

And I want to start by thanking all of you for being here today. I've seen that video a dozen times now. It's pure joy, it's pure Target. And that's why I've never been more excited to be part of this brand, and to lead this great company, that I am right now.

This morning, we announced our most successful year-over-year performance in well over a decade. Our comps sales surged this holiday season, fuelled by unprecedented traffic gains, especially in our stores.

We closed out Q4 with a 5.3% comp, our strongest finish since 2004, putting Target right in the center of the winner's circle. Across the business, we're growing market share in every major category and our guests love what they see.

Our team deserves all the credit. They are more passionate and committed than ever. They are delivering on our purpose, which is helping every family we serve, find joy in all of life's everyday moments.

So while I'm here on stage, holding up some of our strongest results in a generation. This performance isn't simply a reflection of a strong consumer environment. These results were years in the making. Proof of the progress we've achieved against our multi-year strategy, to transform our company, deliver strong, consistent and durable growth, and emerge as one of the industry leading retailers for years to come.

Back in 2017, we laid out an ambitious investment agenda, to reimagine our stores, reinvent our supply chain and fulfillment capabilities to reposition our own brand portfolio, invest in our team. And I think, we can all agree at that time, the plan was not met with universal applause.

I won't name names, but a few of you might have pulled me aside and said, Brian, are you sure this is the path you want to pursue? Do you really want to bet the company on stores? At that time, people were closing stores, not opening them. They were cutting costs, not investing in their teams, but we've never been a brand that falls in line with the crowd. Our guests aren't looking for a Red and Khaki version of someone else. They expect us to be different. They expect us to innovate, and inspire. They expect us to be Target.

So with our guest as our guide, we kept our stores and our people at the center of our strategy, but committed to deploy them in a radically different way. Two years later, we've redefined what it means to be welcoming, inspiring and rewarding and retail.

Our teams are obsessed with finding new ways to make our guest lives just a little easier. When you look at the results, and pick your metric. Traffic,

comps, net promoter scores guest surveys, it's clear, our strategy is working. We're delivering the right outcomes, and folks are taking notice, take a look.

[Video Presentation]

I'm really proud of that work, and I'm really proud of our team. 350,000 people who get up each day, dedicated to making those moments happen for our guests, all across this country. Yet as much of them are encouraged by our success, I'm always the first to say, we still have a lot of work left to do. You know this better than anyone.

As a shakeout in our industry continues, the separation between those who can afford to invest, and those who can't is real. The channel convergence between physical and digital has come full circle. And today Target is leading the way. While we might be ahead of the pack now, this is no time to slow down, and I can promise you, we won't.

As we look to the future, I think it's important to take a moment to step back and look at where we started, so think back to this meeting in 2016. Just three years ago, we were over Chelsea Piers. I remembered it, it was a beautiful day. And I started with an anecdote that was well at the time an aspiration. I talked about how someday, not long in the future, a mom, who works here in New York City, would be able to plan a birthday party, right from her office.

Shop for everything from her phone, from the train, and then pickup her order before shuttling her kids off to swimming lessons. The punch line was that in the future, the whole thing would go off without a hitch.

Fast forward to today. We've let that used case down cold [ph]. We got there, because we spent 2016 showing up the fundamentals. 2017 was about laying out an investment agenda, and developing new capabilities. 2018 was all about acceleration, and innovation, so that in 2019 we can drive adoption, and scale.

Today, that same mom in the city has a multitude of choices, and the shopping experience has never been easier or more convenient. For starters, she could just make that Target run on her lunch hour. Three years ago, we didn't have one single store in Manhattan south of the park.

Today, we have four. And we've opened up eight more across other burrows, and in Long Island. If she doesn't want to schlep [ph] the bags back to her office, we'll keep them and drop them off at her desk before she leaves for the day. We'll drive up, she can keep the kids buckled up in their car seats. We'll put that order in her trunk at the closest store to her home.

And what's shipped she can order same day, and will have everything she wants on her kitchen table within an hour or two. Her shopper will even text her before checkout, see if she wants or needs a few extra candles for the cake. Whatever she wants, today we've got her covered.

In fact, as we enter the next year or a transformational strategy, we're doing so with the most comprehensive suite of fulfillment choices and those extensive coast-to-coast network of any retailer in the industry.

Today, Target is hands down America's easiest place to shop. But ease, reach and convenience are only one part of the equation. Our teams are also making process improvements, to take cost out of every single transaction. They're improving speed through greater efficiency, and maximizing our last mile advantages.

What used to take days is now measured in hours. Costs that were once measured in dollars, can now be measured in cents. So we're focused on driving awareness, and adoption, and helping the guests build these options into their weekly routines. And that's just one example of success in one aspect of our strategy. But what's even more important is that every piece of our strategy is working and it's working together.

Let's start with stores. During the last two years, our property enrolment teams remodeled more than 400 stores, outfitting them with new technology, fixtures, design, totally transforming how they look, feel, and function.

This year, we'll remodel at least 300 more and another 300 more and another 300 in 2020, while continuing to add to our network. Today, we have almost 100 small format stores, and they are highly productive.

Herald Square, just down 6th Avenue, does more sales per square foot than any other store of any size in the company. And we'll continue opening a couple dozen news format stores each year, in cities and on college campuses across the country.

Now of course, as you look at that map, you don't see a big red and white W hovering over Wisconsin, yet I can assure you, John Mulligan and John Hulbert that you know all too well are the two biggest major fans at Target and they are all over this.

This year, we also undertook our most ambitious redesign of how we operate store ever. We're investing in technology, to strengthen, execution and maximize efficiencies in the back of the house. So our teams can shift their focus to driving guests facing service.

We're also making industry leading investments in wage committed to raising our starting wage to \$15 an hour by 2020. Now not only does this move further burnished Target's reputation as a top destination for great talent. It's sends a clear message that we value our communities.

At a recent U.S. Conference of Mayors in Washington, there were a long line of city leaders eager to roll out the welcome mat to Target, because a commitment like this shows, we'll be good neighbors in every single community we serve. Our digital progress continues to be a stand out story.

Once again, our digital sales this holiday season grew much faster than the industry and we finished the quarter up 31%. Now it wasn't longer though that digital was a rounding here, when it came to overall revenue at Target.

In 2012, back in just 2012 our digital sales were just over \$1 billion. Today, digital is delivering more than \$5 billion in sales and still growing, in fact, this was the fifth year in a row that our comp growth topped at least 25%.

And as John will show you in detail, digital growth Target isn't coming at the expense of our stores. It's making stores more relevant because as I said at the top, the convergence between physical and digital, well it's closer than ever at Target, and that's because we invested to build industry leading digital and technology teams. They've created a seamless and inspired user experience that's worthy of our Target brand.

We've invested in infrastructure to support greater scale and speed and strengthen our core and we've invested in building enterprise data and analytical capabilities, to better understand our guests and make smarter decisions.

Today, our engineers are using voice AR, AI, VR to provide greater utility for our guests and integrate richer shopping experiences into their busy lives. And now that we've established the right foundation, we're able to move to the next phase of our journey.

Our team is now building out an even more holistic digital strategy that reaches deeper levels of personalization and engagement across every guest facing part of our ecosystem. Personalization and engagement are also the cornerstones of our evolving loyalty strategy.

As you well know, Red Card and Cartwheel work really hard for Target. Yes, we use these programs, shop more often that our average guest, but they're also geared to our most engaged guests. So building out our loyalty strategy, we saw the opportunity to tap into a full range of shopper types, folks who visit us each week and knows who might only show up once a year.

Last month, we announced the expansion of our new program, Target circle. After testing in Dallas, we're now rolling out to five new markets. This program rewards guests with a 1% rebate. It allows our guests to direct their philanthropic giving and offers special offers tied to key life moments. The largest benefit is that it's yes, opt in over time, we can better understand how they prefer to shop and serve them with more meaningful offers.

Now, if you look back on the headlines over the last two years. One of the biggest news generators for Target was our plan to reinvent our own brand portfolio.

We said, we deliver more than a dozen new brands in 18 months and true to form, our team over delivered by a mile. We've introduced more than 20 new brands and our teams are still growing strong. Fast Company just put Target near the top of the list of the world's most innovative companies, specifically through this body of work.

