March 10th, 2017

NYSE: Foot Locker (FL)

Alec Odnoha

Sector: Consumer Discretionary
Industry: Athletic Footwear and Apparel
Current Price: $76.99
Target Price: $82.95

Company Description: Foot Locker is a leading global athletic footwear and apparel retailer. Stores offer selections of premium products for a variety of activity, such as basketball, running, and training. Foot Locker caters to sneaker enthusiasts and athletes alike and its products are primarily manufactured by top athletic brands. Foot Locker operates 3,383 stores, located in 23 countries globally. Foot Locker implements a direct-to-customer business model and aims to be the top global retailer for athletically inspired shoes and apparel.

BUY

Current Price: $76.99
Target Price: $82.95
Market Cap: 10.2B
S&P Debt Rating: BB+
ROE (LTM): 25.2%
Ke: 7.65%
P/E Ratio: 15.69
Net Income Margin: 8.55
Equity Multiplier: 1.46
Total Asset Turnover: 2.02
Cash/Total Assets: 1.71

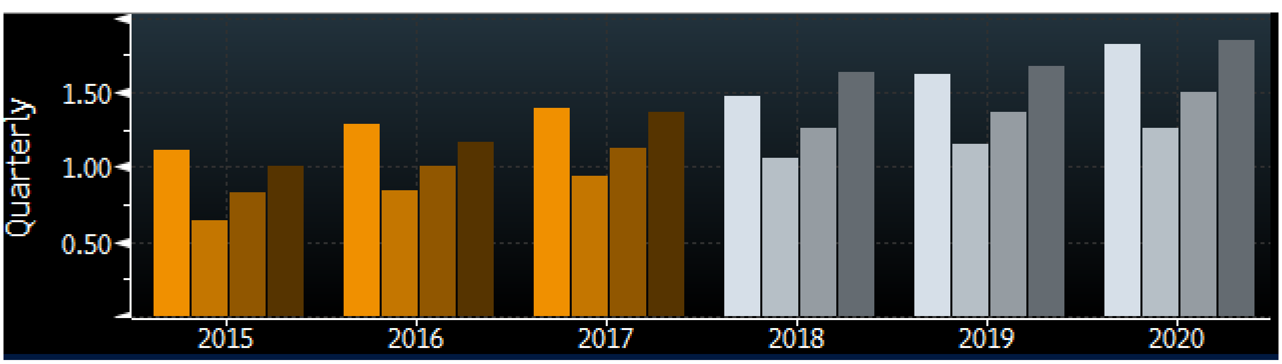
Catalysts:

- **Short Term: Completion of newly remodeled retail stores, demand of lifestyle products**
- **Mid-Term: Continued re-investment in business infrastructure, rise in e-commerce operations**
- **Long-Term: Further expansion into Europe, development of flagship stores in metropolitan areas, investment of technology and customer experience**

Thesis: Foot Locker currently operates in the highly competitive specialty retail market, and has been subject to a decline in the industry in recent years. However, Foot Locker has managed to keep up growth in revenues and solid marginal performance running in two reportable segments, athletic stores and direct-to-consumer. The company has held true to their business model and continues to seek ways to improve operations. Historically, the company has maintained a low level of debt and has increased domestic and foreign exposure to their brand name. As a result, the company has been able to reinvest nicely to improve their business model. Moving forward in 2017, several initiatives are in place to ensure a favorable position in the market. Advancements in technology that management believes are essential to business operations will be in Foot Locker's favor in the future, as digital sales and e-commerce operations become more prevalent in the industry to compensate for dwindling retail presence. Foot Locker envisions aggressive investments to maintain its solid revenue growth and is currently in a healthy enough financial position to do so.

