

TJX

CLIENT REPORT

SONTAG SOLUTIONS



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Executive Summary

TJX Companies, Inc. is the leading off-price retailer of apparel and home fashions in the U.S and worldwide. TJX has over 3,300 stores around the world and is largest off-price retailer in domestic market. The company provides quality, fashionable, brand name and designer merchandise at prices generally 20% to 60% below department and specialty stores. The company operates its business mainly in the U.S but it also has chains in Canada and Europe.

TJX as an off-price retailer takes advantage of overrun and excess inventory created by designers and full-price retail outlets. While specialty or department stores rely on fashion trends and product design to drive profits, TJX depends on its ability to move high volume of goods quickly and depend on relationships with designers and distributors who provide low cost inventory. The company uses its scale with distribution infrastructure to maximize productivity while maintaining the lowest possible price for customers. In order to do so, TJX continuously increases the number of stores around world and sources merchandise globally from 16,000 vendors in more than 75 countries.

Over its 37-year history, TJX have had steady sales and earnings growth. The sales revenue in the fiscal 2015 reached \$29.1 billion and surpassed that of Macy's, the largest department store in the U.S. With the growth of earnings, the company have consistently returned values to shareholders. Recently the company announced that it will raise its quarterly dividends by 20% and repurchase \$1.8 billion amount of common stock during the following year.

Company Background

Founded in 1956, the company evolved from the Zayre discount department store chain which opened its first branch of T.J. Maxx in 1976. In 1988, Zayre sold its nameplate to Ames and T.J. Maxx was renamed as The TJX Companies, Inc. The company now operates its business in four major divisions: Marmaxx (T.J. Maxx and Marshalls) and HomeGoods, both in the U.S., TJX Canada and TJX Europe. The Marmaxx and HomeGoods offer family apparel, home fashions, accent furniture, lamps, rugs, decorative accessories and other merchandise. TJX Canada operates Winners, Marshalls and HomeSense. TJX Europe operates the T.K. Maxx and HomeSense chains in Europe. Recently, in order to expand its business in online sector, TJX acquired Sierra Trading Post, an off-price internet retailer and T.J. Maxx launched its new e-commerce site, tjmaxx.com

As a leading off-price retailer, TJX showed distinct movements from its peer group. The company is taking aggressive inventory turnover and maintain high inventory turnover roughly 55 days/year (Peer group average 85 days/year). By doing so, it offers fresh selections of products and create a treasure hunt experience to spur frequent customer visit. The expansive distribution infrastructure supported close-to-need buying by delivering the goods to the stores quickly and efficiently.

TJX operates in a low cost structure compared to many traditional retailers. Its advertising mainly focuses on promoting its brand name rather than individual products, which contributes to advertising budget remaining low compared to other traditional retailers. Additionally, the company's distribution network is designed to run cost effectively. It does

not spend heavily on store fixtures. The selling space is flexible without walls among departments and free of permanent fixtures. As a result, the company can save cost and can operate store according to customer demand.

TJX also has a strong relationship with its suppliers. Because of the characteristic that off-price retail possesses, the relationship with the vendors is crucial to the company. Historically the buyer-supplier relationship with TJX has been more of a partnership. With the strong cash flows, the company has an ability to pay the vendors promptly so that it can maintain a good relationship with them.

Financial Analysis

Income Statements

Consolidated Statement of Income

Amounts in thousands except per share amounts	Fiscal Year Ended		
	January 31, 2015	February 1, 2014	February 2, 2013 (53 weeks)
Net sales	\$29,078,407	\$27,422,696	\$25,878,372
Cost of sales, including buying and occupancy costs	20,776,522	19,605,037	18,521,400
Selling, general and administrative expenses	4,695,384	4,467,089	4,250,446
Loss on early extinguishment of debt	16,830	—	—
Interest expense, net	39,787	31,081	29,175
Income before provision for income taxes	3,549,884	3,319,489	3,077,351
Provision for income taxes	1,334,756	1,182,093	1,170,664
Net income	\$ 2,215,128	\$ 2,137,396	\$ 1,906,687
Basic earnings per share:			
Net income	\$ 3.20	\$ 3.00	\$ 2.60
Weighted average common shares – basic	692,691	713,470	733,588
Diluted earnings per share:			
Net income	\$ 3.15	\$ 2.94	\$ 2.55
Weighted average common shares – diluted	703,545	726,376	747,555
Cash dividends declared per share	\$ 0.70	\$ 0.58	\$ 0.46

Net sales of TJX increased to \$29.1 billion for fiscal 2015, up 6% over the same period last year. Net sales of fiscal 2014 was increased by 6% from the fiscal 2013. The company is having a constant sales growth with the increase of the number of the stores in operation and selling square footage. The company's operating margin of 12% has been roughly same for 3 years and the figure is much higher than the industry average of 6%. TJX is cost effectively operating its businesses. Earnings growth is expected for the company if it enlarges selling square footage for the following year.

