

Ross Stores, Inc. (ROST)

\$118.26 (As of 02/10/20)

Price Target (6-12 Months): **\$124.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 02/13/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM: C

Value: C

Growth: B

Momentum: F

Summary

Shares of Ross Stores have outperformed the industry in the past three months, driven by its strategic initiatives and a robust surprise trend. Moreover, the company delivered solid results in third-quarter fiscal 2019, wherein earnings and sales outpaced the Zacks Consensus Estimate and grew year over year. Results gained from favorable comps and higher operating margin. Notably, strength across categories has been aiding the company's comps in the past few quarters. Moreover, the company's commitment toward pricing, merchandise initiatives, cost containment and store expansion bodes well. However, higher cost of goods sold along with increased distribution expenses may dent Ross Stores' margins and profits. Its soft ladies apparel business further remains a concern and might hurt comps performance in the fiscal fourth quarter.

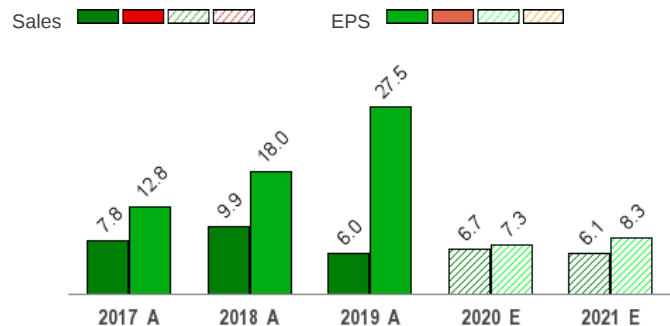
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$122.62 - \$88.31
20 Day Average Volume (sh)	1,763,977
Market Cap	\$42.4 B
YTD Price Change	1.6%
Beta	0.81
Dividend / Div Yld	\$1.02 / 0.9%
Industry	Retail - Discount Stores
Zacks Industry Rank	Bottom 36% (163 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	6.2%
Last Sales Surprise	1.8%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	03/03/2020
Earnings ESP	0.0%
P/E TTM	26.3
P/E F1	23.9
PEG F1	2.3
P/S TTM	2.7

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	4,052 E	4,228 E	4,077 E	4,646 E	16,977 E
2020	3,797 A	3,980 A	3,849 A	4,371 E	15,995 E
2019	3,589 A	3,738 A	3,550 A	4,107 A	14,984 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.24 E	\$1.26 E	\$1.11 E	\$1.35 E	\$4.95 E
2020	\$1.13 A	\$1.14 A	\$1.03 A	\$1.25 E	\$4.57 E
2019	\$1.11 A	\$1.04 A	\$0.91 A	\$1.20 A	\$4.26 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 02/10/2020. The reports text is as of 02/11/2020.

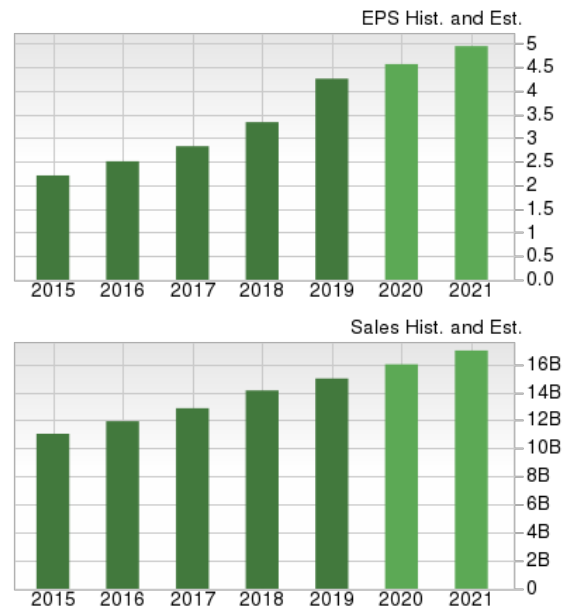
Overview

Based in Dublin, CA, Ross Stores Inc. operates as an off-price retailer of apparel and home accessories, primarily in the United States. The company operates its stores under the Ross Dress for Less (Ross) and dd's DISCOUNTS names. The company's stores are located mostly in community and neighborhood shopping centers in heavily populated urban and suburban areas.