A few days later, we unveil three new brands as part of our full reinvention of our sleepwear and intimates business. To top it off, we created a mountain of buzz with our latest partnership with Vineyard Vines and the guest response has been phenomenal, but introducing new brands month after month is not the goal. We're focused on growing market share, attracting new guest segments and finding white space opportunities in our portfolio.

So let's take Home for example. Threshold by every measure has performed extremely well since we introduced it back in 2013. But instead of stretching threshold to appeal to a broader array of guest taste, to drive growth in the category, we took a different path. We launched four new brands, Opalhouse, Project 62, Made By Design and Hearth & Hand with Chip and Joanna Gaines, which attracted more guests with different style needs and help drive the most successful year-over-year comp growth, we've seen in Home in well over a decade.

With TRU and BRU's exit, we saw an obvious opportunity to pick up market share, and our teams aggressively chase the business making big bets on Toys and Babies.

We finished 2018 with huge market share gains in each, those guests are also looking for Target for inspiration and innovation in places like Apparel and Essentials. So, we recently launched new lines in Art Class and Cloud Island and that's just start.

In the months ahead, you could expect to see a steady stream of newness and exclusivity across the assortment. New brand launches, new

partnerships and a sharper focus on developing best-in-class brand management expertise across every category.

Finally, well it sounds like we're pleased with the progress we've made in our priorities. We know better than anyone. We can't take our eye off the ball, not even for a second, when it comes to the pursuit of flawless execution on the fundamentals.

Over the last few years we reset our pricing and promo strategy and we'll continue to fine tune it. And in 2018, we sort of dedicated teams to tackle persistent challenges in our business, like [Indiscernible] zone merchandise transitions and in store signage.

On a store by store basis, we must ensure we're spending payroll and things that add value for our guests. Because when you multiply by 1800, we're talking about huge opportunity to take cost out and move with greater speed and efficiency.

One of the biggest changes in our operating model is in Food and Beverage, where we decided to bring the full spectrum of merchandising and operations functions in a one team.

Over the last several years, we've made great strides ensuring up our operating challenges, elevating the experience and building more specialized expertise. As a result, we've seen six quarters of positive comps in Food and Beverage which translated in a market share gains in 2018.

Generally that momentum we believe bringing our Food and Beverage, supply chain, operations, merchandising teams under the leadership of Stephanie Lundquist will help us move faster and farther and consistently deliver more value for our guests.

So given all this progress, it's clear our strategy is working. We've built a successful durable model and I'm confident we are well positioned to continue to deliver strong sales and traffic growth in 2019 and for many years to come.

You saw that our guidance this morning, low to mid-single digit comps driven by increased traffic and continued market share gains, but I also know exactly what you're thinking. Brian, at what cost are we counting empty calories or is there going to be more money in the bank.

So I'll head this off straight away, that way you don't have to pull me aside after our presentations this morning.

You want to know how we plan to continue to grow, scale and accelerate our investment agenda and deliver profitable growth and strong returns on invested capital. We said this morning to expect high single-digit growth in EPS. You want to know how we get there and that's exactly what we want to answer for you today.

In a moment, I'll turn it over to Cathy Smith, who will take you through our financial model and how we are prepared for the next phase of our strategy. How will continue to generate strong cash flow and ROIC that will fuel our performance in the years ahead.

Then John Mulligan will share how we build on this momentum. I will keep scaling our strategy, innovating across every aspect of our supply chain and elevating our service model.

He'll talk about how we're incentivizing greater adoption of our services and fulfillment choices. How we're driving demand, how we're getting smarter, more savvy and more efficient on the backend and that will strengthen profitability and grow operating income.

Then I'll come back and offer guidance on our financial performance and expectations for the future.

And with that, I'll turn it over to Cathy Smith.

### **Cathy Smith**

Thanks, Brian. One of the great things about working in retail is that every day, 365 days a year we get a new report card from our guests. Most of the time this real-time feedback, lets us know that things are working as planned.

In contrast, two years ago, those report card were clearly showing that we needed to change and based on last year's strong performance this latest report card shows that we've been successful.

But it's worth taking a look back to see just how far we've come. Here are a couple of the charts I showed you in this same room two years ago. These two annual report cards clearly showed the reversal in our performance between 2015 and 2016.

With that feedback, we took a hard look at ourselves and how we fit into the retail industry, including our strengths and points of differentiation. We did an in-depth assessment of how consumers are evolving and shopping differently. That we are confirmed, we were already focusing on the right priorities, but we weren't moving fast enough.

The greatest hockey player ever, Wayne Gretzky, referred to this as skating to where the puck is going. We were headed in the right direction, but our guests were moving faster.

Fortunately, we had the resources we needed to accelerate, strong operations and well located stores, a fiercely loyal base of guest, robust cash flow and a strong balance sheet and the best team in retail.

So here in this room, two years ago we laid out a bold new plan. We committed to make additional investments of both capital and operating margin to help Target deliver more for our guests faster. These investments were focused on delivering and ever improving guest experience, not just for today but for many years to come.

More than a 1000 store remodels by the end of 2020, new technology to make shopping easier for our guests and more productive for our team. A new supply chain model designed to support an unmatched suite of digital fulfillment options, and to take labor out of the store backrooms.

More than a dozen new owned and exclusive brands, simpler pricing and promotions, with a focus on being priced right daily and importantly, our renewed commitment to our team, including new training, additional hours and meaningful wage increases.

All of these investments were developed through a guest lens. We focused first on the things they already love about Target, like our shopping experience. Our brands and our team, and we asked ourselves if we could do more, that was just the start.

We also committed to becoming the easiest place to shop in America, because as much as our guests continue to love us, we knew, we lose relevance and trips if we didn't make shopping at Target fast and easy. Our multi-year plan was focused on building a durable positioned to thrive in an omnichannel world.

2017 would be an investment year, marked by a step up in CapEx and step down in an operating profits.

In 2018, the year just ended, would be a year of transition, when financial metrics would begin to stabilize, positioning Target for long-term profitable growth. How do things turn out?

Even though we have planned for a transition year, last year turned out to be one of the most productive in our history. As our business generated, the strongest traffic and sales growth and well over a decade, this growth is even more meaningful when you realize that over the last 10 years, our



average store age has nearly doubled and yet, last year we delivered the strongest growth in that entire 10 year period.

The lesson is simple, the age of the stores doesn't matter as long as they're well located and you invest to keep them fresh and relevant.

On the bottom line, last year's adjusted EPS of \$5.39 established a new all-time record for the company, driven by strong comp sales, operating margins that began, operating metrics that began to stabilize and at the benefits of a lower tax rate.

Between the top line and bottom lines let's look back at a few other details of our 2018 performance. Last year's gross margin rate was down about 40 basis points and half of this decline was driven by sales mix.

Even though we saw historically strong sales in our higher margin, Home, Apparel and Beauty categories, we also saw exceptionally strong growth in lower margin categories like Baby and toys.

Beyond the mix, the remainder of last year's gross margin rate decline, reflected the price investments we made throughout 2017 along with the cost of rapid unit growth in digital fulfillment.

As you will hear, later from John, these days we're seeing the most rapid growth in the lower cost fulfillment options, which we began to scale up last year and this year, we're focused on driving efficiencies that will further reduce the unit cost of digital fulfillment.

Last year's SG&A expense rate of 20.9% was about 10 basis points higher than in 2017. This performance reflected the carryover of investments in hours and training we made throughout 2017 combined with continued pressure from wage growth.

Among the offsets, our SG&A rate benefited from disciplined management of expenses throughout the organization and the natural leverage benefit of strong comp sales growth. On the D&A expense lines, dollars were approximately flat last year, resulting in about 10 basis points of rate leverage.

This performance was better than expected and driven by our careful work of our team to optimize the scope of our remodel projects. As a result, accelerated depreciation was lower than expected last year even as we continue to see a 2% to 4% sales lift in our remodeled stores.

Below the operating income line, interest expense was down about \$200 million last year, reflecting both the one-time and ongoing impacts of our

2017 debt retirement and refinancing activities. In addition, like virtually all businesses in the U.S., we benefited from a lower federal tax rate.

