

# Ulta Beauty, Inc.

Exchange: NASDAQ | Ticker: ULTA | Target Price: \$291.00

Luke Greenley | Lead Analyst  
lgreenley@theowlfund.com | (610) 613-0219

Nathan Latimer | Associate Analyst  
nlatimer@theowlfund.com | (484) 868-6191

Fred Shub | Associate Analyst  
fshub@theowlfund.com | (215) 840-9391

## INVESTMENT THESIS

- ULTA stock became pressured following the 3Q'19 earnings report that disappointed investors following a moderation of store opening forecasts. The sell-off continued over the summer, when Amazon announced plans to enter the beauty products market. ULTA's sell off culminated with the 2Q'20 earnings release, when the Company reported a slight miss on revenue, EPS, and comparable store sales growth. Management also guided comp sales and earnings downward for the remainder of FY'20, reflecting industry-wide headwinds in the U.S. cosmetics market that are expected to persist through 2H'20.
- Overall, we understand the negative sentiment around 2Q'20 earnings and management's renewed outlook, however we believe the magnitude of the selloff is highly overblown. Management has cited U.S. cosmetics headwinds since FY'17, and has returned improved efficiency accordingly. We believe the ~30% correction has priced in lower expectations for FY'20, and an untouched long-term outlook reiterates our conviction in ULTA outperforming beauty retail peers and broader retail over the next 12-18 months.
- Looking forward, we expect product innovation supported by omni-channel expansion, coupled with growth in the Ultimate rewards membership program to drive ULTA stock. Further buoyed by supply chain efficiencies and a balance sheet free of debt, we are attracted to the Company's flexibility, further positioning ULTA to capitalize on the next cyclical upswing. ULTA is currently trading at a NTM P/E multiple of 20.1x, representing a 24.0% discount to its 1-year average of 25.0x. Going forward, we expect the aforementioned drivers to propel the stock to a fair value of ~\$291/share, representing a ~21% return from current levels.

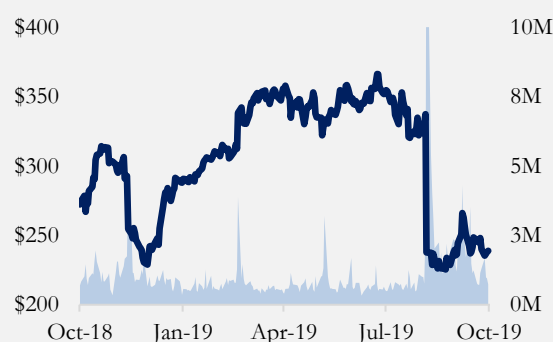
## COMPANY OVERVIEW

Ulta Beauty, Inc. (NASDAQ: ULTA) is the largest beauty retailer in the United States, offering 25k+ products and 500+ brands throughout retail stores, online, and mobile. ULTA offers a broad array of product categories, encapsulating the "All Things Beauty, In All One Place" slogan. ULTA reports revenue through one main segment, which includes sales from retail stores, salon services and eCommerce. The segment, titled Beauty & Cosmetics Retail, can be broken down into five sub-segments by product category. Geographically, all of the Company's revenue exposure is in the United States.

### Key Statistics (US\$ in M, except per share data)

Price (26-Oct)	\$240.90	52-Week Low	\$224.43
Exp. Return	21%	52-Week High	\$368.83
Shares O/S	58.8	Div. Yield	-
Market Cap	\$14,061	Ent. Value	\$15,529

### One-Year Price Graph



### Earnings (Adj.) / Revenue Surprise History

Quarters	EPS	Revenue	Δ Price
2Q'20	(1.28%)	(0.72%)	(29.55%)
1Q'20	6.54%	(0.18%)	1.50%
4Q'19	1.49%	0.72%	8.29%
3Q'19	1.62%	0.09%	(13.13%)

### Earnings Projections (Adj.)

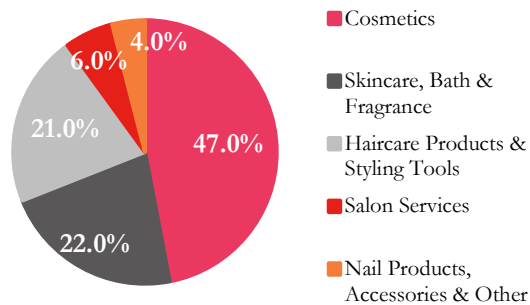
	Q1	Q2	Q3	Q4	FY
2018A	\$2.07	\$1.84	\$1.74	\$2.77	\$8.42
2019A	2.71	2.46	2.19	3.63	10.99
2020E	3.28	2.79	2.14	3.82	12.03
2021E	3.48	3.11	2.56	4.50	13.65

Source: Bloomberg, FactSet, CapIQ

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**ULTA BUSINESS OVERVIEW**

Ulta has one reportable segment, Beauty & Cosmetics Retail, which includes revenues generated from retail stores, salon services, and eCommerce functions. The segment can be broken down into five sub-segments:



**Cosmetics (47% of FY'19 Revenue)**

- This segment includes color cosmetics such as foundations, contouring & highlighting, eye shadows & liners, mascaras, lipsticks & balms, and makeup brushes & other tools. The ULTA business model of “All Things Beauty, In All One Place” is most prevalent in the Cosmetics sub-segment, as the company is the only retailer to offer color cosmetic products across all price ranges and categories across both mass-appeal groups and prestige niches.
- Increasing distribution points for well-known, iconic brands and retaining exclusive distribution for newer, innovative brands have contributed to sustained cosmetics growth. Notable brands within the segment include Kylie Cosmetics, Morphe x James Charles, Urban Decay, Kiehl’s and the Ulta Beauty Collection.

**Skincare, Bath & Fragrance (22% of FY'19 Revenue)**

- This segment includes lotions, cleansers, sunscreens, moisturizers, soaps, washes, and fragrances. Influenced by the substantial growth of health and wellness products and increasing penetration into the cosmetics space, skincare brands have seen strong sales over the past year and diversified ULTA’s sales.
- Significant recent releases within this sub-segment include the *Florence by Mills* skincare line Millie Bobby Brown, the *Kylie Cosmetics: Largely Lit* skincare line by Kylie Jenner, the *Thank U, Next* fragrance by Ariana Grande, and an exclusive fragrance from Jennifer Lopez.

**Haircare Products & Styling Tools (21% of FY'19 Revenue)**

- This segment includes shampoos & conditioners, hair irons & curlers, blow dryers, and other haircare products & tools. At an investor presentation late last month, ULTA management noted increasing market share gains in hair care that should work to further diversify revenue mix away from its traditional cosmetics business. Notable haircare brands sold at ULTA include Redken, Dyson, DryBar, and Matrix. Significant upcoming releases include *Pattern* by Tracee Ellis Ross.

**Salon Services (6% of FY'19 Revenue)**

- This segment includes one-on-one hair, skin, face and brow beauty consulting services with ULTA stylists. Haircuts, coloring, texturing and extensions are significant offerings within the segment. In addition, Salon Services offers beauty lessons and free skin consultations. Strong performance of salon services has contributed to the success of larger hair and skincare sub-segments, as stylists have converted service-only visits to purchases of products across multiple categories.
- Additionally, the improving salon experience has aided the development of an optimized experiential shopping environment at ULTA stores, which in turn has influenced expansion of membership programs and brand awareness across all product categories.

**Nail Products, Accessories, & Other (4% of FY'19 Revenue)**

- This segment includes nail polishes/kits, manicure & pedicure tools, hair extensions, hair clips, and jewelry. Additionally, the revenue breakdown by distribution channel is as follows: Retail (~84%), eCommerce (~11%), Salon Services (~4%), and Other Services (~1%). (Note: In the accompanying valuation workbook, we elected to model the Revenue Build by distribution channel).

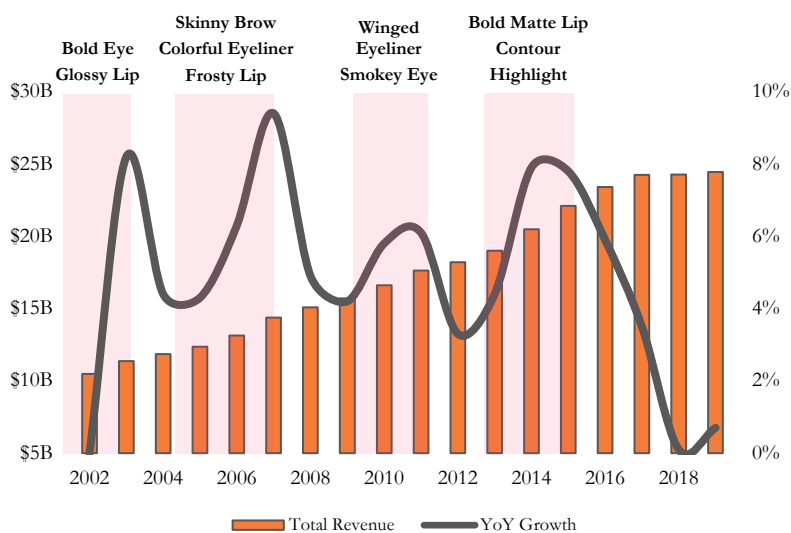
## INDUSTRY OVERVIEW

### Mass/Prestige Makeup

- **Mass:** Mass makeup is cheaper, “drug store” makeup found at stores like CVS, Rite-Aid, Target, and Ulta (on the inexpensive side). Brands include Covergirl, NYX, Maybelline, Neutrogena, Garnier, and L’Oréal.
- **Prestige:** Prestige makeup is higher quality makeup that used to only be available in drug stores. It can now be found in stores such as Ulta, Sephora, Blue Mercury, and boutiques. Brands in this category include Urban Decay, Too Faced, Bobbi Brown, and Lancôme. In 2018, the U.S. prestige beauty industry saw a 6% increase in sales YoY, driven by a 13% growth in skin care.
  - ULTA has honed in on a specialty retailing format incorporating prestige, mass, and salon products that were previously distributed through separate channels industry wide. With an unmatched breadth of product offerings, a bright and open store environment, and a captivating value proposition through the Ultimate Rewards program for the consumer, ULTA has truly differentiated itself from all other peers in the beauty and cosmetics market.
- Recently, the beauty markets experienced a slight uptick in high-end mass cosmetics. These are relatively high-quality cosmetics that are presented in a prestige style. The presentation of mass makeup in stores like ULTA is starting to change to reflect this shift. On the mass side, stores are now allowing brands to design their own fixtures and are not placing products as close together. **At ULTA, most customers shop in both categories, with only 23% of customers shopping one exclusively.**
- Due to lackluster innovation across the makeup industry, growth in both segments has slowed from recent highs, and ULTA management expects market headwinds to persist in the near term through 1H CY’20.

### Cosmetics Innovation Cycle and Revenue Diversification in Retail Cosmetics

- The cosmetics industry is a dynamic, trend-based and consumer-dictated market in which firms must capitalize on newness and innovation to succeed. While the U.S. beauty & cosmetics retail space has seen generally strong revenue growth since the early 2000’s (17-year CAGR of 4.8% through 2018), the ups and downs of the product innovation cycle drove YoY sales growth to as high as 9% and as low as 0%. The graph on the right shows periods of growth driven by industry-wide trends.