Ross Stores primarily offers in-season, branded, and designer apparel, footwear, accessories and other home-related merchandise for everyone in the family. This format primarily targets middle-income households. Prices offered at Ross are generally 20% to 60% below the regular prices of most department and specialty stores.

dd's DISCOUNTS features more moderately-priced first-quality, in-season, name brand apparel, accessories, footwear, and home fashions for the entire family. These stores target moderate-income households. The dd's DISCOUNTS stores offer products at a 20% to 70% lesser price than the moderate department and discount stores.

As of Nov 2, 2019, Ross Stores operated 1,810 outlets, including 1,550 Ross Dress for Less stores and 260 dd's DISCOUNTS stores.



Reasons To Buy:

▲ **Robust Q3 & Upbeat View Aid Stock:** Shares of Ross Stores have rallied 6.5% in the past three months compared with the industry's 3.2% gain. This momentum can be attributed to its robust positive surprise trend, which continued in third-quarter fiscal 2019. Notably, the company's bottom line exceeded the Zacks Consensus Estimates for the seventh consecutive time, when it reported third-quarter fiscal 2019. Moreover, its sales delivered a beat in five of the last seven quarters. Additionally, earnings and sales improved year over year on favorable comparable store sales (comps) and higher operating margin. As a result, management raised earnings per share view to \$4.52-\$4.57 for fiscal 2019. The view signifies growth from the \$4.41-\$4.50 guided earlier and \$4.26 earned in fiscal 2018. For the fiscal fourth quarter, the company expects earnings per share of \$1.20-\$1.25 compared with \$1.20 reported in the year-ago period. Total sales is expected to increase 5-6% in the fiscal fourth quarter.

Ross Stores has been witnessing robust comps driven by strength across categories, except ladies apparel. Comps improved 5% in the fiscal third quarter on improved traffic and average basket size.

▲ **Solid Comps Trend:** Ross Stores has been witnessing a robust comps trend over the past few quarters mainly on improved performance across categories and geographic regions. Notably, comps improved 5% in third-quarter fiscal 2019, driven by higher traffic and increased average basket size. The higher basket size included benefits of increased units per transaction, offset by slightly lower average unit retail (AUR). Comps also outpaced the company's guidance of 1-2%. Notably, comps benefited from strength in the children's category, and in the Midwest region. For fourth-quarter fiscal 2019, the company anticipates 1-2% comps growth.

▲ **Off-Price Model to Drive Growth:** Ross operates a chain of off-price retail apparel and home accessories stores, which target value-conscious men and women, aged 25 to 54 in middle-to-upper middle class households. The decisions of the company, from merchandising, purchasing and pricing to the location of stores are made keeping in mind the customer base. The company has a proven business model as the competitive bargains it offers continue to make its stores attractive destinations for customers in all economic scenarios. Moreover, the off-price model offers strong value proposition and micro-merchandising that drive better product allocation and margins. Further, solid execution of the off-price strategy should boost top and bottom lines.

▲ **Store Expansion Plan:** Ross Stores has consistently been on track, with respect to store expansion plans. The company's store expansion efforts are focused on continually increasing penetration in the existing as well as new markets. Apparently, it successfully reached its target of opening 42 stores in the fiscal third quarter, which included 30 Ross and 12 dd's DISCOUNTS stores. Notably, this also marked the completion of its store opening target for fiscal 2019, with the addition of 98 outlets. Currently, the company operates nearly 1,810 Ross stores and dd's DISCOUNTS stores across 39 states, the District of Columbia and Guam. Over the long term, it expects to expand the Ross chain of stores to 2,400 locations alongside operating about 600 dd's DISCOUNTS stores.

