus on offering fashionable products to its customers and adding value through exceptional customer care service. We believe that the company's strategy of offering fashion-forward and trendy products acts as a catalyst for attracting more customers.
- ▲ **Shareholder-Friendly Moves:** Dillard's healthy cash flows provide the financial flexibility to undertake shareholder-friendly moves as well as engage in-store and online business expansion. In the first nine months of fiscal 2019, the company generated operating cash flow of \$23 million. Further, it remained committed to rewarding shareholders with dividends and buybacks. During the fiscal third quarter, the company bought back 0.6 million shares for \$35.2 million under its \$500-million repurchase program announced in March 2018. As of Nov 2, 2019, it had share buyback authorization worth \$305.4 million remaining under its program. The company also declared a cash dividend of 15 cents per share, payable on Feb 3, 2020.

Dillard's is poised to benefit from the focus on increasing productivity at existing stores, developing a leading omni-channel platform and enhancing domestic operations in the years ahead.

Reasons To Sell:

- ▼ **Stock Appears Overvalued:** Considering price-to-earnings (P/E) ratio, Dillard's looks overvalued compared with the industry. The stock has a trailing 12-month P/E ratio of 15.61x, compared with 8.31x for the industry. Its trailing 12-month P/E ratio is above the median level of 11.99x and below the high level of 17.29x.
- ▼ **Higher SG&A Expenses:** Though Dillard's witnessed gross margin growth in the fiscal third quarter, elevated SG&A expense rate (or operating expense rate) hurt the bottom line on a year over year basis. Notably, SG&A expenses (as a percentage of sales) rose 60 bps from the prior-year quarter to 30.1%. Further, retail operating expenses (as a percentage of sales) for the quarter under review increased 10 bps to 31.2%. In dollar terms, retail operating expenses were nearly flat at \$416.6 million. Driven by higher expenses, the company's bottom line declined 14.8% on a year-over-year basis. Moreover, the persistence of higher expenses remains a threat to the company's earnings in the quarters ahead.
- ▼ **Competitive Threat:** Dillard's operates in the highly competitive retail merchandise industry. Although it is a large regional department store, the company has many rivals at the national level competing with its individual stores, including specialty, off-price, discount, Internet and mail-order retailers. On losing its competitive position, the company might face downward pressure on prices, lower demand for its products as well as reduced margins. Further, the company will not be able to capitalize on new business opportunities and lose much of its market share.
- ▼ **Industry Challenges:** The retail merchandise business is prone to changes in consumer preferences and spending patterns, demographic trends, consumer credit availability and location of competing stores. Like most of its department store peers, the company is facing troubles due to the growth of the e-commerce era. Despite the company's efforts, investors are likely to be skeptical on the department store industry and Dillard's until it fully adapts to the online business.
- ▼ **Volatility in Raw Material Prices:** Dillard's has faced fluctuations in raw material prices in the past and remains prone to this threat in the future too. Any increase in raw material prices or price of labor and fuel can prove to be detrimental to the company's profitability. On the other hand, efforts to pass on these price hikes to consumers may lead to reduced sales volumes. Consequently, raw material price volatility and its reduced availability remain concerns for the company.

Soft revenues and elevated SG&A expenses hurt Dillard's bottom line on a year-over-year basis in third-quarter fiscal 2019 despite rise in gross margin.

Last Earnings Report

Dillard's Q3 Earnings Beat Estimates

Dillard's reported better-than-expected earnings in third-quarter fiscal 2019. Moreover, its comparable store sales (comps) and retail gross margin marked a significant improvement sequentially. Further, significantly lower inventory levels aided results.

Q3 Numbers

Dillard's reported adjusted earnings of 23 cents, significantly beating the Zacks Consensus Estimate of a loss of 29 cents. However, the bottom line declined 14.8% from the year-ago quarter's earnings of 27 cents per share.

Net sales of \$1,423.6 million declined 2.2% from the year-ago quarter. Excluding services and other income, sales fell 2.2% to \$1,388.3 million. Merchandise sales (excluding CDI Contractors, LLC) dipped 0.6% to \$1,334 million. The Zacks Consensus Estimate for sales was \$1,404 million.

Comparable store sales (comps) for 13 weeks (ended Nov 2, 2019) remained flat compared with a 3% increase in the year-ago quarter. However, comps for the quarter under review reflected an improvement on a sequential basis from a 2% decline reported in second-quarter fiscal 2019. Notably, the eastern region performed exceedingly well, followed by western and central regions.

