Aug 26, 2020

Foot Locker(FL)

$29.66 (As of 08/25/20)

Price Target (6-12 Months): **$34.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 08/25/20) Prior Recommendation: Neutral	**Outperform**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**1-Strong Buy**
	Zacks Style Scores:	VGM:F
	Value: B | Growth: F | Momentum: F	

Summary

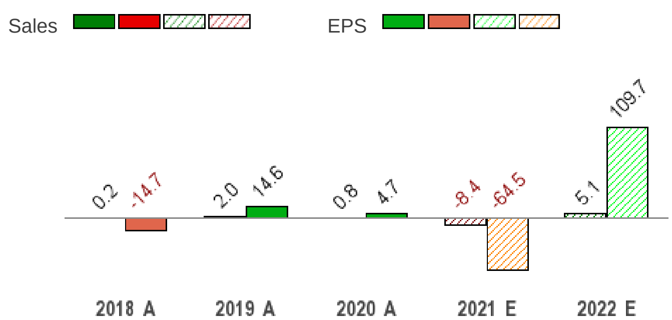
Although shares of Foot Locker have underperformed the industry over the past three months, this provides a good entry point given the stock's attractive valuation, sound fundamentals and encouraging second-quarter fiscal 2020 results. During the quarter the company witnessed huge response for its assortment as stores started reopening. This could be attributed to pent-up demand and the effect of the fiscal stimulus that supported in-store and digital channel sales. Notably, comps rose about 18% during the second quarter. Strong sales coupled with disciplined cost control aided the company to revert to positive earnings per share. Going ahead, management is on track with bolstering digital capabilities and supply chain efficiencies. Furthermore, the company reinstated quarterly dividend program on robust liquidity and a stable cash outlook.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	$47.86 - $17.46
20 Day Average Volume (sh)	4,460,713
Market Cap	$3.1 B
YTD Price Change	-23.9%
Beta	1.34
Dividend / Div Yld	$0.60 / 0.0%
Industry	Retail - Apparel and Shoes
Zacks Industry Rank	Bottom 10% (228 out of 252)
Last EPS Surprise	2.9%
Last Sales Surprise	0.2%
EPS F1 Est- 4 week change	147.3%
Expected Report Date	11/27/2020
Earnings ESP	0.0%
P/E TTM	10.6
P/E F1	17.0
PEG F1	1.6
P/S TTM	0.4

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2022	1,626 E	1,752 E	1,916 E	2,238 E	7,706 E
2021	1,176 A	2,077 A	1,879 E	2,220 E	7,329 E
2020	2,078 A	1,774 A	1,932 A	2,221 A	8,005 A

EPS Estimates

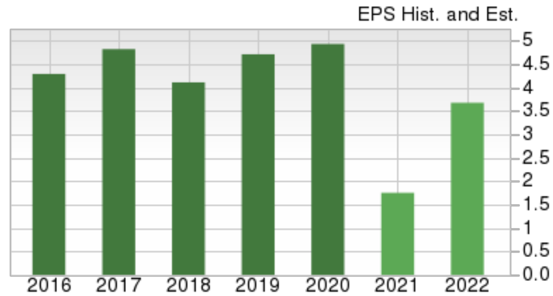
	Q1	Q2	Q3	Q4	Annual*
2022	$0.55 E	$0.62 E	$0.96 E	$1.49 E	$3.67 E
2021	-$0.67 A	$0.71 A	$0.51 E	$1.18 E	$1.75 E
2020	$1.53 A	$0.66 A	$1.13 A	$1.63 A	$4.93 A

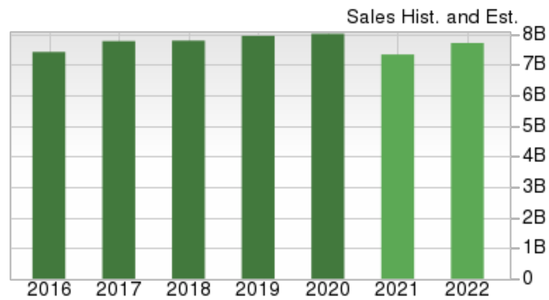
*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/25/2020. The reports text is as of 08/26/2020.

Overview

Founded in 1879 and headquartered in New York, Foot Locker, Inc. (FL) is a retailer of athletic shoes and apparel. The company operates websites and mobile apps, aligned with the brand names of store banners comprising footlocker.com, ladyfootlocker.com, six02.com, kidsfootlocker.com, champssports.com, footaction.com, footlocker.ca, footlocker.eu, footlocker.com.au, runnerspoint.com, sidestep-shoes.com, footlocker.hk, footlocker.sg, and footlocker.my.





