

Carter's Inc

Navigating through a competitive category

Reiterate Rating: UNDERPERFORM | PO: 65.00 USD | Price: 73.44 USD

4Q remains below cons on lower retail sales, gross margin

We remain cautious on an inflection in Carter's U.S. Retail segment (50% of sales) in 4Q and '24 given elevated competition in the children's apparel category. With the stock trading at 8x EV/EBITDA (12x P/E), we see better risk/reward elsewhere in our coverage given less visibility on positive sales trends in '24. Our 4Q EPS of \$2.39 is 8% below cons. due to a lower GM and higher SG&A. Our lower retail sales estimate is offset by higher wholesale. Our '24 EPS of \$6.20 is in line with cons. and includes stable sales and operating margins. We increase our PO to \$65 (prev \$60) based on 7x EV/EBITDA (prev 6.5x) due to the rerating in market multiples.

Wholesale business has puts and takes

We have a more positive outlook for the exclusive wholesale business (50% of total segment), which is business with TGT (Target), WMT (Walmart), and AMZN (Amazon), and a more cautious outlook for the rest of the business (dept stores, clubs, etc). We think CRI is a strong brand, but the product's commoditized nature and pressure from lower-priced alternatives could impact order books beyond 1H24. We are encouraged by expectations for higher order books in 1H24 but note 1H23 wholesale was -12%. We think greater visibility on this business rebounding beyond 1H24 would help sentiment.

Bull case: cotton tailwind, retail improvement

The bull case assumes the company can hold AUR (average unit retail, pricing up roughly 40% since pre-COVID) while benefitting from lower cotton costs (we think this could benefit to gross margin 100bp+). This, coupled with improvements in the U.S. Retail business following two straight years of double-digit comp declines (-10% in F22, -13% in F23E), would boost confidence in the brand's overall health and lead to higher ests. Incremental macroeconomic headwinds in Europe or Asia may provide relative advantages vs peers since roughly 95% of sales are in the US, Canada, and Mexico.

Bear case: pricing declines, discounts worsen

The bear case for the stock focuses on the risk of deeper pricing cuts (compared to the flat to modest cuts that have been communicated) and increased promotions that chip away at the 400bp+ increase in GM compared to '19. Furthermore, if comps don't stabilize in '24, we think there's risk to the multiple (and ests moving lower) given stronger recognition that the business is structurally losing share to private label.

Estimates (Dec) (US\$)	2021A	2022A	2023E	2024E	2025E
EPS	7.87	6.90	5.85	6.20	6.67
GAAP EPS	7.82	6.37	5.76	6.20	6.67
EPS Change (YoY)	89.6%	-12.3%	-15.2%	6.0%	7.6%
Consensus EPS (Bloomberg)			6.05	6.25	6.52
DPS	1.40	3.00	3.00	3.00	3.00
Valuation (Dec)					
P/E	9.3x	10.6x	12.6x	11.8x	11.0x
GAAP P/E	9.4x	11.5x	12.8x	11.8x	11.0x
Dividend Yield	1.9%	4.1%	4.1%	4.1%	4.1%
EV / EBITDA*	5.3x	6.9x	8.4x	8.3x	8.1x
Free Cash Flow Yield*	8.5%	1.8%	11.8%	7.6%	8.2%

* For full definitions of *IQmethod*SM measures, see page 5.

05 January 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	60.00	65.00
2023E Rev (m)	2,948.7	2,954.0
2024E Rev (m)	2,966.2	2,950.0
2025E Rev (m)	3,025.5	3,008.9
2023E EPS	5.84	5.85
2024E EPS	6.10	6.20
2025E EPS	6.60	6.67

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Stock Data

Price	73.44 USD
Price Objective	65.00 USD
Date Established	5-Jan-2024
Investment Opinion	B-3-7
52-Week Range	60.66 USD - 86.76 USD
Mrkt Val (mn) / Shares Out (mn)	2,704 USD / 36.8
Free Float	96.9%
Average Daily Value (mn)	47.52 USD
BofA Ticker / Exchange	CRI / NYS
Bloomberg / Reuters	CRI US / CRI.N
ROE (2023E)	27.2%
Net Dbt to Eqty (Dec-2022A)	50.5%
ESGMeter™	High

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to ["BofA ESGMeter Methodology"](#).