▲ **Shareholder-Friendly Moves:** Ross Stores has a track record of returning value to shareholders from time to time in the form of dividends and share repurchases. In third-quarter fiscal 2019, the company bought back 3 million shares for nearly \$326 million. This brings the total share repurchases for the first nine months of fiscal 2019 to 9.6 million for \$966 million. With this, the company remains on track to repurchase shares worth \$1.275 billion in fiscal 2019. Additionally, it approved a quarterly cash dividend of 25.5 cents per share, payable Dec 31. These shareholder-friendly moves not only underscore Ross's solid financial status but also reflect management's commitment toward enhancing shareholder's return.

Reasons To Sell:

- ▼ **Stock Appears Overvalued:** Considering price-to-earnings (P/E) ratio, Ross Stores looks pretty overvalued compared with the market at large. The stock has a trailing 12-month P/E ratio of 26.3x, compared with 20.5x for the S&P 500. Its trailing 12-month P/E ratio is above the median level of 24.3x and below the high level of 27.1x.
- ▼ **Higher Costs Remain a Headwind:** Though Ross Stores reported strong top and bottom-line numbers in third-quarter fiscal 2019, higher costs continued to partly offset growth. Cost of goods sold (COGS) rose 8.6% to \$2,766.4 million. As a percentage of sales, COGS grew 10 basis points (bps) due to higher distribution expenses of 45 bps. This was partly offset by occupancy and buying costs leverage of 10 bps and 5 bps, respectively, and rise in merchandise margins of 20 bps. Meanwhile, freight costs remained flat. Selling, general and administrative expenses rose 7.7% to \$604.6 million. Going forward, headwinds related to higher expenses and tariffs might dent margins. It now expects operating margin of 13-13.2% for the fiscal fourth quarter compared with 13.2% recorded in the prior-year quarter.
- ▼ **Ladies Category Suffers:** Ross Stores has been witnessing soft performance at the ladies apparel category for the past few quarters. The softness in this category has been hurting the otherwise strong comps performance of the company. Although the company witnessed improving sales trend in ladies apparel business in third-quarter fiscal 2019, Ross Stores does not expect this business to aid performance in the fourth quarter. However, the company remains confident that the initiatives undertaken for this category will drive additional gains during the holiday selling season and into 2020. Nonetheless, a full turnaround of this business is unlikely in the near term.
- ▼ **Competitive Pressure:** Ross operates in a highly fragmented retail apparel market and faces intense competition from other well-established department stores, specialty stores, discount stores, warehouse stores, other off-price retailers, and manufacturer-owned outlet stores. Many of the company's competitors have larger number of stores, greater market presence, more brand recognition and financial resources that may make it difficult for the company to compete.

Higher cost of goods sold along with increased distribution expenses may dent Ross Stores' margins and profits going ahead. Its soft ladies apparel business remains an additional headwind.

Last Earnings Report

Ross Stores Beats on Q3 Earnings, Raises FY19 View

Ross Stores reported robust third-quarter fiscal 2019 results, wherein both the top line and the bottom line surpassed the Zacks Consensus Estimate. This marks the second straight quarter of positive surprise. Further, earnings and sales improved on a year-over-year basis. Also, the company's operating profit margin benefited from solid sales and growth in merchandise margins during the reported quarter. The company updated its fourth-quarter and fiscal 2019 guidance.

For fiscal 2019, the company expects earnings per share to be \$4.52-\$4.57. It reported \$4.26 earnings per share in fiscal 2018. Earlier, the company projected earnings per share of \$4.41-\$4.50 for fiscal 2019. The company continues to expect earnings per share of \$1.20-\$1.25 for the fiscal fourth quarter. It earned earnings per share of \$1.20 in the year-ago period.

Quarter Ending **10/2019**

Report Date	Nov 21, 2019
Sales Surprise	1.80%
EPS Surprise	6.19%
Quarterly EPS	1.03
Annual EPS (TTM)	4.50

Q3 Highlights

Ross Stores posted earnings of \$1.03 per share, which beat the Zacks Consensus Estimate of 97 cents and surpassed the company's guidance of 92-96 cents. Further, earnings grew 13.2% from 91 cents reported in the prior-year period. This was driven by higher revenues and share repurchase activities.

