

## Guess?, Inc. (GES)

**Analyst:** David Itoafa  
**Sector:** Clothing Retail

**Buy**

Price Target: \$15.77

### Key Statistics as of 12/09/2016

Market Price: \$13.89  
Market Cap: 1.17 Billion  
52-Week Range: 12.90- 22.84  
Beta: 1.13

### Catalysts:

- **Short-term (within 3 months):** Next Earning Call.
- **Mid-term (1 to 2 years):** Ability to Expand in Asian Market.
- **Long-term( over 2 years):** Retail Sector Recovery or Demise due to Online Sales

### Company Description:

Guess?, Inc. specializes in marketing, design, licensing, and distribution of fashionable attire and accessories for women, children and men. The business operates in North America Retail, Wholesale, and Licensing. Other segments of the business consist of European and Asian Wholesale and Licensing. Their product lines comprise of full collections of clothing like jeans, pants, dresses, blouses, shirts, jackets, knitwear, and intimate apparel. The company was originally established by Pail and Maurice Marciano in 1981. Their headquarters is in Los Angeles and although the company has had its ups and downs, it has been a staple in the clothing and retail game since its creation.



## Thesis

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- Due to online shopping surging for the holidays; Guess will beat analysts' expectations for the next quarter.
- The company continues to expand and capture the Asian market, which will help them counteract the American struggle in long run
- Operating Costs will decrease due to their plans to shrink the amount of stores in the US.

## Porter Five Forces

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### Bargaining Power Of Suppliers:

In terms of clothing and retail it is very easier for suppliers to vary prices because they generally produce the fabrics for a very minimal price. However, big brands that have been in the industry for a while like Guess have relationships to keep the bargaining power low. This means that they can keep reasonable pricing with their suppliers and in their specific case it is fairly low. Since this industry is currently recovering from a sort of recession this does however give the supplier more bargaining power since they are doing their part and companies like guess are struggling with sales of clothing.

### Bargaining Power Of Customer

Customers do have a substantial amount of power in this industry because if a large number of people stop buying their clothing the prices will have to diminish or companies like Guess will have to close stores. Currently bargaining power is very high because there are so many various brands out on the market that have been a long for a substantial amount of time. Certain customers do become attached to certain brands. For Instance, many American's in the state of Massachusetts will only wear Clothing from companies like Vineyard Vines no matter how high the price for the clothing will rise too. Therefore, bargaining power of customers is fairly mediocre since there are a lot of various companies that could sell their products for very cheap, but there is also brand loyalty.

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### Intensity of Existing Rivalry

Retail clothing has a substantial amount of Intensity of existing rivalry because the majority of competitors have been in the game for over 30 years. There are a lot of stores and certain marketing strategies could positively or negatively affect each customer's impulse to buy a product. If they can't find anything they desire at one store they can always find an appealing deal at another. Therefore, since consumer spending has been high quality brands like Guess have struggled to capture market share and customers because there products are higher quality and highly priced. Also, there is a fairly low industry growth rate and a fairly substantial amount of storage costs in this industry.

### Threat Of Substitutes

When it comes to clothing in general there is a high threat of substitution because there are so many various companies offering clothing at various prices. If a customer is unsatisfied with a price, customer service, or quality they can easily find a replacement at a different store. However, when it comes to European apparel and style Guess is one of the only companies that specializes in this type of clothing allowing them a sort of product differentiation that has kept them afloat since their foundation. The problem that guess and many industry have had is dealing with competitors like Pac- Sun for instance that enable customers a substantially low cost of switching in a time where consumer spending has not been very high.

### Threat Of New Competitors

In this industry there is a very small probability that a startup will come into the market gain rapid market share and contest with big time players. Since the majority of clothing stores have been around for generations unless there is some sort of clothing that changes the game most companies will not be able to survive in this industry. It is not impossible and has been done before, but it is very risky because having a strong brand name that offers a customer confidence in a product is essential. It is also very important to have a strong

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distribution network in order to move goods around. GES has been along for a while and like many other companies have very strong distribution networks, which new competitors would have difficulty Establishing.