Foot Locker has franchise operations in the Middle East. Moreover, in Germany, the franchised stores are operated under the banners of Runners Point.

As of Aug 1, 2020, the company operated 3,100 stores across 27 countries in North America, Europe, Asia, Australia and New Zealand. Apart from these, there are 134 franchised Foot Locker stores in the Middle East and four franchised Runners Point stores in Germany.

Beginning in 2018, the company has two operating segments, North America and International. Prior to 2018, the company had two reportable segments, Athletic Stores and Direct-to-Customers.

North America operating segment includes the results of the following banners operating in the U.S. and Canada: Foot Locker, Kids Foot Locker, Lady Foot Locker, Champs Sports, Footaction, and SIX:02, including each of their related e-commerce businesses, as well as Eastbay business that includes internet, catalog, and team sales.

International operating segment includes the results of the following banners operating in Europe, Asia, Australia, and New Zealand: Foot Locker, Runners Point, Sidestep, and Kids Foot Locker, including each of their related e-commerce businesses.

Reasons To Buy:

> We believe that continuous exploitation of opportunities such as kids' business, shop-in-shop expansion, store refurbishment and enhancement of assortments are likely to benefit the company.

▲ **A Good Entry Point, Q2 Metrics Encouraging:** Although shares of Foot Locker have inched-up 0.8% in the past three months, it has underperformed the industry's 21.7% rally. However, this provides an excellent opportunity for long-term investors, as it has cleared the deck for fresh buying given the stock's attractive valuation, sound fundamentals and encouraging second-quarter fiscal 2020 results. During the second quarter, the company's top and bottom lines outpaced the Zacks Consensus Estimate and grew year over year. While the company delivered an earnings beat after a miss in the previous quarter, it broke the five consecutive quarters of sales miss in the reported quarter. Also, total sales grew 17.1% year over year and 17.3% excluding the foreign-currency effects. Moreover, comparable-store sales jumped 18.6% during the quarter. Results benefited from the company's sturdy efforts along with its digital business. Management also highlighted the huge response to the company's assortment as stores started reopening. Furthermore, the company's board reinstated the quarterly dividend program on robust liquidity and more stable cash outlook.

Through the back-to-school period in the back half, the company remains optimistic about its efforts to offer a robust customer experience. Also, it looks well positioned to cash in on evolving customer shopping patterns with continued focus on digital and other strategic endeavors. Management did not update fiscal 2020 guidance on evolving pandemic-related uncertainties and its potential impact on the back-to-school season, team-sports participation and other government-stimulus packages.

▲ **Growth Catalyst:** Foot Locker is trying to improve its performance through its operational and financial initiatives. The company is effectively managing inventory, investing in digital platforms, improving supply chain efficiencies along with reorganizing corporate and division staff. Management believes that by continually exploiting opportunities like kids' and women's business, shop-in-shop expansion in collaboration with its vendors (such as House of Hoops, PUMA Labs, Jordan Flight 23 shops and The ARMOURY at Champs Sports), store banner.com business, store refurbishment and enhancement of assortments, Foot Locker is likely to benefit in the long run.

International expansion, especially in Europe, is another growth catalyst. Notably, the company deployed new websites in other nine European countries that built off the modernized platform rolled out in North America in the prior year. The company has been focusing on augmenting its e-commerce platform, growing direct-to-consumer (DTC) operations, margin expansion, tapping underpenetrated markets and opening of Power Stores. The company opened six Power Stores in fiscal 2019. The company has rolled out new membership program FLX that inspires customers to remain within the Foot Locker portfolio of banners. DTC channel strengthened and increased 173% during the second quarter of fiscal 2020. As a percent of sales, DTC rose to 33.2% of sales, up from 14.3% last year.

▲ **Restructuring Activities:** Management has decided to consolidate the Runners Point Group business into other operations in Europe in compliance with local legislation. As part of this plan, select Runners Point stores will be converted to either Sidestep or Foot Locker stores, and roughly 40 remaining Runners Point stores and certain Sidestep stores will be closed. In addition, the company plans to restructure and consolidate the Runners Point and Sidestep support and logistics functions into Foot Locker Europe's headquarters in the Netherlands in compliance with local legislation. This transition is likely to occur largely over the remainder of fiscal 2020. Also, the company expects to wind down the Runners Point business by the end of the year. The company plans to combine Champs Sports and Eastbay under a single leadership structure. As a part of this endeavor, the company plans to consolidate select Eastbay operations from Wausau, Wisconsin into the Champs Sports headquarters in Bradenton, Florida.

