

## CarMax, Inc.(KMX)

**\$86.23** (As of 07/09/20)

Price Target (6-12 Months): **\$91.00**

Long Term: 6-12 Months

**Zacks Recommendation:**
**Neutral**

(Since: 06/02/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**3-Hold**

Zacks Style Scores:

VGM:A

Value: A

Growth: A

Momentum: B

## Summary

Store-expansion initiatives and high-quality product offerings are likely to boost CarMax's prospects. The company's omni-channel efforts to improve customer shopping experience are likely to bolster revenues. The firm's initiatives to enhance its online shopping capabilities in the wake of coronavirus-led lockdown bode well. Further, temporary cost cut initiatives undertaken by the firm may offer respite. However, the auto parts retailer is likely to bear the brunt of falling demand of vehicle purchases in the near-term as the pandemic has dented consumer sentiments. Coronavirus-led uncertainty has also prompted CarMax to call off its buyback program. Rising SG&A expenses on account of store expansion and digital enhancements and elevated debt are other headwinds for CarMax. As such, the stock warrants a cautious stance.

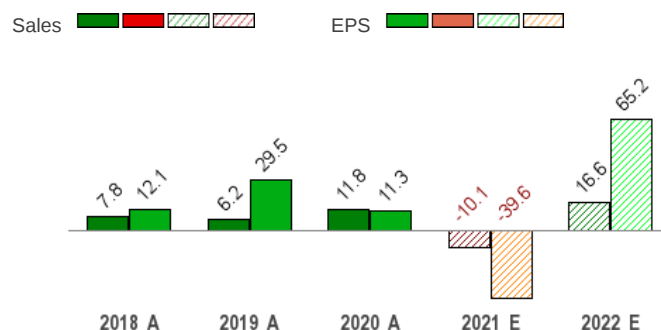
## Price, Consensus & Surprise



## Data Overview

|                            |                                                           |
|----------------------------|-----------------------------------------------------------|
| 52 Week High-Low           | <b>\$103.18 - \$37.59</b>                                 |
| 20 Day Average Volume (sh) | <b>1,708,268</b>                                          |
| Market Cap                 | <b>\$14.1 B</b>                                           |
| YTD Price Change           | <b>-1.6%</b>                                              |
| Beta                       | <b>1.71</b>                                               |
| Dividend / Div Yld         | <b>\$0.00 / 0.0%</b>                                      |
| Industry                   | <a href="#">Automotive - Retail and Wholesale - Parts</a> |
| Zacks Industry Rank        | <b>Top 25% (62 out of 252)</b>                            |

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



|                           |                   |
|---------------------------|-------------------|
| Last EPS Surprise         | <b>483.3%</b>     |
| Last Sales Surprise       | <b>23.9%</b>      |
| EPS F1 Est- 4 week change | <b>23.6%</b>      |
| Expected Report Date      | <b>09/22/2020</b> |
| Earnings ESP              | <b>0.0%</b>       |
| P/E TTM                   | <b>21.7</b>       |
| P/E F1                    | <b>26.8</b>       |
| PEG F1                    | <b>2.2</b>        |
| P/S TTM                   | <b>0.8</b>        |

## Sales Estimates (millions of \$)

|      | Q1      | Q2      | Q3      | Q4      | Annual*  |
|------|---------|---------|---------|---------|----------|
| 2022 | 5,114 E | 5,823 E | 5,308 E | 5,539 E | 21,299 E |
| 2021 | 3,229 A | 5,070 E | 4,867 E | 5,061 E | 18,272 E |
| 2020 | 5,366 A | 5,201 A | 4,790 A | 4,962 A | 20,320 A |

## EPS Estimates

|      | Q1       | Q2       | Q3       | Q4       | Annual*  |
|------|----------|----------|----------|----------|----------|
| 2022 | \$1.52 E | \$1.31 E | \$1.09 E | \$1.52 E | \$5.32 E |
| 2021 | \$0.23 A | \$0.99 E | \$0.95 E | \$1.20 E | \$3.22 E |
| 2020 | \$1.59 A | \$1.40 A | \$1.04 A | \$1.30 A | \$5.33 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 07/09/2020. The reports text is as of 07/10/2020.