And finally last year's EPS reflected a 3.1% reduction in average shares outstanding, driven by our continued disciplined approach to capital deployment. This approach has been consistent at Target for decades.

First, we invest fully in opportunities that meet our strategic and financial criteria. We then support our dividend and look to grow it annually, something we've accomplished every year since 1971 and finally we return any excess cash beyond those first two priorities through share repurchase within the limits of our middle A credit ratings.

Let's review how our capital deployment priorities have played out over the last couple of years. During that time, our business has generated nearly \$13 billion of cash from operations, with this cash along with some overseas cash we repatriated following tax reform, we funded CapEx of \$6 billion, dividends of \$2.7 billion and share repurchases of \$3.2 billion.

In addition in 2017, we have invested more than \$500 million in acquisitions primarily for Shipt and reduced our long-term debt portfolio by about \$1 billion. We also funded a \$900 million increase in last year's ending inventory position. This investment is intended to support strong sales growth, including a continued outsized opportunity in Toys and Baby.

Beyond the sales line, last year's inventory investment supported better in stocks, which ended the year in the best position since we've been measuring them.

So now, I want to talk -- I want to turn to after-tax ROIC, which measures are profitable -- our performance in terms of profitability and the capital required to generate that profit.

Targets after-tax ROIC for the last three years and -- as we're showing you are here and you can see that we perform really well on this metric, but I also want to show what these numbers would have been without discrete benefits resulting from Federal tax reform.

With that additional context, it's really clear that our plan is working. After a temporary decline in 2017, driven by our higher investments in capital and operating margin, we saw a remarkable recovery in 2018 and given our momentum we are positioned to improve on this, already strong performance in 2019 and in the years to come.

One final note regarding 2018, when you're reviewing our financial results keep in mind that the fourth quarter of 2017 included an extra week, one in which we generated about \$1.2 billion in profitable sales.

So when you review our fourth quarter results, you will see on the surface that both the sales and the operating income were essentially flat to the prior year. However, on an apples-to-apples basis last year's fourth quarter and full-year performance was much stronger on both metrics.

An important fact that might not be obvious from a quick scan of those financial statements. I'd like to finish my remarks by talking further about what a durable model should look like, one that will allow Target to thrive in this new and dynamic retail environment.

At the high level the goals are straightforward, the business model has to deliver continued relevance with consumers and sustainable long-term growth and the financial model needs to deliver outstanding returns on the capital we've invested on behalf of our shareholders.

On the top line, based on the capabilities we've built at Target, over the last couple of years, our business is positioned to deliver growth at or above the growth rate of the addressable market in the U.S. And based on the size and breadth of our category offering we think nominal GDP growth is a solid benchmark for the addressable market.

More specifically, in a typical year for GDP growth target is positioned to grow total sales in the low single digit range or better, driven by comp sales growth combined with the contribution from new stores.

And of course, like you saw last year, we are positioned to grow even faster in the phase of unique opportunities like the Toys "R" Us liquidation. As you'll recall in this meeting two years ago, we pointed out that many of our competitor stores would likely be closing, that has certainly played out as expected and it looks like the trend will continue. The reason is simple.

In today's retail environment, those who have the resources to evolve or being those who don't have the resources to evolve or being left behind by their customers. And unfortunately for them, that often means they need to close some or all of their doors. That is why two years ago, we explained why it's so important for Target to invest in fresh, vibrant stores places where our guests can find fun, inspiration and genuine human interaction.

The lesson of the last two years isn't that stores are being left behind, but the consumers have the freedom to choose only the best experiences like a Target run. On the operating income line, our business delivered a 5.5%

rate last year. This will serve as a good benchmark for the years to come, given the strong foundation, we've built.

Specifically, we believe, we have reached a point in which the operating margin rate, headwinds and tailwinds will generally balance. In terms of the tailwinds, we expect to see a benefit from strong sales mix in our higher margin categories, continued cost of goods savings through collaboration with our owned and national brand vendors. Moderation in unit fulfillment costs, as John will discuss in a few minutes.

Labor savings from our work to change our store replenishment. Overall expense discipline, across the enterprise and the leverage benefit of continued strong top line growth. We expect the aggregate benefit from these tailwinds will enable us to offset continued cost pressures on both the gross margin and the SG&A lines. Most notably driven by the growth of our digital fulfillment and continued wage increases.

On the D&A line, we expect to see some moderate rate leverage in the years ahead. This is because last year we have reached a run rate of about 300 remodels a year, which we expect to maintain through 2020. This will allow our D&A dollars to remain roughly flat as well resulting in about 10 basis points of annual D&A leverage -- D&A rate leverage.

When you put this all together, relative stability in the net of our gross margin and SG&A rates and about 10 basis points of annual D&A leverage, we are positioned to deliver about 10 basis points of operating income rate leverage per year as well.

On the income tax line, based on the current rates we are facing at both the federal and state levels, we expect our annual effective tax rate will be in the 23% to 24% range, beginning in 2019.

Regarding capital deployment, we expect to have ample capacity to maintain CapEx at about \$3.5 billion over the next couple of years, deliver low single-digit growth in our annual dividend per share and return excess cash through share repurchases, while maintaining our middle A credit rating.

Based on the expected share count reductions from those repurchases, earnings per share will grow faster than operating income. These financial model -- these financial benchmarks for our new business model are reasonable and achievable over time.

In fact, as I look back to 2018, our full year adjusted EPS of \$5.39 was near to top end of our initial guidance range, that performance reflected several lines of our P&L that weren't notably different from our expectations at the beginning of the year.

On the top line, our business delivered comp sales growth of 5% stronger than our expectation of low single-digit growth. The primary driver of this upside was Toys, in Toys & Baby, where we captured greater market share than we had planned. This outsized growth in Toys & Baby created unexpected mix pressure on our gross margin rate, causing it to be lower than our initial expectations.

And finally, as I mentioned, D&A expense was lower than expected, given our teams work to optimize the remodel program.

Altogether, our business delivered strong growth, market share gains and EPS near the high end of our expectations. This is the mark of a durable model, one that can respond to unexpected events and still deliver on both the top line and the bottom line.

So, while our journey to refine this new business model is ongoing. I hope you will agree that last year served as a meaningful way point, and as Brian said, we're the first to say, we have a lot more to do, but I hope it's also clear, that we feel really good about our momentum.

Many of you were here in this room with us two years ago, as we talked about this journey for the first time. At that time, it might have been seemed hard to imagine that Target would ever deliver the kind of growth we saw this last year.

So today we want to thank you for sticking with us on this journey. And as we look ahead, we hope you will continue with us, as we embark on another promising year of profitable growth. Thank you.

## **John Mulligan**

Good morning, everyone. Two years ago in this room, we laid out the major investments we're making in our business, including users in our stores is fulfillment hubs to get closer to the guests.

Last year in Minneapolis, we showed you the prototype for how those ideas were taking shape and we told you we are making Target the easiest place to shop. Today, I get to show you how we've done that and how the investments you've heard about have become very real, from the way we've remodeling our stores, and how we pick pack ship and deliver out to their doors.

It all starts with our store teams and the expertise and talent they have that brings new services and experiences to life for guests and its supported by our supply chain efforts, that ease the operational workload in our stores.

I'll talk more about those in detail, but, I'm going to start with our fulfillment capabilities, because for our guests, that's what is really stood out this year.

We scaled Shipt to nearly 1500 stores in more than 200 markets in a matter of months, expanded Drive-Up generally 1,000 stores coast-to-coast and are delivering hundreds or thousands of items in two days or less. You all know that operations presentations don't start with a fancy highlights reel and for years, our work was largely behind the scenes, and it's obvious why engineered processes and algorithms don't ever make the marketing cut, but for the past year after launching, both launching and expanding our fulfillment services and seeing guest's excitement for them, we've got a whole lot more sizzle to show. So, here's a look at all the ways, guests can get the Target run done.

[Video Presentation]

For most of Target's history guests have had one way to shop. They came into the store, walk through the aisle and essentially pick their own order and drive it home. In late 1990s, when we had an online business we began shipping orders directly to the guest. At that time, that was a new and radical concept for Target, but today, it's a relatively mature fulfillment method for just about any retailer. Then about five years ago we began offering in-store Pickup.

