



Foot Locker Inc. (FL)

Updated December 7th, 2020 by Josh Arnold

Key Metrics

Current Price:	\$42	5 Year CAGR Estimate:	3.4%	Market Cap:	\$4.4 B
Fair Value Price:	\$40	5 Year Growth Estimate:	3.0%	Ex-Dividend Date:	01/15/21 ¹
% Fair Value:	105%	5 Year Valuation Multiple Estimate:	-1.0%	Dividend Payment Date:	01/31/21 ²
Dividend Yield:	1.4%	5 Year Price Target	\$46	Years Of Dividend Growth:	0
Dividend Risk Score:	C	Retirement Suitability Score:	D	Last Dividend Increase:	N/A

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 3,000 stores in 27 countries. Foot Locker is a \$4.4 billion market capitalization company that should generate about \$7.6 billion in revenue this year.

Foot Locker reported third quarter earnings on November 20th, 2020 and results easily beat expectations on both the top and bottom lines. Revenue was up more than 9% year-over-year to \$2.1 billion, beating estimates by \$160 million. Comparable sales were responsible for most of the gain, coming in at +7.7%, above expectations of a decline of -1.2%. Gross margins were down 120bps to 28.7% of revenue, while operating margin was 8.5% of sales, up from 4.6% in the same period a year ago. SG&A expenses declined 120bps to 20.1% of sales, helping to boost operating margins. Adjusted earnings-per-share came to \$1.21, up from \$1.13 in the same period a year ago, helped along by higher revenue and better margins. Foot Locker ended the quarter with 3,032 stores, down from 3,129 at the beginning of the year. The company opened 27 new stores in Q3, but closed 95 stores, 70 of which were Runners Point stores.

We have raised our estimate of earnings-per-share for this year to \$2.55 after much better Q3 results than expected, but note that even with this raise, Foot Locker is nowhere near normalized earnings. We continue to use \$4 as our estimate of earnings power per share.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$1.10	\$1.80	\$2.58	\$2.89	\$3.61	\$3.84	\$4.82	\$3.99	\$4.71	\$4.93	\$2.55	\$4.64
DPS	\$0.60	\$0.66	\$0.71	\$0.78	\$0.88	\$1.00	\$1.10	\$1.24	\$1.38	\$1.49	\$0.60	\$0.70
Shares³	155	152	150	146	140	137	132	120	113	105	98	80

During the last recession, Foot Locker's earnings dipped ~20%, but since then they had sharply rebounded. From 2008 through 2018 the company was 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%. Moving forward we are more cautious, albeit still optimistic, on the firm's growth prospects. We note growth in 2019 was much slower, and of course, will be negative for 2020.

Share repurchases were restarted in Q3, so we see the stock as having that tailwind once again moving forward.

We're moving our growth estimate to 3% annually from our earnings power base as the coronavirus has introduced more risks, but Foot Locker is responding well to them. The company has rationalized its store base, which should help margins, and comparable sales have been very strong. The once-attractive yield is now much less so given the lower payout, equating to just 1.4% at today's price.

¹ Estimated date

² Estimated date

³ Share count in millions

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.



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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	13.7	12.1	12.6	12.3	14.0	16.9	13.4	13.0	11.3	9.7	10.5	10.0
Avg. Yld.	4.0%	3.0%	2.2%	2.2%	1.7%	1.5%	1.7%	2.4%	2.6%	3.1%	1.4%	1.5%

Over the past decade, shares of Foot Locker have traded hands with an average P/E ratio of about 14 times earnings. The valuation has soared from our last report, but stands at just 10.5 times earnings power today. We've boosted our fair value estimate to 10 times earnings, and as such, we see a small headwind to total returns from a lower valuation in the coming years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	54%	36%	27%	28%	24%	26%	23%	31%	29%	30%	15%	15%

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.

