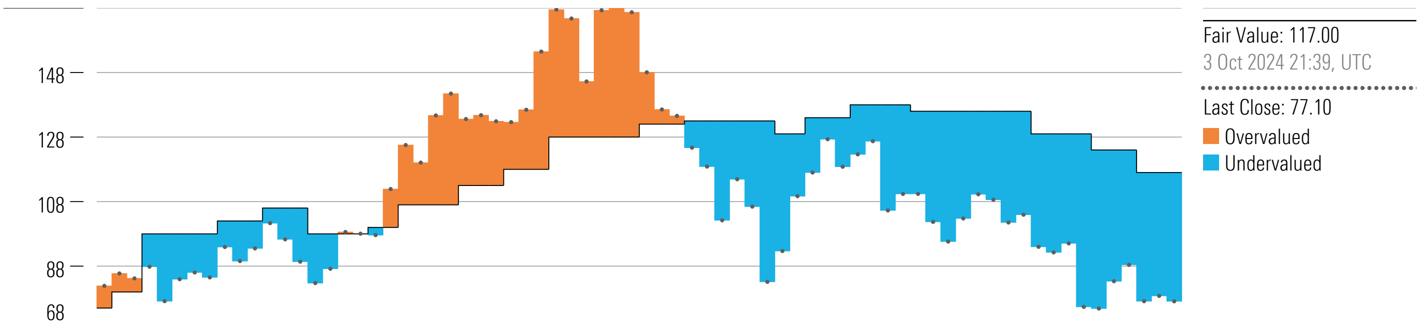
Morningstar Equity Analyst Report | Report as of 20 Dec 2024 03:25, UTC | Reporting Currency: USD | Trading Currency: USD | Exchange: NEW YORK STOCK EXCHANGE, INC.

Nike Inc Class B NKE ★★★★★ 19 Dec 2024 22:40, UTC

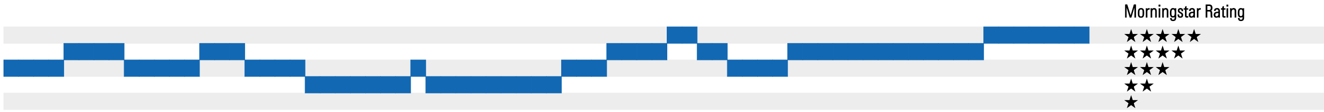
Last Price	Fair Value Estimate	Price/FVE	Market Cap	Economic Moat™	Equity Style Box	Uncertainty	Capital Allocation	ESG Risk Rating Assessment[1]
77.10 USD 19 Dec 2024	117.00 USD 3 Oct 2024 21:39, UTC	0.66	114.76 USD Bil 19 Dec 2024	Wide	Large Value	Medium	Exemplary	4 Dec 2024 06:00, UTC

Price vs. Fair Value



	2019	2020	2021	2022	2023	YTD	
	0.96	1.32	1.30	0.87	0.80	0.66	Price/Fair Value
	37.87	40.64	18.61	-29.04	-6.03	-27.60	Total Return %

Morningstar Rating



Total Return % as of 19 Dec 2024. Last Close as of 19 Dec 2024. Fair Value as of 3 Oct 2024 21:39, UTC.

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The primary analyst covering this company does not own its stock.

[1]The ESG Risk Rating Assessment is a representation of Sustainalytics' ESG Risk Rating.

Nike Earnings: Results and Weak Guidance Suggest Turnaround Not Imminent; Shares Undervalued

Analyst Note David Swartz, Senior Equity Analyst, 20 Dec 2024

Although Nike reported second-quarter sales and earnings above expectations, it was a generally poor result by its usual standards. Moreover, the outlook for the rest of fiscal 2025 is dismal as CEO Elliott Hill, on the job since October, intends to increase discounting to clear inventory ahead of new product releases in fiscal 2026. We expect to cut our $117 per share fair value estimate by a mid-single-digit percentage on the results and guidance, but regard Nike's shares as very undervalued. Our wide moat rating on the firm is based on its brand intangible asset, and we believe Hill is making the right moves to bolster its brand value. His general plan is to invest in Nike's connections to global sports, which we regard as the firm's greatest advantage.

Nike's sales fell 8% in the quarter, but this was slightly better than our estimate for a 9% drop. All its segments posted sales declines, including high-single-digit drops in North America (42% of the total), Europe, the Middle East, and Africa (27%), and Greater China (14%). Footwear was especially weak (sales down 11%) as the company is pulling back on overexposed shoe lines to make room for more innovative products to be more competitive against upstart brands like On and narrow-moat Deckers' Hoka. We think Nike will be successful in this effort, but it has a lot of work to do to improve relationships with wholesale partners and to increase full-price selling in its company-owned digital channels, which have too often been used for clearance.

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Sector	Industry
Consumer Cyclical	Footwear & Accessories

Business Description

Nike is the largest athletic footwear and apparel brand in the world. Key categories include basketball, running, and football (soccer). Footwear generates about two thirds of its sales. Its brands include Nike, Jordan (premium athletic footwear and clothing), and Converse (casual footwear). Nike sells products worldwide through company-owned stores, franchised stores, and third-party retailers. The firm also operates e-commerce platforms in more than 40 countries. Nearly all its production is outsourced to contract manufacturers in more than 30 countries. Nike was founded in 1964 and is based in Beaverton, Oregon.

As sales were soft, Nike's second-quarter EBIT margin fell nearly 3 percentage points to 11.3%, but this was better than our 9.6% forecast as cost-control efforts had some positive effect. Nike is investing in marketing while cutting expenses elsewhere, which we regard as prudent for its brand health. In the long run, we think Nike can return to midteens EBIT margins as it increases full-price sales, releases new merchandise, and increases sales in high-margin markets.

Business Strategy & Outlook David Swartz, Senior Equity Analyst, 3 Oct 2024

We view Nike as the leader of the athletic apparel market and believe it will recover from its recent problems, such as a lack of product innovation, soft demand for sportswear, and a CEO change. Our wide moat rating is based on its intangible brand asset, as we believe it will maintain premium pricing and generate economic profits for at least 20 years. Nike, the largest athletic footwear brand in all major categories and in most markets, dominates areas like running and basketball with popular shoe styles. While it does face significant competition, we believe it has proven over a long period that it can maintain share and pricing.

We think Nike's strategies allow it to maintain its leadership position. Over the past few years, it has invested in its direct-to-consumer network while cutting many wholesale accounts. In North America and elsewhere, the firm has reduced its exposure to undifferentiated retailers while increasing its connections with others that bring the Nike brand closer to consumers, carry a full range of products, and allow it to control the brand message. Nike's consumer plan is led by its Triple Double strategy to double innovation, speed, and direct connections to consumers. The plan includes cutting product creation times in half, increasing membership in Nike's mobile apps, and improving the selection of key franchises while reducing its styles by 25%.

