Target Corporation (NYSE:TGT) Financial Community Meeting Call March 3, 2015 2:30 PM ET

Executives

Brian Cornell - Chairman of the Board and Chief Executive Officer

John Mulligan - Executive Vice President and Chief Financial Officer

Casey Carl - Chief Strategy and Innovation Officer

Kathryn Tesija - Executive Vice President and Chief Merchandising and Supply Chain Officer

Jeffrey Jones - Executive Vice President and Chief Marketing Officer

Analysts

Dan Binder - Jefferies

David Strasser - Janney Capital Markets

Bob Drbul - Nomura Securities

Matt McClintock - Barclays Capital

Greg Melich - Evercore ISI

Craig Johnson - Customer Growth Partners

Joe Feldman - Telsey Advisory Group

Stacie Rabinowitz - Consumer Edge Research

Michael Lasser - UBS

Unidentified Company Representative

Good afternoon, everybody. Thank you for coming. We are really excited to have all of you here today, both here in the room and online.

Before Brian comes up, I have a few housekeeping items. First off, we have a lot to cover today, so we are not going to take a break. Refreshments will be out in the lobby the whole time. The restrooms are right back here. Please watch your step on the way up and down, if you're down on the main level.

And then we have the two standard disclosures, which I'll read verbatim for our legal team. Any forward-looking statements that we make this afternoon are subject to risks and uncertainties, the most important of which are described in our SEC filings. And our earnings press release and SEC filings available on target.com/investors provide reconciliation of adjusted EPS to our GAAP results.

Now with that, we can get started. Thank you.

[video presentation]

Brian Cornell

Good afternoon. We started sharing that video with our team last year, after some of the most challenging events in Target's history. And despite those challenges, our brand remain strong; our guests loyal; and our team, passionate and committed. Since then, our business has shown some early signs of momentum, most recently in our fourth quarter sales; our traffic; our profit performance, both in-store and online.

Today we're in the very early stages of a real shift in our business. And we'll spend this afternoon discussing how we will build on our momentum, as we go deeper into the transformation to create the Target of tomorrow.

Going forward, we will be a brand that separates itself from others based on merchandising authority and experience, centered on ease and on inspiration. We'll enable mobile to be the front door to all of Target. Importantly, we'll reassert our cultural leadership to build unparalleled guest affinity, and we will be a more agile, a more efficient and a more guest-focused headquarter team.

We know that to compete today, speed and simplicity are critically important. And we're looking at every opportunity to eliminate complexity, facilitate efficiency and accountability, to get our guests what they want and get it out to the market as quickly as possible.

We're also being very disciplined in prioritizing our work to accelerate progress in areas that are most important to our guest and to our business. I am absolutely convinced that this new clarity and commitment to reduce complexity will unleash and accelerate innovation throughout Target, and it's something that Casey will discuss later this afternoon.

As a leadership team, we've taken a hard look at our business, and asked ourselves some of the tough questions you've been asking about our path forward. It began with the most comprehensive strategic review that has ever been conducted at Target.

When we conducted this review, we maintained an outside-in perspective, beginning with consumers and shoppers first, before we focused on our Target guests and on our Target brand. As a result of that work, we have a very clear view of today's shopper and our Target guests.

Today's guests are increasingly families. A growing percentage of them are Hispanic. They are digitally connected. They love to shop and they demand great value. We refer to this guest as our demanding enthusiast. And throughout today's remarks we'll show you how we've designed our strategy to serve and meet their needs.

We also have a very clear understanding of our iconic Target brand, its strengths and its meaning to consumers. From the work last year, we know, Expect More, Pay Less, our brand promise, remains relevant with consumers. We also know we're at our best when we deliver on both sides of that promise.

Quite frankly, as we look back, we can see that we decoupled Expect More, Pay Less during the great recession. In many ways, you can say, we lost our brand balance. But today, we have a clear vision of how we differentiate Target in this marketplace and deliver what the guest expects from us. I can promise you, we will not lose our balance again.

We have defined five key priorities, that we will support with resources and investments to enhance the capabilities. First, we will be a leader in providing the guest the ability to shop anywhere and anytime they want, in stores, online and with their mobile devices.

We will take a channel-agnostic approach to growing our business. Delivering products in whatever way is most convenient for our guest, with a focus on experience in an environment that's simple and energizing. That's because the guest becomes much more valuable when they interact with us in more than one channel.

Specifically, compared to a store-only guest, a guest who shops both in-store and through our digital channel, shops about three times more frequently, generating three times the sales and over two-and-a-half times more margin dollars.

Importantly, in-store sales from these guests are much higher than store-only guests, meaning that digital engagement doesn't take away from our stores. It actually creates additional store trips and sales, as our guest develops a deeper and deeper relationship with our brand. What this data shows us is that we'll be much more successful, if we meet the demands of today's guest, no matter how they choose to shop Target.

The second priority is to clearly define roles for our merchandise categories, an approach that Kathee will describe in much greater detail today. In defining these roles, we've chosen to elevate signature categories, the categories our guest has told us are most important to them; namely: Style, Baby, Kids, and Wellness. This clarity is another example of the focus I have mentioned, less organizational complexity, greater simplicity in the experience.

Signature categories account for $20 billion in sales, representing more than a-quarter of our total sales in the U.S. These are the categories that Target has historically been known for. And they play a very key role in differentiating Target from everyone else in the marketplace. Kathee will talk about the strategy, but here is a sneak peek at the campaign, it's all about style.

[video presentation]

Now, while I personally love the campaign, I love the product that Kathee's team has designed and developed even more. And importantly, it's available in our stores and online right now. It's important to note, our signature categories have some of the most attractive gross margins within our assortment, so growth in these categories is positive to our gross margin mix.

Now, I want to pause here for a second and talk about food, because I believe we've created, perhaps I have created some confusion regarding this important category. And while food itself is not a signature category, it will play a key role in our overall assortment.

Food is more than 20% of our business, and it ties very closely to our focus on Wellness. Our guest has told us, they expect to have food in our stores, but they'd like us to offer more choices to support their wellness goals, more natural products, more organic, more gluten-free, items that have simple, cleaner ingredient labels.

In addition, the guest has told us, they'd really like us to be more specialized in food, inspiring them with unique and differentiated items in our assortment. As a result, we believe we have a very clear opportunity to better integrate food into our stores and into our brand, supporting wellness and complementing those style categories. By providing comprehensive solutions for entertainment and occasions, we will help our guests celebrate the joy of food.

With these very, very clear guest insights, we have an idea of where we need to go with food. And I will tell you, the transformational work has already started. We will make progress in this space in 2015, but the biggest changes in our food assortment and presentation will be completed next year.

Our third priority is to become increasingly local in our assortment and personalize in the experience we provide. Today's consumer expects us to have locally relevant assortment and create a shopping environment that reflects their local community. I don't have to tell anyone in the room here today. This is not a new concept in retail. And based on the experience of others who are further down the road, we believe this presents a meaningful opportunity for Target over time.

At Target, we've just begun to scratch the surface in this opportunity. We'll be investing to build the capabilities to deliver a much more relevant in-store and online experience going forward. Similarly, today's consumer expects to receive relevant personal offers and experiences, and we're investing to build digital capabilities to make Target a leader in this space.

We are absolutely thrilled that Mike McNamara will be joining our team as our new CIO, and he'll be able to advance this very important work for us. Mike spent 15 years at Tesco, and has a proven track record, as a leader in technology and in digital. Mike's insights and expertise will help us remake technology at Target.

Fourth, we're focused on delivering new urban formats that allow Target to serve consumers in these rapidly growing, densely populated areas. As consumers across the U.S. move back into cities, we have a compelling opportunity to deliver a differentiated Target assortment and experience. So we're carefully testing and rolling out our new City Target and Target Express formats.

We opened our first City Target stores in 2012, meaning we began to comp these numbers and these sales in 2013. And so far, the City Target results have been phenomenal. While these locations started with strong sales in their first year, as a group they have consistently comped in the mid-to-high single-digits over the last couple of years.

On average, these stores are about 25% smaller than a general merchandise store, and they generate higher average sales per store. This means sales productivity is approximately double the average of our larger stores. In addition, they have a very favorable merchandizing mix, meaning that gross margin rates in a City Target store are in the high 30% range, nearly 10 points higher than the rest of the chain.

By integrating digital into this physical format, the stores also provide access to our full online assortments. And even with the higher investment rates required in these urban and densely populated locations, we're seeing a very strong return on invested capital in our City Target stores.

We're also very excited about our Target Express format. At about 20,000 square feet, it's less than half the size of the City Target. We opened one Target Express store so far in our hometown of the Twin Cities, and we're seeing really strong early results. We will continue to test this format in 2015, as we open up eight new locations throughout the year.

Now, I know some of you have had a chance to walk through a Target Express, when you've come up to Minneapolis. But for those of you who haven't, let's take a quick look.

[video presentation]

If you can't tell, David is really excited about this new format.

Finally, our fifth priority is to simplify the way we work, eliminate complexity, control cost and free-up the resources to fuel the investments in the four growth opportunities I just described. The efficiency of our store productivity model is world-class. And we've got a compelling opportunity to take the best practices from our stores back to headquarters and free-up resources, while becoming more agile in the way we work.

Simplification, cutting complexity at headquarters, will make us more competitive. We're empowering the team in ways they haven't been empowered in years, to act quickly and get new products and services into the market as soon as possible. The outcome is what's vital. It's not about the process.

And as John will outline in more detail, we have identified opportunities to reduce both expenses and cost of goods sold going forward. That's going to fuel our growth. By applying these principles over the next two years, we expect to save an incremental $2 billion, which we'll reinvest in growth and profitability for Target and for our shareholders.

As we focus our resources on making progress in these key five priorities, we expect to accelerate topline growth by driving traffic to our existing stores, by elevating signature categories, enhancing our guest digital engagement with Target, becoming more localized and personalized and ensuring we provide a great in-store experience.

We want to make sure our guests can shop on demand by enhancing our mobile and our supply-chain capabilities, leading to growth in our digital sales and by thoughtfully growing our store base, particularly these urban formats, like City Target and Target Express, to further elevate the overall Target brand. Our entire leadership team is focused on advancing these five priorities to generate profitable growth. And we're excited about the progress we can make over the next few years.

As we work to accomplish these goals, we're applying a set of principles that guides our efforts. We will be very disciplined about prioritizing our work, so our teams make rapid progress against these most important initiatives. This goes hand-in-hand with controlling costs and simplifying the way we work.

We are absolutely committed to maintaining alignment across the organization to ensure everyone is focused on the same priorities that will benefit Target and our shareholders. We'll continue to make the necessary tough decisions to position the company for long-term success by performing rigorous analysis, acting decisively and moving quickly.

And we will focus our teams on delivering outstanding execution, while holding ourselves accountable for results. And this will include performance-based incentives that are aligned with our shareholders. As John will cover in more detail, our plan support a financial algorithm for Target, designed to deliver compelling shareholder value.

In developing this algorithm, we've been very thoughtful in planning the appropriate level of investment to enhance our capabilities, our technology, our supply chain and differentiating Target from our competition. We want to make sure we're properly investing behind these key strategic initiatives.

However, given the fact that our business generates far more cash than our investment needs, we will continue to support our dividend, and we expect to repurchase billions of dollars of shares over time. Importantly, this leadership team is committed to renewed discipline regarding return on invested capital.

Now, this has historically been a strength for Target, but we've underperformed in recent years. With a much more agile, less complex organization, we will not underperform going forward.

So before I conclude, I want to give you a brief overview of our plans for the rest of the day. First, John will provide you more detail on our longer-term financial algorithm and our expectations for financial performance in 2015.