- To combat this volatility, firms have worked to diversify away from traditional color cosmetics into a product base with more predictable trends. Retailers have looked to capitalize on the growth of **health and wellness** initiatives by expanding into skincare and haircare products. According to the Global Wellness Institute, the personal care, beauty and anti-aging market reached a **TAM of ~\$1.1T** in 2017.
- The growth of **salon and beauty consultation services** within traditional cosmetics retail has provided another opportunity for revenue diversification. Cosmetics retailers have expanded hair, nail, skin, and other salon

services to attract more customers, drive incremental revenue and foot traffic, and increase average ticket sizes through upselling and experiential shopping techniques. To drive improved and more comprehensive services, firms have increased wage spending, and the industry-wide wages are expected to increase at an annualized rate of 1.1% through 2024. The volume growth in generally higher-margin service businesses have more than offset increases in operating cost for salon services in retail cosmetics, and profitability should increase as retailers continue to expand services and intertwine other parts of the business in salons. The salon industry represents a **TAM of ~\$59B**.

- Most recently, traditional cosmetics retail began a transition into eCommerce and omnichannel distribution to drive sales. In 2018, the 25 cosmetics retailers in Internet Retailer's Top 1000 list generated 4.9% of total sales exclusively on the web, representing a median annual growth rate of 22%. Despite this growth, beauty remains one of the only retail categories where brick-and-mortar retains strong spending for internet-savvy Generation Z consumers; according to a recent survey from Piper Jaffray, **~90% of American teenagers still prefer to purchase color cosmetics in stores**.
- While online sales are unlikely to ever overtake physical storefront revenue, we see a large potential for the growth of **omnichannel initiatives** through web-based marketing and **experiential shopping** to grow store traffic and topline far more effectively than online sales alone. **Multi-channel customers spend 4x more on average than single channel customers**. They also transact **9x more per annum** than brick-and-mortar only customers, compared to 2x more for online only customers.
- Additionally, almost every beauty/makeup company has implemented a form of **loyalty or rewards program**. Stores like ULTA and Sephora have entered a competition to offer the best reward for shopping at their stores. These initiatives are extremely successful, with over **95% of ULTA's sales** coming from rewards members. (*See Appendix Exhibit III for a detailed breakdown of the difference between Ulta's and Sephora's rewards programs.*)
- Whenever eCommerce penetrates an industry, Amazon is never far behind. Beauty retail has seen some disruption from the eCommerce giant's growing cosmetics business, but overall, brick-and-mortar remains the top dog for the foreseeable future. For reference, only 4% of female teens surveyed declared Amazon as their favorite beauty retailer. Brick-and-mortar retailers such as ULTA have deterred Amazon through developed rewards programs as well as a positive in-store buying experience.
- ULTA and other retailers have also increased partnerships with online indie brands, using their massive influence to attract them and preventing them from partnering with Amazon.

#### Get Off My Lawn Kids... And into Cosmetics Retailers

- Moving forward, positive demographic tailwinds will normalize some of the trend-driven variability in cosmetics retail revenue. By the end of this year, the combined Millennial and Generation Z population is projected to surpass Baby Boomers and represent 40% of the global consumer base by 2020. Additionally, total Millennial income is expected to reach \$8.3T by 2025, surpassing total income for Gen X and Baby Boomers combined.
- To better appeal to a younger demographic, beauty retailers have expanded their presence in the digital and social media space through collaborations with YouTube celebrities and millennial icons, as well as and strategic marketing initiatives across other social media platforms. In 2018, there were over ~170B beauty-related content views on YouTube. During the same period, 59% of Gen Z viewers and 49% of Millennials increased their usage of the site.
- Recently, the industry has seen sparks of innovation from primarily online retailers such as Glossier and Hims. These retailers are looking to overcome the try-before-buy hump and have inspired a wave of online-based "indie brands" that are quick to adopt even the smallest changes in trends. Larger stores such as ULTA have started partnering with these brands to offer their products in stores and drive innovation.

## UNDERVALUATION & THESIS:

- ULTA is currently trading at a NTM P/E multiple of 20.1x, representing a 24.0% discount to its 1-year average of 25.0x, as well as a 19.1% discount to its 2-year average. ULTA also trades at a 14.0% discount to its 1-year average EV/BEst EBITDA of 15.0x.
- **December 6, 2018:** ULTA stock began to face pressure following the 3Q'19 earnings report, in which the company reported stronger than expected revenue and earnings, on top of strong comparable store sales and membership growth. However, a weakened outlook for 4Q'19 due to higher than expected inventories overshadowed an otherwise strong earnings report. Additionally, management guided a narrower, more modest range for store openings throughout 2020 and 2021, to which investors reacted unfavorably. In response to the news, ULTA stock, partially caught up in a broad market selloff due to trade tensions and a weaker than expected jobs report, sold off by ~13%. The stock continued to fall with the market through December 24, where it bottomed ~25% off its recent highs.
- **June-July, 2019:** After a ~10% rally following 1Q'20 results, a tumultuous month for ULTA began at the end of June, as ULTA and peers faced downward pressure when a report surfaced detailing Amazon's entrance into the beauty space. Amazon's plans included store openings focused on the sale of products licensed by stylists, barbers and beauticians. ULTA sold off by ~4%, as investors were concerned that the beauty retailer would be the next victim in the Amazon-induced retail apocalypse. The stock, after a brief rally, once again sold off at the end of July when weak results out of Kylie Jenner's makeup business incited concern around the brand falling under ULTA's umbrella. Over the course of the month, compounded by fears of a currency war with China, ULTA suffered two sell offs upwards of ~9%.
- **August 29, 2019:** The bulk of ULTA's undervaluation is sourced from late August, when the Company reported 2Q'20 results. In terms of numbers, revenue and earnings missed analyst estimates by 1% each, while comparable sales growth of 6.2% fell short of expectations of 6.6%. Guidance for the quarter also came in soft, as CEO Mary Dillon noted industry-wide headwinds in the U.S. cosmetics market. The concerns that were cited regarding the market revolved around a lack of beauty innovation in the space to spur sales of ancillary beauty tools and products. This is a trend that ULTA management has been ahead of since FY'18, when prestige and mass cosmetics first began to show signs of deceleration. Now that ULTA finds itself in the late stages of the 2-3 year beauty product cycle, the Company expects challenges in the market to persist through 2H'20, before reaccelerating thereafter. Revenue growth expectations of +10.5% YoY for the remainder of the year fell below previous expectations of LDD growth, while earnings guidance was also cut to ~\$11.96 at the midpoint from a previous estimate of ~\$12.92. Finally, comparable sales growth guidance of ~5% YoY also marked a step down from previous guidance of ~6.5% YoY. In response to the report, ULTA stock plummeted ~30%.
  - **While the 2Q'19 earnings report was by and large a negative release and warranted a sell-off, we believe the magnitude of the selloff is extremely overblown.** We believe that there was also a significant amount of positive developments that investors are overlooking. For one, the effectiveness of previously executed supply chain investments showed signs of gaining hold. The Company expanded gross margins by +40 bps YoY, signs that ULTA's differentiated business model is also returning improved efficiency. Additionally, and perhaps most importantly, management's long-term guidance of comparable store sales (+5-7% for the next three years) store openings (75 in 2020, 70 in 2020), eCommerce growth (+20-30% YoY and 200 bps of contribution to comp sales), and share repurchases remained untouched. ULTA plans to continue funneling investment towards the buildout of omni-channel capabilities and a more efficient supply chain, as well as in-store initiatives to optimize the guest experience. We understand the clear step down in sentiment regarding the Company's expectations, but at the same time believe that investors reacted rashly, overly discounting the increasingly efficient, best-in-class model that ULTA has developed in the space.

**Outlook**

- Regarding the 3Q'19 sell off, ULTA's moderated store openings were due to stronger than expected performance in recently opened stores, allowing for the deployment of capital elsewhere to support growth, such as omni-channel investment and supply chain efficiencies. Furthermore, **management explicitly did not change the existing long-term outlook** for the Company through the lens of comparable store sales and EPS. With regards to Amazon's entrance into the beauty market, we believe investors' negative response was unwarranted. In addition, ULTA derives ~95% of net sales from its Ultamate rewards members, and is not likely to see any negative effect at all in the form of customer migration to Amazon. ULTA's unmatched breadth of offerings and differentiated specialty retail model hedges it against any one underperforming brand, as no supplier is accountable for more than ~5% of revenue, with individual brands comprising even less. Finally, the majority of ULTA's underperformance throughout the period was exacerbated by geopolitical concerns with China, where ULTA has no revenue exposure and faces extremely muted tariff risk.
- Following 2Q'20 earnings, we believe the ~30% decline in the stock is overdone, but also view the drop as a correction that has entirely priced in the reduction in management's guidance. Additionally, we believe that management's conservative stance presents a much lower bar to surpass upon future earnings reports. The stock has begun to rebound following the news, supported by a flurry of favorable insider transactions and management's stated commitment to improving efficiency. When evaluating the retail and cosmetics market facing industry-wide headwinds, **ULTA is best positioned to outperform** given its strong hedges against a downside scenario, as well as its prime positioning to capture growth upon the next cyclical upswing.
- Operating within a new industry outlook in a more mature beauty and cosmetics market, and given a very cheap valuation relative to its growth prospects that, all things considered are still very strong on a relative and absolute basis, we believe it is a unique value opportunity to buy into a retail stalwart that is poised to outperform its peers and the broader retail sector over the next 12-18 months (*See Appendix Exhibit II*). On the heels of a stainless balance sheet (zero debt on the books) and a commitment to retail expansion and share repurchases, we retain our conviction in ULTA. Going forward, we expect product innovation supported by omni-channel expansion and distribution, along with growth in the Ultamate rewards program to reflect positively on investor sentiment and catalyze the stock, delivering a return of ~21% and returning to a fair value of ~\$291/share.





**CATALYSTS & DRIVERS:**

**OBTAIN: Driving Incremental Growth Through Product Innovation and Strategic Distribution**

Color Cosmetics

ULTA management first identified pockets of weakness in color cosmetics in the company’s 2Q’18 earnings call and has spent the last two years preparing for a downcycle in market-wide innovation while continuing to drive substantial growth across its traditional cosmetics business. Despite apparent softness in management’s outlook for cosmetics growth in the near-term, ULTA still saw **double-digit comp growth in mass** cosmetics and **single-digit acceleration in prestige** in 2Q’20. ULTA’s cosmetics business benefited from the **newness and exclusivity** of its offerings, citing growth from brands such as Lancome, Clinique, Kylie Cosmetics and Tart that offset some of the weaker sales from more established brands in 2Q’20. Even in the face of accelerated category weakness, ULTA management has worked to innovate and spur growth within its mass and prestige cosmetics offerings through **new releases, partnerships, and initiatives**.

