

# Dollar Tree, Inc.

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April 2019



**Michael Zhu**

**Will Smith**

# Company Background

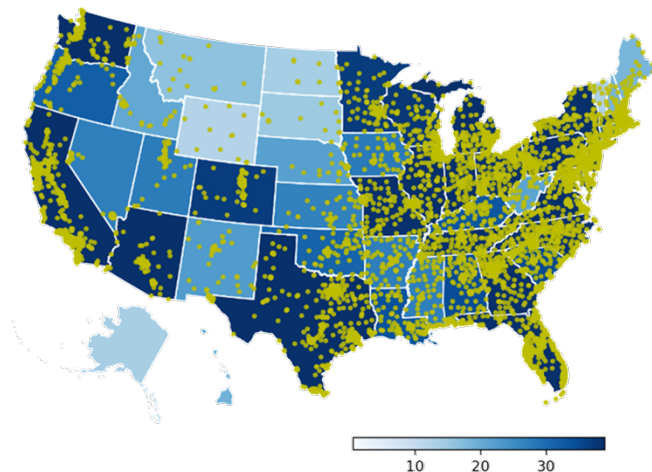
## Company Overview

- Dollar Tree, Inc. operates discount retail stores under the brand names Dollar Tree, Dollar Tree Canada, and Family Dollar
- Closed acquisition of Family Dollar for ~\$9.4 billion on July 6, 2015
- Led by Executive Chairman Bob Sasser and Chief Executive Officer Gary Philbin
- Operates more than 15,000 retail locations in 48 states and 5 Canadian provinces
  - 7,001 Dollar Tree stores
  - 8,236 Family Dollar stores
  - 225 Dollar Tree Canada stores
- Dollar Tree offers merchandise at a fixed price point of \$1 while the Family Dollar prices generally range from \$1 - \$10

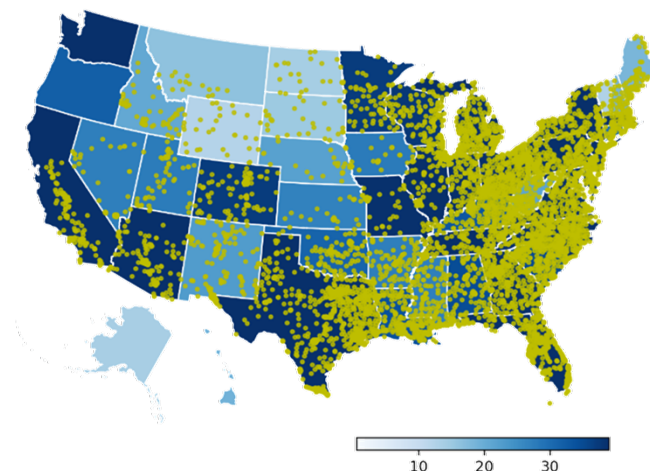
## Key Trading Statistics

Ticker	DLTR
Date	4/5/2019
Price	105.99
Market Cap	25.25B
52 Week High	106.90
52 Week Low	78.78
Adjusted EPS	5.45
P/E Ratio	19.4x
EV/EBITDA	12.0x
Beta	0.54

## Dollar Tree Locations



## Family Dollar Locations



Family Dollar  
Struggles

The market has grown weary of Family Dollar's struggles and is currently ascribing little value to that segment

Activist Investors

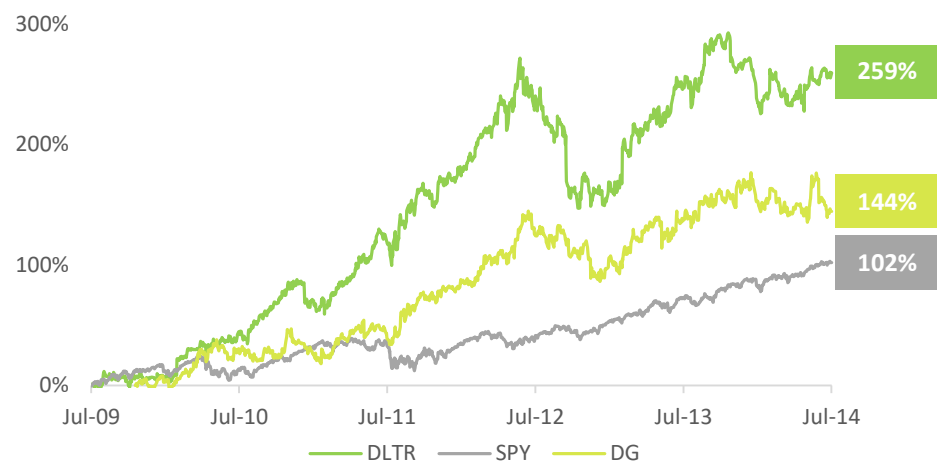
Given recent activist involvement, Dollar Tree will be forced to either turn around Family Dollar and become more profitable, spinoff the segment, or sell it to a private equity firm or strategic buyer – all of these options would create significant shareholder value