Then Casey will highlight the role of strategy and innovation at Target, outline our important efforts to build digital, mobile, supply chain and personalization capabilities. Importantly, Casey will talk about our efforts to rekindle innovation and that innovative spirit throughout the organization.

Following Casey, Kathee will define our merchandising plans and talk to you about category roles, with a focus on style. She will also provide detail around our food reinvention as well as our focus on localization.

And, finally, Jeff will provide insights into our Target brand, and how his team is working to modernize marketing at Target. And he'll show you some examples of the work that support the priorities we've outlined today. Following Jeff's remarks, John and I will host a Q&A session.

Before I turn it over to John, I want to thank you for your attendance today, and importantly, for your continued support. We're excited to share our plans with you. And while we're still in the very early stages of the transformation, and there's so much more work to be done, we are very excited about the progress we're making and very excited about the opportunities in front of us.

With that, I'll invite John to the stage to provide you details of our financial plans. John?

John Mulligan

Now that Brian has outlined our strategic plan and leadership principles, we thought it would be helpful to move right into the specific financial goals, so you know where we're headed for the next five years. Then, Casey, Kathee and Jeff, will provide more specifics on our business and plans to support our strategic priorities and deliver on these financial goals.

But before I get started and get to the heart of my presentation, I want to pause and describe why we now operate as a single segment business. I want to address this topic, because many of you ask us to isolate the economics of our digital business. It's a natural question, because we have some online-only competitors and some other brick and mortar competitors who treat the digital channel as a distinct business.

However, given our operating model and our strategic plans, we don't think of our digital channel as separate. At the highest level our goal is to grow both topline and the bottomline by creating profitable retail relationships with guests. And we are agnostic to the channel, in which a guest chooses to interact with our brand.

As Brian showed you, it's clear that our most profitable relationships are with guests who engage with Target in more than one channel. This is very similar to our merchandise assortment. We offer a broad set of merchandise categories, and our relationship with guests become much more profitable, when they increase the number of categories they shop.

Let's consider diapers and formula for a minute. Given their extremely low gross margins, someone who tried to analyze these as separate businesses would wonder why we choose to sell them. But as you all know, we want to sell a lot of diapers and formula to our guests, because there is overwhelming data showing guests who buy those items at Target are much more valuable than guests who don't. Bottomline, if we invest with discipline and control costs, we will increase Target's return on invested capital when we grow sales across all our channels, by deepening our most profitable guest relationships.

Before I turn to more specific expectations for 2015 and beyond, I want to walk down the P&L and discuss our thinking about the evolution of each line over time. Let's start with sales, and as Brian already described, we'll work to grow the topline in three ways.

First, we're planning modest annual growth of about 1% from our existing stores. Over the next hour, Casey, Kathee and Jeff, will talk about the specific ways we will drive traffic and sales in these existing locations, including our work on category roles, localization, personalization, loyalty and digital capabilities.

Second, we expect to see continued annual growth in digital channel sales of 40% or more. Casey will cover the progress we've already made, which led to industry-leading digital channel growth in 2014. And he will talk about how we're going to build on last year's success with plans to deepen our digital, data and supply-chain capabilities to fuel continued rapid growth in the years ahead.

Finally, we expect some modest net sales growth from new stores, including Target Express and City Target locations. And while we'll be disciplined about rolling out these new formats in the next few years, we believe they will play an important role in our store portfolio over time.

Now let's turn to gross margin rate. And I want to spend a little bit of time here. We believe that a gross margin in a range around 29.5% is achievable and appropriate for Target over time. This would represent a small recovery from our 2014 rate, which was significantly impacted by promotions resulting from the data breach.

Beyond this modest recovery in 2015, there is a set of pluses and minuses that net out to keep us in that range. This slide shows the sources of potential pressure to our gross margin, along with the expected sources of benefit that will keep us in balance.

I want to start by addressing the expected pressures, because I know that's been a cause of concern. And, first, let's focus on the primary concern we've been hearing about lately, which is the potential for gross margin dilution from a higher penetration of digital channel sales. There is no doubt this pressure is real, but perhaps not quite to the extent that many of you are thinking.

Last year, our gross margin on digital channel sales was about 23%, including a fourth quarter dominated by free shipping. But let's break down our digital channel gross margin just a bit further. Without shipping, as you know, our digital channel product margin is meaningfully higher than stores channel, since it benefits from a richer mix of home and apparel sales.

That higher margin is brought down significantly by shipping costs, which, frankly, at Target, are much higher than they should be due to a lack of scale in our digital supply chain. That's why our opportunity to use store as a shipping point is so exciting. We can leverage existing store assets to dramatically lower shipping costs and reach our guests much more quickly.

Even though the capability is new for us, our guests love the shorter shipping times, and our stores love the ability to drive more sales in their buildings. Later, Casey will show a video that provides behind the scenes view of the ship-from-store process.

Looking ahead, with meaningful investments to enhance the flexibility of our supply chain, including rapid expansion of ship-from-store, we believe that greater scale and efficiency will significantly reduce the pressure from shipping costs, which, given where we're starting from could allow us to improve our gross margin on digital channel sales over the next five years, but that's getting ahead of ourselves.

Let's simply assume that supply chain cost savings simply offset other digital channel gross margin pressure, and we maintain current rates, while growing digital channel sales at a 40% pace over the next five years. You all can do math as well as I can, this would drive a total of about 60 basis points of gross margin pressure between now and 2019. That's over five years, not annually. And while that's certainly not trivial, it's something we would manage, if it were to occur.

Also on the minus side, beyond gross margin pressure from digital, we're expecting some pressure from overall pricing, as we live in a world of complete price transparency, in which competition and promotional intensity are expected to remain high. However, on the positive side of the ledger, we have a few tailwinds in gross margin as well.

First, as I mentioned, in 2015, we expect to recover a small portion of last year's gross margin investments and aggressive promotions to regain visits after the data breach. For reference, those investments put about 60 basis points, that number should be familiar by now, a pressure on our gross margin rate last year.

Second, we expect category mix to provide a modest tailwind to our gross margin rate over the next five years. As Brian mentioned, and Kathee will spend more time on later, we're investing to accelerate sales in our signature categories. And these categories have some of the highest gross margin rates within our overall assortment, both in-store and in digital channels. You saw this in our fourth-quarter results, which clearly demonstrated the benefit of positive sales mix in these categories.

Third, our localization efforts will benefit our gross margin rate, as we enhance the local relevance of our merchandise assortment, avoiding clearance markdowns we'd see on less relevant items. And finally, beyond all the other pluses and minuses, about $0.5 billion of the planned cost savings, Brian outlined earlier, are expected to reduce our cost of goods over the next two years. With this savings, we can reinvest in pricing and digital channel growth, without diluting our gross margin rate beyond the range we're expecting in 2015.

Now let's move on to the SG&A line. Our plans envision an SG&A expense rate in the range of 19.5% to 20% over the next five years. Consistent with the last several years, we'll continue to see pressure from our efforts to build new capabilities and invest in store service, as a key differentiator for our brand.

However, with expected savings of approximately $1.5 billion over the next two years and a continued emphasis on controlling costs to create new capacity over time, we believe we can fund the expense investments necessary to grow our business without causing a deterioration in expense rates. We expect to realize about $500 million of these savings in 2015, which will be invested in approximately equal parts between initiatives to drive growth and profitability this year.

As you can see from this chart, in addition to the expected cost of good savings, we've identified a broad set of opportunities on the expense line, ranging from centers of excellence, supply chain efficiencies, non-merchandise procurement and technology.

Now, as you can see, there is no single dominant opportunity, but in concert these efforts will fund the expense investments we need to make to transform our business over the next several years. In a few minutes Casey will provide more details on our efforts to transform the way we work.

I should note that in the near term, some of these changes will result in restructuring charges from time-to-time, beginning in this first quarter. These upfront costs reflect necessary investments we need to make to put our operations on the right long-term path, creating enormous value over time.

Putting our gross margin expense expectations together, we expect to produce EBITDA margins in the 9.5% to 10% range over the next five years. While this expectation is moderately below our peak margins over time, we believe this plan strikes the appropriate balance to allow us to grow gross profit dollars most quickly over time.

Now that we've covered operating margins, I want to spend a few minutes on our capital structure and deployment of cash. First, let's talk about capital expenditures. And here, consistent with our operating margins, where we are saving to reinvest in growth, the mix of our capital expenditures and the makeup of our invested capital base is expected to change over time.

For context, let's look at total CapEx in the U.S. beginning in 2010 through our plan for 2015. You can see that overall CapEx has remained in a range around $2.1 billion that entire time. However, the makeup of our CapEx has changed dramatically. Our 2010 CapEx was dominated by investments in our PFresh remodel program and new stores, which in total represented about three-quarters of our total investment.

In 2015, we expect to invest just under half our total CapEx this year in supply chain and technology, for a total investment of $1 billion to support our digital and flexible fulfillment efforts. In addition, the amount of capital devoted to remodels and merchandising initiatives will remain significant, as we invest to enhance the store experience, particularly in signature categories, which Kathee will cover in a bit.

However, the reason the 2015 CapEx is not expected to be meaningfully higher than the last few years is because a smaller portion will be invested in new stores. Going forward, we're planning a modest number of store openings and an increasing mix of urban formats like Target Express. Specifically, of the 15 new stores we've announced for this year, eight will be Target Express locations, which as Brian mentioned require much less capital than our larger formats.

Let me pause here and be clear. If over time we identify a bigger opportunity to profitably grow our store base, we're not constrained to an arbitrary number, and we will not hesitate to invest in high-return projects. But from today's perspective, we believe the greatest opportunity for incremental store growth will come from the Express format, which is relatively capital light.

So for instance, if our tests in this format continue to go well, I could see us rolling out an increasing number in a few years. But even so, if hypothetically we opened 50 Express stores in a year, those stores would require $300 million to $400 million of capital. I think just as importantly, there is no need to rush the rollout of the Express stores. We expect to continue to carefully test the format in the next couple of years and we'll update our rollout expectations, as we learn more.

So when we look at expected CapEx, we believe we'll stay in the $2 billion to $2.5 billion range over the next five years. And the reason we'd reach the high-end of that range would be the potential to accelerate the pace of openings of Target Express stores. Given this CapEx profile, we expect to generate billions in excess cash every year that we will return to shareholders in the form of dividends and share repurchase.

As you all know, we will prioritize the dividend first, and we're committed to maintaining our record of annual increases, which we've done every year since 1971. Over time, we believe a dividend payout ratio in the 40% range is appropriate, somewhat lower than our current payout ratio.

However, to reach that goal, we'll need to move along a glide path, which would move us towards 40% over the next four to five years. As a result, we expect dividend increases in the next few years will be lower than the 20% rate we have achieved in the last five years. Going forward, increases will more typically be in the 5% to 10% range, as we move along that glide path toward a 40% payout ratio. Beyond cash for dividends, we expect to have billions of additional capital for share repurchase in the next few years.

Now that you've had almost a week to look at our fourth quarter balance sheet, you can see we started the year in a very healthy cash position. We continue to generate cash and we feel good about the trajectory of our business. And as a result, we expect to revisit our plans with the agencies this quarter and begin repurchasing shares soon.

In total, we expect to have the capacity to purchase about $2 billion of our shares this year. Beyond this year, our plans envision the ability to return about $3 billion each year through share repurchase, while maintaining credit metrics in support of our current investment-grade credit ratings.

Everyone knows, I'm a broken record on this, but I want to pause and emphasize our goal to maintain these debt ratings. Given our Expect More, Pay Less, brand promise, this and the conservative balance sheets of large, price-based competitors like Amazon, Walmart, Costco, we believe our single A ratings are strategically important, as they allow us to maintain pricing credibility in both good times and in challenging ones.

