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TGT - Q3 2019 Target Corp Earnings Call

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OVERVIEW:

Co. reported 3Q19 GAAP EPS from continuing operations of $1.37 and adjusted EPS of $1.36. Expects full-year 2019 adjusted EPS to be $6.25-6.45 and 4Q19 comparable sales growth to be 3-4% and adjusted EPS to be $1.54-1.74.

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to the Target Corporation Third Quarter Earnings Release Conference Call. (Operator Instructions) As a reminder, this conference is being recorded Wednesday, November 20, 2019.

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Brian C. Cornell - *Target Corporation - Chairman & CEO*

Thanks, John, and good morning, everybody. We are really pleased with our third quarter financial results, which were well ahead of our expectations on nearly every measure. Comparable sales grew 4.5% in the quarter, about 1 point ahead of our guidance, driven by an acceleration of sales in our stores. This comp performance is on top of 5.1% in last year's third quarter, meaning that we've grown our comparable sales nearly 10% over the last 2 years. Third quarter profitability was also stronger than expected, driven by a much larger-than-expected increase in our gross margin rate. With this upside, operating margin dollars increased more than 22% compared with a year ago, resulting in a nearly 25% increase in adjusted EPS.

In light of this performance and our updated expectations for the fourth quarter, we raised the midpoint of our full year adjusted EPS expectations by $0.30. This reflects really strong performance, well ahead of our expectations going into 2019, and it demonstrates the power of the durable operational and financial model we've been developing over the last several years. None of these results will be possible without the amazing efforts of our team who have designed and implemented meaningful changes across multiple parts of our business, from our store service and operating model to our unmatched digital fulfillment capabilities and our inventory replenishment routines. And while there's much more to do, it's incredibly gratifying to see how these efforts are already driving outstanding operational and financial performance.

When we analyze the components of our comp sales, we're pleased that traffic continues to be the primary driver of our growth. Overall, our traffic grew 3.1% in the third quarter as our guests chose to shop with us more often, both in stores and through our digital options. Among our sales channels, store comps were up 2.8% in the quarter, more than 1 percentage point faster than the second quarter, while digital comps grew 31% and drove 1.7 percentage points of the company's comp growth.

Notably, this year's digital growth was on top of a 49% comp increase last year. And while these numbers add up to 80%, when you're talking about growth rates of this magnitude, the power of compounding really matters. Specifically, when you do the math, you'll see that our third quarter digital comp sales have actually grown more than 95% over the last 2 years. Within our digital sales, 80% of our third quarter growth was driven by same-day fulfillment options: in-store pickup, Drive-Up and Shipt. Given that these same-day options rely on our store assets, team and inventory, they are much more profitable than traditional e-commerce fulfillment.

As we look back at trends within the quarter, we continue to see the benefit of our balanced multi-category assortment, which gives us the flexibility to lean into different seasons and important moments in our guests' lives. At the beginning of the quarter, we enjoyed favorable results in our Back-to-School and Back-to-College assortment. And later in the quarter, as colder weather spread across the country, we saw a rapid acceleration in sales of our weather-sensitive categories.

Beyond these seasonal moments, we continue to benefit from our frequency categories, Food and Beverage, Essentials & Beauty, which drive everyday traffic, guest engagement and sales. We're happy to see continued broad market share gains across many of our core merchandising categories. Apparel saw the most dramatic share gains in the quarter with comp sales growth of more than 10%. This was driven by even stronger trends in Jewelry, accessories and Shoes, intimates and sleepwear, young contemporary and women's ready-to-wear.