Unique  
Resistance to E-  
Commerce

Investors have been worried about the effects of e-commerce on the retail industry, but Dollar Tree is uniquely insulated from this threat compared to other retailers due to the nature of their products and customer base

# Recent Stock Performance

## 5 Years Prior to the Merger<sup>1</sup>

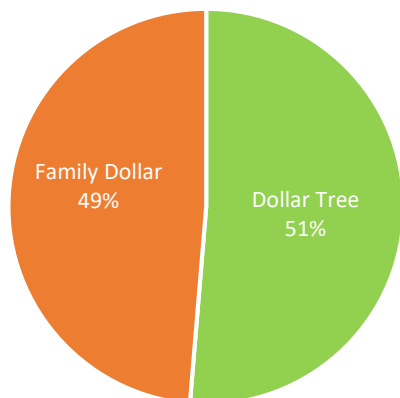


## Since the Acquisition of Family Dollar<sup>2</sup>

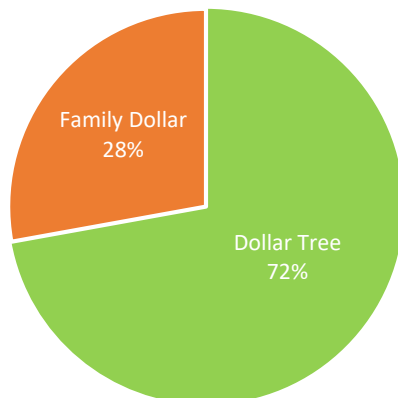


## Segment Breakdown

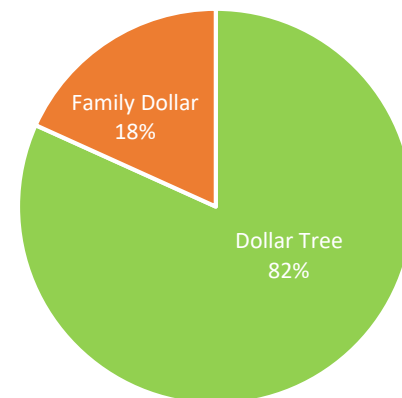
### Revenue



### EBITDA



### Operating Profit (EBIT)<sup>3</sup>



Source: Company filings, Yahoo Finance

<sup>1</sup> DLTR adjusted for "2 for 1" stock split on June 27, 2012; adjusted for "3 for 2" stock split on June 25, 2010 4

<sup>2</sup> Closed acquisition of Family Dollar on July 6, 2015

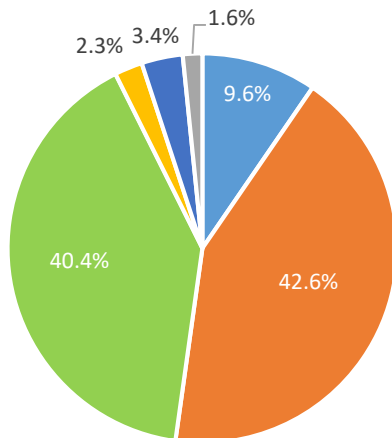
<sup>3</sup> EBIT breakdown based on FY'2018 adjusted operating profit

# Deep Discount” Retail Industry

## Industry Overview

- Demand is driven by consumer spending, primarily among lower-to-middle class consumers
- “Deep discount” retailers provide a less diverse merchandise mix but are able to offer their products at a much steeper discount
- Consistently outperformed department retailers in recent years and tends to perform significantly better through economic downturns
- Dollar Tree and Dollar General represented two-thirds of all new stores in “food deserts” in 2015 and continue to undercut smaller independent grocery stores

## Market Share



■ Big Lots, Inc: BIG   
 ■ Dollar General: DG   
 ■ Dollar Tree: DLTR  
■ Five Below: FIVE   
 ■ Fred's: FRED   
 ■ Ollie's: OLLI