You need only look back over the last 18 months to see what I mean. On top of challenges that emerged in Canada in the middle of 2013, we faced the additional challenge of a data breach at the end of the year.

Throughout 2014 our balance sheet allowed us to continue investing in the business, while engaging in aggressive promotions to restore traffic. In our view that's what a balance sheet should do, enable the strategic management of the business, not handcuff a management team, when they need to act.

So let's step back from all of that and look at the state of the business today. As we undertake the transformation that Brian walked through earlier, we have an outstanding brand and fiercely loyal guests. Nearly 1,800 well located great looking stores, 38 distribution centers, nearly 350,000 team members and almost 15 million REDcard holders.

Guests visit our stores more than 25 million times a week, our digital channels more than 15 million times a week. And we're the only retailer who has been named Mobile Retailer of the Year by Mobile Commerce Daily, twice.

We generate well over $70 billion in sales. We have very attractive operating margins. Our operations generate more than $5 billion of cash annually. And we have a long history of returning cash to our shareholders through dividends and share repurchase.

So while we're at the early stage of the transformation, and there is a lot of work to do over the next several years, we clearly start from a position of strength. And we have a well-defined plan, a focused set of priorities, driven by insights on what our guests want Target to deliver.

Before I move on to the longer-term financial algorithm for 2016 and beyond, I'm going to start with our guidance for 2015, a year in which we'll move beyond a very difficult 2014 and make progress through the early stages of our transformation. On the sales line we're expecting total growth of 2% to 3%, reflecting comparable sales growth of 1.5% to 2.5%.

Within our comparable sales, digital channel sales are expected to grow another 40%, contributing about half of the overall comp. We expect to see modest improvements in both our gross margin and expense rates, as we annualize the intense post-breach promotions in the first three quarters of 2014 and begin to benefit from the cost savings initiatives outlined earlier.

As a result, we expect an EBITDA margin rate about 20 basis points to 30 basis points higher than 2014. We expect to invest between $2 billion and

$2.5 billion in capital expenditures, reflecting $1 billion of investment in technology and supply chain to enhance our ability to deliver shopping on demand for our guests. We expect to grow our quarterly dividend between 5% and 10% later this year.

And finally, as I've mentioned, we expect to resume share repurchase soon, with a capacity to retire $2 billion of our shares by yearend. Altogether, this plan will deliver $4.45 to $4.65 of adjusted EPS compared with 2014 adjusted EPS of $4.27. Outside of adjusted EPS, we expect to record first quarter 2015 restructuring charges of approximately $100 million, resulting from some of the cost saving initiatives, I outlined earlier.

Moving beyond 2015, let's put everything together to see how our strategic plan delivers the elements of a straightforward financial algorithm over time. Specifically, beginning next year in our fiscal 2016 and beyond, we expect total sales growth of about 3% annually, driven by sales growth of about 1% from existing stores, digital channel sales growth of 40% or more, and up to 0.5% from net new physical assets.

On that growth we expect to deliver EBITDA margins in the 9.5% to 10% range. To support our strategic plan, we expect CapEx in the $2 billion to $2.5 billion range. We expect to grow the dividend in the 5% to 10% range annually, as we move along that glide path toward a 40% payout ratio about five years from now.

We expect to repurchase about $3 billion in shares annually. Put that all together, and we expect annual EPS growth in the 10% range, which with the dividend, will put total annual shareholder return well into double digits. Importantly, given that we plan to grow profits on a stable base of invested capital, we expect to grow our after-tax return on invested capital from the low-teens in 2015 into the mid-teens over the next five years.

I want to stress that we've been very thoughtful in developing this financial plan. The work began with last year's strategic review, which provided the foundation for bottoms-up guest-focused plans for investment, category sales, margin, and expense, all of which roll up to this plan. We're confident this plan is achievable. And we are building management incentives that are based on delivering or exceeding this plan.

With that, I'm going to turn it over to Casey, Kathee, and Jeff, who will outline the business plans that will support these goals. Casey?

Casey Carl

Good afternoon. I'd like to start this afternoon by explaining my role as Chief Strategy and Innovation Officer and the leader of our newly established transformation office. My enterprise strategy team sets the strategic agenda for the corporation, identifies the critical priorities and investments, and determines key capabilities needed to position Target for sustainable market share growth, which creates a defensible business model that keeps us out in front of our competitors, and most importantly, deepens guest loyalty for this brand.

Now, we've been on a multiyear journey to define Target and our core business for the future. We started this work by developing a deeper understanding of just who that guest is, learning what is most important to them. And with those insights, we defined the strategic priorities that Brian just laid out. To deliver, we will be more intentional about building the foundational capabilities that we need today and those that we will need to fuel and accelerate future growth.

This will include being more declarative about our assortment and what we stand for, especially in the signature areas where we want to be famous, leading with mobile and managing our supply chain and inventory differently to support the new ways our guests want to shop; strengthening our data and analytics and technology capabilities as they underpin our entire strategic agenda, including our approach to both loyalty, localization, and personalization; and fostering a new culture of innovation, one that rekindles entrepreneurial spirit that's defined Target's success, but also one that creates disruptive capabilities and new revenue streams of growth to inform the Target of the future.

Now, in order to successfully execute our strategic agenda, drive growth, and fuel innovation, late last year we stood up a transformation office to carry out four primary objectives: to transform our headquarters and our central management organization into a higher-performing, more efficient, agile and guest-focused team; to create a scalable and more sustainable cost structure; to realign resources and investments to accelerate our most important priorities and to fuel innovation; and finally, to simplify how we work.

That's our organizational structure, our operating routines, and our culture at large. This work will reach out to every corner of the company and has the full support of the leadership team for holding the entire company accountable for realizing this transformation.

But before we can talk about where we're going, it's important to look back at where we have been. Beginning late last spring, we started the most comprehensive and honest review of our business that we have ever done. There were no sacred cows. We looked at the industry, where we fit, and determined where we can win.

We took a hard look at ourselves from the most important perspective, through the eyes of our guests. And several key things really stood out. First, while the great recession challenged many companies to shift strategies to become more promotion and value-oriented, we decoupled our Expect More, Pay Less brand promise far too often. That cost us our style leadership and eroded guest love for this brand.

As technology moved from a support function to core capability and a guest-facing experience, we saw that we were too reliant on third-party vendors, and we lack a strong bench of in-house expertise. And as consumers rapidly embraced digital, we reacted too slowly. We played catch-up, and we treated the businesses separately, while competitors who doubled down their investments and moved to integrate their organizations grabbed market share.

Now, to be candid, these were some hard truths to face. We learned a lot, and we will not be caught flat-footed again. But this work was also instrumental. And have made very clear where we should focus our efforts to reposition Target as a growth company once again.

So if you look at where we have been and where we want to go, there are several critical capabilities that we have prioritized. In some cases, we moved very far, very fast. In others, we've closed some important gaps. And in places like mobile and in personalization, we think we are well-positioned to lead.

Now, as you well know, to truly become a growth company in retail, the future is digital. The key for Target, of course, is to fully integrate it into every aspect of the guest experience. We have been making considerable progress on this front, and many in the media and in the analyst community have taken note.

Digital sales are growing at a breakneck pace. We delivered a 50% increase in digital conversion last year and sales grew three-times faster than the industry average. And much of that growth is occurring in our signature categories, including home and apparel. Not only are we closing the gap, but digital sales are beginning to play a meaningful role in achieving our overall financial goals. Digital sales accounted for more than half of our total comp growth last year.

Now, there are a number of factors that are helping drive these results. First and foremost, we brought in the right digital expertise to both the business and the technical teams. Second, we aggressively invested in technology and supply chain infrastructure. Now, as you heard from John, we are spending $1 billion on supply chain and technology infrastructure this year alone, and that's on top of an aggressive amount of spending in the last two years. When you look across our competitive set, this positions us as a leading retailer, both as a percentage of CapEx and in total dollars.

We've made some dramatic improvements to the user experience. We have reconfigured our team structures to move faster, and we took friction out of the guest shopping experience. More than 70% of our digital experiences are brand-new including our desktop, mobile apps, and registry experience.

We've adapted our operating model to give our teams the right structure for greater agility and faster speed to market. In the year ahead, we will continue to invest and expand these capabilities, including moving to more cloud-enabled technology to expand capacity, improve speed, and reduce overall costs.

And just last week, we cut our free shipping threshold in half. At $25, we are now well below our primary competitors. Given the strong response we saw from an aggressive free ship policy this past holiday, we wanted to signal to our guests that shopping our digital channels has never been easier.

We've also seen nothing short of explosive growth in mobile. If you look at our guests and how they want to shop, mobile is truly the new front door to Target. Now, this is a staggering statistic. 98% of Target guests shop digitally, and the vast majority of that shopping occurs using a mobile device. From a routine trip for groceries to creating a wedding registry, almost everything begins on mobile. Last year mobile traffic grew 44% and conversions shot up 69%.

But an important focus for us isn't how we grow mobile as a sales channel, but how we will apply a mobile-first approach in every way we engage with our guests. Every touchpoint is an opportunity to inspire, to anticipate a need, and to help simplify our guests' busy lives. Here's a short video that shows how we are leveraging mobile to better serve our guests.

[video presentation]

Now, as you saw in the video, we're going to continue to improve on the mobile experience in a number of ways this year; evolving the user experience by improving our in-store location and navigation capabilities, greater mobile payments integration, and testing new technologies like iBeacons to make shopping even more personalized.

We are going to continue to build on the success of Cartwheel, which has already generated more than $1 billion in sales. With more than 13 million users, it's one of the most downloaded retail apps ever. And we'll continue to test more personalized and meaningful offers with a guest set that enjoys the gamification of shopping and the savings that this app provides.

The role of the supply chain matters more than it ever has before. It's no longer about simply moving goods from factory to shelf. It has become a guest-facing operation capable of driving significant sales. Fulfillment choice has become a baseline expectation. The key is to continue to improve the overall experience.

In 2013, we rolled out store pickup chain-wide, and today 12% to 15% of our digital orders are fulfilled in store. But in key seasonal moments like those final days before Christmas, store pickup orders spiked, accounting for almost 50% of all digital transactions.

And store pickup is not only a convenient option for our guests. It's delivering meaningful savings on our shipping costs as well. Ship from store, which we launched last year is operating in 136 stores. It allows us to dramatically improve speed to guests and saves significant shipping costs, as these locations are much close to where are guests live. In fact, we can reach 91% of all Americans within one to two days by shipping from these locations.

We can also better balance inventory across our network. As items sell through late in the season, it helps ensure that we are always in stock as long as we have at least one item anywhere in the system. We have plans to expand this capability to at least 350 more stores by October of this year.

And our store teams love this fulfillment method, because it's easy to execute and they get credit for every order they fill in their total store sales results.

[video presentation]

In addition to these fulfillment options, we're also exploring new ways to get products to our guests like curbside pickup and rush delivery. Data and analytics is one of the capabilities where we know we need to make up ground quickly. But we also believe it has the potential to be one of our biggest strategic differentiators.

Today, we have lots of different data sources that give us unrivaled insights into our guests and their preferences. But we are not getting as clear a picture as we could because this work has been largely decentralized. So we're bringing all of our data and analytics together under a newly created center of excellence to help us scale these capabilities even faster.

Guests live in an on-demand world and they expect personalized experiences, offers, promotions, content, and more, that's curated to their wants, their interests, and their needs. Our goal is really about building the foundation, so we're providing a unique Target experience for each guest every time they shop.

In just six months we created a personalization engine that combines our in-store and online purchase and browse data. We are currently one of the only retailers leveraging the power of both sets of data at this scale. We have already launched product recommendations with this capability. We rolled it out on Target.com to all guests last fall, and we've seen conversion increase by more than 30%.