This started to change the game from the two extremes of guest shopping only in-stores and Target shipping only from warehouse. Guests like placing order online and picking it up, not far from that home that same day. Since then we've quickly grown the options we offer our guests. They want it next day, same day in their car or at the door; we have a way to deliver. Whether it's same-day delivery shop by Shipt or newer service Drive-Up. Placing an order and waiting for Shipt is something consumers already know how to do, but having an order popped in your trunk, just an hour after you order it, it is a pretty new concept.

As Drive-Up expands we're helping guest experience a whole new kind of convenience. Take a look at how Drive-Up is making the Target run easier than ever.

[Video Presentation]

We may close to 2 million of those parking lot deliveries last year, nearly all of them took less than two minutes, many even less than one minute from park card to product hand-off, guests love it. The net promoter score repeat rates for Drive-Up are extremely high and they tell us it's easier and more convenient than having a box dropped on their step.

Here's a look at an actual email. We got from a guest on a cold night in January and no, it wasn't during the week that was 30 below zero at Minneapolis. It was just a regular night for a mom who didn't have much time, should be meaning to try the service and finally did in less than two minutes in her parking lot she saw how Target really understood what she needed. That's just one email, but it speaks to what we hear from guests whenever we enter a market.

In fact in Minneapolis, the first market to have the service. We've seen it grow more than seven fold, year-over-year. With that excitement and fast adoption in just one market. We expect to see a lot of growth in Drive-Up across the country. As we continue to expand to most of the chain. Each of our fulfillment options satisfies a different need, it serves a different kind of shopping churn. As guests are learning about these services and experiencing how conveniently we are, they're choosing them more often.

For example, we're seeing guests choose Pickup instead of shipping and we expect demand for our newer service to continue growing the fastest. Now what if I told you, we can offer all those services in a way that makes us faster, lowers our costs and leverages existing assets to drive higher productivity in ROIC. Most of you would be pretty interested, right?

That's the foundation of our stores as hubs strategy. Using our more than 1,800 stores in neighborhoods across the country to handle online orders not far from the guest who bought them. Many retailers are just starting to talk about this concept, but we've been doing it. A few years ago, when other set stores didn't matter, we doubled down on ours. We shared our plans to use them for both in-store experiences and digital fulfillment, and because of the investments we've made to put our stores at the center, Target has a delivery option to meet just about any guess need for speed and to make shopping even easier.

Understanding how our stores make us faster is simple. They are already in city neighborhoods just miles from our guest doorsteps. So we can ship online orders at least a full day faster than we can ship from an upstream fulfillment center and we can deliver same-day orders within hours.

Managing our fulfillment cost is much more complex. We do this in several ways. First, we reduced the distance of delivery and fulfill orders in stores where we already carry the items, our guests want most just miles from their homes. It's why we're shipping millions of orders off the back of 1400 local stores, which is more than 40% cheaper per unit on average than upstream shipping, and we offer convenient services like order Pickup and Drive-Up which cost nearly 90% less on average and fulfilling from a warehouse.

We also manage the cost by offering different fulfillment models that add revenue and control costs. For next day delivery of essentials guests pay \$2.99, to fill a box with items like cereals, dish soap and paper towels. And we ship from local stores which lowers the cost of delivery.

Delivery from store is similar, cash up the store and pay \$7 to have their purchases delivered home. These orders tend to be five times higher than the average Target basket and full of higher margin categories like home. And the crowd sourcing technology we acquired with Grand Junction a few years ago matches our orders with local couriers who can hit our delivery promise most efficiently.

And their Shipt, a same day Shipt -- shopping and delivery service, we acquired last year, rolled out to all major markets. For \$99 a year, guests can place an order through Shipt and have it delivered in an hour or two. Shipt earns additional revenue from that annual fee and its 80,000 shoppers across the country are shopping for a growing number of retailers on its marketplace.

Finally, we find efficiency in our operations to lower overall cost of fulfillment. When we first launched order Pickup in 2013, we were literally working from a folding table setup in the backroom. It took us a number of years and lots of technology and process improvements to go from scrappy to smooth. When we had our Pickup down [Indiscernible] we took it to the parking lot, giving our guests the convenience of swing it by the local store without even getting out of the car.

You saw how Drive-Up works and the technology and processes that we've built for our team to move faster and spend less time per order. Across the board, we've put some serious technology equipment and automation behind our delivery methods to make us faster and more efficient. This operation could be anywhere, a warehouse in Phoenix, Colorado or Virginia. But it's a local store in Minnesota, doing the work of our fulfillment center just behind the sales floor.

With these kinds of investments in every delivery method, we lowered our average unit cost of fulfillment by 20%, driven by our fastest growing fulfillment methods by Shipt from store and Drive-Up.

By fulfilling closer to the store shelf, adding new delivery options and optimizing our operations. We saved hundreds of millions of dollars in fulfillment costs in 2018. Today's shipping is what guests know best, but our newer delivery services like Drive-Up that have lower costs and are more profitable are growing the fastest because once guests try them they love them.



Of course, the P&L is only part of the financial store. Using our stores as hubs has allowed us to keep up with the incredible growth we're seeing in our digital businesses. In the past two years, guest bought twice as many units from Target.com and all of that growth was fielded by stores. Buildings we already own and we're in the lights that already on.

Our stores have Shipt four times the number of items out there back doors and they managed triple the demand for store Pickup services. This year during our fourth quarter, stores fulfilled nearly three of every four orders, effectively doing the work of 14 fulfillment centers, that means we didn't have to spend nearly \$3 billion on new warehouses over the past few years, to accommodate that growth, and with our store replenishment efforts that enables stores to fulfill a growing number of digital orders will continue to have capacity over the next few years.

Not some of you would call that capital avoidance but as you've seen in the investments we're making across our operations. We're not avoiding investing capital where it's productive. Using our stores to do the work of additional warehouses at the most efficient way to deploy our resources. It's also important to note that while our stores are fulfilling more digital orders it's not coming at the cost of in-store sales.

Since 2016, we've made our stores more productive by using them as fulfillment centers. Our fulfillment sales per square foot have grown at an average 67% rate per year. Now more than \$14 a foot, as our stores increasingly support our digital business. At the same time, our in-store sales per square foot have gone on a 4% rate per year which means our Target stores can support incremental growth from Target.com without hurting in-store sales.

So our in-store -- our stores as hubs strategy isn't putting our core business at risk. It's simply helping us grow faster. While fulfillment refers to digital orders to guest, replenishment is all about sending stores inventory to replace what they sold. And a key part of enabling so much work in our stores is getting replenishment rate.

I mean, sending our stores only the inventory they need, right when they need it. And moving demanding operational work like unpacking boxes and storing at the product, out of the stores and into our warehouses. To do that, the supply chain team is continuing to modernize our upstream supply chain to be fast, but precise. We're building a custom automation solution like the one you see here from our Perth Amboy facility outside New York City to better support our stores. This is the future.

One warehouse doing work for a whole group of store backrooms, sorting product, organizing items by store aisle and picking an individual unit or case pack based on the stores demand. The robotics allow our warehouse teams to manage the really complex sortation of millions of units and to handle each one individually bound for different stores at different times.

In the end, the warehouse team will organized carts, stock with only the items what store needs and sorted by IO onto a truck had to do in nearby store. Once it arrives, the store team grabs the cart, wheels to the sales floor and fills the shelf, literally in minutes. It's a far cry from the trucks we packed like a game of Tetris that take hours, if not a full shift to unload.

Instead, our team spends more time on the sales floor helping guests, using their expertise and talent and service to build the basket. And at the same time, stores get a precise amount of product sometimes delivered several times a day, our out-of-stocks improve and more reduce working capital by cutting the amount of product just sitting around in the back. It will take a while before we deploy this model across the country.

We prioritize the Northeast areas like Boston in New York, where our small format growth depends on it. You've seen these stores and they're small and with the real estate at a premium, we're using every possible square foot for selling space, leaving us with little to no back room. So we keep the sales floor in New York and essentially move the backroom to Jersey. And for our stores, it's made all the difference, but don't just take it from me hear it from them.

[Video Presentations]

What we're doing in supply chain is the reason we're able to grow in dense urban areas, where we can serve new guest, but, it also makes it possible for our full-size stores to access efficient local fulfillment hubs, because the product it needs in-store guest and online orders.