Consolidated gross margin expanded 53 basis points (bps) in the fiscal third quarter. Gross margin from retail operations improved 13 bps mainly due to lower inventory levels. Notably, gross margin from retail stores reflected significant gain on a sequential basis from a decline of 319 bps reported in second-quarter fiscal 2019.

Dillard's SG&A expenses (as a percentage of sales) rose 60 bps from the prior-year quarter to 30.1%. In dollar terms, SG&A expenses (operating expenses) dipped 0.2% to \$418.1 million. Meanwhile, retail operating expenses (as a percentage of sales) for the quarter under review increased 10 bps to 31.2%. In dollar terms, retail operating expenses were nearly flat at \$416.6 million.

Financial Details

The company ended the fiscal third quarter with cash and cash equivalents of \$79.1 million, long-term debt and finance leases of \$366.7 million, and total shareholders' equity of \$1,612.4 million. As of Nov 2, 2019, merchandise inventories declined nearly 4% to \$1,970 million. This compared favorably with flat inventories at the end of second-quarter fiscal 2019.

In the first nine months of fiscal 2019, the company generated operating cash flow of \$23 million. Moreover, it remained committed to rewarding shareholders with dividends and buybacks.

During the fiscal third quarter, the company bought back 0.6 million shares for \$35.2 million under its \$500-million repurchase program announced in March 2018. As of Nov 2, 2019, it had share buyback authorization worth \$305.4 million remaining under its program.

Store Update

As of Nov 2, 2019, Dillard's had about 259 namesake outlets and 30 clearance centers, operating in 29 states, alongside an online store at www.dillards.com. The company's total square footage as of Nov 2 was 48.9 million.

Further, it announced plans to open three stores by the end of fiscal 2019 and in the first quarter of fiscal 2020. Notably, the company plans to open expanded stores at Killeen Mall in Killeen, TX; Columbia Mall in Columbia, MO; and Richland Fashion Mall in Waco, TX. All these facilities will be dual-anchored locations, with two company-owned stores replacing existing leased stores. The company expects to open the Killeen-based store by the end of fiscal 2019, Columbia-based store in the first quarter of fiscal 2020 and the Waco-based store by early 2020.

Additionally, Dillard's announced planned closure of the Fiesta Mall Clearance Center in Mesa, AR, by January 2020.

Fiscal 2019 View

For fiscal 2019, Dillard's expects rentals of \$27 million compared with \$29 million in fiscal 2018. It anticipates net interest and debt expenses of \$46 million, suggesting a decline from \$53 million in fiscal 2018. Furthermore, the company now projects capital expenditure of \$115 million for fiscal 2019 compared with \$125 million stated earlier. Notably, it spent \$137 million in fiscal 2018.

For fiscal 2019, the company projects depreciation and amortization expenses of \$224 million, suggesting no change from the fiscal 2018 level.

Quarter Ending **10/2019**

Report Date	Nov 14, 2019
Sales Surprise	-1.12%
EPS Surprise	179.31%
Quarterly EPS	0.23
Annual EPS (TTM)	4.48

Recent News

Dillard's Declares Quarterly Dividend – Nov 22, 2019

Dillard's declared a quarterly cash dividend of 15 cents per share on Class A and Class B shares, payable on Feb 3, 2020, to shareholders of record as of Dec 31, 2019.

Valuation

Dillard's shares are up 9% over the trailing 12-month period. Stocks in the Zacks sub-industry are down 28.9% but the Zacks Retail-Wholesale sector is up 21.2% over the past year.

The S&P 500 index is up 25.6% in the past year.

The stock is currently trading at 18.41X forward 12-month earnings, which compares to 11.79X for the Zacks sub-industry, 25.43X for the Zacks sector and 18.88X for the S&P 500 index.

Over the past five years, the stock has traded as high as 23.67X and as low as 8.1X, with a 5-year median of 12.64X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$73 price target reflects 19.22X forward 12-month earnings.