Total sales rose 8.4% to \$3,849.1 million and also surpassed the Zacks Consensus Estimate of \$3,774 million. Comparable-store sales (comps) improved 5% driven by higher traffic and increased average basket size. The higher basket size included benefits of increased units per transaction, offset by slightly lower average unit retail (AUR). Comps also outpaced the company's guidance of 1-2%.

Comps gained from strength in the children's category, and in the Midwest regions. Also, sales trend in ladies business continued to improve in the quarter. However, Ross Stores does not expect Ladies apparel business to aid performance in the fourth quarter. Nevertheless, the company remains confident that the initiatives undertaken for this category will drive additional gains during the holiday selling season and into 2020.

Cost of goods sold (COGS) rose 8.6% to \$2,766.4 million. As a percentage of sales, COGS grew 10 basis points (bps) due to higher distribution expenses of 45 bps, which was offset by occupancy and buying leverage of 10 bps and 5 bps, respectively, and rise in merchandise margins of 20 bps. Meanwhile, freight costs remained flat. Selling, general and administrative expenses rose 7.7% to \$604.6 million. As a percentage of sales, SG&A expenses decreased 10 bps.

Operating margin of 12.4% was better than expected, driven by higher sales and improved merchandise margin. The company had earlier guided operating margin in the range of 11.8-12% for the third quarter.

Store Update

The company successfully reached its target of opening 42 stores in the fiscal third quarter, which included 30 Ross and 12 dd's DISCOUNTS stores. As of Nov 2, 2019, Ross Stores operated 1,810 outlets, including 1,550 Ross Dress for Less stores and 260 dd's DISCOUNTS stores. Furthermore, with this third round of store opening, the company completed its target for fiscal 2019.

Financials

Ross Stores ended the fiscal third quarter with cash and cash equivalents of \$1,142.7 million, long-term debt of \$312.8 million, and total shareholders' equity of \$3,276.8 million.

In the reported quarter, the company repurchased 3 million shares for \$326 million. This brings the total share repurchases for the first nine months of fiscal 2019 to 9.6 million for \$966 million. With this, the company remains on track to repurchase shares worth \$1.275 billion in fiscal 2019.

Concurrent to the earnings release, Ross Stores also announced a quarterly dividend payout of 25.5 cents per share, payable Dec 31 to shareholders of record as of Dec 6.

Guidance

For the fourth quarter of fiscal 2019, the company anticipates comps growth of 1-2%. It expects total sales to increase 5-6%. Operating margin is projected at 13-13.2%. The same was 13.2% in the prior-year quarter. Moreover, the company estimates net interest income of \$2.3 million in the fiscal fourth quarter, with a tax rate of 22-23%.

Valuation

Ross Stores shares are up 1.6% in the year-to-date period and nearly 24.8% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Retail-Wholesale sector are up 0.3% and 3.5% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and the sector are up 35.3% and 17.8%, respectively.

The S&P 500 index is up 3.3% in the year-to-date period and 20.3% in the past year.

The stock is currently trading at 23.82X forward 12-month earnings, which compares to 23.76X 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 25.95X and as low as 16.18X, with a 5-year median of 20.63X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$124 price target reflects 24.98X forward 12-month earnings.

The table below shows summary valuation data for ROST

Valuation Multiples - ROST					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	23.82	23.76	25.41	19.12
	5-Year High	25.95	23.76	26.2	19.34
	5-Year Low	16.18	17.95	19.07	15.18
	5-Year Median	20.63	20.07	23	17.47
P/S F12M	Current	2.5	1.41	1.07	3.53
	5-Year High	2.66	1.41	1.1	3.53
	5-Year Low	1.46	0.95	0.8	2.54
	5-Year Median	1.92	1.13	0.92	3
EV/EBITDA TTM	Current	18.28	19.1	15.71	11.36
	5-Year High	18.77	19.7	15.71	12.85
	5-Year Low	9.55	11.11	10.79	8.47
	5-Year Median	12.49	13.82	12.39	10.7