This year we'll focus on more personalized email marketing, more tailored promotions, and targeted offers with Cartwheel in our flagship app. In addition to developing a centralized function for data and analytics, we are also prioritizing efforts to improve our technology performance, including updating our development and our delivery models.

Now, as Brian mentioned, we have a new CIO in Mike McNamara, who brings a wealth of experience in weaving technology into guest experience and supply chain capabilities. Last year we made a lot of progress in a few key areas, including delivering strong operational performance during peak season, simplifying our structures to drive faster results, embedding technology teams into the business to focus on stronger alignment to business goals, and building capacity and enhanced capabilities in data security. But we know we have a lot more work to do and we have to quickly drive more productivity, given the amount we already spent.

What we've talked about so far are the fundamental capabilities we focused on to drive our core business. But now I want to shift gears and talk about what we're doing to push outside of the traditional bricks and mortar box. And it all rest on what I said at the beginning, and that's rekindling the spirit of innovation that Target has drawn upon on our very best days to vow our guests and to build love for this brand. We need to be creative in imagining new ways to leverage our existing strengths and assets. And we need to build more innovation muscle, so that we're prototyping and developing a pipeline of new revenue streams.

We have established an enterprise growth initiatives team based in Minneapolis and San Francisco to identify, evaluate and concept new products, services, even platforms. It stretches from looking at what wholesale opportunities might exist for our own brands in international markets to figuring out where to play in the Internet of Things, which was by far the biggest buzz at this year's CES.

There's a huge market opportunity around connected devices, up to $3 trillion, but no retailer has capitalized on it yet. From Fitbits to Sonos sound systems, our guests love these products. But in most cases they don't fully understand how they work or if they can work together. How could Target connect disparate experiences from a Nest Thermostat to your Apple Watch and create a platform for consumers? How can we help guests better understand these products potential?

Now, while it's too soon to tip our hand, we're getting close to unveiling a really exciting new project where we'll help entrepreneurs test concepts, get first access to new products and convene with others in inventing new technologies in the Internet of Things space. This team is also focused on developing products and solutions that we can bring to market ourselves.

[video presentation]

Now, as a busy parent of two boys I certainly would have loved to have this diaper dispenser. Now, clearly a lot of cool things are coming out of this team. And some of them may never see the light of day, but others have the potential to be total game changers. But relying on a single office as a hub for innovation would be thinking too small.

Throughout Target's history, so much for our breakthrough work has come as a result of collaboration between our teams and our partners. So we're working to foster a new culture of innovation that challenges and empowers our teams to push boundaries and do what's right for our guest, even if that means disrupting ourselves.

We recently hosted an in-house design competition where one of the winning ideas was adding a mobile phone holder to our shopping carts. This guest-centric solution came from a member of our internal marketing team, a father who knows all too well as anyone, that juggling his three kids, a cart, and an iPhone takes more than two hands.

Great ideas can come from anywhere. Not every idea needs to be the next Uber, but we have 350,000-plus team members who are also our guests. As an organization we are challenging all of them to look at every aspect of a guest experience and figure out how to make it better. And sometimes all it takes is a plastic tray.

Finally, underlying all this work is the need for new talent and expertise. And we are looking for the best and brightest from around the globe. A quarter of our leadership team and nearly all of our senior management for Target.com in mobile, marketing, and data security joined Target within the last two years.

We have been aggressively hiring data scientists, engineers, product managers, and visual merchandisers. And we have recently established an entrepreneur-in-residence program. And within that same timeframe we have opened up West Coast offices in San Francisco and Sunnyvale and expanded our presence in Bangalore and New York. And while these cities represent rich pools of design and engineering talent, they also give us a better ability to connect with smaller startups and VC firms looking to build more partnerships and strategic alliances.

Bottomline, for a company whose roots stretch back door than 100 years in Minnesota and that has historically managed centrally from there, we are branching out to other places where great talent resides and where innovation is flourishing. These capabilities are already transforming Target, and we know they are critical to driving our strategic agenda forward.

Continuing to evolve will require trade-offs and change, but we are committed as a leadership team to stay focused on our guests and the strategies that will drive growth for Target. We are pleased with the progress we've made this year, but we know we need to be bolder in investing these capabilities to fuel innovation and future growth.

And now, I'll turn it over to Kathee.

Kathryn Tesija

Well, by now I hope that you all know it all starts with our guest. We are driving change across our merchandising strategy and we're putting the guest first, style forward, and making shopping at Target both easier and inspiring.

Now, for a couple of decades the boomer mom was our core guest. She drove a minivan, lived in a nice house in the suburbs, and she wanted it all, kids, career and this crazy schedule that came with it. Fast-forward to today, and that mom is still shopping Target, but our guests are so much more diverse, more Hispanic, more millennial, more urban, more families, more dads, two dads, more kids. They all care about great style for themselves, for their kids, and for their homes. They buy products to express who they are. They care about wellness. And they want it easy and available. They love to shop. They love a great deal. And most importantly, they love Target.

Based on our research here is where Target over indexes, people who are digitally connected, love to shop, and demand great value. Now, at the intersection of these three sits our strategic target, who we call the demanding enthusiast. And Target, more than any other retailer, resonates with this consumer, which makes us uniquely positioned to win.

Call it, the center of the bull's eye, but when we talk about the demanding enthusiast, we are really talking about a mindset, and their mindset is different. Shopping isn't weekly routine. It's part of everyday life. They have a computer in the palm of their hand, so the lines between shopping and living are forever blurred.

Now, almost 75% of our guests begin their shopping on a mobile device. Think about that. They tap out a list. They read advice from a friend. They swipe open our app long before they step through the glass doors. Mobile is Target's front door. And the guests who walk through it shop three times as often and spend three times as much as the guests who only shop our stores.

Their expectations for quality, value, and great design have also dramatically evolved. They want products with stories. How was it made? What was the inspiration? The back story matters. Beyond products lies a thirst for solutions. How can Target make their lives easier and make them feel more confident? And they want help, whether that's product tips in the beauty aisle or turning that Pinterest forward into a party, they want Target to be their style accomplice.

As a mass retailer, we still need to appeal to a broad range of shopper types. And by designing a strategy with the demanding enthusiast in the center of the bull's eye, we'll raise the bar for everyone. The key, though, is to make sure that we are focused on what they care about most, the things that stir passion for our brand, the things we can do better than anyone else. And that's our four signature categories: style, baby, kids and wellness.

Now, after a detailed review of our entire portfolio, we have assigned all of our categories to one of four roles: signature, outperform, perform, and reposition. Each one represents billions of dollars in sales and billions of dollars in gross margin. So they are all important, but for very different reasons.

We will set more aggressive growth targets in areas where we're allocating more resources, and we'll expect other areas to grow more modestly with industry trends. Most importantly, we made these designations based on one factor, and that's what's most important to our guests. Not what I like, not what Brian likes, but what's most important to our guests.

Now, signature categories are the most important categories to the demanding enthusiasts. We need to drive outsized results, and we'll dedicate the resources to do that. These are not just big businesses that we will do well in. These are the categories that we will be famous for.

With our second category, outperform, Target can't perform unless these categories outperform the industry. These are our bedrock businesses. Take laundry detergent as an example. It's about a $1 billion business at Target and last year grew at about 1%. Now, that's much faster than the industry, but that's not going to drive a 3% total Target comp. And we are not going to be famous for laundry detergent. But it's a big bedrock business that's really important to our guests. They expect it from us, so we'll carry it. So we will invest to keep these businesses robust and outpacing their industry growth.

The perform category is about making smart and opportunistic choices. We can't over-invest here, because we won't the famous for these categories, nor are they bedrock businesses. They are convenient to purchase, while you're at Target, or they complement the signature categories like sunglasses complement style. So we need an enticing, tightly curated assortment.

Reposition is a temporary category. These are businesses that we need to assess and reinvent, because we don't have a strong enough point of view or the category is evolving and we need to get out ahead of it. Now, food is a great example. Overall, food is a big business. But what our guest sees today isn't what they expect from us. So we will invest here to develop and test a strong point of view for Target, iterating based on guest feedback. We will dive more into food in a few minutes.

Before I move on, though, I want to pause and make one thing very clear. This is not going to be a nibble around the edges kind of exercise. Nothing is sacred. We are putting every part of our go-to-market strategy on the table from our products quality to the aesthetic to price and presentation. We are changing the incentive structure for our teams to really drive the mental shift.

We are moving faster than we ever have to stand behind the things that matter most to our guest. And I will hold my team accountable for the results. While we have aggressive plans to accelerate growth in all of our signature categories, today I will focus on style to give you a better sense of the progress that we are making. And then I'll talk about how we are applying the same approach to reinventing our food business.

So style has always been a critical part of Target, core to our DNA, and it's what it evokes Tarjay. In recent years, as we've focused on gross margin rate improvements and decoupled our Expect More, Pay Less brand promise, we lost our edge. There's a lot of reasons why this happened, but no excuses. Let's talk about what we are doing to get back on top.

The recipe for reclaiming our style leadership has three ingredients, reasserting our merchandising authority with exciting, innovative, and differentiated product; more inspirational and compelling presentation across every channel; and strong, engaging marketing. A key capability for delivering this is one of the largest and most talented product design and development teams in the world.

[video presentation]

We are guest obsessed. We leverage research to understand our guests' style preferences, which provides input into both our brand portfolio and our business strategy. We build brands to address their needs and style preferences, which leads to love and loyalty for Target. Our guest insights team provides a constant drumbeat of what's important and what's emerging.

Our creative teams shop the world, consult with industry experts, and immerse themselves with culturally relevant experiences to be on the leading edge of trends. We translate these trends through our own brands, and develop meaningful products and solutions that our guests will love.

Now, apparel is a place that we've been driving change during the last year and momentum is starting to build. Apparel and our signature categories within it outperformed much of the rest of our business and many of our competitors in the fourth quarter. And we expect this strong performance to continue.

Target's clean, well-lit aisles have long been a differentiator at mass, but as our guests expectations have evolved, pulling a great look together from a sea of racks just wasn't cutting it anymore. So we introduced a new presentation including mannequins to help guests navigate between brands and better understand outfit options. Less than a year ago, we had mannequins in just 15 stores. Now, we are well on our way to 1,000.

So let's talk about a few of the highlights for the spring season. We are really proud of the work, but this is still just the beginning. We are looking at all of our brands top to bottom and everything is on the table. We built momentum in the fourth quarter, and we'll continue to see and feel more dramatic improvements over time.

The style aesthetic of the Merona brand is modern classic, and our guests have told us that this style represents the largest opportunity for Target. Our spring collections were inspired by the runway and our team's trips to South America, fueled by the excitement of the World Cup and the upcoming Olympics, which put Brazilian culture front and center on the world stage. This collection is a playful riff on the bohemian lifestyle, reinterpreted for the classic guest.

We think our classic guest will especially love the maxi dresses, crochet, and embroidered tops and printed bottoms. The summer collection is a continuation of the bohemian trend, but with the cleansing palette of white on white. Soft shades of white and ivory will come together with hints of metallic that will bring it to life. The Merona woman will love our soft feminine tops and crocheted bag as well as lei scarves.

The foundation of our own brand is a collection of amazing basics and must-have items. We'll offer industry-leading value by delivering best-in-class quality, performance, design, and price. Enhancements started hitting the floor this spring and will continue over the next year.

Now, Target dominates swim. We have been the number-one market share leader for years. But there is still a huge opportunity for driving sales. We will offer a broader portfolio of style aesthetics by expanding our assortment online. A great example of the kind of personalization that we want to offer is what I like to call our bikini blender. It's an online mix-and-match experience that gives guests that ability to pair different tops and bottoms to create their unique style expression and a perfect fit.