In the Home category, which was annualizing really strong growth a year ago, we saw a low single-digit comp increase in the third quarter, driven by strength in the kitchen and home storage categories. Among our frequency categories, we continue to benefit from amazing strength in beauty and cosmetics, which delivered high single-digit comp growth in the quarter. We also saw high single-digit growth in our over-the-counter [illegible]omen's d hih moa396 Tw129 0 1 36 202.45 T1(Notably,omeSepy abn

Within our Hardline categories, we saw particular strength in mobile and continued growth in toys, offny'i4iTm(topo1s)Tj0 p engacd14.4s. We're ontinue

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At the same time, I want to congratulate Michael Fiddelke on his new responsibilities. Michael knows our business incredibly well having worked across multiple parts of our business and operations over the last 15 years. I'd also like to thank Jill Sando and Christina Hennington for their

the third quarter, we completed another 153 remodels, putting us at just under 300 for the year. And given our ongoing efforts to improve the process, we've realized efficiencies that have delivered spending favorability compared to our plan.

Also encouraging, we found ways to reduce the sales disruption that occurs in stores undergoing a remodel, driving a notable improvement in the average disruption compared with last year. We continue to see remodel sales lifts in line with our assumptions, and we've seen a meaningful second year lift that wasn't originally part of our modeling for these projects. We plan to maintain our current pace of remodels for 1 additional year in 2020 and then ramp down to a longer-term pace of 150 to 200 per year beginning in 2021.

In addition to our remodels, we continue to see encouraging results from our investments in new small-format stores. We opened 7 small-format locations in the third quarter plus another 6 in November. And sales from this year's entire group of new stores are running ahead of our plan. We plan to continue opening about 30 of these smaller stores per year because they drive guest engagement and deliver strong financial performance, including much higher-than-average sales productivity and meaningfully higher gross margin rates compared with our larger-format stores.

And behind the scenes, our teams continue their work to modernize our supply chain, enabling growth and efficiency in an increasingly complex omnichannel retail environment. One of these investments is in the development of a new inventory planning and control system, which is designed to deliver enhanced precision in the placement and positioning of our inventory throughout our supply chain. The benefits of this new system include lower backroom inventory levels, better on-shelf availability of our store inventory and a higher percentage of replenished items that flow straight to the shelf.

We've been developing this system over the last couple of years, and we've been ramping up the percent of our assortment being managed by this new system. It's currently active on approximately 15% of our assortment, representing 20% to 30% of total replenishment that flows to our stores. For the items being managed by this new system, we are seeing favorable outcomes, including lower out-of-stocks and lower levels of backroom inventory.

We're also testing and rolling out distribution center automation designed to increase our speed and simultaneously reduce store backroom labor and inventory. While the new technology at our Perth Amboy facility is one example of this capability, we're also testing a complementary technology at our distribution center here in the Twin Cities. This new technology is focused on moving sortation labor out of store backrooms, organizing shipments to minimize the number of footsteps needed to restock our sales floors and reducing the amount of excess inventory in our store backrooms. We've been testing this new technology, which is integrated into a new warehouse management system, in our Twin Cities DC this year. And based on learnings and encouraging early results, we plan to extend the test into several other facilities next year.

And finally, our store teams have been rolling out a system designed to optimize intraday replenishment between our store backrooms and the sales floor. The goal of this new system is to have fuller shelves and enhanced availability for our guests while simultaneously reducing backroom inventory levels. Since rolling out this new system in August, we've seen very encouraging results, including a 17% reduction in backroom inventory units. Our teams are telling us that their backrooms have never been so well organized going into a holiday season, something which should translate into strong execution during our busiest time of the year.

And one final note, I've spoken several times in prior earnings calls about our work to improve processes and drive efficiency in our store fulfillment capabilities like ship-from-store, Order Pickup and Drive-Up. But it's always one thing to hear about these improvements and another to see how they work. So our communications team, in cooperation with our store and headquarters team, put together a video showing how our team accomplishes these tasks and how these capabilities work for our guests. This video can be accessed by visiting corporate.target.com, and I encourage you to take a look.

