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Target Bets Credit Discount Will Lead to More Visits

By ANN ZIMMERMAN

Target Corp.'s credit-card portfolio hurt its performance in the recession, as delinquencies and defaults soared.

Now, the discounter sees credit cards as an important way to spur sales as the country slowly climbs out of the economic doldrums.

This fall, customers using Target-branded credit cards will get a 5% discount on every purchase at its stores. Gauging by the results of an eight-month test Target recently concluded in Kansas City, the company expects the program to drive a 1% to 2% nationwide increase in sales at stores open at least a year by luring shoppers to its stores more frequently to take advantage of the savings.

"A 5% discount every day on every transaction is unique in the retail world and has the power to drive profitable sales to Target," said Terry Scully, president of Target Financial Services.

In addition to leading to meaningful sales gains, some Wall Street analysts think Target's credit-card rewards program will be a powerful low-price hook that competitors would have trouble matching. [Wal-Mart Stores Inc.](#), in particular, has a larger base of lower-income shoppers who would be hard-pressed to qualify for a credit card.

"I think it is one of the most innovative programs to come along in retail in a long time," said Colin McGranahan, a retail analyst at Sanford C. Bernstein LLC. "Five percent off prices that are already discounted and are almost at parity with Wal-Mart is a good deal," he added.

The program is not without its risks. If the credit-card discounts do not induce shoppers to buy more than they previously did, Target could lose money on the program.

But if the program is a success, it will be an ironic turnabout for Target's credit-card business.



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Reuters

A customer purchases items at a Target store in

The Minneapolis-based company's sales and profit suffered in the recession as customers searched for the cheapest prices and shopped for only the barest of necessities. Target's shoppers shied away from the company's clothing and home furnishings, which account for about 40% of its yearly sales.

Target posted declining profit for eight consecutive quarters before breaking its streak this fall, even as rival Wal-Mart performed relatively well. Target's dismal performance during the recession led to an expensive and distracting proxy fight last spring, when one of its largest shareholders at the time, hedge fund activist Bill Ackman, attempted to get himself and four

A customer purchases items at a Target store in Dallas last September.

fund activist Bill Ackman, attempted to get himself and four other dissident candidates elected to the Target board.

Target's credit-card portfolio was a particular sticking point for Mr. Ackman, who had pushed Target to sell a stake in its credit-card business to J.P. Morgan Chase & Co. in 2008 and insisted it should unload the rest. Once a prime contributor to Target's profit, the credit-card business saw its charge-off rate jump to 15%. Its profit plunged through much of the recession and even notched a pretax loss in the quarter ended January 2009.

Shareholders resoundingly defeated Mr. Ackman's candidates at Target's annual meeting.

Since December, Target has begun to turn things around. It has reported monthly same-store sales gains as shoppers begin to slowly trade back up and to buy more discretionary products such as apparel. In May, sales gains slowed a bit, rising just 1.3%, below the company's plan.

Target said the gains are also the result of its efforts to advertise and promote its discount prices.

Earlier this year, Target began matching competitors' advertised prices on items. It also has been adding grocery departments—with fresh food and an expanded assortment of refrigerated and frozen items—to its stores, resulting in more shopping trips from its customers.

Target also has seen improvement in its financial-services business. The percentage of customers who are 30 and 60 days behind on their Target credit-card bills declined in the quarter ended May 2.

Now, Target sees the credit-card rewards program as another sales generator, geared to what remains an uncertain consumer-sales environment.

Target said the Kansas City test led cardholders to spend more at its stores and also led to an increase in applications for both its Target-branded credit card and its debit card that deducts payments immediately from the customers' checking account.

Target recently discontinued issuing new Target Visa cards, but the discount will still be available to customers who use those cards.

Peter Davis, president of Vesdia Corp., which creates rewards programs for merchants and banks, said Target's new program "is a rich offer." However, he warned that consumer savings will be eroded if shoppers carry a balance on their cards, which have a 25.4% interest rate.

One headwind Target faces with its new program is that credit-card usage in the U.S. is slowing.

Revolving credit, made up mostly of credit-card debt, in April decreased 12% compared with a year ago, according to the Federal Reserve. Revolving credit has declined for 19 consecutive months.

Analysts note the simplicity and immediacy of the offering, particularly compared with other retail credit rewards that require shoppers to amass a certain amount of purchases to qualify for a discount coupon used on future purchases.

"Those programs are frustrating and hard to keep track of," Sanford Bernstein's Mr. McGranahan said.

The new 5%-off program replaces Target's current program in which account holders receive an initial 10% off coupon and existing cardholders earn coupons for a future shopping visit.

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