



Foot Locker Inc. (FL)

Updated May 27th, 2019 by Josh Arnold

Key Metrics

Current Price:	\$44	5 Year CAGR Estimate:	17.8%	Volatility Percentile:	96.8%
Fair Value Price:	\$66	5 Year Growth Estimate:	6.0%	Momentum Percentile:	41.4%
% Fair Value:	67%	5 Year Valuation Multiple Estimate:	8.4%	Growth Percentile:	52.1%
Dividend Yield:	3.4%	5 Year Price Target	\$89	Valuation Percentile:	95.4%
Dividend Risk Score:	B	Retirement Suitability Score:	B	Total Return Percentile:	93.9%

Overview & Current Events

Foot Locker was established in 1974 as part of the FW Woolworth Company, and became independent in 1988. The company has outlived its former parent, which closed in 1997. The athletic apparel retailer, known for its namesake Foot Locker brand, operates more than 3,200 stores in 27 countries. Foot Locker is a \$5 billion market capitalization company that should generate more than \$8 billion in revenue this year.

Foot Locker reported Q1 earnings on 5/24/19 and results sent the stock 16% lower on the day. Revenue and earnings came in slightly weaker than expected, but we see the move in the stock as overblown.

Comparable sales came in at +4.6% in Q1, which is a very strong performance. Total sales were up 2.6% thanks to a lower store count and foreign exchange headwinds. Indeed, on a currency-neutral basis, revenue would have risen 4.7% in Q1. Regardless, we see Foot Locker's Q1 revenue performance as largely positive.

Gross margins came in a 33.2% of revenue, a 30bps gain from the prior year's comparable period. SG&A costs deleveraged 100bps, however, to 20% of revenue, bringing the company's operating margin rate down to 12.2% of revenue in Q1. The deterioration of SG&A costs was due to planned strategic investments in the company's digital fulfillment capabilities.

The company's share count, thanks to its ever-present buyback, was down to 113 million from 119 million year-over-year. This helped salvage earnings-per-share growth despite essentially flat operating earnings during the quarter, with the former rising from \$1.38 to \$1.52.

Foot Locker updated its guidance for this year to a high-single digit gain in earnings-per-share; we've therefore updated our estimate to \$5.10 per share for this year, representing an 8% increase over last year's \$4.71.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$0.54	\$1.10	\$1.80	\$2.58	\$2.89	\$3.61	\$3.84	\$4.82	\$3.99	\$4.71	\$5.10	\$6.82
DPS	\$0.60	\$0.60	\$0.66	\$0.71	\$0.78	\$0.88	\$1.00	\$1.10	\$1.24	\$1.38	\$1.52	\$2.08
Shares	157	155	152	150	146	140	137	132	120	116	113	95

During the last recession, Foot Locker's earnings dipped ~20%, but since then they have sharply rebounded. Indeed, from 2008 through 2018 the company has been able to increase earnings-per-share by over 20% annually. However, this was during a time when Foot Locker's net profit margin improved from ~2% to ~7% and the share count was reduced by 25% as well. Moving forward we are more cautious, albeit still optimistic, on the firm's growth prospects.

Share repurchases ought to continue to aid in bottom line growth, but we do not believe margins will expand at a rate anywhere near what was accomplished in the last decade. This was supported again by Q1 results and indeed, 2019 guidance, as management believes a lower share count will be responsible for the majority (or all) of projected earnings-per-share growth this year.