- On August 20th, ULTA debuted **Millie Bobby Brown’s** clean beauty brand, Florence by Mills, which includes a variety of exclusive mascaras, lip glosses, and eyeshadow palettes totaling 14 SKUs. Priced at a more moderate range of \$10-\$34, Florence by Mills appeals mostly to ULTA’s growing Gen Z customer base.
- On September 8th, ULTA released the \$35 **Morphe x Jeffree Star** Artistry Palette in stores.
- On October 20th, ULTA launched the exclusive new KKW Beauty by **Kim Kardashian West** collection, a total of 67 new SKUs including contour and highlight kits along with lip color and fragrance. The company and KKW will also be dropping an exclusive holiday collection near the end of the fall. KKW products fall on the upper end of ULTA product price ranges, with the exclusive sets selling between \$35 and \$65 and the full “glam bundle” retailing at \$150. Given the higher ASP of the line, KKW products mainly target millennial customers.

The three influencers, who together reach an audience of ~200mm on Instagram alone, expand ULTA’s addressable market significantly, especially within the target Gen Z and Millennial markets. This massive popularity of brand partners, combined with the exclusive nature of the products, will lead to significant incremental in-store and online traffic and drive cosmetics comp re-acceleration through simultaneous transaction and ticket growth. The pure attractive power of the new launches brings new customers into stores, and the company’s leading experience-based business model generates added value through upselling, pairing with services, and exclusive promotions.

- ULTA has taken a **strategic, long-term view** on the short-term weakness in color cosmetics sales, driving internal innovation while the broader market searches for its newest trend. When innovation-led headwinds eventually alleviate, the company will benefit from its **growing market share and innovative business model**.

Diversified Products

As both an opportunity to diversify into growthy revenue streams and a defensive maneuver against cosmetics innovation slowdowns, ULTA has expanded its product mix to encapsulate its “All Things Beauty, All in One Place” business model, with special attention to the growing health and wellness markets. The company’s top performing categories in 2Q’20 were skincare, haircare, and personal care appliances. Skincare drove double-digit comp growth on the back of innovative and new offerings, while the Gorgeous Hair and Jumbo Love promotional events helped haircare reach single-digit comp growth in the quarter. Thanks to the success of exclusive new YSL and Versace fragrances, fragrance comp growth reached mid-single digits, and high demand for Dyson, Revlon, and Bed Head products drove strong sales in personal care products. Moving forward, ULTA will utilize strong industry tailwinds paired with strategic partnerships and new product rollouts to generate continued revenue growth in its non-cosmetics product mix.



- On September 22nd, ULTA released the exclusive, in-store only Kylie Skin collection, an extension of the massively popular Kylie Cosmetics collection by Kylie Jenner. Kylie Skin is a series of toners, serums, and face washes selling for \$20-\$28.
- To add to the excitement on the 22nd, ULTA also released the Pattern haircare collection by Tracee Ellis Ross. The 16 SKU, \$9-\$42 price range products includes shampoos, conditioners, and serums designed specifically for curly, coiled hair.
- On August 18th, ULTA rolled out Ariana Grande's exclusive, online-only Thank U, Next perfume in three sizes with prices ranging from \$42-\$62. The fragrance became available in stores on September 1st.

These three influencers, who together reach an audience of ~320mm on Instagram alone, will help ULTA gain a larger mainstream audience for its growing non-cosmetics offerings that coincides with the growth of health and wellness, which ULTA management believes is “not slowing down anytime soon”. The large names associated with recent releases will help drive incremental traffic across ULTA's distribution channels, which will also benefit innovative albeit less mainstream products such as Awake, Fountain of Truth, and Cannuka, which drove strong 2Q'20 skin and hair care growth even without the noteworthy debuts. Continuing strength in health and wellness products shields ULTA from further downside related to an extended downcycle in color cosmetics innovation and positions the company to capture wallet share among a high-growth consumer base.

#### Omnichannel: “All Things Beauty” goes All Places

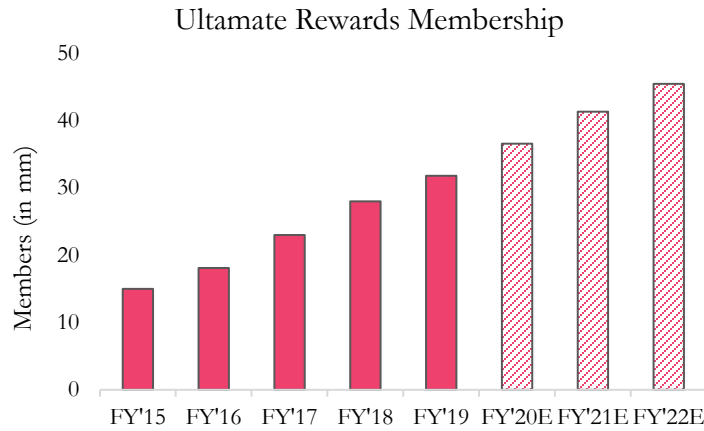
Accelerating strength in ULTA's releases will benefit from the company's strategic distribution channels and supply chain. Across brick and mortar stores and the ecommerce platform, ULTA is improving customer engagement and experience while aiding brand and product newness through partnerships, apps, and other promotions.

- ULTA plans to offer two-day eCommerce shipping by **FY'21** and converted its Romeoville, Illinois distribution center into a Fast Fulfillment Center (FFC) capable of fulfilling 30,000 orders per day. This FFC fulfilled ~10% of total orders at the end of 2Q'20 and worked to improve on-time delivery trend by 80bps YoY. ULTA plans to open a second FFC in Jacksonville, Florida in the summer of 2020.
- ULTA is also opening stores to capitalize on a growing customer base. ULTA opened 80 stores in FY'19, is on track for 75 in FY'20, and plans to open 70 in FY'21. These stores will be clustered around suburban areas and will be optimized for foot traffic at around 10,000 sq. ft. Historically, ULTA has had success with store openings, with no closures due to underperformance since 2004 and all locations becoming profitable within the first year. ULTA is expanding into Canada, where prestige makeup is expected to grow 5% YoY in 2019 and beyond.
- In 2Q'20, ULTA successfully implemented Buy Online Pickup In Store (BOPIS) in all its stores. While results from this will not be seen until next quarter's earnings, management stated that initial readings “exceeded initial expectations.” To drive traffic to the website, ULTA is improving the layout and accessibility of its mobile site and app. One notable offering is Glam Lab, which allows for a virtual try-on experience. While this technology is still in early stages of development, we see this as an opportunity to generate BOPIS sales.
- Additionally, ULTA is rolling out the AfterPay installment payment platform on its website. With this, ULTA is appealing to the debt-averse younger generation. Customers will be able to receive products immediately and pay for them in four interest-free installments.
- Recently, ULTA created a whole team dedicated to partnering with smaller, digitally native brands. As of the end of 2Q'19, this team identified 30 unique brands that allow ULTA to stay on top of changing consumer preferences. **We project these initiatives to increase retail and eCommerce revenue by 8% and 27% YoY for FY'20, respectively. Considering the historical precedent of ~30% comp growth contribution from new items, this acceleration translates to comp growth meeting or exceeding the upper end of management's guidance for 2H'20.**

**RETAIN: The Ulta-mate Partnership**

The Ultimate rewards program is ULTA’s primary way to interact with and retain its customers. The program allows for the accumulation of points upon purchase of items that accumulate over time, translating to discounts on products with future purchases. Ultimate rewards has emerged as a key differentiator for ULTA (*See Appendix Exhibit III*), and also a crucial driver for sales growth as the program’s members are accountable for 95% of annual sales. Therefore, as Ultimate membership grows, so too does the top line.

- Favorable secular and demographic trends are supporting continued growth of the Ultimate loyalty program. For one, ULTA’s target market of “beauty enthusiasts,” or customers who shop for beauty products out of pleasure rather than necessity, is a fruitful and growing category. 57% of women 18+ are considered part of this category, while dominating 77% of all beauty spending in the United States. Ultimate rewards has surpassed 33mm members, representing a market-leading 30% share of total beauty enthusiasts. In



terms of measuring ULTA’s influence over the category, the average woman spends **\$600 annually** on beauty products, of which ULTA retains **one-third of the wallet share**, equating to **\$200/member** annually on average.

- The U.S. beauty and cosmetics market is highly fragmented (*See Appendix Exhibit V*), as Specialty Beauty retailers account for ~15% of the overall distribution. Additionally, ULTA carries a 7% market share of the \$87B beauty products market, indicating a high ceiling for growth. Furthermore, the Company controls 23% of the prestige makeup market, which is growing at a solid clip of MSD. Prestige growth was driven primarily by the emergence of skincare (+13% YoY), as the segment drove 60% of the industry’s gain. Mass cosmetics also posted LDD YoY gains.

Awareness is Everything

- ULTA has successfully established its strength of generating awareness and customer engagement throughout its expansion. Currently, ULTA’s unaided awareness is up to 58%, from 42% in FY'16. Additionally, aided awareness remains above 90%, exemplifying the effectiveness of ULTA’s touchpoints with customers. ULTA continues to pour marketing dollars to boost awareness and transactions within the market’s most lucrative pocket of spending to drive further growth and reinforce the strength of its customer bonds. The Company delivers on this initiative through multiple perks included in the Ultimate loyalty rewards program, including promotions, birthday gifts, points, and the use of an ULTA credit card.

Keeping Up with the Kustomers

- ULTA has begun to realize strong growth in members moving up the loyalty spectrum to platinum and diamond status, indicating increased spending per member and presenting a lucrative opportunity for wallet share growth. In 2018, ULTA announced additional tiers to its loyalty program, the Platinum (\$450 spent annually) and Diamond (\$1,200 spent annually) tiers. This strategy has proved to be effective for the Company, as retention for the upper tier members sits at **96%**. Furthermore, ULTA **retains 41% wallet share** from these customers, indicating enhanced profitability and retention from the customers who spend the most. Looking forward,

ULTA plans to expand the Ultimate rewards program by converting existing lower level members to the Platinum and Diamond tiers, while simultaneously converting new customers and customers of the Company's salon services, positioning the program for sustained long-term growth as ULTA builds out its retail footprint.

Incremental Changes Translating to Incremental Growth

- Going forward, innovative products and expanded offerings are poised to drive increased wallet share of these customers while buoying retention as well. As more brands are made available, ULTA will supplement the offerings with increased marketing and promotional spending, using AI/data analytics capabilities to target ads more effectively and boost engagement. ULTA has also developed a credit card that incorporates a payment plan structure, fueling further customer engagement and reducing churn. Furthermore, the Company's goal is to convert 94% of salon customers into loyalty rewards members, as to integrate and recycle customers throughout the more profitable multifaceted business.
- Additionally, ULTA consistently updates the perks offered with the Ultimate membership. Most notably, this year the Company announced that members can spend their Ultimate points on in-store services as well, not just cosmetic products. This is a huge step for ULTA, as it promotes increased store traffic and cements the Company's truly differentiated, experience-based specialty retail business model. The integration is still in its early stages, and will be instrumental in contributing to meaningful comparable store sales growth for years to come. We expect these initiatives to contribute to incremental membership and wallet share growth, and as members are retained, they only become more profitable over time for ULTA through the tiered membership. Our expectations for ULTA include membership growth of +15.0% YoY, reaching 36.6mm members with outsized gains within the upper tiers of membership (Platinum and Diamond), contributing to x.xB in total top line growth for the company in FY'20.