So before I turn the call over to Michael, I want to pause and thank the entire team, from our team at headquarters through the supply chain and our stores, for all the work that has gotten us to where we are today. In many ways, we are still early in the journey, but that doesn't mean there's been a small amount of effort. We've designed and are now implementing comprehensive changes to how we move product, how we replenish our store inventory, how we operate our stores, how we interact with our guests and how we fulfill their digital orders. Any of these changes in isolation won't be big, but when you put them all together, it's been an incredible effort. In the face of challenges, I've seen our team respond with

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passion, enthusiasm and seemingly endless energy to move from theory to reality, and today, I'm proud to share what the team has already accomplished and equally excited about what lies ahead.

Now I'll turn the call over to Michael who will share his thoughts on third quarter financial performance and our outlook for the fourth quarter and full year. Michael?

Michael J. Fiddelke - *Target Corporation - Executive VP & CFO*

Thanks, John, and good morning, everyone. I'm really excited to join you on this morning's call, and I look forward to meeting with many of you in the months ahead.

As Brian mentioned earlier, our third quarter financial results were outstanding, reflecting unexpected strength across multiple parts of our business. As a result, we delivered EPS well above our expectations, and we have increased the midpoint of our full year adjusted EPS guidance by $0.30 compared with the previous range. Third quarter comparable sales increased 4.5%, about 1 percentage point higher than both our second quarter growth and our expectations. When you compound this growth on top of our 5.1% increase last year, you'll see that comparable sales have grown nearly 10% over the last 2 years.

Among sales channels, store comparable sales increased 2.8% in the quarter, more than 1 percentage point faster than our second quarter pace of 1.5%. Digital comp sales grew 31% in the quarter on top of 49% last year and contributed 1.7 percentage points to our total company comp.

As you know, we focus first on driving traffic in our business because it indicates the continued relevance of our brand and growing engagement among our guests. That's why we're pleased that traffic continues to be the primary driver of our growth. Comparable traffic was up 3.1% in the third quarter, driven by increases in both our stores and digital channels. Growth in average ticket drove another 1.4 percentage points of our comp growth.

On the operating income line, we saw a rate increase of about 80 basis points compared with last year. This was well ahead of our expectations, reflecting multiple beneficial factors. The first was category mix, which contributed about 30 basis points of gross margin improvement in the quarter. This was the result of exceptional strength in apparel combined with soft sales trends in our electronics and Entertainment categories. On top of the mix benefit from stronger-than-expected apparel sales, we also saw a rate benefit within that category as the business delivered a higher-than-expected mix of full price sales.

Outside of category mix, we also enjoyed a favorable mix in fulfillment, which took 2 forms. The first was a stronger-than-expected mix of sales in our stores, which is our lowest cost fulfillment channel. In the third quarter, all of the upsides to our comp expectations occurred in our stores. In addition, within our digital fulfillment options, same-day services drove 80% of our growth. And as we've outlined in prior calls, these options have much more favorable cost and profit dynamics compared with shipping to our guests' homes.

On top of category and fulfillment mix, our buying teams continue to develop merchandising strategies that deliver strong margin performance based on our ongoing efforts to optimize costs, pricing, promotions and assortment within each of their individual categories. In total, our third quarter gross margin rate was up about 110 basis points from a year ago, reflecting the benefits I've cited above, combined with a favorable comparison over some elevated costs reflected in last year's gross margin results. Specifically, as you'll recall, last year, we experienced elevated supply chain expenses in the third quarter driven by meaningful investments in toy and baby inventory and a rapid buildup of holiday receipts,

On the depreciation and amortization expense line, we saw an increase of $45 million or 8.5% compared with last year. This increase reflects a number of factors, including base investment trends, our decision to roll out new flexible store fixtures which accommodate incremental peak capacity for pickup and Drive-Up orders and the impact of timing compared with last year. In total, third quarter operating margin dollars were up more than 22% from last year, reflecting the combination of unexpectedly strong sales and rate performance.

