

December 8, 2017

**Nike: NKE**

John Graziano

**Sector: Consumer Discretionary**

**Industry: Textiles, Apparel,  
and Luxury Goods**

**Current Price: \$61.30**

**Target Price: \$61.85**

**Company Description:** NIKE, Inc. designs, develops, and markets athletic footwear, apparel, equipment, and accessory products for men, women, and children. The company sells its products worldwide to retail stores, through its own stores, subsidiaries, and distributors.

## HOLD

Current Price: \$61.30

Target Price: \$61.85

Market Cap: 100B

Average Volume: 10.1M

ROIC: 25.45%

ROIC/WACC: 2.88



## Thesis:

Nike has an equal mixture of both bear and bull signals which causes the stock to garner a hold rating. Black Friday sales are estimated at all time highs which give Nike a head start to begin one of the busiest times of the year. Nike still remains and extremely popular brand which will continue to drive growth for the athletic apparel behemoth. Nike has begun to implement the Consumer Direct Offense, its plan for future growth in the competitive retail industry. However all of these bull signals are offset by major industry headwinds which will impact the company for the next four to six quarters and possibly beyond.

## Catalysts:

- **Short Term(within the year):** Record Black Friday Numbers
- **Mid Term(1-2 years):** Industry weakness
- **Long Term(3+):** Long Term Customer Direct Offense and Nike's history of success

## Industry Performance and Outlook:

It is no secret that the retail industry has been facing massive headwinds in the last twelve to twenty-four months. This will most likely continue into the first half of 2018 as well with Andy Campion the Nike CFO stating that “We believe there will be short-term headwinds within the U.S. retail landscape that will dampen growth. NIKE’s primary measure of success in North America in the near-term will be driving growth in our NIKE Direct businesses and through new NIKE consumer experiences with our strategic partners.” This shift to DTC business and consumer experience is what is now necessary to succeed in the hyper competitive retail industry. Increasing DTC sales increases margin and with DTC comes a more personal and controllable customer interaction experience. This is an integral part of the developing landscape of retail in both North America and worldwide. The retail tracking ETF <sup>[SEP]</sup>XRT is down 4.2% YTD compared to the S&P 500 which is up 18%. Going forward, companies <sup>[SEP]</sup>will have to adapt and expand within a few key <sup>[SEP]</sup>categories. First, technology will be a major driver in <sup>[SEP]</sup>the industry both on the companies’ side with <sup>[SEP]</sup>increased operating efficiencies and on the customer <sup>[SEP]</sup>side in terms of how they purchase product. Second <sup>[SEP]</sup>will be the creation of a meaningful experience for the customer within the store as foot traffic numbers are down across the board. Third there needs to be an increased customization in both the online and in store channels a report by KPMG stated “The importance of personalization in retail, shows that businesses that are currently personalizing online user journeys, and who are also able to quantify the improvement, are seeing an increase in sales of 19 percent on average.”



## Business Description:

Nike focuses on product offerings in nine key categories: Running, NIKE Basketball, the Jordan Brand, Football (Soccer), Men’s Training, Women’s Training, Action Sports, Sportswear (sports-inspired lifestyle products) and Golf. Men's Training includes our baseball and American football product offerings. The company also market products designed for kids, as well as for other athletic and recreational uses such as cricket, lacrosse, tennis, volleyball, wrestling, walking and outdoor activities. NIKE’s athletic footwear products are designed primarily for specific athletic use, although a large percentage of the products are worn for casual or leisure purposes. The company places considerable emphasis on innovation and high-quality construction in the development and manufacturing of their products. Sportswear, Running and the Jordan Brand are currently our top-selling footwear categories these categories are expected to continue to



lead in footwear sales. Nike also sells sports apparel covering the previously mentioned categories, which feature the same trademarks and are sold predominantly through the same marketing and distribution channels as athletic footwear. The sports apparel, similar to the athletic footwear products, is designed primarily for athletic use and shows the company’s commitment to innovation and high-quality construction. Nike also has wholly-owned subsidiaries of Converse and Hurley.

