



# FOOT LOCKER, INC. (FL)

## Closer to the GOAT

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CYPRUS VALUE INVESTOR CONF. OCT 4-5, 2021

JOHN ZOLIDIS

QUO VADIS CAPITAL, INC.

[JOHN.ZOLIDIS@QUOVADISCAPITAL.COM](mailto:JOHN.ZOLIDIS@QUOVADISCAPITAL.COM)



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## Presenter Experience with Foot Locker

- Have followed the company closely and the industry including key suppliers and competitors for nearly 20 years
- Have personally conducted multiple 100s of Foot Locker and competitor store visits in many U.S. markets and in multiple countries
- LONG FL was one of our best-ever recommendations in a previous sell-side role, rising ~400% from <\$11 to over \$50 from 2009 to 2014

## Intro: Foot Locker, Inc. (FL)

Foot Locker is a global retailer of athletic footwear, apparel and accessories, currently operating ~2,700 stores in 27 countries

- Estimated FY21 revenues of \$9.0B
- EBITDA margin: estimated near 14% for FY21 vs. 10-year average of 12.4%
- 2021E Capex ~\$260M (2.9% of sales).
- Balance Sheet: \$745M\* cash, \$10M in long-term debt. Has leases. We forecast a 2021 leverage ratio of 3.2x lease adj. debt to EBITDAR.
- FY21 Free cash flow estimated at \$485M (\$4.64 share, 9.4% yield);
- \$1.30 annual dividend (2.7% yield)
- Recent price \$47 (as of Oct 1, 2021), current market cap: \$5.2B.

\* After planned \$1.1B expenditures for acquisitions expected to close in the current quarter