Balance Sheets

Consolidated Balance Sheets

Amounts in thousands except share amounts	Fiscal Year Ended	
	January 31, 2015	February 1, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 2,493,775	\$ 2,149,746
Short-term investments	282,623	294,702
Accounts receivable, net	213,824	210,094
Merchandise inventories	3,217,923	2,966,490
Prepaid expenses and other current assets	356,824	345,327
Federal, state, and foreign income taxes recoverable	12,475	—
Current deferred income taxes, net	137,617	101,639
Total current assets	6,715,061	6,067,998
Property at cost:		
Land and buildings	888,580	722,645
Leasehold costs and improvements	2,780,932	2,720,391
Furniture, fixtures and equipment	4,671,029	4,255,210
Total property at cost	8,340,541	7,698,246
Less accumulated depreciation and amortization	4,472,176	4,103,745
Net property at cost	3,868,365	3,594,501
Non-current deferred income taxes, net	24,546	31,508
Other assets	210,539	194,328
Goodwill and tradenames, net of amortization	309,870	312,687
TOTAL ASSETS	\$11,128,381	\$10,201,022
LIABILITIES		
Current liabilities:		
Accounts payable	\$ 2,007,511	\$ 1,771,294
Accrued expenses and other current liabilities	1,796,122	1,681,834

Federal, state and foreign income taxes payable	126,001	64,715
Total current liabilities	3,929,634	3,517,843
Other long-term liabilities	888,137	732,999
Non-current deferred income taxes, net	422,516	446,071
Long-term debt	1,623,864	1,274,216
Commitments and contingencies (see Note M and Note O)		
SHAREHOLDERS' EQUITY		
Common stock, authorized 1,200,000,000 shares, par value \$1, issued and outstanding 684,733,200 and 705,016,838, respectively	684,733	705,017
Additional paid-in capital	—	—
Accumulated other comprehensive income (loss)	(554,385)	(199,532)
Retained earnings	4,133,882	3,724,408
Total shareholders' equity	4,264,230	4,229,893
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$11,128,381	\$10,201,022

TJX had improvement in its current ratio from 1.51 in fiscal 2013 to 1.72 in fiscal 2014. It maintained its liquidity, having current ratio for fiscal 2015 of 1.71. Since the company retains large amount of cash and cash equivalents which result from earnings growth, it has the ability to redeem all the current liabilities right away. It also has relatively small amount of long-term debt compared to the total shareholders' equity. Overall TJX has strong financials with high earnings and healthy balance sheets.

Competitive Analysis

Internal Rivalry

Off-price retail is a large industry with high growth rate. The total sales for the U.S's five largest off-price retailers grew 11% compared to a 4% increase in national apparel sales. The big competitors of TJX are Ross Stores, Burlington stores and Big Lots but TJX is much larger in the size of sales revenue, and the number of stores. Because of the high profitability of the business, the competition is intensifying. Some of the department stores

plan to increase its clearance stores. Especially, the Nordstrom rack expects to reach a total of 300 stores by 2020. Nordstrom currently has 167 Rack stores. Also, there are outlets, factory stores and online off-price retailers that are rival to TJX.

Buyer Power

TJX buys the excess inventory from specialty retailers or department stores at a 20%-60% discount, and pass these savings onto consumers. The switching cost of customer is relatively high in this market. Because of the unusual characteristics of off-price retail, the products are different for all the retailers. Unlike the department store, off-price retailers purchase vast amount of inventory from random vendors so their products are also random. Some products that T.J. Maxx has may not be in the other retailers. Therefore, the switching cost of customers depend on how diverse assortment the retailers can provide. Since TJX is dealing with 16,000 vendors, it has comparative advantage over the other retailers. Also, TJX differentiates its products by having several subsidiaries which offer different types of products, ranging from fashion apparel to home furnishings. It makes the switching cost of customers even higher.

Supplier Power

TJX source merchandise globally from over 16,000 vendors in more than 75 countries. There are numerous suppliers for the company. Since fashion market is unpredictable and it is hard for designers or retail stores to anticipate the consumer demand, it is crucial for them to get rid of their excess inventories. Also, TJX has a financial ability to pay vendors promptly, so it is in a good position to negotiate with the vendor.