Findings from the Jefferies Shopper Survey

- Converting first-time and infrequent shoppers to Ultimate rewards members reaps distinct advantages for ULTA, especially when considering the spending behavior of its dedicated customer base. The Fall 2019 Jefferies Shopper Survey found that ULTA's customer base was one of the highest-spending frequent shopper groups of any large US retailer.
- The report found that on average, ULTA shoppers were younger, more affluent, and were higher and more frequent spenders on beauty products when compared to competing cosmetics and personal care retailers and distributors.
- Additionally, the report discovered that ULTA shoppers alter their makeup and skincare routines more often than other beauty customers.
- ULTA shoppers tend to be more influenced by social media and beauty influencers.
- When ULTA customers cross-shop, 70% of the group's mindshare is concentrated in a few retail peers, but the majority of the consumer's beauty-specific wallet is retained by ULTA. The highest wallet shares behind ULTA are Sephora (a prestige cosmetics retailer) and Walmart and Target (providers of mass cosmetics). ULTA's business model holds a superior advantage in retaining customer mindshare against its beauty peers because of its attention to innovative mass and prestige cosmetics.

**See how your points add up**

We'll let the numbers do the talking.  
Tip: you can cash in your points on those coveted, rarely discounted products, too.



- 100 POINTS = \$3 OFF
- 250 POINTS = \$8 OFF
- 500 POINTS = \$17.50 OFF
- 750 POINTS = \$30 OFF
- 1000 POINTS = \$50 OFF
- 2000 POINTS = \$125 OFF

PEER GROUP ANALYSIS



**Estee Lauder**

**Estee Lauder Companies, Inc. (NYSE: EL)** is a manufacturer and marketer of skincare, color cosmetics, fragrances and hair care products.. EL operates ~1,500 freestanding retail stores for the sale of its top brands, including MAC, Origins, and Aveda. The company generated 43% of FY'19 revenues in EMEA, 32% in the Americas, and 25% in the APAC region. Total revenue for FY'19 was \$14.8B, representing ~9% growth YoY.

**Sally Beauty**

**Sally Beauty Holdings, Inc. (NYSE: SBH)** operates domestic and international beauty supplies retail stores that offer cosmetics, hair care and skincare products to salon professionals and retail consumers. The company generated 81% of FY'18 sales in the United States and 19% in other countries. SBH FY'18 revenues fell 0.1% YoY to \$3.9B.

**Revlon**

**Revlon, Inc. (NYSE: REV)** manufactures and markets color cosmetics, hair care, skincare, fragrance, and other beauty and personal care products and appliances. In FY'18, REV generated 53% of sales in North America, 28% in EMEA, 9% in Asia, and 5% in Latin America and 5% in APAC. The company's FY'18 sales fell 5% YoY to \$2.6B.

**Coty**

**Coty, Inc. (NYSE: COTY)** is a global manufacturer and marketer of luxury consumer and professional beauty products, including prestige fragrances, prestige and mass color cosmetics, and hair care products. In FY'19, COTY generated 44% of revenues in Europe, 31% in North America, and 26% in ALMEA. The company's revenue fell 8% YoY to \$8.6B in FY'19.

**Procter & Gamble**

**The Procter & Gamble Company (NYSE: PG)** manufactures and sells beauty, grooming, healthcare and family care products across 180 countries. In FY'18, 44% of the company's revenue came from North America sales, with 24% from Europe, 9% from APAC, 9% from Greater China, 7% from Latin America, and 7% from IMEA. PG generated \$67.7B of revenue in FY'19, representing 1% growth YoY.

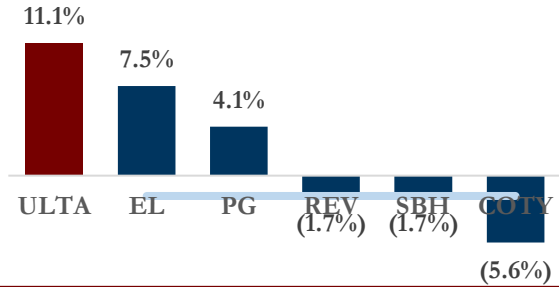
PEER GROUP ANALYSIS

Primary Peer Group																	
Company	Market Statistics			Growth Analysis				Margin Analysis				Valuation Analysis					
Ticker	Market Cap	Enterprise Value	Sales		EPS		EBITDA Margin		Profit Margin		Enterprise Value /				Price / Earnings		
			LTM	2020E	LTM	2020E	LTM	2020E	LTM	2020E	LTM	2020E	LTM	2020E	LTM	2020E	
Ulta Beauty, Inc.	ULTA	\$14,061	\$15,625	14.1%	11.1%	30.8%	10.3%	18.7%	18.7%	9.8%	9.8%	12.9x	11.9x	2.1x	1.9x	19.7x	17.9x
Estee Lauder Companies, Inc.	EL	67,736	68,186	8.6%	7.5%	18.3%	11.6%	19.3%	19.3%	12.0%	12.0%	19.6x	17.8x	4.3x	4.0x	31.5x	28.2x
Sally Beauty Holdings, Inc.	SBH	1,971	3,524	(0.1)%	(1.7)%	19.6%	2.6%	14.3%	14.3%	6.6%	6.6%	6.2x	6.3x	0.9x	0.9x	7.4x	7.6x
Revlon, Inc.	REV	1,435	4,622	(4.8)%	(1.7)%	(64.1)%	17.9%	8.6%	8.6%	(11.5)%	(11.5)%	17.7x	17.4x	1.8x	1.8x	-	-
Coty, Inc.	COTY	8,885	16,667	(8.0)%	(5.6)%	(11.5)%	135.8%	(31.6)%	(31.6)%	(43.8)%	(43.8)%	12.2x	11.7x	2.0x	2.1x	17.3x	15.7x
Proctor & Gamble Co.	PG	311,203	333,626	1.3%	4.1%	4.8%	12.6%	13.3%	13.3%	5.8%	5.8%	18.0x	17.1x	4.7x	4.6x	25.4x	23.9x
<b>High</b>		<b>\$311,203</b>	<b>\$333,626</b>	<b>14.1%</b>	<b>11.1%</b>	<b>30.8%</b>	<b>135.8%</b>	<b>19.3%</b>	<b>19.3%</b>	<b>12.0%</b>	<b>12.0%</b>	<b>19.6x</b>	<b>17.8x</b>	<b>4.7x</b>	<b>4.6x</b>	<b>31.5x</b>	<b>28.2x</b>
<b>Mean</b>		<b>67,548</b>	<b>73,708</b>	<b>1.9%</b>	<b>2.3%</b>	<b>-0.3%</b>	<b>31.8%</b>	<b>7.1%</b>	<b>7.1%</b>	<b>-3.5%</b>	<b>-3.5%</b>	<b>14.4x</b>	<b>13.7x</b>	<b>2.6x</b>	<b>2.5x</b>	<b>20.3x</b>	<b>18.7x</b>
<b>Median</b>		<b>11,473</b>	<b>16,146</b>	<b>0.6%</b>	<b>1.2%</b>	<b>11.6%</b>	<b>12.1%</b>	<b>13.8%</b>	<b>13.8%</b>	<b>6.2%</b>	<b>6.2%</b>	<b>15.3x</b>	<b>14.5x</b>	<b>2.1x</b>	<b>2.0x</b>	<b>19.7x</b>	<b>17.9x</b>
<b>Low</b>		<b>1,435</b>	<b>3,524</b>	<b>-8.0%</b>	<b>-5.6%</b>	<b>-64.1%</b>	<b>2.6%</b>	<b>-31.6%</b>	<b>-31.6%</b>	<b>-43.8%</b>	<b>-43.8%</b>	<b>6.2x</b>	<b>6.3x</b>	<b>0.9x</b>	<b>0.9x</b>	<b>7.4x</b>	<b>7.6x</b>

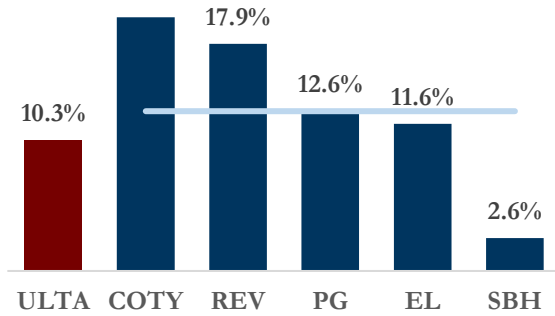
Company	General Statistics			Returns Analysis			2019A Leverage Analysis			2019A Coverage Analysis			Liquidity Profile		Credit Profile		
Ticker	Tax Rate	Beta	Dividend Yield	ROIC	ROE	ROA	Total Debt /			EBITDA / Int. Exp.	(EBITDA -Cpx)/Int. Exp.	EBIT / Int. Exp.	Quick Ratio	Current Ratio	Moody's	S&P	
							Cap	EBITDA	Equity								
Ulta Beauty, Inc.	ULTA	23.3%	0.76	-	25.1%	38.3%	18.0%	0.0x	1.3x	0.0x	-	-	-	0.66	2.32	-	-
Estee Lauder Companies, Inc.	EL	22.2%	0.85	0.9%	22.8%	39.3%	13.9%	43.6x	1.2x	77.4x	21.6x	16.0x	17.4x	1.05	1.57	A2	A+
Sally Beauty Holdings, Inc.	SBH	21.4%	0.89	-	21.6%	-	12.4%	117.8x	2.9x	-	5.5x	4.6x	4.3x	0.26	2.35	-	BB-
Revlon, Inc.	REV	-	0.70	-	(2.2)%	-	(7.2)%	152.1x	13.0x	-	0.5x	0.2x	(0.5x)	0.46	1.07	-	CCC+
Coty, Inc.	COTY	-	0.98	4.2%	-	(56.3)%	(18.8)%	60.3x	-	151.9x	(9.0x)	(10.5x)	(11.5x)	0.43	0.94		
Proctor & Gamble Co.	PG	34.7%	0.73	2.4%	-	8.3%	3.7%	38.7x	3.3x	63.2x	16.3x	9.8x	10.8x	0.51	0.75		
<b>High</b>		<b>34.7%</b>	<b>0.98</b>	<b>4.2%</b>	<b>25.1%</b>	<b>39.3%</b>	<b>18.0%</b>	<b>152.1x</b>	<b>13.0x</b>	<b>151.9x</b>	<b>21.6x</b>	<b>16.0x</b>	<b>17.4x</b>	<b>1.05</b>	<b>2.35</b>		
<b>Mean</b>		<b>25.4%</b>	<b>0.82</b>	<b>2.5%</b>	<b>16.8%</b>	<b>7.4%</b>	<b>3.7%</b>	<b>68.8x</b>	<b>4.3x</b>	<b>73.1x</b>	<b>7.0x</b>	<b>4.0x</b>	<b>4.1x</b>	<b>0.56</b>	<b>1.50</b>		
<b>Median</b>		<b>22.8%</b>	<b>0.81</b>	<b>2.4%</b>	<b>22.2%</b>	<b>23.3%</b>	<b>8.0%</b>	<b>52.0x</b>	<b>2.9x</b>	<b>70.3x</b>	<b>5.5x</b>	<b>4.6x</b>	<b>4.3x</b>	<b>0.49</b>	<b>1.32</b>		
<b>Low</b>		<b>21.4%</b>	<b>0.70</b>	<b>0.9%</b>	<b>(2.2)%</b>	<b>(56.3)%</b>	<b>(18.8)%</b>	<b>0.0x</b>	<b>1.2x</b>	<b>0.0x</b>	<b>(9.0x)</b>	<b>(10.5x)</b>	<b>(11.5x)</b>	<b>0.26</b>	<b>0.75</b>		