We are also introducing an exclusive line of swimwear on Target.com by designer and Sports Illustrated model Tori Praver. Her high-end line starts at $200 at retailers like Barney and Saks Fifth Avenue, while our line will sell for less than $55. So my advice is buy three suits at Target and you'll still come out ahead and the editors agree. We debut the line in Miami with them last month, and they went crazy for the collection.

Now, at more than $17 billion a year, the plus-sized market is an incredibly valuable one. But beyond a few niche players, no one has gotten it quite right. We missed the mark ourselves and caught heat from some very vocal, influential critics. And quite frankly, they were right. But instead of slinking away in retreat, we doubled down. We asked our critics to come on in and sit down with our design team, and they obliged.

Together, we are proud to put forth Target's first-ever plus-size own brand, Ava & Viv. This brand is happy, vibrant, and will enable our guests to express themselves through their style choices. The pre-launch buzz was overwhelmingly positive, and we are beating initial sales plan by double digits.

Now, just as Ava & Viv opened up a market with incredible untapped potential, we are deepening our reach in other areas. For example, we already over-index with Hispanics in apparel, so we've been testing an assortment that leads with the Latina guest in 50 stores. We are learning a great deal about what they love and what they don't.

And given the initial results, we are blowing this test out to 200 more stores later this year. We are also working to grow greater affinity by partnering with style ambassadors like Rodner Figueroa. The Univision host has more than 1 million followers on Twitter and Instagram, and we look to him to inspire our guests to look their best.

Now, Target pioneered limited-time-only design partnerships. We have done more than 150 collaborations to date. And, while many have emulated the model, I can say with authority, because I've been here for every single one of them, nobody does LTOs like Target. So when we are thinking about what is really resonating with our guests these days? Its print and pattern. And who does that better than Lilly Pulitzer. As you saw in the PD&D video, this collection is bright, beautiful. And if it doesn't say spring, I know what does. It's showing every sign that this will be one of our best collaborations yet.

Now, big moments like these are driving style leadership for this season and beyond. But little surprises around every corner is what's keeping our assortments exciting every day for our guests. We have a lot of great products in the works, and here's an example of a couple of our favorites. This spring, on Target.com we are curating a collection of men's products from brands like Billykirk and Duluth Pack under a banner we call Target Collective.

And when it comes to reasserting our style leadership, there's no better place to look than Room Essentials and Threshold. Now, these brands cover a lot of ground and together generate more than $3.5 billion in annual sales. We recently gave them both a major overhaul. Room Essentials is our entry point, but over time its appeal slipped with the millennial guests as its aesthetics started to look too much like dorm decor.

We needed the brand to grow up and play at parity with CB2 and West Elm. So we reinvented the brand last summer, elevated the quality and the product and modernized our packaging. Room Essentials finished the year strong, up almost 3% after being down about 9% midyear. Threshold evolved from the Plain Jane Target home to one of our most iconic brands. It's routed and relaxed classic aesthetic with the brand promise of quality and design for your home.

For spring, our trend inspiration was taken from the seaside villages along the Mediterranean. The color was inspired by watery blues from indigo to turquoise paired with chalky whites. Sun-bleached wood tones and shimmery silvers serve as foundational materials. Some of our favorite items are these hammered metal side tables, wood and rope lanterns, and acacia wood trays and bowls that are perfect for entertaining.

Here's a sneak peek of what we've put together for fall. It is the most beautifully designed product that our team has ever done. And we are confident that our guests are going to love it. Now, we hear from guests all the time that they love the product, but they want more help in seeing how the pieces work together.

So we started testing this insight in Minneapolis last fall and we're seeing phenomenal results. We created vignettes and set product as you would in your home. Guests say it doesn't feel like Target, and that's a good thing. We are changing mindsets from errand to inspiration. This presentation will be in 250 stores by mid-fall.

Now, registry is an incredibly important part of our home business. And we are totally reinventing the experience, leading with mobile, allowing our guests to add to their registry any time from their mobile app. Last fall, we launched a new registry platform. We replaced in-store kiosks with iPads and traded out scan guns with web-enabled iPods. And we are seeing double-digit gains in a number of registries created, registry size, and sales.

Now, shifting gears to food, Brian couldn't have been more clear. Food is an undeniably important business to our guests. And at nearly $20 billion, it's an undeniably important business to us as well. But overall, we lack a clear positioning and the shopping experience hasn't matched with our guests expect of our brand. Food is something that our guests shop for while they are at Target, not why they come to Target. And that has to change.

At the highest level, we have made a strategic shift and have begun talking about and thinking about food versus grocery, because groceries are transactional and food is emotional. We've spent the past six months talking to our guests to understand what matters most to them and how can we bring joy to their lives. We are redesigning food, the food strategy with the demanding enthusiast at the center. Now, the good news is they see our potential and they want us to thrive in food.

But there's a few things that are also really important to them, and we must get them right. They use food to show their families and friends affection. Wellness is a must, more organics and naturals, but they want help simplifying their choices and making it more attainable. The food rut is real. They stick to the same six-meal rotation, worried that the kids won't try something new. And while they want to be inspired, they wind up with the same six ingredients for those meals back in the cart.

So our solution is to bring joy to food in two ways, put those better-for-you options within reach, and provide fresh ways to celebrate every day. We know that there's a few occasions where we really need to shine, social gatherings like birthdays and dinner parties, as well as meal solutions so we can help answer every family's most frequently asked question, what's for dinner tonight?

We also know that there are six key categories that rise above the rest for the demanding enthusiast. So we'll be testing ways to improve the assortment, the presentation for these specific categories, so we can connect emotionally with our guests. Now, the size of the prize for the demanding enthusiast is big. One extra trip every three months is worth $2.5 billion in incremental sales annually.

It's important to set the right expectations, though, for how we'll reposition this business. We will spend 2015 testing and iterating and then amplifying our efforts in 2016. We are looking externally for expert talent to lead this repositioning. Bold changes will take time to test and mature, and but we are not standing still.

Right now, we have immediate opportunity to perform better. We will elevate the guest experience. We'll offer locally relevant assortments and we will inspire through differentiation. So it starts with delivering freshness. We are cutting our transit time from farm to store by 30%, and we are displaying products in a way that signals freshness and abundance. We will help guests discover new options for tasty, easy, better for you meals, through our recipe portal. You've heard us talk about localization. And nowhere is that more important than in food.

Segmenting local brands for staples like coffee and bread has been something that we've done for years, but we need to broaden that to all categories and incorporate presentation and signing. We're still the very early stages of this work, and we'll be using Chicago as our test market. And we will have it remerchandised by this summer.

The third priority is to inspire through a differentiated assortment. We'll do that through our strong portfolio of owned brands like Simply Balanced and Archer Farms, as well as meaningful exclusives like our recent partnership with Starbucks for their Estate blends and, from Chef David Chang, Milk Bar baking mixes.

Now, on the call last week we talked about this, but I can't underscore enough and how important innovation like Made to Matter is for our wellness strategy, both in terms of food and across our broader assortments. This is what we mean by making wellness more accessible to our guests. Made to Matter is an incredible partnership with like-minded companies who agree to develop new, better-for-you products designed with the Target guest in mind. It started with 16 vendors last year, and this year will expand to 31. And more are vying to earn the right to be a part of this collaboration. We expect sales will hit $1 billion this year.

Now, if this were a standalone-owned brand, it would already eat one of our 10 largest. We're driving change across merchandising, and we are reasserting our style leadership. Guests want us to be their style accomplice and help them express their individual styles. Our job is to make shopping both easier and inspiring and put the Tarjay back into Target. Now, I will introduce Jeff.

Jeffrey Jones

Thanks, Kathee. We are in the home stretch, by the way. I want to apologize in advance too for a voice that's been recovering from laryngitis for the last week. So my apologies.

Over the last decade, Target marketing has been defined by iconic ad campaigns and live events. Target marketing has also been the one to define the creative standard in retail, and when we're at our best for brands overall. That creative spirit is absolutely alive and well at Target today.

Now, these top marketing moments, the tip of the iceberg, if you will, are what most people see. And while iconic advertising and experiential marketing will continue to be important, it's really just one piece of what makes Target marketing work. I want to give you a sense of how we are modernizing marketing and reasserting our cultural leadership. And let me start with the foundation, which is the health of this brand.

One of the measures that we pay very close attention to is the top box metric of favorite retailer. 38% of all Target guests say Target is their favorite brand. That number is back to pre-breach levels. 46% of our strategic Target, the demanding enthusiasts say Target is their favorite brand. And given the macro shifts in society, it's really important that 54% of Hispanic millennials say, Target is their favorite brand. These are absolutely strong brand health metrics. But we still see opportunity to improve.

Now, given the shifts in attitudes and behavior that Kathee mentioned about the demanding enthusiast, it's absolutely essential that we evolve our marketing mix, so we can inspire and connect with these demanding enthusiasts in new ways. These modern marketing capabilities enable us to be where the guest is, online and on their mobile device. We continue to improve our ability to deliver content and value in the palm of their hand.

And at the same time, we have to remind America of that aspirational feeling they have when they shop at Target. Here are four examples of what I mean: our total digital media spend, the way we are harnessing the power of social media, our evolving loyalty portfolio, and the importance of marketing our new services.

First, we've made dramatic shifts in our media mix. In key growth areas like video and mobile, we've had double-digit growth in both of these channels, outpacing the industry growth by nearly 30% over the last few years. Our investment in search is up 55% and we see very meaningful results online and in store, given the mobile behavior that you've already heard about. Email-driven sales are up nearly 40% year over year. And this past holiday our digital spend represented 43% of our total budget and was up 40% over 2013.

Social media Target is now a channel where we can deepen guest engagement, enable the guests to share their love for Target, and drive meaningful traffic to Target.com. We now have the largest and most engaged social media audience in retail. We also have a best-in-class facility we call Guest Central. This enables us to have real-time insight and the ability to shape the social conversation.

Guests engage positively with our brand in social media more than 35,000 times every day. That's a positive message about our brand every 10 seconds. In addition to being recognized broadly for creative excellence, social is emerging as a meaningful traffic driver to Target.com. We've seen Target.com traffic and sales from social media double since 2013, driving nearly 30 million visits to Target.com last year. Last fall, our TOMS for Target collection, social media drove 8.5% of our digital traffic, four times the normal contribution from social.

Now, beyond engagement and traffic we are partnering closely with each of these platforms to be early adopters of their innovation and providing input on their product development roadmap. With both Instagram and Pinterest, we were among the first to make these platforms shoppable. We are one of the first two brands to join Facebook and partner with them on their new product ads, which they just announced last month. We've already seen a 20% increase in conversion just from these new ads alone.

Now, let's talk about loyalty. We see significant upside for our suite of loyalty programs. REDcard and Pharmacy Rewards continue to offer unique value. As you heard from Casey, Cartwheel is now a $1 billion business. We also believe that our mobile-first non-tender reward program like REDperks has the potential to attract millions of guests who are not interested in a credit or a debit product. Just a couple weeks ago I was in the test market of Raleigh-Durham. And based on that very early feedback, guests love this idea.

Now, the combination of analytical and personalization capabilities that Casey mentioned with the data and front-end engagement of these programs, we are able to think about lifecycle marketing in ways that add tremendous value to the guests and to Target. Like Brian said, consumers today expect shopping on demand. And our services help make this possible. Whether it's a subscriptions or in-store pickup, we have created a really simple visual language that gets recognized. And we continue to build awareness of these offerings.

Last year for the first time we advertised these services and saw a 50% increase in traffic to the Cartwheel subscriptions in-store pickup sites. This year we'll continue to integrate all of these messages broadly into our marketing communications, and in early summer we will introduce the new executions as part of this campaign.