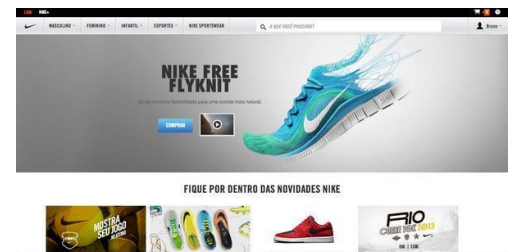
## Segments:

Nike segments its business in a two tiered system, first the company splits by geography into seven locations and two operating divisions, and second within those geographies sales are broken into footwear, apparel, and equipment as well as wholesale and DTC. The North American segment of Nike's business is the portion facing the greatest industry headwinds due to both the emergence of Amazon and the high amount of promotional activity needed. North American same store sales growth was 3% which was a solid number as many North American retailers have seen a flat or negative growth over the last year. The other six segments compose Nike's international exposure which makes up 55% of business and is growing. The Segment has reported same store sales growth of 9-17% which is consistent with the international retail industry outlook which is much stronger. This strength is due to less promotional activity and a strong demand for Nike product, especially in Asia and Western Europe.

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## Long Term Growth:

Nike has introduced the company's long term growth strategy called The Consumer Direct Offense in which they input their Triple Double Strategy. This Strategy is focused on doubling speed, innovation, and consumer direct which will result in growth over the long term and succeeding even in strong industry headwinds.



Nike provided an update on these long term plans during an investor day held on October 25th. The information provided at this information day were met well in the market with share prices jumping 7% on this news. There were several key parts of information at the meeting. First, is that 75% of growth for Nike is coming from the international portion of business. Second was the guidance given for the next 5-7 years stating that Nike's revenue would grow in the high single digits with mid-teens growth in EPS. Third was the investment Nike is making in production which will get midsole production down from 50 minutes to 2.5 minutes. Fourth, was overall company gross margin is expected to grow by 50 Bps per year for the next five years. This will be done by growth in DTC, enhancing the price to value relationship, cost initiatives, and increased efficiencies from 2x speed and 2x direct. Last, Nike is pursuing investment/partnerships in data-analytics, machine learning, AR, AI, and digital creation. These five factors give guidance to the future and show that Nike is committed to evolving and growing its industry leading position.

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## Competition:

Within the retail industry the subsection of athletic apparel and shoe companies is even more competitive than the broader industry. This competition boils down to three main companies, Nike, Adidas, and Under Armour. In the last 24 months Adidas has begun to make major strides into eating into Nike's market share however, they have relinquished some of these gains in the last 6 months. Three years ago, Under Armour was taking the athletic apparel sub industry by storm however in the last twelve months Under Armour has been getting hammered by product delays and shrinking demand. This is shown in the chart below where Adidas is closing the gap in terms of ROIC/WACC, P/E, and has a better one-year total return vs Nike.

Under Armour is headed in a different direction as shown in the chart and is desperately looking for a turnaround.

Name	Ticker	Mkt Cap	ROIC LF	ROIC/WACC Ratio	EV/BE EBITDA Curr Yr	1Y Tot Ret	P/E
Median		6.74B	16.80%	1.52	17.39	29.59%	26.71
100) NIKE INC -CL B	NKE US	97.97B	25.45%	2.88	17.80	20.74%	25.56
101) SKECHERS USA INC-CL A	SKX US	5.58B	15.70%	1.36	11.12	34.46%	21.95
102) ADIDAS AG	ADS GR	43.88B	17.91%	1.99	15.17	29.59%	26.71
103) PUMA SE	PUM GR	6.74B	--	1.52	17.39	62.07%	43.70
104) UNDER ARMOUR INC-CLASS A	UA US	5.59B	5.34%	-0.18	20.49	-55.34%	31.90