COMPARABLE BENCHMARKING

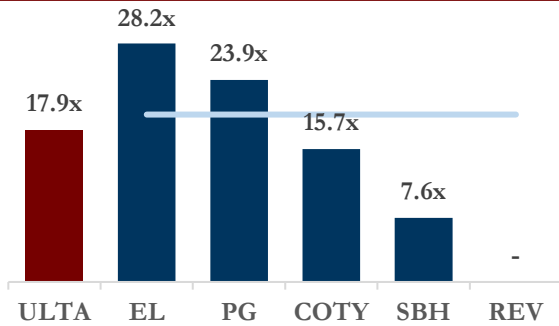
Revenue Growth 2019E



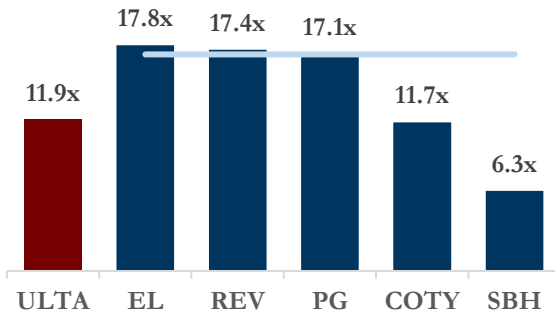
EPS Growth 2019E



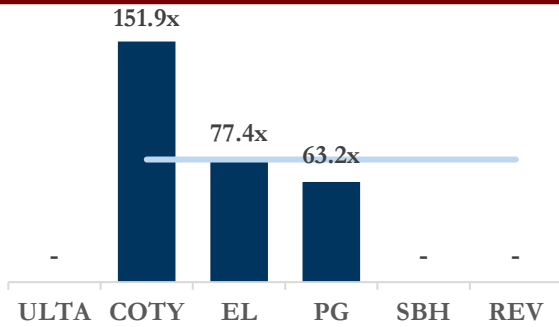
NTM P/E



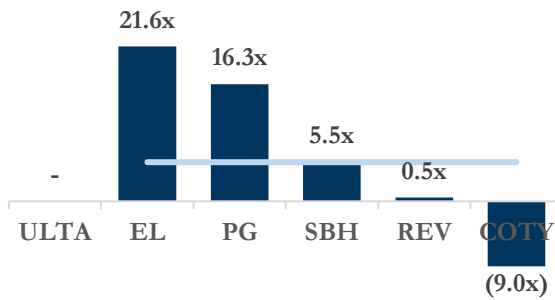
NTM EV/EBITDA



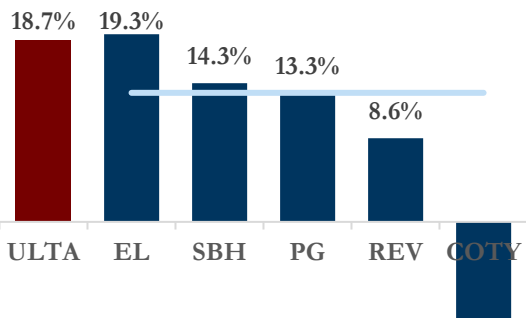
Total Debt/Equity



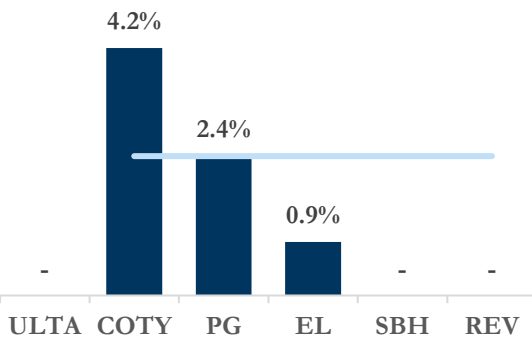
Interest Coverage (EBITDA/Int.)



LTM EBITDA Margin



Dividend Yield



## RISKS TO INVESTMENT THESIS

### Prolonged Slump in Cosmetics Innovation Cycle

- In our eyes, the biggest risk in the innovation cycle is not a shift to a more natural look, but **the idea of no shift whatsoever**. Beauty products rely on trends in order to keep demand high, but a lack of innovation has recently troubled the industry. While we believe that innovation is around the corner, there is the risk that nothing new emerges within our investment horizon. Should this occur, ULTA will continue to face secular headwinds, but will be able to rely on growing segments such as health and wellness to boost growth.
- In the past, we have seen investors react negatively to management guiding poor expectations for innovation. Continued guidance in this direction will negatively affect the stock.

### Shifting Consumer Preference to Online Cosmetic Shopping

- As we have outlined, ULTA has greatly improved its eCommerce presence and experience. While this initiative is accretive to the company, it will not protect ULTA in the face of a sharp shift in consumer preferences. If consumers suddenly decide to purchase cosmetics more online than in stores, ULTA will likely be left lagging behind due to its heavy investment in brick and mortar and relatively young eCommerce segment.
- Any legitimate risk from a consumer preference shift would need to be a **heavy** shift that comes extremely rapidly. If eCommerce continues to grow at the pace that we've seen, ULTA will be able to adapt.

### Margin Pressures

- With an increase in growth initiatives comes an increase in costs. In the past quarter, management guided for an increase in expected SG&A for the full fiscal year. The guidance was for a deleverage of 60-70bps compared to prior guidance of ~10bps leverage.
- The pressures stem from higher spending on growth initiatives and innovation. Additionally, ULTA is selling more in the Health and Wellness and Salon Services segments. These segments have naturally lower margins than traditional color cosmetics.

## ECONOMIC MOATS

### Rewards Program

- ULTA's Ultimate rewards program works to protect the company in the face of industry-wide issues. Should issues in the industry ramp up, ULTA will benefit from a consistent customer base that spends more on products, doing so more often than the average consumer. With a vast majority of sales coming from this program, ULTA has a more consistent revenue stream than some smaller players in the market. Most notably, Platinum and Diamond level guests (>\$450 & >\$1,200 of annual spending) have retention rates above 96%.
- The rewards program also helps to protect ULTA from new entrants into the market, as those who are entrenched in ULTA's rewards program have a high opportunity cost of switching to another brand. When you already spend \$500/year at ULTA, and have accumulated points you can redeem for free products, **why would you ever switch?** ULTA also partners with new brands, so we don't see new entrants as a potential threat.

### Differentiated Business Model

- ULTA's business model is well equipped to handle a variety of consumer preferences and industry shifts. Mainly, the store itself is appealing to multiple types of consumers, with both prestige and mass makeup lining the stores. Additionally, ULTA's focus on partnerships with digitally native brands allows it to react to changing trends in the makeup industry. Lastly, ULTA's partnerships with influencers and social media personalities gives it a wide reach over Gen Z and millennials, the driving force within cosmetics spending. We believe that ULTA, through its store layout, product mix, and internet presence has an industry-leading business model that is properly equipped adapt to shifting trends, returning outperformance regardless of the macro industry environment.

**Bear Case Assumptions for \$185 PT:**

- A slower than expected product innovation cycle weighs on margins in the short-term, as ULTA’s investments do not materialize enough to offset mass and prestige softness. Revenue growth of MSD is driven by comparable store sales on or below the low end of management’s 2H’20 forecast.
- Expenses get out of hand, weighing on margins with no internal solution to mitigate losses over the forecast period. Margin deterioration aligns ULTA with broader retail peers that it usually outperforms.
- Inventory costs weigh further on the Company, sourced from inaccurate forecasts.

**Bull Case Assumptions for \$359 PT:**

- Revenue growth remains above +10% annually, on the heels of stronger than expected comparable store sales growth on the higher end of management’s guidance due to a faster than anticipated reacceleration of U.S. cosmetics.
- eCommerce business gains solid footing, expanding at +30% YoY through 2021.
- Capex levels remain flat, as ULTA delivers and adds to the store opening program over the forecast period.
- SG&A expenses reach a step down as ULTA stores become more profitable. Also, gross margins realize meaningful expansion up to 37.8%.
- ULTA successfully converts Salon Services customers to Ultimate rewards members, while also promoting further sales through the program and reaching over 50mm members over the forecast period.



Perpetuity Growth (PGR) Method	
Terminal Year FCF:	\$690
PGR:	1.5%
Terminal Value:	23,420
PV of Terminal Value:	19,840
PV of Stage 1 Cash Flows:	964
<b>Implied Enterprise Value:</b>	<b>\$20,804</b>
(+) Cash & Equivalents:	177
(-) Preferred Stock:	0
(-) Total Debt:	0
(-) Pension Obligations:	0
(-) Non-Controlling Interests:	0
(-) Capital Leases:	0
<b>Implied Equity Value:</b>	<b>\$20,982</b>
Diluted Shares O/S:	58.4
<b>Implied Share Price:</b>	<b>\$359.28</b>
% Return:	49.1%

Perpetuity Growth (PGR) Method	
Terminal Year FCF:	\$320
PGR:	1.5%
Terminal Value:	10,853
PV of Terminal Value:	9,194
PV of Stage 1 Cash Flows:	1,419
<b>Implied Enterprise Value:</b>	<b>\$10,614</b>
(+) Cash & Equivalents:	177
(-) Preferred Stock:	0
(-) Total Debt:	0
(-) Pension Obligations:	0
(-) Non-Controlling Interests:	0
(-) Capital Leases:	0
<b>Implied Equity Value:</b>	<b>\$10,791</b>
Diluted Shares O/S:	58.4
<b>Implied Share Price:</b>	<b>\$184.78</b>
% Return:	(23.3%)