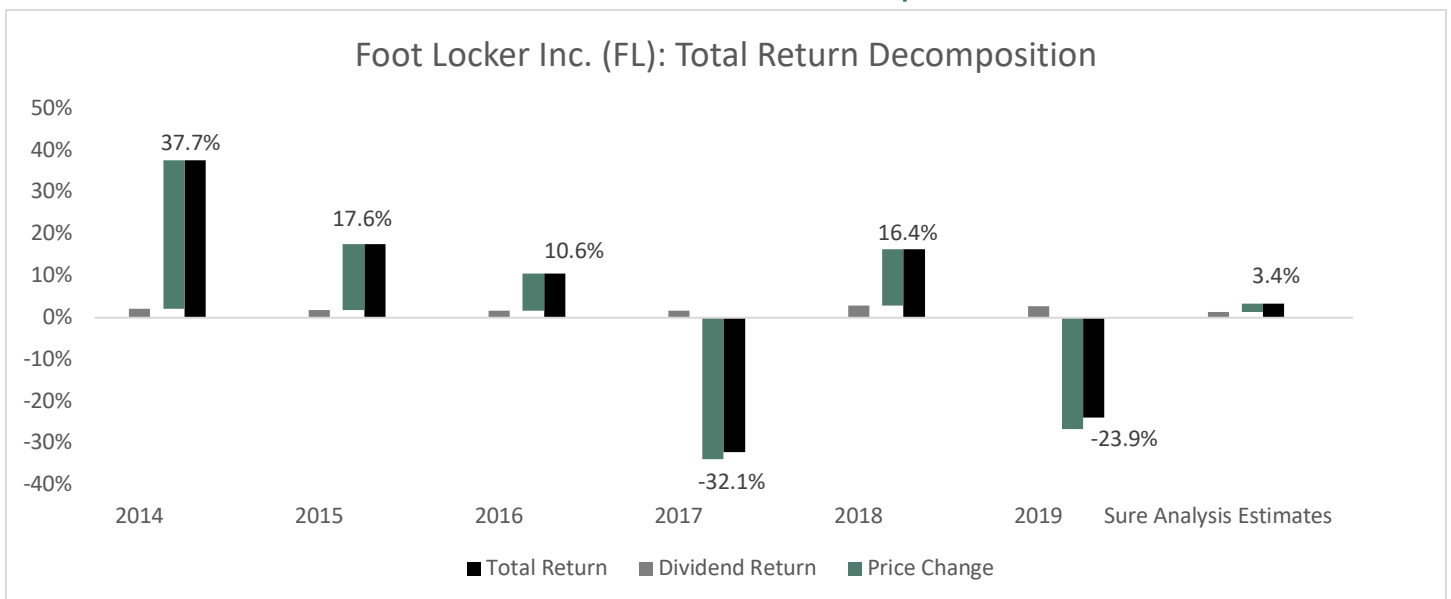
This does not mean that earnings power will not deteriorate in tougher times. During the last recession, Foot Locker posted earnings-per-share of \$0.67, \$0.54 and \$1.10 through the 2008 to 2010 stretch, while the dividend was held steady. This gives a fair indication of the company's ability to withstand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

The new dividend is quite low relative to earnings, so the payout should be safe for the foreseeable future. We also see the resumption of share repurchases as a vote of confidence from management.

Final Thoughts & Recommendation

We are more positive on Foot Locker's fundamentals and outlook after Q3 results, but see the share price as pricing in much of that already. With the yield quite low and the valuation ahead of our estimate of fair value, we rate Foot Locker a sell given poor total return prospects of just 3.4% per year.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	5,049	5,623	6,182	6,505	7,151	7,412	7,766	7,782	7,939	8,005
Gross Profit	1,516	1,796	2,034	2,133	2,374	2,505	2,636	2,456	2,528	2,543
Gross Margin	30.0%	31.9%	32.9%	32.8%	33.2%	33.8%	33.9%	31.6%	31.8%	31.8%
SG&A Exp.	1,138	1,244	1,294	1,334	1,426	1,415	1,472	1,501	1,614	1,650
D&A Exp.	106	110	118	133	139	148	158	173	178	179
Operating Profit	272	442	622	666	809	942	1,006	782	736	714
Operating Margin	5.4%	7.9%	10.1%	10.2%	11.3%	12.7%	13.0%	10.0%	9.3%	8.9%
Net Profit	169	278	397	429	520	541	664	284	541	498
Net Margin	3.3%	4.9%	6.4%	6.6%	7.3%	7.3%	8.6%	3.6%	6.8%	6.2%
Free Cash Flow	229	345	253	324	522	563	578	539	594	509
Income Tax	88	157	210	234	289	296	340	294	172	184

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	2,896	3,050	3,367	3,487	3,577	3,775	3,840	3,961	3,820	6,599
Cash & Equivalents	696	851	880	858	967	1,021	1,046	849	891	907
Accounts Receivable	41	49	68	99	78	94	101	106	87	100
Inventories	1,059	1,069	1,167	1,220	1,250	1,285	1,307	1,278	1,269	1,208
Goodwill & Int. Ass.	217	198	185	230	206	201	197	206	181	176
Total Liabilities	871	940	990	991	1,081	1,222	1,130	1,442	1,314	4,119
Accounts Payable	223	240	298	263	301	279	249	258	387	333
Long-Term Debt	137	135	133	136	132	129	127	125	124	122
Shareholder's Equity	2,025	2,110	2,377	2,496	2,496	2,553	2,710	2,519	2,506	2,480
D/E Ratio	0.07	0.06	0.06	0.05	0.05	0.05	0.05	0.05	0.05	0.05

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	5.9%	9.4%	12.4%	12.5%	14.7%	14.7%	17.4%	7.3%	13.9%	9.6%
Return on Equity	8.5%	13.4%	17.7%	17.6%	20.8%	21.4%	25.2%	10.9%	21.5%	20.0%
ROIC	8.0%	12.6%	16.7%	16.7%	19.8%	20.4%	24.1%	10.4%	20.5%	19.0%
Shares Out.	155	152	150	146	140	137	132	120	113	105
Revenue/Share	32.22	36.42	40.14	43.22	48.98	52.64	57.48	60.84	68.38	73.37
FCF/Share	1.46	2.23	1.64	2.15	3.58	4.00	4.28	4.21	5.12	4.67

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

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