In the past couple of years, we've lowered our out-of-stocks as a total company. Now, we are focused on reducing out-of-stock variability between individuals stores, to do that, we're improving how we transition merchandise from one season to the next and improving our direct-to-store deliveries. And we'll see even more out of stock improvement as we scale our replenishment model over time.

It all comes down to this, investing in how we replenish stores has given us a sturdy set of rails to serve those stores. And with the strong foundation in place, our fulfillment operation glides right on top. So we can offer our guests so much more ease and convenience from their local stores.

Digital fulfillment is a big platform for growth and this is an enormous opportunity to serve our guests in new ways, but at the end of the day, an overwhelming majority of retail experience is still happen in the store. So, make no mistake, our store teams have to nail it. Helping guest find what they need before they even ask. Sharing their expertise to make recommendations, presenting merchandise in a way that's easy to shop and fund to explore.

The point of our investments, upstream is to put more team members on the sales floor, helping guests instead of in the backroom, checking off tasks. A couple of years ago, the stores team kicked off an effort to modernize the way we run our stores, from how we use our talent to the many ways we invest in our team. And all against the backdrop of our commitment to reach a \$15 minimum hourly wage by the end of 2020.

We started training our team to be specialists so they could bring expertise to how we serve our guests in each area of the store. We improved the technology they have at their fingertips, to make their service even better. Today, our team can help guest checkout anywhere in the store or place an order for something not in stock or from their mobile device. It's all about continuing to elevate the guest service and experience.

So here's a video, we use this for all of our annual Company meeting. It's our team talking to our team, about what we're doing inside our stores to serve our guests better than ever. Take a look.

[Video Presentation]

We're modernizing both inside and out. As we continued remodeling 100s of stores across the country, the biggest difference, we've enhanced our experience with updated to core, lighting and color or opening sight lines that really let the product shine. Last year, we completed more than 300 end-to-end new outlets. And the most we've done it any time in our history.

The reaction and complete excitement from guests doesn't get old. They tell us they love what we've done with the place but even better, they shop us more often. We consistently see an average 2% to 4% sales lift per store after remodel. We moved at an unprecedented rate to touch a majority of our stores in just a few years. We'll do another 300 this year as part of our effort to have more than 1000 remodeled stores by the end of 2020.

Beyond that, we'll continue remodeling the in-store experience across the chain but at a more moderate pace for the long-term. While we're investing in existing stores, we're also finding new sites to serve new guests. Last year, we opened more than 1 million square feet of sales floor in small

format stores and in big markets like New York and new markets like Vermont.

In fact, some of our most recent openings have already become our highest volume small format stores. Even if the traffic in our mature small formats has continued to rise. This year we'll open doors in growth areas like LA and Washington, D.C. your college campus is in Seattle and in East Lansing and also in new communities for Target like Cape Cod and Santa Barbara.

These stores help us enter new neighborhoods where a full-size store wouldn't fit and where we see a need we can fill. And it continued to show strong financial performance being our chain average and comparable sales growth and productivity. To a building owner or developer, Target's a strong brand and a sought after tenant which has positioned us well to capture great opportunities during a time when 100s of empty retail boxes are suddenly up for sale.

We'll continue to evaluate where we can meet new guests or better serve existing ones and maintain our pace of opening approximately 30 new stores a year over the next few years. Target's confidence in stores hasn't changed, it's were everything we're doing for the guests comes together to create experiences that are differentiated, inspiring and easy. We're using our stores and stores, stores performance centers, stores is the local connection to our guests even if they don't come inside for every trip.

And are more than 1800 stores with a passion and talent of our incredible team, we remain at the center of how we deliver, grow and differentiate for years to come.

Thank you.

## **Brian Cornell**

So, clearly a lot of incredibly exciting work is underway and the future is just as bright. So, as you've heard from Cathy and John, we're clearly focused on harnessing the success. Using it to fuel sustained growth across the business as well as reducing costs, improving speed and efficiency. We're building a durable financial model that will propel Target forward in any economic environment.

It's a model that translates topline growth to bottom-line performance. So, in a typical year, you should expect to see low single-digit comps leading to mid-single digit growth in operating income, and a high single-digit growth in EPS. The model is also built to deliver higher after-tax ROIC pushing us further into the mid-teens during the next few years.

So, let's walk through what this means for 2019, starting on the topline. You saw the detailed numbers in the morning's press release. For the full-year, we're guiding to comp sales growth in the low to mid-single digits that will reflect the combination of increased traffic to our physical stores, strong market share gains in digital, greater adoption of our fulfillment capabilities and market share growth in every major category across both stores and digital.

Moving down the P&L. as you heard from John, we're acutely focused on controlling costs to offset increased pressure for our wage investment and fulfillment growth generated by our growing digital business. With that discipline in 2019, we're planning to deliver moderate improvement in our operating income rate which will translate in the mid-single digit growth in operating margin dollars.

And combined with the benefit of a low share count, this operating performance will translate into high single-digit growth in EPS. As you heard from Cathy, for many years Target's taken a consistent disciplined approach to capital deployment. In 2019, we expect another year of continued robust cash flow which we'll use to fund CapEx of about \$3.5 billion which on top of the investments from 2017 and 2018 will put our three year stack at nearly \$10 billion.

We're also positioned to deliver a low single-digit increase in our quarterly per share dividend; a commitment we've upheld nearly 50 years running. And we expect continued capacity, return cash to shareholders through share repurchases within the limits of our debt rating. Altogether, this performance will translate into strong after-tax ROIC of nearly 15%.

As for the near term guidance, for the first quarter we expect to deliver comp sales growth in the low to mid-single digits, perhaps just a little stronger and will deliver for the full-year. In light of the continued opportunity in our toy and baby business. We also expect to see a low single-digit increase in operating margin dollars but a small decline in rate reflecting the mix impact of the unusual strength in both toys and baby.

And likely for the full-year, we expect high single-digit growth in our first quarter EPS. So, we covered a lot of ground today but the story in my mind is actually quite simple. During the last three years, while the future of the industry was anything but certain, Target laid out an ambitious agenda to reimagine our stores. To re-event our supply chain and fulfillment capabilities to reposition our own brand portfolio and to invest in our team.

We did this so that we could transform our company, build a durable model that deliver strong consistent growth that puts Target right in the center of

the winner circle in retail. Two years later, that's exactly what we've done. Today, Target is America's easiest place to shop and one of the world's most innovated companies.

As we carry into 2019, you can expect Target will continue to deliver, will continue to adapt, evolve, innovate, invent. We'll continue to inspire and we'll continue to succeed so that Target will continue to lead this industry for many years to come. 2018, was a great year for Target but I'll leave you with a new headline; 2019 will be even better.

So, thank you for being here this morning.

That concludes our prepared remarks and now we want to use remaining time to answer your questions. I'm going to try and get through as many questions as we can. So, I'd ask you to limit your questions to one per person. I'd appreciate if you started by introducing yourselves and the organization you represent and while I'll be here on stage, I've got several members of our leadership team that are ready to jump in and provide expertise on the various topics we'll cover today.

So, we got mike runners around the floor today, all the hands just went up at once, that's great. Simeon, why don't we start right here with you.

## **Question-and-Answer Session**

### **Q - Simeon Gutman**

Thanks Brian, good morning. Simeon Gutman, Morgan Stanley. So, you're guiding to profitable growth and you said this is the durable model going forward. I think on TV you said we're getting to the path of stabilization, so I'm curious if there's anything that you're looking out that's maybe more subdued like why that comment.

And then second of all, given that the business now has this potential, was there any debate of guiding to flattish margin, just you have more ammunition to invest.

### **Brian Cornell**

Yes, it's a great place to start. Again if you look inside of our Q4 results, we started to see that margin stabilization and as we adjust for the 53<sup>rd</sup> or the 52<sup>nd</sup> week changes, we're starting to see that improvement and we expect that to extent in the 2019. So, when you look at our focus on efficiency on reducing costs, as you see demand shift to more profitable fulfillment measures, we expect 2019 will be a year where we deliver consistent

operating margin improvement coupled by very solid single-digit mid-single digit comp growth in the first quarter, single-digit throughout the year.