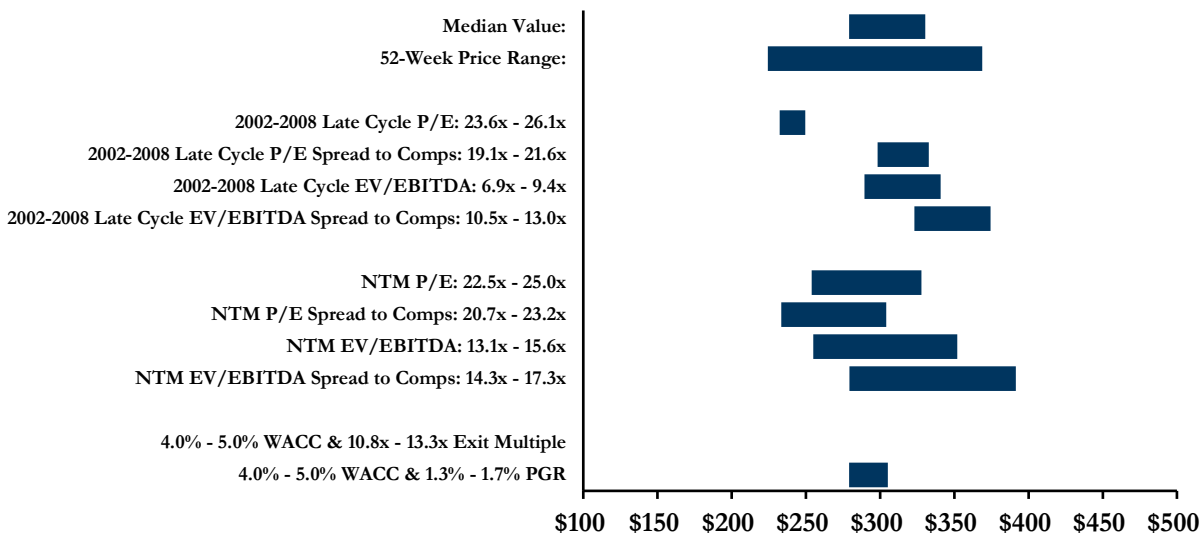
**VALUATION ANALYSIS**

**DCF Assumptions:**

Our base case implies FY'20 sales of \$7.4B, representing 10.4% growth YoY. This reflects our assumptions for continued expansion of mass and prestige cosmetics sales and strong 4Q'20 sales, partially offsetting moderated comparable store sales growth in 2H'20. Overall FY'20 comparable store sales are assumed at +8.1% YoY. We also expect ULTA's eCommerce platform to realize YoY growth of 27.2%, driven by digitally native brands as well as the Company's commitment to improving distribution and fulfillment. Overall, our gross profit, EBITDA, and EPS forecasts remain in-line with consensus forecasts, and margins (EBIT, EBITDA, profit) are expected to reach moderate expansion before moderating in 2022, a forecast we deemed conservative with future potential for upside.

DCF	2017	2018	2019	2020e	2021e	2022e	2023e	2024e
Revenue	\$4,854.7	\$5,884.5	\$6,716.6	\$7,483.7	\$8,249.8	\$9,077.2	\$10,018.9	\$11,098.1
EBITDA	878.8	1,005.7	1,133.6	1,873.8	1,449.0	1,655.9	1,716.9	2,125.8
EBIT	654.8	785.3	854.1	1,016.4	1,278.7	1,456.9	1,507.8	1,892.2
Income Tax Benefit (Expense)	(246.0)	(231.6)	(200.6)	(224.2)	(292.7)	(335.1)	(346.8)	(435.2)
<b>NOPAT (EBIAT)</b>	<b>\$408.9</b>	<b>\$553.7</b>	<b>\$653.5</b>	<b>\$792.1</b>	<b>\$986.1</b>	<b>\$1,121.8</b>	<b>\$1,161.0</b>	<b>\$1,457.0</b>
Depreciation & Ammortization				857.4	170.3	199.0	209.1	233.6
Stock-Based Compensation				20.9	16.5	18.2	20.0	22.2
Capital Expenditures				(354.9)	(318.1)	(290.5)	(320.6)	(355.1)
Goodwill Impairment				-	-	-	-	-
(Increase)/Decrease in Working Capital				(540.5)	(218.5)	(132.9)	(139.9)	(160.3)
(Increase)/Decrease in LT Items				(549.2)	(1,148.7)	(488.4)	(486.8)	(507.8)
<b>Unlevered Free Cash Flow</b>				<b>\$88.3</b>	<b>(\$512.4)</b>	<b>\$427.2</b>	<b>\$442.9</b>	<b>\$689.6</b>
Full-Year Discount				0.28	1.28	2.28	3.28	4.28
Mid-Year Discount				0.14	0.78	1.78	2.78	3.78
Discount Factor				0.99	0.97	0.92	0.89	0.85
<b>Present Value of Future Free Cash Flow</b>				<b>\$87.8</b>	<b>(\$495.2)</b>	<b>\$395.1</b>	<b>\$392.0</b>	<b>\$584.2</b>
% Growth					(664.0%)	(179.8%)	(0.8%)	49.0%

**Ulta Beauty, Inc. - Valuation Summary**



Valuation Multiple Sensitivity Analysis (Returns of 15%-30% in Green)

Implied Share Price

		NTM P/E				
		21.3x	22.5x	23.8x	25.0x	26.3x
EPS	\$10.36	\$ 220.31	\$ 233.26	\$ 246.21	\$ 259.16	\$ 272.12
	\$11.28	\$ 239.75	\$ 253.84	\$ 267.94	\$ 282.03	\$ 296.13
	\$12.19	\$ 259.19	\$ 274.42	\$ 289.66	\$ 304.90	\$ 320.14
	\$13.10	\$ 278.63	\$ 295.01	\$ 311.39	\$ 327.77	\$ 344.15
	\$14.02	\$ 298.06	\$ 315.59	\$ 333.11	\$ 350.63	\$ 368.16

Implied % Return

		NTM P/E				
		21.3x	22.5x	23.8x	25.0x	26.3x
EPS	\$10.36	(8.5%)	(3.2%)	2.2%	7.6%	13.0%
	\$11.28	(0.5%)	5.4%	11.2%	17.1%	22.9%
	\$12.19	7.6%	13.9%	20.2%	26.6%	32.9%
	\$13.10	15.7%	22.5%	29.3%	36.1%	42.9%
	\$14.02	23.7%	31.0%	38.3%	45.6%	52.8%

Implied Share Price

		NTM EV/EBITDA				
		11.8x	13.1x	14.3x	15.6x	16.8x
EBITDA	\$1,036	\$ 212.41	\$ 234.58	\$ 256.75	\$ 278.92	\$ 301.08
	\$1,127	\$ 230.89	\$ 255.01	\$ 279.13	\$ 303.26	\$ 327.38
	\$1,218	\$ 249.36	\$ 275.44	\$ 301.52	\$ 327.60	\$ 353.68
	\$1,310	\$ 267.84	\$ 295.87	\$ 323.91	\$ 351.94	\$ 379.98
	\$1,401	\$ 286.31	\$ 316.30	\$ 346.29	\$ 376.28	\$ 406.27

Implied % Return

		NTM EV/EBITDA				
		11.8x	13.1x	14.3x	15.6x	16.8x
EBITDA	\$1,036	(11.8%)	(2.6%)	6.6%	15.8%	25.0%
	\$1,127	(4.2%)	5.9%	15.9%	25.9%	35.9%
	\$1,218	3.5%	14.3%	25.2%	36.0%	46.8%
	\$1,310	11.2%	22.8%	34.5%	46.1%	57.7%
	\$1,401	18.9%	31.3%	43.7%	56.2%	68.6%

Price Calculation: Average NTM P/E Multiple

NTM EPS			
\$12.19			
1-Yr NTM P/E	=	Target Price	=
23.8x		\$289.66	
			% Upside
			~20%

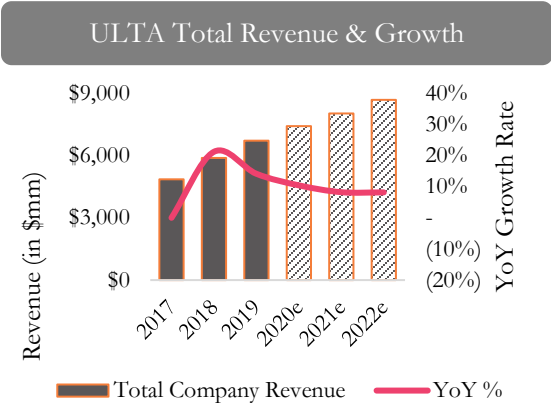
FINANCIAL ANALYSIS

ULTA Segment Revenue Model

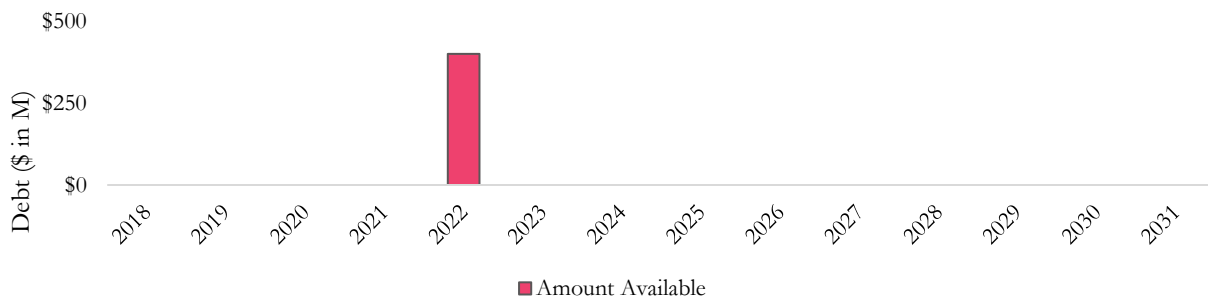
Summary	2017	2018	2019	2020e	2021e	2022e	2023e	2024e
<b>Total Company Revenue</b>	\$4,854.7	\$5,884.5	\$6,716.6	\$7,417.1	\$8,027.4	\$8,682.9	\$9,420.8	\$10,261.3
% Growth		21.2%	14.1%	10.4%	8.2%	8.2%	8.5%	8.9%
<b>Retail Revenue</b>	\$4,272.2	\$5,037.6	\$5,646.0	\$6,103.8	\$6,461.6	\$6,849.3	\$7,274.0	\$7,746.8
% Growth		17.9%	12.1%	8.1%	5.9%	6.0%	6.2%	6.5%
% of Total Revenue	88.0%	85.6%	84.0%	82.3%	80.5%	78.9%	77.2%	75.5%
<b>eCommerce Revenue</b>	\$339.8	\$569.4	\$767.1	\$975.4	\$1,199.2	\$1,439.1	\$1,726.9	\$2,072.3
% Growth		67.6%	34.7%	27.2%	23.0%	20.0%	20.0%	20.0%
% of Total Revenue	7.0%	9.7%	11.0%	13.2%	14.9%	16.6%	18.3%	20.2%
<b>Salon Services Revenue</b>	\$242.7	\$277.5	\$236.4	\$262.4	\$283.5	\$304.7	\$323.0	\$337.6
% Growth		14.3%	(14.8%)	11.0%	8.0%	7.5%	6.0%	4.5%
% of Total Revenue	5.0%	4.7%	4.0%	3.5%	3.5%	3.5%	3.4%	3.3%
<b>Other Services Revenue</b>	\$0.0	\$0.0	\$67.2	\$75.5	\$83.1	\$89.8	\$96.9	\$104.7
% Growth		N/A	N/A	12.5%	10.0%	8.0%	8.0%	8.0%
% of Total Revenue	0.0%	0.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%

Total Revenue:

- In 2Q'20, ULTA reported adjusted revenue of \$1.67B vs. \$1.68B expected, representing a 12% YoY increase but a decrease of 4% QoQ.
- According to management, this quarterly contraction was attributable to softness across a plurality of top brands in mass and prestige cosmetics. The slowdown of notable prestige brands was partially offset by the growth of newer introductions such as Kylie Cosmetics and Tarte.
- Revenue diversification increased in the past quarter, as skincare, haircare, salon, and other/nail sub-segments all reported increased revenues as a percent of total reported revenue while cosmetics fell from 53% of total revenue in 1Q'20 to 47% in 2Q'20. Significant strength from skincare, which respective sub-segment moved from 21% to 22% in 2Q'20, benefited from strong innovation and new ingredients and offerings.
- Management has guided down its full-year revenue forecast to a range of 9%-12% from low double-digit growth due to headwinds and volatility in the cosmetics market largely related to a maturing innovation cycle. Additionally, internal models suggest weakness experienced within top mass and prestige cosmetics brands in 1H'19 will continue through 2H'19 as the cosmetics space searches for new trends.
- We remain optimistic in ULTA management's ability to drive internal innovation in recently-lagging prestige and mass cosmetics while limiting the impact of a prolonged innovation draught through growing diversified revenues, all while generating substantial incremental revenue from its expanding loyalty program.