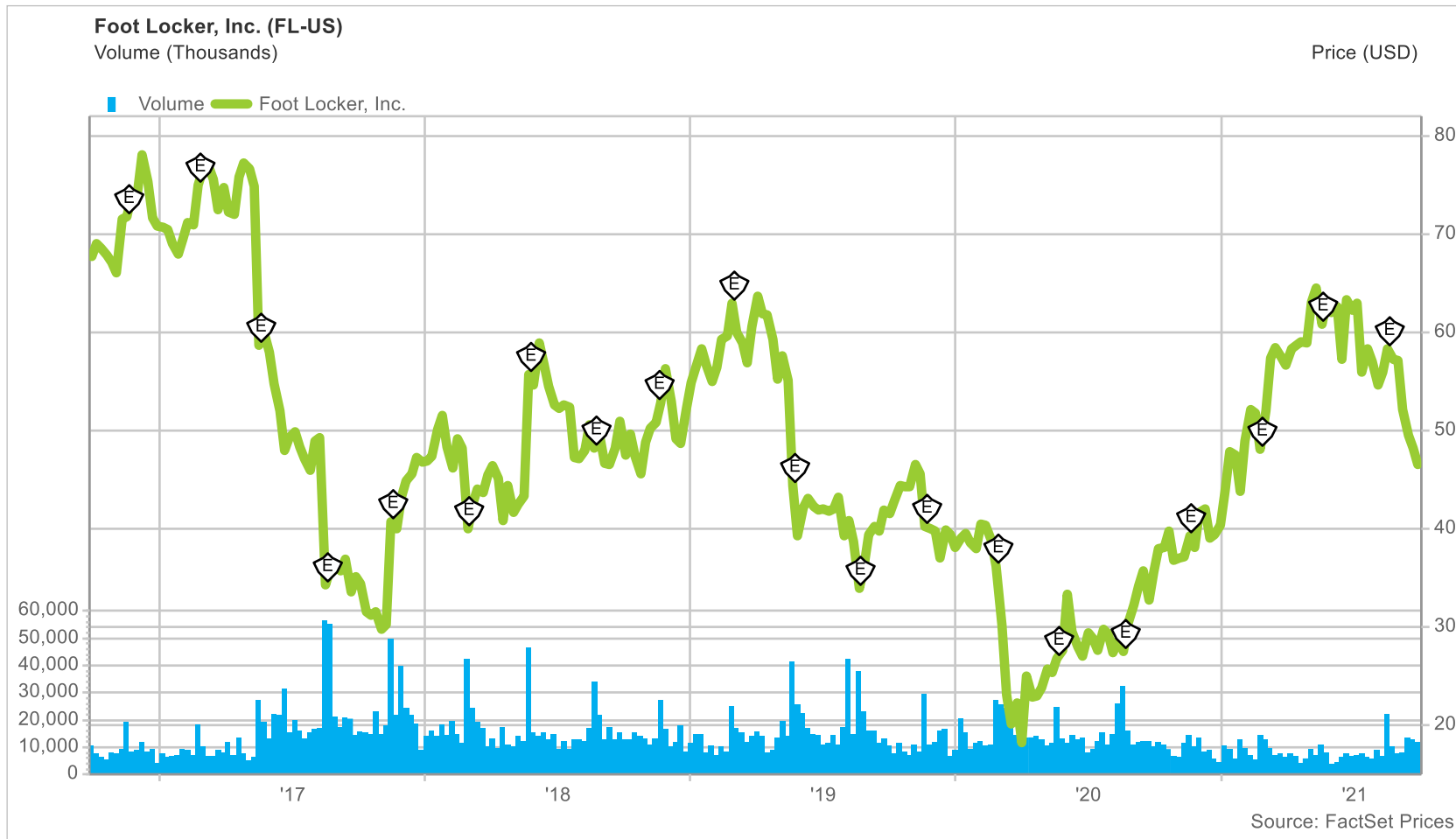
## Foot Locker, Inc. (FL) Select Data

- Banners operated include Foot Locker, Lady Foot Locker, Kids Foot Locker, Champs, Footaction, Sidestep, & Eastbay.
- Geographic distribution: ~27% of revs outside the U.S.
- Product distribution: 84% footwear, 12% apparel, 4% accessories
- Channel distribution: 22% DTC (online orders)
- Vendor concentration: 75% of all products purchased from Nike, Inc. (Nike, Brand Jordan, Converse) with 91% from five suppliers
- *Change in store count over the past five years -12%.*
- Loyalty program: FLX (launched Feb 2020) offers exclusive/ early access and free shipping (no program fee) and had 25M members recently



# Five Year Chart: >40% below All Time High of \$78

Added to Quo Vadis LONG idea list on 10/1/2020 @ \$33.03



# ***FOOT LOCKER IS NOT A CHAIN OF STORES SELLING SHOES***



***INSTEAD: FOOT LOCKER IS A MECHANISM FOR  
MONITIZING JORDANS VIA A CASH PAYING  
CUSTOMER***





## *Investment Thesis*

***Foot Locker should realize higher sales, margins and market share*** due to industry dynamics and Nike strategies. In contrast, the Street fears & FL shares are priced for “disintermediation.”

We expect upward revisions to Street estimates and valuation expansion ***with FL shares offering a potential double from current levels.***

# ***1. The Valuation***



## FL shares currently trade at 7x P/E on FY22E & 4x EV/ FY22E EBITDA

	VS. FY22 CONSENSUS ESTIMATES	VS. 10 YEAR HISTORICAL AVERAGE
EV to Sales	0.5x	0.6x
EV to EBITDA	3.7x	4.5x
P/E	6.9x	11.2x
EV TO FCF	5.9x	7.9x
DIV YIELD	2.6%	2.3%

Source: Quo Vadis Capital Estimates, FactSet, EV adjusted for pending acquisitions