And that's going to translate into high single-digit EPS. So, all the work we've been doing for the last few years is starting to come together. And I've talked about this a number of times, the great part of our strategy is it's not driven by one single element; it's all of these elements now coming together. Maturing at scale and importantly the guest and the consumer is voting with their wallet and with their feet.

So, it's all starting to come together and we're building that flywheel that we'll extend it to 2019 and beyond.

**Michael Lasser**

Good morning, it's Michael Lasser from UBS.

**Brian Cornell**

Good morning, Michael.

**Michael Lasser**

Good morning, Brian. You laid out several factors that'll drive gross margin stability. How much have you assumed you're going to have to invest incrementally in promotions and price to achieve your goal of gaining market share across every category?

**Brian Cornell**

Yes. Michael and I'll let Mark jump in here in a second. And one of the things we talked about in our prepared comments and we've talked about it over the last couple of years is this investment we made to enhance our pricing and promotional capabilities. And we've made tremendous progress, the real expertise. So, we feel very good about our pricing position today, the value we're offering against our entire portfolio.

And as we look to 2019, we'll make sure that we can do and be competitive that we're priced right daily, that we offer a great value to our guests, that's at the heart of our brand promise when you think about expect more and pay less. That's going to continue and we think that's going to be very durable as we go forward.

So, we're committed to being priced right daily delivering our guests great value across all of our categories and I think we're well prepared for 2019 as we think about our pricing and promotional position. Mark?

## **Mark Tritton**

Yes. Hi, Michael, hi. I just add that to reiterate what Brian said last two years has been about creating a lot of stability in terms of price and promo as well as helping with our trips and traffic. And we've been outpacing regular price sales versus promo sales for the last two years and created great stability and trust with the guest regular price as we manage price values. It's really working for us.

## **Brian Cornell**

Good. Alright, why don't we go right at front? Team, we've got lots of hands doing up, so we're going to make sure we try to get everyone.

## **Eddy Yruma**

Hi, thanks. This is Eddy Yruma from KeyBanc. You've made some management changes within food and beverage. It seems like you're putting some real muscle there. How do you dimensionalize the opportunity, any kind of early findings?

## **Brian Cornell**

Yes. When I'll go back to the progress we made over last several years and we've made major commitments to improving our food and beverage supply chain, our merchandizing, our in-store operations but we did make the decision earlier this earlier to bring all of those functions together under one leader and Stephanie is here today.

And as we looked at that business, we recognize it's very different from many other parts of our portfolio. The products we source, the perishability of it, the coal chain environment, how we manage product from a store level. So, we made the decision to bring all of those elements together under one leader. The functions will still work very closely with their counterparts; in supply chain; in merchandizing; in pricing; in marketing.

But having one dedicated leader who thinks about food and beverage every single day and is connecting the needs and supply chain to merchandizing to store operations, I think it's going to yield significant benefits in the year to come. But we've been growing our food and beverage business for over six quarters now. 2018 was a year where we took market share gains in many of our key in essential food categories and I think with Steff's leaderships we're just going to continue to build on that in years to come.

Why don't we get to the back of the room?



**Greg Melich**

Great. Hi, Greg Melich with Evercore ISI.

**Brian Cornell**

Good morning, Greg.

**Greg Melich**

Good morning. So, a couple of years ago you talked about investment and how that was going to invigorate traffic and it's worked. As you look out now, the next couple of years and after that, where are we on that investment cycle in terms of in the P&L versus CapEx?

So, more specifically, it sounds like green models or peak the next couple of years, so maybe could CapEx start to come down again or will investment then go back into the P&L. and on the supply chain, do we need to now ramp-up at some point supply chain investment.

Just where are we on the cycles of that would be really helpful.

**Brian Cornell**

Yes. Greg, honestly two years ago we talked about the significant investments we're going to make; in-stores; and reimagining our stores; the investments we're going to make in our brands; the investments we're going to make in fulfillment capabilities and our team. I think now we're at the point of maturing and scaling those investments.

Now, John talked about in great detail the work that we've done from a replenishment standpoint of fulfillment standpoint we're going to continue to build awareness and adoption of those fulfillment capabilities in 2019 and beyond. We'll continue to remodel stores and we certainly like to see the lift in the return that we're getting with those stores.

We think we've got a pathway to open up many more small formats but many of the big investments we made are going to start to normalize over time. So, I know one of the questions that's been on every one's mind is is there another big Brian billion dollar investment. Is there a need for additional CapEx?

As you look at our guidance and you look at our plans today, the answer is no. we'll continue to invest in our stores, we'll continue to open up new small formats. John and his team will continue to scale and mature our replenishment and supply chain. Mark and his team will continue to develop and roll out exciting new brands.

But many of the big capabilities are now in place and you're starting to see the leverage in our guidance for operating income in years to come. So, I know all of you have been waiting to ask that question, there is no billion dollar surprise for today, there is no major new initiative, we're going to continue to execute the strategies in place that's working today, that's being well-received for by our guests for many more years to come.

Back up front.

### **Peter Benedict**

Hi Brian, Peter Benedict at Baird. You talked about the new replenishment model that's going to be rolled out to some of the smaller stores. I'm curious what's the timeline for getting that to start impacting the larger stores and related to that or somewhat related, are there any marketing or pricing plans in place to incentivize customer use of the different fulfillment options that you have for digital?

### **Brian Cornell**

When I handle the back end and then John why don't you talk about some of the timing, and Rick why don't you jump in from a marketing standpoint?

One of the things that we didn't talk about specifically today is the path and the journey we're being benign with our fulfillment capabilities and building awareness. While we've been working on many of these for upwards of five years, pick up with something we started talking about almost five years ago.

Now, over the last year or so we started talking about the fact that we've gone from testing drive up to scaling to almost a 1000 locations. It was December 2017 when we acquired shipt, in that same time period in major metro markets we started offering our same-day courier service leveraging our Grand Junction capabilities.

But it literally wasn't until the fourth quarter of 2018 that we started talking about it to our guests, actually starting to build it into our "Target Run and Done" campaign.

So, as we said earlier today, now it's about building awareness because what we here time-and-time again when our guest realizes that they can place an order, drive in our parking lot and within two minutes we'll put that order in their trunk, they love it and their promoter scores are the highest we've received for any service. But in many cases, they just haven't been aware of it.

Because we wanted to make sure we built the processes; we had the systems in place; we had the measures that we knew our guests were looking for before we started to really talk about it. As we go into 2019 and beyond, we're going to incorporate that into our "Target Run and Done" campaign, make sure that America knows we are the easiest place to shop and we give you all these choices; over 1800 great stores to stop.

You can order from your desk and come by a couple of hours later and pick up that order. If you want to drive into the parking lot on a chilly day, leave the kids in the car, we'll put it in your trunk. If you want a personal shopper from ship to do the shopping for you and come by in a couple of hours, we can offer that. So, we're going to continue to build awareness but as we build awareness we're getting a great response from the guests.

And one of the things I talked about earlier today is the good news is as we think about order pick-up or drive-up, while it's more profitable for us as John showed you, it's also preferred by the guest. They love the convenience of knowing they don't have to wait several days for something to be left on their front door, they have the reliability knowing they can pull into our parking lot or walk into our store and we'll have that order ready for them.

So, it's both more profitable but importantly looking through the guests lens is preferred by our guests. So, that's a great combination for us.

John, you want to talk about the timeline for advancing some of our replenishment capabilities?

### **John Hulbert**

Sure. So, I'll go back to what I talked about. I think we're starting in the northeast, we're into scale Perth Amboy first of all and service the small formats, the significant number of small formats we've opened and will open in the northeast to start with.

Right now, the team is thinking about what retrofitting an existing building looks like. We've run iteration probably number three of that right now. We need to get a little bit further into the Perth before we finalize that. I would tell you the thing we think about is we've move cautiously to start. And the concern is we don't get to shut down a building because we don't get to stop selling for some period of time for the stores that are served by that building. And so, we will move cautiously at the beginning, we want to ensure we don't have buildings that are disrupted during Q4 because we don't want to create problems there. So I think you'll see us start a retrofit of an existing building probably early next year, get one of those behind us and then, Peter, I think, we will have a much better idea how that goes, we

will obviously refine it and then how quickly we can scale across the rest of the country.

