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**MBA 520**

**Financial Analysis Case 4**

# Investment Decision

When evaluating these companies, it is clear to me that the better investment between them is with Target. The financial performance of Target, specifically return on assets and equity and inventory turnover coupled with their distribution channels suggests not just stability, but a strong return on investment. Target's growth pre-pandemic gives me a lot of confidence as they have had consistent growth that has been accelerated during the pandemic despite supply chain issues. Their expansive in-house brands offers quality alternatives to name brands at affordable prices that gives consumers options while dealing with inflationary conditions. As the supply chain returns to form, I see Target learning lessons on improving their e-commerce market to adapt to consumer needs which lends itself to opportunities like expanding operations abroad. Target providing dividends is not only another sign of stability within the company, it is a smart option to allow you to passively earn income on your investment.

# Ratio Comparison Table

|  |  |  |  |
| --- | --- | --- | --- |
| **Date of Ratio: 1/30/2021** | **Target** | **Dollar Tree** | **Department Stores** |
| **Return on Assets** | 9.29% | 6.66% |  |
| **Return on Equity** | 33.25% | 19.82% |  |
| **Inventory Turnover** | 6.74 | 5.10 |  |
| **Current Ratio** | 1.03 | 1.35 |  |
| **Net Profit Margin** | 4.67% | 5.26% |  |

# Ratio Explanation

The return on assets and return on equity ratios are profitability ratios that gives insight into how much profit a company is able to generate from their assets and from shareholders equity. For ROA, a ratio above 5% is considered good. For ROE, a ratio between 15-20% is considered good. Inventory turnover is a ratio that indicates the rate in which a company sells through their stock of goods. A ratio between 5-10 is considered good. Current ratio measures the liquidity of a company and their ability to meet their short-term obligations. A ratio between 1.5-3 is considered good. Net profit margin measures a company's profitability as a percentage of revenue. 10% is considered average and 20% is considered good.

I find these ratios to be important because they are able to highlight how is the company generating a profit, how are they working through inventories, how are they able to navigate difficult situations and meeting obligations how well are they generating a profit.

As I compare these two, I put significant focus on ROA, ROE and inventory turnover ratios. I do so because the ability to generate significant returns and working through inventories to me shows a level of stability. Target has a significant advantage with these ratios. They are able to move inventories more effectively and generate a better return for investors. I do have some concern on the current ratios for both, particularly with Dollar Tree as they navigate through consolidation and restructuring their Dollar Tree and Family Dollar brands. Despite my concern, I see it more as ratios of note rather than influencing my decision.

# Ratio Trend Table

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Target Ratios** | **1/30/2021** | **2/1/2020** | **2/2/2019** | **2/3/2018** | **1/28/2017** |
| **Return on Assets** | 9.29% | 7.81% | 7.20% | 7.50% | 7.04% |
| **Return on Equity** | 33.25% | 28.37% | 25.60% | 25.78% | 22.87% |
| **Inventory Turnover** | 6.74 | 5.93 | 5.89 | 6.05 | 5.81 |
| **Current Ratio** | 1.03 | 0.89 | 0.83 | 0.96 | 0.94 |
| **Net Profit Margin** | 4.67% | 4.20% | 3.90% | 4.01% | 3.89% |

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Dollar Tree Ratios** | **1/30/2021** | **2/1/2020** | **2/2/2019** | **2/3/2018** | **1/28/2017** |
| **Return on Assets** | 6.66% | 5.00% | -10.66% | 10.70% | 5.67% |
| **Return on Equity** | 19.82% | 13.90% | -24.81% | 27.27% | 18.30% |
| **Inventory Turnover** | 5.10 | 4.70 | 4.74 | 5.05 | 4.98 |
| **Current Ratio** | 1.35 | 1.20 | 2.05 | 1.60 | 1.87 |
| **Net Profit Margin** | 5.26% | 3.50% | -6.97% | 7.71% | 4.33% |

**Ratio Trend Analysis Explanation**

Target has shown a number of promising signs when reflecting on these ratio trends. There has been consistent growth in terms of ROA and ROE while inventory turnover has been relatively steady prior to 2021 numbers. What stands out to me with Target is the considerable jump in each metric for 2021 and I believe the pandemic played an impact in that. Their distribution channels enabled this growth as demand for goods, particularly through digital mediums.

Dollar Tree and their figures needs a different consideration when evaluating. Their dip in 2019 in terms of ROA, ROE and profit margin I would attribute to their consolidation efforts and their growth in consecutive years reflects that these decisions have been worth the risk so far. Their numbers in 2018 were rather strong and I would infer that in the next year's reporting, numbers should be closer to 2018. Despite being in the same industry as Target, they have not had the same pandemic successes due to limited channels, but as the economy began to reopen around the country, I believe this will have a positive impact on their figures.

