Holding the Focus

by Peter Millard

In retailing, "hot" turns to "not" with abruptness, usually when the initial concept hits a market saturation point. So when 86th-ranked Gantos, with 127 high-end apparel stores for working women, strayed from its formula by buying less expensive and less well-known products, investors fretted.

Gantos has set a torrid pace over the past three years, adding some 60 stores and raising revenues 22% or so each year to $170 million in 1988. So why fiddle with a winning concept in a slow apparel year? That good question was followed by a shake-up in which two of the three Gantos brothers left.

Now CEO L. Douglas Gantos swears the firm won't stray again and has put buying under a hotshot lured from the Limited. "I don't want to change any of the basics of what we do," says the remaining Gantos, whose Lebanese parents opened a linen store in Grand Rapids, Mich., during the Depression.

A 1.5 million share offering in June capitalized on a sharp run-up in Gantos common to generate $17.5 million (lowering insider ownership from 47.8% to 33%). Unfortunately, most of it replaces equity lost when the brothers' stakes were bought out with $10.6 million in borrowed funds. The rest will help reduce long-term debt from 49% of capital to 32%. Interest savings offset any earnings dilution, says Gantos CFO James Curley. Prescott, Ball & Turben's Elizabeth Armstrong sees the stock at 31 in six to nine months, 35% above the current price. Swergold Chefitz's more conservative Terence McEvoy only goes to the high 20s within 18 months. Gantos has carved out a niche, says Alex. Brown's Fred Wintzer, and if it "acts like it is being chased," will steadily increase market share.

Certainly there are plenty of high-end malls, maybe 600 suitable for a Gantos unit. Most recently Gantos has added 10 in the San Francisco Bay area. With over 50% of its stores in the Midwest, and 37 in Michigan and Illinois alone, the company is pushing toward both coasts. "If you draw a line from North Carolina over to Denver and then over to San Francisco, everything north of that line is where we think we can easily find the numbers to grow to 300 stores by 1991 and 400 by 1994," Gantos figures.

Such growth will make it hard any time soon for Gantos to bring its 8% return on capital up to, say, the Limited's 17% or the Gap's 27%. Its returns were depressed by a high debt load and Curley says the better yardstick is return on equity—around 20% since going public in 1986. Arguably, the relatively small equity inflated that.

Gantos and Curley minimize any recession threat. "The company made its money and growth in the Rust Belt around Detroit during some of the worst recessions in recent times," says Curley.

So the only question is, where's that saturation point? ■

business sold to Britain's Tate & Lyle, while Imperial and Holly merged. Meanwhile, Savannah Foods became the largest factor in the industry, broadening its geographic distribution and diversifying into beet sugar by acquiring $95 million-in-sales Michigan Sugar in 1984. Two years later, Savannah acquired $265 million-in-sales Colonial Sugar, which increased the company's cane sugar capacity by 50%. Both were cash deals.

Meanwhile, with its nearly debt-free balance sheet Savannah could easily afford to install modern boilers and automated packaging equipment.

"They've handily turned Colonial Sugar around," says Lee Wilder, of Robinson-Humphreys in Atlanta.

Savannah improved its operating margin from 4.1% in 1986 to 5.1% in 1988, which brought the company to the verge of a record earnings year.

"Savannah Foods is considered to be the industry's low-cost producer, which is why it has grown and prospered even though the industry has been flat or no growth," says Smith. He foresees earnings of $3 to $3.25 in 1989 and 1990, up from $1.50 last year.

Of course, Savannah's results were helped by last year's drought, which wrecked 15% of the beet crop. Since 85% of its sugar is cane, Savannah is still benefiting from the drought this year, because the sugar crop comes to market six months after it is harvested.

Savannah reported earnings of 52¢ for the first quarter, compared with 12¢ in 1988. Wilder predicts earnings of $2.90 this year and a "conservative" $2.50 in 1990, depending on how strong the beet sugar crop is in 1990. Even though the stock has moved from a high of 18 in 1988 to over 30, Smith says, "Savannah is selling at a discount to the market at a little over 10 times estimated earnings. And that earnings level is sustainable."

After next year, however, it's anyone's guess since the Farm Bill expires in 1991. With the domestic sugar price at roughly 24¢ a pound, more than double the world price, most analysts believe that our disgraceful price supports (FW, Apr. 4) could fall slightly. Particularly if Europe starts dropping agricultural price supports prior to 1992. But they're in no particular danger of extinction. "It isn't a costly program to the U.S. Treasury," explains Leo Polopolus, an agriculture economist specializing in sugar at the University of Florida.

In the meantime, however, Savannah common looks like an attractive, and fairly conservative, short-term play. *—Holt Hackney*
NASDAQ (SVAN), 31½, div. 54¢, yld. 1.7%.

FUQUA INDUSTRIES SO WHAT'S CHANGED?

Investing in old-fashioned conglomerate like $1.1 billion-in-sales Fuqua Industries demands patience and fortitude. Few could predict earnings much less figure what businesses founder J.B. Fuqua would buy. Certainly his melding of garden tools (Snapper), photo finishing and a Georgia S&L did little to offset the cyclical earnings which last year, plunged from $2.92 to 48¢ a share.

So you might expect analysts to be pushing the stock now that Fuqua, 70, has relinquished active management. Hardly. Fuqua now is in the orbit of Charles "Red" Scott, the La Jolla, Cal., investor and the new chairman of Fuqua. Scott's holdings include a passel of publicly traded vehicles such as Pier 1 Imports, and Western Sizzlin. These are controlled by Scott, 60, through Intermark and the Triton Group, two holding companies whose shares also trade.

