

TIFFANY & Co.

STOCK ANALYSIS
ST. JOHN'S UNIVERSITY
STUDENT MANAGED INVESTMENT FUND

Recommendation: Purchase of 350 Shares

Total Purchase: \$15,004.50

Percent of SMIF Holdings: 1%

Industry: Specialty Retailers

Share Data:

Price: \$42.87

Date: 18 November 2005

52 Week Range: \$28.60-\$43.80

Market Cap: 5.89B

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EXECUTIVE SUMMARY

It is the recommendation of this group to purchase 350 shares of Tiffany & Co. stock. As of 18 November 2005, the price per share was \$42.87. This would account for just over 1% of the holdings had by the Student Managed Investment Fund.

Through both our absolute and relative valuation models, it was determined that Tiffany & Co. is undervalued by the market. It was determined via relative valuation that Tiffany & Co. is worth \$56.63 per share. This is assuming buyback of shares will take place. This price was chosen over the absolute valuation price of \$60.17 because the growth rate used may be too high.

In comparison to its competitors and the specialty retail industry, Tiffany & Co. has a better financial standing. Its operating and liquidity ratios are higher than its competitors. The company is not leveraged through long-term debt, leaving it open to a wide array of investment possibilities.

In addition, a correlation exists between the price of Tiffany & Co. and that of various gold indices and stock. It is forecasted that gold is increasing, meaning that if the historical correlation holds, Tiffany & Co. could potentially see its stock price increasing as well.

COMPANY OVERVIEW

Tiffany & Co. is a retailer that specializes in fine jewelry. Traded publicly on the New York Stock Exchange under the ticker symbol "TIF", Tiffany's has become one of the most well known companies in the world. Continuing to grow, the company has been able to stay successful over a long period.

Tiffany & Co designs and manufactures goods such as timepieces, silver, china, crystal, and stationery. Tiffany & Co. has been able to expand its consumer market by expanding its product line to include lower priced merchandise. This includes items such as key chains and porcelain mugs that sell for less than \$50. The goods produced by Tiffany & Co. are available in some 150 stores and boutiques worldwide, through its catalog and website.

Tiffany & Co plans to expand by opening new locations in such venues as upscale shopping centers. The store sizes will be kept between 4,000 to 7,000 square feet, as opposed to the previous store sizes of 1,500 to 16,000 square feet.

With its products selling all around the world, Tiffany generates revenues from many different countries. For FYE 2005, Tiffany's generated revenues from the following areas: the United States, which represented about 59% of Tiffany's net sales, Japan, which represented 22%, Asia-Pacific, which represented 7%, and Europe, which represented 6%. The remaining 6% is spread among smaller countries not located in the regions above.

Tiffany & Co. uses four channels of distribution: U.S. retail, international retail, direct marketing, and other. Retail occurring in the United States accounts for about 48% of yearly sales that come from sales in Tiffany & Co. stores. International retail makes up about 39% of total sales, which come from markets outside U.S. as well as internet sales. Direct marketing includes business to business, as well as internet and catalog sales in the U.S. and it accounts for 9% of total sales. Direct marketing has been substantially growing over the past couple of years due to the popularity and easiness of online shopping. Sales from the company's diamond sourcing and manufacturing operations accounts for 4% of sales.

Tiffany's plans to expand through Little Switzerland, of which it owns 98%. Little Switzerland consists of more than 20 duty free cruise ship destinations in the Caribbean, Alaska, and Florida. Tiffany has opened two new concept stores that focus on pearls, called Iridesse. Up to 20 such stores, where jewelry is sold in the price from of \$100 to \$40,000, are in plans to open over the next five years.

In 2003, Tiffany & Co purchased a stake in Temple St. Clair for \$13 million to diversify its retail operations. Temple St. Clair is a New York based jewelry maker with its home office located in Soho. This store once sold its pieces in specialty stores like Bergdorf Goodman and Saks Fifth Avenue until it was bought by Tiffany & Co in 2003. Tiffany & Co does not sell any products under the Temple St. Clair brand name nor does Temple St. Clair sell any products under the Tiffany brand name. Temple St. Clair does, however, make a couture line of jewelry for the Tiffany & Co brand that ranges in price from \$500 to \$35,000. Its target market is women ages 30 to 60 who buy for themselves

and tend to favor more gold and colored stones. Two stores featuring Temple St. Clair jewelry were recently opened in California and New Jersey.



Figure #1: Tiffany & Co. Stock Price – One Year
Source: BigCharts.com

The last year has shown a tremendous growth for Tiffany's stock. Starting at just above \$30, it has hit a high just under \$44. Over the last year, Tiffany's has constantly outperformed earnings expectations. For instance, Thompson Financial forecasted \$519.6 million in sales for the 2nd Quarter. Tiffany's, however, reported sales in the amount of \$526.7 million. The major increase in both volume of stock traded and increase in price shown in the end of August was due to this announcement.

In 2004, the Company sold off its 15% ownership of Aber Diamond Corporation. This was because Tiffany believes that it no longer needs this company as a holding. Originally purchasing Aber for \$70 million, Tiffany's 13.9% stake in Aber was sold for \$268 million. This affects Tiffany's because it no longer will receive diamonds from Aber at a discount. In addition, an agreement is in affect until 2013 that requires

Tiffany's to buy at least \$50 million in diamonds, one-third of its annual needs, from Aber each year.

In 2003, Tiffany's announced it would buyback \$400 million in shares from its stockholders. This buyback will be completed by 2007. For purposes of this valuation, it is assumed that 80% of the announced buyback amount will actually be bought back. This would mean that \$320 million total would be purchased back from its shareholders. By the end of FYE 2004, \$75 million had already been purchased back. The remaining \$245 million was used to assist in the creation of the pro forma income statement.

EARNINGS ANNOUNCEMENTS

Over the course of the last year, Tiffany's stock price has been influenced by its earnings announcements. The following is an overview of the first three quarters for FYE 2006 and how the stock price was affected by the announcement.