▲ **Strategic Partnership:** The company entered into a partnership with Nike for a pop-up store called Sneakeasy NYC and made a strategic investment of $15 million in Carbon38, which owns and operates an e-commerce destination for active and performance wear for women. The company also took minority interest in Goat, a managed marketplace for authentic sneakers, making an investment of $100 million. It invested $3 million in Super Heroic, a kid's footwear brand and $12.5 million in "Rockets of Awesome" a children's apparel company. The company also made a strategic investment of $3 million in NTWRK, a leading youth culture e-commerce and content platform. These investments widen the company's scope to expand products and brands, access new business segments and take advantage of innovative technologies.

▲ **Capital Allocation Plan:** Foot Locker remains committed toward strategic investments for achieving long term goals. The company's investments are directed toward community-based power stores in markets worldwide. It will continue focusing on digital advancement and enhancement of its U.S. supply chain. The company's digital endeavors comprise improvement of mobile and web platforms, implementation of new point-of-sale software worldwide, and expansion of data analytics capabilities. Apart from these, the company plans to spend a major portion of the capital on its fleet of stores, including revamping and remodeling of the same. Further, it is exploring off-mall retail formats opportunities and executing shop-in-shop spaces in collaboration with vendors. During second-quarter fiscal 2020, the company incurred capital expenditures of $31 million, funding the opening of 18 stores and remodeling or relocating of 26 stores. Management expects investing about $156 million in fiscal 2020. Meanwhile, the company is committed to boost shareholder value by reinstating its dividend program and lifting suspension on share repurchases.

▲ **Financial Flexibility:** Foot Locker's cash and cash equivalents at the end of second-quarter fiscal 2020 increased 35.7% sequentially to $1,373 million. Further, its long-term debt of $2,703 million (including long-term lease obligations) dipped 0.3% on a quarter-on-quarter basis. Also, at the end of the quarter, the company's debt-to-capitalization ratio was a respectable 0.53 compared with 0.74 for the industry. During fiscal second quarter, the company has repaid the $330 million earlier borrowed from its credit facility.

Risks

- **Gross Margin Under Pressure:** Foot Locker's gross margin continued to remain under pressure during the second quarter of fiscal 2020. The metric contracted 420 basis points (bps) to 25.9% in the reported quarter from 30.1% in the year-ago quarter. Moreover, merchandise margin rate decreased 700 bps, mainly owing to use of markdowns to clear aging-assortments and increased mix of DTC. With respect to gross margin, management forecasts a continued promotional environment. In addition, the company has been monitoring higher rates from its shipping partners, which are expected to increase freight costs in the back half of the fiscal.

  We note that in fiscal first quarter the metric remained under stress. Foot Locker's gross margin contracted significantly to 23% from 33.2% during the first quarter on account of deleverage of 850 basis points in occupancy and buyers' compensation expenses and 170 basis points decrease in merchandise margin.

- **Prone to Currency Fluctuations:** Foot Locker generates a significant amount of net sales outside the U.S. Due to high exposure to international markets, the company remains prone to currency fluctuations. The weakening of foreign currencies against the U.S. dollar may require the company to either raise prices or reduce profit margins in locations outside of the U.S. An increase in prices may have an adverse impact on the demand for Foot Locker's products.

- **Fashion Obsolescence a Threat:** Fashion obsolescence remains the main concern for Foot Locker's business model, which involves a sustained focus on product and design innovation. The company's pioneering position may be hurt by delays in its product launches. The company operates in the highly competitive athletic footwear and apparel segment. It faces stiff competition from athletic footwear specialty stores, sporting goods stores, department stores, discount stores and traditional shoe stores in terms of distinctiveness, innovativeness, quality and pricing, which may weigh on its results.

- **Dip in Consumer Sentiment May Impact Sales:** Any dip in consumer confidence – a key determinant of the economy's health – may have serious bearing on spending. The company's customers remain sensitive to macroeconomic factors including interest rate hikes, increase in fuel and energy costs, credit availability, unemployment levels, and high household debt levels, which may negatively impact their sentiment. This may adversely impact its growth and profitability.