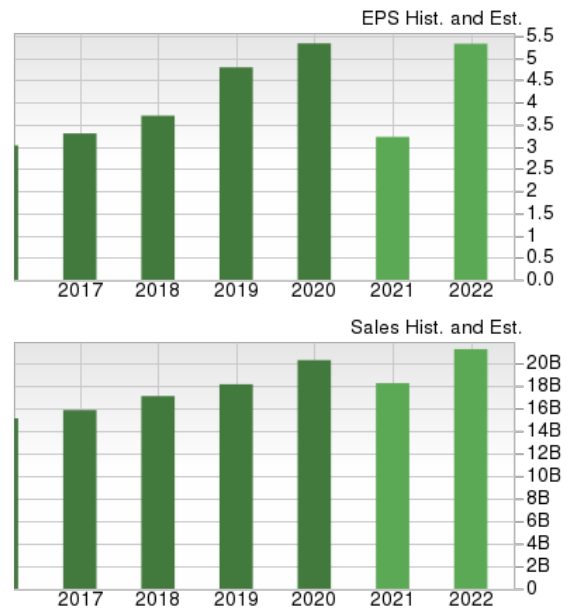
## Overview

Headquartered in Richmond, VA, CarMax Inc. operates as a specialty retailer of used and new vehicles. The range of vehicles includes both cars and light trucks. It is one of the largest retailers of used vehicles in the United States. CarMax also provides customers with a full range of related services including financing of vehicle purchases and sale of extended warranties, accessories and vehicle repair services through CarMax Auto Finance (CAF).

CarMax is a holding company, which conducts its operations through wholly owned subsidiaries. The company operates under two reportable segments: CarMax Sales Operations and CAF. Under the CarMax Sales Operations segment, the company undertakes all auto merchandising and service operations, excluding financing. The CAF segment provides vehicle financing through CarMax stores.

CarMax acquires its used-vehicle inventory directly from consumers through its in-store appraisal process as well as from other sources including local and regional auctions, wholesalers, franchised and independent dealers and fleet owners, such as leasing and rental companies. The company conducts the in-store appraisal process through its car-buying centers (about five) intended to increase appraisal traffic and generate incremental vehicle purchases by individual consumers, but not sale of vehicles. Out of the vehicles purchased through the in-store appraisal process, those which do not meet the company's retail standard are sold through on-site wholesale auctions.

The company has more than 200 stores worldwide. Most of its store locations are in the Southeastern United States. Chicago, Los Angeles, Houston, Dallas and Washington D.C. are some of the cities where the company enjoys a strong presence. In fiscal 2020, used vehicles contributed 84.5% while wholesale vehicles contributed 12.3% to total revenues. Other sales and revenues (such as new vehicle sales, commission on the sale of extended service plans (ESP), service department sales and third-party finance fees) contributed 3.2% to total revenues.



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## Reasons To Buy:

- ▲ The company's omni-channel efforts to improve customer shopping experience are likely to generate revenues. Notably, it recently initiated a curb-side pick-up option to bolster sales amid the coronavirus-led lockdown. The firm's initiatives to enhance its online shopping capabilities bode well for sales growth. Ship-to-home next day, buy online, pick-up in stores and commercial customer ordering are picking pace, driving traffic to the company's online site.
- ▲ Store-expansion initiatives, fast delivery and high-quality products are improving the company's market share. CarMax follows an aggressive store expansion initiative in existing as well as new markets. Unlike its peers, CarMax focuses more on the used-car market. Expensive new vehicles led to robust demand for cheaply available used vehicles. The firm will also continue to invest in modernizing its wholesale auction platforms, which will enable it to operate all auctions simultaneously online and in person. Further, its customer-friendly sales process, positions CarMax well.
- ▲ In response to the uncertainties caused by the coronavirus pandemic, CarMax has initiated a series of cost-saving initiatives throughout the enterprise, including substantial staffing adjustments, furloughs, compensation cuts, reducing inventory levels and slashing marketing spend. The focus on cost discipline is anticipated to provide some respite amid the financial crisis.

The company's omni-channel efforts and digital ramp up to improve customer shopping experience in the wake of virus outbreak bode well.

