Foot Locker, Inc.
NYSE:FL

Analyst: Audrey Barrucand
Sector: Consumer Disc.

BUY

Price Target: $79.19

Key Statistics as of 10/07/2016

Market Price:	$69.05
Industry:	Specialty Retail
Market Cap:	$9.2B
52-Week Range:	$50.90-71.67
Beta:	0.48

Catalysts:

- GDP growth, holiday shopping season
- Increasing number of products made by Nike, Adidas, etc., especially product line made by famous stars

Company Description:

Foot Locker, Inc. is one of the biggest specialty retailers in apparel and footwear. They offer athletic footwear, apparel, and equipment for men, women, and kids. The company is currently selling in the United States, Europe, Canada, Australia, and New Zealand. Foot Locker operates in two segments: athletic stores, such as Foot Locker, Lady Foot Locker, Kids Foot Locker, Champs Sports, Footaction, SIX:02, Runners Point, and Sidestep; and direct-to-customers segment, through their online presence. The company generates revenues based on fashion trends within the athletic industry.

Thesis

- In recent years, there has been a surge in health and fitness, which creates a greater market and increases the demand for Foot Locker's products.
- People have become more and more interested in buying athletic apparel as a fashion style, not as a workout outfit.
- The newly designed female-focused store format SIX:02 has the potential to become one of Foot Locker's primary growth engines in 2016 and beyond.

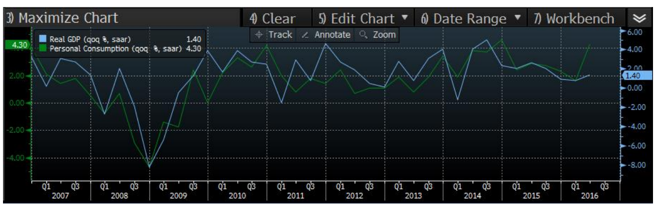
Macro Environment

Looking at the macro environment in the United States, real GDP has started picking up since the beginning of the year with a Q1 2016 growth of 0.8% and a Q2 2016 growth of 1.4%. Forecasts predict an upward trend for 2017. An estimated two-thirds of the U.S. gross domestic product comes from retail consumption.

As for the global environment, economic growth is predicted to reach 3.2% in 2016 and 3.4% in 2017, according to the IMF. Because Foot Locker is in the consumer discretionary sector, its revenues are dependent on consumers' ability and willingness to buy i.e. on GDP growth. If the economy is growing, they will be more willing to buy non-necessary products.

Industry Outlook

The retail industry for non-necessary goods is driven by GDP growth, employment and interest rates. Looking at 2017, the forecast is bullish for the industry. Because of the growth in the US economy, consumer confidence increased and so did personal consumptions, by 1.6% in Q1 2016 and by 4.3% in Q2 2016 in 2016.



In recent years, e-commerce has been gaining more and more success. The shift to e-commerce is pressuring retail traffic in the U.S. and a lack of catalysts for improvement may further challenge sales at apparel and footwear brands, as well as at retailers.

Porter's Five Forces

Bargaining Power of Suppliers: **Medium/High – 56**

Foot Locker is highly dependent on its suppliers, since it does not produce its own products. Its main suppliers, such as Nike, Adidas, and Under Armour, need to keep up with changing fashion trends, in order to appeal to customers. If these brands do not supply Foot Locker stores, the company will have no products to sell.

Bargaining Power of Customers: **Medium – 43**

Customers do not have a lot of bargaining power when it comes to prices. Items produced by Nike have the same price whether they are sold in a Nike store, at a Foot Locker store, or at Dick's Sporting Goods.

Threat of Substitutes: **Medium – 67**

There are a lot of substitutes in the shoes and clothes industry. There are a lot of types of clothes and shoes. Foot Locker differentiates itself from any common clothes shop by the type of its products and their quality. If shoppers are looking for good quality sportswear, they will not go to any clothing shop; they will go to a Foot Locker, or a direct competitor.

Intensity of Existing Rivalry: **Medium – 42**

Foot Locker has a few competitors such as Dick's Sporting Goods or Finishing Line. Rivalry between these retailers is high but there are not many of them, and considering the high demand from shoppers for sporting goods, all three shops are selling plenty of products.