13 May 2005

- Tiffany & Co announced its first quarter earnings: net sales increased 12% to \$509,901,000, while net earnings rose 9% to \$40,058,000. U.S. based Tiffany & Co. stores reported an earnings growth of 11%; the company as a whole reported a gross margin of 53.9%. Tiffany & Co repurchased 1,036,792 shares of their common stock at an average of \$32.77 for a total cost of \$33,978,000. The closing price of the stock for May 13, 2005 was \$29.30.

31 August 2005

During the second quarter, net sales increased 11% to \$526,701,000 while net earnings increased 53% to \$50,551,000. The company repurchased 1,538,520 shares of

their common stock at an average of \$32.48 for the total of \$49,970,000. The closing stock price on August 31, 2005 was \$32.74.

30 November 2005

Earnings for the third quarter were reported as expected. Net sales, however, did not meet expectations. Net sales increased by 8% from the second quarter to \$500,105,000, while net earnings grew by 37% to \$23,789,000. In total, the company had a gross margin of 54.1%. Tiffany's also repurchased 790,997 shares of its stock at an average price of \$38.42. The stock closed at \$40.70, a decrease of \$1.44 from the previous day. The total amount of shares repurchased during the three quarters is 33,366,309 shares at the total value of \$83,948,000. Tiffany & Co has about \$295 million left over for future repurchases.

INDUSTRY ANALYSIS

Specialty retail contains various companies with a broad scope of product offerings. Generally, retailers in this industry only sell one product or specialize in one area. According Standard & Poor's, the specialty retail market accounted for 72% of the \$3.5 trillion in U.S. retail sales in 2004.

INDUSTRY LIFE CYCLE

The specialty retail industry is currently in the mature stage of the industry life cycle. From the 1970's to the 1990's, the specialty retail industry experienced a large growth with the increase in shopping malls in the United States. Over the last few years, that growth has slowed, leading to the success of larger specialty retailers. Wholesale

clubs, for example, were able to attract customers with lower prices than those that were offered in malls. A channel being used for many specialty retailers to grow is the internet. Companies of all sizes are able to offer their products online to a larger consumer base than previously possible.

Future sales and profits in the specialty retail industry will be higher in proportion to those of years past. This is primarily due to the expansion of internet sales.

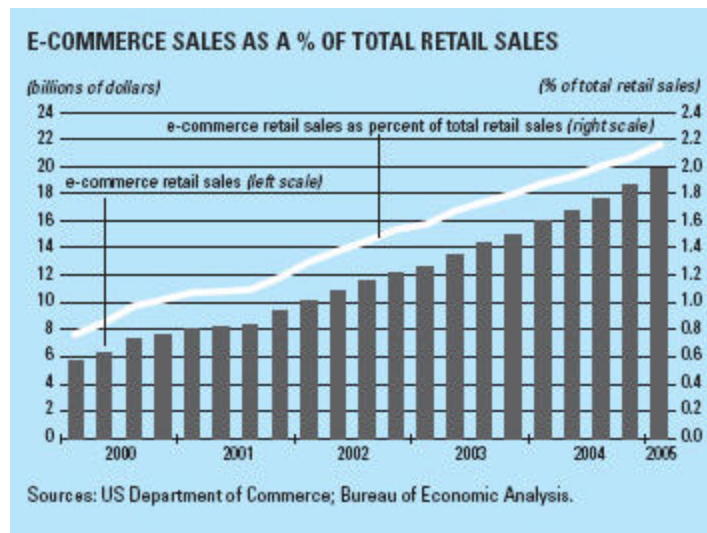


Figure #2: E-Commerce Sales As A % Of Total Retail Sales
Source: US Dept of Commerce

As shown in Figure #2, e-commerce sales increased from about 0.6% to close to 2%, measuring to over \$14 billion dollars, of total retail sales since 2000. Jewelry stores in the specialty retail industry showed this growth, as well. Two online luxury jewelry stores, Blue Nile Inc. and Odimo Inc., saw sales increases of 30% and 26%, respectively, from 2003 to 2004. This shows that while the majority of sales happen in store, there is a market for luxury items offered online.

MARKET TRENDS

In the jewelry portion of the specialty retail industry, a clear factor determines the up or downward trend.



Figure #3: Comparison between TIF and XAU
Source: BigCharts.com

Figure #3 shows Tiffany and Co. in relation to a gold index. XAU trades on the AMEX and contains 12 gold companies. This figure shows that areas of growth and decline for TIF and XAU occur at the same time. Since the beginning of 2005, both have grown 40%.

One of the stocks that XAU tracks is Placer Dome Inc. The symbol for Placer Dome is PDG.



Figure #4: Comparison Between TIF, PDG, and S&P 500
Source: BigCharts.com

Figure #4 shows Tiffany in relation to both Placer Dome and S&P 500. Throughout the course of this chart, it is shown that PDG is an indicator for how Tiffany's will perform. Despite the drop-off for Tiffany in the 2004-year, the rise in late 2005 in relation to the growth of PDG shows that it is possible for Tiffany's to continue to rise. Both Tiffany's and the S&P 500 were at the same area at the end of 2001, but Tiffany's has outperformed this index five years since.

MICHAEL PORTER'S ANALYSIS OF COMPETITIVE FORCES

Michael E. Porter developed the model of the Five Competitive Forces in his book "Competitive Strategy: Techniques for Analyzing Industries and Competitors." These forces determine the intensity of competition and can assist in the decision making of firms in any industry.

RIVALRY

The specialty retail industry faces fierce rivalry among its competitors. There are many factors that contribute to this intense rivalry. Low switching costs for consumers is one of the characteristics. When customers can switch from one product to another easily, that causes difficulties for the firm to retain customers. The large number of firms in this industry have also intensified the rivalry. All these firms must compete with each other to attract the same customers.

To gain an advantage in this industry, firms should differentiate their products and make use of vertical integration or distribution channels. Product differentiation includes applying innovations and improving features of the products.

THREAT OF NEW ENTRANTS

In the specialty retailer industry, there are a few significant entry barriers for new entrants to enter this industry. They are product differentiation and capital requirement.