Although its recovery in China has been slow due to economic conditions, native competition, and a political controversy, we still believe Nike has a great opportunity for revenue growth there and in other emerging markets. The firm experienced double-digit annual sales growth in six of the past nine fiscal years in Greater China and, fueled by high government investment in athletics, we think it will do so again after the current difficulties have passed. Moreover, with worldwide distribution and a huge direct-to-consumer operation that brought $21.5 billion in Nike brand digital sales in fiscal 2024, the firm should benefit as more people in China, Latin America, and other developing regions move into the middle class and gain broadband access.

Bulls Say David Swartz, Senior Equity Analyst, 3 Oct 2024

- Although uneven of late, the global sportswear market should expand, especially in Asia and other developing areas. As the share leader in most countries, Nike is positioned to benefit.
- Nike's restructuring efforts to achieve $2 billion in cost cuts and its Triple Double strategy (increased innovation, direct-to-consumer sales, and speed) should allow for improved margins.

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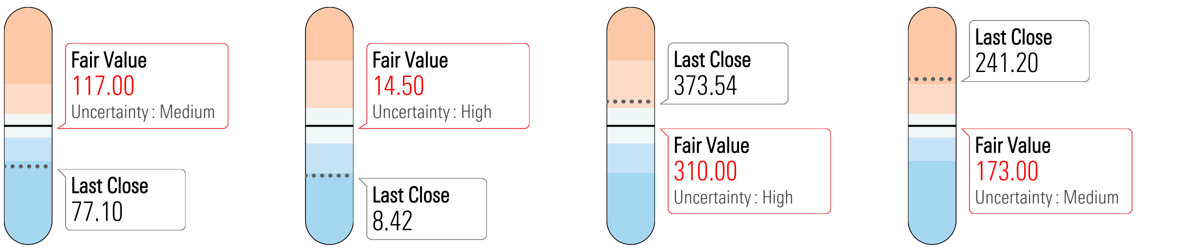
Competitors

	Nike Inc Class B NKE	Under Armour Inc Class A UAA	Lululemon Athletica Inc LULU	adidas AG ADS



	Nike Inc Class B NKE	Under Armour Inc Class A UAA	Lululemon Athletica Inc LULU	adidas AG ADS
Economic Moat	Wide	None	Narrow	Narrow
Currency	USD	USD	USD	EUR
Fair Value	117.00 3 Oct 2024 21:39, UTC	14.50 25 Nov 2024 05:23, UTC	310.00 17 Dec 2024 15:45, UTC	173.00 16 Oct 2024 00:55, UTC
1-Star Price	157.95	22.48	480.50	233.55
5-Star Price	81.90	8.70	186.00	121.10
Assessment	Undervalued 19 Dec 2024	Undervalued 19 Dec 2024	Overvalued 19 Dec 2024	Overvalued 19 Dec 2024
Morningstar Rating	★★★★★ 19 Dec 2024 22:40, UTC	★★★★ 19 Dec 2024 22:41, UTC	★★ 19 Dec 2024 22:43, UTC	★ 20 Dec 2024 01:32, UTC
Analyst	David Swartz, Senior Equity Analyst	David Swartz, Senior Equity Analyst	David Swartz, Senior Equity Analyst	David Swartz, Senior Equity Analyst
Capital Allocation	Exemplary	Standard	Exemplary	Standard
Price/Fair Value	0.66	0.58	1.20	1.36
Price/Sales	2.38	0.69	4.59	1.87
Price/Book	8.18	1.83	11.45	8.17
Price/Earning	22.03	791.59	26.90	111.09
Dividend Yield	1.96%	0.00%	0.00%	0.30%
Market Cap	114.76 Bil	3.64 Bil	45.49 Bil	42.16 Bil
52-Week Range	70.75—123.39	6.17—11.89	226.01—516.39	163.14—245.40
Investment Style	Large Value	Small Blend	Mid Growth	Large Growth

- Somewhat depressed lately, we anticipate Nike's gross margins will rise through automation, e-commerce, and higher prices. Nike is pulling back from undifferentiated retailers to increase full-priced sales.

Bears Say David Swartz, Senior Equity Analyst, 3 Oct 2024

- As a worldwide business, Nike has felt the effects of issues like the war in Ukraine, shipping delays, currency volatility, and inflation. These and other issues could continue to impair its results.
- The Chinese sportswear market is increasingly competitive as nationalism has boosted native brands and as international brands like Lululemon expand. Nike must continue to lead this market to meet long-term profit goals.
- Nike's dominance in running shoes has been challenged by the success of relative newcomers like Hoka and On. It has fallen behind some others on innovation.

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Economic Moat David Swartz, Senior Equity Analyst, 3 Oct 2024

We assign a wide moat rating to Nike based on its brand intangible asset. Nike is the world's-largest athletic apparel and footwear company, with global operations and more than $50 billion in annual revenue. Its sales have increased in 13 of the past 14 years, with the pandemic-affected fiscal 2020 as the sole exception.

As evidence of its competitive edge, Nike's adjusted returns on invested capital, including goodwill, have averaged 34% over the past five fiscal years, well above our 8% estimated weighted average cost of capital. Moreover, we forecast that the company's annual adjusted ROICs, including goodwill, will average 39% over the next decade and exceed its WACC for at least the next 20 years, as required for our wide moat rating. Nike's ROICs possibly get a boost from the firm's outsourcing of production to third-party factories, but we believe its returns on investment would be high even if its asset base were larger.

In addition to quantitative factors, we evaluate activewear producers like Nike using five specific criteria: geographic reach; pricing; sponsorships/visibility; product quality/performance; and control over distribution. We rate Nike as high in geographic reach, sponsorships/visibility, pricing, and product quality/performance, but moderate in control over distribution. While there are a small number of other companies, such as Lululemon, that produce quality products and may have stronger direct control over selling than Nike, none of them can approach its visibility and global reach.

A key part of our wide moat rating, Nike benefits from the worldwide popularity of athletics and its products are available in most of the world's industrialized and developing nations. The company ships products to more than 190 countries (with more than half its sales outside North America), has 6,000 or so branded stores that are operated by franchisees, primarily in Greater China, and directly operates more than 1,000 stores (two thirds outside of the US). At a global share of 18%, Nike's annual revenue is more than double that of the world's second-largest sportswear firm, narrow-moat Adidas (Euromonitor). In North America, its share of the sportswear market—estimated to be about $166 billion in retail sales—was 18.1% in 2023, far ahead of second-place Adidas' 4.9% and third-place Lululemon's 4.5% (Euromonitor). In Western Europe, with $71 billion in retail sales, Nike's leading 17.9% share was 5.7 percentage points above Adidas. While these markets are highly competitive, we anticipate Nike will hold its leading positions due to its innovation, sponsorships, advertising, and the enduring popularity of its products.