Threat of New Competition: **Medium – 58**

Entering in this industry is difficult. In order to succeed, companies must obtain partnerships with reliable suppliers and be located in high-traffic areas, such as malls. To do so requires a large amount of capital, which starting companies do not necessarily have.

Focus on Growth

Over the past few months, Foot Locker has been going through a change in its business model. It has been focusing on investing in store remodeling and other initiatives to improve productivity and online operations. Spending is expected to reach 3.7% of sales, based on consensus revenue, up from the projected 2.9% in 2015 and 2.7% the previous year. Foot Locker uses remodeling and branded shop-in-shops to draw incremental traffic and drive sales per square foot in existing stores.

Foot Locker has also been focusing on decreasing its stores openings, and managed to yield more revenue and profit per square foot after closing underperforming Lady Foot Locker stores, which helped gross margins. Improved management of store-workers' wages through the use of software and other optimization tools also helped.

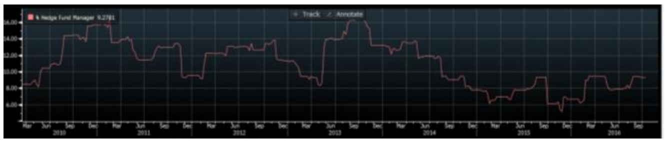
As well, the newly designed female-focused store format SIX:02 has the potential to become one of Foot Locker's primary growth engines in 2016 and beyond. The stores carry a larger mix of apparel items vs. footwear, capitalizing on the expanding popularity of "athleisure" and other products from large companies such as Nike and Under Armour. This will allow women to shop at only one store for a full outfit.
In the past months, Foot Locker has also been focusing on the development of SIX:02, their fitness clothing and athletic shoes for women. They are about to open 2 stores in NYC in 2017 and 2018. NYC being the US capital of fashion, and with increasing fashion trends, the stores will hold more fashion led clothes than previously.

Ownership

Foot Locker is mainly owned by Investment Advisors and Hedge Fund Managers.
The ownership for Hedge Fund Managers has always been low, with a high of 16% in 2013. It has seen an increase of 1% in the past month, meaning hedge fund managers are increasingly confident the stock will increase, especially since the beginning of the year, with a 3.5% increase in ownership.

54) Ownership Type	10/02/16	Curr	Change
41) Investment Advisor	76.96	76.94	-0.02
42) Hedge Fund Manager	9.27	9.28	+0.01
43) Bank	5.27	5.27	0.00
44) Pension Fund	3.00	3.00	0.00
45) Government	2.52	2.53	+0.01
46) Individual	1.31	1.31	0.00

Hedge fund manager trend:



Financials

Foot Locker is in a good position financially with increasing comparable revenues over the past 5 years, as well as consistent growth in EBITDA, and net margins.

In Millions of USD	FY 2013	FY 2014	FY 2015	FY 2016	Current/LTM	FY 2017 Est	FY 2018 Est
12 Months Ending	02/02/2013	02/01/2014	02/01/2015	01/30/2016	07/30/2016	01/31/2017	01/31/2018
Market Capitalization	5,186.4	5,613.5	7,496.8	9,254.2	9,200.9		
- Cash & Equivalents	928.0	867.0	967.0	1,021.0	945.0		
+ Preferred & Other	0.0	0.0	0.0	0.0	0.0		
+ Total Debt	133.0	139.0	134.0	130.0	129.0		
Enterprise Value	4,391.4	4,885.5	6,663.8	8,363.2	8,384.9		
Revenue, Adj	6,182.0	6,505.0	7,151.0	7,412.0	7,568.0	7,779.9	8,147.4
Growth %, YoY	9.9	5.2	9.9	3.6	4.3	5.0	4.7
Gross Profit, Adj	2,034.0	2,133.0	2,374.0	2,505.0	2,565.0	2,649.4	2,788.3
Margin %	32.9	32.8	33.2	33.8	33.9	34.1	34.2
EBITDA, Adj	740.0	805.0	946.0	1,090.0	1,119.0	1,168.2	1,252.2
Margin %	12.0	12.4	13.2	14.7	14.8	15.0	15.4
Net Income, Adj	404.0	435.0	522.0	606.0	623.6	643.3	683.8
Margin %	6.5	6.7	7.3	8.2	8.2	8.3	8.4
EPS, Adj	2.63	2.89	3.57	4.30	4.52	4.76	5.24
Growth %, YoY	45.9	10.1	23.7	20.4	14.3	10.6	10.1

As for profitability, Foot Locker has also been increasingly profitable with a return on investing capital of 21.93 in FY 2016, double the one from 2011.