- ***Product Differentiation:***

Product differentiation plays a very essential role in reducing competition in the industry. High-end specialty retailers usually differentiate their products by hiring skillful designers to create some unique products. Very often, their products are patterned or trademarked.

- ***Capital Requirement:***

Capital cost is one of the main entry barriers in this industry. The cost of raw material is very high. Raw materials like diamonds, precious stones, silver and gold are very expensive. The price of diamonds and precious metal has increased over the past

few years. Example would be the price of gold. New Entrants may face difficulties in acquiring high quality raw materials due to lack of capital. In addition, the new firm may not be able to afford an excellent store location and million dollars advertising campaign.

THREAT OF SUBSTITUTE PRODUCTS / SERVICES

A product that serves the same purpose of another product to satisfy customers' need is called a "Substitute product". In the specialty retail industry, the threat of substitute products or services is low. It is because most specialty retailers carry excellent brand loyalty. Brand loyal is very important element in fighting the threat of substitute products. High-end specialty retailer usually has a rather strong brand loyalty. Although other companies are capable of breaking into the industry with similar products, many consumers still stick with the high-end retailer because of their confidence in the brand name.

BARGAINING POWER OF SUPPLIERS

It is necessary for specialty retailers to maintain excellent relationships with its suppliers in order to provide products and services to the customers. The bargaining power of the suppliers is rather strong. In most cases, the company will enter an agreement with the supplier to ensure the source of materials. In the case of the jewelry industry, if a company does not have a supplier, it will not have product to sell.

BARGAINING POWER OF BUYERS

The bargaining power of buyers in the specialty retail industry is weak. Products provided in jewelry sector are not standardized; therefore, consumers cannot switch to another product very easily. For example, jewelry stores may offer a precious stone. Buyers in the jewelry sector are fragmented, so consumers do not have much influence on products and price.

ANALYSIS OF STRATEGIES

For the past few years, the main goal of Tiffany & Co. is to ensure the long-term integrity of the company's brand. Tiffany has pursued many strategies in order to achieve that goal. Strategies included discontinuing wholesale sales to independent retailers in the U.S. and Europe, as well as exiting from segments of the sales division that was focused on low-profit employee service-award programs. In addition, Tiffany's ended wholesale fragrance distribution around the globe. The company is trying to rebalance its product assortment with greater emphasis on high-priced, quality jewelry.

Tiffany & Co. also is a design-driven company. The Tiffany Legacy Collection is the best example. The company has maintained an active pace every year in introducing new products. A successful example would be the introduction of the ATLAS collection. Customers have responded to the ATLAS collection very well and the sales of that collection have exceeded expectations. Another example is the "Elsa Peretti Diamonds by Yard earrings", an original design copyrighted by Elsa Peretti. In 2004, the company introduced many new collections and new designs in tableware and accessories. Tiffany also introduced a new line of jewelry focused on pearl jewelry named "Iridesse".

COMPETITIVE STRENGTHS OF TIFFANY:

Tiffany & Co. Brand

Customers around the world trust and respect the brand. This customer loyalty is what the company believes is a critical element in the jewelry industry. Tiffany's believes, however, that its customer base can expand. The company's strategy for enhancing potential customers' awareness is to advertise and expand its public relations programs. This would include activities like educating customers about the brand and its fine products. For example, Tiffany's has advertised its products via posters on telephone kiosks as well as full-page advertisements in special publications around the world. The company aims to maintain a strong voice to customers so that they can experience the joy of shopping at Tiffany.

High Quality Control

According to Tiffany & Co., “Tiffany is about things that last, and the company maintains an uncompromising commitment to the highest standards, both in materials and craftsmanship.”

Tiffany offers a wide variety of products and designs. From classical to contemporary, the company believes in style, not fashion. Tiffany & Co. has an excellent merchandizing department who maintain an active role in developing new designs, timepieces, tableware and accessories.

Distribution Control

The company controls most of Tiffany’s distribution. The company currently has more than 150 stores in 17 countries. The goal is to add about 6 to 10 locations every year. Besides distributing products from the stores, the company engages in direct marketing activities. The company sells products through e-commerce, catalog and business gift sales.

RELATIVE INDUSTRY VALUATION

The S&P 500 is one of the most commonly used benchmarks for the overall U.S. stock market. By comparing the S&P 500 index with the specialty retail index, it is possible to see which index outperformed the other over a specific time period.

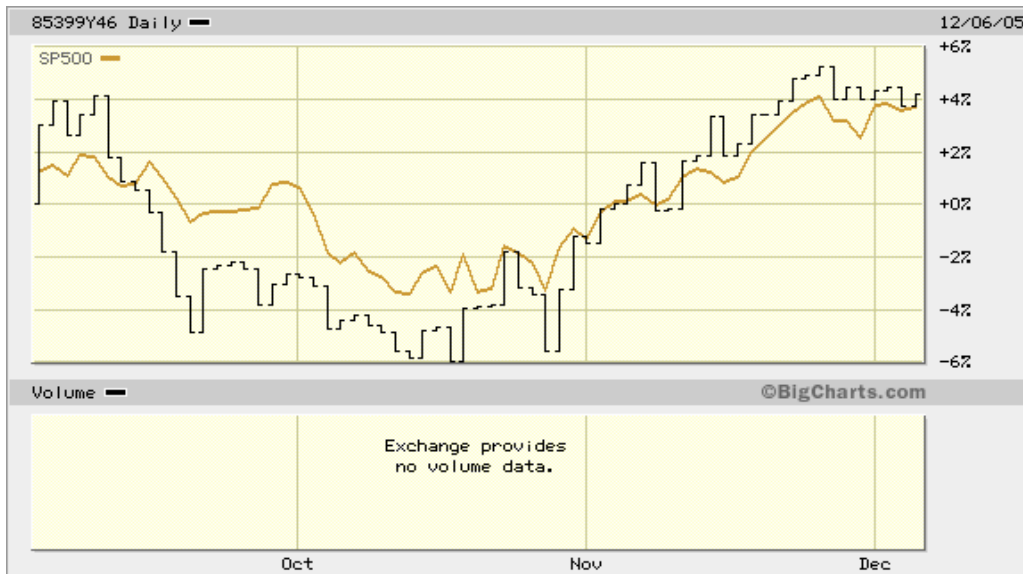


Figure #5: S&P 500 – Past Three Months
Source: BigCharts.com

As shown in Figure #5, in the past three months both the S&P 500 and the S&P 500 specialty retail stores index have been following the same pattern. At the end of September and beginning of October, the S&P 500 Index had significantly outperformed the S&P 500 specialty retail stores index. For November and December, the indices have followed the same pattern.