Threat of New Entrants

Threat of new entry is relatively high. Although it might be capital intensive business to have strong distribution channel for appealing to diverse demographic, minimum efficient scale is small relative to market size. Also, off-price retail market has grown significantly. The growth rate surpassed that of the full-price retail market. Therefore there are a lot of large firms that are capable of paying that large costs. TJX has strength in efficient inventory management and distribution network specific to the off-price business model. The cost of expansive distribution infrastructure can be a barrier to the new entrants, but since they do not require high technologies, a company with huge capital can easily catch up. Moreover, there are online off-price retailers which do not need that much capital for distribution network. Although the individual online retailers might not be a great threat to the TJX, if the number of retailers increases, TJX will have to compete them with price. The threat of these entrants will eventually erode the high profitability of the market and TJX.

Threat of Substitutes

The substitutes of TJX are full-price retailers and department stores which offer brand new products. The switching cost of customers to the substitute is relatively high since TJX provides goods that are 20%-60% off from the original price. TJX takes advantage of overrun, canceled order, and forecasting mistakes made by full-price retailers. Therefore, the threat of substitute is not significant.

SWOT Analysis

Strengths

TJX's strong market position and large operational base enables it to maintain a competitive edge over its peers. With strong market presence, the company has comparative advantage in expanding its market share and customer base. By the end of fiscal 2015, the company had over 3,300 stores in the U.S, Canada and Europe. TJX plans to continuously increase stores so that it can reach to a larger demographic. Additionally, TJX has high rate of growth in its earnings. With the consecutive earnings growth, the company could retain large amount of cash and cash equivalents, which causes improved liquidity and financial stability.

Weaknesses

TJX is primarily confined to U.S with a significant portion of its revenue coming from domestic market despite its presence in Canada and Europe. Their main revenue source is Marmaxx group which contributes over 60% of consolidated sales revenue. Together with HomeGoods, business operations in U.S market take over 70% of consolidated sales revenue. As a result, TJX is vulnerable to the risks related to political and economic conditions prevailing in that region. Therefore, the company should expand its geographic presence in order to mitigate the current concentration risk and enhance revenue generation.

Opportunities

TJX has an opportunity to expand its business globally, especially in Canada and Europe. It is already present in Canada and Europe market, having continuous earnings growth. Therefore, addition of new stores in those regions will develop TJX into global off-price retailer. The company plans to build 20 more stores in Canada and 50 more in Europe during the following year. Such network expansion could help the company better reach its customer base.

E-commerce business is one of the major growth catalyst for TJX. With the rising trend of online shopping, the company has huge potential to increase its profitability through e-commerce. These days, more and more customers prefer to shop online and place their order in their home. For customers, the online shopping is more convenient and reduces time visiting the offline store. TJX started e-commerce business by acquiring Sierra Trading Post and launching tjmaxx.com. As the company already has a presence in online sector, the company could further enhance its competitive position in the e-commerce market. By focusing more on e-commerce, the company will be able to enhance its sales by appealing to larger customer base and save on operating cost which is much lower in online retail.

Threats

The company is involved in a highly competitive market. TJX faces competition through local, regional and national retailers with low cost operators. Also, since the large department chains such as Nordstrom and Saks Fifth Avenue plan to increase their

clearance stores, the competition is more intensifying. TJX's competitors may have greater financial strength, better access to products and greater market penetration. Such an intense competition poses a threat to the company's existing market share.

TJX operates in global apparel and fashion domain and its business mainly depends on the customer preferences and changing fashion trend. The company should be able to react quickly to those changes to maintain its competitive position in the market. The customer's purchasing decisions are highly subjective and could be influenced by various factors such as brand name and product design. Any failure to detect those preferences can adversely affect consumer acceptance of brand and future business growth.

Strategic Recommendations

Revenue by Geographic

TJX has over 3,300 stores in U.S and worldwide. The stores are concentrated especially in U.S with the number over 2,000. In U.S, it seems that the stores are proportionally located in all the states but in fact a large number of stores is concentrated in a certain region.

Store Locations (U.S)

	T.J. Maxx	Marshalls	HomeGoods
Alabama	22	5	3
Arizona	13	15	9
Arkansas	11	3	4
California	110	137	59
Colorado	15	8	6
Connecticut	27	24	12
Delaware	3	3	2
District of Columbia	4	3	1
Florida	81	86	44
Georgia	47	32	14
Hawaii	3	—	—