Earnings Performance: Foot Locker and both of its segments experienced strong performance in Q4 of 2016. Net income achieved earnings of $189 million in Q4, up approximately 19.6% from $158 million in Q4 a year prior. The company as a whole also saw a gain in annual revenue, measured at $7.8 billion, which is up 4.8% from last years' reported total of $7.4 billion. Foot Locker's two primary segments, athletic stores and direct-to-consumer, also saw growth. Athletic retail stores attained a 4% comparable sales gain in Q4, and direct-to-consumer sales increased to 15.3% of net sales for the quarter, and 13.2% of net sales for the year, up from 14.6% and 12.7%, respectively. Foot Locker has experienced some downswings in sales numbers in a few of their retail locations, specifically Germany and its difficult retail climate. Nonetheless, the company was still able to achieve financial growth and it resulted in an end-year record for full year net income margin for the company, at 8.4%. EPS increased from $4.29 to $4.82, up about 12 %. The company introduced a $1.2 billion share repurchase plan in 2016, which, as a result of the repurchasing, is slated to spark a double digit increase of EPS, which can be assumed as a result of less number of shares outstanding. As shown in Exhibit 1, the company has increased its quarterly values of EPS year-over-year, and those projections continue in the years ahead.

Exhibit 1: (**Source: Bloomberg)**



Along with its share repurchase plan, Foot Locker returned $147 million of cash to shareholders, finalizing at 85% of net income returned to shareholders. The company's historically consistent increase in performance and belief in re-investing run consistent with some of their main strategies, which are to continue to drive performance in core business and pursue expansionary opportunity. The company's strong financial performance puts them in a position where those goals are not out of reach, and can surely create value.

Industry Outlook: North American apparel and footwear brands are continuing to face a shrinking sales growth; retailers are taking a more cautious position on inventory, limiting future levels. Retail is dwindling; foot traffic in malls is on the decline, roughly by about 5.7% on average per month through November. There is an ever present shift in mobile digital sales and e-commerce operations, and Foot Locker has that direct-to-consumer capability. Apparel and footwear are two of the fastest growing categories in e-commerce, which reiterates the need for brick-and-mortar retailing. Foot Locker can utilize that trade-off, as main strategies call for both expansionary measures taken with brick-and-mortar stores, and the development of a more powerful digital business in hopes to better connect with customers and adhere to their preferences. Foot Locker's brick-and-mortar style retail stores accumulated 87% of revenue in FY 2016, while digital business and online websites and vendors (direct-to-consumer) totaled 13%.

European Presence: Being a global brand, Foot Locker and its subsidiaries spread globally in numerous countries. The company believes that market share in Europe is vital to core business operations, and offers substantial opportunity for growth. One of Foot Locker's primary growth strategies is to re-invest into itself to remodel store layouts and revamp product lines. The European sector of the company maintained high levels of profitability and productivity during 2016 despite a slower sales increase. The company has added 22 stores over fiscal year 2016, and is currently seeking ideal retail opportunities to invest in, as evidenced by the opening of a "Jumpman" store in Paris, a segment of the Jordan brand of shoes, a rapidly growing brand. Basketball sneakers, which drive a large amount of U.S. sales for the company represent a great opportunity to increase target marketing. Emphasis on basketball coupled with the running shoe preference that is prevalent in Europe offer channels for growth. Foot Locker's Sidestep and Runner's Point Germany locations, that infiltrate the running shoe and lifestyle markets, struggled with growth in Q4 of last year, but that can be attributed to the company undergoing a management change coupled with the rough retail environment in Germany. The company plans to continue to establish new banner stores across the region and work internally with its vendors to better position banner stores for the years to come.

Margins	FY 2014	FY 2015	FY 2016	FY 2017
12 Months Ending	2/1/2014	2/1/2015	1/30/2016	1/28/2017
Gross Margin	32.79	33.2	33.8	33.94
EBITDA Margin	12.25	13.2	13.29	14.91
Operating Margin	10.21	11.26	11.29	12.88
Net Income Margin	6.59	7.27	7.3	8.55

Financial Performance: According to historical data, Foot Locker has seen strictly positive increases in performance margins, although some may be incremental. According to the following snapshot, it is apparent that Foot Locker has maintained a high level of operation. The increase in each margin can be indicative of continued revenue growth. Executive teams at Foot Locker have also taken measures to cut costs. SG&A expenses decreased as a direct result of better management of variable expenses and levering of fixed expenses. Gross margin increased a total of 10 basis points for the full year 2016, which is consistent with the company's annual guidance. One of the focuses for this year is the opening and closing of store locations, to better focus on optimal placement for growth. Foot Locker is slated to open 90 stores, including some flagship locations, while also closing down 100. What this will do is cut down operating costs marginally as a result of fewer stores opening, which can lead to a continual increase in EBITDA margin.