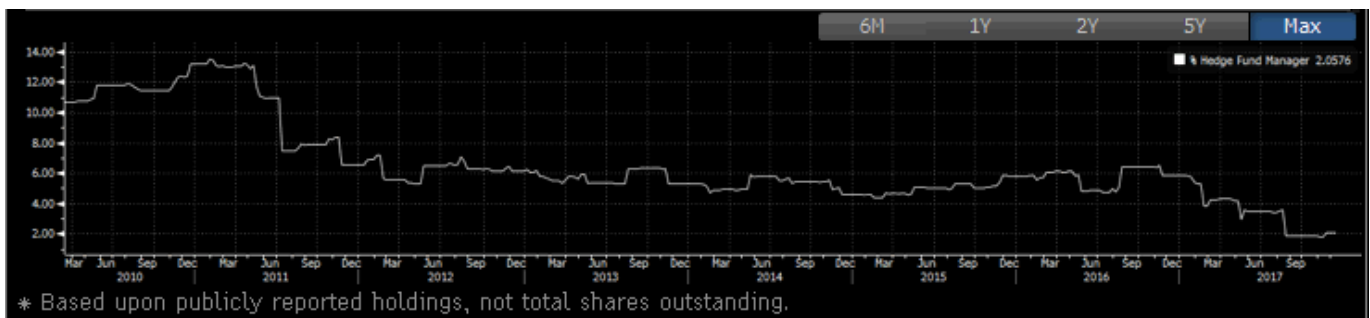
(Accounting Adjustments: Adjusted for Abnormal Items When Applicable)

10 Analyze List

## Ownership:

Nike is owned 91% by institutional investors with 83% coming from investment advisors and only 2% from hedge funds. Hedge funds have been steadily reducing their positions within Nike and this is due to the headwinds the industry are facing short term. In 2011 Hedgefunds held 14% of the float compared to the two percent currently. This is all with a low short interest as investors aren't betting against Nike, rather there is just not enough possible return for the allotted risk.

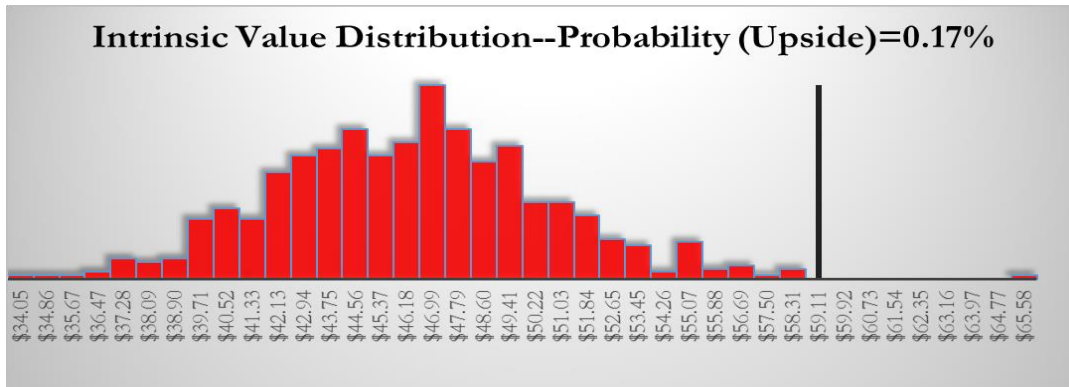
54) Ownership Type	12/03/17	Curr	Change
41) Investment Advisor	83.12	83.12	0.00
42) Pension Fund	5.17	5.17	0.00
43) Bank	2.64	2.64	0.00
44) Individual	2.11	2.11	0.00
45) Hedge Fund Manager	2.06	2.06	0.00
46) Government	1.65	1.65	0.00
47) Insurance Company	1.19	1.19	0.00
48) Sovereign Wealth Fund	0.84	0.84	0.00
49) Brokerage	0.80	0.80	0.00



