



Operating Lease Disclosures: New Standard's Effect on Large Retail Firms

October 2019

Background

ASC 842, Leases, is a new accounting standard that went into effect for most publicly traded firms at the start of 2019.

- Firms must report:
 - **cost of operating leases on balance sheet**, listing those costs as liabilities. Previously reported in the notes to the financial statements.
 - **corresponding right-of-use (ROU) asset** on asset side of balance sheet. This is the first time firms have reported ROU assets.

We observe significant spikes in assets and liabilities, due to reporting changes under the new standard. These changes significantly impacted return on assets, debt-to-equity, and other key performance metrics. The adoption of ASC 842 creates a significant challenge for investors in interpreting and accounting for its impact.

What We Did

Calcbench reviewed lease disclosures reported by 36 large retailers firms in Q2 2019. Retailers can be especially sensitive to ASC 842, given their heavy reliance on leased real estate for operations.

- Examined all operating lease liabilities and ROU assets reported on balance sheet;
- Calculated the standard's effect on firms' total liabilities and assets;
- Calculated changes in the firms' return on assets and debt to equity ratios;
- Examined reported discount rates and average remaining leasing terms.

Firms We Studied

Abercrombie & Fitch	Conn's	Gap Inc.	Michaels Companies
American Eagle Outfitters	CVS Health	Home Depot	Nordstrom Inc.
Bed Bath & Beyond	Designer Brands	J C Penney Co.	Ollie's Bargain Outlet
Best Buy	Dick's Sporting Goods	Kohl's	Ross Stores
Big 5 Sporting Goods	Dillard's	Kroger's	Signet Jewelers Ltd.
Big Lots	Dollar General	L Brands	Sportsman's Warehouse
Boot Barn Holdings	Dollar Tree	Lands' End	Target Corp.
Burlington Stores	Foot Locker	Lowe's Companies	Tiffany & Co.
Children's Place	Gamestop	Macy's	Walmart Inc.

Summary of Findings

Among the 36 retailers we examined, below shows the change in their collective assets and liabilities after adopting ASC 842. The adjustment in the bottom row refers to total ROU assets and operating lease liabilities reported in Q2 2019, respectively. In both cases, **ASC 842 seems to account for all the change in assets and liabilities for Q2 2019**, and then some.

	Total Assets	Total Liabilities
Q4 2018	\$756,402,106,000	\$541,146,249,000
Q2 2019	\$845,907,988,000	\$631,165,617,000
Change	\$89,505,882,000	\$90,019,368,000
Percentage Increase	11.83%	16.63%
ASC 842 Adjustment	\$114,974,305,000	\$121,782,395,000