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Timestamp: 05 January 2024 12:01AM EST

iQprofileSM Carter's Inc

iQmethodSM – Bus Performance*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Return on Capital Employed	15.3%	13.9%	13.0%	13.3%	13.3%
Return on Equity	35.8%	30.6%	27.2%	27.1%	26.4%
Operating Margin	14.4%	12.1%	10.5%	10.4%	10.4%
Free Cash Flow	231	48	319	206	222

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash Realization Ratio	0.8x	0.3x	1.8x	1.4x	1.4x
Asset Replacement Ratio	0.4x	0.7x	1.1x	1.2x	1.1x
Tax Rate	22.5%	21.3%	23.0%	23.0%	23.0%
Net Debt-to-Equity Ratio	0.7%	50.5%	47.9%	44.7%	38.8%
Interest Cover	8.5x	9.3x	10.0x	11.0x	11.2x

Income Statement Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Sales	3,486	3,213	2,954	2,950	3,009
% Change	15.3%	-7.9%	-8.1%	-0.1%	2.0%
Gross Profit	1,662	1,472	1,394	1,414	1,445
% Change	26.6%	-11.4%	-5.3%	1.4%	2.2%
EBITDA	595	452	374	375	388
% Change	59.0%	-24.0%	-17.3%	0.3%	3.3%
Net Interest & Other Income	(59)	(42)	(31)	(28)	(26)
Net Income (Adjusted)	338	268	213	211	217
% Change	87.7%	-20.8%	-20.7%	-0.6%	2.9%

Free Cash Flow Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Net Income from Cont Operations (GAAP)	335	246	207	210	217
Depreciation & Amortization	90	62	61	65	70
Change in Working Capital	0	0	0	0	0
Deferred Taxation Charge	(14)	(1)	(4)	0	1
Other Adjustments, Net	(144)	(218)	119	11	15
Capital Expenditure	(37)	(40)	(65)	(80)	(80)
Free Cash Flow	231	48	319	206	222
% Change	-58.6%	-79.2%	563.8%	-35.3%	7.7%
Share / Issue Repurchase	(288)	(296)	(163)	(96)	(96)
Cost of Dividends Paid	(60)	(118)	(111)	(102)	(98)
Change in Debt	0	(396)	(120)	1	1

Balance Sheet Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash & Equivalents	984	212	132	141	170
Trade Receivables	231	199	202	202	206
Other Current Assets	698	778	627	639	651
Property, Plant & Equipment	216	190	188	203	213
Other Non-Current Assets	1,072	1,061	1,070	1,070	1,071
Total Assets	3,202	2,440	2,219	2,254	2,311
Short-Term Debt	0	0	0	0	0
Other Current Liabilities	731	529	472	469	477
Long-Term Debt	991	617	497	498	499
Other Non-Current Liabilities	87	76	70	70	71
Total Liabilities	2,252	1,643	1,467	1,465	1,474
Total Equity	950	801	762	799	847
Total Equity & Liabilities	3,202	2,445	2,229	2,264	2,321

* For full definitions of iQmethodSM measures, see page 5.

Company Sector

Apparel

Company Description

Carter's Inc is the largest branded marketer in the US of apparel exclusively for babies and young children. They own the Carter's and OshKosh brands and distribute their products through department stores, chain and specialty stores, discount retails and operate their own branded strip center and outlet retail stores.

Investment Rationale

We think the risk/reward is skewed to the downside as we see risk to margins from a more normalized promotional environment, think the success of price increases is dependent on peer behavior, and see continued competition from private label.