In Millions of USD except Per Share	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
12 Months Ending	01/29/2011	01/28/2012	02/02/2013	02/01/2014	02/01/2015	01/30/2016
Returns						
Return on Common Equity	8.51	13.45	17.70	17.61	20.83	21.43
Return on Assets	5.92	9.35	12.37	12.52	14.72	14.72
Return on Capital	8.39	12.99	17.00	16.95	20.02	20.63
Return on Invested Capital	10.08	14.89	19.10	18.52	21.61	21.93

A negative point about Foot Locker's financials is the fact that they keep a lot of cash on hand, without reinvesting it for a greater return (twice the amount since 2011; over $1B). This cash could be used to expand its business or continue growing some of its smaller lines, or internationally, as predicted by analysts.

As for its products segments, Foot Locker's brick-and-mortar stores generated 87% of total revenue in fiscal 2016, followed by the company's e-commerce sites including Footlocker.com and Eastbay.com (13%). The U.S. market represents 72% of total sales.
Looking at the 3-year growth, its stores sales increased by 5.12% compared to 15.42% for its direct-to-customers segment. There could be an opportunity for further development of its direct-to-customer segments, especially since people find less and less time to go shopping and are more and more shopping online.

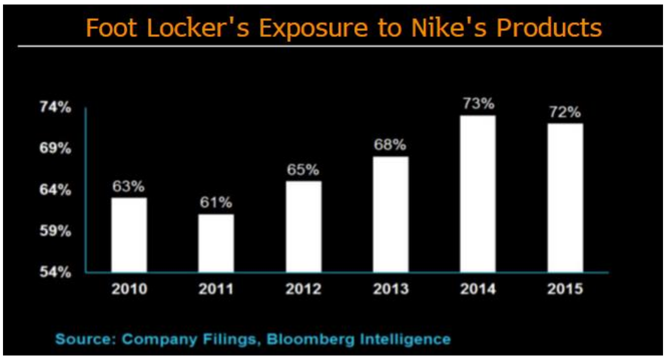
Compared to competitors, the consistent expansion in same-store sales and efficient cost controls enables Foot Locker to lead its peer group in profitability. The retailer's fiscal 2016 operating margin was well above the Finish Line (4.4%) and Dick's Sporting Goods (7.5%)

Valuation

The target price that was calculated in the pro forma is $79.19 with an intrinsic value of $68.15. According to the sensitivity attribution analysis, revenues and operating expenses are what mostly drive the stock price.
To obtain this result, the growth rate was kept equal to the last reported, even if it is expected to increase in the next quarter. As for operating expenses, they remained the same as historical, even if Foot Locker showed a slight increase in its gross and net margins. Moreover, the beta played a big role in this valuation as Foot Locker is very sensitive to it. It was historically reported at 0.72 and last reported at 0.52. A beta of 0.7 was added for the continuing period, meaning that values were added in a conservative manner. The result of $68.15 for the intrinsic value shows that Foot Locker is a little overvalued, but taking into account its expected growth, the stock will rise.

Risks

As stated before, Foot Locker is highly dependent on its suppliers, such as Nike. Foot Locker's exposure to Nike's products was 72% in 2015. But with the rising popularity of fashion-oriented athletic footwear, including recent successes from Adidas and Under Armour, it may reduce Foot Locker's reliance on Nike's products. A large exposure to just one vendor elevates the risk of lost sales in the case of disruptions in product supply, which is a non-negligible risk for investors.



Changes in fashion trends can also negatively affect the sales of the business. Retail stores have to constantly keep up with changing styles and can lose a lot of money it they do not.

Important Dates and Catalysts

When the next line of products made by a star comes out, sales will increase dramatically. The price of the stock could follow that trend if investors become more and more confident in the stock. There is a new line coming out at least every 6 months, whether it is from Nike, Puma, etc.
Another date to look at would be the day of the Q3 earnings call, November 18th. During last quarter's (8/19/16), the price of the stock increased from 61.68 to 68.49 on the day, with a volume increase to 11.840 M from an average of 1.934 M. Next quarter's earning call could have the same impact, if it again beats the estimates.