## Industry Outlook

Although retail clothing has struggled in reason year, the future looks very positive. According to the national retail federation job growth higher wages and other factors will boost consumer spending in the next year. Consumer confidence will remain high and will positively affect Guess in the future. Various companies are struggling with retail sales, which have been decreasing year over year for almost all companies in this sector. This is why revenue growth is not as influential determinant of the price, but Capex and Operating Expenses are the two major keys. GES like all of its competitors are cutting down on the number of retail stores in order to decrease operating costs. One of the main drivers for GES in the future, will be that the majority of their revenue comes from licensing and not retail. This means that even if we see a shrinkage of shopping in clothing retail in the near future contrary to the expected industry outlook, there are still somewhat protected. Since GES has a respected and high quality brand name there is a possibility of licensing their products to online clothing stores in the future as well. This would provide protection to these potential risks. Another speculative theory that will affect every business or person is the President Elect's tax cuts. Nobody knows exactly how much or which taxes he will cut until it is made final, but lower income taxes would enable more consumer shopping and possibly nicer margins for retail stores like GES. Although, one could argue that the corporate side of this has already been factored in the price, it would be difficult for the market to price exactly how much cutting income taxes would affect GES's revenue in the future.

## Emerging Markets in Asia

There is no hiding the fact that Guess has been struggling in the American Market for quite some time now as seen in their past 4 years of revenue data per country:

| In Millions of USD except Per Share | FY 2013        | FY 2014        | FY 2015        | FY 2016        |
|-------------------------------------|----------------|----------------|----------------|----------------|
| 12 Months Ending                    | 02/02/2013     | 02/01/2014     | 01/31/2015     | 01/30/2016     |
| Revenue                             | 2,658.6 100.0% | 2,569.8 100.0% | 2,417.7 100.0% | 2,204.3 100.0% |
| Rest of the World                   | 1,339.7 50.4%  | 1,316.9 51.2%  | 1,228.1 50.8%  | 1,080.2 49.0%  |
| US                                  | 1,028.5 38.7%  | 988.7 38.5%    | 951.1 39.3%    | 900.7 40.9%    |
| Canada                              | 290.3 10.9%    | 264.1 10.3%    | 238.4 9.9%     | 223.4 10.1%    |

Source: Bloomberg

Although all of these numbers are decreasing revenue in the US, which used to be one of the main generators has been decreasing at the fastest rate. Even in the last earnings call the CEO has warned investors that they have never been an American Company and it is not their main area of focus. The company had a lot of success in the US during in the 90's and 2000's because many Americans were very interested in European trends that GES provides. This made them substantial revenue in the past, but times change and so do people resulting in American's not being as attracted to GES products. This is the main reason why the company is at their lowest point in terms of share price. The most recent earning's call is showing much of the same in the US, but Europe and Asia are showing very positive signals.

- Americas Retail revenues decreased 4.7% in U.S. dollars and 4.6% in constant currency; retail U.S. dollars and 4.8% in constant currency.
- Europe revenues increased 16.4% in U.S. dollars and 16.8% in constant currency.
- Asia revenues increased 9.8% in U.S. dollars and 6.4% in constant currency.
- Americas Wholesale revenues decreased 4.3% in U.S. dollars and 2.2% in constant currency.
- Licensing revenues decreased 14.3% in U.S. dollars and constant currency.

Source: Q3 Earning's Call

European fashion will always do well in Europe, but one market that is finally opening up is in Asia where the company will focus on in the future. The main reason for this increase in revenue is that just as the US did in earlier years, Asian countries are becoming less traditional and more mainstream. Since GES is already positioned in this market they will be able to capture considerable market share as these trends start to pick up resulting in more revenue in the future along with nicer margins.

## Devil's Advocate

With every investment there are risks and there are macroeconomic factors that could hinder GES in the future potentially. If trade deals between China

And America under the new president fail GES stands to be negatively impacted. This is because if they look to move further into Asian Markets and the dollar strengthens as Asian currencies depreciate revenue and expenses will put GES in a very tough position. Moreover, if they do not do a good job of transitioning into in store mobile devices new loyalty programs, utilizing internet of things to enhance shopping experience the company could be in trouble. There has also been substantial controversy surrounding the company's ownership that could put them at risk. The majority of their management team is very old and in order to survive In the future they will need new blood to keep up with current trends. No company is perfect and GES does have certain elements that could negatively affect them in the future as well as some positives.

## Financials

Although the company is trading close to its 52 week low and does not look to be in the best position at this time short interest remains fairly low.