Stock Data

Average Daily Volume

647,029

Quarterly Earnings Estimates

	2022	2023
Q1	1.66A	0.98A
Q2	1.30A	0.64A
Q3	1.67A	1.84A
Q4	2.29A	2.39E

**Exhibit 1: CRI Income Statement**

We forecast F24E EPS of \$6.20, in line with Visible Alpha consensus

Carter's	FY 2022	1Q 23	2Q 23	3Q 23	4Q 23E	FY 2023E	1Q 24E	2Q 24E	3Q 24E	4Q 24E	FY 2024E	1Q 25E	2Q 25E	3Q 25E	4Q 25E	FY 2025E
Income Statement (\$ mn)		Mar	Jun	Sept	Dec		Mar	Jun	Sept	Dec		Mar	Jun	Sept	Dec	
U.S Wholesale	1,080.5	280.0	186.9	300.3	255.5	1,022.7	285.6	196.2	303.3	258.0	1,043.2	291.3	200.1	309.4	263.2	1,064.0
U.S Retail	1,680.2	323.7	323.5	374.8	473.3	1,495.3	304.3	314.1	375.1	468.6	1,462.1	310.4	320.3	382.6	477.9	1,491.2
International	452.1	92.2	89.9	116.5	137.4	436.0	94.0	91.7	118.8	140.2	444.7	95.9	93.5	121.2	143.0	453.6
Total Net Sales	3,212.7	695.9	600.2	791.7	866.2	2,954.0	683.9	601.9	797.3	866.9	2,950.0	697.6	614.0	813.2	884.1	3,008.9
Cost of Goods Sold	1,740.4	386.4	308.3	415.3	449.9	1,559.9	372.9	303.2	414.2	445.9	1,536.3	379.7	308.6	421.7	453.9	1,563.9
Gross Profit	1,472.4	309.5	291.9	376.4	416.3	1,394.1	311.0	298.8	383.1	420.9	1,413.7	317.9	305.4	391.5	430.2	1,445.0
SG&A Expenses	1,110.0	258.4	258.3	285.8	303.9	1,106.4	257.5	261.3	299.7	308.5	1,127.0	262.6	266.7	305.9	315.0	1,150.2
Royalty Income	25.8	6.5	4.3	5.7	4.9	21.5	5.9	3.9	5.1	4.4	19.3	5.3	3.5	4.6	4.0	17.4
Operating Income	388.2	57.6	38.0	96.3	117.3	309.2	59.4	41.3	88.5	116.9	306.1	60.6	42.2	90.2	119.2	312.2
Net Interest Expense/(Income)	41.5	8.9	7.1	7.6	7.5	31.0	6.9	6.9	7.0	7.0	27.7	6.9	6.9	6.9	7.0	27.8
Other (Income)/Expense	1.0	(0.3)	(0.8)	0.5	0.5	(0.0)	(0.3)	(0.8)	0.5	0.5	(0.0)	(0.5)	(0.5)	(0.5)	(0.5)	(2.0)
Pretax Income	345.7	48.9	31.6	88.3	109.4	278.2	52.8	35.2	81.0	109.4	278.4	54.1	35.8	83.8	112.8	286.4
Taxes	73.6	12.0	7.5	19.9	24.7	64.1	12.1	8.1	18.6	25.2	64.0	12.4	8.2	19.3	25.9	65.9
Tax Rate	21.3%	24.5%	23.6%	22.6%	22.6%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%
Net Income	268.0	36.3	23.7	67.0	83.7	210.7	39.6	26.1	61.4	83.2	210.3	40.7	26.6	63.5	85.8	216.6
Earnings Per Share	\$6.90	\$0.98	\$0.64	\$1.84	\$2.39	\$5.85	\$1.14	\$0.76	\$1.81	\$2.48	\$6.20	\$1.23	\$0.81	\$1.96	\$2.68	\$6.67
Diluted Shares Outstanding	38.9	37.1	36.8	36.4	35.0	36.4	34.7	34.3	33.9	33.5	34.1	33.2	32.8	32.4	32.0	32.6
Dividend Per Share	\$3.00	\$0.75	\$0.75	\$0.75	\$0.75	\$3.00	\$0.75	\$0.75	\$0.75	\$0.75	\$3.00	\$0.75	\$0.75	\$0.75	\$0.75	\$3.00
Y/Y Growth																
Total Sales	-7.9%	-10.9%	-14.3%	-3.3%	-5.0%	-8.1%	-1.7%	0.3%	0.7%	0.1%	-0.1%	2.0%	2.0%	2.0%	2.0%	2.0%
Operating income	-22.5%	-43.9%	-49.7%	5.2%	-1.0%	-20.4%	3.2%	8.9%	-8.2%	-0.4%	-1.0%	2.0%	2.0%	2.0%	2.0%	2.0%
EPS	-12.3%	-41.1%	-50.6%	10.0%	4.4%	-15.2%	16.9%	18.2%	-1.6%	3.9%	5.9%	7.3%	6.3%	8.3%	7.9%	7.7%
Royalty Income	-10.0%	-12.8%	-22.5%	-21.4%	-10.0%	-16.7%	-10.0%	-10.0%	-10.0%	-10.0%	-10.0%	-10.0%	-10.0%	-10.0%	-10.0%	-10.0%
Dividends	5.0%					5.0%					5.0%					5.0%
Margins																
Gross Margin	45.8%	44.5%	48.6%	47.5%	48.1%	47.2%	45.5%	49.6%	48.0%	48.6%	47.9%	45.6%	49.7%	48.1%	48.7%	48.0%
bp change y/y	(185)	(97)	136	228	250	136	100	100	50	50	73	10	10	10	10	10
GM vs. 2019	302	213	629	491	558	439										
SG&A Expense Rate	34.6%	37.1%	43.0%	36.1%	35.1%	37.5%	37.6%	43.4%	37.6%	35.6%	38.2%	37.6%	43.4%	37.6%	35.6%	38.2%
bp change y/y	41	387	572	114	192	290	51	38	150	50	75	(0)	2	2	4	2
SG&A dollar growth	-6.7%	-0.6%	-1.2%	-0.2%	0.5%	-0.3%	-0.4%	1.2%	4.9%	1.5%	1.9%	2.0%	2.1%	2.1%	2.1%	2.1%
SG&A vs. 2019																
Royalty Income % of Sales	0.8%	0.9%	0.7%	0.7%	0.6%	0.7%	0.9%	0.6%	0.6%	0.5%	0.7%	0.8%	0.6%	0.6%	0.5%	0.6%
bp change y/y	(2)	(2)	(8)	(17)	(3)	(8)	(8)	(7)	(8)	(6)	(7)	(10)	(8)	(8)	(6)	(8)
Operating Margin	12.1%	8.3%	6.3%	12.2%	13.5%	10.5%	8.7%	6.9%	11.1%	13.5%	10.4%	8.7%	6.9%	11.1%	13.5%	10.4%
bp change y/y	(218)	(486)	(444)	98	55	(167)	41	54	(107)	(6)	(4)	(0)	0	0	0	(0)

