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## Return on Investment

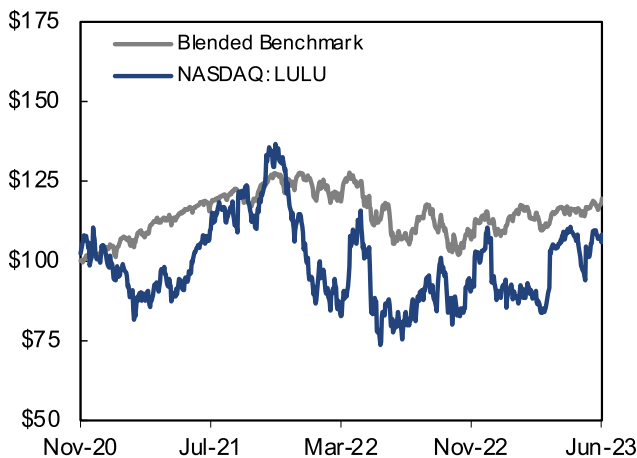
Current Share Price	\$378.50
Target Price	\$365.00
Dividend Yield	0.00%
Implied Return	(4%)
Conviction Rating	1

## Market Profile

52-Week Range	\$263.38 - \$386.71
Market Capitalization (US\$m)	\$48,090
Net Debt (US\$m)	\$148
Enterprise Value (US\$m)	\$48,238
Beta (5-Year Monthly)	1.43

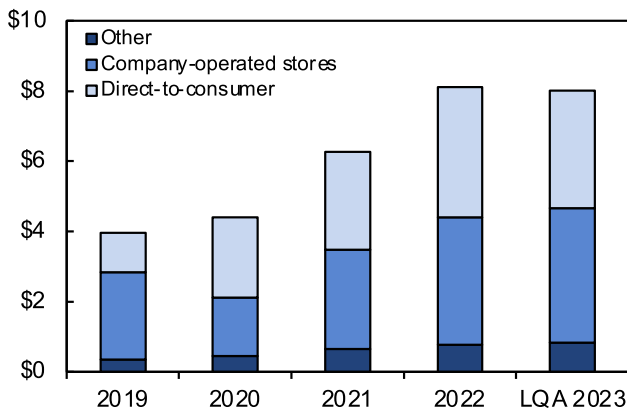
Metrics	2023E	2024E	2025E
Revenue (US\$m)	\$6,969	\$8,420	\$9,692
EBITDA (US\$m)	\$1,872	\$2,214	\$2,604
EPS (US\$)	\$8.35	\$9.86	\$11.60
EV/EBITDA	25.8x	21.8x	18.5x

## Holding Period Trading Performance (Indexed to \$100)



Source: S&P Capital IQ

Figure 1: Segmented Revenue (US\$B)



Source: Company Filings and S&P Capital IQ

## Business Description

lululemon athletica (NASDAQ: LULU) is a designer, distributor, and retailer of athletic apparel, footwear, and related accessories. The Company reports in three segments: (1) Company-operated stores, (2) Direct-to-consumer, and (3) Other. As of Q1 2023, the Company operates 662 stores in 18 countries, with ~53% of its retail locations in the U.S., ~18% in China, and ~11% in Canada. LULU's direct-to-consumer segment includes sales from its e-commerce website and mobile app. All other revenues, including sales from outlets, temporary locations, wholesale, lululemon Studio, Recommerce, and license arrangements are captured through LULU's "Other" segment.

## Industry Overview and Competitive Landscape

LULU operates within the retail apparel industry and has developed a niche in the activewear vertical. The Company directly competes with several publicly-traded companies (NYSE: NKE, UAA, VFC; XTRA: ADS, PUM) as well as direct-to-consumer brands, such as Gymshark, Alo Yoga, and Sweaty Betty. Expenses incurred by firms within the industry are primarily concentrated around procuring input materials, labour, and logistical services. In 2022, the cost of logistical services and input materials, such as cotton, increased significantly, resulting in suppressed margins across the industry. In recent months, freight rates and cotton prices have decreased materially, and the Fund believes this will allow retail apparel manufacturers such as LULU to improve margins.