## Recent Retail Bankruptcies

JCPenney

claire's

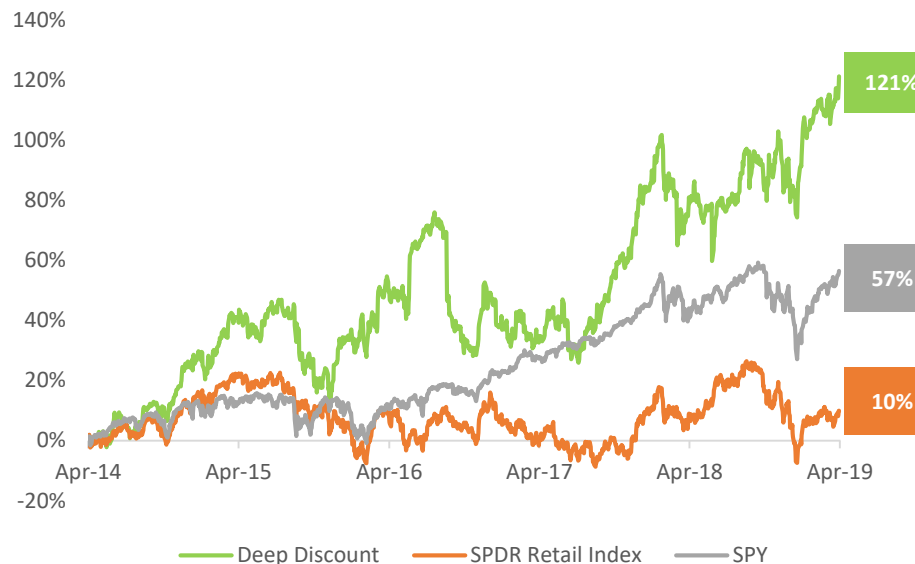
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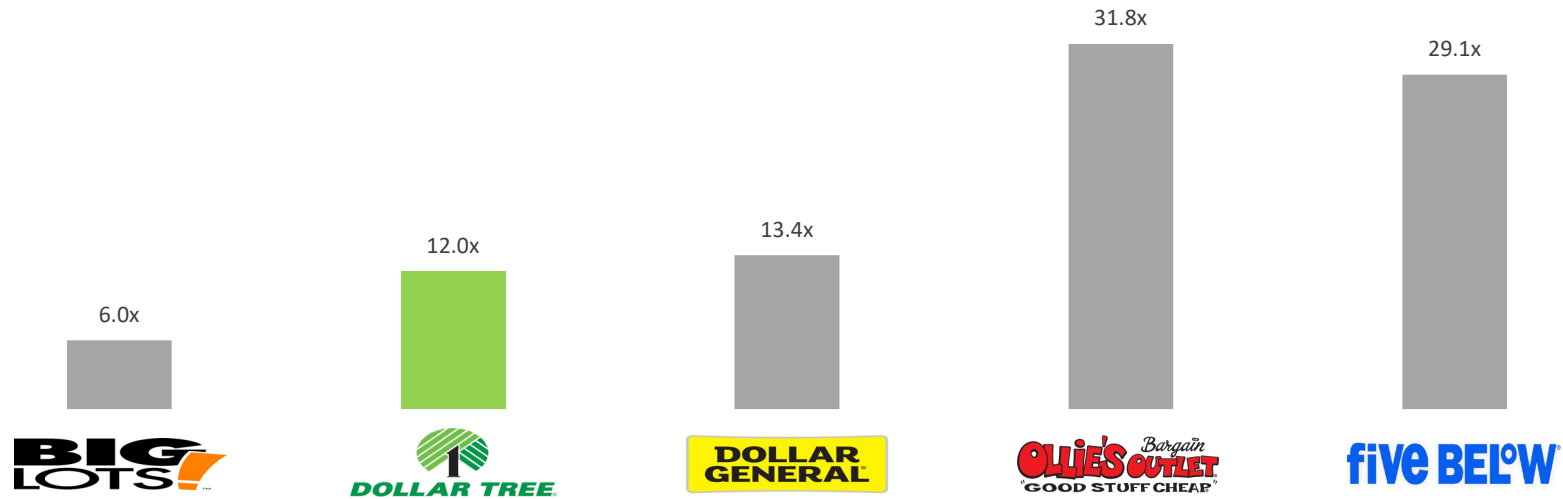
SEARS

