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## COMPANY SPOTLIGHT:

# Foot Locker Inc.

## COMPANY DESCRIPTION

Headquartered in New York, NY, Foot Locker is a leading operator of retail apparel and athletic footwear stores. The company offers merchandise under the names of Foot Locker, Lady Foot Locker, Champs Sports, Footaction, Kids Foot Locker, Runners Point, and Sidestep.

Dick Johnson, who joined the company in 2003, is the CEO and Chairman of the Board.

## COMPANY HIGHLIGHTS AND FINANCIALS

Founded in 1974, Foot Locker is a leading global athletic retailer operating approximately 3,200 stores in 27 countries. Unlike their competitors, Foot Locker focuses on high end sneakers and athletic footwear with a higher profit margin. Their company strategy is to generate long-term growth by empowering youth culture across communities. They demonstrated this with the opening of their Detroit store where they teamed with local artists, musicians, and athletes on store decoration, design concepts, and apparel offerings geared towards greater community and local youth connection.

### KEY POINTS

- ⌘ Tapping into youth culture and its use of footwear to express individuality
- ⌘ Collaborating with key industry partners to engage potential customers through the innovative use of new digital and interaction technology
- ⌘ Strong balance sheet with little debt
- ⌘ Strong history of raising dividends
- ⌘ Consistent returns on capital and free cash flow generation
- ⌘ Compelling valuations based on historical operating metrics and future growth projections

Over the next four years, Foot Locker is planning to aggressively invest in mobile and digital interaction technology to improve their adjustability to core customer shopping patterns. They will also revise merchandising and sales strategies with their main suppliers (e.g., Nike and Adidas). For example, in their newest New York City store in Washington Heights, Foot Locker customers can download the NikePlus app for product information and shoe availability—the first time Nike has made available their shopping technology to a third-party store. Customers can also use the Foot Locker app directly to shop for apparel and shoes across all brand offerings, and reserve forthcoming shoes prior to their in-store launch.

Simultaneously, Foot Locker is shrinking their mall footprint from 80% to 70% of physical stores and increasing their standalone 'power store' format. These larger store concepts include design features and apparel offerings that reflect local communities and support the more interactive shopping experience. They include expansion across Asia, where the sneaker culture continues to gain popularity. In 2018 they opened a new power store in Hong Kong, and added digital platforms by partnering with Alibaba's Tmall.com,

which sells to Chinese consumers. These growth initiatives set the company up to deliver strong returns on capital, consistent profits, and dividend growth for shareholders in the coming years.

## VALUATION AND RISKS

Foot Locker is trading at very attractive valuation levels. At their current sales and cash flow multiples, they are trading at roughly a 20% discount compared to their historical operating performance. Investor concerns over changing consumer shopping behavior surrounding physical mall locations are putting pressure on their shares. We realize that consumer shopping behavior is changing. Based on our analysis, we feel the market is overly pessimistic regarding the future of Foot Locker. If our analysis is incorrect, we believe there is a large margin of safety built into their current price.

Risks we will monitor going forward include the company's transformation from a traditional brick-and-mortar footprint to a digital one promoting local community experience, and Foot Locker's relationship with their suppliers (e.g., Nike). Weighing both potential rewards and risks, we are optimistic that Foot Locker is a good long-term investment.

—Patrick Mason, Investment Analyst, Cairn Investment Group



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