Sportswear is a relatively mature category in North America and Western Europe, but Nike has excellent growth prospects in China. The Chinese sportswear market is estimated at $58 billion at retail in 2024, roughly triple 2013's level. Although athletics has not been part of its culture historically, China has hosted two Olympics and become a power in many sports due to massive government investment and

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growing opportunities. For example, hundreds of marathons are held each year in China, with leading races attracting tens of thousands of entrants. As the market leader with 23% sportswear share in 2023, Nike is positioned to benefit from China's athletic aspirations. The company's revenue in Greater China increased to $7.5 billion in fiscal 2024 from $3.9 billion in fiscal 2016, and we forecast compound annual average sales growth of 11% over the next decade. However, we are aware that Nike faces challenges from American and European firms in the region, as well as growing native competitors like narrow-moats Anta and Li Ning, which had market shares of about 20% and 10%, respectively, in 2023 (Euromonitor). Nike is responding to these threats with new flagship stores, greater marketing, and products designed specifically for Chinese consumers.

Very high visibility is a significant part of Nike's success, and it benefits from the immense popularity of athletics. For example, Nike is heavily involved with global football (soccer), and more than 40% of the world's people are fans of the sport, per WorldAtlas. Indeed, there are more than 200 countries with national men's football teams, and more than 120 have women's national teams as well (FIFA). The vast reach of athletics benefits Nike as it sponsors many of the world's most popular athletes, leagues, and teams in virtually all major sports. For example, it is the uniform provider for each of the three-largest sports leagues in the US (NFL, NBA, and MLB). Individuals sponsored by Nike include many of the world's most famous athletes, including Cristiano Ronaldo (football/soccer), Kevin Durant (basketball), and LeBron James (basketball), all three of which have the equivalent of lifetime deals with the brand.

Nike's success in sports sponsorships largely stems from its more than 40-year relationship with Michael Jordan. More than 20 years since the basketball great retired, Nike's Jordan premium sub-brand remains the gold standard for sports marketing, generating $7 billion in wholesale-equivalent sales in fiscal 2024 alone. Nike's relationships with athletes at all levels gives it visibility and credibility that no other company in its industry has amassed.

While marketing is important, Nike needs to offer quality products to maintain its position. We believe the firm's technical innovations contribute to its brand and support our wide-moat view. It has been known for its innovative products ever since it introduced running shoes with pressurized air in their soles in the 1980s. Nike produces shoes for many sports, but its most important shoes may be those made for runners. Recent editions to its large family of running shoes include Epic React (foam cushioning), VaporMax, and shoes with ZoomX technology. Nike claims the ZoomX substance was developed for the aerospace industry and returns as much as 85% of energy to the runner. While it may be hard to prove such a claim, the firm's dominance in running shoes is clear as the category produces about $4 billion in annual sales. Indeed, most of the world's leading track and field athletes wear Nike shoes, as do millions of amateur runners. As for basketball and international football, about three quarters of NBA players wear either Nike or Jordan, while about half of the players in the 2022 FIFA World Cup wore Nike cleats.

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Nike supports its innovation with high investment in research and development. Its annual research and development spending exceeds $500 million, or about 1% of sales. While its competitors also invest in innovation, their total spending is less due to their smaller revenue bases. In 2023, Adidas' research and development expenditure was EUR 151 million, while that of no-moat Puma was EUR 89 million.

Nike offers products in many channels and at many price points, but it achieves premium pricing on key products, supporting our view of its brand power. The firm has always been led by footwear, which accounts for about two thirds of its sales. Many styles of its athletic shoes regularly sell for more than $150 per pair, putting it at or near the top of the market in many categories. Nike also offers limited-edition shoes at high prices, such as the footwear offered through a 2022 collaboration with Louis Vuitton that retailed for about $3,000 per pair. Moreover, there is a large secondary market for Nike shoes, with many styles commonly changing hands at more than $1,000 per pair. For example, the Nike-Louis Vuitton items commonly sell for thousands of dollars above original retail prices on resale sites. We regard Nike's ability to sell high-priced items in large quantities as support for a brand-based intangible asset.

As for its distribution, Nike has made a big push into direct selling over the past several years. It has intentionally cut many retailers off from its wholesale distribution to support its own selling efforts and to prioritize third-party sellers that showcase the brand. Nike has invested heavily in its physical stores, including in large flagships in major cities worldwide. It also has a very large digital presence. The firm generated about $12 billion in Nike brand e-commerce sales from its digital marketplaces in fiscal 2024, up from about $1.5 billion in fiscal 2015. Nike intends to increase its digital sales further, which should be achievable as it adds more app users in developed markets and as more consumers in developing markets (such as China, India, and Latin America) move into the middle class and gain access to broadband services.

Nike has dozens of apps worldwide and a sizable loyalty program. In 2023, the company disclosed that its primary apps had reached 500 million users. The high usage of Nike's digital tools is a great opportunity for full-price selling with limited marketing costs and a source of vast amounts of consumer data. While other athletic apparel companies have e-commerce, none of them have the reach of Nike.

Even so, Nike continues to have high exposure to wholesale accounts, especially in North America, where it sells through specialty sporting goods stores, department stores, and elsewhere, and in China, where most of its sales come through franchised stores. Nike's exposure to third-party sellers has contributed to inventory and discounting problems at times, but it is also an opportunity to reach large numbers of consumers without the cost of operating thousands of stores. One way that Nike is benefiting from its wholesale distribution is by integrating its loyalty program with those of key retailers, such as narrow-moat Dick's Sporting Goods in the US and UK-based JD Sports.

We do not believe Nike has a moat based on a cost advantage. Although Nike may have some cost edge over competitors in sponsorships due to its status as the premier sportswear brand, we don't view this as significant or maintainable. Moreover, endorsements are great for brand building, but they are difficult to quantify in terms of profit margins. On the production side, Nike has limited advantage in the procurement of raw materials and other costs as virtually all its production is outsourced to factories that serve other sportswear firms as well. Narrow-moat Shenzhou International, for example, is one of Nike's largest suppliers but also produces apparel for Adidas, Puma, and others.

Our view is that Nike's moat is based solely on its brand intangible asset. While Nike's financial resources and relationships with suppliers likely allow for production investment unavailable to others in the short term, any advantage in this area is likely to be transitory. Further, competing producers can probably gain access to similar technologies. Moreover, much of apparel manufacturing remains manually intensive. Competing products to Nike's footwear and clothing are widely available. As such, we do not believe there is any network effect or efficient scale in the apparel business, and switching costs are nonexistent.