Source: BofA Global Research estimates, company reports

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Price objective basis & risk

Carter's Inc (CRI)

Our \$65 price objective is based on a 7x EV/EBITDA ('24E) multiple, lower than its historical average given the ongoing macro uncertainty and downside EPS risks.

Upside risks to our price objective are better-than-expected children's apparel sales, successful market share gains through the company's Age Up strategy, and a more defensive business model during a potential recession.

Downside risks to our price objective are emphasis by wholesale partners on private label, exposure to weakening outlet centers, and a heightened competitive pricing environment.

Analyst Certification

I, Christopher Nardone, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Softline Retailing and Dept Stores Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Bath & Body Works Inc	BBWI	BBWI US	Lorraine Hutchinson, CFA
	Burlington Stores	BURL	BURL US	Lorraine Hutchinson, CFA
	Crocs, Inc.	CROX	CROX US	Christopher Nardone
	Deckers Outdoor Corp	DECK	DECK US	Christopher Nardone
	European Wax Center	EW CZ	EW CZ US	Lorraine Hutchinson, CFA
	lululemon athletica Inc	LULU	LULU US	Lorraine Hutchinson, CFA
	Oddity Tech	ODD	ODD US	Lorraine Hutchinson, CFA
	PVH Corp	PVH	PVH US	Christopher Nardone
	Ralph Lauren	RL	RL US	Christopher Nardone
	Ross Stores Inc	ROST	ROST US	Lorraine Hutchinson, CFA
	Tapestry Inc.	TPR	TPR US	Lorraine Hutchinson, CFA
	TJX Companies	TJX	TJX US	Lorraine Hutchinson, CFA
	Urban Outfitters	URBN	URBN US	Lorraine Hutchinson, CFA
	Victoria's Secret & Co	VSCO	VSCO US	Alice Xiao
NEUTRAL				
	American Eagle	AEO	AEO US	Christopher Nardone
	Birkenstock	BIRK	BIRK US	Lorraine Hutchinson, CFA
	FIGS, Inc.	FIGS	FIGS US	Alice Xiao
	Foot Locker	FL	FL US	Lorraine Hutchinson, CFA
	Levi Strauss & Co.	LEVI	LEVI US	Christopher Nardone
	Nike	NKE	NKE US	Lorraine Hutchinson, CFA
	Signet Jewelers	SIG	SIG US	Lorraine Hutchinson, CFA
	Ulta Beauty	ULTA	ULTA US	Lorraine Hutchinson, CFA
	Under Armour Inc	UAA	UAA US	Lorraine Hutchinson, CFA
UNDERPERFORM				
	Aritzia	YATZ	ATZ CN	Alice Xiao
	Aritzia	ATZAF	ATZAF US	Alice Xiao
	Carter's Inc	CRI	CRI US	Christopher Nardone
	Gap Inc.	GPS	GPS US	Lorraine Hutchinson, CFA