Meanwhile, the dividend remains an important component due to its propensity to grow over time. While the current yield is reasonable, income investors stand to collect meaningfully higher payouts if earnings continue to grow. The recent selloff in the stock has the yield a full percentage point higher than our last update at 3.4%.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



Foot Locker Inc. (FL)

Updated May 27th, 2019 by Josh Arnold

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	19.6	13.7	12.1	12.6	12.3	14.0	16.9	13.4	13.0	11.3	8.7	13.0
Avg. Yld.	5.7%	4.0%	3.0%	2.2%	2.2%	1.7%	1.5%	1.7%	2.4%	2.6%	3.4%	2.3%

Over the past decade, shares of Foot Locker have traded hands with an average P/E ratio of about 14 times earnings. Given the reaction of investors to the Q1 report, we've lowered our fair value estimate from 14 times earnings to 13, but that still represents enormous upside to the current trough valuation of just 8.7 times this year's earnings. As such, we see a massive 8.4% tailwind to total returns from a higher valuation in the coming years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	111%	54%	36%	27%	28%	24%	26%	23%	31%	29%	30%	31%

Foot Locker's competitive advantage is in its valuable brand names, its decades of experience in athletic apparel retailing and its enormous scale. Moreover, Foot Locker's balance sheet affords the company financial stability that others crave during a recession.

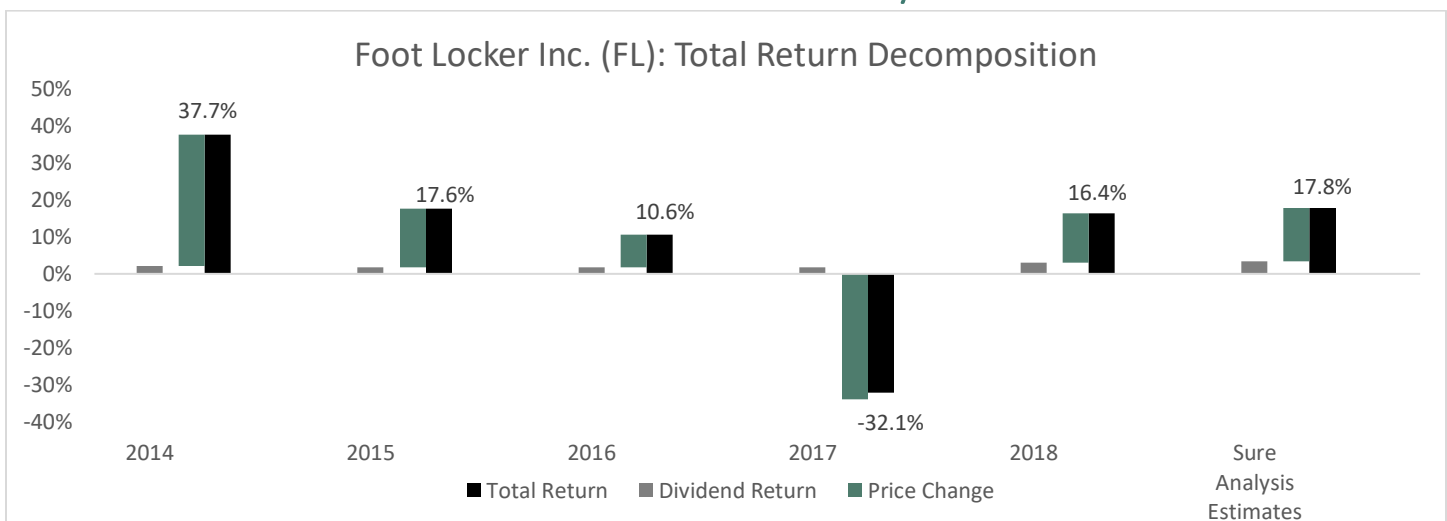
This does not mean that earnings power will not deteriorate in lesser times. During the last recession Foot Locker posted earnings-per-share of \$0.67, \$0.54 and \$1.10 through the 2008 to 2010 stretch, while the dividend was held steady. However, it does give a fair indication of the company's ability to withstand tougher times and bounce back.

The company's payout ratio has been reduced significantly since the last recession and stands at less than a third of earnings. This sets up well for faster dividend growth, a robust share repurchase program, or both in the years to come.