***We think these multiples are pretty darn low***

# Lowest Multiple vs. Peer Group & Discount to Historical

## Quo Vadis Capital Select Retailers

### Relative Growth, Profitability, Balance Sheet & Valuation Metrics (Consensus Forecasts)

for  
reference

#### FOOTWEAR & SPORTING GOODS RETAILERS

10/4/2021	AVG.	DBI	SCVL	BOOT	ASO	DKS	FL	HIBB	BGFV	GCO	CAL	NKE
Recent Price	\$ 14.45	\$ 33.05	\$ 90.64	\$ 40.19	\$ 121.72	\$ 46.65	\$ 72.21	\$ 24.11	\$ 59.90	\$ 22.82	\$ 147.06	
Mkt Cap (\$B)	\$1.1	\$0.9	\$2.7	\$3.9	\$10.7	\$4.9	\$1.2	\$0.5	\$0.9	\$0.8	\$237.5	
ENT VALUE (\$B)*	\$1.3	\$0.8	\$2.7	\$4.5	\$8.9	\$4.2	\$1.0	\$0.4	\$1.3	\$1.1	\$233.4	
<b>Valuation Metrics*</b>												
Vs. 2019A EPS (P/E)	26.6	9.4	22.6	55.3	25.2	33.0	9.5	31.0	56.1	13.1	10.9	91.9
Vs. 2020A EPS (P/E)	24.9	NM	59.0	47.2	10.5	19.9	16.6	11.8	9.5	NM	NM	41.3
Vs. 2021E EPS (P/E)	9.3	12.9	7.4	21.9	6.6	9.3	6.5	6.3	5.7	10.2	6.7	34.5
Vs. 2022E EPS (P/E)	10.2	10.7	10.0	23.1	7.5	12.4	6.9	7.2	7.8	10.3	6.7	29.2
Vs. 2023E EPS (P/E)	9.5	8.9	8.6	20.2	6.9	11.0	6.6	7.1	NA	9.2	6.8	25.0
EV / 2022 Sales	0.7	0.4	0.7	2.2	0.7	0.8	0.5	0.6	0.4	0.5	0.4	4.4
EV / 2020A EBITDA	14.9	NM	19.1	24.8	4.8	8.6	6.7	6.1	4.5	28.1	31.7	37.9
EV / 2021E EBITDA	5.9	7.1	4.4	15.0	5.0	4.7	3.6	3.7	3.0	8.0	5.0	27.6
EV / 2022E EBITDA	5.9	5.5	5.1	13.2	5.6	5.7	3.7	4.1	3.7	7.8	4.9	23.9
EV / 2023E EBITDA	5.8	5.2	4.6	12.4	5.4	5.4	3.6	3.9	NA	7.3	4.7	21.0
Free Cash Flow Yield ( <u>'21</u> )	9.6%	0.0%	13.9%	5.3%	5.9%	9.2%	9.9%	NA	NA	12.2%	20.5%	2.2%
Dividend Yield	0.5%	0.0%	0.8%	0.0%	0.0%	1.9%	2.6%	0.0%	0.0%	0.0%	0.0%	0.8%
<b>EV/ NTM EBITDA 5-Year Valuation History*</b>												
HIGH	10.7	NM	13.6	17.0	6.4	8.3	8.0	7.6	8.1	7.3	19.8	34.1
LOW	2.3	NM	2.1	3.6	4.4	2.3	1.4	1.0	1.8	0.7	3.1	13.8
AVERAGE	5.6	2.1	6.2	10.3	5.6	5.7	5.0	4.8	4.8	4.6	6.7	21.7
<b>Current EV/ EBITDA on FY22 Compared to 5-Year Average*</b>												
% Premium or Discount	-1%	NM	-19%	28%	1%	-1%	-27%	-14%	-23%	69%	-26%	10%

Note: BOOT uses March FY; \* Our EV and other LT debt values **exclude** leases; FL EV adjusted for pending acquisitions

Source: FACTSET, Company Reports, Quo Vadis Capital, Inc. estimates



***Undeniable That FL is a Very Cheap Stock***

***So, by now you should suspect there is something  
VERY wrong...***

## ***2. What the Market has WRONG***

***Two areas:***

***1. The Market Thinks Nike is Planning a “Last Dance” with Foot Locker***

***2. We believe investors are underestimating the effects of rationalization in the industry and post Covid demand***

***Investors are also focused on current supply chain disruptions (due to Vietnam factory closings) & tough stimulus-check compares in 1QNY***

***But the market sees only the near-term challenge and not the long-term benefit***



In 2017, Nike announced a new strategy called  
“Consumer Direct Offense”

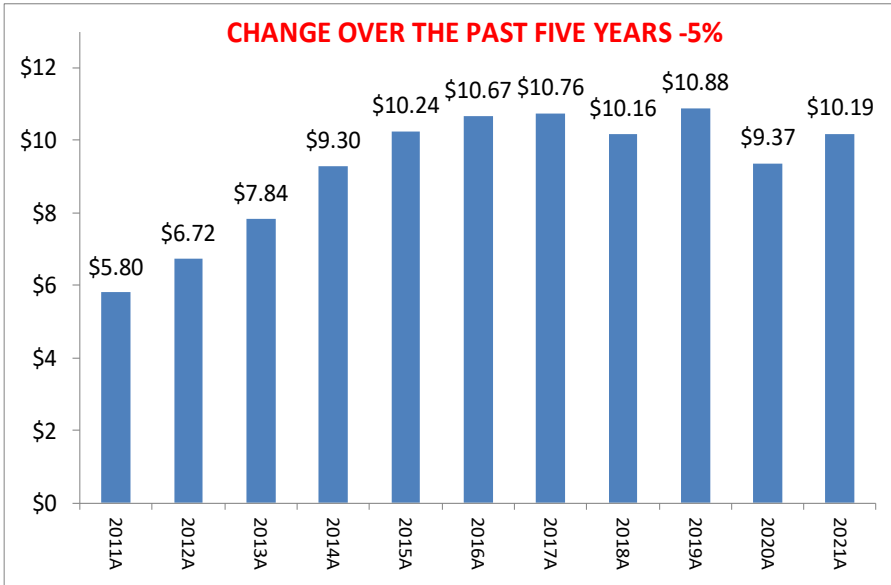
*Bears interpreted this strategy to mean that Nike plans a  
“Last Dance” with Foot Locker* and will pull product and  
demand more margin