# Stock Price Trend Table

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Target** | **2021** | **2020** | **2019** | **2018** | **2017** |
| **Year End Stock Price** | $259.62 | $176.53 | $128.21 | $66.09 | $65.25 |

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Dollar Tree** | **2021** | **2020** | **2019** | **2018** | **2017** |
| **Year End Stock Price** | $107.76 | $108.04 | $94.05 | $90.32 | $107.31 |

**Stock Price Trend Analysis Explanation**

I don’t find Dollar Tree's dip between 2018 and 2019 concerning as their restructuring likely played a role in the price fluctuations. What I find optimism in is that in the following years, stock prices have returned to pre-restructure levels and have remained consistent despite the uncertainty in the markets from the pandemic.

Target has shown to be a worthwhile investment in terms of stock gains. Each year there has been an increase in price with a 94% increase from 2018 to 2019 and significant growth each year following. The fact that valuation increases were not impacted by or reliant on market volatility or increased demand by the pandemic should bring confidence to current and potential investors.

# SWOT Analysis

Both Target and Dollar Tree had their financial performance acknowledged as a strength as well as multiple selling channels. It’s the point about Target's inventory turnover ratio that further supports my recommendation and I think also supports the opportunities in launching new products and putting emphasis on e-commerce. I find that the e-commerce opportunity for Dollar Tree is not only valid, but the next step for the company, but Target's current presence provides more stability in investment.

As it is a strength for Target, it's appropriate for inventory turnover to be a weakness for Dollar Tree, but I can see this improving as they expand their network. For Target, international presence does lack as they primarily operate in the US and this limits their ability to generate revenue, especially compared to competitors in the space. The threats of supply chain issues and risk with suppliers is not unique to each of these companies, but are two of the biggest concerns. As companies across all industries struggle with supply chain issues, I believe Target is in a better position to adapt as needed.

# Financial Journal Review

Target's multi-channel sales has been a strong point of theirs each year with significant increases during the pandemic years. As highlighted in the Motley Fool, comparable sales were up 12.7% in the third quarter earnings released this week with high traffic and consumer demand as well as gains in use of same-day digital fulfillment services. Target's adaptability and financial strength has provided them the opportunity to reroute goods to less congested ports and charter their own shipping vessels (Kare 11, 2021). Target's private brands gives them additional options in capturing market share and now has competitors attempting to copy their success. Of their 48 private brands, 10 are worth a billion dollars according to a Target spokesperson (Monteros, 2021).

Dollar Tree, as well as other discount stores, are seeing a drive in sales Jill Shah writes for Bloomberg. Discount stores saw a 65% increasing in spending compared to 2019 as consumers find ways to manage their budgets due to current inflation concerns. As activist investor Mantle Ridge stakes $1.8 billion into the company, he looks to capitalize on Dollar Tree's potential, particularly with Family Dollar, to try and expand the company's reach and adjust pricing to improve margins (Lee, 2021). These growth opportunities are not being wasted with Dollar Tree as earlier this month they announce a partnership with grocery delivery service Instacart to provide 1-hour delivery service from it’s nearly 13,000 stores within the US (Mulloy, 2021). As this partnership develops, Dollar Tree is able to better serve customers as their shopping habits change and generate additional traffic and revenue.

# Conclusion

After assessing the data, Dollar Tree is a stock that would be worth putting on a watchlist rather than in your portfolio at this point, especially considering current supply chain issues and demand. Diversity is the optimal way to mitigate risks. The growth of Target, particularly when assessed against competitors in the retail space such as Walmart and Amazon, is a worthwhile investment. While I do not suggest they will take market share away from them, they have the ability and infrastructure to remain a major player in the space while generating consistent return on investment through increased stock valuation and dividend yield. With the current infrastructure in place, Target is better equipped to adapt to the changes in the industry and consumer shopping trends.

# Reflection on the Financial Analysis Case

In the reflection section, reflect on what you have learned in this financial analysis case and how you will be able to apply these skills to your personal and work life.

My thoughts on the financial analysis cases changed throughout the term. At the beginning, I saw it as just a major assignment I had to do in order to pass the class. I was relatively indifferent towards these as my undergrad was in marketing and management and my current concentration is business analytics. After not scoring well on the first one, according to my standards, I began to reshape my thinking. I may not be in or working towards the accounting and finance functions of business, being able to read reports and analyze them is still incredibly important for my education and future career development.

I was able to further my knowledge of financial statements and better understand the decisions made within these companies. I spent time looking at other companies as well to look at how they’ve navigated through the pandemic and the challenges it has brought. I have passion for economics and have been able to find the connection between these two and it has helped me better understand economic conditions and how businesses and corporations play a part in that. As I consider my career prospects and the possibility of starting my own business, having a better working knowledge of financial analysis can help me in my own decision making.

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