Change in Total Assets, by Firm

Company Name	Q2 2019	Q4 2018	Change	ROU assets Q2 2019
Abercrombie & Fitch Co /DE/	3,407,004,000	3,557,727,000	(150,723,000)	1,216,998,000
American Eagle Outfitters Inc	3,359,159,000	1,903,378,000	1,455,781,000	1,462,544,000
Bed Bath & Beyond Inc	7,988,195,000	7,536,744,000	451,451,000	1,990,963,000
Best Buy Co Inc	14,978,000,000	12,901,000,000	2,077,000,000	2,774,000,000
BIG 5 SPORTING GOODS Corp	699,864,000	419,561,000	280,303,000	262,288,000
Big Lots Inc	3,192,295,000	2,023,347,000	1,168,948,000	1,208,349,000
Boot Barn Holdings, Inc.	810,601,000	655,646,000	154,955,000	154,815,000
Burlington Stores, Inc.	5,046,437,000	3,079,172,000	1,967,265,000	2,160,828,000
Childrens Place, Inc.	1,303,537,000	727,046,000	576,491,000	430,145,000
Conns Inc	2,146,225,000	1,884,907,000	261,318,000	248,707,000
CVS HEALTH Corp	218,904,000,000	216,668,000,000	2,236,000,000	20,865,000,000
Designer Brands Inc.	2,557,246,000	1,620,584,000	936,662,000	975,963,000
Dick's Sporting Goods, Inc.	6,915,215,000	4,187,149,000	2,728,066,000	2,454,929,000
Dillard's, Inc.	3,512,079,000	3,431,369,000	80,710,000	52,608,000
Dollar General Corp	21,917,529,000	13,204,038,000	8,713,491,000	8,405,346,000
Dollar Tree, Inc.	19,493,800,000	13,501,200,000	5,992,600,000	6,014,300,000
Foot Locker, Inc.	6,720,000,000	3,820,000,000	2,900,000,000	2,976,000,000
GameStop Corp.	2,987,900,000	4,044,300,000	(1,056,400,000)	769,700,000
Gap Inc	14,043,000,000	8,049,000,000	5,994,000,000	5,807,000,000
Home Depot, Inc.	52,010,000,000	44,003,000,000	8,007,000,000	5,789,000,000
J C Penney Co Inc	8,260,000,000	7,721,000,000	539,000,000	925,000,000
KOHL'S Corp	14,542,000,000	12,469,000,000	2,073,000,000	2,428,000,000
Kroger Co	44,319,000,000	38,118,000,000	6,201,000,000	6,819,000,000
L Brands, Inc.	10,618,000,000	8,090,000,000	2,528,000,000	3,209,000,000
Lands' End, Inc.	1,109,504,000	1,110,911,000	(1,407,000)	28,980,000
Lowe's Companies Inc	40,695,000,000	34,508,000,000	6,187,000,000	3,967,000,000
Macy's, Inc.	20,741,000,000	19,194,000,000	1,547,000,000	2,625,000,000
Michaels Companies, Inc.	3,707,149,000	2,128,336,000	1,578,813,000	1,611,029,000
Nordstrom Inc	9,935,000,000	7,886,000,000	2,049,000,000	1,801,000,000
Ollie's Bargain Outlet Holdings, Inc.	1,544,341,000	1,159,003,000	385,338,000	321,428,000
Ross Stores, Inc.	9,151,947,000	6,073,691,000	3,078,256,000	2,932,199,000
Signet Jewelers Ltd	5,965,600,000	4,420,100,000	1,545,500,000	1,729,300,000
Sportsman's Warehouse Holdings, Inc.	584,461,000	388,897,000	195,564,000	183,486,000
Target Corp	41,566,000,000	41,290,000,000	276,000,000	2,062,000,000
Tiffany & Co	6,315,900,000	5,333,000,000	982,900,000	1,073,400,000
Walmart Inc.	234,861,000,000	219,295,000,000	15,566,000,000	17,239,000,000

From our group of 36 firms...

- 19 firms where ROU assets exceeded increase in total assets;
- 14 firms where total assets increased, by more than the ROU assets;
- 3 firms where total assets fell despite addition of ROU assets.

Change in Total Liabilities, by Firm

Company Name	Q2 2019	Q4 2018	Change	Operating Lease Liabilities Q2 2019
Abercrombie & Fitch Co /DE/	2,403,709,000	2,414,271,000	(10,562,000)	1,503,598,000
American Eagle Outfitters Inc	2,130,582,000	615,823,000	1,514,759,000	1,617,841,000
Bed Bath & Beyond Inc	5,926,201,000	4,633,469,000	1,292,732,000	2,185,498,000
Best Buy Co Inc	11,693,000,000	9,595,000,000	2,098,000,000	2,873,000,000
BIG 5 SPORTING GOODS Corp	524,997,000	244,700,000	280,297,000	274,532,000
Big Lots Inc	2,547,752,000	1,330,306,000	1,217,446,000	1,260,722,000
Boot Barn Holdings, Inc.	534,906,000	400,885,000	134,021,000	170,252,000
Burlington Stores, Inc.	4,731,300,000	2,756,462,000	1,974,838,000	2,347,024,000
Childrens Place, Inc.	1,054,281,000	412,609,000	641,672,000	469,523,000
Conns Inc	1,509,490,000	1,264,932,000	244,558,000	364,408,000
CVS HEALTH Corp	157,305,000,000	157,947,000,000	(642,000,000)	20,642,000,000
Designer Brands Inc.	1,827,999,000	788,207,000	1,039,792,000	1,091,515,000
Dick's Sporting Goods, Inc.	5,150,129,000	2,282,988,000	2,867,141,000	3,015,374,000
Dillard's, Inc.	1,866,235,000	1,752,988,000	113,247,000	52,108,000
Dollar General Corp	15,168,369,000	6,786,645,000	8,381,724,000	8,395,946,000
Dollar Tree, Inc.	13,628,100,000	7,858,300,000	5,769,800,000	5,982,400,000
Foot Locker, Inc.	4,208,000,000	1,314,000,000	2,894,000,000	3,247,000,000
GameStop Corp.	2,178,200,000	2,708,100,000	(529,900,000)	764,200,000
Gap Inc	10,418,000,000	4,496,000,000	5,922,000,000	6,590,000,000
Home Depot, Inc.	53,170,000,000	45,881,000,000	7,289,000,000	6,094,000,000
J C Penney Co Inc	7,297,000,000	6,551,000,000	746,000,000	1,171,000,000
KOHL'S Corp	9,087,000,000	6,942,000,000	2,145,000,000	2,805,000,000
Kroger Co	35,787,000,000	30,283,000,000	5,504,000,000	7,102,000,000
L Brands, Inc.	11,547,000,000	8,955,000,000	2,592,000,000	3,621,000,000
Lands' End, Inc.	797,239,000	788,200,000	9,039,000	33,908,000
Lowe's Companies Inc	38,055,000,000	30,864,000,000	7,191,000,000	4,547,000,000
Macy's, Inc.	14,426,000,000	12,758,000,000	1,668,000,000	3,162,000,000
Michaels Companies, Inc.	5,294,719,000	3,754,531,000	1,540,188,000	1,676,032,000
Nordstrom Inc	9,176,000,000	7,013,000,000	2,163,000,000	2,149,000,000
Ollie's Bargain Outlet Holdings, Inc.	526,872,000	216,351,000	310,521,000	319,343,000
Ross Stores, Inc.	5,855,683,000	2,767,945,000	3,087,738,000	3,046,071,000
Signet Jewelers Ltd	4,261,300,000	2,603,200,000	1,658,100,000	1,823,800,000
Sportsman's Warehouse Holdings, Inc.	495,754,000	310,237,000	185,517,000	213,600,000
Target Corp	29,730,000,000	29,993,000,000	(263,000,000)	2,111,000,000
Tiffany & Co	3,122,800,000	2,202,100,000	920,700,000	1,186,700,000
Walmart Inc.	157,730,000,000	139,661,000,000	18,069,000,000	17,874,000,000