\* NKE supplied 75% of FL’s 2020 product

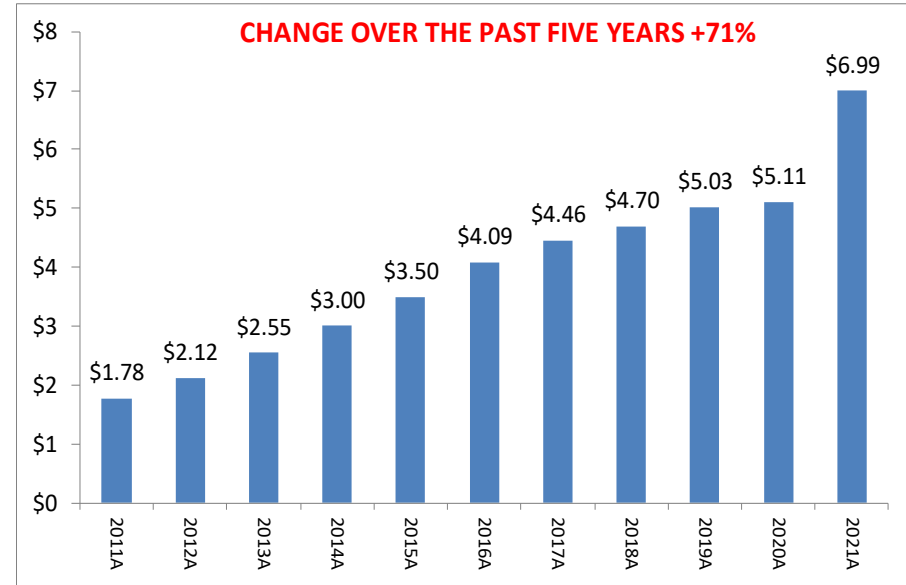
***Put differently: The bear case is that FL is a disintermediation candidate***

# What has happened? Over Five Years, Nike Shrank N.A. Wholesale 5% and Grew DTC 71%

NIKE ANNUAL SALES TO NORTH AMERICAN WHOLESALE CUSTOMERS \$B



NIKE ANNUAL NORTH AMERICAN DIRECT TO CONSUMER SALES \$B



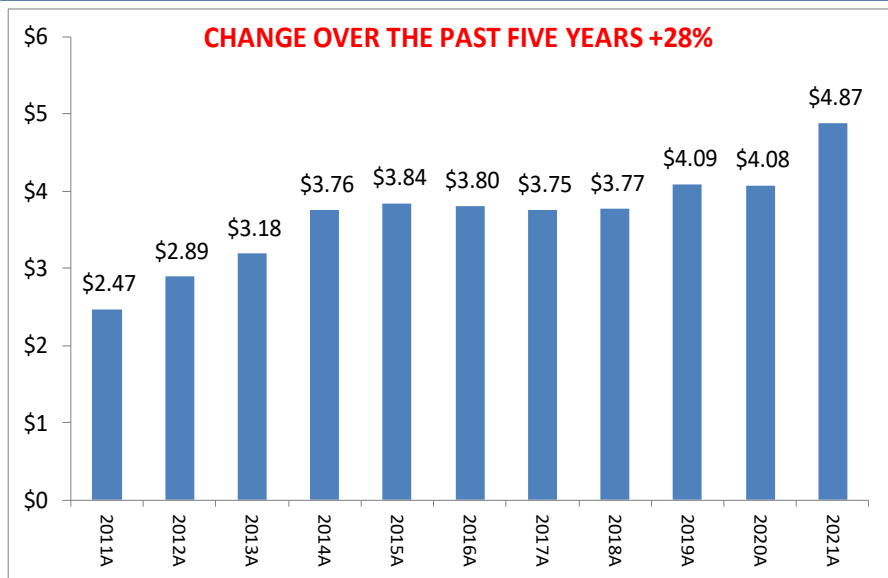
Source, Nike, Quo Vadis Capital, Inc. estimates