Now, let me shift back to a few of the big marketing moments and how we'll support our signature businesses and reassert cultural leadership. First, the Grammys. This has been Target's Super Bowl for years, given its audience, its role in culture, and the importance of music to this brand. Now, last year we stole the show with Justin Timberlake. This year we created the show with Imagine Dragons. For the first time in history, CBS cut from a live broadcast in LA to a live four-minute performance by the Imagine Dragons in downtown Las Vegas. In case you missed it live, here's 30 seconds that captures that spirit.

[video presentation]

Now, we clearly gave viewers what they wanted, which was more music during the Grammys, and they responded with incredible numbers. Our #moremusic was the number one trending topic in America and the number two trending topic in the world during and after the performance. Social sentiment was 97% positive, which was better than anything Target had seen, and better than that brand's breakout performance in the Grammys the year prior.

That event earned Target nearly 1 billion media impressions nationwide, but this one's clearly my favorite. I loved a headline as a wonderful reward for our team who took this risk and did something that's never been done before. The fact that people didn't know what to call it, was it native advertising, was it content marketing, what's it a commercial, all that confirmed for me that we pushed into uncharted territory.

Let me shift back to one of our signature business, which is baby. As Kathee mentioned, we've taken many steps to grow the baby business, including reinventing the registry. Our number one job in marketing with baby is to compel people to register. Our creative muse for the baby campaign is the Hispanic millennial mom. You just have to look online to see that today's expectant mom shares every single stage of her journey, and some of you might say she over shares every single stage of her journey. But the reality is she's connected to her mobile device. So this year our marketing approach is going to be almost 100% digital.

In each channel, we'll organize our content around themes that capture these major elements of pregnancy and parenting. Bump style, so mom feels good rocking her bump; baby dig, so mom is inspired what her nursery could be and makes a great choice in the registry; and strolling to make sure dad isn't left out and the couple registers for cool gear, not just the stuff they need. This is just a sample of some of the creative tone and aesthetic that will appear online.

Now for 2015, Target's style will be a continuous campaign throughout the year and be our second largest investment behind holiday. This campaign recaptures that unique Target point of view that's made our work both famous and effective. In the spot Brian showed you, you heard that infectious remake of Groove is in the Heart by Charli XCX and Questlove. Music will once again being an enormous part of this brand in the campaign.

Kathee mentioned the importance of swim. Across the year, we'll also make smart tactical media decisions to ensure we are part of the cultural conversation. Right now, between Spring Break plans and the Sports Illustrated: Swimsuit Edition, we know that our guest is thinking, breathing, talking, tweeting, everything about swim.

We want to be an authentic part of those conversations across social channels, bringing them great products and great value, including this week's buy one get one 50% off promotion. This includes a Target style swim spot that debuted nationally last week. Take a quick look.

[video presentation]

Target will be part of March Madness. It's an extremely popular TV event with demanding enthusiasts. It's the fourth most-watched event on TV. We'll do ball in Target style.

[video presentation]

Digitally, we'll continue to create and distribute content in partnership with well-known style experts like Emily Henderson or our well-known beauty blogger Miss Maven. Even Julie Guggemos, who you heard earlier, will help share the story about all we're doing, and these are powerful and relevant voices that will help speak on our behalf.

Digital video continues to grow in importance for us. These little 10-second videos will begin to replace traditional banner ads.

[video presentation]

Now, Kathee has already shared the product and the role that these collaborations have played for Target for years. Within hours of this announcement, the Lilly Pulitzer collection was an instant classic. The #LillyForTarget generated more than 350 million impressions across 50 media outlets. But I think even more importantly to Kathee and I, the guest reaction to the pictures of this product was incredible. We obviously can't wait until April 19.

Now, as we've all mentioned a few times, the Hispanic guest is incredibly important to Target, and we start from a position of strength. As this segment becomes the new mainstream, we know they're trying to balance a sense of culture and authenticity, but are also trailblazing a path forward for their family and their community.

We'll tap into these insights in a new campaign called, SinTraducción, which celebrates the significance of those uniquely Hispanic moments and traditions that are literally untranslatable into English. On March 9, we'll introduce this campaign in Spanish on the hit comedy Jane the Virgin on CW. This is also a first for any brand.

Now, as I joke with my team all the time, welcome to the starting line. We know this is our moment and we know momentum is building, but we also know we've got a lot more work to do. This has just been a glimpse at how we'll support our signature businesses and reassert our cultural leadership, and we love where things are headed.

Now, let me invite Brian back on stage, and we'll wrap things up. Thank you.

Brian Cornell

Well, thanks, Jeff. And for those of you who don't realize it, a few hours ago, Jeff actually didn't have a voice, and it is one of the great comebacks I have ever seen over the course of a day.

Now, before we go to questions, I'd really like to thank many of you for taking the time to visit with us over the last few months. You've certainly given me a great sense for what's on your mind, and some of the questions that you're looking for us to answer. I know many of you have been wondering, are we focused on driving traffic and frequency? And I hope you walk away today realizing, it's absolutely on the top of our list.

As we said last week, as we talked about in our fourth quarter results, our fourth quarter growth was built on a traffic increase. We want to continue to focus all of our efforts in deepening that relationship with our guests to drive more trips, to drive sales, but bring them both into our stores and into our digital channels.

But traffic is critically important, it underlines everything we have talked about today. As we think about engaging with a guest anywhere anytime they want to shop, elevating those signature categories that Kathee talked about today, becoming more relevant, becoming more personal in our interaction with the guest, and making sure we have urban formats that allow us to follow consumers into the market. It's absolutely our focus on engaging with that guest and driving more traffic to our stores and more visits to our site.

Over the last week, we received a number of questions about wages, and are we going to stay competitive? And the answer is clear, it's absolutely. Our store teams have always been a differentiator for Target. And as you shop our stores, many of you have talked me about the great in-store experiences that you've had.

We pride ourselves in having the very best team in retail, and we're going to continue to make sure we invest in their development. We want to make sure from a marketplace standpoint we are very competitive from a wage standpoint. That allows us to continue to attract top talent who become great team members.

One of the questions that many of you have asked me very directly is, Brian, do you have the right leadership team in place? And hopefully, you'll walk away today recognizing the talent we have in our leadership team.

As you've listened to Casey talk about strategy; John talk about our financial outlook; Kathee take you through what we believe are incredibly exciting plans for our merchandising standpoint; and Jeff talked to you about how we're modernizing marketing at Target. The addition of Mike McNamara to our team, to lead technology and allow us to transform and build the capabilities, will certainly strengthen our team. But I can tell you we have a very strong team.

Across the entire organization, we're going to hold that team accountable to deliver results. To make sure that we continue to build the right organization, we're going to continue to draw external talent. But we want to make sure we have a team that's focused on execution, and you're going to hold me accountable, I'm going to hold the entire leadership team accountable for delivering against this plan.

But I have been asked time and time again. Do we have the right team in place? And I will tell you, absolutely. We've the right team in place. We're going to hold ourselves accountable, and we are going to focus on execution.

A number of you have asked me, do we have the right level of investment in place to fuel our future success? And I can tell you, John and I have spent hours and hours looking at our financial plan. We absolutely believe we have the right capital plan in place, and we build it from the bottom-up. So we're confident we have the appropriate level of investment to enhance our capabilities, to improve technology and supply chain as we go forward.

We have looked at it so carefully, because we recognized this will be what differentiates Target going forward. We've got to make sure we match up a great strategy with the right resources, the right team and the capabilities going forward. And we're confident that we have the fuel to invest in those resources.

I'm sure a few of you are sitting out there wondering, if we've been too conservative with our guidance today. And I will tell you all, there is certainly upside. We believe we're being appropriately conservative in this environment, providing a very balanced approach and developing an achievable plan over the next couple of years.

I am sure we sparked a little bit of interest, when we said we will resume share repurchases. And John used a very specific term, he said, soon. So you're probably wondering what soon means? Well, it means soon. But importantly, consistent with what John talked about, we want to make sure we maintain our investment grade credit rating.

If you have any questions about where we are in the transformation? A few of you have said, you know, Brian, how much longer until it's complete? I want to make sure you recognize, while we're very excited about the progress, we are in the very early stages of the transformation at Target. And we're going to need to work on these plans and this transformation for the next couple of years.

But I'm absolutely convinced that when we come back together three years from now, we will be a different company. We'll be a leader in the digital and mobile commerce space. We'll also be much more nimble, we'll be much more agile and we'll be an even more guest-focused company than we are today. Three years from now, I believe we'll be standing here talking about how we've recaptured our position in those signature categories that Kathee talked about today, and you'll see that reflected in increased guest traffic.

I believe three years from now we'll have enhanced those critical capabilities that Casey talked about, data, analytics, technology, They'll position us well in the future marketplace. And I'm absolutely convinced we're going to recapture that innovative spirit. It will be rejuvenated at Target. It's going to keep us fresh and it will redefine us in this new marketplace.

So in many ways, the transformation isn't the end of our story today. It's really the beginning of the next stage in our company history. And if we accomplish these goals, more importantly, when we accomplish these goals, we'll create a company that is very well-positioned to compete in a new marketplace.

So putting it all together, I can tell you I am really excited, and importantly I am really committed to the goals we've set. I personally deeply believe in this Target team. We are committed to our guest, we're committed to making sure we have a very competitive spirit, and we have the ability in place to execute this plan. What's more I know that executing this plan will translate into growth and the profitability we've outlined today.

Now, in case there is questions we haven't answered, I think we have about 30 minutes. And John and I and the rest of the leadership team would be very happy to answer those questions.

A few housekeeping requests. If you have a question, please raise your hand. We'll make sure we get you a mic. We'd like to make sure out of respect for those that are on the webcast, please use the mic. I'd ask you to state your name and your firm before asking any questions.

So with that, John would you join me on stage?

Question-and-Answer Session

Q - Dan Binder

Good afternoon. It's Dan Binder of Jefferies. You touched a little bit on the ideas you have for food. And when I'm in your store, I think about what parts are not complete for the total shop. I'm just curious as you think about food this year and testing stuff, do you envision ever becoming sort of a full shop with fresh bakery and a wider assortment of fresh produce and meats?

Because it seems like that's was really missing from the experience. While a lot of the things that you touched on were being constructive, that would probably make the biggest difference in gaining incremental shops.

Brian Cornell

Well, I'll start by saying, we're not going to ever say never. But as we look at what the guest is looking for from Target, Kathee talked about the feedback and the very clear feedback we've received. They are certainly looking for us to change our approach to the category. And I think it's very important that we transition from talking about grocery to food, because food is much more personal, it's much more inspirational and it's much more positioned with our brand and our brand promise.

So we want to make sure we get the basics right, and that includes improving assortment, delivering the type of products our guest is looking for from Target, more natural, more organic, more gluten-free, local items and items that have cleaner, simpler labels. We need to make sure we merchandise in a much more inspirational way, where we can help the guests celebrate the joy of food. But we want to make sure as we bring our new food reinvention plans to market, we're true to the brand, we're true to who we are and what we stand for.

So we're going to make sure we carefully test and learn, as we go forward. But we clearly recognize the guest has asked us to deliver food products, to elevate our assortment, to make sure we elevate the in-store experience and really celebrate the joy of food when they shop our stores.

So we'll understand a lot more in the next year, as we continue to test and learn. Understand what elements we need to enhance. But we clearly think it represents a significant opportunity for us, and we're going to partner with the guests, as we make those enhancements and changes.

David Strasser

David Strasser, Janney Capital Markets. You laid out a lot of merchandising changes at the stores today, most of which look really exciting out there. And more importantly, you're looking at really reshaping the entire culture of the company, whether it's going from a process-driven company to a customer-driven company, whether it's from a centralized business to a more decentralized/localized business or even store-centric to omni channel.