Interest expense was down slightly in the third quarter, reflecting lower average debt balances, while our income tax provision increased approximately 100% compared with last year. This increase reflected higher pretax earnings this year combined with the impact of discrete items in last year's results, which made last year's effective tax rate unusually low. All together, our operations generated adjusted EPS of $1.36, an increase of nearly 25% compared with $1.09 last year. Third quarter GAAP EPS from continuing operations of $1.37 was up more than 18% from last year when we recorded $0.07 of benefit from the discrete tax items mentioned previously.

Now I want to turn to cash flow and our priorities for capital deployment, and I first want to briefly reiterate those priorities, which have remained consistent for decades. We first look to fully invest capital in projects that meet our strategic and financial criteria. Second, we support our dividend and seek to extend the company record of annual increases in dividend per share, something we've accomplished every year since 1971. And finally, we use share repurchase to return any excess cash beyond those first 2 uses with the goal of maintaining our middle A credit ratings.

Turning first to CapEx. We now expect to spend somewhat less than our original plan of $3.5 billion in 2019 and have an updated spending expectation of approximately $3.1 billion for this year. Savings from our original plan are primarily driven by efficiencies we've realized on a portion of our capital projects, combined with the smaller benefit from the retiming of some project spending into next year. As we look ahead, we continue to expect to invest about $3.5 billion in CapEx in 2020, reflecting our plan to complete nearly 300 additional store remodels for the year.

In 2021 and beyond, we expect to moderate the pace of our remodels to a range of about 150 to 200 stores per year. With this moderation in the number of remodel projects, we expect our pace of CapEx will move into the $2.5 billion to $3 billion range annually, closer to the amount of D&A we record on our cash flow statement.

Turning next to inventory. Our third quarter balance sheet showed a decline of nearly $1 billion or about 8% compared with last year. However, given that this inventory position was about 8% higher than 2 years ago, the year-over-year decline is largely a reflection of the specific inventory investments we made in advance of the fourth quarter last year. As we approach this year's peak season. We feel very good about both the level and makeup of our inventory, which should position us to extend the strong sales and earnings performance we've seen so far this year.

So with that as context, let's review how our capital deployment priorities have played out so far in 2019. Through the first 3 quarters of the year, our operations have generated more than $4.1 billion in cash, up more than $500 million from the same period last year. We have deployed that cash along with a portion of our cash on hand at the beginning of the year to fund $2.4 billion of CapEx, paid just under $1 billion in dividends and repurchased about $900 million of our shares.

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increase in operating margin dollars and an expected range for adjusted EPS of $1.54 to $1.74. And today, based on our third quarter performance and fourth quarter outlook, we raised our full year guidance range for adjusted EPS to $6.25 to $6.45. The midpoint of this new range is $0.30 higher than the midpoint of our prior guidance range.

If we achieve performance at the midpoint of our expectations, that would translate into full year comparable sales growth of about 4%, operating income dollar growth in the low teens and EPS growth in the mid- to high teens. All of these metrics are much stronger than we anticipated at the beginning of the year driven by upside in sales, category mix and fulfillment mix within our digital channels.

At the beginning of the year, Cathy articulated our longer-term financial expectations for the durable financial model we have been developing

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Christopher Michael Horvers - *JP Morgan Chase & Co, Research Division - Senior Analyst*

Can you talk a little more specifically about the cadence of the quarter? Do you think weather had any impact on the business given the warm September? And do you think this was fully made up for given the strong end to the quarter?

Brian C. Cornell - *Target Corporation - Chairman & CEO*

I mean Chris, we saw really balanced performance throughout the 13 weeks of the quarter. And I think you saw the really exceptional performance in categories like apparel where we performed extremely well, growing at a rate of over 10%, picking up significant market share. And as I highlighted in my earlier comments, all of those subcategories within apparel performed really well. So we saw strength in our business throughout the 13 weeks, and I think the team saw really strong performance across all of our categories.