The table below shows summary valuation data for DDS

Valuation Multiples - DDS					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	18.41	11.79	25.43	18.88
	5-Year High	23.67	18.34	26.13	19.34
	5-Year Low	8.1	9.31	18.99	15.17
	5-Year Median	12.64	11.38	22.91	17.44
P/S F12M	Current	0.27	0.29	1.08	3.5
	5-Year High	0.83	0.73	1.1	3.5
	5-Year Low	0.22	0.26	0.8	2.54
	5-Year Median	0.32	0.41	0.9	3
EV/EBITDA TTM	Current	5.55	6.55	15.28	11.99
	5-Year High	7.68	8.43	15.3	12.86
	5-Year Low	3.5	4.66	10.27	8.48
	5-Year Median	5.04	6.4	12.33	10.67

As of 01/10/2020

Industry Analysis Zacks Industry Rank: Bottom 20% (204 out of 254)



Top Peers

Burlington Stores, Inc. (BURL)	Neutral
J. C. Penney Company, Inc. (JCP)	Neutral
Nordstrom, Inc. (JWN)	Neutral
Kohls Corporation (KSS)	Neutral
Macys, Inc. (M)	Neutral
Ross Stores, Inc. (ROST)	Neutral
The TJX Companies, Inc. (TJX)	Neutral
Walmart Inc. (WMT)	Neutral

Industry Comparison Industry: Retail - Regional Department Stores				Industry Peers		
	DDS Neutral	X Industry	S&P 500	JCP Neutral	KSS Neutral	M Neutral
VGM Score	B	-	-	C	A	C
Market Cap	1.73 B	5.50 B	24.03 B	323.20 M	7.26 B	5.50 B
# of Analysts	3	5	13	4	8	6
Dividend Yield	0.86%	1.19%	1.78%	0.00%	5.78%	8.48%
Value Score	A	-	-	C	A	A
Cash/Price	0.05	0.06	0.04	0.45	0.06	0.06
EV/EBITDA	4.60	5.20	14.04	8.85	5.57	4.83
PEG Ratio	1.70	0.92	2.02	NA	0.97	0.87
Price/Book (P/B)	1.08	1.00	3.32	0.37	1.36	0.91
Price/Cash Flow (P/CF)	4.68	3.24	13.52	1.22	4.05	2.44
P/E (F1)	16.72	9.65	18.82	NA	9.65	6.55
Price/Sales (P/S)	0.27	0.25	2.63	0.03	0.36	0.22
Earnings Yield	5.98%	8.17%	5.31%	-103.96%	10.35%	15.27%
Debt/Equity	0.37	1.16	0.72	5.90	1.09	1.24
Cash Flow (\$/share)	14.93	5.07	6.94	0.83	11.45	7.31
Growth Score	C	-	-	C	B	F
Hist. EPS Growth (3-5 yrs)	-8.49%	-1.58%	10.56%	NA	6.85%	-1.58%
Proj. EPS Growth (F1/F0)	-31.65%	-14.19%	7.49%	-11.17%	-14.22%	-34.97%
Curr. Cash Flow Growth	4.90%	6.93%	14.83%	-59.25%	11.63%	6.93%
Hist. Cash Flow Growth (3-5 yrs)	-7.34%	-2.50%	9.00%	18.26%	1.24%	-2.50%
Current Ratio	1.64	1.47	1.23	1.51	1.42	1.28
Debt/Capital	27.11%	53.72%	42.99%	85.51%	52.13%	55.31%
Net Margin	2.03%	2.77%	11.08%	-1.92%	3.50%	3.91%
Return on Equity	7.14%	11.17%	17.16%	-24.09%	15.19%	17.44%
Sales/Assets	1.74	1.39	0.55	1.39	1.40	1.18
Proj. Sales Growth (F1/F0)	-1.33%	-2.43%	4.20%	-7.51%	-2.61%	-2.25%
Momentum Score	F	-	-	A	C	A
Daily Price Chg	2.00%	0.51%	-0.33%	-5.61%	0.46%	0.56%
1 Week Price Chg	-5.53%	-2.25%	-0.30%	-3.51%	-3.44%	0.12%
4 Week Price Chg	-1.28%	0.44%	1.71%	-10.62%	-5.62%	13.37%
12 Week Price Chg	-1.95%	-0.97%	6.05%	0.00%	-9.20%	12.86%
52 Week Price Chg	7.54%	-17.99%	22.39%	-21.09%	-30.33%	-31.79%
20 Day Average Volume	199,753	1,887,227	1,580,816	5,995,306	3,574,702	15,948,531
(F1) EPS Est 1 week change	-0.16%	-0.08%	0.00%	0.00%	-1.09%	2.42%
(F1) EPS Est 4 week change	-0.16%	-0.08%	0.00%	0.00%	-1.09%	2.42%
(F1) EPS Est 12 week change	18.93%	3.81%	-0.50%	14.52%	-8.49%	-6.90%
(Q1) EPS Est Mthly Chg	-0.25%	-0.47%	0.00%	-36.36%	-0.69%	4.36%

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.

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	F
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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