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## Reasons To Sell:

- ▼ Coronavirus has taken a toll on the auto sector, with factory closures, low footfall at dealerships and supply chain distortions. Auto parts retailer, CarMax, is likely to bear the brunt of falling demand of vehicle purchases as the pandemic has dented consumer sentiments. This is likely to put pressure on the firm's revenues and earnings in the coming quarters. Amid the coronavirus-led uncertainty, the company has also suspended stock buybacks, dampening investors' confidence.
- ▼ In fiscal 2020, CarMax's SG&A expenditure witnessed year-over-year rise of roughly 12% to \$1.9 billion. This increase was primarily due to expenses related to store openings. Increased investments to develop technology platforms and digital initiatives along with share-based compensation expenses are also increasing expenses for the company. Moreover, as the business improves after COVID-19, CarMax expects SG&A costs to rise further, as associates return from furlough, advertising expenses increase based on increasing demand and the firm continues to invest in strategic initiatives.
- ▼ Tariff woes in China remain a major headwind that may affect the top-line growth of CarMax. These are escalating the cost of raw materials and may eat into some of the profits of the firm. The firm's stretched balance sheet is also a major headwind. CarMax has a high long-term debt-to-capital ratio of 0.81, higher than the industry's ratio of 0.79. A high total debt-to-capital ratio often restricts the financial flexibility of the firm and limits its growth. Moreover, the company's times interest earned ratio of 10.13 is unfavorable to the industry ratio of 13.79.

CarMax is likely to bear the brunt of falling demand of vehicle purchases as the pandemic has dented consumer sentiments.

## Last Earnings Report

### CarMax Q1 Earnings & Sales Surpass Estimates

CarMax posted first-quarter fiscal 2021 (ended May 31, 2020) net earnings per share of 23 cents against the Zacks Consensus Estimate of a loss of 6 cents. The outperformance can be attributed to higher-than-expected revenues from used vehicles. Precisely, used-vehicle sales totaled \$2786.2 million, surpassing the consensus mark of \$1,281 million. A profit of \$1.59 per share was reported in the year-ago quarter.

Net sales in the reported quarter decreased 39.8% year over year to \$3,228.8 million. The top line, however, beat the Zacks Consensus Estimate of \$2,607 million. Total gross profit slid 52.3% year over year to \$354.2 million.

In first-quarter fiscal 2021, CarMax opened four stores in its existing markets, Tampa, Philadelphia, New Orleans and Los Angeles.

### Segmental Performance

During the quarter under review, CarMax's used-vehicle sales declined 38.6% from the prior-year period to \$2,786.2 million due to store closures and lower footfall amid coronavirus-induced lockdown. The units sold fell 39.8% year over year to 135,028 vehicles. The average selling price of used vehicles increased 1.5% from the year-ago quarter to \$20,346. Used-vehicle gross profit per unit came in at \$1,937 compared with \$2,215 in the year-ago period. Comparable store used-vehicle units and revenues dropped 41.8% and 40.8%, respectively, from the prior-year level.

Wholesale vehicle revenues plummeted 48.2% from the year-ago period to \$342.9 million in the reported quarter. Units sold also plunged 47.6% year over year to 63,295 vehicles due to lower traffic and a reduction in the appraisal buy rate. The average selling price of wholesale vehicles was down 2% from the prior-year quarter to \$5,110. Wholesale vehicle gross profit per unit came in at \$978 versus \$1,043 in the year-ago period.

Other sales and revenues decreased 38.9% year over year to \$99.7 million in the fiscal first quarter, primarily owing to a reduction in extended protection plan revenues, which declined 34.1% from the year-ago level to \$73.4 million.

CarMax Auto Finance reported a 56.1% year-over-year plunge in income to \$51 million in the quarter amid higher loan loss provision. Provision for loan losses increased to \$122 million from \$38.2 million in the prior year quarter.

### Costs, Financials and Share Buyback

Selling, general and administrative expenses fell 23.7% from the prior-year quarter to \$373.7 million. CarMax had cash and cash equivalents of \$658 million as of May 31, 2020 and \$1.08 billion of unused capacity on the credit revolver. Long-term debt amounted to \$1,705.1 million, reflecting a decrease from \$1,789.5 million in the year-ago period.

In the wake of coronavirus-induced uncertainty, CarMax tapped brakes in the stock buyback program. Prior to suspension of buybacks, the firm spent \$40.7 million to repurchase 515,500 shares during first-quarter fiscal 2021. As of May 31, 2020, it had \$1.51 billion remaining under the share-repurchase authorization.