Source: Bloomberg

There is very high volume meaning the majority of people are buying into the company at this moment of time, but not shorting. Additionally, margins have been improving in Europe And US.

| In Millions of USD except Per Share | FY 2011    | FY 2012    | FY 2013    | FY 2014    | FY 2015    | FY 2016    |
|-------------------------------------|------------|------------|------------|------------|------------|------------|
| 12 Months Ending                    | 01/29/2011 | 01/28/2012 | 02/02/2013 | 02/01/2014 | 01/31/2015 | 01/30/2016 |
| Return on Common Equity             | 27.63      | 23.62      | 15.68      | 13.58      | 8.43       | 7.77       |
| Return on Assets                    | 18.90      | 15.94      | 10.85      | 8.82       | 5.62       | 5.21       |
| Return on Capital                   | 27.45      | 23.55      | 15.68      | 13.82      | 8.63       | 8.03       |
| Return on Invested Capital          | 26.60      | 23.45      | 15.53      | 13.07      | 7.79       | 8.03       |
| <b>Margins</b>                      |            |            |            |            |            |            |
| Gross Margin                        | 43.83      | 43.01      | 40.14      | 37.99      | 35.90      | 35.72      |
| EBITDA Margin                       | 18.98      | 17.73      | 13.70      | 12.10      | 8.73       | 8.71       |
| Operating Margin                    | 16.27      | 14.78      | 10.33      | 8.66       | 5.21       | 5.51       |
| <b>By Geographic Segments</b>       |            |            |            |            |            |            |
| Licensing                           | -          | -          | -          | -          | 91.10      | 88.70      |
| Wholesale                           | -          | -          | -          | -          | 20.40      | 18.40      |
| Europe                              | -          | -          | -          | -          | 8.00       | 7.60       |
| Asia                                | -          | -          | -          | -          | 2.90       | 4.30       |
| Retail                              | -          | -          | -          | -          | -1.30      | 1.70       |

Source: Bloomberg

Recent improvement in these sectors of their business will be very positive in the long run because in recent years as seen in historical data their competitors are blowing them out of the water in an industry that has pulled back.

|             | EBITDA Margin |      |
|-------------|---------------|------|
|             | History       | LFY  |
| GES         | 9.6%          | 3.7% |
| Competitors | 10.5%         | 7.2% |

The good news is that there is room for improvement in terms of profitability and reducing operating expenses in the future. This will enable the company to provide substantial returns in the future because no it isn't an industry leader, but does have potentially to grab the Asian market. Moreover, if retail recovers or GES is able to survive by switching to a more electronic and technologically advanced company. All financial ratios and analysis prove that this company is not an industry leader, but was once upon a time. They know what it takes to be on top and has to change very little in terms of operating expenses to make it an undervalued company.

## Conclusion

Currently the company is trading at its all-time lowest point because revenue is decreasing and operating expenses remain very high. The company is implementing some changes that even if slightly have a positive impact could offer a boost in the price. Closing down American stores and expanding seems to be the future of the company in order to survive and prosper. Although there are risks associated to this company there is a lot of room for improvement financially and the industry outlook does stand to help GES recover in the future.

- Point Of Entry: \$13-\$14
- Target Price: \$15.77
- Target Return: %15-20%
- Time Horizon: 1- 1.5 year's

**Guess?, Inc. (GES)**

**CENTER FOR GLOBAL FINANCIAL STUDIES**

**BULLISH**

Analysis by David Isaacs  
12/10/2016

Current Prices:  
Dividend Yield:

\$13.99  
6.9%

Intrinsic Value:  
Target Price:

\$14.98  
\$15.77

Target 1 year Return: 20.44%  
Probability of Price Increase: 7



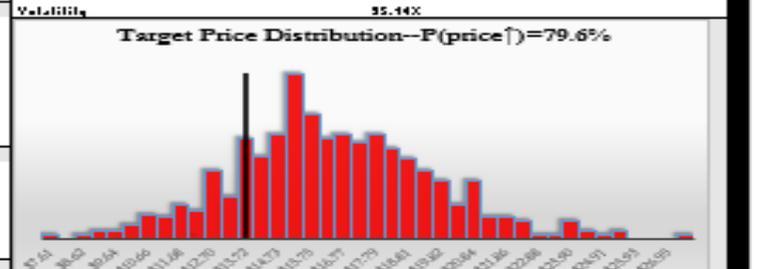
**Description**  
Guess?, Inc. designs, markets, distributes, and licenses lifestyle collections of contemporary apparel and accessories for men, women, and children that reflect the American lifestyle and European fashion sensibilities.