Figure #6: S&P 500 – Past One Year
Source: BigCharts.com

According to the Figure #6, the S&P 500 Index is steadier without great fluctuations. The S&P 500 specialty retail stores index has more significant increases and decreases. The S&P 500 specialty retail stores index decreases around April and then increases around July and August.

Overall, the S&P 500 index is more steady than the specialty retail index. This can be attributed to the fact that most specialty retailers have higher fourth quarter returns than that of other quarters. With the S&P 500 consisting of numerous sectors, the index can better handle quarterly changes.

OPERATING PERFORMANCE RATIOS

Operating performance ratios measure the efficiency of a firm in utilizing its assets to generate sales.

Return On Equity

Return on Equity					
	2001	2002	2003	2004	2005
Tiffany	22.65%	17.69%	16.92%	16.11%	19.20%
Zale	10.12%	16.19%	-5.21%	15.48%	13.87%
Finlay	21.96%	13.12%	4.72%	5.57%	9.99%
Industry	11.40%	13.70%	14.80%	18.20%	18.00%

Return on Equity (ROE) shows how much profit a company generates with the money shareholders have invested in it. ROE is useful for comparing the profitability of a company to other firms in the same industry. The ROE of Tiffany's is greater than its competitors and slightly above the industry.

Gross Margin

Gross Margin					
	2001	2002	2003	2004	2005
Tiffany	56.86%	58.73%	59.27%	57.87%	56.06%
Zale	50.00%	50.60%	50.20%	51.30%	51.40%
Finlay	50.40%	49.70%	51.60%	51.20%	51.80%
Industry	34.90%	35.80%	36.20%	39.70%	40.00%

Gross margin represents the proportion of each dollar of revenue that the company banks as gross profit. If a company's gross margin is 40%, this means it would make \$0.40 from each dollar of revenue generated. It measures mark-up over cost-of-goods. Tiffany and Co.'s gross margin is higher than its competitors and once again higher than the industry.

Net Margin

Net Margin					
	2001	2002	2003	2004	2005
Tiffany	11.43%	10.81%	11.13%	10.78%	13.80%
Zale	3.97%	6.57%	-1.84%	4.62%	4.48%
Finlay	2.65%	1.95%	0.76%	0.93%	1.74%
Industry	3.10%	3.90%	4.30%	5.20%	5.40%

This ratio measures the net profitability as a percentage of revenue. The higher the net margin, the more efficient a company has been operating and the more income the company generates out of each dollar of sales after all expenses. Once again Tiffany and Co.'s net margin has been much higher than its competitors and the industry.

LIQUIDITY RATIOS

These following ratios show how well the company can convert short-term assets into cash and cover its short-term obligations.

Current Ratio

Current Ratio					
	2001	2002	2003	2004	2005
Tiffany	2.98	2.8	3.57	3.41	4.02
Zale	2.84	2.68	2.5	2.57	2.55
Finlay	1.77	2.03	2.11	2.22	2.38
Industry	1.46	1.51	1.45	1.59	1.62

This ratio is used to give an idea about a company's ability to pay back its short-term liabilities with its short-term assets. The higher the current ratio, the more capable the company is at paying its liabilities. Tiffany and Co.'s current ratio, as shown, is about 2 times as greater than its competitors and almost 3 times greater than the industry.

Quick Ratio

Quick Ratio					
	2001	2002	2003	2004	2005
Tiffany	1.05	1	1.13	1.21	1.35
Zale	0.1	0.25	0.1	0.17	0.15
Finlay	0.24	0.34	0.48	0.58	0.51
Industry	0.41	0.51	0.55	0.67	N/A

This ratio is the same the current ratio except it considers only cash and marketable securities. The higher the quick ratio, the better the position of the company. Tiffany and Co.'s quick ratio was greater than the competition and the industry. This ratio shows that Tiffany and Co. was able to settle its obligations about one and a half times.

Inventory Turnover Ratio

Inventory Turnover					
	2001	2002	2003	2004	2005
Tiffany	1.24	1.05	1.03	1.05	1.01
Zale	1.5	1.4	1.4	1.4	1.4
Finlay	1.6	1.5	1.6	1.6	1.7
Industry	5.51	5.68	5.69	6.7	N/A

This ratio that shows how many times the inventory of a firm is sold and replaced over a specific period. A low turnover implies poor sales and, therefore, excess inventory. The low numbers shown by Tiffany's is not necessarily a negative implication. Tiffany and Co. is more of a high-end brand, which means its products are slightly more costly than its competition. The more costly the product is on sale for, the slower the turnover.

LONG-TERM SOLVENCY

Debt To Equity

Debt to Equity					
	2001	2002	2003	2004	2005
Tiffany	0.26	0.17	0.25	0.27	0.23
Zale	0.13	0.09	0.28	0.27	0.16
Finlay	1.67	1.51	1.51	1.47	1.18
Industry	0.38	0.4	0.42	0.32	0.27

Tiffany's debt to equity ratio in 2005 is 0.23, which means the company is not highly leveraged. The company uses more equity than debt to financial its activities. Compared to its competitors, Zales' debt to equity is 0.16, which means Zales also is not highly leveraged. Competitor Finlay is highly leveraged with a debt to equity ratio of 1.18. The industry as a whole uses more equity than debt with a ratio of 0.27.