Quarter Ending **05/2020**

| Report Date      | Jun 19, 2020 |
|------------------|--------------|
| Sales Surprise   | 23.87%       |
| EPS Surprise     | 483.33%      |
| Quarterly EPS    | 0.23         |
| Annual EPS (TTM) | 3.97         |

## Valuation

CarMax's shares are down 1.6% in the year-to-date period and 2.8% over the trailing 12-month period. Stocks in the Zacks Automotive - Retail and Wholesale – Parts industry and the Zacks Auto sector are down 6.2% and up 11.9% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 2.4% and up 25.3%, respectively.

The S&P 500 index is down 1.4% in the year-to-date period and up 6.2% in the past year.

The stock is currently trading at 21.66X forward 12-month earnings, which compares to 19.55X for the Zacks sub-industry, 22.62X for the Zacks sector and 22.52X for the S&P 500 index.

Over the past five years, the stock has traded as high as 31.61X and as low as 8.1X, with a 5-year median of 16.21X.

Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$91 price target reflects 22.86X forward 12-month earnings per share.

The table below shows summary valuation data for KMX:

| Valuation Multiples - KMX |               |       |              |        |         |
|---------------------------|---------------|-------|--------------|--------|---------|
|                           |               | Stock | Sub-Industry | Sector | S&P 500 |
| P/E F12M                  | Current       | 21.66 | 19.55        | 22.62  | 22.52   |
|                           | 5-Year High   | 31.61 | 21.41        | 26.62  | 22.52   |
|                           | 5-Year Low    | 8.1   | 12.62        | 8.19   | 15.27   |
|                           | 5-Year Median | 16.21 | 17.72        | 9.91   | 17.59   |
| EV/EBITDA TTM             | Current       | 24.05 | 22.84        | 12.22  | 12.1    |
|                           | 5-Year High   | 25.76 | 23.99        | 12.28  | 12.45   |
|                           | 5-Year Low    | 15.21 | 15.25        | 7.1    | 8.04    |
|                           | 5-Year Median | 17.97 | 20.35        | 9.35   | 10.76   |
| P/S F12M                  | Current       | 0.75  | 1.73         | 0.83   | 3.53    |
|                           | 5-Year High   | 0.93  | 1.96         | 0.83   | 3.53    |
|                           | 5-Year Low    | 0.34  | 1.15         | 0.49   | 2.52    |
|                           | 5-Year Median | 0.68  | 1.7          | 0.61   | 3.04    |

As of 07/09/2020

## Industry Analysis Zacks Industry Rank: Top 25% (62 out of 252)



## Top Peers

| Company (Ticker)                     | Rec          | Rank |
|--------------------------------------|--------------|------|
| Advance Auto Parts, Inc. (AAP)       | Neutral      | 3    |
| AutoZone, Inc. (AZO)                 | Neutral      | 3    |
| Dillards, Inc. (DDS)                 | Neutral      | 4    |
| J. C. Penney Company, Inc. (JCPNQ)   | Neutral      | 2    |
| Kohls Corporation (KSS)              | Neutral      | 3    |
| O'Reilly Automotive, Inc. (ORLY)     | Neutral      | 2    |
| U.S. Auto Parts Network, Inc. (PRTS) | Neutral      | 3    |
| Macys, Inc. (M)                      | Underperform | 5    |