US - Softline Retailing and Dept Stores Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Kohl's	KSS	KSS US	Lorraine Hutchinson, CFA
	Nordstrom	JWN	JWN US	Lorraine Hutchinson, CFA
	Revolve	RVLV	RVLV US	Alice Xiao
	V F Corp	VFC	VFC US	Lorraine Hutchinson, CFA

IQmethodSM Measures Definitions**Business Performance**

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

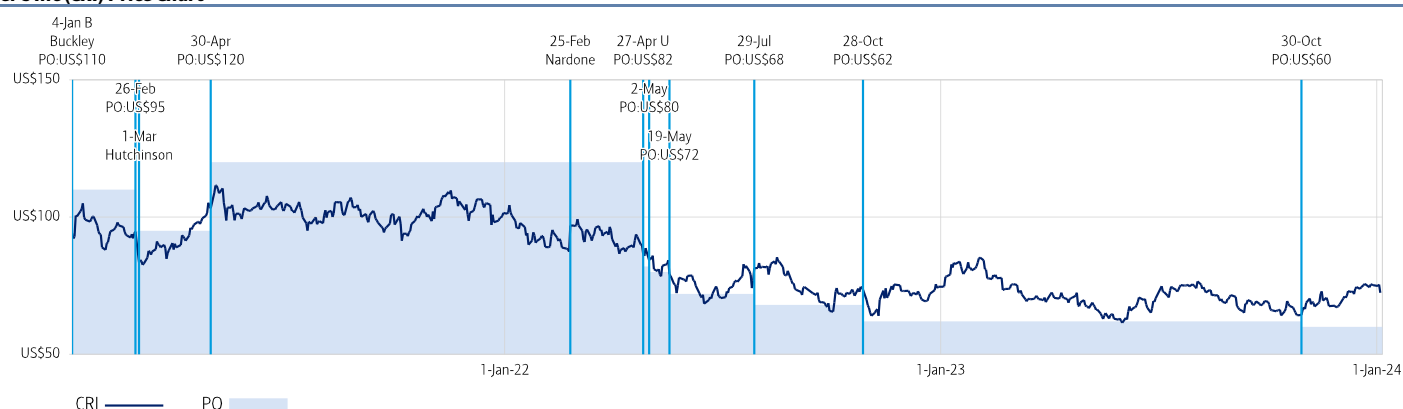
Sales

Basic EBIT + Depreciation + Amortization

IQmethodSM is the set of BofA Global Research standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and valuations. The key features of IQmethod are: A consistently structured, detailed, and transparent methodology. Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

IQdatabase[®] is our real-time global research database that is sourced directly from our equity analysts' earnings models and includes forecasted as well as historical data for income statements, balance sheets, and cash flow statements for companies covered by BofA Global Research.

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Disclosures**Important Disclosures****Carter's Inc (CRI) Price Chart**

B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Textiles/Apparel Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	13	52.00%	Buy	8	61.54%
Hold	6	24.00%	Hold	3	50.00%
Sell	6	24.00%	Sell	2	33.33%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

FUNDAMENTAL EQUITY OPINION KEY: Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. VOLATILITY RISK RATINGS, indicators of potential price fluctuation, are: A - Low, B - Medium and C - High. INVESTMENT RATINGS reflect the analyst's assessment of both a stock's absolute total return potential as well as its attractiveness for investment relative to other stocks within its Coverage Cluster (defined below). Our investment ratings are: 1 - Buy stocks are expected to have a total return of at least 10% and are the most attractive stocks in the coverage cluster; 2 - Neutral stocks are expected to remain flat or increase in value and are less attractive than Buy rated stocks and 3 - Underperform stocks are the least attractive stocks in a coverage cluster. An investment rating of 6 (No Rating) indicates that a stock is no longer trading on the basis of fundamentals. Analysts assign investment ratings considering, among other things, the 0-12 month total return expectation for a stock and the firm's guidelines for ratings dispersions (shown in the table below). The current price objective for a stock should be referenced to better understand the total return expectation at any given time. The price objective reflects the analyst's view of the potential price appreciation (depreciation).

Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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