The company is liquid, and has never really relied on debt to fund their operations. The company's primary source of liquidity comes from the cash flow from earnings. Cash is typically used for funding inventory and other working capital requirements, such as CAPEX for store openings and re-modelings which run consistent with the company's plan to upgrade stores globally to attract newer customers and make the store a more inviting consumer experience. The Cash Ratio, Current Ratio, and Quick Ratio have been maintained at safe levels over a number of years, which shows that the company has been consistently able to fulfill any short-term obligations that they may incur.

In Millions of USD except Per Share	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
12 Months Ending	01/28/2012	02/02/2013	02/01/2014	02/01/2015	01/30/2016	01/28/2017
Cash Ratio	1.55	1.46	1.38	1.39	1.46	1.71
Current Ratio	3.79	3.72	3.75	3.53	3.72	4.30
Quick Ratio	1.64	1.57	1.54	1.50	1.59	1.71

Source: Bloomberg

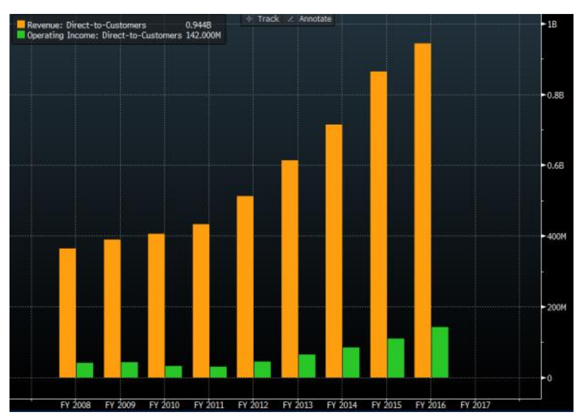
In comparison to others in the industry, Foot Locker is shown to be outperforming in terms of certain measures of risk. Despite this last year having a low WACC compared to competitors, the historical WACC of Foot Locker still lingers close to the average value for competitors. Basically, that indicates that there is a slightly higher amount of risk associated with operations of the company. However, having a lower unlevered beta than competitors, both historically and LTM, is indicative of lesser risk, since the lower beta means that the company is not as volatile as its competitors in relation to the market. Also, as shown, Foot Locker tends to generate a higher return on invested capital than its competitors.

ROIC	History	LFY
FL	17.0%	22.5%
Competitors	16.3%	13.3%

WACC	History	LFY
FL	14.1%	9.1%
Competitors	12.2%	19.2%

Unlevered Beta	History	LFY
FL	1.07	0.57
Competitors	1.25	0.81

E-Commerce: E-commerce is quickly overtaking retail stores as the preference for consumers when it comes to shopping. Since e-commerce started gaining prominence, Foot Locker has seen marginal gains in overall performance from online sales, both from their subsidiary Eastbay.com, and Footlocker.com. With the retail industry gradually adapting to that method, it is likely a premiere specialty retailer could utilize this technology. For the company, this segment increased 9.1% in revenue generated, up to $944 million from $865 million last year. As evident in the graph, Foot Locker has seen immense increases in both revenues and operating income year-over-year for direct-to-consumer operations. With plans set to enhance their



Source: Bloomberg

digital business even further by investing in newer technology and the introduction of newer generation e-commerce platforms and point-of-sales systems, it is likely that performance in this segment will continue to rise.

Kid's Foot Locker/SIX:02 : Among the company's growth pillars, Kid's Foot Locker proves to continually be the largest dollar sales increase. A key initiative by Foot Locker is to grow the base of Kid's Foot Locker both domestically and internationally while also promoting an exciting and appealing environment. Younger customers are connected at an early age, and one risk with expansion of this brand would be that some styles are not available to the consumer right away, which can be attributed to the dip in sales for Kid's Foot Locker. However, this dip was more than offset by comparable sales increases in the adult banner stores of kid's footwear. Continuing to lead in lifestyle running and basketball shoe markets will lead to more growth opportunity in the Kid's Foot Locker brand of the business.