**General Information**  
Sector: Consumer Discretionary  
Industry: Specialty Retail  
Last Guidance: November 3, 2015  
Next earnings date: March 17, 2017  
Estimated Country Risk Premium: 3.48X  
Efficient Tax rate: 24X  
Efficient Operating Tax rate: 22X

| Market Data                          | Market Beta |
|--------------------------------------|-------------|
| Market Capitalization                | \$1,171.78  |
| Daily volume (mil)                   | 1.43        |
| Shares outstanding (mil)             | 84.96       |
| Diluted shares outstanding (mil)     | 83.75       |
| X shares held by institutions        | 74X         |
| X shares held by investment Managers | 58X         |
| X shares held by hedge funds         | 5X          |
| X shares held by insiders            | 27.52X      |
| Short interest                       | 3.43X       |
| Days to cover short interest         | 5.33        |
| 52 week high                         | \$22.84     |
| 52 week low                          | \$12.38     |
| Levered Beta                         | 0.78        |
| Volatility                           | 35.44X      |

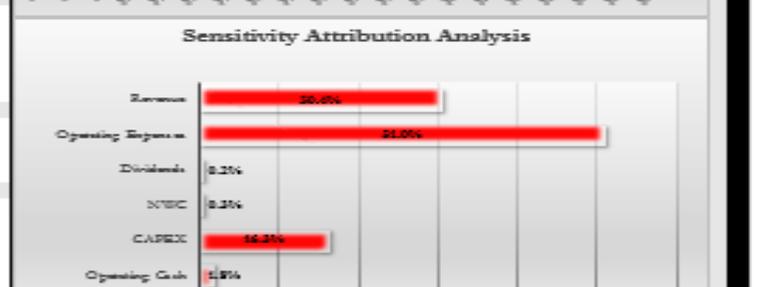
| Quarter ending | Revenue | EBITDA   |
|----------------|---------|----------|
| 10/24/2015     | -3.47X  | 7.24X    |
| 1/28/2016      | -3.33X  | -3.58X   |
| 4/28/2016      | -3.83X  | -294.83X |
| 7/28/2016      | -2.16X  | 12.33X   |
| 10/23/2016     | -4.55X  | -24.85X  |
| Mean           | -3.42X  | -61.64X  |
| Standard error | 1.4X    | 58.5X    |

| Position                       | Total compensation grant  | Total volume in shares/holders |
|--------------------------------|---------------------------|--------------------------------|
| Co-Founder, Executive Chairman | -5.14X per annum corr Eq  | -5.56X per annum corr Eq       |
| Chief Executive Officer and    | N/A                       | -22.47X per annum corr Eq      |
| Co-Founder and Chairman Emer   | -46.35X per annum corr Eq | -5.56X per annum corr Eq       |
| Chief Financial Officer and    | -5.5X per annum corr Eq   | -14.28X per annum corr Eq      |
| Vice President of Finance and  | N/A                       | N/A                            |
| General Counsel and Secretary  | N/A                       | N/A                            |



| Management          | Position                       | Total compensation grant  | Total volume in shares/holders |
|---------------------|--------------------------------|---------------------------|--------------------------------|
| Marciano, Paul      | Co-Founder, Executive Chairman | -5.14X per annum corr Eq  | -5.56X per annum corr Eq       |
| Marciano, Raige     | Chief Executive Officer and    | N/A                       | -22.47X per annum corr Eq      |
| Marciano, Maurer    | Co-Founder and Chairman Emer   | -46.35X per annum corr Eq | -5.56X per annum corr Eq       |
| Roddy, Sandeep      | Chief Financial Officer and    | -5.5X per annum corr Eq   | -14.28X per annum corr Eq      |
| Bracewells, Fabrice | Vice President of Finance and  | N/A                       | N/A                            |
| Miller, James       | General Counsel and Secretary  | N/A                       | N/A                            |