Christopher Michael Horvers - *JP Morgan Chase & Co, Research Division - Senior Analyst*

Understood. And then as you look ahead, there's some countervailing factors. So electronics and toys do go up substantially in the mix. How are you thinking about those categories into the holiday? But then on the other hand, obviously, the e-commerce stack was very impressive and -- at least back here in the fourth quarter. So how are you thinking about the holiday broadly and electronics, toys and e-commerce as you look ahead?

Brian C. Cornell - *Target Corporation - Chairman & CEO*

Chris, I think we are really well prepared for the fourth quarter. Our teams have done an exceptional job in putting together the right assortment for the holiday season. And as always, we know that during that holiday period, we're going to amplify our focus on electronics and toys. We're well prepared in those categories with a number of new and exclusive items. So I think we're in a terrific position as we get ready for the upcoming weeks. And particularly from an electronics, toy and seasonal standpoint, I think we're going to stand tall.

Operator

The next question comes from Michael Lasser with UBS.

Michael Lasser - *UBS Investment Bank, Research Division - MD and Equity Research Analyst of Consumer Hardlines*

One way to interpret the combination of your very healthy digital growth and the decline in your REDcard penetration is that you're bringing in more marginally attached guests, and now you have the ability to transition those guests to more regular customers and regular guests. Is that the right way to think about it? And what does the adoption look like as the guest goes from trial of these various fulfillment options to broader adoption?

Brian C. Cornell - *Target Corporation - Chairman & CEO*

Yes. Michael, I'd start with the real health that we're seeing in overall traffic growth. So obviously, we're seeing more footsteps in our stores, more visits to our site. I think that's going to translate into a guest that's shopping more categories and greater relevance and a stronger relationship with that guest. So we can try to parse how that guest is changing over time, but I think the important thing is we just continue to see really strong

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started to visit Target and now may come in for toys that are shopping other categories in beauty and essentials begin to shop in our style categories more frequently. So those are the indicators that we look at as we plan for the future.

Michael Lasser - *UBS Investment Bank, Research Division - MD and Equity Research Analyst of Consumer Hardlines*

That's helpful. And my follow-up question is, as you look towards next year and you think about the algorithm that you laid out, will more of the margin expansion inherent in your expectation of mid-single-digit operating income growth come from gross margin, like you've experienced in recent quarters due in part to the mix shift to both better categories and fulfillment options? Or will it come from more SG&A leverage? And how should we think about the drivers between those 2 factors in the next couple of quarters?

Michael J. Fiddelke - *Target Corporation - Executive VP & CFO*

Well, we aren't going to get into the specifics for 2020 in today's call. But we feel really good about the gross margin strength we've seen so far this year, and we'd expect a moderate increase to gross margin rate in Q4 as well.

Operator

The next question comes from Matt McClintock with Raymond James.

Matthew J. McClintock - *Raymond James & Associates, Inc., Research Division - Research Analyst*

Congrats, Michael, and best wishes to both Cathy and Mark. Brian, you talked about apparel for a little bit, but I wanted to dive more into it because greater than 10% growth in your apparel business probably means you grew in absolute dollars more than anybody in the entire United States apparel industry. So -- and even if that's not the case, it's an acceleration from 5% last quarter. So can you dig more into what's driving that? Is that private label brands? Is that national brands, like what you saw at Levi's? And then what exactly are you doing in Jewelry and accessories that's driving that growth there?

Brian C. Cornell - *Target Corporation - Chairman & CEO*

Yes. So I appreciate the call-out, Matt. We did certainly see an oversized increase in market share during the quarter in apparel. I think our teams have done a fabulous job of curating our owned brand assortment, really having the right assortment in front of the guests. We've delivered exceptional quality and value in those categories. I think we've been on trend for the season. And I think our commitment to our new store operating model, where we have dedicated business owners in that apparel category that are helping our guests each and every day, is really driving great results. So the combination of the work we've done with our own brand assortment, adding some new national brands like Levi's in select stores, the service that we're delivering in store and the inspiration we're creating online has really come together in the apparel category.