## 5-Yr. Industry Returns

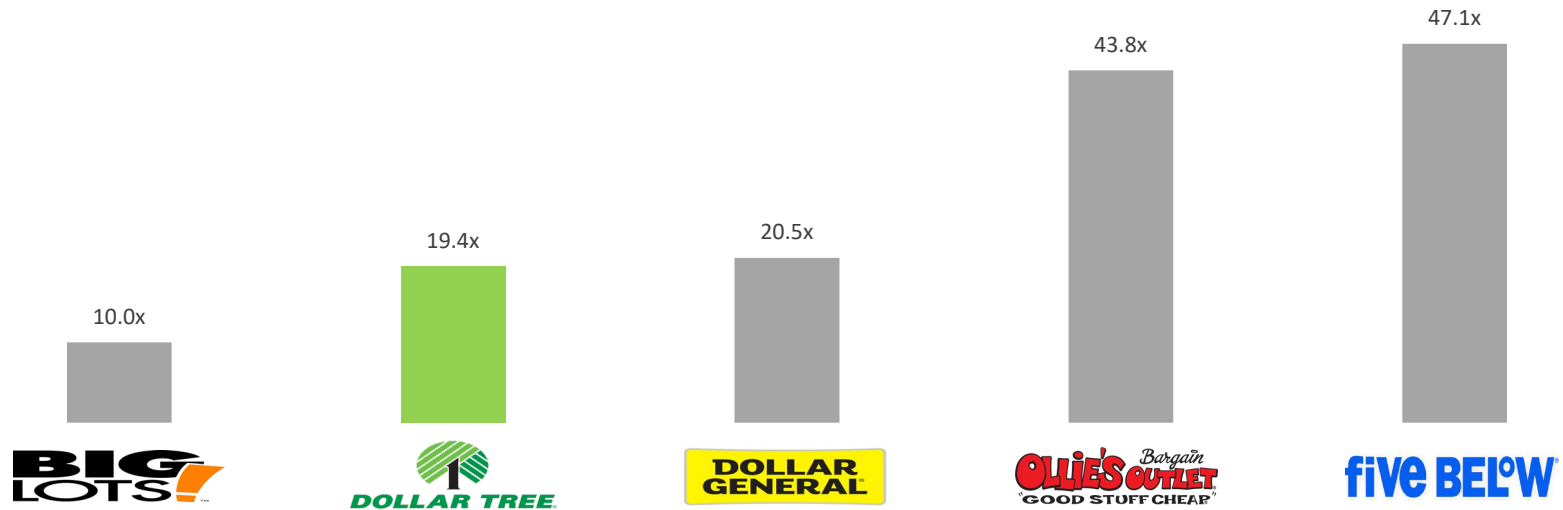


# Comparable Company Analysis

## TEV / LTM EBITDA



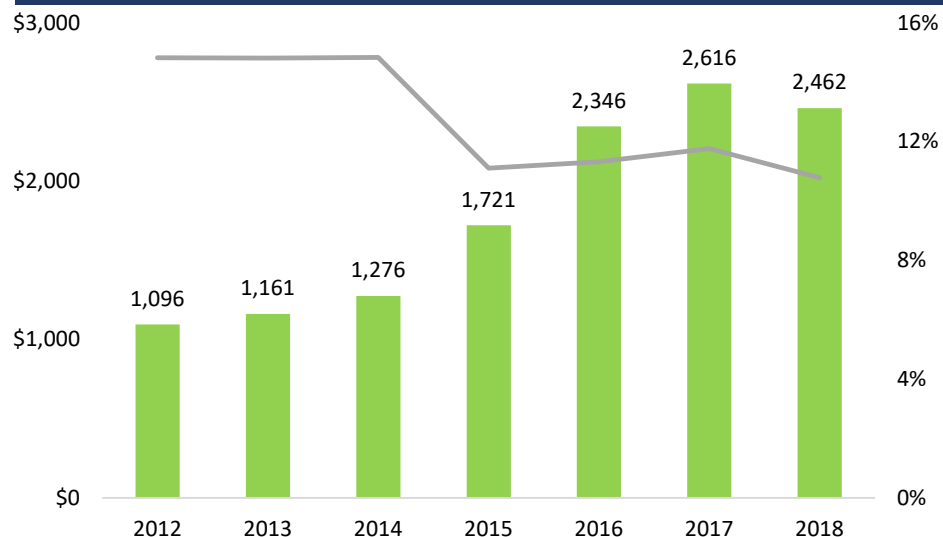
## Price / LTM EPS



## Revenue



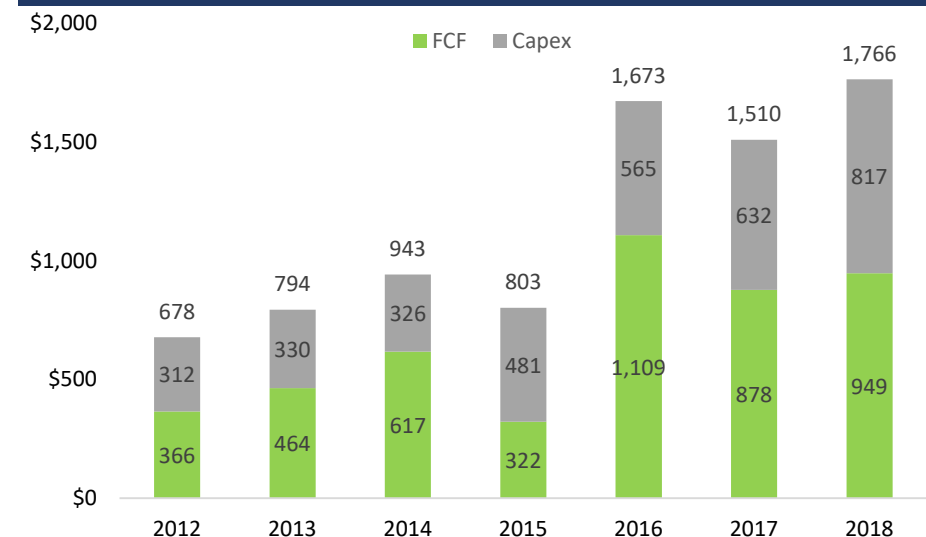
## EBITDA Growth & Margins<sup>1</sup>



## Operating Income Growth & Margins



## Free Cash Flow<sup>2</sup>



Source: Capital IQ, Company Filings

<sup>1</sup> Based on FY'2018 adjusted operating profit

<sup>2</sup> Free cash flow defined as operating cash flow less capex

# Intrinsic Valuation

## Financial Projections

(in millions USD)

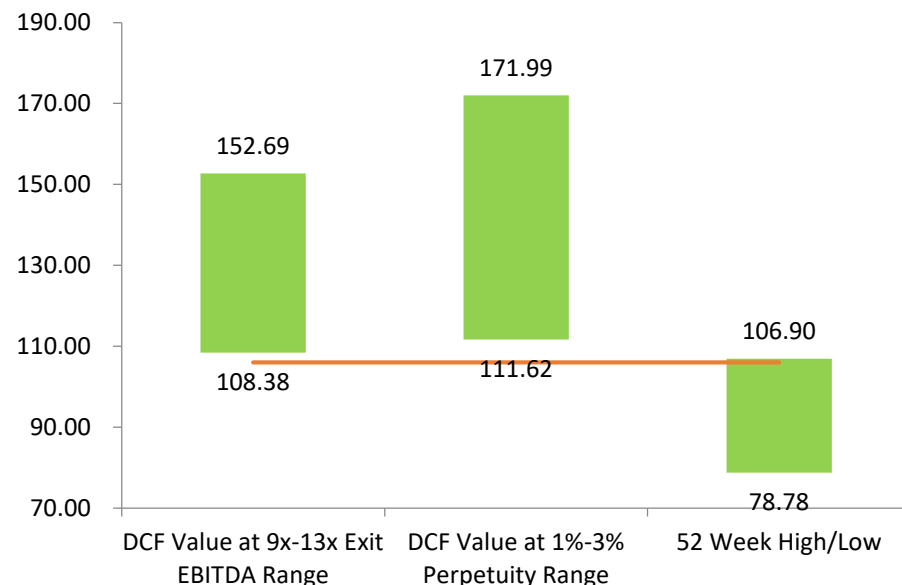
Fiscal year	2016A	2017A	2018A	2019P	2020P	2021P	2022P	2023P
Revenue	20,719	22,246	22,823	23,770	24,833	26,020	27,340	28,804
<i>Revenue growth</i>	33.7%	7.4%	2.6%	4.2%	4.5%	4.8%	5.1%	5.4%
