

TJX COMPANIES, TJX

Retailing is an industry we normally shy away from as investors--not because we think it's going away anytime soon, but simply because it's such a tough business. The difficulty in creating a competitive advantage as a retailer is perhaps exceeded only by maintaining it. We can all think of many retail chains that were ultimately forced to close despite being successful for a while (some even very successful). How many of the major department stores from the 1960's or 1970's are even around anymore? Correctly anticipating the public's taste for merchandise, pricing it right, and creating advertising that reaches a specific target audience is never easy. In fact, it would be an interesting and powerful shift if a business could somehow benefit from uncertainties in retailing. In a sense, discount retailer TJX Companies actually does that.

As the largest off-price apparel and home fashions retailer in the U.S., TJX has greatly benefited from the recent economic downturn. Bargain shoppers have lifted year-over-year sales for TJX, while name-brand manufacturers increasingly look to the company in order to convert bloated inventories into cash. This combination of increased buying opportunities and consumer demand has put the company on track to post record sales and net income for the current fiscal year. Our interest in TJX is part of our effort over the past couple of years to add dominant, high quality companies to our portfolio that would likely emerge stronger following the economic downturn. In good part, that seems to be playing out for TJX, although even quicker than we anticipated.

While the current environment is nearly ideal for the company, TJX hasn't always escaped the struggles faced by the average retailer. For years, it followed the more traditional clothing retail model. Then in the mid 1970's, TJX merchandise manager Ben Cammarata took on the task of developing an upscale, but off-price, retail concept on a nationwide basis. Traveling across the country in search of name-brand manufacturers with excess inventory, Cammarata paid cash for small amounts of carefully selected product and was able to stock his stores with widely recognized, good quality merchandise at prices never seen before. His offer to convert excess inventory to cash on the spot made manufacturers happy and meant great prices for TJX. Also, buying in low volumes meant the selection in stores was nearly always fresh. Not surprisingly, his concept—called T.J. Maxx—was a big hit with customers. Today, TJX remains loyal to this synergistic

business model. More than 10,000 vendors rely on it to help manage their inventories, and its core brands, T.J. Maxx and Marshalls, are gaining customers and growing sales even in the worst economy in a generation. In fact, the model has proven to be incredibly resilient: Since 1995, earnings per share have increased every year but one, averaging more than 23% annual growth over that period.

TJX still enjoys the benefits of Cammarata's leadership. As Chairman, he's actively involved in the company's management of its 2,500 stores and \$19 billion in sales. He, along with President and CEO Carol Meyrowitz, aspire to grow TJX into a global leader in off-price retailing. The company expanded to Canada in 1990, the U.K. in 1994 and the European continent in 2007. It's taken somewhat longer to get the mix right, but the international operations are profitable. TJX has also grown through applying its discount model to new categories, such as home furnishings through its HomeGoods stores. We feel these concepts of international and category expansion are likely the most favorable approaches to growth going forward, so we're pleased to see a renewed focus there, as opposed to the acquisition strategies attempted in the early 2000's with little success. Management also deserves credit for its focus on maintaining a superb balance sheet. TJX's strong cash position and excellent overall financial health help provide the resources to exploit the best buying opportunities, even during the toughest times. The current environment provides a great example. We're also pleased to find a growing dividend at TJX, but we are disappointed with the company's appetite for share buybacks, seemingly without regard to price. Generally, we feel that buying back stock at non-bargain prices is a poor use of shareholder wealth.

We began with a caution about the retailing business in general, and that still applies here. Despite its successes and powerful business model, TJX's continued success is far from certain. After all, the model itself is no secret, and others have replicated it in some form. In fact, the "discount outlet" concept could be viewed as a direct response to TJX's success. Generally, though, the TJX model results in lower customer prices, and an increasing number of vendors rely on TJX. For them, TJX remains a part of their inventory management process. For shoppers, TJX is a partner in helping to save money. We find this symbiotic model compelling.

While the current economy is a powerful reminder of how even the best companies can struggle, we continue to believe TJX will further deepen its

relationship with shoppers searching for bargains and struggling vendors searching for cash, and continue its long-term growth.

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