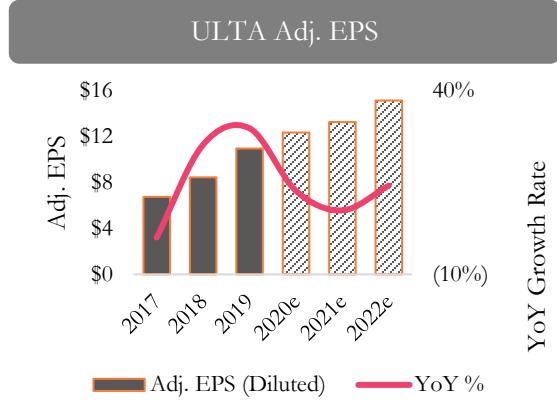


Debt Distribution:



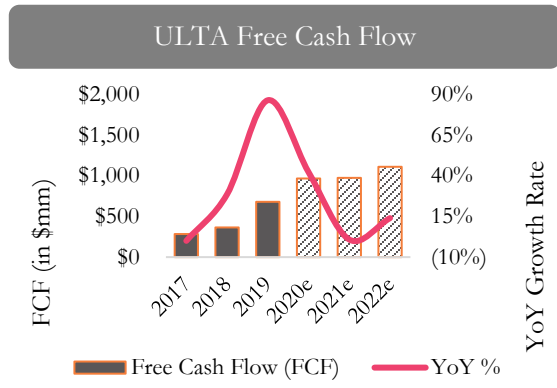
**Earnings:**

- Since its IPO in late 2007, ULTA has only missed earnings in four quarters. In that same timeframe, the average surprise is + 11.2% with an average price change of 9.13%. Earnings have grown 23.66% in the past 5 years
- In 2Q'20 the company missed estimates by 1.28% and saw a price change of (29.55%). EPS came in at \$2.79, increasing from \$2.46 in 2Q'19. The drop in price, as previously mentioned, was mainly due to a cut in guidance amid secular headwinds.
- For 3Q'20 the street is estimating EPS of \$2.14, a slight decrease from the \$2.19 ULTA reported in 3Q'19.
- Moving forward we expect adjusted EPS growth of 12.7% in FY'20.



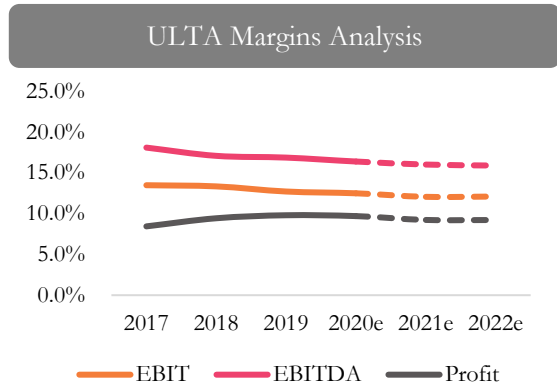
**Cash Flow/Capital Expenditures/Shareholder Returns:**

- In FY'19, ULTA generated \$636.7mm of Free Cash Flow, +88.0% YoY. The increase was driven by an increase in operating income, a favorable change to the tax code, and a decrease to capital expenditures.
- Capital Expenditures peaked in FY'17 at \$440.7mm before returning to more stable levels in FY'18 at \$319.4mm. FY'19 expected FCF is \$328.9mm, a slight increase from FY'18.
- While the pace at which ULTA is dedicating investment into its supply chain is accelerating, the magnitude is moderating. Expectations point to \$345mm in FY'19 as the Company ramps up spending in store openings, merchandise, and IT.
- ROIC expanded to ~35% in 2Q'19, with further expansion anticipated with the moderation of capex.
- In 2Q'20 ULTA repurchased \$270.9mm of shares, bringing the total for the first fiscal year to \$378.3mm. As of August 3, 2019, it can still repurchase \$517.3mm of its original \$875mm repurchase plan laid out in March 2019.



**Margins:**

- In 2Q'19, ULTA grew gross margin by 40 bps YoY and 100 bps QoQ to 36.4%, primarily due to optimized marketing and merchandising spending and alleviating fixed store costs. Weakness in high-margin prestige cosmetics sales led to a more unfavorable sales volume mix that weighed on margins.
- Operating margin fell to 12.5%, a QoQ and YoY decrease of 8.4% and 4.2%, respectively. SG&A expenses grew 90 bps QoQ to 23.6% of revenue due to increased labor investments across salon services and promotional in-store initiatives.
- Net income margin fell 2.9% YoY and 12.3% QoQ to 9.7%, with the contraction partially offset by an effective tax rate decrease to 23.1%.



**APPENDIX**
**Exhibit I: Consolidated Financial Statements**

Consolidated Income Statement	Historical							
	2017	2018	2019	2020e	2021e	2022e	2023e	2024e
<b>Revenue</b>	<b>\$4,855</b>	<b>\$5,885</b>	<b>\$6,717</b>	<b>\$7,417</b>	<b>\$8,027</b>	<b>\$8,683</b>	<b>\$9,421</b>	<b>\$10,261</b>
<i>% Growth YoY</i>		21.2%	14.1%	10.4%	8.2%	8.2%	8.5%	8.9%
<b>Gross Profit</b>	<b>\$1,747</b>	<b>\$2,097</b>	<b>\$2,409</b>	<b>\$2,710</b>	<b>\$2,901</b>	<b>\$3,126</b>	<b>\$3,391</b>	<b>\$3,694</b>
<i>% Margin</i>	36.0%	35.6%	35.9%	36.5%	36.1%	36.0%	36.0%	36.0%
<b>EBIT</b>	<b>\$655</b>	<b>\$785</b>	<b>\$854</b>	<b>\$927</b>	<b>\$968</b>	<b>\$1,051</b>	<b>\$1,093</b>	<b>\$1,201</b>
<i>% Growth YoY</i>		19.9%	8.8%	8.5%	4.5%	8.5%	4.0%	9.9%
<i>Margin</i>	13.5%	13.3%	12.7%	12.5%	12.1%	12.1%	11.6%	11.7%
<b>Net Income (Loss)</b>	<b>\$410</b>	<b>\$555</b>	<b>\$659</b>	<b>\$719</b>	<b>\$741</b>	<b>\$801</b>	<b>\$833</b>	<b>\$915</b>
<i>% Growth YoY</i>		35.5%	18.6%	9.2%	3.0%	8.1%	4.0%	9.9%
<i>Margin</i>	8.4%	9.4%	9.8%	9.7%	9.2%	9.2%	8.8%	8.9%
<b>Adj. EPS (Diluted)</b>	<b>\$6.74</b>	<b>\$8.44</b>	<b>\$10.94</b>	<b>\$12.33</b>	<b>\$13.24</b>	<b>\$15.11</b>	<b>\$16.65</b>	<b>\$19.45</b>
<i>% Growth YoY</i>		25.2%	29.7%	12.7%	7.4%	14.1%	10.2%	16.8%
<b>EBITDA</b>	<b>\$879</b>	<b>\$1,006</b>	<b>\$1,134</b>	<b>\$1,216</b>	<b>\$1,286</b>	<b>\$1,381</b>	<b>\$1,430</b>	<b>\$1,557</b>
<i>% Growth YoY</i>		14.4%	12.7%	7.3%	5.8%	7.3%	3.6%	8.9%
<i>Margin</i>	18.1%	17.1%	16.9%	16.4%	16.0%	15.9%	15.2%	15.2%

Consolidated Balance Sheet	Historical							
	2017	2018	2019	2020e	2021e	2022e	2023e	2024e
Cash & Cash Equivalents	\$385	\$277	\$409	\$488	\$152	\$81	\$145	\$257
Accounts Receivable	89	100	136	139	154	133	145	157
Inventory	944	1,096	1,214	1,357	1,366	1,294	1,404	1,529
Prepaid & Other Current Assets	119	220	155	46	38	174	170	154
<b>Total Current Assets</b>	<b>1,536</b>	<b>1,694</b>	<b>1,915</b>	<b>2,030</b>	<b>1,709</b>	<b>1,682</b>	<b>1,863</b>	<b>2,098</b>
PP&E, Net	\$1,004	\$1,189	\$1,226	\$1,323	\$1,404	\$1,465	\$1,552	\$1,657
Intangible Assets, Net	0	0	4	4	4	4	4	4
Goodwill	0	0	11	11	11	11	11	11
Other Non-Current Assets	11	25	35	1,747	2,396	2,636	2,899	3,189
<b>Total Non-Current Assets</b>	<b>1,016</b>	<b>1,215</b>	<b>1,276</b>	<b>3,085</b>	<b>3,814</b>	<b>4,115</b>	<b>4,466</b>	<b>4,860</b>
<b>Total Assets</b>	<b>2,552</b>	<b>2,909</b>	<b>3,191</b>	<b>5,115</b>	<b>5,523</b>	<b>5,796</b>	<b>6,329</b>	<b>6,958</b>
Accounts Payable	260	326	404	575	588	548	595	648
Accrued Liabilities	261	302	221	464	509	428	464	506
Other Current Liabilities	9	14	199	159	159	150	163	177
<b>Total Current Liabilities (Excl. Debt)</b>	<b>529</b>	<b>642</b>	<b>824</b>	<b>1,198</b>	<b>1,256</b>	<b>1,126</b>	<b>1,222</b>	<b>1,331</b>
Revolver	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
LT Debt (Incl. Current Portion)	0	0	0	0	0	0	0	0
Deferred Income Taxes	86	59	84	87	87	87	87	87
Other Non-Current Liabilities	386	433	463	1,719	1,719	1,719	1,719	1,719
<b>Total Non-Current Liabilities</b>	<b>472</b>	<b>492</b>	<b>547</b>	<b>1,806</b>	<b>1,806</b>	<b>1,806</b>	<b>1,806</b>	<b>1,806</b>
<b>Total Liabilities</b>	<b>1,002</b>	<b>1,134</b>	<b>1,371</b>	<b>3,004</b>	<b>3,062</b>	<b>2,932</b>	<b>3,028</b>	<b>3,137</b>
Common Stock & APIC	\$659	\$700	\$739	\$787	\$771	\$754	\$735	\$714
Retained Earnings	906	1,093	1,106	1,445	2,185	2,986	3,819	4,734
Treasury Stock	(15)	(19)	(25)	(291)	(1,006)	(1,721)	(2,436)	(3,151)
Accumulated Other Comprehensive Income (AOCI)	0	0	0	0	0	0	0	0
<b>Total Shareholder's Equity</b>	<b>1,550</b>	<b>1,774</b>	<b>1,820</b>	<b>1,941</b>	<b>1,950</b>	<b>2,019</b>	<b>2,118</b>	<b>2,297</b>
Noncontrolling Interests	0	0	0	0	0	0	0	0
<b>Total Equity</b>	<b>1,550</b>	<b>1,774</b>	<b>1,820</b>	<b>1,941</b>	<b>1,950</b>	<b>2,019</b>	<b>2,118</b>	<b>2,297</b>
<b>Total Liabilities &amp; Shareholder's Equity</b>	<b>2,552</b>	<b>2,909</b>	<b>3,191</b>	<b>4,944</b>	<b>5,012</b>	<b>4,951</b>	<b>5,145</b>	<b>5,434</b>