From our group of 36 firms...

- 24 firms where operating lease liabilities exceeded increase in total liabilities;
- 8 firms where total liabilities increased, by more than operating lease liabilities;
- 4 firms where total liabilities fell despite addition of operating lease liabilities.

Changes to Return on Assets

Taken altogether, return on assets for our retailer group has risen from 4.64 to 5.23 percent since ASC 842 took effect at the start of 2019. That said, **Walmart's strong performance had an outsized influence for the whole group.** *Without Walmart's assets and net income, ROA actually fell for the other 35 firms.*

	Total Assets	Net Income (TTM)	Return on Assets
Q4 2018 (all)	\$756,402,106,000	\$35,126,108,000	4.64 percent
Q2 2019 (all)	\$845,907,988,000	\$44,236,008,000	5.23 percent
Q4 2018 (w/o WMT)	\$537,107,106,000	\$27,947,108,000	5.20 percent
Q2 2019 (w/o WMT)	\$611,046,988,000	\$31,020,008,000	5.08 percent

Changes to Return on Assets: Examples

	Burlington Stores	Michael's Cos.
Q4 2018 Net Income TTM	\$414,745,000	\$319,545,000
Q4 2018 Assets	\$3,079,172,000	\$2,128,336,000
Q4 2018 ROA	13.47%	15.01%
Q2 2019 Net Income TTM	\$423,532,000	\$327,410,000
Q2 2019 Assets	\$5,046,437,000	\$3,707,149,000
Q2 ROA	8.39%	8.83%
ROA Change	-5.08%	-6.18%
Q2 2019 ROU Assets	\$2,160,828,000	\$1,611,029,000
Q2 2019 ROA w/o ROU Assets	14.68%	15.62%

Burlington Stores and **Michael's Cos.** are two examples of the distorting effect that ASC 842 can have upon return on assets.

In both cases, the firms increased their net income, yet ROA fell because the size of total assets grew even faster — and that growth in total assets was entirely due to reporting changes required by ASC 842.

Without the new leasing disclosures, both firms would have seen their ROA **rise** in Q2 2019 rather than fall.

Changes to Debt-to-Equity Ratio

Taken altogether, the debt-to-equity ratio for our retailer group rose from 2.44 at the end of 2018 to 2.79 by Q2 2019.