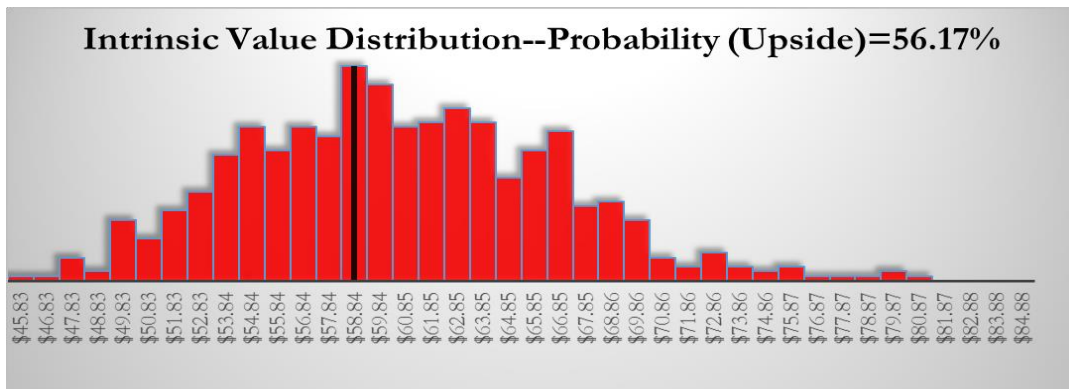
## Conclusion:

In conclusion, Nike is an industry leader in an industry that has been and will continue to face headwinds in the coming months. These headwinds have caused hedge funds to withdraw their positions recently. However, Nike has a proven track record and a 5 year plus business plan in the Consumer Direct Offense that is aiming to hit specific financial goals. There is also the possibility that the industry is beginning to come out of its slump after Black Friday reported record sales. All of this taken into account will lead to three distinct possibilities.

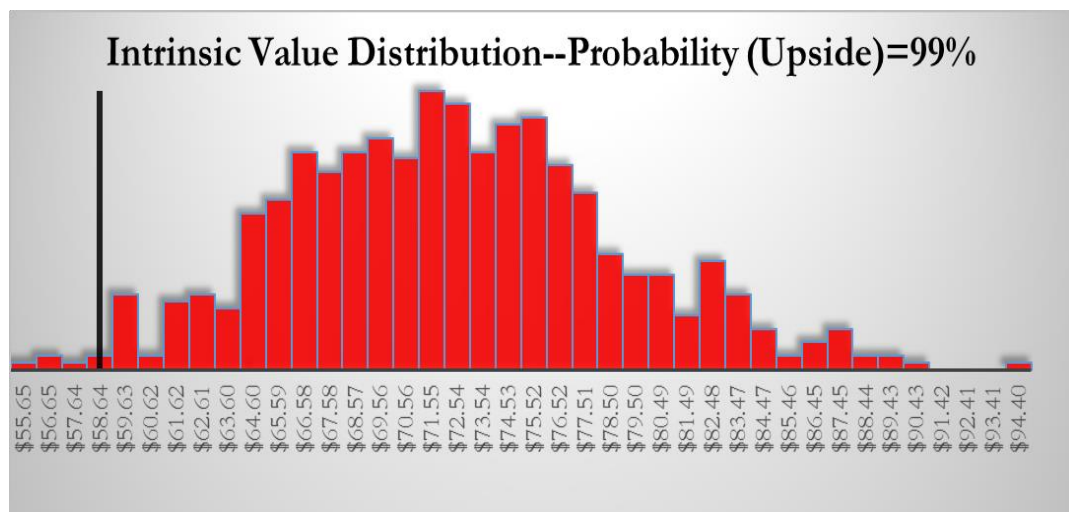
**Bear Case:** In the bear case, industry headwinds prove to be stronger than expected and the long-term strategy that Nike put in place doesn't work to the full extent. This causes slower growth and more promotional activity leading to slimmer margins and a one-year target price of 47.79 which results in a 22% loss



**Realistic Case:** In the realistic case, everything pans out as described in the report and the industry headwinds are as expected causing the one-year target price to be 61.85 which is just \$0.65 higher than the current price.



**Bull Case:** Last is the bull case where the DTC business picks up quicker than expected, industry headwinds are neutralized and the implementation of the Consumer Direct Offense lead to margin improvement quicker than expected this would lead to a one-year target price of 73.56 for a return of 20%.