So I'm really proud of the work the team has done there. I think it's a great example of how our strategies come together, where we remodel stores and create an inspiring in-store environment, we surround our guests with exceptionally well-trained team members who are providing on-trend styles at a great value. And we're providing a similar experience online. So I really, really feel great about the work the team has done there, and I think it's one of the highlights of our quarter, if not for the entire year.

Matthew J. McClintock - *Raymond James & Associates, Inc., Research Division - Research Analyst*

And then, John, clearly, you're excited about same-day options this holiday season. And I was just trying to think about, given -- strategically, given that it's a shorter holiday season than in years past, is it even more of a strategic competitive advantage to offer same-day options? And do you think that that's actually going to accelerate adoption by customers?

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John J. Mulligan - *Target Corporation - Executive VP & COO*

We do. And I mean, I am excited about the great progress the team has made over the past year in our same-day offerings, Order Pickup, Drive-Up, Shipt, all the investments we've made there to improve the efficiency of the team and their ability to ensure that we have a package ready for you in an hour or less regardless of how you're going to interact with us. And I think you're right. When people become time strapped, digital is an easy way. And being able to knock it off your list very quickly that day, if you want to pick it up, great; if you just want to swing by, we'll put it in your car; or we'll deliver it to your home, I think that becomes incredibly important.

And as always, I think the stores are at the center of how we deliver. That gives us great speed. And as you get near the end of the holiday season, the stores become such a huge advantage for us. We'll be well stocked. We'll have a great team there, like Brian pointed out, providing service. And if you -- again, if you want to order it online, we'll have it sitting there waiting for you either to put in your car or come in and grab it. So we're very excited about the opportunity this holiday season with the growth we've seen and the growth that's in front of us from a same-day perspective.

Operator

Our next question comes from Scott Mushkin with R5 Capital.

Scott Andrew Mushkin - *R5 Capital Ltd - Founder & CEO*

So my first question is actually to Michael. I think you talked about at the end what surprised you kind of going into the -- what the performance is versus what it was going to the year. And I was wondering if you could just get in a little more detail why you were above plan and the sustainability of some of those trends.

Michael J. Fiddelke - *Target Corporation - Executive VP & CFO*

Sure, Scott. Thanks for the question. I think it starts on the gross margin line and kind of back to the key themes from my remarks earlier, strength there. When apparel is running at 10% comp, that's really healthy on the margin line, good gross margin rates in that category. And we sell more product at reg price versus a discount at the end of the season when our style categories do well.

The second was the stronger-than-expected store sales. That's always helped lift the margin. And then finally, to maybe piggyback on some of what John just said, where our digital fulfillment growth came from. When those same-day options that the guest is responding to drive 80% of our digital growth, that's healthy from an operating margin rate perspective as well on a year-over-year basis.

Scott Andrew Mushkin - *R5 Capital Ltd - Founder & CEO*

And the sustainability of some of these trends in your mind?

Michael J. Fiddelke - *Target Corporation - Executive VP & CFO*

I think the teams worked hard to build an algorithm that's got good sustainability in the long run. When it comes to Q4, Q4 is its own animal. So we built Q4 bottoms-up, looking at how all those factors fit together. And so we'd expect, again, moderate gross margin rate expansion in Q4, but it will be modest compared to the point of expansion we saw in Q3.

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Brian C. Cornell - *Target Corporation - Chairman & CEO*

Scott, I wouldn't describe it as a surprise. But I think as you look at the third quarter, I started with the strength in traffic, up 3.1%; the strength in our stores comping at almost 3%. The continued strength in digital in our 2-year stack in the quarter rounds to 10%. So we're putting good numbers on top of good numbers. We'll continue to do that over time. But I think the balance in our portfolio where both our style and essential categories are performing, our stores are driving growth, our digital channels are continuing to accelerate, the overall composition of the quarter, to me, was a very high-quality quarter where all factors of our business were working together as one.