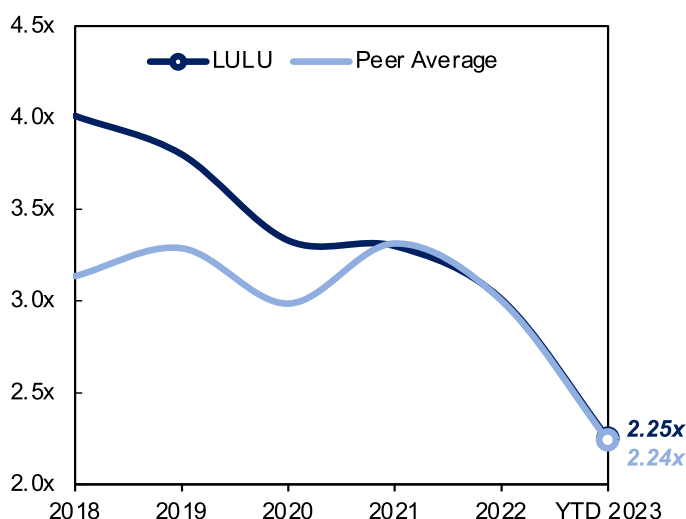
LULU has recently expanded into leisure and workplace apparel, benefiting substantially from the increase in the popularity of athleisure fashion. Athleisurewear consists of apparel designed with comfortable material typically used in activewear yet, appears professional enough to be worn in office settings. The COVID-19 pandemic positively impacted the activewear industry as individuals prioritized comfort and had less need for formal attire; however, in a post-pandemic environment activewear brands such as LULU may not be able to realize a level of growth comparable to what was experienced during the COVID-19 pandemic.

## Mandate Fit

**Quality Management:** CEO Calvin McDonald joined LULU in 2018 and has led the Company through immense growth domestically and internationally. During his tenure as CEO, LULU's North American and international revenues have grown at five-year CAGRs of 38% and 24%, respectively. In April 2019, McDonald introduced the Company's "Power of Three" strategy that aimed to double men's and e-commerce revenue as well as quadruple international revenue by 2023; management was able to successfully implement its strategy and achieve targets ahead of schedule. In April 2022, the Company announced its "Power of Three x2" strategy that aims to replicate the same level of growth achieved via the "Power of Three" campaign announced in 2018. Management has shown alignment with shareholders through its executive team compensation structure, with 84% of executive compensation being at-risk.

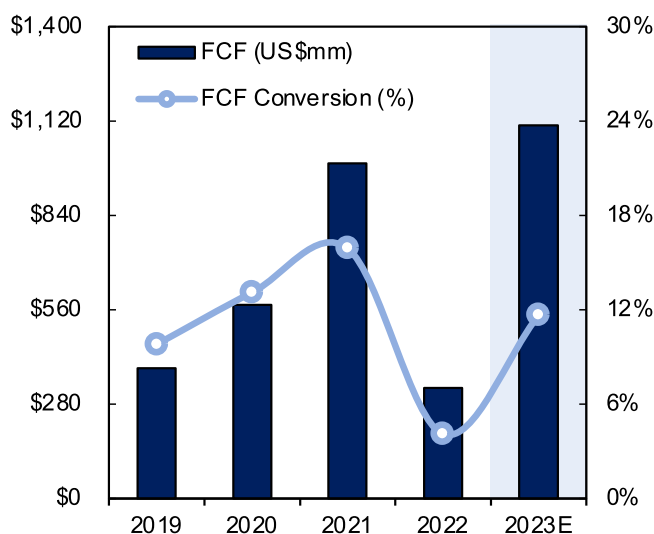
**Competitive Advantage:** LULU is uniquely positioned within the activewear segment to capitalize on the menswear (cont.)