Leverage Ratio

Leverage Ratio					
	2001	2002	2003	2004	2005
Tiffany	1.73	1.63	3.17	1.61	1.6
Zale	1.66	1.57	1.98	1.85	1.69
Finlay	4.51	3.92	3.89	3.89	3.32
Industry	N/A	N/A	N/A	N/A	1.66

This ratio indicates how much the company has borrowed. Tiffany's leverage ratio is not too high. At 1.60 indicates that the company has low borrowing. In fact, the company has been executing its stock repurchase program. Competitor Zales and the industry also have a low leverage ratio. However, competitor Finlay has an extremely high leverage ratio as 3.32. Finlay relies heavily on borrowing for its financial activities.

DUPONT ANALYSIS

The DuPont Model of Return of Equity contains three elements: Net profit margin, Total asset turnover and financial leverage.

$$\text{ROE} = \text{Net Profit Margin} * \text{Total Asset Turnover} * \text{Financial Leverage}$$

FYE 2003:

$$\begin{aligned} \text{ROE} &= 0.1113 * 0.4801 * 3.1667 \\ &= 0.1692 = 16.92\% \end{aligned}$$

FYE 2004:

$$\begin{aligned} \text{ROE} &= 0.1078 * 0.9271 * 1.6122 \\ &= 0.1611 = 16.11\% \end{aligned}$$

FYE 2005:

$$\begin{aligned} \text{ROE} &= 0.1380 * 0.8720 * 1.5957 \\ &= 0.1920 = 19.20\% \end{aligned}$$

According to this analysis, it shows that total asset turnover and financial leverage have driven the Return on Equity for the past 3 years. The total asset turnover increased dramatically from 2003 to 2004, going from 0.4801 to 0.9271. The financial leverage ratio has dropped from 3.1667 in 2003 to 1.5957 in 2005. Return on Equity based on the DuPont Model has increased from 16.92 % in year 2003 to 19.20% in year 2005 due to the significant changes in total asset turnover and financial leverage.

REVENUE FORECAST

Tiffany & Co. ends its fiscal year in January. This means that for every fiscal year ending, 11 of the 12 months reported were for the previous calendar year. The one month

that is part of the calendar year in which the annual report is released in is the month of January. In order to forecast FYE 2007, the remaining unannounced quarters of FYE 2006 must be forecasted as well. In this instance, the third and fourth quarters for FYE 2006 would need to be determined.

For FYE 2006, the first and second quarters had announced financials. The third and fourth quarters, however, were still unannounced. In order to forecast these numbers, the relationship between quarterly sales were observed from FYE 2002 to FYE 2005.

Quarterly Sales							
	2002		2003		2004		2005
1st Quarter	336,401	3.19%	347,129	14.03%	395,839	15.44%	456,960
	10.37%		7.86%		11.79%		4.30%
2nd Quarter	371,301	0.84%	374,427	18.18%	442,495	7.71%	476,597
	-10.30%		-2.24%		-2.80%		-3.24%
3rd Quarter	333,074	9.90%	366,033	17.51%	430,123	7.21%	461,152
	69.86%		69.11%		70.09%		75.67%
4th Quarter	565,759	9.41%	619,013	18.19%	731,588	10.73%	810,122
Total Revenues	1,606,535		1,706,602		2,000,045		2,204,831

Figure #7: Quarterly Sales – FYE 2002 to FYE 2005

Figure #7 shows the quarterly sales, in millions, as well the percentage change from quarter to quarter and from year to year. It was determined that from the second to third quarters, sales lowered at around 2.5%. From the third to fourth quarters, sales rose 70%. This produced the following forecast for FYE 2006.

Quarterly Sales	
	2006
1st Quarter	\$509,900 actual
2nd Quarter	\$526,700 actual
3rd Quarter	\$513,533 est.
4th Quarter	\$873,005 est.
Revenues	\$2,423,138 est.

The forecasted revenues for FYE 2006 is \$2,423,138,000. This number assists in the forecasting of FYE 2007's revenues.

Sales					
	2002	2003	2004	2005	2006
Tiffany & Co.	1,606.50	1,706.60	2,000.00	2,204.80	2,423.10
Industry Sales	162,538.00	176,083.00	191,741.00	121,708.00	140,000.00
Market Share	0.988%	0.969%	1.043%	1.812%	1.731%

Figure #8: Market Share
Source: Valueline

Figure #8 details the market share of Tiffany's from FYE 2002 to FYE 2006. The FYE 2006 industry sales number, like the Tiffany's revenue number, is a forecast. We estimate that the market share of 1.731% for FYE 2006 will be the same for FYE 2007. This number will remain unchanged and will be the primary source for forecasted FYE 2007's revenue for Tiffany's.

According to Value Line, the forecasted sales for the specialty retail industry for FYE 2007 are \$160 billion dollars. In keeping with Tiffany's market share of 1.731% gained from its FYE 2006, FYE 2007 for Tiffany's would produce revenues in the amount of \$2,769 million.

PRO FORMA INCOME STATEMENT

After forecasting revenues for both FYE 2006 and FYE 2007, a pro forma income statement was established. For both years, a percentage of sales approach was used to determine the various numbers on the income statement. The only number that is not affected by this is the income tax number, which was forecasted to be 35% for that year. The percentage used for FYE 2006 was determined after viewing the income statements

from FYE 2002 to FYE 2005. In addition, the percentages used for FYE 2006 were the same percentages used for FYE 2007.

Income Statement								
	2002	% of Sales	2003	% of Sales	2004	% of Sales	2005	% of Sales
Revenue	1,606.50	100.00%	1,706.60	100.00%	2,000.10	100.00%	2,204.80	100.00%
COGS	663.1	41.28%	695.2	40.74%	842.7	42.13%	974.3	44.19%
Gross Profit	943.5	58.73%	1,011.40	59.26%	1,157.40	57.87%	1,230.50	55.81%
Operating Expenses								
SG&A	633.6	39.44%	692.3	40.57%	801.9	40.09%	936	42.45%
R&D	---		---		---		---	
Other	0	0.00%	0	0.00%	0	0.00%	0	0.00%
Operating Income	309.9	19.29%	319.2	18.70%	355.5	17.77%	294.5	13.36%
Net Int Inc & Other	-20.6	-1.28%	-19.6	-1.15%	-12.8	-0.64%	177.6	8.06%
Earnings Before Taxes	289.3	18.01%	299.6	17.56%	342.7	17.13%	472.2	21.42%
Income Taxes	115.7	39.99%	109.7	36.62%	127.2	37.12%	167.9	35.56%
Earnings After Taxes	173.6	10.81%	189.9	11.13%	215.5	10.77%	304.3	13.80%
Acctg Changes	---		---		---		---	
Disc Operations	---		---		---		---	
Ext Items	---		---		---		---	
Net Income	173.6	10.81%	189.9	11.13%	215.5	10.77%	304.3	13.80%
Diluted EPS, Cont Ops\$	1.15		1.28		1.45		2.05	
Diluted EPS\$	1.15		1.28		1.45		2.05	
Shares	150		148		148		148	
Basic EPS					1.49		2.10	
Shares					145		145	