Scott Andrew Mushkin - *R5 Capital Ltd - Founder & CEO*

Great. And then a quick follow-up question. I think there was a comment that the remodels in the second year are performing better than expected. And I was just wondering if you could give -- some of our survey data is actually showing the same thing. So I was wondering if you could give us a reason why you think that's happening and, again, the sustainability of that.

Michael J. Fiddelke - *Target Corporation - Executive VP & CFO*

We're a few years into this now, and we have consistently seen the second year performance. We didn't expect that going into this, honestly, and we didn't model for it as we looked at the financials of the remodels, but it's certainly a pleasant surprise. So we believe it is sustainable because we continue to see it for the second year of the second year, I guess, you would say. So we're pleased with that.

I think what drives it is the guests come in, it takes them a little while to figure out the store. We see them engage with the store immediately because the environment is so much better, the presentation is better. You pair that, as Brian said earlier, with the change in the operating model and better service in the store -- in many parts of the stores, great training for our team so that they can be of more assistance to the guests, and then we see the guests continue to engage in different parts of the store and really experience the whole -- everything we have to offer. And so it's really the culmination of everything we're doing to create that great in-store experience that continues to build as we go through the remodel process.

Brian C. Cornell - *Target Corporation - Chairman & CEO*

And Scott, I'll give you a little additional insight. When we talk to guests who come into a newly remodeled store, and they might have been a previous Target shopper in that store, some of the feedback we get is have we added new categories, have we added new assortment. So because of the changes we've made in the core, the layout, the experience, they start to discover even more categories than they had shopped before. And I think that's a big part of what we're seeing in year 2.

additional categories, and I think that's heleing us pick up market she stin those remodeled stores in multiple categories.

Scott Andrew Mushkin - *R5 Capital Ltd - Founder & CEO*

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Operator

Our next question comes from Ed Yruma with KeyBanc Capital Markets.

Edward James Yruma - *KeyBanc Capital Markets Inc., Research Division - MD & Senior Research Analyst*

I guess, first, to unpack a little bit more gross margin gains, obviously very impressive. How much of it -- I know you called out apparel, but how much of it do you think broadly is from success in your investments and your process in private label? And kind of how do you see penetration moving as we think about 2020? And then second, obviously, you've seen some very strong success in same-day pickup. I know you're adding labor there. But how do you feel about your ability to scale that business from even a physical perspective, either from a backroom or from front of the house perspective?

Brian C. Cornell - *Target Corporation - Chairman & CEO*

Ed, why don't we let Michael start and talk about some of the gross margin gains and obviously, the benefits of the 40 new owned brands we've rolled out over the last couple of years. And then John can talk about the scalability of our fulfillment models.

Michael J. Fiddelke - *Target Corporation - Executive VP & CFO*

Yes. Thanks, Ed. On the owned brand front, it really starts with providing products that we think the guests will respond to and so curated owned brand product that drives repeat purchase and loyalty over time. So we start there. And when that owned brand product does well, it translates favorably to the gross margin line. And so the strength we've seen and the growth that will bring us over time has definitely been a positive on the margin side.

John J. Mulligan - *Target Corporation - Executive VP & COO*

So Ed, we will -- the way I'd start is we will pick, pack and deliver either in store, through pickup and Drive-Up or Shipt to guests more packages in the next 5 weeks than we did in the entire year of 2015. And so the teams have done an outstanding job of going back, redoing processes, investing in technology, investing in training, reengineering our processes continually. And this year, we've seen productivity increases in pick, prep and pack and ship of close to 60% in store. So we believe we have a significant runway in front of us to continue that.