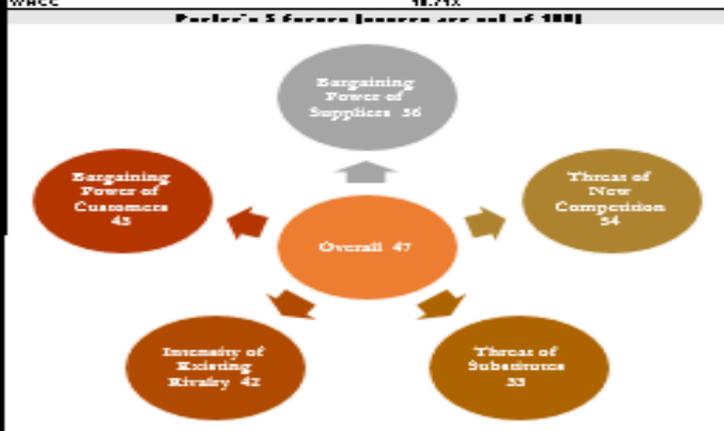
| Profitability               | GES [5 years historical as | Industry [LTM] |
|-----------------------------|----------------------------|----------------|
| ROIC                        | 5.5X                       | 14.87X         |
| MOPAT Margin                | 5X                         | 12.42X         |
| Revenue/Invested Capital    | 1.84                       | 1.83           |
| ROE                         | -1.6X                      | 8.14X          |
| Adjusted net margin         | -2X                        | 7.82X          |
| Revenue/Adjusted Book Value | 8.33                       | 1.84           |



| Balance Sheet                          | GES [LTM] | Industry [LTM] |
|--|-----------|----------------|
| Total Cash/Total Capital               | 15.3X     | 18.5X          |
| Estimated Operating Cash/Total Capital | 16.3X     | 18.4X          |
| Non-revolving Capital/Total Capital    | 16.3X     | 15.3X          |
| Levered Capital/Total Capital          | 33.2X     | 37.5X          |

| Capital Structure              | GES [5 years historical as | Industry [LTM] |
|--------------------------------|----------------------------|----------------|
| Total Debt/Common Equity [LTM] | 8.78                       | 1.44           |
| Cost of Existing Debt          | 23.54X                     | 23.48X         |
| Estimated Cost of New Debt     | 22.92X                     | 22.92X         |
| CGPS Risk Rating               | F                          | C              |
| Unlevered Beta [LTM]           | 0.55                       | 1.33           |
| WACC                           | 18.74X                     | 7.33X          |

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|--|----------------------------|----------------|
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| Non-revolving Capital/Total Capital    | 16.3X                      | 15.3X          |
| Levered Capital/Total Capital          | 33.2X                      | 37.5X          |



| Period         | Revenue growth | Value | ROIC/WACC |
|----------------|----------------|-------|-----------|
| Year Year      | -2.4X          | 5.2X  | 0.51      |
| 10/23/2017     | 1.8X           | 7.1X  | 0.67      |
| 10/23/2018     | 1.5X           | 12.8X | 1.36      |
| 10/23/2019     | 2.8X           | 12.5X | 0.88      |
| 10/23/2020     | 3.8X           | 13.3X | 0.52      |
| 10/23/2021     | 4.8X           | 14.8X | 0.33      |
| 10/23/2022     | 4.1X           | 14.6X | 1.04      |
| 10/23/2023     | 4.1X           | 14.6X | 1.04      |
| 10/23/2024     | 4.1X           | 14.4X | 1.02      |
| 10/23/2025     | 4.1X           | 14.5X | 1.04      |
| 10/23/2026     | 4.1X           | 14.5X | 1.04      |
| Cooling Period | 4.1X           | 14.5X | 1.04      |

| Period     | Revenue    | Value      | ROIC/WACC |
|------------|------------|------------|-----------|
| Year Year  | \$2,164.65 | \$826.82   | 0.51      |
| 10/23/2017 | \$2,192.37 | \$643.33   | 0.67      |
| 10/23/2018 | \$2,213.47 | \$1,451.42 | 1.36      |
| 10/23/2019 | \$2,147.88 | \$1,434.58 | 0.88      |
| 10/23/2020 | \$2,834.37 | \$1,343.71 | 0.52      |
| 10/23/2021 | \$2,845.25 | \$1,266.52 | 0.33      |
| 10/23/2022 | \$1,825.11 | \$1,281.36 | 1.04      |
| 10/23/2023 | \$2,733.42 | \$1,158.55 | 0.98      |
| 10/23/2024 | \$2,316.27 | \$1,875.31 | 0.98      |
| 10/23/2025 | \$2,374.31 | \$1,857.42 | 0.81      |
| 10/23/2026 | \$3,853.78 | \$1,853.31 | 0.88      |

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