This is a massive cultural change in a lot of respects. It seems like, how do you prioritize these changes? Which of them do you think are the most difficult? Can you do them all simultaneously with a lot of confidence? And just lastly, are you adding any consulting consultants to help you do all of this?

Brian Cornell

Well, I think within there, there is about 25 different questions. So let me see if I can kind of tease out a few of the most important ones. And this is a question that we have received from many of our shareholders. And importantly it's a question we have been asking ourselves as a leadership team. It's why throughout the discussion today we've said all of our initiatives start with a view of the guest and the feedback that we have received from the guests, as we think about this new strategy.

We have focused today on five-only priorities. Not six, not seven, not 10. So five very important elements that we know we have to address to transform the company. And as we do that, it will require a cultural change. And that change is taking place, as we stand here today. We've got to make sure we're a simpler organization. We've got to rid the organization of complexity.

To execute against these plans, not only do we have to be very guest focused, but we have to be more agile, more nimble. We've got to have the right capabilities in place. We've got to create a innovative culture throughout Target. And we got to make sure we have the right capabilities and tools that underpin the strategy.

So as a leadership team, we've spent hours and hours debating these priorities. We recognized that we will not deliver this plan overnight. It's going to take us several years to build those digital capabilities; to build the capabilities that allow us to meet the needs of the guests, no matter where and when they shop; to meet their demand very differently in the future than we can today. It's exciting to talk about. It's going to take us some time to achieve that vision.

We have a very clear set of signature categories. Categories that are going to make us famous, that we're going to elevate going forward, both with the type of great content and product that Kathee showed you today, but also by enhancing the in-store experience, and the online and mobile experience.

And so we have a very clear view of the importance of Style, and Baby, and Kids and Wellness, it's not going to happen overnight. You're seeing some of those changes in store today. You'll see more later this year and it will continue to evolve into 2016. But we're focused on a very finite number of signature categories. And we can't let ourselves get distracted, as we think about the reinvention of our categories and the elevation of those signature categories.

I talked about the importance of localization, and this isn't new for anyone who has been following retail over the last few years. But we are in the very early stages of that. We're in one market today, Chicago, where we're testing localization. It's going to take us time, but we're committed to building the right capabilities, having the right tools in place to execute localization and personalization going forward.

It's one of the reasons we're so excited about having Mike McNamara join our team. Mike's been through this before at Tesco. And we can take some of the rich learning and Mike's critical experiences and apply to our business, so we can move even faster going forward.

We're excited about the early results with our urban formats. I showed you the results of City Target. We're very excited about our initial Target

Express, but we're taking a very measured approach going forward. Next year, we're going from eight City Targets to nine, by adding one new location.

We have one Target Express today. And while we're very pleased with the results, we're not opening up 50, we're opening up eight new locations, so we can test and learn along the way. So I recognize that this is going to take some time, but we have been very declarative about the priorities we're going to set, the timelines that we have in place, and we're going to test carefully and learn.

There have been a number of questions about food and food reinvention. Kathee and her team are not standing still, we're making some changes today, but it's going to take us several years to complete. And my direction to Kathee and the team, it's not how fast we go, it's making sure we make the right changes and make the right bold changes that are going to be right for the guests.

So we're going to set very clear priorities. We recognize that we have to be very disciplined about how we invest and how we execute against those initiatives. But we think we have a very clear set of priorities. We have aligned the entire organization around those priorities. And we recognized culturally, we have to make sure we change the organization, so that we can be simpler, more efficient, more effective, and really enable the organization and empower the organization to execute against those plans.

Bob Drbul

I just have three questions. John, first question, tax rate for '15 and beyond, can you just talk about the expectations this year? D&A, can you just give us a little flavor there? And then, the bigger question that I have is, on e-commerce the expectation for an acceleration 40% on top of what you just did in '14, can you just talk a little bit more about the main drivers to accelerate from where we are today on your e-commerce business?

John Mulligan

Yes, so really quick, tax rate up a little bit from where we are in 2014. So I think the tax rate in general going forward, I think mid-30s. It will bounce around that mid-30s number, 35% or so. But that's a pretty good basis for where we think we'll be here for the next several years.

D&A on a dollar basis, pretty consistent, up a little bit in 2015. We're still absorbing. We've talked about this a few times. A little bit of faster depreciation from the acceleration in our investments in technology, but on a dollar basis, not moving materially, up a little bit. And then the digital sales growth, I think there are many drivers there that are driving the 40%. And Casey can talk about this probably a little bit better than me. I'll let you jump in, Casey, if you want.

Casey Carl

From a .com perspective there is a lot of levers, as John talked about, that will fuel the growth. First and foremost, as Kathee mentioned, it's really around a lot of the great assortment and content that's going to be available on the site, and really smart assortment expansion, and those categories they really matter most to our guests.

Secondly, it's going to be around leveraging our supply chain and advancing our capabilities there, as I walk through to, again, not only leverage more stores in terms of the speed to guest, but that speed to guest also drives significant improvements in guest conversion.

And then obviously, as Jeff talked about, significant shifts again in our media mix, as we continue to shift more and more towards digital and specifically mobile, which is truly that front door for our guest. Those are just some of the critical levers that will drive the growth.

John Mulligan

The other thing I would add, the 40% isn't something that we talk about, it would be nice to do, ultimately growing that digital channel. When you look at the guest and the way they engage with us, growing that digital channel is about us maintaining relevance going forward, right. The more they engage there, the more they engage in the store. So this is about something we need to do. We need to drive guests in that channel. That's more engagement for Target overall. And ultimately, as you saw from Brian's slide, more profitability for us.

Matt McClintock

Matt McClintock talking from Barclays Capital. Just on the 29.5% gross margin target that you put out there, I just wanted to know if you could elaborate more on the investments you are making there and the confidence you believe that that's the appropriate level? Specifically on the pricing, we understand the digital mix shift.

And then, as a follow-up to Bob Drbul's question, just on e-commerce, the digital conversion rates that you're getting specific to mobile, what are you doing that is driving those conversion rates in the mobile channel? It really seems like you're leading the industry there.

John Mulligan

On the margin rate, particularly, we'll talk about pricing I guess. If you look at last year, we made significant investment in pricing, as I said, 60 basis points of promotions. We're not expecting much of that to come back this year.

Now how are we going to use that investment that we've made last year, we want to use it a little bit differently. Part of it is, as Kathee said, in bringing quality back to some of the merchandise we offer in apparel and in home. Some of it is ensuring we're priced right online, although overall we feel good about where we're pricing. But I think pricing is something we'll constantly react to and constantly balance with our product quality, and it's about delivering the value the guest wants.

So I think the 29.5% is reflective of investments we have already made. We recognized there will be more investments for us to make going forward, both in digital perhaps in pricing. But we feel like we've got a significant number of offsets to continue to allow us to invest in that like we talked about earlier today.

Brian Cornell

Kathee, you want to spend a few minutes and talk about your confidence in the margin targets we're setting for 2015 and beyond?

Kathryn Tesija

Yes, absolutely. I thought John laid it out really well. There's a lot of things that we think are going to be positive to margin, and there are some things that we think will detract from it. But all-in, we feel really confident about that number. So some of the things that we're doing that will be in our favor, we talked a lot today about signature categories, and those are all at a much higher gross margin rate.

And so as we accelerate that growth, that will enhance gross margin, and you saw that in the fourth quarter. Things like pricing that John mentioned, it's a very competitive world, as you know, and it's completely transparent today. So we need to make sure that we maintain our pricing against our key competitors and that's in-stores and online. And so we always want to maintain the ability to be able to make those adjustments and make them really quickly, so that our guest has great price for the quality at Target and that we become their top choice.

There is also a lot that we're doing on the cost of good side, in how we're negotiating for products and understanding all of the factors that go into it, what we should be paying for it and making sure that we are getting the right cost to begin with. So that will be a plus to gross margin.

And then as John said, we spent a lot on markdowns last year to really make sure that we were driving the guests back into their stores and online and reestablishing their traffic pattern, and that cost us a lot. And so we won't be taking those this year. You saw our traffic in the fourth quarter, very healthy. That's where we got most of our growth. So we have that available to us to be able to invest in price or quality or wherever we think it's necessary.

Brian Cornell

Just finishing up on pricing and clearly a very dynamic topic. Kathee has talked about the fact that these signature categories that the guest has prioritized for us happen to be some of the highest margin mix categories for us. We're also, as we think about building capabilities, investing in new capabilities to make sure we're even more surgical in pricing, and then we have even better analytics behind the pricing decisions we make.

And finally, over time as we do localize our assortment, we recognize that's going to have benefits from a gross margin standpoint. Having the right items in the right stores does lead to fewer markdowns. So those elements provide some benefits going forward. Some are going to arrive sooner than others. But overall, I think we're very comfortable with the margin targets that we've set.

Greg Melich

Hi, it's Greg Melich from Evercore ISI up here in the rafters. I have one for Brian and then a follow-up for John. Brian, basically given so much change going on in the company, how have you changed the incentive structure for the merchants and the store operators to really align them, whether it's [ph] Kimroy or whoever it was. Just tell us how that's changed and when that is affected?

And then, John, $1.5 billion out of SG&A, I think your total SG&A is roughly $15 billion. Help us understand, does that touch the stores at all or is that just out of headquarters? A little more flavor on those different buckets where they lie?

Brian Cornell

Greg, why don't I turn it back to Kathee. Let her talk about the changes we are making to ensure we have the right alignment in merchandising versus the initiatives that we're establishing.

Kathryn Tesija

Yes, Greg, so we've been talking a lot about Target over team. And as we've picked signature categories and the things that are guest has told us they want us to lean forward on, we want everybody to be incented to be able to drive that for Target. And so we are looking at a Target number, not a department number. The guest doesn't really care what department number we assign to something. They care about how we perform overall.

That we think will enable us to be able to make the right investments and have a team be really supportive about that and actually bring those ideas up to us where we ought to be able to move resources and invest in what the guest cares about. So their incentive is really focused on Target, not a department, not a classification.

And of course, we're looking at the things that we typically do like sales, as well as profit dollars. We've moved away from rate. We've talked about where we felt like we got too focused on gross margin rate in the past. We're much more concerned about the dollars than we are at rate. And, of course, return on invested capital.

So my team cooks up a lot of ideas that we think are going to be interesting to our guests, but we need to make sure that they are interesting in that they pay off at the right amount. So we're also interested in return on invested capital.

Brian Cornell

Greg, I think it's a very important topic as we think about the implementation of category roles, and Kathee walked everyone through those four different category roles we have established. Well, we have very different expectations from a growth standpoint, but each one of those roles is critically important.

They generate significant sales and importantly significant gross margin dollars. But we had recognized that depending on the category role you fit in tomorrow, you have different expectations. You might be giving up some of the circular space you had in the past. You might receive fewer end caps, but your category still has a very important role to deliver over the course of the year.

So we've really tried to make sure we're elevating Target ahead of team and getting the team to understand that we have to win as an enterprise going forward, which means there's going to be some trade-offs and there's going to be some changes, but if we execute those plans and we step forward and think about what's best for the guests, what's best for Target and our shareholders, we think we're going to make that cultural shift in a relatively short period of time.

John Mulligan

You know on expense, Greg, we took a very, very broad look. Hopefully, when you saw the pie chart, it demonstrated we looked across the entire enterprise, and I think as we looked at the stores, our thought was they've been doing this for a long time. We've asked them to improve productivity every year. We've invested behind that to ensure that they could improve productivity every year, but bringing that back to the rest of our enterprise, and that is where we are primarily focused.