| Industry Comparison Industry: Automotive - Retail And Wholesale - Parts |           |            |           | Industry Peers |         |         |
|-------------------------------------------------------------------------|-----------|------------|-----------|----------------|---------|---------|
|                                                                         | KMX       | X Industry | S&P 500   | AAP            | AZO     | ORLY    |
| Zacks Recommendation (Long Term)                                        | Neutral   | -          | -         | Neutral        | Neutral | Neutral |
| Zacks Rank (Short Term)                                                 | 3         | -          | -         | 3              | 3       | 2       |
| VGM Score                                                               | A         | -          | -         | B              | A       | B       |
| Market Cap                                                              | 14.06 B   | 14.06 B    | 21.19 B   | 9.24 B         | 25.87 B | 31.13 B |
| # of Analysts                                                           | 5         | 8          | 14        | 9              | 9       | 10      |
| Dividend Yield                                                          | 0.00%     | 0.00%      | 1.96%     | 0.75%          | 0.00%   | 0.00%   |
| Value Score                                                             | A         | -          | -         | B              | B       | B       |
| Cash/Price                                                              | 0.08      | 0.04       | 0.07      | 0.13           | 0.02    | 0.01    |
| EV/EBITDA                                                               | 19.03     | 12.82      | 12.56     | 12.23          | 12.82   | 16.77   |
| PEG Ratio                                                               | 2.23      | 1.91       | 2.85      | 1.95           | 1.87    | 1.83    |
| Price/Book (P/B)                                                        | 3.93      | 16.53      | 3.00      | 2.61           | NA      | 286.11  |
| Price/Cash Flow (P/CF)                                                  | 12.76     | 13.19      | 11.41     | 11.27          | 13.62   | 19.05   |
| P/E (F1)                                                                | 27.11     | 23.13      | 20.79     | 20.88          | 17.63   | 25.38   |
| Price/Sales (P/S)                                                       | 0.77      | 1.51       | 2.19      | 0.98           | 2.14    | 3.05    |
| Earnings Yield                                                          | 3.73%     | 3.94%      | 4.52%     | 4.79%          | 5.67%   | 3.94%   |
| Debt/Equity                                                             | 4.15      | 1.10       | 0.76      | 0.92           | -4.84   | 56.35   |
| Cash Flow (\$/share)                                                    | 6.76      | 11.86      | 6.94      | 11.86          | 81.35   | 22.02   |
| Growth Score                                                            | A         | -          | -         | F              | B       | C       |
| Hist. EPS Growth (3-5 yrs)                                              | 13.75%    | 14.06%     | 10.90%    | -1.61%         | 14.38%  | 18.82%  |
| Proj. EPS Growth (F1/F0)                                                | -39.55%   | -7.77%     | -9.99%    | -21.77%        | -0.93%  | -7.58%  |
| Curr. Cash Flow Growth                                                  | 7.77%     | 7.27%      | 5.51%     | 7.27%          | 15.07%  | 4.97%   |
| Hist. Cash Flow Growth (3-5 yrs)                                        | 9.70%     | 9.09%      | 8.55%     | -0.81%         | 8.49%   | 11.32%  |
| Current Ratio                                                           | 2.85      | 1.05       | 1.30      | 1.36           | 0.94    | 0.91    |
| Debt/Capital                                                            | 80.58%    | 66.53%     | 44.46%    | 47.79%         | NA      | 98.26%  |
| Net Margin                                                              | 3.45%     | 4.10%      | 10.62%    | 4.10%          | 12.90%  | 13.41%  |
| Return on Equity                                                        | 18.00%    | 13.20%     | 15.75%    | 13.20%         | -91.18% | 670.84% |
| Sales/Assets                                                            | 0.89      | 0.96       | 0.55      | 0.83           | 1.00    | 0.96    |
| Proj. Sales Growth (F1/F0)                                              | -10.08%   | -0.51%     | -2.52%    | -1.19%         | 0.88%   | -0.51%  |
| Momentum Score                                                          | B         | -          | -         | A              | C       | B       |
| Daily Price Chg                                                         | -2.78%    | -0.59%     | -1.52%    | -1.98%         | -0.91%  | -0.26%  |
| 1 Week Price Chg                                                        | 3.05%     | 2.98%      | 3.66%     | 1.32%          | 3.99%   | 2.98%   |
| 4 Week Price Chg                                                        | -1.21%    | 1.10%      | 0.36%     | 0.47%          | 1.10%   | 2.57%   |
| 12 Week Price Chg                                                       | 45.98%    | 14.07%     | 10.41%    | 13.80%         | 13.21%  | 14.07%  |
| 52 Week Price Chg                                                       | -2.86%    | -2.86%     | -8.70%    | -14.42%        | -3.58%  | 6.59%   |
| 20 Day Average Volume                                                   | 1,708,268 | 900,359    | 2,339,510 | 900,359        | 212,724 | 572,196 |
| (F1) EPS Est 1 week change                                              | 0.00%     | 0.00%      | 0.00%     | 0.00%          | 0.00%   | 0.00%   |
| (F1) EPS Est 4 week change                                              | 23.61%    | 1.00%      | 0.00%     | 1.75%          | -0.14%  | 1.00%   |
| (F1) EPS Est 12 week change                                             | -13.40%   | -3.08%     | -7.77%    | -10.83%        | 0.99%   | -3.08%  |
| (Q1) EPS Est Mthly Chg                                                  | 114.24%   | 1.10%      | 0.00%     | 1.98%          | 1.04%   | 1.10%   |

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## 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.

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### 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   | 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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