Last Earnings Report

Foot Locker's Q2 Earnings Beat Estimates, Increase Y/Y

Quarter Ending	07/2020
Report Date	Aug 21, 2020
Sales Surprise	0.16%
EPS Surprise	2.90%
Quarterly EPS	0.71
Annual EPS (TTM)	2.80

Foot Locker came up with stellar second-quarter fiscal 2020 results, wherein the top and bottom lines outpaced the Zacks Consensus Estimate and grew year over year. Results benefited from the company's sturdy efforts along with the digital business. Management also highlighted the huge response to the company's assortment as stores started reopening. Furthermore, the company's board reinstated the quarterly dividend program on robust liquidity and more stable cash outlook.

However, management did not update fiscal 2020 guidance on evolving pandemic-related uncertainties and its potential impact on the back-to-school season, team-sports participation and other government-stimulus packages. Foot Locker had withdrawn its fiscal 2020 guidance in March. Nevertheless, the company believes that it is well poised to maneuver amid the coronavirus pandemic.

Q2 Details

The athletic-shoes and apparel retailer posted adjusted earnings of 71 cents per share and outshone the Zacks Consensus Estimate of 69 cents. The bottom line also rose 7.6% year over year.

On a GAAP basis, the company reported earnings of 43 cents a share compared with 55 cents recorded in the prior-year period.

Total sales of $2,077 million grew 17.1% year over year and slightly came above the consensus estimate of $2,074 million. Excluding the effect of foreign-currency fluctuations, total sales rose 17.3%. Moreover, comparable-store sales jumped 18.6% during the quarter, against a decline of 42.8% witnessed in the previous quarter.

Foot Locker's gross-margin rate contracted 420 basis points (bps) to 25.9% during the quarter. However, SG&A expense rate fell 360 bps to 18.6%.

Store Update

During the reported quarter, Foot Locker opened 18 outlets, remodeled or relocated 26 stores, and shuttered 31. As of Aug 1, 2020, the company operated 3,100 stores across 27 countries in North America, Europe, Asia, Australia and New Zealand. Apart from these, there are 134 franchised Foot Locker stores in the Middle East and four franchised Runners Point stores in Germany.

Other Financial Details

The company ended fiscal second quarter with cash and cash equivalents of $1,373 million, long-term debt of $121 million, and shareholders' equity of $2,403 million. The company has repaid the $330 million earlier borrowed from its credit facility. As of Aug 1, 2020, merchandise inventories were $1,194 million, down 2.7% from the prior-year period. On a constant-currency basis, inventory declined 3.7%.

As part of its cash-preservation actions, management did not pay dividend or buy back shares in the reported quarter. However, it announced a quarterly cash dividend of 15 cents per share, payable Oct 30, 2020 to shareholders of record as on Oct 16.

Recent News

Foot Locker Opens New Store in Singapore – Aug 17, 2020

Foot Locker has opened its largest store in Singapore, at Orchard Gateway @Emerald. The store showcases basketball culture, featuring multi-branded basketball collections and a half-court in B2.

Valuation

Foot Locker shares are down 23.9% year-to-date period and 16% over the trailing 12-month period. Stocks in the Zacks sub-industry are down 17% but the Zacks Retail-Wholesale sector is up 34.5% in the year-to-date period. Over the past year, the Zacks sub-industry is down 1.7% but the sector is up 45.9%.

The S&P 500 index is up 6.9% in the year-to-date period and 20.3% in the past year.

The stock is currently trading at 9.87X forward 12-month earnings, which compares to 40.93X for the Zacks sub-industry, 33.65X for the Zacks sector and 23.04X for the S&P 500 index.

Over the past five years, the stock has traded as high as 22.86X and as low as 3.63X, with a 5-year median of 11.26X. Our Outperform recommendation indicates that the stock will perform better than the market. Our $34 price target reflects 11.31X forward 12-month earnings.

The table below shows summary valuation data for FL

Valuation Multiples - FL

		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	9.87	40.93	33.65	23.04
	5-Year High	22.86	87.27	34.77	23.04
	5-Year Low	3.63	8.16	19.08	15.25
	5-Year Median	11.26	14.22	23.47	17.58
P/S F12M	Current	0.41	0.61	1.29	3.76
	5-Year High	1.38	1.09	1.29	3.76
	5-Year Low	0.24	0.32	0.82	2.53
	5-Year Median	0.76	0.8	0.97	3.05
EV/EBITDA TTM	Current	7.53	12.71	20.45	13.09
	5-Year High	9.51	12.71	20.45	13.09
	5-Year Low	3.02	4.71	10.68	8.25
	5-Year Median	6.83	6.64	12.97	10.92

As of 08/25/2020

Industry Analysis Zacks Industry Rank: Bottom 10% (228 out of 252)

