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| **Company: Carmax** | Ticker: KMX Current Price: $58.05 | Industry: Consumer Discretionary | Sub Industry: Automotive Retail |
| Target Price: $68  Stop Loss: $46.44  52 Week High/ Low: $53.56-75.40 | TTM P/E: 19.98  Forward P/E: 16.56  EPS: $2.94 | Beta: 1.26  Credit Rating: --  Rating Outlook: -- | Market Cap: $11.72(B)  Avg Vol (12 Month): 1.9 mil  Dividend Yield: 0 |

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| **Company Background:** |
| CarMax, Inc. is the largest U.S. retailer of used cars. As of April 1, 2015, CarMax owned and operated 146 used car superstores. It also sells new vehicles at locations under franchise agreements with four new car manufacturers. The company provides financial services to customers through CarMax Auto Finance (CAF). The company's strategy is to overcome important sources of customer dissatisfaction with traditional auto retailers, while maximizing operating efficiencies. |
| **Industry Outlook:** |
| The industry is highly fragmented. While CarMax is the largest used auto retailer, it still represented only about 2% of the total late model used units sold. During the past few years, Internet marketing has taken on great significance for the used vehicle and vehicle financing markets. The outlook for this industry is positive. Many new and restyled vehicles, combined with updated in-vehicle technology and greater fuel efficiency, as well as more vehicles coming off leases, should also drive new vehicle sales. |
| **Investment Thesis:** |
| Automotive Retail has a #2 industry ranking in Value Line, with a great potential under the current market situation. CarMax has increased revenue and profitability at a remarkable rate and has a significantly higher operating margin compared with its competitors. In addition, CarMax stock is near the bottom of its 12-month trading range, but due to the better-than expected showing in the August quarter, it has a great appreciation potential. Also, its share repurchase grogram shows the confidence of the board, and this company is most probably undervalued. |
| **Investment Risks:** |
| * Rising investment in new facilities and ongoing share repurchases will likely limit capital available in other purposes, and also increase its debt ratio * Based on the EPS, KMX recently traded at a premium to the average of automobile retailers * Demand for and pricing of used vehicles could be weaker than analysts expect |
| **3-5 take away from last quarter investor call transcript:** |
| * Facing the new competitors, Carmax is trying to make sure its customers can do transactions from home. And its huge competitive advantage is the 50,000 selections of inventory, which can be searched by customers online; * Despite the gas prices are low, rates are low and employment is improving, the showroom traffic was stagnant. The CEO said it’s hard to explain it on a quarter to quarter basis, and maybe customers are more prepared before they show up, which is just as good as getting more traffic; * In terms of the pace of new stores opening, Carmax replied that they don’t want to accelerate the growth pace blindly, they are focused on making operational improvement in their existing stores; |

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| **Financial Performance:** | **Discounted Cash Flow** |
| |  |  |  |  |  |  |  | | --- | --- | --- | --- | --- | --- | --- | |  | 2012 | 2013 | 2014 | Q1-2015 | Q2-2015 | Q3-2015 | | Revenue | 10,003.60 | 10,962.82 | 12,574.30 | 3,750.20 | 3,599.19 | 3,405.23 | | Operating Profit | 700.16 | 732.60 | 829.65 | 282.90 | 258.28 | 219.71 | | Net Income | 413.80 | 434.28 | 492.59 | 169.65 | 154.52 | 130.05 | | Revenue Growth % | 11.45 | 9.59 | 14.70 | 13.26 | 10.90 | 15.77 | | EBITDA% | 7.83 | 7.55 | 7.41 | 8.27 | 7.97 | 7.31 | | Operating Profit % | 7.00 | 6.68 | 6.60 | 7.54 | 7.18 | 6.45 | | Net Income Margin | 4.14 | 3.96 | 3.92 | 4.52 | 4.29 | 3.82 | | D/E | 175.79 | 194.48 | 228.62 | 239.20 | 245.44 | 277.04 | | Interest Coverage | - | - | - | - | - | - | | EPS | 1.83 | 1.90 | 2.20 | 0.77 | 0.71 | 0.61 | | PE Ratio | 17.15 | 20.54 | 22.42 | 19.35 | 22.68 | 23.35 | | Current Ratio | 2.87 | 3.38 | 3.02 | 2.74 | 2.77 | 2.77 | | ROE | 16.85 | 15.26 | 15.55 | 16.10 | 16.20 | 17.11 | | ROA | 5.35 | 4.77 | 4.56 | 4.56 | 4.54 | 4.58 | | Dividend Per share | - | - | - | - | - | - | |  |  |  |  |  |  |  | |  |  |  |  |  |  |  | | |  |  |  | | --- | --- | --- | |  | 2001-14 | 2015-19 | | Avg Revenue growth | 11.56% | 11% | | Avg EBITDA Margin | 5.14% | 8% | | Avg Net Income Margin | 2.91% | 4% | | Avg Debt/Equity | 71.92% | 303.15% | | Avg Interest / EBITDA | 3.46% | 3.18% | | Cost of Debt | | 1.8% | | Tax Rate | | 38% | | Cost of Equity | | 11.1% | | WACC | | 7% | | Perpetuity Growth Rate (Terminal) | | 4.7% |   Analyst Opinion   |  |  |  | | --- | --- | --- | | Buy: 10 | Hold: 8 | Sell: 0 |  |  |  |  | | --- | --- | --- | |  | Rating | Target | | S&P Net Advantage | B+ | $68 | | Morning Star | 3 star | $63 | | Value Line | Timeliness2 | $80-120 | |

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| **Relative Valuation** | **Total Return** |
| |  |  |  |  |  |  |  | | --- | --- | --- | --- | --- | --- | --- | | FY2014 | PENSKE | AUTONATION | LITHIA | GROUP 1 | Industry | Company | | P/E | 14.30 | 15.27 | 16.35 | 12.42 | 27.89 | 19.80 | | P/B | 2.60 | 3.09 | 3.86 | 2.18 | 4.49 | 3.69 | | Dividend Yield | 2.12 | - | 0.62 | 0.91 | 0.37 | - | | PEG Ratio | 1.19 | 1.14 | 0.89 | 0.95 | 2.25 | 1.21 | | EPS | 3.50 | 4.05 | 6.69 | 6.03 | 6.97 | 2.99 | | Rev Growth (3 Yr) | 15.63 | 11.39 | 27.11 | 17.90 | 12.29 | 12.59 | | NI Growth (1 Yrs) | 16.24 | 11.27 | 25.67 | 73.00 | 16.05 | 11.46 | | Operating Margin | 3.24 | 4.25 | 3.49 | 3.45 | 9.58 | 7.44 | | Debt / Equity | 236.63 | 225.42 | 234.20 | 270.00 | 297.04 | 306.28 | | Market Cap | 4,549.73 | 7,068.52 | 3,037.94 | 2,113.28 | 8,568.83 | 11,716.35 | |  |  |  |  |  |  |  | |  |  |  |  |  |  |  | | |  |  |  |  | | --- | --- | --- | --- | |  | KMX | Sector | S&P 500 | | YTD | -11.73% | 14.03% | 3.92% | | Last 3 Years | 69.46% | 83.61% | 58.47% | | Last 5 Years | 89.52% | 148.97% | 95.90% |   **CSR Characteristics**   |  |  |  | | --- | --- | --- | |  | Company | Industry | | ESG Disclosure Score | 17.36 | 14.58 | | Governance Disclosure Score | 55.36 | 51.14 | | Social Disclosure Score | 19.30 | 14.04 | | Environmental Disclosure Score | -- | 5.94 | |