<b>Gross Profit</b>	<b>6,395</b>	<b>7,022</b>	<b>6,948</b>	<b>7,393</b>	<b>7,773</b>	<b>8,198</b>	<b>8,700</b>	<b>9,252</b>
<i>Gross margin</i>	30.9%	31.6%	30.4%	31.1%	31.3%	31.5%	31.8%	32.1%
<b>EBIT</b>	<b>1,705</b>	<b>1,999</b>	<b>1,841</b>	<b>1,997</b>	<b>2,086</b>	<b>2,239</b>	<b>2,439</b>	<b>2,655</b>
Less: taxes	(433)	10	(282)	(381)	(403)	(440)	(483)	(529)
Add: Depreciation and amortization	693	627	621	698	734	811	898	997
Add: Stock based compensation	62	66	63	65	68	71	75	78
Less: Change in net working capital	23	(896)	(226)	(40)	(105)	(117)	(127)	(141)
Less: Capital expenditures	(565)	(632)	(817)	(1,000)	(993)	(1,041)	(1,094)	(1,152)
<b>Unlevered Free Cash Flow</b>	<b>1,484</b>	<b>1,173</b>	<b>1,200</b>	<b>1,340</b>	<b>1,387</b>	<b>1,524</b>	<b>1,708</b>	<b>1,909</b>

## Inputs & Results

Cost of debt	4.3%
Cost of equity	6.6%
We	85.3%
Wd	14.7%
WACC	6.1%
Exit EV / EBITDA Multiple	12.0x
Perpetuity growth rate	2.0%