Idaho	6	1	1
Illinois	47	44	22
Indiana	23	12	5
Iowa	10	5	2
Kansas	7	5	1
Kentucky	14	5	4
Louisiana	12	10	2
Maine	9	4	3
Maryland	21	29	14
Massachusetts	51	55	25
Michigan	39	24	13
Minnesota	15	13	10
Mississippi	10	3	3
Missouri	16	15	7
Montana	5	—	—
Nebraska	4	3	2
Nevada	9	10	5
New Hampshire	16	9	6
New Jersey	36	47	30
New Mexico	3	4	1
New York	71	74	38
North Carolina	34	24	15
North Dakota	3	1	1
Ohio	43	27	14
Oklahoma	9	5	1
Oregon	10	8	4
Pennsylvania	43	37	20
Puerto Rico	9	20	6
Rhode Island	6	6	4
South Carolina	21	11	6
South Dakota	2	—	—
Tennessee	25	14	7
Texas	59	75	30
Utah	11	3	4
Vermont	5	1	1
Virginia	32	28	16
Washington	19	16	4
West Virginia	6	3	1
Wisconsin	21	7	5
Total Stores	1,119	975	487

There are 306 TJX stores located in California and that is the largest number among the states. Compared to the total store number of 2,581, more than 10% of total stores is located in California. However, only 16% of total sales revenue came from the West.

Revenue Information (Percentage of revenues by geography)

	Fiscal 2015	Fiscal 2014	Fiscal 2013
United States			
Northeast	23%	24%	24%
Midwest	12	12	13
South (including Puerto Rico)	25	25	25

West	16	15	14
Subtotal	76	76	76
Canada	10	11	11
Europe	14	13	13
Total	100%	100%	100%

The chart shows us that the large number of stores located in California does not contribute much to the total sales revenue. Therefore if TJX is considering expansion in domestic market, I recommend the company to have more stores in Northeast or South where the large amount of revenue is expected. The company should focus more on such states as New York, Texas, Florida and Pennsylvania where population size is large and population density is relatively high. In this way, TJX will be able to maximize its profit in the limited number of stores.

State Population by Rank, 2014

Rank	State	July 2014 population
1.	California	38,802,500
2.	Texas	26,956,958
3.	Florida	19,893,297
4.	New York	19,746,227
5.	Illinois	12,880,580
6.	Pennsylvania	12,787,209

Source: U.S Census Bureau, Population Division

Subsidiaries

TJX has several subsidiaries including T.J Maxx, Marshalls, HomeGoods and Sierra Trading Post. All those subsidiaries are retailers that differ themselves by product assortment. Over 60% of total revenue comes from Marmaxx and revenue from

HomeGoods and Sierra Trading Post is minimal. There would be an opinion that the company should focus on its main business. However, HomeGoods had continuous increase in profits and showed growth potential in the future.

Earnings of HomeGoods

Dollars in millions	Fiscal Year Ended		
	January 31, 2015	February 1, 2014	February 2, 2013
Net sales	\$ 3,414.4	\$2,993.7	\$2,657.1
Segment profit	\$ 463.2	\$ 386.5	\$ 324.6
Segment profit as a percentage of net sales	13.6%	12.9%	12.2%
Increase in same store sales	7%	7%	7%
Stores in operation at end of period	487	450	415
Selling square footage at end of period (in thousands)	9,537	8,865	8,210

Diversifying business is important in the sense that HomeGoods can make up the losses when demand for fashion apparel is low at a certain period. Additionally there is an advantage of having subsidiaries of same kind. They can share distribution infrastructure such as storage and shipping method so that they can spread fixed cost to a larger number of units and reduce cost of goods. For those reasons, I recommend the company to keep operating all its subsidiaries.

Global Expansion and E-commerce

As mentioned in SWOT Analysis section, TJX has huge opportunity to expand its business in global market. Particularly, TJX Europe has shown a good performance for years.

Earnings of TJX Europe

U.S. Dollars in millions	Fiscal Year Ended		
	January 31, 2015	February 1, 2014	February 2, 2013
Net sales	\$ 4,092.3	\$3,621.6	\$3,283.9
Segment profit	\$ 337.4	\$ 275.5	\$ 215.7
Segment profit as a percentage of net sales	8.2%	7.6%	6.6%

Increase in same store sales	3%	6%	10%
Stores in operation at end of period			
T.K. Maxx	407	371	343
HomeSense	33	28	24
Total	440	399	367
Selling square footage at end of period (in thousands)			
T.K. Maxx	9,109	8,383	7,830
HomeSense	545	464	411
Total	9,654	8,847	8,241

With 440 stores, TJX Europe operates in only four of the European countries: U.K, Ireland, Germany and Poland but still had a decent result. If the company can expand its business to a larger region in Europe, it may earn a higher revenue. Having stores in several regions can also reduce the country specific risk regarding political and economic issues.

E-commerce business has the largest potential. Although its earning is very minimal compared to the earnings from offline segment, there will be more and more demand for online shopping in the near future. The important thing is that the website should provide user friendly interface where customers can have access to all the products that TJX stores are having. With the online segment, the company can reach to the customers who cannot visit the offline stores.