**Brian Cornell**

Okay. Why don't we go right here, Chuck?

**Chuck Grom**

Thanks. Good morning, Brian. Chuck Grom from Gordon Haskett. On the Target + initiatives, one thing you didn't discuss this morning. So I was wondering if you could shed some light on that effort? And I think it's probably been 10 years since I've asked the CO this question, but on the number of store opportunities ahead for the small format at Target?

**Brian Cornell**

Great. Rick, do you want to talk about that Target +?

**Rick Gomez**

Target + is new initiative that we are very excited about because it has the opportunity to grow our dotcom business in a profitable way. And what it's about is how we can expand our online assortment into new white space, it's Target's version of a marketplace, but it is different than our other competitors and it's different because we are known for curation and our consumers, our guests expect that. So Target + will be invitation-only. It's not intended to be a catalog of a list of products and products and products, rather we're going to go very deliberately, very intentionally after the right categories, the right brands and then offer them on Target + and with third parties.

And for us, it's a profitable way to grow our dotcom business because the third parties deal with the supply chain components of it and then what we offer, which I think is a competitive advantage is you can take your product and if you are not happy with it and you want to return it, you can take it to a Target store, which is something that our competitors can't offer. But the one point, I would just say, is it's still in its early stages, but we think long-term can be a profitable growth driver for us.

**Brian Cornell**

Chuck, on the new store front, we certainly think for small formats we've had dozens and dozens of opportunities in front of us and we've taken a very disciplined approach. I mean, just a few years ago, we were still testing and learning how to operate in a smaller-sized store, our merchants were

learning how to curate the right assortment store-by-store. Our store teams were learning how to operate in a different environment. From a supply chain replenishment standpoint, we had to figure out how to deliver and replenish those stores, where you can't pull up a 40-footer.

So we've taken a very disciplined approach. The great part today is we now have demand coming our way. We have local communities that are putting up their hands, saying, we'd love to have a small Target store on our college campus, in our local neighborhood. So we're seeing an abundance of opportunities and we'll continue to be disciplined as we move forward, but we see opportunities to open dozens and dozens of stores across the country in urban settings and on more college campuses in the years to come.

And as I said earlier, there our most productive stores in America, delivering some of the highest sales per square foot that we've seen across the country and the demand for these stores continues to grow, so we'll continue to meet that demand over time. We'll go right here.

Q - Chris Horvers

Thanks, good morning. Chris Horvers, JPMorgan. Can you talk about sort of what you're expecting in terms of share gains within the low to mid-single digit comp and then sales a little bit better? What categories outside toys which will annualize Toys "R" Us after the first quarter? What the driver of that is and where you see the opportunity? And then specifically on gross margin, do you expected to be flat in 2019, given that you're scaling the fulfillment options and toys will create some pressure on 1Q, could we see actually gross margin start to improve later in the year and then into 2020?

**Brian Cornell**

Yes. So Chris, when I start with our approach to market share gains, and I'll let Cathy talk little bit about gross margin, but I'll go back to our results in 2018. While we are very excited and Mark and the entire team did a sensational job of taking advantage of the TRU closure, the BRU closures and we took significant share in those categories. In 2018, we grew share across every one of our major categories, in apparel, in home, we had a very strong year in beauty. We grew share in food and beverage. All of our major merchandising categories are growing share right now. We expect that to continue in 2019.

We expect our growth to be driven by traffic gains, like we saw this year, equating to market share increases across both our physical and digital space. So we continue to see market share opportunities across our entire portfolio. And obviously, as we see unique opportunities, we'll lean in to take advantage of opportunities category by category. But for this team, they

expect to take market share across every one of our major categories in 2019 and take advantage of the opportunities we see in the competitive market. Cathy, why don't you talk about gross margin?

**Cathy Smith**

Yes. So let's start with operating income rate, first, because that's the better place to start. We said that we'll see moderate expansion there this year. As we think 2018, 2018 was a good way point as we think about going forward. So we've got enough insight into headwinds and tailwinds that will balance. So then when you move back up, we haven't been as specific between gross margin and SG&A, but we actually don't expect a big change, right. So we already understand where the business is at, we understand Q1 is going to be a little lighter on the margin side because of a little bit of mix business that Brian talked about in his prepared remarks. So Q1, but in the rest of the year kind of expect a balance between gross margin and SG&A and a little bit of leverage on the up income line.

**Brian Cornell**

All right. Next question.

**Bob Drbul**

Hi, Brian, it's Bob Drbul from Guggenheim Securities. I guess, my first question is around the new brands in the private brands that you've launched, I think 20 is the number and you said there is more to come. Can you just talk about the rate going forward? What you've learned? Can you comp those businesses and just how we should think about that aspect of it?

**Brian Cornell**

So let me set it up and then I'll turn it over to Mark. And I think Bob, it's important to recognize the commitment we've made to our own brand portfolio and the work that's being done by our product development and design teams, our sourcing teams, our merchants, the role that Rick and his team play from a marketing standpoint and then the in-store execution and experience. We've made a major commitment to making sure that we use our own brands as a point of differentiation that we bring great style and quality to our guests at a great value.

But the path we've been on and the pace is going to slow. The team has made remarkable progress in a short period of time. And I've said this a few times publicly, the team has done three or four years of work in about 18 months to make sure that we took advantage of the opportunity. We're going to be more surgical now, we'll be focused much more around making

sure we're managing those brands and building brand management expertise into our teams, but we'll continue to look for white space opportunities and to strengthen our portfolio with great own brands that drive market share gains, drive traffic to our stores and more visits our site, but the team has done a remarkable job and it's certainly been a big part of our market share gains and the change in guest perception as we bring great newness, great quality and value to our portfolio. Mark?

### **Mark Tritton**

Yes. Change will be a constant, but the velocity will change. So as Brian said a compacted amount of work as we moved into reestablished and stabilized mode of our own brand portfolio and the redefinition and curation of our total portfolio offer. And so you'll see a velocity change as we move to stabilize and optimize that assortment. Question around, can we anniversary that? Yes, we can. Yes, we have. And yes, we will. So good things lie ahead, but expect the change rate to be different.

### **Brian Cornell**

Yes. Mark, why don't you spend a couple of seconds and talk through the performance of Cat & Jack, which in many cases, I remember standing here actually three years ago with many of you talking about our commitment to Baby, the Cat & Jack brand, the progress that we expected to make in that space and obviously Mark that's played a big role in attracting more moms to our stores, it's been a big part of our success story in 2018. But I also think it's a great story of a brand that's continued to build support momentum on a multi-year basis.

### **Mark Tritton**

Yes. It was a bold reinvent of a business in kids that was performing in low single-digit growth when the market wasn't. So we said, why change, and all we want to do was connect with our guests and deepen our relationship with them. Two years on what we found is that that's a trusted and beloved brand across the U.S. And if you match that to the sense of authority that we want to create with moms, kids, babies, our most recent market share gains in TRU and BRU exit and the strength of our market share there really starts to build an ecosystem more authority with guests archetypes and relationships, so we can be Americas easiest place to shop.

The Cat & Jack continues to build from strength-to-strength. We look at both category growth as well as year-on-year growth of existing space to really develop that strength. And what we see, even in the examples that Brian shared today, example in home where we had one brand and now we have up to four or five brands, the sense of the sum of the parts or the authority

that we create in these individual spaces, home, baby, kids continues to be a key market share driver for us.

**Kelly Bania**

Thank you. Kelly Bania from BMO Capital.

**Brian Cornell**

Good morning, Kelly.

**Kelly Bania**

Going back to the replenishment model, can you just give some more specifics in terms of the cost of the technology that you're putting into Perth Amboy? It sounds like maybe one of these are going to be added in next year, I guess, that means 2020. And just some specifics on the financial impact on the P&L as you start to really ramp implementing those longer-term, and has this been tested at any of the suburban larger stores?

**Brian Cornell**

John, do you want take that one?

**John Mulligan**

I thought Brian said one question, there's is about eight there.

**Brian Cornell**

John, there are only seven. We'll try to compact it down at one.