***Looks really bad for a Nike retail partner, right?  
The music for the last dance is playing!***

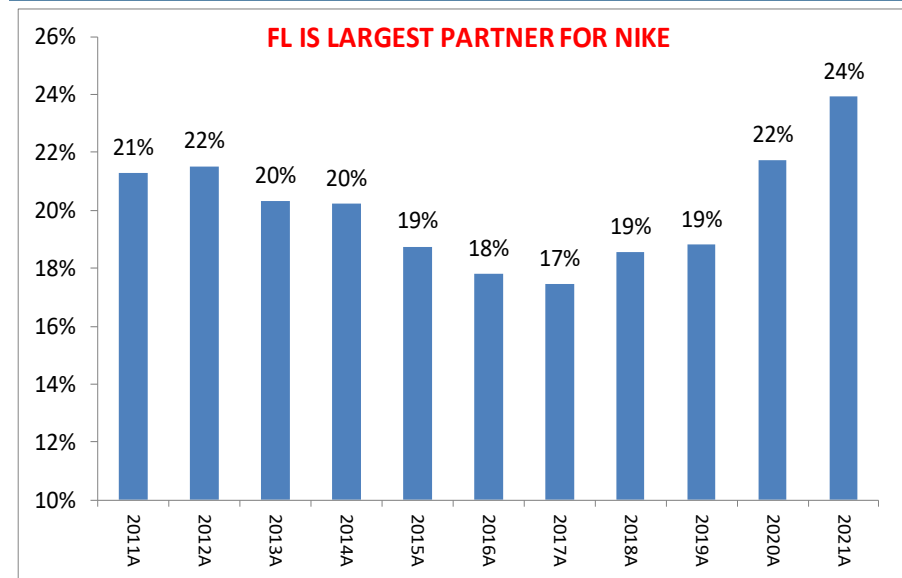
But Wait! Even as Nike Shrank N.A. Wholesale, **Foot Locker's relationship with NIKE has deepened, GROWING 28% over the past five years**



FL EST. NORTH AMERICAN ANNUAL RETAIL SALES OF NIKE PRODUCTS \$B



FL EST. SHARE OF NIKE NORTH AMERICAN WHOLESALE REVS



Source: Nike, Foot Locker, Quo Vadis Capital, Inc. estimates

## Further, *Nike Has Publicly Supported Foot Locker* on Many Occasions; Meanwhile...

Nike has cut off the following retailers altogether:

- DSW
  - Urban Outfitters
  - Shoe Show
  - Big Five Sporting Goods
  - Dunham's Sports
  - Olympia Sports
  - VIM
  - Perhaps 100s of small independent retailers
  - And ***EVEN AMAZON DOT COM*** *was canceled by NIKE*
- |              |
|--------------|
| Belks        |
| Dillard's    |
| Zappos       |
| Bob's Stores |
| Fred Meyer   |
| EbLens       |
| City Blue    |

## **But that's not all, plenty of Competitors Stopped Getting Nike in Virtue of No Longer Existing...**

**Former retailers of NKE goods that have closed permanently (year):**

- **The Sports Authority 2016**
- **Modell's 2020**
- **MC Sports 2017**
- **City Sports 2015**
- **Eastern Mountain Sports & Shorts Chalet 2017**
- **Numerous Department Store Chains & Independents together operating 1000s of doors**

## Current Supply Chain Problems *ARE HELPING*

[...over the last three years, we've actually exited about 50% of our undifferentiated accounts, [...]. And so we believe that we will continue down this strategy, [...], ***we believe that the supply-related reductions will likely trigger an even greater acceleration in the transformation of the marketplace towards NIKE and our most important wholesale partners.***]

***Nike CFO Matt Friend on 9/23/2021***



## Summing Up The Impact Nike Consumer Direct Offense

- Nike's interest is to raise its average selling prices and lower discounting (increase margin)
- Nike cut off retailers and eliminated 1000s of points of distribution
- Nike pulled its product from Amazon.
- Covid accelerated rationalization of the industry
- Foot Locker's business with Nike has grown
- Short-term supply chain issues will accelerate permanent shifts

There is no question in our opinion, that rather than disintermediation ***the outcome has been inverted is massively positive for Foot Locker***