Earnings per share for FYE 2007 was estimated into two different scenarios. This is due to the expected buyback in shares that is taking place up to the end of FYE 2007. First, the earnings per share were forecasted assuming no buyback of shares. Then, a forecast of the earnings per share was forecasted based off 80% of the buyback announced, which is the average amount bought back by companies after its announcement.

Income Statement				
	2006	% of Sales	2007	% of Sales
Revenue	2,423.13	100.00%	2,769.60	100.00%
COGS	1,017.71	42.00%	1,163.23	42.00%
Gross Profit	1,405.42	58.00%	1,606.37	58.00%
Operating Expenses				
SG&A	969.25	40.00%	1,107.84	40.00%
R&D	---		---	
Other	0.00	0.00%	0	0.00%
Operating Income				
Net Int Inc & Other	-14.54	-0.60%	-16.62	-0.60%
Earnings Before Taxes				
Income Taxes	147.57	35.00%	168.67	35.00%
Earnings After Taxes				
Acctg Changes			---	
Disc Operations			---	
Ext Items			---	
Net Income				
Diluted EPS, Cont Ops\$	1.89		2.16	
Diluted EPS\$	1.89		2.16	
Shares	145		145	
Basic EPS	1.93		2.21	
Shares	142		142	
After buyback				
Diluted EPS, Cont Ops\$			2.24	
Diluted EPS\$			2.24	
Shares			140	
Basic EPS			2.29	
Shares			137	

RELATIVE VALUATION

Relative valuation focuses on determining a company's value compared to its peers and its industry. In the attempt to find how Tiffany & Co. is valued, benchmarks must be obtained. For its competitors, Movado, Zales, and Finlay were chosen. The industry was determined to be specialty retailers. The consumer discretionary sector of the S&P 500 was also chosen.

Using the Price/Earnings ratio, it is possible to determine the value of Tiffany's compared to various benchmarks. Before the comparison may begin, the actual P/E's of each benchmark must be obtained.

	FYE					
P/E	2001	2002	2003	2004	2005	Average
Tiffany & Co.	29.80	31.00	18.20	27.30	15.30	24.320
Movado Group	7.90	12.40	11.10	15.50	17.70	12.920
Zales	14.30	10.20	N/A	13.60	16.60	13.675
Finlay	4.80	5.60	5.30	6.90	9.60	6.440
Industry Avg	21.80	37.00	19.20	22.30	18.40	23.740
S&P 500- Consumer Dict		29.55	19.18	23.61	20.50	23.210

Figure #9: Price/Earnings Ratios
Source: Morningstar

Figure #9 shows the P/E for each benchmark for the ending of that fiscal year. After obtaining each of the P/E's, the relationship between Tiffany's and that P/E must be determined. This proportion is the next step in determining the value of Tiffany's.

	FYE					
P/E	2001	2002	2003	2004	2005	Average
TIF/ Movado	3.77	2.50	1.64	1.76	0.86	2.107
TIF/ Zales	2.08	3.04	N/A	2.01	0.92	2.013
TIF / Finlay	6.21	5.54	3.43	3.96	1.59	4.146
TIF/ Industry	1.37	0.84	0.95	1.22	0.83	1.042
TIF/ SP500	N/A	1.05	0.95	1.16	0.75	0.975

Figure #10: Proportion of TIF P/E to Benchmark

Figure #10 shows how Tiffany's relates to the given benchmark for the year, and then shows the average of this proportion over the five-year period. The averages are calculated from the fiscal year ending 2001 year to the fiscal year ending 2005 year.

The next step in the relative valuation process is to find the P/E's for the FYE 2006 and FYE 2007 years. It was determined that if P/E could not be obtained, the historical average would be used for that given fiscal year.

P/E	FYE	
	2006	2007
Tiffany & Co.	18.10	22.74
Movado Group	16.20	12.50
Zales	12.60	11.47
Finlay	6.44	6.44
Industry Avg	23.74	23.74
S&P 500-CD	18.86	15.78

Figure #11: Forecasted P/E for FYE 2006 and FYE 2007

Figure #11 has the forecasts for the FYE 2006 and FYE 2007 P/E ratios. Certain problems were faced when initially obtaining these numbers. All but two expected P/E's for the benchmarks were found. Finlay's forecast for FYE 2006 and FYE 2007 P/E's were forecasted to be negative. The specialty retail P/E forecast was not able to be found. In order to gain some type of valuation off the historical proportion, the P/E average from FYE 2001 to FYE 2005 was used.

Three relative valuations were done for Tiffany's. The first as based off the FYE 2006 year. The second and third were based off the FYE 2007 year. The 2007 year includes a valuation assuming buyback of Tiffany's shares and a valuation assuming no buyback of Tiffany's shares.

The basic earnings per share (EPS) for FYE 2006 is expected to be \$1.93. The basic EPS for FYE 2007 assuming no buyback was \$2.21. The basic EPS for FYE 2007 assuming there was a buyback in shares was \$2.29.

Using the forecasted P/E for FYE 2006 and FYE 2007, multiplying it by the historical proportion between the benchmark and Tiffany's, and then multiplying it by the basic EPS for that FYE, a value of Tiffany's can be determined.

