Detail in Retail

Many experts have been predicting that brick-and-mortar retailers will struggle to survive over the long term. We agree that two key trends – evolving technology and demographics – have changed the retail landscape. First, technology has changed the way people communicate, find information and – very importantly – shop. Second, with baby boomers retiring, their spending power is gradually switching over to the millennial crowd – younger consumers who are familiar and very comfortable with e-commerce and who may have different priorities.

Despite these trends, we believe that going shopping will continue to be an important aspect of our society for the foreseeable future. We believe investors should own a mix of retailers that invest in an online strategy, have a product offering that provides a competitive advantage or offer a customer experience that can't be replicated online.

1 Technology: How the Internet Threatens Retailers

The Internet has been one of the most disruptive threats to retailers in many years. Since most Internet-only retailers, like Amazon, don't have brick-and-mortar locations with rent, mortgages, or utility costs, they can offer cheaper prices — and they charge no state taxes (except for the 10 states where online sales are subject to state taxes). While we understand these threats, we believe most brick-and-mortar stores can stay competitive by developing an omnichannel presence and offering products with limited online market penetration.

Omnichannel Retailers

Omnichannel retailers have websites that consumers can use from all types of devices, from cell phones to tablets and desktops. True omnichannel retailers have the ability to ship from their stores or distribution centers and to their stores for in-store pick-up. Today, most brick-and-mortar retailers allow free shipping on returns, and all retailers allow items purchased on their websites to be returned to stores. This is a key differentiator because recently, more Internet-only retailers are charging for returns. Another difference is that more robust websites allow some retailers to offer additional products online that aren't available in physical stores.

Investment Ideas:

We believe Kohl's (KSS), Walmart (WMT) and Target (TGT) are the furthest along in their omnichannel efforts among the stocks we cover.

Not All Retail Categories Are Equal

Studies also show that more and more products are now available on the Internet. According to *Internet Retailer,* apparel, toys and mass consumables have reached double-digit market penetration, with office supplies and books/movies at 40% penetration (a measure of adoption compared to the total market for that product). But some items, by definition, are harder to buy online. Food, hardware, health and beauty, and auto parts have the lowest penetration online, which we see as a competitive advantage over retailers that sell products in higher-penetration categories.

Investment Ideas:

Lowe's (LOW), Tractor Supply (TSCO) and O'Reilly (ORLY) currently operate in industries with low online penetration.

Please see the full company research reports for important disclosures on the companies mentioned in this report. You can also contact a local Edward Jones financial advisor, or write the Research Department, Edward Jones, 12555 Manchester Road, St. Louis, MO 63131, to receive a complete company opinion.

Edward Jones®
MAKING SENSE OF INVESTING

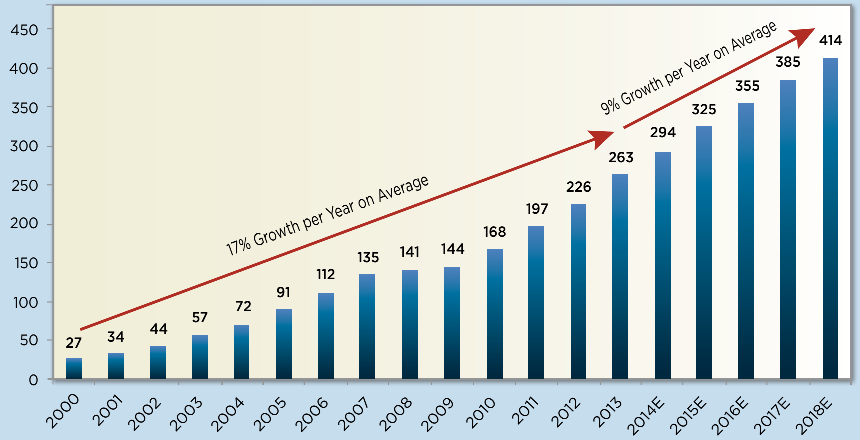
The Evolving Retailer

We believe retailers with a wide variety of products online, seamless checkout, product reviews, strong customer service in stores and differentiated products will be successful over the longer term. In a creative effort, some retailers have started offering tablet and smartphone applications (apps) to provide consumers with coupons and deals, suggested item pairings and social media integration.