***Supply of Nike is becoming concentrated in fewer retailers.***

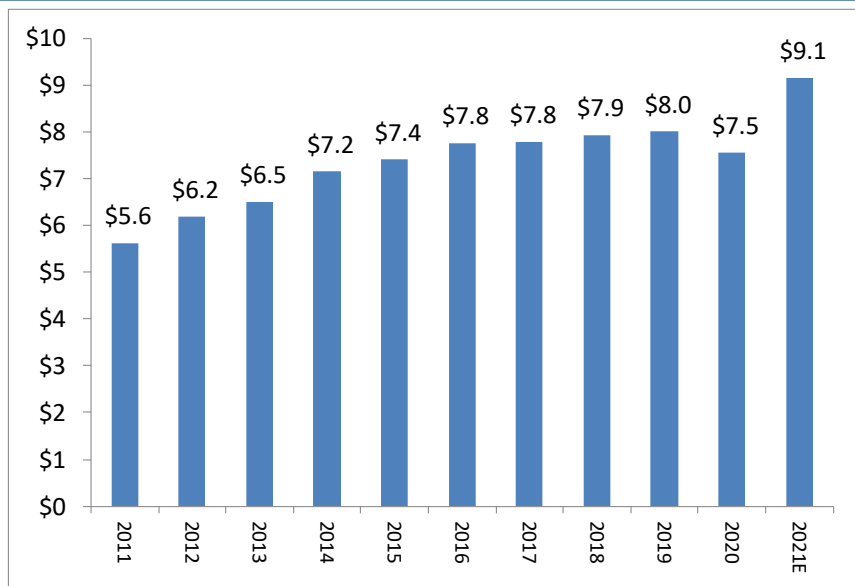
***What about demand?***

## Demand Side of the Equation is Also Very Positive

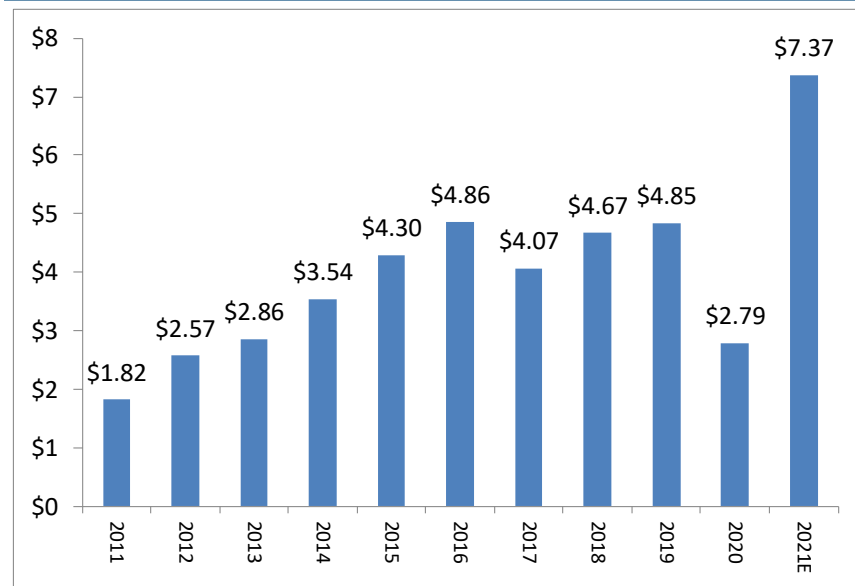
- **Consumer interest in fitness and athletic activity have been amplified by Covid**
- **Work/ School-from-home have accelerated casualization, which benefits comfortable athletic looks**
- **Foot Locker customer skews younger and less affluent and likely benefits from Child Tax Credit & other govt. transfer payments**

Given all this, it should be no surprise that **Foot Locker is on track in 2021 to report its highest revenues and profits in the history of the company**

ANNUAL REVENUES \$B



ANNUAL EPS



Source: Company Reports, Quo Vadis Capital, Inc. estimates



### ***3. The Catalyst***



## Analysts and Investors are Skeptical

- The Street is modeling FL as if FY21 sales and margin performance is a 1x Event (believe FL is overearning) (& this is how the stock is priced)

### Foot Locker, Inc.

#### Annual Earnings Model And Selected Financial Data

#### CONSENSUS FORECASTS

(\$ in Millions, Except per Share Data)