Fair Value and Profit Drivers David Swartz, Senior Equity Analyst, 3 Oct 2024

We are lowering our fair value estimate on Nike's shares to $117 from $124. The company's fiscal 2025 first-quarter earnings per share of $0.70 surpassed our $0.51 estimate. However, its quarterly sales fell 10%, and it guided to a slow recovery in sales and margins due to uncertain economic conditions in key markets and weak demand for some lifestyle and footwear products. Indeed, second-quarter sales are set to fall 8%-10%. Thus, for fiscal 2025, we have lowered our sales forecast to a 7% decline from a 5% drop previously, and our EPS forecast to $2.77 from $3.09. Our fair value estimate implies a fiscal 2025 price/earnings ratio of 42 and an enterprise value/adjusted EBITDA ratio of 30.

Despite the anticipated sales decline in fiscal 2025, we forecast compound average sales growth for Nike of 5% over the next 10 years. We expect it will achieve compound annual revenue growth of 2% in North America, perhaps slightly below expected market growth. We think Nike's innovative products and e-commerce will allow it to hold its market position and premium pricing, but we acknowledge that the market has become very competitive. In Greater China, its fastest-growing segment prior to recent challenges (such as virus-related lockdowns and the forced labor controversy), we expect compound average growth of 11% over the next decade.

Although Nike's fiscal 2024 gross margin of 44.6% was below fiscal 2022's 46% on weak sales of some products and poor digital sales, we forecast a return to 46% in about two years as its sales growth returns in fiscal 2026 and as its inventory situation has improved. In the long run, we project gradual improvement to about 48% in 10 years. The firm may increase gross margins through greater production and distribution efficiencies, its shift to digital sales, product mix changes, and price increases.

We think Nike's operating margins will rise as it achieves cost efficiencies, shifts sales to direct channels, and increases sales in Greater China, its most profitable market. The firm's new restructuring plan is expected to bring about $2 billion in expense reductions by the end of fiscal 2026. We forecast Nike's overall EBIT margins will gradually increase from below 13% in fiscal 2024 to 17% over the next decade. In Greater China, we forecast its EBIT margins will rise to 34% from 30%-31% recently. Nike's EBIT margins in the region have recently been inconsistent due to economic conditions and competition from native brands but should improve as sportswear demand in the market returns to its high-growth path. In North America, we forecast segment operating margins of about 27% as it increases its direct-to-consumer sales and limits discounting of its products.

Risk and Uncertainty David Swartz, Senior Equity Analyst, 3 Oct 2024

Our Morningstar Uncertainty Rating on Nike is Medium. Nike struggled with supply chain problems and excess inventory in the 2021-22 period but has made progress in fixing these issues.

Nike is vulnerable to weakness in US physical retail. Department stores that carry its products have been downsizing and cutting orders. However, the firm should be able to make up for slowness in some areas of retail through its direct-to-consumer sales.

As a global business, Nike is affected by economic conditions in many parts of the world. Consumer spending on the company's products has been uneven due to inflation, war, currency movement, trade restrictions, and other issues.

The athleisure trend and growth in activewear has attracted new competition. While Nike is the market leader in many categories and in most markets, competitors like Hoka and On have emerged as challengers. Nike is under constant pressure to release new products that resonate with consumers and may miss sales projections if it fails to do so.

We do not believe the environmental, social, and governance risks that affect Nike will materially impact its financial results or investment prospects. Nonetheless, the firm tends to be a lightning rod for controversy due to its high visibility. There are ongoing controversies concerning the treatment of its female and minority employees, its efforts to reduce taxation, and the treatment of workers in its supply chain. Moreover, Nike has become entangled in a forced labor controversy in China that has caused a consumer backlash in the country and international criticism. Any lasting effects on its operations in the nation could be damaging, as China is the fastest-growing sportswear market in the world and Nike's most profitable region. We may revisit our view of Nike's ESG risks if any of these controversies endanger its profit potential.

Capital Allocation David Swartz, Senior Equity Analyst, 3 Oct 2024

We assign an Exemplary Capital Allocation Rating to Nike. In the 15 years between October 2009 and

October 2024, Nike generated an average annual total return to investors of 13% (includes dividends). Nike is the largest US-based apparel firm and the largest athletic apparel company in the world. Its adjusted ROICs, including goodwill, have averaged 34% over the past five years, well above our estimated weighted average cost of capital on the company of 8%.

Elliott Hill, a Nike veteran of more than 30 years, was named to replace John Donahoe as CEO. We do not expect that this change will affect the firm's capital allocation policies.

Nike has a strong balance sheet, having operated in a net cash position for most of the past decade. Although the firm issued $6 billion in unsecured notes when the pandemic hit in the spring of 2020, we believe this was just a precaution, and that the firm now has more cash than it needs to fund operations and capital return plans. We forecast Nike will generate an annual average of $5.3 billion in free cash flow to the firm over the next five years. Most of Nike's long-term debt matures after 2028.

Nike has been investing heavily in its direct-to-consumer efforts in recent years, and we have viewed this as a sound and successful strategy. The firm has been expanding its physical store base and its online operations. Its direct-to-consumer sales accounted for 44% of its Nike brand revenue in fiscal 2024, up from less than 20% before 2015. We forecast Nike's fiscal 2025 capital expenditures at $1.1 billion (2.2% of sales), with much of the investment going into its direct-to-consumer efforts. As it is a high growth and high profit margin opportunity, we anticipate Nike will continue to build its direct-to-consumer operations for years to come.

We think Nike has created value through acquisitions and dispositions. In 2003, Nike bought Converse for just $305 million. Converse, known for its casual athletic canvas shoes, had gone bankrupt in 2001 and had just $205 million in sales in 2002, but Nike resurrected it. In fiscal 2024, Converse produced $2.1 billion in sales and nearly $500 million in operating profit. While Nike continues to own Converse, it has divested other brands. In 2012, for example, it sold Cole Haan for $570 million, 24 years after it had bought it for $95 million. In 2019, Nike sold Hurley, which it had acquired in 2002, for an undisclosed amount. We view dispositions of niche brands as beneficial to shareholders as they allow Nike to focus on its core business.

Nike has returned significant cash to shareholders through dividends and stock buybacks. The company issues about $2 billion in yearly dividends, and we expect its long-term dividend payout ratio will be roughly 40%. Nike also returns cash to shareholders through buybacks, having repurchased about $8 billion in shares over the past two fiscal years. The company has reduced its share count by roughly 15% over the past decade, and we expect it will repurchase $16 billion (net) in stock over the next five years. We believe companies increase shareholder value when repurchasing shares below our fair value estimates, as has recently been the case for Nike.