As of 02/10/2020

Industry Analysis Zacks Industry Rank: Bottom 36% (163 out of 255)



Top Peers

Big Lots, Inc. (BIG)	Neutral
Burlington Stores, Inc. (BURL)	Neutral
Costco Wholesale Corporation (COST)	Neutral
Dollar General Corporation (DG)	Neutral
Dollar Tree, Inc. (DLTR)	Neutral
Target Corporation (TGT)	Neutral
The TJX Companies, Inc. (TJX)	Neutral
Walmart Inc. (WMT)	Neutral

Industry Comparison Industry: Retail - Discount Stores				Industry Peers		
	ROST Neutral	X Industry	S&P 500	DG Neutral	DLTR Neutral	TJX Neutral
VGM Score	C	-	-	B	B	C
Market Cap	42.44 B	17.89 B	24.00 B	39.61 B	20.63 B	74.18 B
# of Analysts	11	9	13	23	6	12
Dividend Yield	0.86%	0.83%	1.78%	0.82%	0.00%	1.49%
Value Score	C	-	-	C	B	C
Cash/Price	0.03	0.03	0.04	0.01	0.02	0.03
EV/EBITDA	18.65	17.54	14.07	19.38	11.50	16.43
PEG Ratio	2.30	1.93	2.04	1.78	1.82	2.04
Price/Book (P/B)	12.95	5.13	3.28	5.96	3.37	13.38
Price/Cash Flow (P/CF)	22.85	16.67	13.58	20.01	4.41	21.87
P/E (F1)	23.89	21.31	18.86	20.96	16.71	21.65
Price/Sales (P/S)	2.70	0.88	2.65	1.45	0.88	1.83
Earnings Yield	4.19%	4.62%	5.30%	4.77%	5.99%	4.62%
Debt/Equity	0.89	1.45	0.71	1.57	1.33	1.81
Cash Flow (\$/share)	5.18	6.08	6.89	7.77	19.78	2.82
Growth Score	B	-	-	A	A	B
Hist. EPS Growth (3-5 yrs)	17.25%	11.35%	10.80%	13.32%	18.83%	11.16%
Proj. EPS Growth (F1/F0)	8.32%	7.58%	7.23%	11.59%	10.40%	8.20%
Curr. Cash Flow Growth	20.22%	14.92%	9.51%	25.19%	163.96%	1.26%
Hist. Cash Flow Growth (3-5 yrs)	12.95%	7.44%	8.55%	8.34%	43.00%	5.93%
Current Ratio	1.26	1.15	1.20	1.12	1.09	1.22
Debt/Capital	47.07%	59.12%	42.90%	61.12%	57.13%	64.47%
Net Margin	10.47%	4.51%	11.76%	6.09%	-6.82%	7.70%
Return on Equity	49.88%	24.88%	16.98%	25.53%	20.85%	57.63%
Sales/Assets	1.87	1.84	0.54	1.38	1.30	1.94
Proj. Sales Growth (F1/F0)	6.14%	5.19%	4.15%	7.63%	4.37%	6.00%
Momentum Score	F	-	-	B	F	D
Daily Price Chg	0.71%	0.57%	-0.64%	0.40%	0.05%	0.44%
1 Week Price Chg	4.67%	1.96%	-2.60%	1.02%	0.08%	3.96%
4 Week Price Chg	-1.43%	-2.69%	0.72%	0.95%	-3.96%	-1.39%
12 Week Price Chg	5.41%	3.28%	4.69%	-2.74%	-20.06%	3.53%
52 Week Price Chg	25.64%	14.40%	16.01%	32.70%	-10.68%	25.56%
20 Day Average Volume	1,763,977	1,203,160	1,961,054	1,355,121	2,828,656	4,236,279
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	-0.26%	0.00%
(F1) EPS Est 4 week change	0.00%	-0.06%	-0.00%	-0.06%	-0.14%	0.00%
(F1) EPS Est 12 week change	0.37%	0.53%	-0.16%	0.73%	-11.83%	0.98%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.00%	1.23%	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	C
Growth Score	B
Momentum Score	F
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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