	Perpetuity	EBITDA
Enterprise value	41,464	39,055
Less: Net debt	4,336	4,336
<b>Equity value</b>	<b>37,128</b>	<b>34,719</b>
Diluted shares	238.90	238.90
<b>Equity value per share</b>	<b>\$155.41</b>	<b>\$145.33</b>
<i>Market premium / (discount) to fair value</i>	(31.8%)	(27.1%)

## Valuation Summary

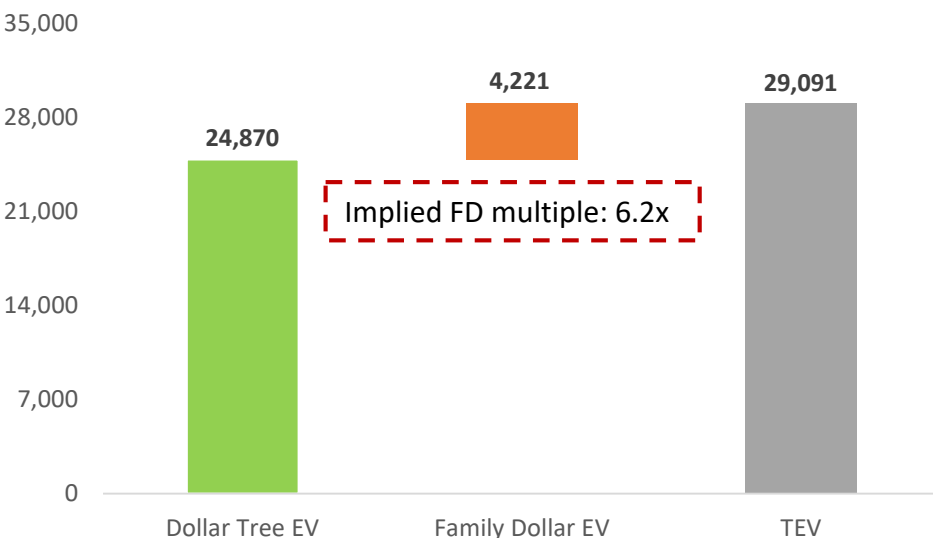




## Commentary

- While most investors view Family Dollar as an anchor that is weighing down on Dollar Tree's stock, we view it as a growth opportunity
- Recent renovations have shown comparable sales growth in excess of 10%, indicating that management is executing well on their strategy
- Although the segment is currently underperforming, it still maintains a healthy cash flow profile, making it an attractive buyout opportunity for a private equity firm
- We believe a large private equity fund would be able to pay upwards of 12.1x LTM EBITDA for Family Dollar, which is almost double its current implied multiple of 6.2x

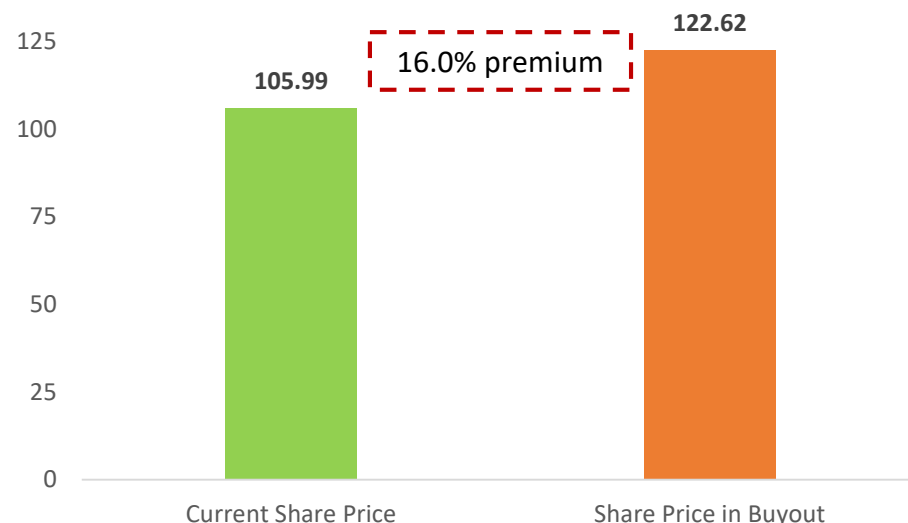
## Sum of Parts Valuation<sup>1</sup>



## Leveraged Buyout Analysis

Terminal EBITDA	\$1,574
Exit Multiple	10.0x
Enterprise Value	\$15,739
Less: Net Debt	(2,618)
Equity Value	\$13,121
Sponsor Ownership at Exit	90.0%
Sponsor Equity Value at Exit	\$11,809
Sponsor Required IRR	25.0%
Sponsor Equity at Closing	3,869
Net Debt at Closing	4,456
Implied TEV at Closing	8,325
LTM EBITDA	686
<b>Implied EV / EBITDA</b>	<b>12.1x</b>