Analyst Notes Archive

Nike Earnings: Substandard Results Met Expectations as CEO Change Looms; Shares Attractive

David Swartz, Senior Equity Analyst, 2 Oct 2024

Matching our estimate, Nike's sales declined 10% in fiscal 2025's first quarter. More significantly, CFO Matt Friend (who handled the earnings call solo ahead of CEO Elliott Hill's arrival on Oct. 14) suggested that sales and margin improvement are developing slowly. Indeed, second-quarter sales are set to fall 8%-10%, below our estimate for a 6% decline. Current challenges include unsettled economic conditions in major markets, as well as Nike's decision to pull back on the supply of some major footwear franchises to avoid excessive discounting. While this move is hurting sales at present, we think it is necessary to protect its brand value, the source of our wide moat rating.

Given the dim near-term outlook, we expect to reduce our $124 per share fair value estimate by a mid-single-digit percentage, in line with the Oct. 1 postmarket decline. Even so, we regard the price weakness as an investment opportunity. In time, we expect a turnaround as economic conditions improve and as Nike introduces new products and repairs its relationships with wholesale accounts.

First-quarter sales by region aligned with our estimates. As expected, Nike posted double-digit sales declines in North America (42% of total) and Europe, the Middle East, and Africa (27% of total). Sales in Greater China (14% of total) dropped 4%, but this was slightly better than our forecast for a 6% drop. Despite these results, we think Nike has growth opportunities in all regions as it reclaims lost market share in running and casual footwear and benefits from the global popularity of sports.

Despite the sales decline, Nike's quarterly earnings per share of $0.70 bested our forecast by $0.19. Its 45.4% gross margin beat our estimate by 90 basis points, and its overhead expenses benefited from cost cuts. Even so, we are encouraged that Nike continued to spend heavily on marketing around the Olympics and other events (demand creation expense up 15%).

Nike: CEO Switch Is Part of Plan to Return to Winning Ways; Shares Undervalued David Swartz, Senior Equity Analyst, 20 Sep 2024

Nike announced that CEO John Donahoe is leaving and will be replaced by former executive Elliott Hill. Donahoe has been under intense pressure in recent months after the firm had essentially no sales growth in fiscal 2024 and guided to lower revenue in fiscal 2025. Although he had a strong background in consulting and technology when he was named CEO in 2019, he did not have apparel and footwear experience. In contrast, Hill worked at Nike for 32 years before his retirement in 2020, with his last title being president of consumer and marketing. Clearly, Nike's board (including the controlling Knight family) wanted a leader with extensive company knowledge to address its recent problems, the most pressing of which is that Donahoe's efforts to prioritize direct selling over product development and retail relationships have seemingly created opportunities for more innovative competitors.

We are not making any revisions to our $124 fair value estimate and view Nike's shares as very attractive. In the short run, the firm faces a challenging market without a compelling new product to drive sales. Indeed, we expect it will report a large (10%) sales decline when it releases its first-quarter results on Oct. 1. However, we anticipate that sales will pick up in subsequent quarters as new products are released. In the long run, we forecast mid-single-digit percentage sales growth and operating margins that improve to the high teens from around 12% of late as the firm capitalizes on its strengths, including its leading share in all major sportswear markets, unmatched marketing, and vast product lineup. Nike's deep integration with international athletics underpins our wide moat rating based on a brand intangible asset.

We are also maintaining our Exemplary Capital Allocation Rating. After issuing $2 billion in dividends and repurchasing $4 billion in shares in fiscal 2024, we expect it will continue to return most of its free cash flow to shareholders.

Nike Earnings: Dim Sales Outlook Slams Shares but Patient Investors Could Be Rewarded David Swartz, Senior Equity Analyst, 28 Jun 2024

Nike's shares roughly doubled their year-to-date decline with a 12% tumble in June 27 aftermarket trading as persistent sales weakness has added uncertainty to the firm's turnaround. Although the firm had warned of a difficult demand environment for sportswear and we had lowered our estimates, market conditions are more challenging than expected. Specifically, after posting flat sales growth in (May-ended) fiscal 2024, Nike guided to a mid-single-digit percentage sales decline for fiscal 2025. Given that we had projected 1% sales growth, we expect to reduce our fair value estimate of $129 per share by a low-single-digit percentage. Even so, we regard the share price weakness as an opportunity for long-term investors, given that the wide-moat sportswear leader stands to benefit over the next few years from its planned marketing and product initiatives and the growth of the global market.

Nike's 13.3% EBIT margin in its fiscal 2024 fourth quarter beat our estimate by 80 basis points and led to earnings per share of $0.99 that eclipsed our forecast by $0.11. However, this outperformance was mainly driven by a 9% reduction in overhead expenses and was overshadowed by the quarter's 2% sales decline, short of our estimate for a minimal (1%) gain. The firm attributed the slow sales to a few areas, including digital (down 10%), lifestyle products, some footwear, and uneven demand in key markets. Nike brand sales in North America (42% of total) and Europe, the Middle East, and Africa (26%), fell 1% and 2%, respectively, which was shy of our estimates for 1% growth and a 1% decline; while 3% sales growth in Greater China (15%) was short of our 7% projection. In the latter region, Nike's thousands of branded stores experienced double-digit traffic declines amid a very promotional market, suggesting that a return to historical sales growth levels above 10% are unlikely before fiscal 2026. That said, we anticipate a sharp turnaround as the nation's sportswear market develops.

Nike Earnings: Brand Investments Look Promising, but Near-Term Outlook Is Dim; Shares

Undervalued David Swartz, Senior Equity Analyst, 22 Mar 2024

Wide-moat Nike matched our forecast with flat sales growth in its third-quarter fiscal 2024 (end-February), but this result was overshadowed by guidance for a low-single-digit percentage sales decline in first-half fiscal 2025. This outlook suggests that subpar consumer demand for sportswear in North America, China, and other key markets is likely to persist longer than many industry participants have anticipated. As such, our forecast for Nike to rebound to 7% sales growth in fiscal 2025 is likely out of reach and we expect to lower our $136 fair value estimate by a mid-single-digit percentage. Even so, we think investments in products, marketing, and its supply chain will allow it to regain lost share and outpace market growth when sportswear demand improves. Historically, investing in Nike's shares in difficult periods has been a very successful strategy.

Nike's third-quarter sales were close to our expectations in most segments. North America sales (41% of the total) rose 3%, slightly above our 2% estimate, as the company reported lower markdowns in the holiday period than many competitors. However, Nike's outlook suggests that this market is likely to remain challenging. Moreover, sales fell 3% in Europe, Middle East, and Africa (25% of the total) due to weaker economic conditions. Nike plans to introduce new products around the summer 2024 Paris Olympics that should eventually drive an improvement in sales across all regions.