Investment Ideas:

For example, Target's (TGT) Cartwheel offers deals through its customers' mobile phones.

Online Sales Growth (Billions)



Source: U.S. Department of Commerce, Forrester Research Inc.

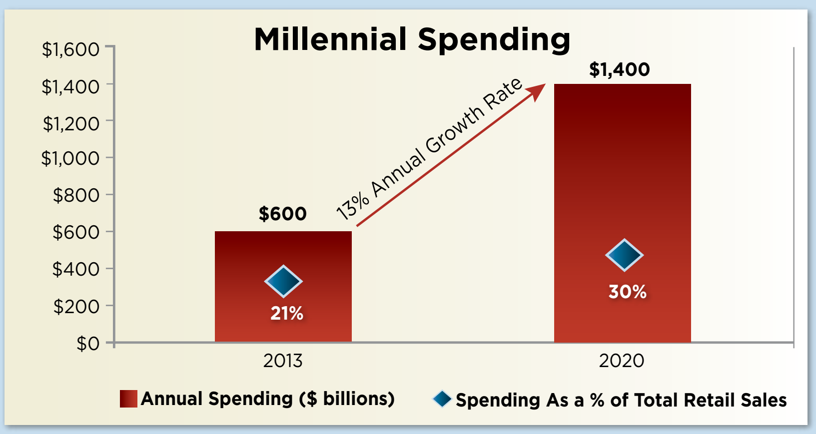
2 Demographics: What the Spending Shift to Millennials Means

We believe the shift from baby boomers to millennials will also change the retail landscape over the coming years. While baby boomers are more interested in visiting brick-and-mortar stores, purchasing cruises and going to the movies, millennials seem to be more focused on social media, socially and environmentally friendly products, healthier lifestyles, online travel and convenience. With the boomer crowd retiring and spending less, the consumer-spending burden will shift to millennials, who will drive an even greater need for truly omnichannel retailers.

A More Educated Consumer

Born between 1980 and 2000, there are roughly 80 million millennials in the U.S., about 25% of the population. The millennials exceed the number of baby boomers by about 4 million. Millennials are the highest educated among all generations and use technology not just for communication but as a way to improve life, make better choices and contribute to society.

Due to their higher levels of education, we believe millennials overall will have greater spending power than baby boomers, and we expect this generation to be the future driver of consumer spending. Some reports expect that millennial spending in the U.S. will grow to $1.4 trillion annually by 2020 and represent 30% of total retail sales.* We believe retailers will need to aggressively invest in technology to cater to the millennial crowd.



Source: "Who are the Millennial shoppers? And what do they really want?" *Accenture*, June 2013. Edward Jones estimates.

Investment Ideas: Coach (COH) and VFC Corporation (VFC) offer brands we believe will remain in favor with the millennial crowd.

But millennials still like to visit brick-and-mortar stores too, so these physical locations will remain important. A survey by the Urban Land Institute showed two-thirds of millennials like to visit the mall at least once a month because they see it as a way to enjoy time with friends and family. Millennials can be fickle, however, so retailers will need to invest in stores to make sure they don't lack freshness, newness and excitement.

Catering to a Healthier Lifestyle

Younger generations are very interested in health and wellness and are more likely to focus on healthier eating habits and being active, with over 60% of millennials saying they work out on a regular basis. They have a large interest in natural and organic foods and understand the actual ingredients in their foods. This group is much more inclined toward buying fresh versus buying packaged foods, which we believe is a reason we are seeing many large packaged foods companies struggle to drive volume growth. The natural/organic industry has been growing at a rate of over 15% for the past eight years, and we expect the industry to continue to show 7% to 9% annual growth for the foreseeable future.

Investment Ideas:

Regardless of the popularity of online shopping, we believe millennials enjoy physically visiting Whole Foods (WFM) markets, so this company will be a big beneficiary of these demographic trends for the coming years, in our view.

Retail Investment Ideas

Edward Jones provides coverage on a good mix of growth as well as mature retailers. The chart below highlights our Buy-rated retailers and where they fit in to today's evolving retail landscape.