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Brian C. Cornell - *Target Corporation - Chairman & CEO*

Yes. Kate, why don't I start. And for several years now, we've been talking about our commitment to being priced right daily and making sure that we're communicating to our guests that every time you shop Target, we're delivering great value. And we've been talking for several quarters now about the benefits of that investment, the benefits of that communication and the fact that we're seeing a significant portion of our business move to everyday pricing, and I really describe it as everyday value. So that continued in the quarter, and I think that's going to continue for some time to come as we continue to reinforce to our guests that every time you shop our stores, we're going to deliver great value, we're going to be priced right daily on those items that we know are so important to our guests. And that's a commitment that's been in place for several quarters and will continue for years to come.

Katharine Amanda McShane - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

Okay. And if I can just follow up. I know tariffs continue to be headlines at this point and nothing is certain, but could you walk us through if List 4B were put to effect, how much you've been able to or you can mitigate versus how much price you think you'll need to take?

Brian C. Cornell - *Target Corporation - Chairman & CEO*

Yes. Kate, we've been watching the headlines as others have each and every day. And we've been obviously working for several years now to diversify our sourcing matrix. I think we are well positioned to deal with some of the challenges that could be in front of us. I think we've said the last couple of quarters -- in Q2, tariffs pressured us by about $50 million. In Q3, that's going to be about a $60 million pressure. But our teams, particularly our merchants and our sourcing team, have done a phenomenal job of really working through this challenging landscape and allowing us to deliver great value to our guests at a time when they need it most.

So we'll watch the next list. We'll see what happens as we go into the next couple of weeks and into the start of 2020, but I think we're well prepared to react. And obviously, we're all facing the same tariff issues together. I think our size, scale, the sophistication of our team and our vendor partners positions us well to kind of navigate this uncharted water.

Operator

Our next question comes from Karen Short with Barclays.

Karen Fiona Short - *Barclays Bank PLC, Research Division - Research Analyst*

Congratulations on a great quarter.

Brian C. Cornell - *Target Corporation - Chairman & CEO*

Thank you. We appreciate that.

Karen Fiona Short - *Barclays Bank PLC, Research Division - Research Analyst*

Just wanted to actually follow up on that tariff question. Taking the opposite angle, if List 4 were to not be enacted, would there maybe be a little upside to the guidance for 4Q?

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Brian C. Cornell - *Target Corporation - Chairman & CEO*

We'll watch it carefully obviously. If some of the tariffs are pulled back, there's going to be upside going forward. I wish I could tell you what's going to happen, but we're watching the same reports that everyone else is right now. So obviously, we're going to hope for the best. And depending on what happens, it will give us a chance to either invest in the business and drive even greater acceleration in our trends. But we'll watch it carefully, Karen, and we'll decide once we have greater clarity.

I think for all of us right now, the biggest challenge is uncertainty. And as soon as we get greater clarity, we'll be able to make better decisions and navigate these choppy waters. But right now, Target, like all of our peers, we're looking for greater clarity, greater certainty, and as soon as we get that, we'll decide how to deploy those funds.

Karen Fiona Short - *Barclays Bank PLC, Research Division - Research Analyst*

Okay. And then I wanted to just ask about -- obviously, there's so much going on in apparel that's positive, and you called out many of it, but you actually didn't mention the 20th anniversary collection. I was just wondering if you could give a little color on that. I mean we know it's not a huge comp driver, but any context you could give on that, on how it went?

Brian C. Cornell - *Target Corporation - Chairman & CEO*

Well, I think it was incredibly well received by our guests. I think our team did a fabulous job of executing the plan. It built enormous awareness and traffic to our stores. And it's just one of those moments where we can surprise and delight our guests. And going back and thinking about thethat,os. Ny

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Paul Lawrence Lejuez - *Citigroup Inc, Research Division - MD and Senior Analyst*

Can you talk a little bit about the Good & Gather line, just the initial response? Also curious, what percent of your Food and Beverage was private label prior to launching Good & Gather? And where do you expect that to go over the next few years?

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