Valuation	FYE 2006	FYE 2007
Movado	\$65.89	\$58.22
Zales	\$48.95	\$51.03
Finlay	\$51.53	\$59.00
Industry	\$47.73	\$54.65
SP500	\$35.50	\$34.01
After Buyback		
Movado	N/A	\$60.33
Zales	N/A	\$52.88
Finlay	N/A	\$61.14
Industry	N/A	\$56.63
SP500	N/A	\$35.24

Figure #12: Relative Valuation

Figure #12 shows the valuation of Tiffany's compared to its competitors, the specialty retailers industry, and the consumer discretionary sector of the S&P 500. Two valuations were done for FYE 2007 was to incorporate the potential buyback in shares that Tiffany's has announced it would be doing.

The average valuation of Tiffany's for FYE 2006 is \$49.92. The average valuation for FYE 2007 with no buyback is \$51.38. The average valuation for FYE 2007 assuming there is a buyback is \$53.24. As of 18 November 2005, the stock was priced at \$42.87.

The valuation chosen out of all five benchmarks was that of the Industry. Despite the fact that the P/E for FYE 2006 and FYE 2007 was given the historical average, the

relationship between Tiffany's and the Industry in terms of P/E cannot be ignored. First, the proportion was the closest to 1 out of the benchmarks. Movado has a large proportion showing a large difference in the P/E ratio. Zales has its year ending over the summer, meaning it shares only half a year with Tiffany. Finlay is expected to have negative P/E's in both FYE 2006 and FYE 2007. The S&P Consumer Discretionary sector has a slightly larger difference in proportion than that of the industry.

DIVIDEND DISCOUNT MODEL

To calculate the cost of capital for Tiffany & Co. is the first step of the dividend discount model. The CAPM method and the long-term debt plus risk premium method are used in this case. The long-term debt plus risk premium method is based on adding the yield to maturity of long-term debt to the equity risk premium. The cost of capital is calculated to be 9.56% using long-term debt plus risk premium method. The cost of capital calculated from CAPM method, which is risk free rate plus beta times market risk premium, is 16.33%. There is a huge difference between the cost of capital from the CAPM method and the cost of capital from the long-term debt method. In the case of Tiffany, the 9.56% of cost of capital is being used. The CAPM model is not being used because of the weaknesses of this model: too simple to capture the risk of the company and the assumption of beta never changing.

The next step is to forecast the dividend per share for year 2007. Initially, the average payout ratio was taken and multiplied by the EPS of 2006. This, however, produced a DPS that was under the DPS of 2006, which was \$.30. Due to this, it was determined that the DPS for 2007 will remain at \$.30, which would be the unchanged

amount from 2006. The payout rate, with this DPS for 2007, is 13.89%. Then, the annual average growth rate of dividend, which is 12.25%, was used to determine the future dividends from 2007 to 2011. This 12.25% is being used in this case because it is the annual average growth rate of dividend from 2001 to 2007 and most of the data of Tiffany in this report goes from year 2001.

The following page shows the detailed calculations for the Dividend Discount Model. The page is broken into various sections. First, the various percentages used for calculating both the cost of equity are shown. The calculations for earnings per share follow, with the dividends per share following. After the average annual growth rates are presented, the estimated dividends for the each of the costs of equity are determined.

At the bottom of the chart, a scenario analysis is shown using different growth rates from 3% to 9%. At 8.7679%, the intrinsic value of Tiffany's is equal to the stock price of 18 November 2005. It was determined that the future growth rate would be 9%,

At growth rate of 9%, the terminal value of the stock in year 2011 is \$92.705. The final step is to find the present value of the dividends stream and the terminal value. With the two calculated present value added together, Tiffany's intrinsic value was calculated to be \$60.166. The current stock price as of 18 November 2005 is \$42.87. Compared the current stock price and the intrinsic value, Tiffany is undervalued.

10 year strip rate	4.75%	Long-term debt YTM	6.56%
Beta	1.93	Equity Risk Premium	3%
Risk Premium	6%		

CAPM (K1) 16.33% K2 = 9.56%

	2000	2001	2002	2003	2004	2005	2006	2007	
EPS (diluted)	\$ 0.98	\$ 1.26	\$ 1.15	\$ 1.28	\$ 1.45	\$ 2.05	\$ 1.89	\$ 2.16	
Payout ratio		11.90%	13.91%	12.50%	13.10%	11.22%	15.87%		13.89%
	1999	2000	2001	2002	2003	2004	2005	2006	2007
DPS	\$ 0.09	\$ 0.11	\$ 0.15	\$ 0.16	\$ 0.16	\$ 0.19	\$ 0.23	\$ 0.30	\$ 0.30

Average Annual Growth Rate:

1999 to 2007	17.08%
2000 to 2007	14.97%
2001 to 2007	12.25%

Estimated Dividends:

		PV (using k=16.33%)	PV (using k= 9.56%)
2007	\$ 0.300	\$ 0.258	\$ 0.274
2008	\$ 0.337	\$ 0.249	\$ 0.281
2009	\$ 0.378	\$ 0.240	\$ 0.287
2010	\$ 0.424	\$ 0.232	\$ 0.294
2011	\$ 0.476	\$ 0.224	\$ 0.302
sum:		\$ 1.202	\$ 1.438

Under K= 16.33%

7 estimates of 2012 dividends:

terminal value for 2011:

PV:

Estimated Price:

3.00%	\$ 0.491	\$ 3.680	\$ 1.727	\$ 2.930
4.00%	\$ 0.495	\$ 4.017	\$ 1.886	\$ 3.088
5.00%	\$ 0.500	\$ 4.414	\$ 2.072	\$ 3.274
6.00%	\$ 0.505	\$ 4.887	\$ 2.294	\$ 3.496
7.00%	\$ 0.510	\$ 5.462	\$ 2.564	\$ 3.766
8.00%	\$ 0.514	\$ 6.175	\$ 2.899	\$ 4.101
9.00%	\$ 0.519	\$ 7.083	\$ 3.325	\$ 4.527

Under K= 9.56%

Terminal Value

PV:

Price:

3.00%	\$ 0.491	\$ 7.478	\$ 4.737	\$ 6.175
4.00%	\$ 0.495	\$ 8.909	\$ 5.644	\$ 7.082
5.00%	\$ 0.500	\$ 10.967	\$ 6.948	\$ 8.386
6.00%	\$ 0.505	\$ 14.181	\$ 8.984	\$ 10.422
7.00%	\$ 0.510	\$ 19.907	\$ 12.611	\$ 14.049
8.00%	\$ 0.514	\$ 32.973	\$ 20.888	\$ 22.326
8.7679%	\$ 0.518	\$ 65.401	\$ 41.431	\$ 42.869
9.00%	\$ 0.519	\$ 92.705	\$ 58.728	\$ 60.166

Current stock price: \$42.87
(11.18.05)

MARKET RISK

The following are risks that could affect the future of Tiffany & Co.