	Total Liabilities	Shareholder Equity	D/E Ratio
Q4 2018	\$541,146,249,000	\$214,646,717,000	2.52
Q2 2019	\$631,165,617,000	\$214,126,271,000	2.95

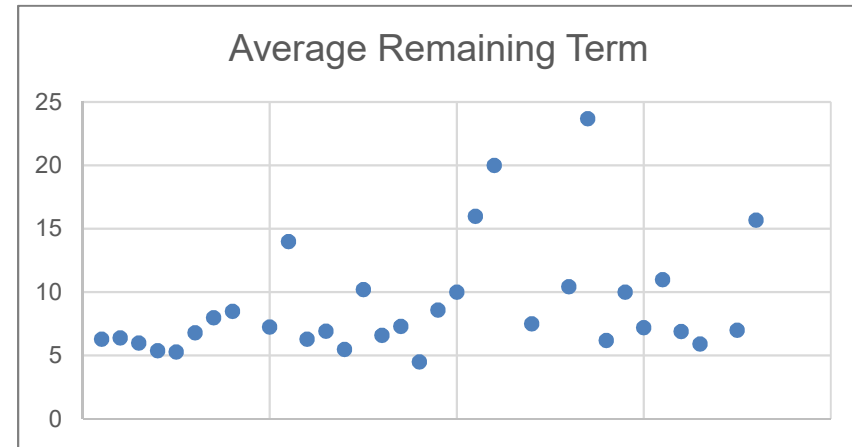
Individually, 31 of the 36 retailers in our sample saw debt-to-equity ratios rise from Q4 2018 to Q2 2019. The other five saw their ratios fall.

Changes in Debt-to-Equity: Examples

	Kroger	Best Buy	Sportsman Warehouse	Burlington Stores	American Eagle
Q4 2018 Liabilities	\$30,283,000,000	\$9,595,000,000	\$310,237,000	\$2,756,462,000	\$615,823,000
Q4 2018 Equity	\$7,835,000,000	\$3,306,000,000	\$78,660,000	\$322,710,000	\$1,287,555,000
Q4 2018 Debt-to-Equity	3.87	2.90	3.94	8.54	0.48
Q2 2019 Liabilities	\$35,787,000,000	\$11,693,000,000	\$495,754,000	\$4,731,300,000	\$2,130,582,000
Q2 2019 Equity	\$8,532,000,000	\$3,285,000,000	\$88,707,000	\$315,137,000	\$1,228,577,000
Q2 2019 Debt-to-Equity	4.19	3.56	5.59	15.01	1.73
Debt/Equity Ratio Increase	+8.5%	+22.6%	+41.7%	+75.8%	+262.6%
Q2 2019 Op. Lease Liabilities	\$7,102,000,000	\$2,873,000,000	\$213,600,000	\$2,347,024,000	\$1,617,841,000
Q2 Debt-Equity w/o Leases	3.36	2.68	3.18	7.57	0.42

Discount Rates and Remaining Term

Registrants disclose the weighted average remaining term of the operating leases (in years) as well as the weighted average discount rates a firm uses to calculate the Net Present Value of its leasing liabilities. The charts below, show the great variability in these reported numbers. One could have expected more uniformity in the reported numbers, especially in the discount rates, for companies in a similar business.



Final Thoughts

We examined the initial impact of ASC 842 on a group of retailers. ASC 842 seems to have had a significant impact in many companies' assets and liabilities. This impact resulted, in this group, in a **reduction in the Return On Assets (ROA)** and an **increase in the debt-to-equity ratio**.

In addition, the impact of ASC 842 on the assets and liabilities of companies was not always the same. As a result, many companies saw an **impact on stockholders' equity** and the underlying book value of the company.

The **variability in the discounts rates** used by companies along with the impact on significant ratios (ROA and D/E), create a **significant challenge for investors in interpreting and accounting for the impact of ASC 842**.

Looking into the future, the introduction of Right-of-Use assets on the balance sheet also raises the possibility of impairing those assets, including deliberate attempts to tank quarterly results for earnings management.

Calcbench Has the Data!

Balance sheet displays. Our [Company-in-Detail database](#) lets you see what a specific firm reports on its balance sheet, including comparables to prior years.

Standardized leasing metrics. Our [Multi-Company database](#) lets you search ‘operating lease right-of-use asset’ or ‘operating lease liability’ to see reported numbers for one or more firms.

Footnote disclosures. Our [Interactive Disclosure database](#) lets you search for any disclosures related to leases (usually listed as ‘Commitments and Contingencies’ or ‘Leasing’) or for specific text related to leasing operations as well. Users can also find the discount rates a firm uses to calculate NPV and the average remaining lease term.

Also see [our Analysis Guide for Operating, Finance, and Capital Lease Disclosures](#).



Thank you



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