Exhibit II: ULTA vs Other Retailers Comps Growth

Ultra vs. Other Retailers' Comp Growth

Ticker	Comp Growth (Last Full Year)	Comp Growth (Last Quarter)	LTM P/E
ULTA	8.1%	6.2%	20.27x
FIVE	3.9%	1.4%	46.24x
TJX	6.0%	2.0%	29.88x
DG	3.2%	4.0%	25.45x
HD	5.2%	3.0%	22.95x
RH	4.0%	-	22.36x
TIF	4.0%	-3.0%	21.47x
TGT	5.0%	3.4%	18.27x
KMX	1.9%	6.3%	18.19x
AZO	3.0%	3.0%	17.78x
WSM	3.7%	6.5%	15.48x
BBY	4.8%	1.6%	12.95x
URBN	8.0%	-3.0%	11.94x
JWN	1.7%	-5.1%	10.85x
AEO	8.0%	2.0%	10.82x
KSS	1.5%	-2.9%	10.04x
FL	2.7%	0.8%	9.48x
SBH	-1.5%	0.1%	7.53x
GME	-0.3%	-11.6%	5.14x
MIK	0.8%	0.3%	4.51x
JCP	-3.1%	-9.0%	-
<b>Group Average</b>	<b>3.13%</b>	<b>-0.01%</b>	<b>16.91x</b>

<b>Percent Difference vs. Group Average - Full Year Comp</b>	<b>159.20%</b>
<b>Percent Difference vs. Group Average - LTM P/E</b>	<b>19.85%</b>

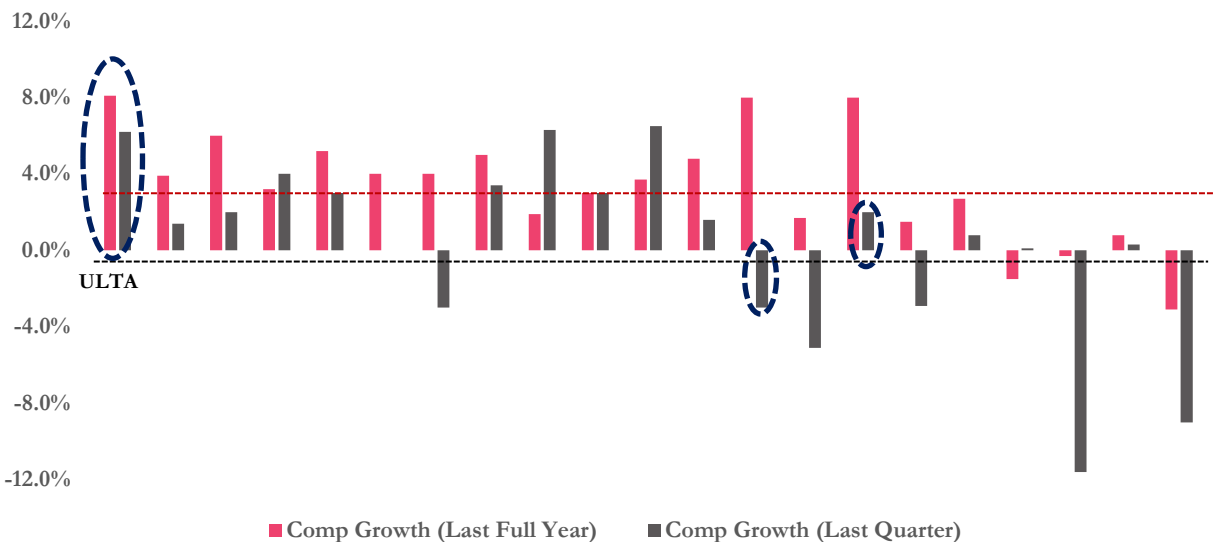


Exhibit III: Ulta vs Sephora Rewards Program

Ultamate Rewards vs Beauty Insider Breakdown

ULTA		SEPHORA	
<b><u>Member (\$0)*</u></b>		<b><u>Insider (\$0)*</u></b>	
Free birthday gift		Free birthday gift	
Double points in birthday month		Two day shipping for \$15/year	
1 point/dollar spent		One point per dollar spent	
<b><u>Platinum (\$450)*</u></b>		<b><u>VIB (\$350)*</u></b>	
1.25 points/dollar spent		1.25 points/dollar spent	
Points never expire		Free birthday gift OR 250 points	
\$10 birthday coupon		Seasonal Savings	
<b><u>Diamond (\$1200)*</u></b>		<b><u>Rouge (\$1000)*</u></b>	
1.5 points/dollar spent		1.5 points/dollar spent	
Free shipping on orders \$25+			
\$25 annual beauty services card			

\*Annual Spend

Exhibit IV: ULTA 3Q'20 Product Launches

Brand Name	Product Type	Product Launch Dates		Additional Notes
		Online	In-Store	
Florence by Mills	Skincare	9/8/2019	9/22/2019	14 SKUs, \$10-\$34
KKW Beauty	Makeup			Fall
Kylie Skin	Skincare	N/A	9/22/2019	6 SKUs, \$20-\$28. Not available for BOPIS
Morphe x Jeffree Star	Makeup	8/25/2019	9/8/2019	\$35 Artistry Palette
Ariana Grande	Fragrance	8/18/2019	9/1/2019	Exclusive "Thank U Next"
Pattern by Tracee Ellis Ross	Haircare	9/22/2019	9/22/2019	16 SKUs, \$9-\$42

Exhibit V: Beauty and Personal Care: Distribution by Channel

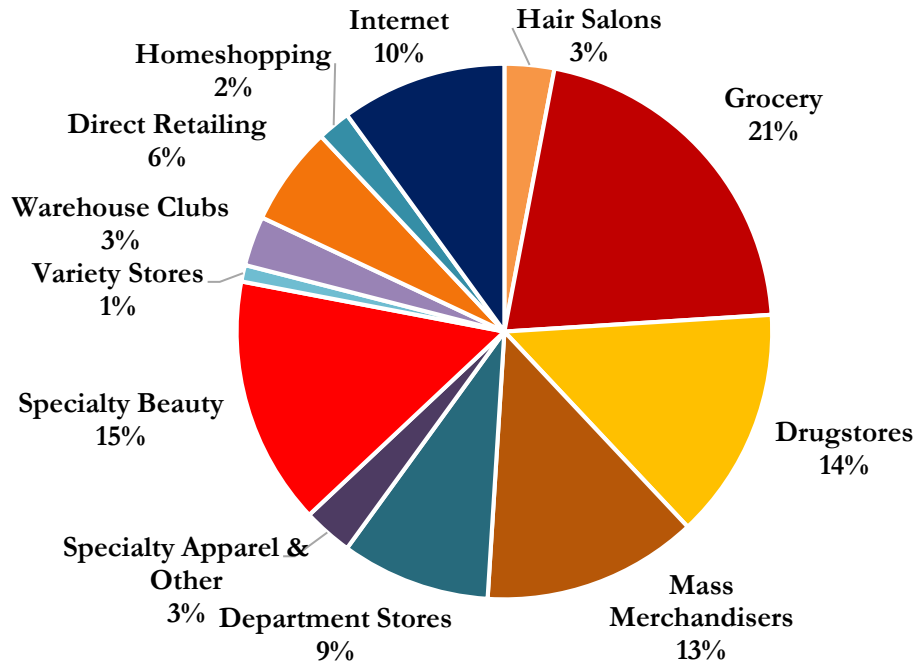
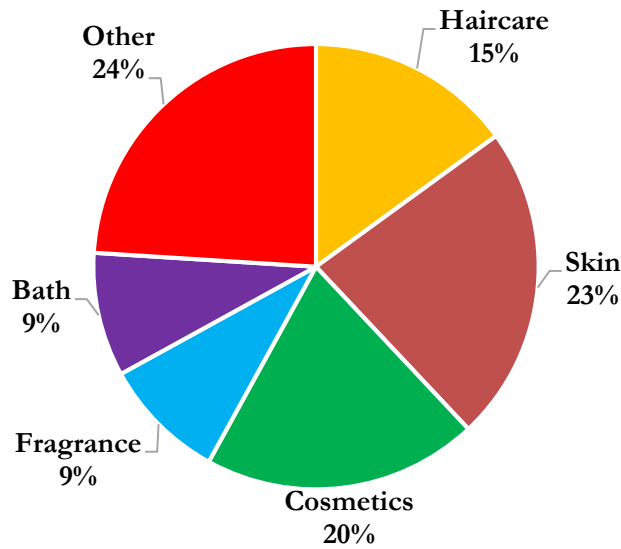


Exhibit VI: U.S. Beauty Products Market





**Exhibit VII: ULTA 1-Year LTM P/E**



**Exhibit VIII: ULTA 1-Year LTM EV/EBITDA**



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**DISCLAIMER**

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This report is prepared strictly for educational purposes and should not be used as an actual investment guide. The forward-looking statements contained herein are simply the author's opinions. The writer does not own any Ulta Beauty, Inc. (ULTA) stock.

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**TUIA STATEMENT**

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Established in honor of Professor William C. Dunkelberg, former Dean of the Fox School of Business, for his tireless dedication to educating students in “real-world” principles of economics and business, the William C. Dunkelberg (WCD) Owl Fund will ensure that future generations of students have exposure to a challenging, practical learning experience. Managed by Fox School of Business graduate and undergraduate students with oversight from its Board of Directors, the WCD Owl Fund's goals are threefold:

- Provide students with hands-on investment management experience
- Enable students to work in a team-based setting in consultation with investment professionals.
- Connect student participants with nationally recognized money managers and financial institutions

Earnings from the fund will be reinvested net of fund expenses, which are primarily trading and auditing costs and partial scholarships for student participants.