Foot Locker's SIX:02 stores, a female-focused store format that has been introduced, could potentially be a huge driving factor in growth for the company. The number of locations of Lady Foot Locker has been in a steady decline, and the opening of a SIX:02 flagship store on 34th street is slated to introduce a vast number of new customers. Similar pinnacle stores are currently in the works for development and location for later this year. The addition of SIX:02 stores will help the company to be able to attain a solid female client base and will likely be a contributing factor in sales growth in the future.

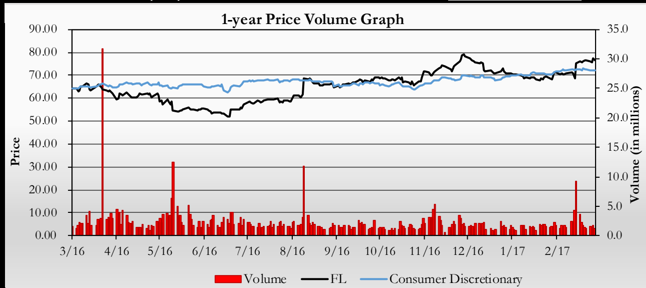
Conclusion:

In summation, despite already holding shares, I am proposing a BUY for Foot Locker stock. The company has kept up a level of performance over the years that is top-notch and has been able to strategically maneuver around multiple markets to gain market share in their industry. I find that a healthy financial infrastructure and effective initiatives lay out the groundwork for a sharp increase in value in the coming months. The advancements being made in technology to benefit the industry and strategic use of capital allocation to reinvest into the company will lead to a strong performance for 2017. The ever changing retail market is evolving, and Foot Locker still maintains the capability of being the premiere global specialty retailer they strive to be. A target price of $82.95 is surely within reach by the end of this year.

SIENA college | BJORKLUND FUND

Foot Locker, Inc. (FL) — CENTER FOR GLOBAL FINANCIAL STUDIES — BULLISH

Analysis by Alec Odnoha	Current Price:	$76.99	Intrinsic Value	$135.54	Target 1 year Return: 75.43%
3/11/2017	Divident Yield:	1.8%	Target Price	$133.66	Probability of Price Increase: 100%



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	May 19, 2017
Estimated Country Risk Premium	6.25%
Effective Tax rate	40%
Effective Operating Tax rate	34%

Market Data

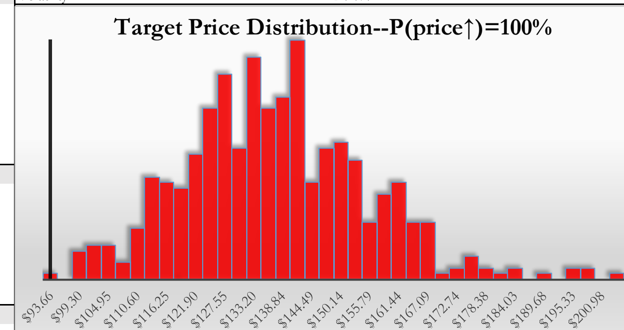
Market Capitalization	$10,190.78
Daily volume (mil)	1.22
Shares outstanding (mil)	132.36
Diluted shares outstanding (mil)	135.10
% shares held by institutions	74%
% shares held by investments Managers	76%
% shares held by hedge funds	9%
% shares held by insiders	1.28%
Short interest	6.91%
Days to cover short interest	5.11
52 week high	$79.43
52-week low	$50.90
Levered Beta	0.57
Volatility	24.47%

Past Earning Surprises

Quarter ending	Revenue	EBITDA
1/30/2016	-2.05%	-0.69%
4/30/2016	-2.93%	-3.42%
7/30/2016	-0.06%	-2.07%
10/29/2016	-1.67%	-1.33%
1/28/2017	-1.45%	-2.45%
Mean	-1.63%	-1.99%
Standard error	0.5%	0.5%