# NIKE, Inc. (NKE)

## CENTER FOR GLOBAL FINANCIAL STUDIES

NEUTRAL

Analysis by John  
12/4/2017

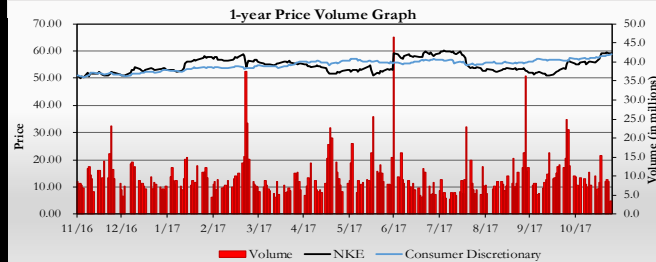
Current Price:  
Divident Yield:

\$59.50  
1.2%

Intrinsic Value  
Target Price

\$52.73  
\$59.39

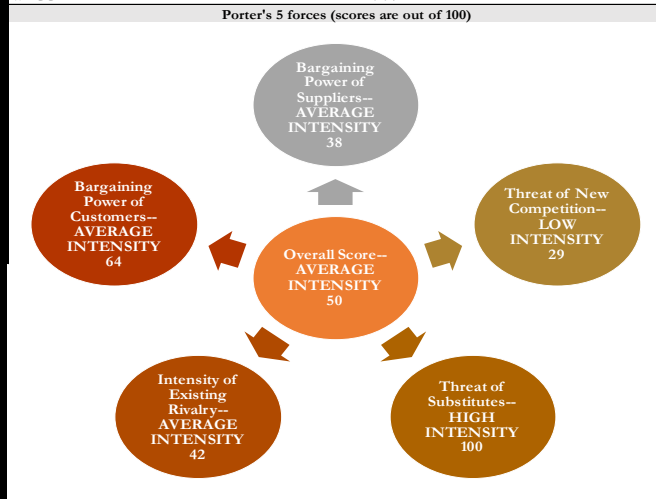
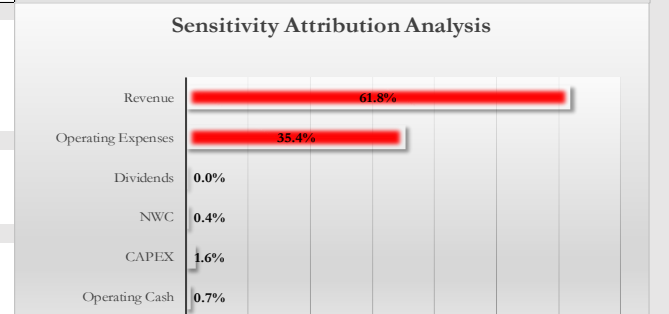
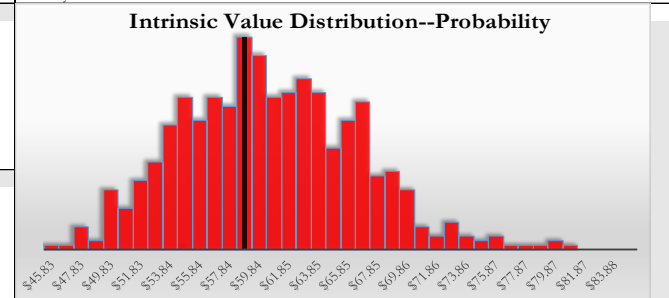
Target 1 year Return: 1.06%  
Probability of Price Increase: 56.17%



Description	
NIKE, Inc., together with its subsidiaries, designs, develops, markets, and sells athletic footwear, apparel, equipment, and accessories worldwide.	
General Information	
Sector	Consumer Discretionary
Industry	Textiles, Apparel and Luxury Goods
Last Guidance	November 3, 2015
Next earnings date	December 21, 2017
Estimated Country Risk Premium	6.80%
Effective Tax rate	22%
Effective Operating Tax rate	22%

Market Data	
Market Capitalization	\$97,287.45
Daily volume (mil)	6.99
Shares outstanding (mil)	1631.52
Diluted shares outstanding (mil)	1684.00
% shares held by institutions	116%
% shares held by investments Managers	53%
% shares held by hedge funds	2%
% shares held by insiders	21.16%
Short interest	2.23%
Days to cover short interest	3.62
52 week high	\$60.53
52-week low	\$50.06
Volatility	20.86%