**John Mulligan**

I'll start kind of in reverse. We have tested a variety of things in multiple distribution centers across the country, all of them doing different things, some of it automation, some of it being done manually. There's one in Minneapolis that we have used as our kind of core test and that is providing daily replenishment to a store, a large store in Minneapolis.

Two things I would say. One, this is much beyond -- we show the automation because that's -- it's easy to see and you can take a video of it. There is so much more going on around this. There is a new warehouse management system. There is a new order management system. We changed the way we do transportation. We changed the way things physically moved through that building. We changed the way things



physically moved for the stores. So the change here is significant when we start rolling out across the country.

As far as impacts, I would tell you, it's in the guidance, the long-term guidance Brian talked about. It will be in -- it's in our capital goals. It's in the way we're thinking about the operating margins going forward. So the balance of when we do this and the cost and the payback is all thought of within our current long-term guidance. So we feel good that that's in there, we have more work to do, like I said, to figure out the exact cadence, which will mean the exact timing of when capital comes, but we want to be thoughtful here given the magnitude of what we're changing across the supply chain.

### **Brian Cornell**

John, it might be helpful for us to spend a few minutes and make sure you understand the work that's going on really across the company from a replenishment standpoint because [Indiscernible] obviously automation, robotics are part of the future. John, we're doing a a lot of things, changing how the sortation process in stores that's driving immediate efficiency to how we replenish, it's impacting our in-stock position, it's take -- it's reducing inefficient touches in our stores.

So we might want to leave the group with a sense for the fact there's things happening immediately, longer-term automation robotics will enhance that, but we're not waiting for robotics and automation to drive efficiency in how we are operating our stores.

### **John Mulligan**

No, I think that's right. We've done many things much more manually, we do -- we've done things upstream in the distribution centers to help the stores. And as Brian said, even the way the stores work there unload process today has changed almost 180 degrees from where we were a year ago. That has created significant efficiency for the stores. It has put more team members on the sales floor, which again is a big part of what we're doing here.

We've done manual stuff in all the buildings and how we load trucks and how we sequence and where pallets are relative to case pack. So there's a lot of manual work being done, all of that headed toward walking down the path of where we ultimately want to get to as we bring the automation and the new order management and the new warehouse management and the new inventory planning system, all of that will come online as well in parallel. And so we're marching down the path and again it's cool to see the sexy

automation, that's just one piece of what we're doing from a replenishment standpoint.

### **Brian Cornell**

Yes. But the changes we're making from a process standpoint, a system standpoint, that's also fueling this operating margin income improvement that we're projecting in 2019 and beyond. So there's more to come, but some of the foundational work that we're doing more manually is also contributing to an improved operating environment. Here we go?

### **Craig Johnson**

Craig Johnson, Customer Growth Partners. Brian, you've made great progress beginning right here two years ago and making your offerings more relevant to how people live, work, spend their money today. A generation or two ago, people divided up their spending about half between goods and services. Now, it's 69% services, 31% goods. To what extent are you all looking at the services side, which is the dominant part of the wallet as an opportunity for you all? And if so, if you're thinking about it, are you thinking to build, buy or partner?

### **Brian Cornell**

Yes. And Craig, we'll also -- we'll always look at ways to meet the needs of the guests. Right now, our strategy is very focused, it's very centered around the initiatives we've been talking about to-date. We'll look at the appropriate role that services play and we'll continue to make sure that our brand meets the changing needs of consumers. I think we go back to some foundational components and I go back two years ago.

Standing here two years ago, there were lots of questions about the role of physical stores. I think we know today that American consumers still enjoy shopping in physical stores and upwards of 90% of the business is still done there. So we want to make sure we leverage our store assets to provide a great in-store experience. We continue to modernize the store experience. We invest in our teams to provide great customer service. In the future, we may complement that with other services. We want to make sure that fulfillment and that digital experience is really easy, really convenient.

So we want to make sure that we're focusing on the needs of today's consumer, but also always looking around corners to what tomorrow brings. So two years ago, many people were questioning whether investing in stores was the right thing to do. In the holiday quarter, our store comps grew almost 3% and consumers continue to enjoy that shopping experience. We'll continue to make sure we look around corners and find out what's next, but

we think we're on the right path and we've got the flexibility and I think we've proven to be flexible and adaptable to changing consumer needs that'll be part of our future as well.

## **Ed Kelly**

Hi. It's Ed Kelly, Wells Fargo. Brian, you've had about, I don't know, maybe 50 basis points or so of pressure on the gross margin over the last couple of years from a fulfillment standpoint on digital. It sounds like what you're seeing today is that you expect that pressure to start to ease. Could you just maybe give us a little bit more color around what drives that? How should we be thinking about the incremental margin or the margin now on an incremental e-commerce sale? And how that's evolving over time?

And then the second question I had for you is around wages. So I think I heard you reiterate a commitment of \$15. That's expensive, I believe, right. So how does that play into the financial guidance and particularly how you're thinking about 2019?

## **Brian Cornell**

So Ed, starting with wages, that's built into the model that we talked about today. We talked several years ago about the fact that we would be on a path to get to a starting minimum wage of \$15, that's built into our plans for future years. We've talked several times today about the fact that the guests is now moving to fulfillment options that are actually more profitable for us. We expect that to continue going forward.

And obviously, there's always short-term anomalies. As we thought about 2018, we didn't anticipate that TRU was closing and BRU would be closing. We made big investments to make sure that we were going to garner market share in those important categories. It's going to drive long-term benefits for us, as families come to Target more frequently for toys and items for babies and kids. So that was a long-term investment. Those were lower margin categories, but it was the right thing to do during 2018. That will moderate over time.

So one of the things that we didn't talk about today, but I think it's so important to our overall plan is the balance of our multi-category portfolio. The fact that we had this very unique portfolio, where we're growing market share across all of our categories, but they're still really balanced. 20% of our business in apparel, a very high margin category. 20% in home, a hardline and toy business, it's about 20% of our business. Beauty and essentials being 20% and then food and beverage.

So we have this very balanced portfolio that I think provides us a pathway during good times and bad, where we have a durable model, where we can meet the needs of consumers no matter what the economic environment. So we expect the investments we made this year to stabilize over time. And along with the changes that we're going to make and the benefits that we'll see through new fulfillment capabilities, we expect that to strengthen our gross margin, our operating income over the years to come. So it is officially double zero here.

We didn't get to the question right up front, why don't we just take one more because your hand has been up the entire time and I'll feel guilty if I walk off without giving you a chance to ask a question?

**Mike Baker**

Thank you, Brian. It's Mike Baker from Deutsche Bank and it's going to be one last question in three parts. And it's probably -- it's a financial question maybe for Cathy, but the EPS growth, if we just do the midpoints of the guidance versus the adjusted EPS, it is a little bit slower in the first quarter, a little bit faster throughout the year. And I get what you said about the gross margin, but shouldn't the better sales from toys and the like offset it?

So why does it ramp throughout the year? And maybe related to that, in the first quarter, any impact on things like tax refund, snap, even the late Easter people are going to want to know about? And lastly, and again related to all that; how should we think that the comps throughout the year as your comparisons get 2% to 3% harder each quarter? Thank you. So one question, three parts, all about the pace of the year.

**Brian Cornell**

All right, Cathy, you packed a lot in there to wrap this up.

**Cathy Smith**

I'm happy to take it. But -- so as we said, we'll see a little bit of pressure on the op income line in the first quarter, but to Brian the guidance we gave today, low to mid-single top line, and that was Q1 and full year. So you can expect and you guys know what our costs for this last year so you can think about the two year tax going there, but you can expect a pretty consistent. There is always -- we're not giving guidance for second, third and fourth quarter right now. But you're going expect a pretty consistent pace there, if you think about low to mid in the first quarter and low to mid for the full year, it's not hard to figure that one out.

And then to your point about the EPS side, same thing, if you look at the course of the year you know, first off, we have to start with sales and if we expect sales to be not too biggest wins in any given quarter, you should expect a similar path on the bottom line. So that's where I would go for now. Obviously, we put that in our guidance in the first quarter and the full year.

And then we don't actually see a big impact in our business on snap or tax refunds we do always keep an eye on that as you can imagine, but because of our multi-category assortment, because of our incredibly loyal base of guests, we see pretty consistent business and we don't see the impacts there typically.