Final Thoughts & Recommendation

After a declining share price since our last update, Foot Locker now stands to produce outstanding total returns in the coming years. We are forecasting 17.8% annual returns consisting of the 3.4% yield, 6% earnings growth, and an 8.4% tailwind from a rising valuation. As such, we see the security as suitable for value investors, those seeking a safe yield for income, and those looking for moderate rates of growth. We think the stock has been unfairly punished after the Q1 report, and rate it a buy.

Total Return Breakdown by Year



[Click here to rate and review this research report. Your feedback is important to us.](#)

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



Foot Locker Inc. (FL)

Updated May 27th, 2019 by Josh Arnold

Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	5237	4854	5049	5623	6182	6505	7151	7412	7766	7782
Gross Profit	1460	1332	1516	1796	2034	2133	2374	2505	2636	2456
Gross Margin	27.9%	27.4%	30.0%	31.9%	32.9%	32.8%	33.2%	33.8%	33.9%	31.6%
SG&A Exp.	1174	1099	1138	1244	1294	1334	1426	1415	1472	1501
D&A Exp.	130	112	106	110	118	133	139	148	158	173
Operating Profit	156	121	272	442	622	666	809	942	1006	782
Operating Margin	3.0%	2.5%	5.4%	7.9%	10.1%	10.2%	11.3%	12.7%	13.0%	10.0%
Net Profit	-80	48	169	278	397	429	520	541	664	284
Net Margin	-1.5%	1.0%	3.3%	4.9%	6.4%	6.6%	7.3%	7.3%	8.6%	3.6%
Free Cash Flow	237	257	229	345	253	324	522	563	578	539
Income Tax	-21	26	88	157	210	234	289	296	340	294

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	2877	2816	2896	3050	3367	3487	3577	3775	3840	3961
Cash & Equivalents	385	582	696	851	880	858	967	1021	1046	849
Accounts Receivable	53	N/A	41	49	68	99	78	94	101	106
Inventories	1120	1037	1059	1069	1167	1220	1250	1285	1307	1278
Goodwill & Int. Ass.	257	244	217	198	185	230	206	201	197	206
Total Liabilities	953	868	871	940	990	991	1081	1222	1130	1442
Accounts Payable	187	215	223	240	298	263	301	279	249	258
Long-Term Debt	142	138	137	135	133	136	132	129	127	125
Shareholder's Equity	1924	1948	2025	2110	2377	2496	2496	2553	2710	2519
D/E Ratio	0.07	0.07	0.07	0.06	0.06	0.05	0.05	0.05	0.05	0.05

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	-2.6%	1.7%	5.9%	9.4%	12.4%	12.5%	14.7%	14.7%	17.4%	7.3%
Return on Equity	-3.8%	2.5%	8.5%	13.4%	17.7%	17.6%	20.8%	21.4%	25.2%	10.9%
ROIC	-3.5%	2.3%	8.0%	12.6%	16.7%	16.7%	19.8%	20.4%	24.1%	10.4%
Shares Out.	157	155	152	150	146	140	137	132	120	116
Revenue/Share	34.01	31.06	32.22	36.42	40.14	43.22	48.98	52.64	57.48	60.84
FCF/Share	1.54	1.64	1.46	2.23	1.64	2.15	3.58	4.00	4.28	4.21

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

Disclaimer

Nothing presented herein is, or is intended to constitute, specific investment advice. Nothing in this research report should be construed as a recommendation to follow any investment strategy or allocation. Any forward-looking statements or forecasts are based on assumptions and actual results are expected to vary from any such statements or forecasts. No reliance should be placed on any such statements or forecasts when making any investment decision. While Sure Dividend has used reasonable efforts to obtain information from reliable sources, we make no representations or warranties as to the accuracy, reliability or completeness of third-party information presented herein. No guarantee of investment performance is being provided and no inference to the contrary should be made. There is a risk of loss from an investment in marketable securities. Past performance is not a guarantee of future performance.