Past Earning Surprises			
Quarter ending	Revenue	EBITDA	
8/31/2016	2.25%	5.32%	
11/30/2016	1.34%	15.64%	
2/28/2017	-0.35%	10.73%	
5/31/2017	0.58%	8.37%	
8/31/2017	-0.20%	12.55%	
Mean	0.72%	10.52%	
Standard error	0.5%	1.8%	
Management		Peers	
Position		Total compensations growth	Total return to shareholders
Parker, Mark	Chairman, CEO & President	3.87% per annum over 6y	5.25% per annum over 6y
Campion, Andrew	CFO & Executive VP	-18.56% per annum over 1y	-3.06% per annum over 1y
Sprunk, Eric	Chief Operating Officer	5.36% per annum over 6y	5.25% per annum over 6y
Edwards, Trevor	President of NIKE Brand	7.44% per annum over 6y	5.25% per annum over 6y
Spillane, Michael	President of Categories & Pr	N/M	N/M
Knight, Philip	Co-Founder and Chairman Emer	N/M	N/M
Profitability		Peers' Median (LTM)	
NKE (LTM)		NKE (5 years historical average)	
Return on Capital (GAAP)	25.1%	26.33%	8.44%
Operating Margin	9%	8.98%	4.54%
Revenue/Capital (GAAP)	2.82	2.93	1.86
ROE (GAAP)	29.7%	25.3%	17.0%
Net margin	10.6%	10.4%	3.8%
Revenue/Book Value (GAAP)	2.80	2.43	4.50
Invested Funds		Peers' Median (LTM)	
NKE (LTM)		NKE (5 years historical average)	
Cash/Capital	30.6%	33.9%	17.1%
NWC/Capital	29.2%	17.9%	11.4%
Operating Assets/Capital	39.5%	47.2%	63.9%
Goodwill/Capital	0.7%	1.0%	7.5%
Capital Structure		Peers' Median (LTM)	
NKE (LTM)		NKE (5 years historical average)	
Total Debt/Market Capitalization	0.34	0.22	0.62
Cost of Existing Debt	3.4%	2.4%	4.4%
CGFS Rating (F-score, Z-score, and default Probability)	BBB	BBB	BBB
WACC	9.9%	9.1%	9.9%



Valuation	
Period	Revenue Growth Forecast
Base Year	4%
8/31/2018	7%
8/31/2019	7%
8/31/2020	7%
8/31/2021	12%
8/31/2022	11%
8/31/2023	10%
8/31/2024	10%
8/31/2025	8%
8/31/2026	6%
8/31/2027	4%
Continuing Period	2%
NOPAT Margin Forecast	
Base Year	12.5%
8/31/2018	11.7%
8/31/2019	12.3%
8/31/2020	12.5%
8/31/2021	12.5%
8/31/2022	13.0%
8/31/2023	13.5%
8/31/2024	14.1%
8/31/2025	14.6%
8/31/2026	15.1%
8/31/2027	15.6%
Continuing Period	16.1%
Revenue to Capital Forecast	
Base Year	2.15
8/31/2018	2.09
8/31/2019	1.79
8/31/2020	1.57
8/31/2021	1.48
8/31/2022	1.40
8/31/2023	1.32
8/31/2024	1.24
8/31/2025	1.16
8/31/2026	1.07
8/31/2027	0.98
Continuing Period	0.88
WACC Forecast	
Base Year	9.9%
8/31/2018	10.4%
8/31/2019	10.2%
8/31/2020	10.3%
8/31/2021	10.2%
8/31/2022	10.2%
8/31/2023	10.2%
8/31/2024	10.3%
8/31/2025	10.3%
8/31/2026	10.4%
8/31/2027	10.4%
Continuing Period	10.4%
Price per share Forecast	
Base Year	\$51.69
8/31/2018	\$58.22
8/31/2019	\$64.05
8/31/2020	\$70.20
8/31/2021	\$76.52
8/31/2022	\$83.06
8/31/2023	\$89.86
8/31/2024	\$96.90
8/31/2025	\$104.14
8/31/2026	\$111.52
8/31/2027	\$119.01
Continuing Period	\$119.01