COMMODITY PRICES

One risk that could affect Tiffany and Co. is commodity prices. As the prices of precious metals become higher, Tiffany's would more than likely pass this cost to its consumer. If the price of gold, silver, and platinum become more valuable, the possibility exists for fewer unit sales. In the past 3 years, the price for an ounce of gold has gone up.

CONSUMER SPENDING - JAPAN

In Japan, there is currently a recession. The highest revenue generating quarter for Tiffany's is the fourth quarter. If consumer spending declines, Tiffany's will be affected greatly. After a third quarter that showed lower than expected earnings, a rebound of high fourth quarter revenues is important. Japan, with its growing number of Tiffany stores, plays an important role in the global revenue stream Tiffany's has built for itself over the years.

DISCRETIONARY SPENDING

Tiffany & Co. sells luxury products. In the specialty retail market, the high-end jewelry sector is the quintessential discretionary outlet. If, for some reason, the economy of the United States falters, Tiffany and its luxury products could face a stagnant revenue stream heavily affecting fourth quarter and FYE 2007 results.

INVESTMENT DRIVERS

Many factors will assist in the performance of the Tiffany stock in the next few years. The key drivers are as follows:

INTERNET SHOPPING

As stated in the industry life cycle, internet shopping has increased dramatically in the specialty retailer industry. Even in the jewelry sector of the industry, an increase in online purchasing has taken place.

TARGET DEMOGRAPHIC

Tiffany's is always on the lookout for new customers. With 71 million Americans born between 1977 and 1994, there is a new generation entering adulthood. This segment spends over \$36.3 billion on clothes and jewelry annually, according to Standard & Poor's. This segment is the largest spending segment, with women from the ages of 34 to 54 coming in second. As reported from the U.S Department of Commerce, U.S personal consumption expenditures have risen from 250 billion to 1 trillion over the last 29 years.

STORE GROWTH

As stated in the company overview, Tiffany generates revenues from many areas around the world. In 2004, Tiffany had opened 10 stores. This brings its total amount of stores to 151. Tiffany's also plans to operate more than 20 Iridesse stores in the United States within the next five years, according to Standard & Poor's.

TECHNICAL ANALYSIS



Figure #13: Tiffany and the 50 and 200 Day Moving Average
Source: BigCharts.com

Figure #13 shows the stock price compared to the 200 and 50-day moving averages. Tiffany’s has outperformed both averages since the end of the first quarter. The significant volume increases in the price are due to the announcement of earnings. This occurred in January, September, and December.

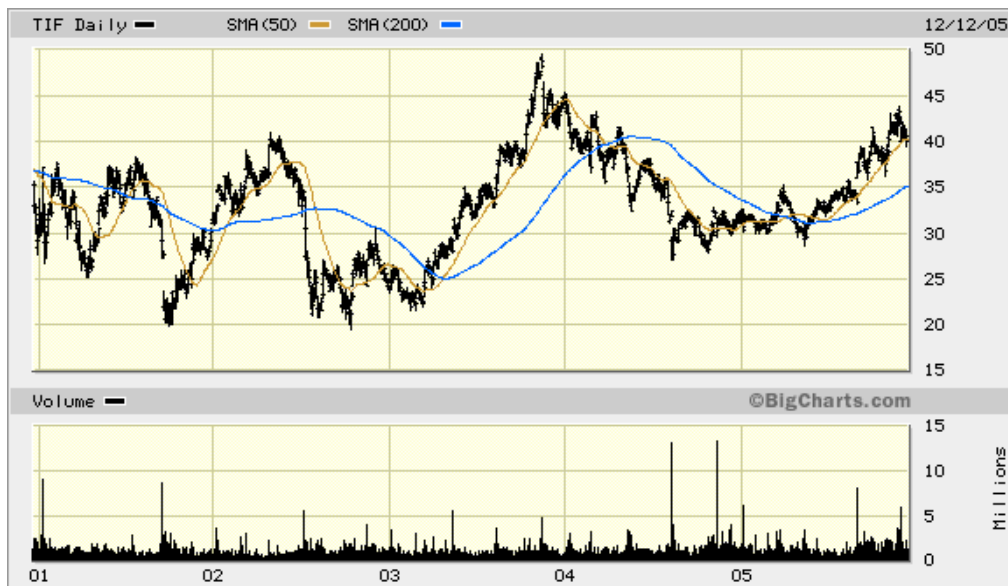


Figure #14: Tiffany and the 50 and 200 Day Moving Average
Source: BigCharts.com

Figure #14 shows a more specific support and resistance level for the Tiffany's stock. For 2001, 2002, and 2003, Tiffany's broke above its resistance level during the third quarter, and then saw its stock drop below the support level. In late 2001 and 2002, the stock went as low \$20. This support level increased, however, to almost \$30 between 2004 and 2005. In 2004, Tiffany's broke through the 50-day moving average and went as high as \$40. The stock remained at this resistance level until late 2004, when it began a downward slope which continued to mid 2005. At present time, Tiffany's is lower than both the 50-day and 200-day moving averages.

In the last year, the stock price has seen a steady increase, something that occurred most recently in 2003. During that year, the 50 day moving average rose to as high as \$45, with the stock price coming near \$50. This was followed by a sharp decline that continued into the third quarter of 2004. The point in the 2003 year that this decline occurred was the fourth quarter, the same quarter that Tiffany is in right now.

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