Top Peers

Company (Ticker)	Rec	Rank
Tapestry, Inc. **(TPR)**	Outperform	1
American Eagle Outfitters, Inc. **(AEO)**	Neutral	4
AbercrombieFitch Company **(ANF)**	Neutral	4
Boot Barn Holdings, Inc. **(BOOT)**	Neutral	3
The Gap, Inc. **(GPS)**	Neutral	4
Levi StraussCo. **(LEVI)**	Neutral	3
Urban Outfitters, Inc. **(URBN)**	Neutral	3
Capri Holdings Limited **(CPRI)**	Underperform	5

Industry Comparison Industry: Retail - Apparel And Shoes

	FL	X Industry	S&P 500	ANF	LEVI	TPR
				Industry Peers		
Zacks Recommendation (Long Term)	Outperform	-	-	Neutral	Neutral	Outperform
Zacks Rank (Short Term)	1	-	-	4	3	1
VGM Score	F	-	-	F	F	F
Market Cap	3.09 B	573.00 M	23.77 B	667.72 M	5.02 B	4.13 B
# of Analysts	11	4	14	10	4	11
Dividend Yield	0.00%	0.00%	1.65%	0.00%	2.53%	0.00%
Value Score	B	-	-	D	B	B
Cash/Price	0.48	0.33	0.07	1.13	0.31	0.36
EV/EBITDA	5.19	6.72	13.35	5.66	7.37	-19.25
PEG Ratio	1.64	1.98	3.03	NA	NA	0.81
Price/Book (P/B)	1.29	1.40	3.17	0.84	4.31	1.81
Price/Cash Flow (P/CF)	4.33	4.36	12.81	3.07	9.43	7.94
P/E (F1)	16.95	30.62	21.72	NA	NA	8.12
Price/Sales (P/S)	0.42	0.41	2.47	0.20	1.00	0.83
Earnings Yield	5.90%	1.99%	4.45%	-26.94%	-1.89%	12.32%
Debt/Equity	1.12	1.05	0.75	1.78	1.29	1.49
Cash Flow ($/share)	6.86	1.88	6.93	3.53	1.34	1.88
Growth Score	F	-	-	F	F	F
Hist. EPS Growth (3-5 yrs)	-3.56%	-2.63%	10.41%	2.25%	NA	1.52%
Proj. EPS Growth (F1/F0)	-64.47%	-70.24%	-4.92%	-499.32%	-124.23%	89.78%
Curr. Cash Flow Growth	-1.10%	-1.10%	5.20%	-6.25%	29.04%	-48.91%
Hist. Cash Flow Growth (3-5 yrs)	1.64%	1.68%	8.50%	-5.89%	NA	-6.40%
Current Ratio	1.70	1.46	1.33	1.32	1.92	1.47
Debt/Capital	52.94%	55.28%	44.20%	63.97%	56.26%	59.81%
Net Margin	2.88%	-4.47%	10.25%	-5.50%	0.19%	-13.14%
Return on Equity	12.40%	2.47%	14.66%	-14.29%	13.47%	9.65%
Sales/Assets	1.10	1.07	0.51	0.98	1.06	0.60
Proj. Sales Growth (F1/F0)	-8.44%	-11.87%	-1.45%	-14.46%	-29.57%	1.54%
Momentum Score	F	-	-	F	F	C
Daily Price Chg	1.68%	0.00%	-0.03%	2.46%	-0.24%	-2.54%
1 Week Price Chg	-4.04%	-4.31%	-1.45%	-6.56%	-4.08%	-8.73%
4 Week Price Chg	-1.49%	8.51%	3.76%	7.97%	0.80%	10.59%
12 Week Price Chg	1.78%	0.63%	5.99%	-8.98%	-11.28%	3.03%
52 Week Price Chg	-16.03%	-27.19%	4.07%	-34.58%	-24.18%	-27.05%
20 Day Average Volume	4,460,713	545,800	1,880,903	2,088,085	1,136,805	5,631,664
(F1) EPS Est 1 week change	-18.69%	0.00%	0.00%	-0.34%	0.00%	0.00%
(F1) EPS Est 4 week change	147.32%	0.00%	1.03%	-4.33%	0.00%	14.61%
(F1) EPS Est 12 week change	171.95%	-32.88%	3.40%	-237.17%	-151.65%	16.91%
(Q1) EPS Est Mthly Chg	-24.28%	-12.30%	0.00%	-91.67%	0.00%	-13.60%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	B
Growth Score	F
Momentum Score	F
VGM Score	F

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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