Fiscal Year Ends January

	Fiscal 2018A	Fiscal 2019A	Fiscal 2020A	Fiscal 2021E	Fiscal 2022E	Fiscal 2023E
<b>Total retail sales</b>	\$ 7,939.0	\$ 8,005.0	\$ 7,548.0	\$ 8,879.6	\$ 9,110.8	\$ 9,299.0
% change	2.0%	0.8%	-5.7%	10.9%	2.6%	2.1%
<b>EBITDA</b>	\$ 914.0	\$ 893.0	\$ 596.0	\$ 1,204.0	\$ 1,130.3	\$ 1,155.4
% change	-4.3%	-2.3%	-33.3%	34.8%	6.1%	2.2%
<b>EBITDA MARGIN</b>	11.5%	11.2%	7.9%	13.6%	12.4%	12.4%
<b>Diluted EPS</b>	\$4.67	\$4.85	\$2.79	\$ 7.16	\$ 6.78	\$ 7.10
% change	14.7%	3.8%	-42.4%	47.7%	-5.3%	4.7%
<b>% Δ in same-store sales</b>	2.9%	2.3%	-0.2%	18.0%	-0.8%	1.8%
<b>Free cash flow per share</b>	\$5.12	\$4.66	\$8.60	\$3.48	\$6.53	\$6.48

Source: Company data, FACTSET, Quo Vadis Capital, Inc. estimates (1) 53 week year



# We see nearly \$8 in EPS & FCF/ Share by FY23

➤ Assuming continued demand and a structurally more profitable industry

Foot Locker, Inc.						
Annual Earnings Model And Selected Financial Data						
QUO VADIS CAPITAL, INC. ESTIMATES						
(\$ in Millions, Except per Share Data)						
Fiscal Year Ends January						
	Fiscal 2018A	Fiscal 2019A	Fiscal 2020A	Fiscal 2021E	Fiscal 2022E	Fiscal 2023E
<b>Total retail sales</b>	\$ 7,939.0	\$ 8,005.0	\$ 7,548.0	\$ 8,897.8	\$ 9,507.3	\$ 9,729.7
% change	2.0%	0.8%	-5.7%	17.9%	6.8%	2.3%
<b>EBITDA</b>	\$ 914.0	\$ 893.0	\$ 596.0	\$ 1,240.6	\$ 1,224.4	\$ 1,292.1
% change	-4.3%	-2.3%	-33.3%	108.2%	-1.3%	5.5%
<b>EBITDA MARGIN</b>	11.5%	11.2%	7.9%	13.9%	12.9%	13.3%
<b>Diluted EPS</b>	\$4.67	\$4.85	\$2.79	\$7.14	\$7.24	\$7.98
% change	14.7%	3.8%	-42.4%	155.9%	1.4%	10.2%
<b>% Δ in same-store sales</b>	2.9%	2.3%	-0.2%	21.3%	1.3%	3.4%
<b>Free cash flow per share</b>	\$5.12	\$4.66	\$8.60	\$4.64	\$6.95	\$7.69

Source: Company data, Quo Vadis Capital, Inc. estimates <sup>(1)</sup> 53 week year



*If we are right on sustainability of demand,  
together with higher selling prices and margins*

*We expect upward revisions to Street estimates to  
drive multiple expansion*

*At a P/E of ONLY 10x\*, FL shares could rise to >\$80,  
nearly doubling*

*This likely underestimates true upside*

*\*This is below FL's five year average NTM P/E of 10.6x*



## ***4. The Other Considerations & Ways to Win***



## Investment in GOAT

- Foot Locker made a strategic minority investment in online sneaker reseller GOAT in 2019 for \$100M.
- GOAT recently conducted (in June) a series F fundraising valuing the total business at \$3.7B.
- Foot Locker's stake is now listed at \$728M (\$7 share) and is listed on the balance sheet.
- This could be distributed to shareholders or monetized.
- We have not considered the GOAT stake in any of our valuation work.

## Estimated P&L for Recent Deals

- Foot Locker recently announced the acquisitions of WWS and atmos for \$1.1B. Guidance is for accretion of \$0.44-\$0.48 per share in FY22.
- FL shares are trading lower since deals were announced Aug 1, suggesting the market is ascribing no value to these assets.
- Yet we estimate ~\$100M of EBITDA by FY23

	FY20A	FY21E	FY22E	FY23E
WWS & ATMOS	\$425M \$170M			
<b>Revs Both deals</b>	<b>\$595M</b>	<b>\$714M</b>	<b>\$821M</b>	<b>\$931M</b>
<i>% change</i>		20%	15%	13%
EBITDA <i>margin</i>			\$80M 10%	\$102M 11%
<b>EPS to FL</b>		<b>\$0.20 (4QFY21)</b>	<b>\$0.44-\$0.48</b>	<b>\$0.61</b>