**Figure 2: Inventory Turnover vs Peers**



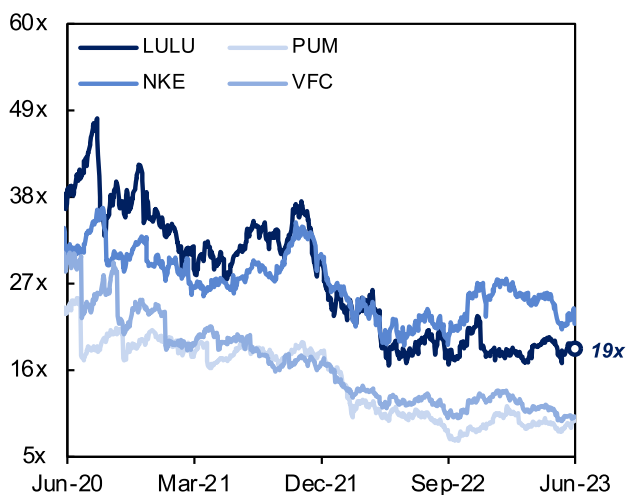
Source: S&P Capital IQ

**Figure 3: LHS FCF vs RHS FCF Margin**



Source: Company Filings

**Figure 4: Holding Period NTM EV/EBITDA vs Peers**



Source: S&P Capital IQ

athleisure movement. Prior to the rise of athleisure fashion during the COVID-19 pandemic, LULU commanded very little market share within men’s fashion; however, did retain a strong brand identity across genders. The Fund believes this has benefited the Company immensely as LULU’s brand identity has allowed it to develop a niche within menswear and emerge as a leader in men’s athleisure fashion. Other brands, such as NKE and ADS, have well-defined niches within men’s apparel, making it much more difficult for these companies to become market leaders in men’s athleisurewear. The Fund believes that LULU’s North American brand loyalty will also aid the Company in achieving international growth, as North American culture tends to trend globally.

**Strong Balance Sheet:** LULU has no debt in its capital structure and has not raised equity investment in recent years. LULU’s account payable days outstanding is the lowest amongst peers, with an average days payable outstanding of 28 compared to the peer average of 60. The onset of the COVID-19 pandemic and supply chain distributions over the last two years has resulted in inventory turnover diminishing across industry bringing LULU’s inventory turnover in-line with peers.

**Growing Free Cash Flow:** Between 2018 and 2021, the Company grew FCF at a CAGR of 24%. In 2022, LULU saw FCF decrease 67% YoY as the Company incurred US\$664mm in capital expenditures as a result of building purchases and developments. While 2022 FCF was suppressed due to capital reinvestment, FY 2022 CFO was 45% higher than pre-pandemic levels, illustrating LULU’s attractive growth profile. LULU’s ROIC for Q1 2023 was 25.1%, with its peer group averaging a ROIC of 7.9%.

**Risks**

The success of LULU’s international growth strategy is highly dependent on its Chinese market, as 18% of the Company’s stores are in the PRC. China’s post-pandemic recovery has stagnated and is likely to negatively impact LULU’s international growth strategy if the trend continues. The Company has been positively impacted by recent fashion trends, such as the increased popularity of athleisure; however, as fashion trends evolve, an inherent risk facing the Company is its ability to maintain relevancy as trends change.

**Original Investment Thesis**

In November 2020, the CPMT initiated a position in LULU as it believed the Company maintained robust fundamentals, was a well-established brand, and had potential for market growth. The Fund held a positive view of LULU’s distinct brand identity, a wide range of products, and focus on innovation. Additionally, the Fund viewed LULU’s e-commerce platform favourably as it aided the Company in navigating the challenges posed by the COVID-19 pandemic. Overall, the CPMT considered LULU a strong player in the market and a compelling addition to its consumer discretionary holdings.

**Revised Investment Thesis and Valuation**

LULU was valued at US\$365 using a five-year DCF with a WACC of 9.2%. The terminal value was determined through a 50/50 blend of (1) the Gordon Growth method, using a 4.0% terminal growth rate, and (2) an EV/EBITDA exit multiple of 17.5x. The CPMT believes LULU trades at a premium to its peers due to its track record of delivering outsized growth in both the top-line and operating margin. The CPMT stands by its view of LULU being a high-quality name but has not yet come to a definitive view on intrinsic value. In turn, the Fund intends to launch a broader strategic review of the name to determine its future as a holding.