Nike's 10.9% EBIT margin in the quarter outpaced our estimate by 150 basis points as expense controls were better than we had expected. Moreover, although the firm incurred $340 million in restructuring charges in the period, this was less than the $425 million assumed in our forecast. Due to this margin outperformance, EPS of $0.77 beat our estimate by $0.14. For the fourth quarter, Nike's outlook suggests that sales growth may be below our 3% estimate, but also that the bottom-line impact may be offset by cost controls.

Nike Earnings: Near-Term Outlook Dims but Margin Improvement Still Likely; Shares Undervalued

David Swartz, Senior Equity Analyst, 22 Dec 2023

Wide-moat Nike's earnings in its (November-ended) fiscal 2024 second quarter surpassed our forecast, but this result was overshadowed by a disappointing second-half sales outlook, especially in greater China and Europe, the Middle East, and Africa, or EMEA. Specifically, the firm guided to 1% sales growth for the full fiscal year, below our 4% estimate. Moreover, Nike announced a new restructuring plan that will bring $400 million-$450 million in one-time charges in the second half. This plan, which will include layoffs, increased automation, and product eliminations, is expected to generate as much as $2 billion in cost savings over the next three years to fund efficiency, speed, and product development efforts.

Reversing recent gains, Nike's shares slid about 12% in Dec. 21 aftermarket trading. While we expect to reduce our short-term sales estimates to reflect the new outlook, the impact on profitability (excluding the special charges) should be limited. In the long run, we still expect Nike can generate mid-single-digit annual sales growth and build to high-teens operating margins. Thus, we do not expect to make any material change to our $136 fair value estimate, leaving shares attractive.

Nike's 1% sales growth in the quarter aligned with our estimate even as reported sales in its largest regions, North America (42% of total sales), EMEA (27% of sales), and greater China (14% of sales), were slightly below expectations. Like many peers, Nike faced weak retail demand and wholesale orders (sales down 2%). Even so, its profitability was strong, as its 14.2% EBIT margin in the quarter beat our estimate by about 3 percentage points due to operating cost control and lower freight costs and price increases that allowed its gross margin to increase 170 basis points to 44.6%.

We expect to adjust our Morningstar Uncertainty Rating on Nike to Medium from High based on the stabilization of its business after the pandemic and our quantitative model.

Nike Earnings: Brand Strength Shines Despite North America Weakness; Shares Undervalued David Swartz, Senior Equity Analyst, 29 Sep 2023

Wide-moat Nike's profit margins eclipsed our estimates in its (August-ended) fiscal 2024 first quarter despite a tough demand environment in North America and negative currency effects. We believe the firm's competitive advantages, including its innovative product, robust marketing, and global focus, are allowing it to outperform competitors. Although second-quarter sales growth is likely to be negligible, we do not think Nike will need to resort to heavy discounting as its inventory was down 10% at the end of the first quarter. Nike's shares edged up by 8% in Sept. 28 postmarket trading, but we still rate them as undervalued in relation to our fair value estimate of $136, which we do not expect to revise materially. Nike's shares have rarely traded at such a sizable discount to our valuation over the past decade.

In the quarter, Nike's 2% sales growth matched our forecast even though wholesale sales in North America fell 8%. The firm recorded sales increases of 5% and 8% in greater China (13% of sales) and Europe, the Middle East, and Africa (28% of sales), respectively, versus our estimates of 2% growth for both. On a constant-currency basis, greater China sales rose 12%, which we rate as a solid result given the slow economic recovery in the region. We model compound average annual sales growth of 13% for Nike in greater China in the long run as investments allow to it maintain its premium positioning and interest in athletics among Chinese continues to rise.

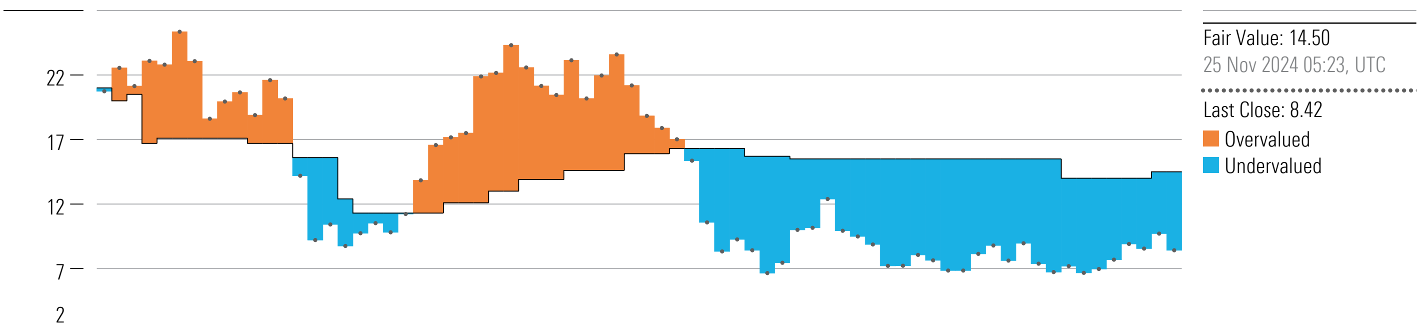
Nike's 44.2% and 12.4% gross and operating margin, respectively, surpassed our forecast by 70 and 240 basis points. Its margins likely benefited from the mix shift as well as successful price increases and lower shipping costs. Although there is uncertainty as to its ultimate impact, we think Nike's transition away from wholesale in favor of its own channels will bring about steady margin increases, with gross and operating margins reaching about 49% and 18%, respectively, in 10 years.

Morningstar Equity Analyst Report | Report as of 20 Dec 2024 03:25, UTC | Reporting Currency: USD | Trading Currency: USD | Exchange: NEW YORK STOCK EXCHANGE, INC. Page 14 of 24

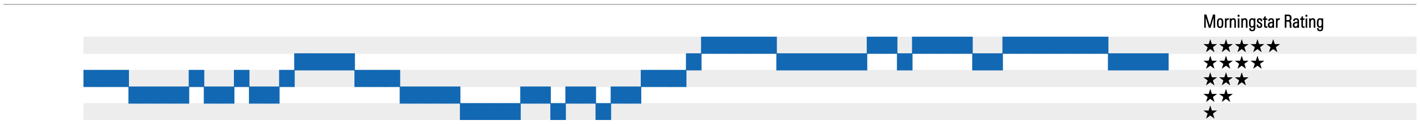
Nike Inc Class B NKE ★★★★★ 19 Dec 2024 22:40, UTC