Scott already has 15% of Fuqua and has vowed to buy control. He has paid an average $34 a share, considerably above the present market.

What worries analysts like Mabon, Nugent's Barry Rothberg is that Scott intends to achieve a creeping rather than a total takeover. If successful, this will do little for the minority holders.

It is likely Scott will do it with Fuqua's money. To the $82 million cash on hand on Jan. 1, the firm recently added $242 million (equal to just under $15 a share) by selling Georgia Federal Bank. Prior to that sale, Scott, under Federal Home Loan Board rules, would have had to seek approval anytime he had raised his stake above 10%.

Now Oppenheimer's Mel Schmidt sees Scott increasing his Fuqua stake to around 25% and then having Fuqua use part of the S&L proceeds to buy in stock at around $35 and to shrink the base. Not much of a premium there.

Nor is there likely to be much upward stock movement on the basis of this year's earnings. Most analysts are predicting around $2.50 a share, still below 1987's record.

There is a glimmer left. Fuqua owns 51% of Qualex, a 1988 joint venture with Kodak and the largest wholesale photo-processing concern in the U.S. Qualex, a $590 million year business, has two-thirds of this market. Balis Zorn's Jan Loeb feels if it raises the price of processing a print 1¢ Fuqua would reap an extra $50 million in profits or $1 a share. Competition is such, says Loeb, that Qualex could increase prices for several years ahead. That alone, he says, makes Fuqua worth as much as $48. *—Peter Millard.*
NYSE (FQA), 27¾, div. 32¢, yld. 1.1%.

Fred Langenberg will give up without a fight and indeed he has put several antitakeover provisions in place. Langenberg is a career metallurgist who started with U.S. Steel in 1951 and moved on to become president of the American Iron and Steel Institute in 1975 before joining Interlake in 1979 as president and chief operating officer. In 1982, he took charge of a company battered by recession and inflation. Since then, he has transformed a commodity metals manufacturer into a diversified technology-based collection of small industries.

The restructuring paid off. Earnings are up, debt down. Langenberg wants to continue building his portfolio with small technology-rich businesses. Unfortunately, Alfiero probably won't let him. Either way, investors would do well if they hung in there and watched the bidding. —*Jagannath Dubashi*

NYSE (IV), $15 1/4, no div.

NYSE (IK), $54, div. $1.50, yld. 2.7%.

NATIONAL EDUCATION'S BAD REPORT CARD

Like a bunch of unruly school kids, investors have fled from National Education, the nation's largest industrial training firm with revenues approaching $530 million. Since January, its stock has plunged 12 points, wiping fully 50% off the year-ago market value. It now trades at its lowest level in three years.

The events that triggered the stampede—a boardroom brouhaha and difficulties involved in an overly aggressive acquisitions campaign—appear to be rectified. If so, National Education, whose stock, adjusted for splits, had climbed tenfold in six years, may again be worth buying.

The turmoil in the executive suite began about a year ago when newly elected President James Cwiertnia quit in a row with longtime Chief Executive David Bright. This summer, Cwiertnia, 49, is back and Bright is out, replaced by General David Jones, a former chairman of the Joint Chiefs of Staff. Jones, 67, is something of a professional director—he's also on USX's and General Electric's boards. Likely he is keeping the top seat warm for Cwiertnia. But for that job Cwiertnia could have competition.

In May, the board also named Kenneth Riedlinger to run Applied Learning, a key subsidiary that offers videodiscs and computer software for training programs. Riedlinger comes with a proven executive record after stints with Ford and EDS.

What the trio now must do in a hurry is bury any ego problems and amalgamate a couple of recent acquisitions that boosted revenues by 45% but may have caused earnings to stall after quadrupling in the three prior years. The first acknowledgement of a problem came with the second-quarter earnings, which amounted to a net loss of $1.5 million, compared with a $7.5 million gain last year.

Through a handful of subsidiaries, National Education provides personal and corporate training and publishes textbooks. But integrating recent acquisitions has been difficult and has met resistance from the sales staffs. Just how severe the problem is will be more apparent as the year progresses. Last year National Education booked fully one-third of its business in the final quarter. That's when budget managers spend their remaining allocations.

Kidder, Peabody's Clarke Walser hopes year-to-year fourth-quarter earnings will be flat to modestly down, indicating that a turnaround is already under way. For the full year, Oppenheimer's Dennis Rosenberg has downscaled 1989 earnings projections from $1.25 to 75¢, compared with 1988's $1.57.

Clearly National Education needs some remedial work to clear up a credibility problem, but after that analysts say they expect to again give it a good report card. —*Peter Millard Jr.*

NYSE (NEC), 15 1/4, no div.

HOW DO YOU SAY TOYS "R" US IN GERMAN?

The inventory doesn't turn quite as rapidly as it once did. The gross margins aren't what they were. But the big surprise was that sales at Toys "R" Us units opened a year or longer hadn't advanced in the quarter ended July 31. Is some of the luster coming off the wunderkind of retailing?

Certainly not in West Germany. The opening of a new outlet caused a 14-mile backup on the local autobahn. Nor in other parts of Europe, Canada and the Far East, where Toys soon will have 70 units, with more planned in Italy and Australia in 1990.

Any fears that the grinch will steal this Christmas are decidedly premature. "I'm surprised to find the stock as cheap as it is," says Kathryn Ellis, of Morgan Stanley.

While Toys hasn't exactly sat out this leg of the bull market, its stock has stalled somewhat when compared with its earlier ascents. Analysts like Monroe Greenstein of Bear, Stearns are puzzled. "It's selling at the bottom of its multiple in recent years," says Greenstein, who foresees a 21% increase in