## Buyout Stock Price Premium



## Background

- Carl Icahn disclosed a “significant” stake in DLTR in October 2018 then exited the position in January
- Jana Capital Partners and Corvex Management both disclosed a stake in DLTR in November 2018
- Starboard Value disclosed a 1.7% stake in DLTR in January 2019
  - Expressed intent to change DLTR’s \$1 pricing strategy, consider the sale of Family Dollar, and replace members of the board
  - Dropped proxy fight in early April because it has been pleased with the progress on key initiatives
  - Management announced intentions to perform a significant test of multiple price points at Dollar Tree stores

## Activist Initiatives

Accelerate Family Dollar renovations

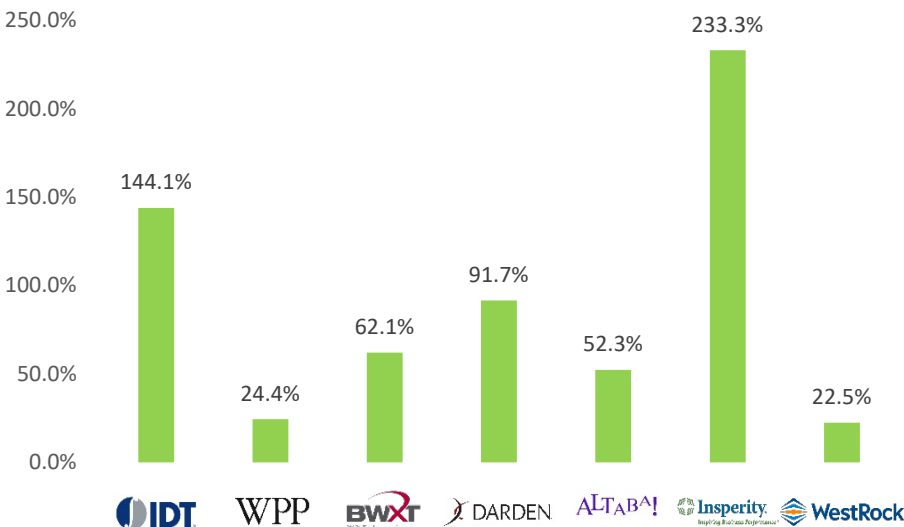
Change Dollar Tree’s \$1 pricing strategy

Explore a sale of the Family Dollar segment

Improve operational efficiencies and margins

Take control of board seats to hold management accountable

## 3-Yr. Returns after Starboard Involvement



## Select Case Studies



Jana announced a 10% stake in Petsmart in 2014 and pushed a sale months later for \$8.7B



Corvex accumulated a stake in Yum! Brands in 2015 and successfully split Yum! Brands and Yum! China



Starboard replaced the entire board of Darden and set changes to improve food quality, diner experiences, and kitchen operations