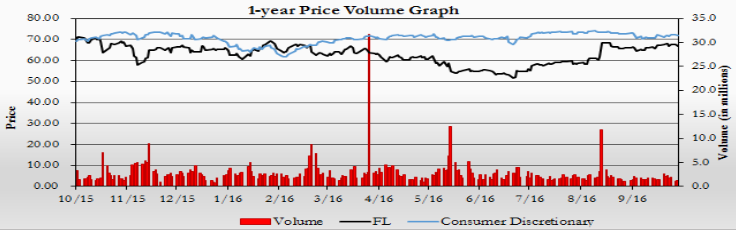
Summary

Foot Locker is a company with opportunities of growth. By focusing on growing some lines of its business, such as SIX:02, it can grow its revenues and thus, increase the value of its stock and attain the target price of $79.19 within a year, especially if GDP growth keeps increasing in the next quarters, and consumer confidence increases. With increasing demand for these products, from sports addicts to simple fashion junkies, Foot Locker is bound to see its revenues increase as well as its stock price.

CENTER FOR GLOBAL FINANCIAL STUDIES

Foot Locker, Inc. (FL) — **NEUTRAL**

Analysis by Audrey Barrucand	Current Price:	$69.05	Intrinsic Value	$67.01	Target 1 year Return: 16.24%
10/7/2016	Divident Yield:	1.6%	Target Price	$79.19	Probability of Price Increase: 91.8%



Description

Foot Locker, Inc. operates as an athletic shoes and apparel retailer.

General Information

Sector	Consumer Discretionary
Industry	Specialty Retail
Last Guidance	November 3, 2015
Next earnings date	November 19, 2016
Estimated Country Risk Premium	9.51%
Effective Tax rate	36%
Effective Operating Tax rate	32%

Market Data

Market Capitalization	$9,054.30
Daily volume (mil)	2.59
Shares outstanding (mil)	133.25
Diluted shares outstanding (mil)	138.25
% shares held by institutions	103%
% shares held by investments Managers	80%
% shares held by hedge funds	11%
% shares held by insiders	1.29%
Short interest	9.13%
Days to cover short interest	6.29
52 week high	$71.67
52-week low	$50.90
Levered Beta	0.65
Volatility	25.46%

Past Earning Surprises

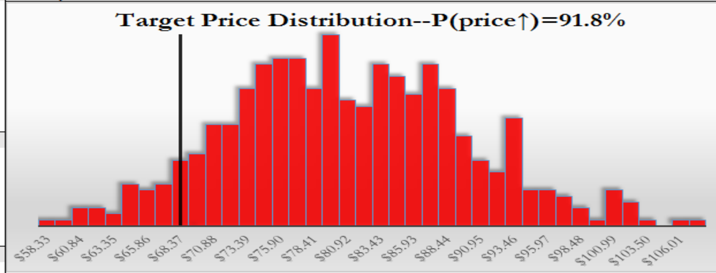
Quarter ending	Revenue	EBITDA
8/1/2015	-0.29%	13.85%
10/31/2015	-1.64%	-1.16%
1/30/2016	-2.05%	-0.69%
4/30/2016	-2.93%	-3.42%
7/30/2016	-0.06%	-2.07%
Mean	-1.40%	1.30%
Standard error	0.5%	3.2%

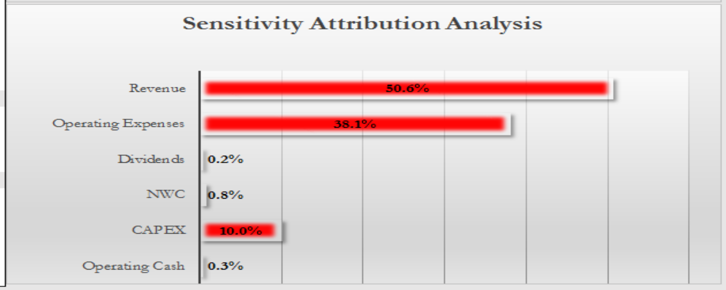
Peers

Under Armour, Inc.
Ralph Lauren Corporation
Dick's Sporting Goods Inc.
PVH Corp.
V.F. Corporation
Finish Line Inc.
DSW Inc.
Ascena Retail Group Inc.