Competitors Price vs. Fair Value

Under Armour Inc Class A UAA

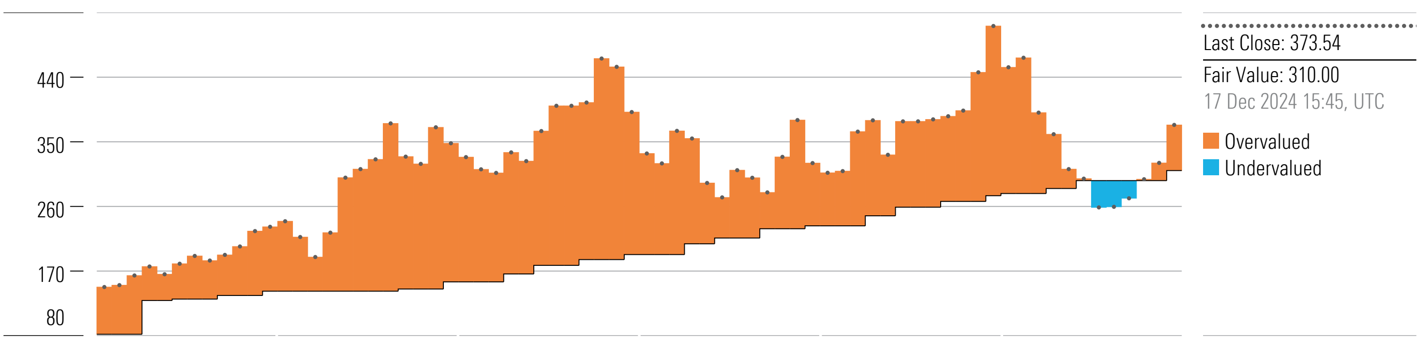


	2019	2020	2021	2022	2023	YTD
Price/Fair Value	1.29	1.42	1.33	0.66	0.57	0.58
Total Return %	22.24	-20.51	23.41	-52.05	-13.48	-4.21

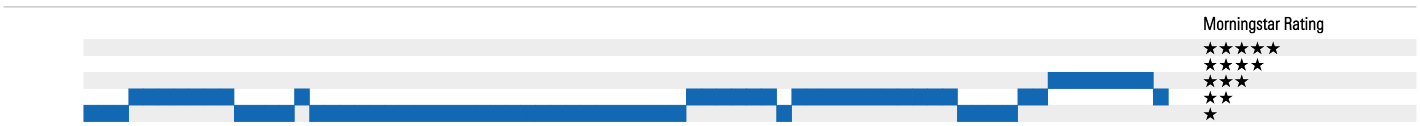


Total Return % as of 19 Dec 2024. Last Close as of 19 Dec 2024. Fair Value as of 25 Nov 2024 05:23, UTC.

Lululemon Athletica Inc LULU



	2019	2020	2021	2022	2023	YTD
Price/Fair Value	1.63	2.25	2.03	1.38	1.86	1.21
Total Return %	90.50	50.23	12.48	-18.16	59.59	-26.94



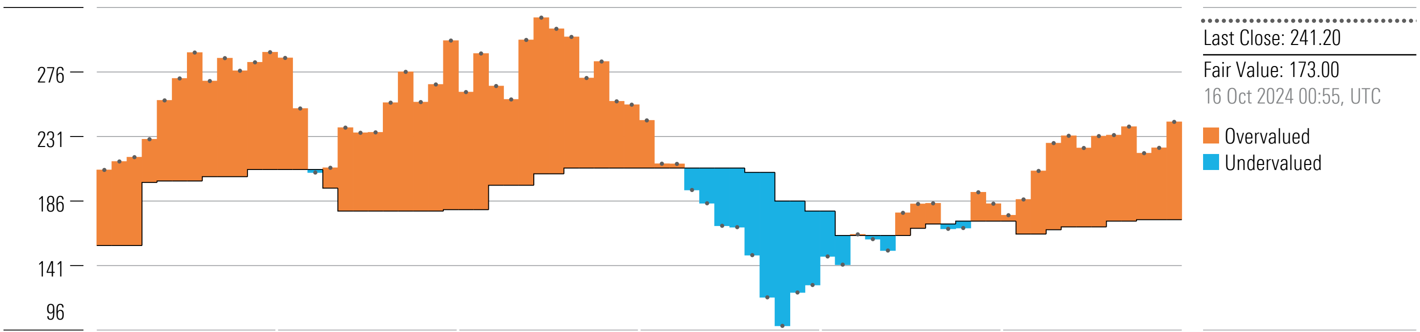
Total Return % as of 19 Dec 2024. Last Close as of 19 Dec 2024. Fair Value as of 17 Dec 2024 15:45, UTC.

Morningstar Equity Analyst Report | Report as of 20 Dec 2024 03:25, UTC | Reporting Currency: USD | Trading Currency: USD | Exchange: NEW YORK STOCK EXCHANGE, INC. Page 15 of 24

Nike Inc Class B NKE ★★★★★ 19 Dec 2024 22:40, UTC

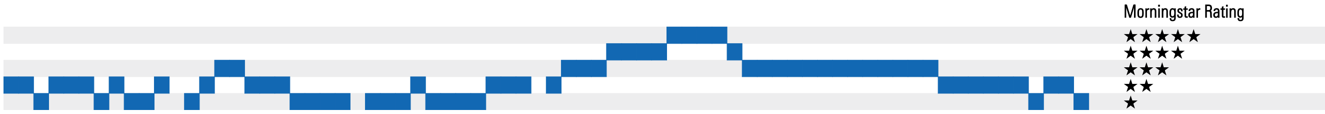
Competitors Price vs. Fair Value

adidas AG ADS



	2019	2020	2021	2022	2023	YTD
Price/Fair Value	1.39	1.66	1.21	0.71	1.07	1.36
Total Return %	60.72	2.80	-14.00	-48.36	45.03	31.35

Morningstar Rating



Total Return % as of 18 Dec 2024. Last Close as of 18 Dec 2024. Fair Value as of 16 Oct 2024 00:55, UTC.