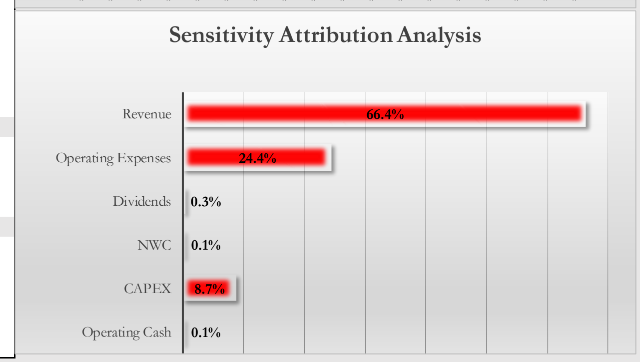
Peers

- Under Armour, Inc.
- Dick's Sporting Goods, Inc.
- PVH Corp.
- Ralph Lauren Corporation
- DSW Inc.
- V.F. Corporation
- The Finish Line, Inc.
- L Brands, Inc.

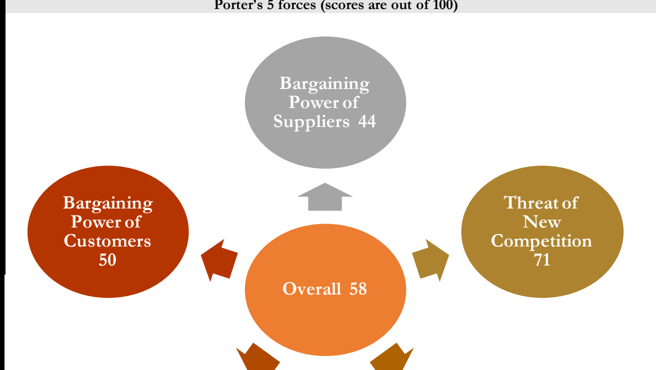


Management	Position	Total compensations growth	Total return to shareholders
Johnson, Richard	Chairman, Chief Executive Of	-100% per annum over 4y	11.37% per annum over 4y
Peters, Lauren	Chief Financial Officer and	-100% per annum over 4y	11.37% per annum over 4y
McHugh, Robert	Executive Vice President 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	12.2%	11.32%	20.49%
NOPAT Margin	12%	13.21%	6.9%
Revenue/Invested Capital	1.05	0.86	2.98
ROE	23.9%	21.08%	24.37%
Adjusted net margin	10%	10.94%	6.2%
Revenue/Adjusted Book Value	2.47	1.93	3.93
Invested Funds	**FL (LTM)**	**FL (5 years historical average)**	**Industry (LTM)**
Total Cash/Total Capital	12.6%	12.9%	19%
Estimated Operating Cash/Total Capital	12.6%	12.7%	N/A
Non-cash working Capital/Total Capital	11.7%	11.5%	19%
Invested Capital/Total Capital	97.9%	97.4%	82%
Capital Structure	**FL (LTM)**	**FL (5 years historical average)**	**Industry (LTM)**
Total Debt/Common Equity (LTM)	0.55	0.62	0.24
Cost of Existing Debt	5.83%	7.85%	7.24%
Estimated Cost of new Borrowing	6.09%	6.09%	7.24%
CGFS Risk Rating	D	D	D
Unlevered Beta (LTM)	0.45	0.73	0.95
WACC	6.34%	8.02%	9.59%



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



Valuation

Period	Revenue growth	NOPAT margin	ROIC/WACC
Base Year	4.8%	11.7%	1.92
1/28/2018	3.8%	12.4%	1.96
1/28/2019	3.1%	12.9%	2.07
1/28/2020	2.9%	12.5%	1.90
1/28/2021	2.6%	12.5%	1.93
1/28/2022	2.6%	12.4%	1.94
1/28/2023	2.8%	13.5%	2.15
1/28/2024	3.1%	14.6%	2.36
1/28/2025	3.3%	15.7%	2.58
1/28/2026	3.6%	17.0%	2.83
1/28/2027	3.8%	18.0%	3.02
Continuing Period	4.1%	19.1%	2.59

Period	Invested Capital	Net Claims	Price per share
Base Year	$6,359.34	$5,049.33	$196.38
1/28/2018	$6,730.97	$4,319.18	$209.70
1/28/2019	$6,957.95	$4,466.17	$221.31
1/28/2020	$7,189.05	$4,459.02	$229.72