We think there's great opportunity to improve productivity in our technology area and get more for what we're spending. We think there's opportunity in our supply chain. As we're forcing our supply chain to become more flexible, we have the opportunity to step back and evaluate the entirety of the supply chain, and again take out expense for things that don't really serve a purpose anymore for where we are going.

We've talked about our headquarters, getting to a more simple and nimble structure there. And it's interesting that you asked the question because you certainly know the story about Target ironing its underwear. There's a cost to doing that, and there's a cost to making sure that everything is correct to the last 15 decimal places. And so getting more nimble and being more efficient in how we do things at headquarters. So we think there's opportunity across the entirety of the business.

And I think as we think about the stores, it is really only in so far as work is being forced to them from other parts of the organization, whether it's from marketing or merchandising or from the finance team or wherever it's coming from, eliminating that work so that they can focus on serving the guest, which is what their primary focus should be.

Craig Johnson

Brian, over here. Craig Johnson, Customer Growth Partners. I'd like to drill down on the core issue of traffic of rebuilding or rebuilding of traffic. On the one hand, you all talk about having fiercely loyal customers, but apparently you are under indexing in terms of share of customers, share of the customer trip, or you are under indexing on share of trips of look-alike customers that maybe aren't in your franchise. Could you talk to us about how well you understand the dynamics of why you're underperforming there, and what you are doing to either win or win back those trips as the case may be?

Brian Cornell

Craig, as we talked about, we spent a significant amount of time really understanding our position with the guest and the consumer today. And while it's early days, from a traffic standpoint, we are already seeing really good progress. If you look at our Q4 comp results, we are up 3.8%. We talked about the fact the majority of that was driven by a traffic increase.

So we're bringing the guest back. They are coming back to us more frequently. As we go forward, we are recognizing that that guest is shopping both in-store and online, and we want to make sure it's very convenient for them to interact with the brand. So while its early days, we are already seeing traffic improve in our stores, and we're going to continue to focus on driving traffic by making sure we elevate those signature categories. Those categories, the guest has told us are most important to them, style being critically important. Categories like apparel and home and beauty.

And you had a preview of some of the work that Kathee and her team are doing, as we think about 2015. We want to excite that guest to say we need to go back to Target to see what's new, what's exciting in those categories. We recognize how important baby is and the lifetime value of that guest who comes into Target, because they're shopping for their first child. They are buying their first stroller and car seat. They are buying diapers for the first time. We want to continue to make sure we deepen our relationship with that guest and bring them back more and more often.

We know how important wellness is, and it's why we are going to continue to make sure we evolve our position in that important wellness space. But we're going to have the right product, we got to have the right content, we got to have the right newness and innovation that gives the guest a reason to shop our stores more frequently, and it's not just in-store, we want to make sure we're complementing that with a great digital and mobile experience.

So all of our efforts as you think about building out our digital capabilities, enhancing our focus on signature categories, becoming more localized and personalized, making sure we can reach the U.S. consumer that each and every week is moving back to these densely populated urban settings, that's the key to us increasing traffic and deepening that relationship.

So it's not going to happen overnight. We've got a lot of work to do, but certainly our results in Q3 and Q4 were very encouraging, and it's great to sit here today and say our comps were driven by increased traffic in our stores. But we've got to continue to delight the guest every time they shop and make sure we greet them with the great in-store experience, with exciting new product, with products that we know are on track for what our guest is looking for from Target. And you had a preview today of some of the exciting plans that we have in place for 2015 with a lot more to come over the next couple of years.

Joe Feldman

Back here guys are. Joe Feldman, Telsey Advisory Group. Wanted to ask about space allocation in the stores. Obviously, a lot of effort is being made on the merchandising side, on the marketing side to support that, but will there be changes? Will there be a contraction of the food area or keep it the same? Will there be the signature categories getting any more space? Can you share some ideas on that?

Brian Cornell

Kathee, why don't we talk about some of the changes that we are making right now? And you discussed today some of the changes we made in apparel, a preview of the changes in home. Why don't you walk them through some of the future changes that we're contemplating?

Kathryn Tesija

Yes, I think of it very much in terms of rightsizing. And so we were very clear about what each product category does, why our guests like it, what it means to them in their lives. Therefore, we've given it sort of a home in terms of outperform or perform. So everybody in the organization understands what it does and what our guest thinks about it.

And then as we look at each of those, we are what I refer to as rightsizing, and that might be rightsizing the investment, it might be rightsizing the space. I think Brian mentioned it might be things like less or more circular space, less or more end cap space, all to get the category right based on what the guest wants.

So will there be changes, certainly. We're in the early stages of figuring out what that is. I think some of the reinventions in store you've seen that probably the clearest, where as we roll out a new presentation, we get that rightsizing sort of taken care of.

Online, we are also rightsizing our assortment there. Adding in the signature categories where it is most meaningful to our guests and making sure that we have the breadth of assortment and aesthetic that's important to them.

Brian Cornell

So we'll continue to look at how we rightsize those categories, but equally important, how we utilize the existing space to make sure it's more inspirational, it's more impactful, it features some of the great new items we have in store. But that's going to be something that we're going to look at very carefully. We're going to test and learn before we roll too aggressively.

We are very excited, and many of you have been up to Minneapolis and have seen the new home section that we've created in one of our stores in Stinson. We are very excited about it. We are carefully expanding. We're not moving into hundreds of stores, we are taking a very measured approach to make sure we test, we learn, we get it right. And when we get it right, we'll move aggressively. But it's going to be an iterative process, and the guest is going to guide us through that journey.

Stacie Rabinowitz

Stacie Rabinowitz, Consumer Edge Research. I actually had two. The first one was two questions ago when you were talking about driving traffic. A lot of what you were talking about sounded like engaging deeper with the existing guests and generating more trips, larger basket. As you think about the next few years, how much are you thinking about the existing guests and getting them to engage deeper with Target versus new customers or customers who have deserted you over the past couple of years?

And then my second question was actually on the style categories. Today it seems like you're talking about them very broadly and very cohesively? And the new food strategy almost seems like food is becoming a bit of a style category too. What changes are you making on the backend, and at Target Corporate, or making or not making I guess to think about style and helping those different categories and departments work together to be on trend?

Brian Cornell

Jeff, do you want to spend a few minutes and talk about style and the approach we are taking to style? And Kathee, I'm sure can jump in and provide some additional fodder.

Jeffrey Jones

So first on traffic and your point, I think we have absolutely an opportunity to win back lapsed guests. And many of the things that we are talking about are the reasons why they left. And so clearly, with 25 million people a week to the store and 15 million a week online, there are a lot, but there are those that have left us for the reasons we are addressing. So I think win back is a really important part of strategy.

In style, in general, you think about apparel, you think about home, you think about beauty. The way the guest shops is they do think holistically about those categories as a reflection of themselves. So it's very intentional, and you're picking up on that intentionality and constantly being available for her for inspiration. That's why there's so much work being done in the digital channels where that line that Kathee mentioned is blurring all the time.

We hear from guests regularly that they receive an email, they buy something and they didn't even realize they were shopping. That's just become the dynamic. And so being present in social, being present on her handset, all of those are ways that we can help her come back to Target by being inspired, so a few thoughts.

Brian Cornell

And going back to the traffic question, I think we've been very upfront throughout our discussion today that during the recession, we really decoupled our brand promise of Expect More, Pay Less. As we bring that brand promise back together and really elevate the signature categories, we certainly want to win back some of those guests that we disappointed during that period of time.

But we also recognize we're going to be appealing to a broader group of new consumers, and we talked about the work that was done really started from an outside in perspective. It started with the broader consumer and the broader shopper base. And we recognized that as we stand here today and as we go forward into the future, our guest is going to increasingly be a Hispanic shopper. And we want to make sure we are taking that Hispanic consumer and converting them into future Target guests. So they play a very important role.

So we certainly want to make sure we're winning back the trust of our existing Target guests, but as we think about our plans both from a marketing standpoint, from a mobile standpoint, from a product standpoint, we certainly want to appeal to new consumers, and we certainly hope that our existing guests become our best advocates to allow us to acquire new shoppers as they talk to friends, as they talk to family about the outstanding experience they had when they were shopping in our stores or interacting with us online.

So we certainly recognize that existing Target guest has to be our best advocate. They've got to be talking to their friends, they've got to be talking to their family about the great experience that they had, how they saw for themselves Expect More, Pay Less come to life when they were shopping our stores or shopping online. But we clearly want to make sure we are meeting the needs of today's guests, while we attract new consumers to our Target formats.

We've got time for it looks like one more question. So I know a few hands have been up for a while -- double waving in the back. That looks like a winner back there.

Michael Lasser

It's Michael Lasser from UBS. You targeting $1.5 billion to take out of your cost structure, how do you minimize the friction or potential distraction that the organization is going to seek, because inevitably some of that's going to come from labor? And as part of that question, can you address the need to reinvest labor back into the stores as you demand more from them?

Brian Cornell

Let me start with the first part of that question. And as a leadership team, we have been very transparent about the strategy that we put in place. We've really tried to make sure we galvanize that strategy across the organization. We match up priorities against those strategies, the resources and capabilities that we're going to put in place to make sure we can execute that strategy. But we've also been very clear about the things we are going to stop doing, and how we're going to redirect the organization and work very differently.

So we recognize that we are talking about significant cultural change, but it's driven by an understanding of what the consumer and the guest is looking for from Target. We've set very clear priorities. We're going to make sure that we organize and design our focus around delivering those key priorities, and we are going to make sure we are very open and clear in how we build and structure the capabilities to execute against these plans.

So we recognize it is a time of significant change and transformation at Target. But as a leadership team, we are committed to that change. We think we actually have the right guest-focused strategies in place. We know it's going to take time, but we are going to make sure that we are very clear about the path that we are going to build to get there.

It's why we've asked Casey in addition to his role of leading innovation and strategy at Target to lead our transformational office. To make sure we're very clear about the changes that are in front of us, we bring the organization along on this journey. We are very clear about the changes that we are making and how we're going to implement those changes, but we are putting dedicated leadership behind the transformation of the company, both in how we work and how we begin to really shape the future of this great organization. So not something that we've taken lightly. We've put tremendous time behind it, and we recognize that we have to have the right leadership every single day guiding us through this significant transformation.

John Mulligan

You know on the hours, I think that's an outstanding question, when you look at the home reinvention, that's going to require extra time for the stores to make sure that's set appropriately all day long as guests shop that area. So one of the things like Brian said, one of the reasons we're easing into that is to make sure we understand the requirements of the store and are adding back the appropriate hours. That's part of the reinvestment in the business. And there will be other areas as we reinvent the store that may require additional hours.

We want to be thoughtful about that and test into it. It's not just the sales results that are important. It's making sure we can execute on what we are putting out there. So it is about all of this. Reducing expense is one thing to talk about, but there's reinvestment that goes along with that. And if you look at our EBITDA rates, that's absolutely the expectation we have set for ourselves and for the organization.

Brian Cornell

Just to build on John's point and as we've looked at some of those changes in store, whether its changes we're making in apparel, changes we're making in home, the one question we have asked the team is, can we sustain that? Can we make sure that 52 weeks a year as we make these changes can we sustain it for the guests?

So to do that, we've got to make sure we have the right approach, the right routines, the right hours in place to make sure that it's not something that you see one time and it drifts away. It's something that we can sustain day after day and year after year. So it's a very important screen and filter we've put in place.

End of Q&A

Brian Cornell

Well, as we wrap up today, we certainly appreciate your time. Hopefully, we've got a chance to walk you through our plans for the future. I hope you walk away recognizing that we've really put the guest in the forefront of our vision. And we have got very clear plans and priorities in place that we will update you on each and every quarter as we continue to transform and create the Target of the future. So thanks for joining us today. Travel safely, and we look forward to seeing you next year. So thank you.