Technologically Advanced Retailers – investing more in e-commerce sites	
Kohl's (KSS) Target (TGT) Walmart (WMT)	• Strong brick-and-mortar locations and an omnichannel presence • Innovation on industry-leading mobile apps, price comparisons and website deals • Growing their exclusive products offerings
Millennial-reaching Retailers – relate to millennials' unique tastes	
Coach (COH) TJX Corporation (TJX) Ulta Beauty (ULTA) VF Corp (VFC)	• Strong brands that should benefit from an increase in spending by millennials • Exclusive products and unique shopping experience
Whole Foods (WFM)	• Benefits from millennials' preference for healthy food
Competitively Advantaged Retailers – operate in industries with low Internet penetration	
Lowe's (LOW) O'Reilly Auto (ORLY) Tractor Supply (TSCO)	• Operate in product categories that have low Internet penetration • Physical locations provide a high level of customer service to make the in-store experience more valuable

How We Value and Recommend Stocks

When valuing consumer companies, we use various methods that include comparing price-to-earnings ratios and PEGY ratios (price-to-earnings ratio divided by growth plus dividend yield) to historical and peer averages and more. We also use discounted cash flow models to incorporate long-term growth expectations.

Investment Risks

Risks to investing in retail companies include deteriorating economic conditions, a slowdown in consumer spending, failure to adapt to the changing retail landscape, higher commodity prices and currency fluctuations.

Actions for Investors

We understand that technology and evolving demographics will impact retail, but we don't think it's "dying," as some experts may claim. Retail stores and the shopping experience will continue to be a presence in American lives for the foreseeable future. And we believe stocks in this industry still have a place in a diversified stock portfolio. Talk to your Edward Jones financial advisor today about how retail stocks may help you work toward your long-term financial goals.

*Source: "Who are the Millennial shoppers? And what do they really want?" Accenture, June 2013.

Analyst Certification

I certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers; and no part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in the research report.

Robin Diedrich, CFA; Brian Yarbrough, CFA

Important Disclosures

Past performance does not guarantee future results.

Dividends can be increased, decreased or totally eliminated at any time without notice.

All investment decisions need to take into consideration individuals' unique circumstances such as risk tolerance, taxes, asset allocation and diversification.

The Edward Jones' Research Rating referenced does not take into account your particular investment profile and is not intended as an express recommendation to purchase, hold or sell particular securities, financial instruments or strategies. You should contact your Edward Jones financial advisor before acting upon the Edward Jones Research Rating referenced.

The firm has organizational and administrative arrangements in place to prevent and avoid conflicts of interest in respect of research recommendations.

It is the policy of Edward Jones that analysts or their associates are not permitted to have an ownership position in the companies they follow directly or through derivatives.

Analysts are not compensated based upon investment banking services transactions or activities.

This publication is for information only. While the statements contained in this report are taken from sources that we believe to be reliable, we do not guarantee their accuracy. However, this statement does not apply to disclosures concerning Edward Jones or analyst certification. Some of this information is provided by an independent research service.

The issues mentioned herein are subject to price change without notice. Additional information is available upon request. Diversification does not guarantee a profit or protect against loss. You should make investment decisions based upon your unique objectives, risk tolerance and financial circumstances.

Investing in equities involves risks. The value of an investment will fluctuate with changes in market conditions and may lose some or all of its principal.

Buy-rated companies mentioned in this report that are followed by Edward Jones (prices as of Aug. 29, 2014):

Coach (COH – $36.83)

Kohl's (KSS – $58.79)

Lowe's (LOW - $52.51)

O'Reilly Auto (ORLY - $155.98)

Target (TGT - $60.07)

TJX Corporation (TJX - $59.61)

Tractor Supply (TSCO - $66.95)

Ulta Beauty (ULTA – $97.31)

VF Corp (VFC – $64.12)

Walmart (WMT – $75.50)

Whole Foods (WFM – $39.14)

Brian Yarbrough, CFA
Brittany Weissman
Equity Analysts

www.edwardjones.com

Member SIPC

Edward Jones®
MAKING SENSE OF INVESTING