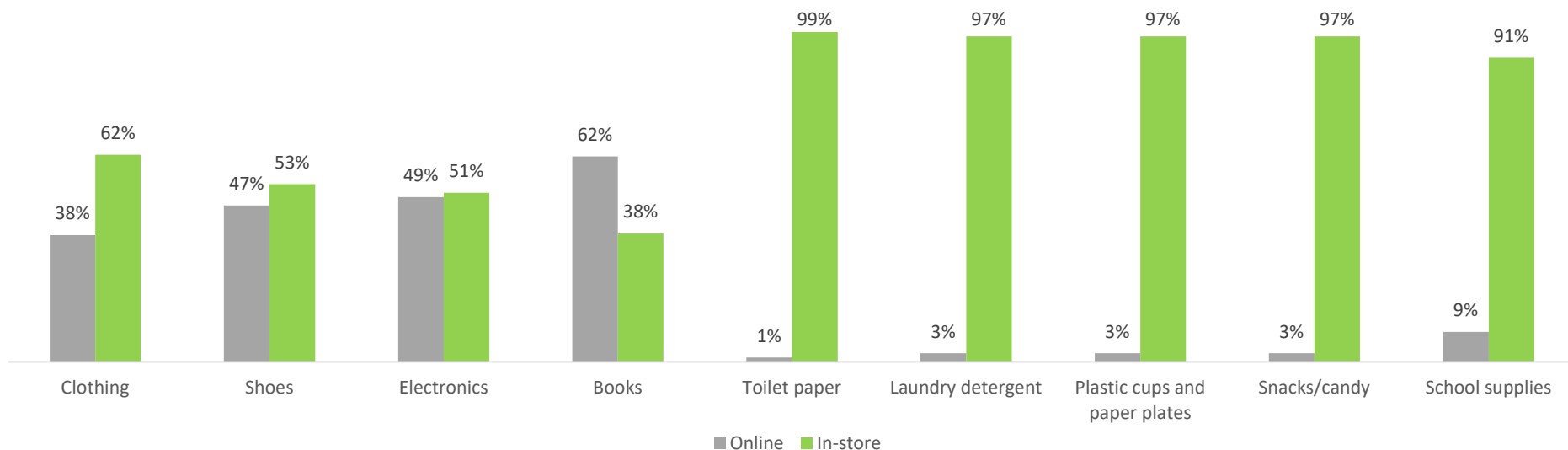
## Commentary

- Based on our customer survey, online shopping is increasingly competitive for infrequent purchases, but most people still visit a store for daily consumer goods
- The most popular items at Dollar Tree are generally unaffected by e-commerce
- Average ticket sizes at Dollar Tree and Family Dollar are much smaller than traditional retailers, making them less vulnerable to e-commerce disruption
- Investors have been concerned about Amazon's entry into the retail space, but they are not a near to medium term threat to deep discount retailers, such as Dollar Tree and Family Dollar

## Consumer Spending Per Trip



## Customer Survey<sup>1</sup>



## Investment Thesis

- ✓ Our group has assigned a **Strong Buy** rating on DLTR stock
- ✓ While investors and analysts have many concerns with Dollar Tree, deeper digging reveals that many of these concerns have been overblown and could even serve as catalysts for further growth for the company
- ✓ The below are areas where we believe investors and analysts have been misguided:
  - ✓ **Family Dollar Struggles** – The market has grown weary of Family Dollar’s struggles, and is currently ascribing little value to that segment
  - ✓ **Activist Investors** – Given recent activist involvement, Dollar Tree will be forced to either turn around Family Dollar and become more profitable, spinoff the segment, or sell it to a private equity firm or strategic buyer – all of these options would create significant shareholder value
  - ✓ **Unique Resistance to E-Commerce** – Investors have been worried about the effect of e-commerce on the retail industry, but Dollar Tree is uniquely insulated to this threat compared to other retailers due to the nature of their products and customer base
- ✓ As Dollar Tree management and activist investors execute a strategic turnaround or potential sale of the lagging Family Dollar segment, we believe the market will react positively, and Dollar Tree will begin to trade at a multiple that reflects their status as a leader in the retail industry

# Appendix

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# DLTR Stock Trends with Retail

## DLTR stock performance vs. SPDR Retail Index



# Credit Analysis

## Long-term Debt

Tranches	As of February 2, 2019		
	Principal	Interest rate	Maturity
\$1.25 Billion Revolving Credit Facility	0.0	L + 1.125%	NA
Senior Note	300.0	5.00%	2021
Senior Floating Rate Note	750.0	L + 0.70%	2020
Senior Note	1,000.0	3.70%	2023
Senior Note	1,000.0	4.00%	2025
Senior Note	1,250.0	4.20%	2028
<b>Total Long-term Debt</b>	<b>4,300.0</b>		






## Leverage Metrics

Debt / EBITDA	1.75x
Net Debt / EBITDA	1.55x
EBITDA / Interest	11.48x

**“As a result of our successful progress with integration and free cash flow in excess of investment needs, we expect to pay down our variable rate outstanding debt” – CEO, Gary Philbin**



# Operating Comparables

Company	Ticker	Operating Statistics (5 Year Avg.)			Profitability (5 Year Avg.)		
		Sales Growth (%)	EPS Growth (%)	EBITDA Margin (%)	ROA (%)	ROE (%)	ROIC (%)
<b>Deep Discount Retailers</b>							
	DLTR	5.9%	21.9%	12.7%	13.2%	27.5%	18.3%
	DG	7.9%	14.6%	11.2%	10.6%	22.0%	14.2%
	BIG	0.2%	6.8%	6.9%	9.4%	20.9%	18.6%
	FIVE	25.0%	NA	13.9%	16.7%	29.1%	27.3%
	OLLI <sup>1</sup>	14.8%	37.4%	12.1%	6.1%	10.3%	7.5%

# Balance Sheet Comparables



**DLTR**

**DG**

**BIG**

**FIVE**

**OLLI**

**Total Cash**

\$422

\$236

\$46

\$252

\$52

**Net PPE**

\$3,445

\$2,971

\$822

\$301

\$119

**Total Debt**

\$4,265

\$2,853

\$374

\$0

\$0

**Current Ratio**

2.0x

1.5x

1.8x

2.5x

2.4x

**Quick Ratio**

0.2x

0.1x

0.1x

1.3x

0.3x

**Debt / Equity Ratio**

75.6%

44.6%

74.8%

0.0%

0.1%

**Debt / EBITDA**

1.8x

1.1x

1.5x

0.0x

0.0x

**Net Income Margin**

(7.0%)

6.2%

3.0%

9.6%

10.9%