Source: Company reports and Quo Vadis Capital, Inc. estimates



## Could FL be acquired by Nike?\*

- Nike could acquire Foot Locker to accelerate its Consumer Direct Offense
- NKE market cap is \$240B. FL market cap is \$5B. NKE had \$14B in cash and \$11B in LT & ST debt at the end of August.
- Even in a scenario where NKE paid nearly a 100% premium or \$8.3B (our \$80 target) *and* lost ½ of FL's non-Nike business, we still estimate this deal would add materially to NKE pre-tax income
- A deal in NKE shares or a combination of stock and cash would also be possible and immediately very accretive

*\* We have no knowledge of any talks between these two companies nor have we discussed this idea with either company. Also, perhaps the best argument against this idea is the fact that it hasn't already happened.*

## *Conclusions*

- **Foot Locker is a very cheap stock**
- **The environment has changed in a very favorable way for the company**
- **Revenues and earnings will reach all-time highs this year**
- **However, analysts and investors believe this is due to temporary factors**
- **We believe higher profits and earnings are structural and durable & ultimately aided by supply chain issues**
- **We see upward revisions and potential for multiple expansion**
- **Potential @10x P/E = \$80 representing nearly a double**



## Risks and Other Considerations

Foot Locker (FL) is a global retailer of athletic footwear, apparel and accessories.

- On a near-term basis, supply chain disruptions related to ocean freight and Covid19 will impact results.
- A majority of Foot Locker stores are located in shopping malls, which are experiencing long term secular declines in traffic.
- One vendor (Nike) accounts of 75% of sales (via three brands) if this vendor fails to produce desirable product or its brand becomes damaged it would be difficult for FL to pivot and replace this business.
- FL faces competition from online-only retailers and brands selling directly to customers.
- FL is exposed to labor rate inflation.
- The company is exposed to economic factors that impact consumer spending.

## Presenter Bio – John Zolidis

- **Founded Quo Vadis Capital, an equity research consultancy and Registered Investment Advisor (RIA) in 2017**
- **Analyst following U.S. consumer sector since 1999**
- **Named to Wall Street Journal's Best on the Street list in 2005**
- **Education at Kenyon College & University of Oxford (Mansfield College)**
- **Former PhD candidate in Philosophy**
- **Presenter at value investment conferences in Klosters, Vail & Cyprus**
- **Based mostly in Paris, France**

**More at [quovadiscapital.com](http://quovadiscapital.com)**

## Quo Vadis Capital, Inc. Stock Selection Process

- Our focus is on consumer sector, and we specialize in companies which can be analyzed by estimating and segmenting **unit economics**
- We solve for ROIC and **Return on Incremental Invested Capital (ROIIC)** at the unit and corporate level
- In LONGS we look for companies with upside to consensus estimates, a high ROIC and/or a rising trend in ROIC, rising margins, or accelerating growth and attractive valuations
- In SHORTS we look for companies with downside to consensus forecasts, weak ROIC or deteriorating trend in ROIC, margin contraction, decelerating growth and unattractive valuations
- OUR FAVORITE INVESTMENT THEME is finding a company **where the next dollar to be invested in the business has a significantly different return profile than the base business**. In other words, return on incremental investment is materially greater or lower than return on overall investment (ROIIC is > or < ROIC)

## Previous ideas from Value Investment Conferences

CALL	COMPANY	SYMBOL	EVENT	DATE	PRICE	1 YEAR LATER	PRICE	12M % CHANGE
LONG	SPROUTS FMRS MKT	SFM	KLOSTERS	1/29/2020	\$ 15.71	2/29/2020	\$ 20.95	33%
SHORT	SHAKE SHACK	SHAK	CYPRUS	9/23/2019	\$ 102.89	9/24/2020	\$ 65.75	-36%
LONG	YUM CHINA	YUMC	VAIL	6/14/2019	\$ 41.16	6/13/2020	\$ 49.25	20%
LONG	BRINKER	EAT	KLOSTERS	1/29/2019	\$ 42.36	1/29/2020	\$ 44.57	5%
LONG	DOLLAR TREE	DLTR	CYPRUS	10/4/2018	\$ 81.11	10/4/2019	\$ 115.73	43%
LONG	STARBUCKS	SBUX	VAIL	6/28/2018	\$ 48.54	6/28/2019	\$ 83.83	73%
LONG	DSW, INC.	DSW	CYPRUS	10/3/2017	\$ 21.32	10/3/2018	\$ 33.30	56%

\*Source: FactSet, Excludes dividends



# Disclosures

## General Disclosures:

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