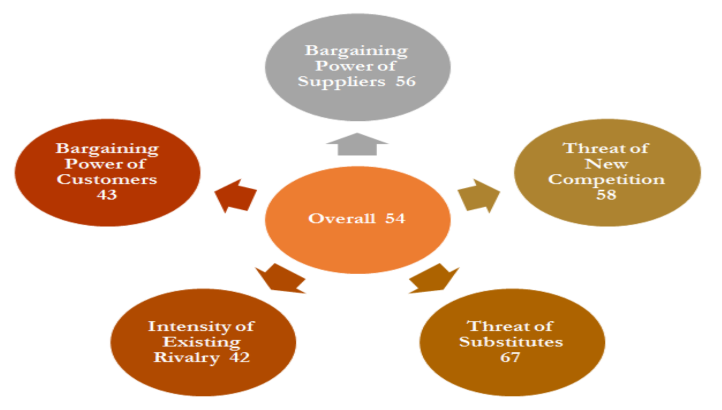
Management	Position	Total compensations growth	Total return to shareholders
Johnson, Richard	Chairman, Chief Executive Of	-100% per annum over 4y	11.37% per annum over 4y
Peters, Lauren	Chief Financial Officer and	-100% per annum over 4y	11.37% per annum over 4y
McHugh, Robert	Executive Vice President of	-100% per annum over 4y	11.37% per annum over 4y
Verma, Pawan	Chief Information Officer an	N/M	0% per annum over 0y
Cipriano, Giovanna	Chief Accounting Officer and	N/M	N/M
Maurer, John	Vice President of Investor R	N/M	N/M

Profitability	FL (LTM)	FL (5 years historical average)	Industry (LTM)
ROIC	19.2%	18.21%	22.01%
NOPAT Margin	16%	14.69%	7.5%
Revenue/Invested Capital	1.19	1.24	2.93
ROE	42.1%	41.93%	26.09%
Adjusted net margin	15%	14.10%	7.2%
Revenue/Adjusted Book Value	2.73	2.97	3.61
Invested Funds	**FL (LTM)**	**FL (5 years historical average)**	**Industry (LTM)**
Total Cash/Total Capital	14.6%	15.7%	19%
Estimated Operating Cash/Total Capital	14.6%	15.5%	N/A
Non-cash working Capital/Total Capital	15.0%	14.3%	19%
Invested Capital/Total Capital	100.3%	99.9%	82%
Capital Structure	**FL (LTM)**	**FL (5 years historical average)**	**Industry (LTM)**
Total Debt/Common Equity (LTM)	0.45	0.50	0.24
Cost of Existing Debt	2.33%	2.29%	7.24%
Estimated Cost of new Borrowing	2.02%	2.02%	7.24%
CGFS Risk Rating	AA	AA	AA
Unlevered Beta (LTM)	0.52	0.76	0.94
WACC	7.83%	9.27%	12.17%





Porter's 5 forces (scores are out of 100)



Valuation

Period	Revenue growth	NOPAT margin	ROIC/WACC
Base Year	4.3%	16.1%	2.45
7/30/2017	3.9%	14.7%	1.61
7/30/2018	4.1%	14.4%	1.56
7/30/2019	4.4%	14.2%	1.59
7/30/2020	4.0%	14.0%	1.56
7/30/2021	4.0%	13.9%	1.56
7/30/2022	4.0%	13.9%	1.57
7/30/2023	4.0%	13.9%	1.58
7/30/2024	4.0%	13.8%	1.59
7/30/2025	4.0%	13.8%	1.60
7/30/2026	4.0%	13.8%	1.61
Continuing Period	4.1%	13.6%	1.61

Period	Invested Capital	Net Claims	Price per share
Base Year	$5,011.20	$3,762.26	$65.88
7/30/2017	$5,424.35	$2,644.50	$78.04
7/30/2018	$5,784.87	$1,505.12	$89.86
7/30/2019	$6,037.88	$509.89	$101.79
7/30/2020	$6,345.04	-$478.12	$113.95
7/30/2021	$6,474.91	-$1,490.06	$126.31
7/30/2022	$6,766.68	-$2,637.79	$139.78
7/30/2023	$6,941.58	-$3,664.62	$152.50
7/30/2024	$7,275.04	-$4,698.23	$165.38
7/30/2025	$7,616.58	-$5,737.87	$178.41
7/30/2026	$7,951.37	-$6,782.72	$191.56
Continuing Period			