Morningstar Equity Analyst Report | Report as of 20 Dec 2024 03:25, UTC | Reporting Currency: USD | Trading Currency: USD | Exchange: NEW YORK STOCK EXCHANGE, INC. Page 16 of 24

Nike Inc Class B NKE ★★★★★ 19 Dec 2024 22:40, UTC

Last Price	Fair Value Estimate	Price/FVE	Market Cap	Economic Moat™	Equity Style Box	Uncertainty	Capital Allocation	ESG Risk Rating Assessment[1]
77.10 USD 19 Dec 2024	117.00 USD 3 Oct 2024 21:39, UTC	0.66	114.76 USD Bil 19 Dec 2024	Wide	Large Value	Medium	Exemplary	4 Dec 2024 06:00, UTC

Morningstar Historical Summary

Financials as of 31 Aug 2024

Fiscal Year, ends 31 May	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	YTD	TTM
Revenue (USD Bil)	28	31	32	34	36	39	37	45	47	51	12	50
Revenue Growth %	9.8	10.1	5.8	6.1	6.0	7.5	-4.4	19.1	4.9	9.7	-10.4	-2.8
EBITDA (USD Mil)	4,266	4,824	5,164	5,465	5,219	5,492	4,234	7,734	7,515	6,774	1,393	6,758
EBITDA Margin %	15.4	15.8	16.0	15.9	14.3	14.0	11.3	17.4	16.1	13.2	12.0	13.5
Operating Income (USD Mil)	3,680	4,175	4,502	4,749	4,445	4,772	3,115	6,937	6,675	5,915	1,209	5,916
Operating Margin %	13.2	13.6	13.9	13.8	12.2	12.2	8.3	15.6	14.3	11.6	10.4	11.8
Net Income (USD Mil)	2,693	3,273	3,760	4,240	1,933	4,029	2,539	5,727	6,046	5,070	1,051	5,301
Net Margin %	9.7	10.7	11.6	12.3	5.3	10.3	6.8	12.9	12.9	9.9	9.1	10.6
Diluted Shares Outstanding (Mil)	1,812	1,769	1,743	1,692	1,659	1,618	1,592	1,609	1,611	1,570	1,502	1,519
Diluted Earnings Per Share (USD)	1.49	1.85	2.16	2.51	1.17	2.49	1.60	3.56	3.75	3.23	0.70	3.49
Dividends Per Share (USD)	0.47	0.54	0.62	0.70	0.78	0.86	0.96	1.07	1.19	1.33	0.37	1.48

Valuation as of 29 Nov 2024

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Recent Qtr	TTM
Price/Sales	2.9	3.5	2.6	3.0	3.2	4.0	5.9	5.8	3.8	3.3	2.6	2.4
Price/Earnings	28.7	30.3	22.4	27.1	55.9	35.5	80.0	43.7	33.0	31.6	23.7	22.6
Price/Cash Flow	28.9	24.5	26.2	30.6	21.4	32.5	75.8	39.2	42.0	31.1	18.2	15.2
Dividend Yield %	1.04	0.93	1.3	1.18	1.11	0.89	0.71	0.68	1.07	1.28	1.67	1.88
Price/Book	7.1	8.0	6.8	8.6	13.4	16.9	21.0	17.7	11.9	11.6	9.1	8.4
EV/EBITDA	18.7	21.3	15.8	18.3	22.3	29.4	52.9	33.8	24.4	24.6	0.0	0.0

Operating Performance / Profitability as of 31 Aug 2024

Fiscal Year, ends 31 May	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	YTD	TTM
ROA %	14.9	16.3	17.5	19.0	8.4	17.4	9.2	16.6	15.5	13.0	2.8	14.2
ROE %	24.6	27.8	30.1	34.4	17.4	42.7	29.7	55.0	43.1	34.6	7.4	38.0
ROIC %	21.9	25.0	26.6	27.8	13.0	30.8	15.1	24.6	22.6	18.8	4.0	20.3
Asset Turnover	1.5	1.5	1.5	1.5	1.6	1.7	1.4	1.3	1.2	1.3	0.3	1.3

Financial Leverage

Fiscal Year, ends 31 May	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Recent Qtr	TTM
Debt/Capital %	10.0	7.8	14.0	21.9	26.1	27.7	60.5	49.2	43.4	45.6	43.2	—
Equity/Assets %	58.2	58.8	57.3	53.3	43.5	38.1	25.7	33.8	37.9	37.3	36.8	—
Total Debt/EBITDA	0.3	0.3	0.4	0.7	0.7	0.6	3.1	1.7	1.7	1.8	8.7	—
EBITDA/Interest Expense	—	—	—	—	—	—	—	—	—	—	—	—

Morningstar Analyst Historical/Forecast Summary as of 03 Oct 2024

Financials

			Estimates		
Fiscal Year, ends 31 May 2024	2023	2024	2025	2026	2027
Revenue (USD Mil)	51,217	51,362	47,558	50,025	53,084
Revenue Growth %	9.7	0.3	-7.4	5.2	6.1
EBITDA (USD Mil)	6,774	7,172	5,647	6,771	7,745
EBITDA Margin %	13.2	14.0	11.9	13.5	14.6
Operating Income (USD Mil)	5,915	6,311	4,849	5,932	6,855
Operating Margin %	11.6	12.3	10.2	11.9	12.9
Net Income (USD Mil)	5,070	5,700	4,137	4,956	5,714
Net Margin %	9.9	11.1	8.7	9.9	10.8
Diluted Shares Outstanding (Mil)	1,570	1,530	1,496	1,458	1,429
Diluted Earnings Per Share(USD)	3.23	3.73	2.77	3.40	4.00
Dividends Per Share(USD)	1.33	1.45	1.45	1.57	1.76

Forward Valuation

			Estimates		
	2023	2024	2025	2026	2027
Price/Sales	3.1	2.8	2.4	2.3	2.2
Price/Earnings	32.6	25.5	27.8	22.7	19.3
Price/Cash Flow	—	—	—	—	—
Dividend Yield %	1.3	1.5	1.9	2.0	2.3
Price/Book	11.8	10.1	8.6	9.1	8.8
EV/EBITDA	24.1	20.1	20.6	17.2	15.1

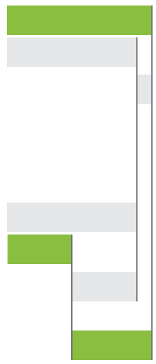
Morningstar Equity Analyst Report | Report as of 20 Dec 2024 03:25, UTC | Reporting Currency: USD | Trading Currency: USD | Exchange: NEW YORK STOCK EXCHANGE, INC. Page 17 of 24

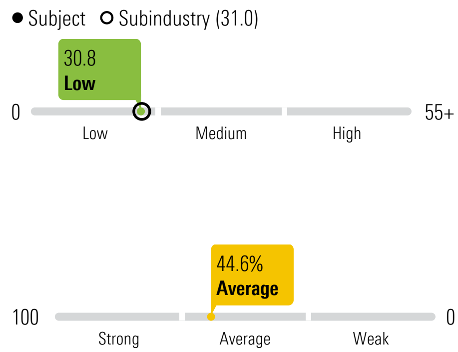
Nike Inc Class B NKE ★★★★★ 19 Dec 2024 22:40, UTC

Last Price	Fair Value Estimate	Price/FVE	Market Cap	Economic Moat™	Equity Style Box	Uncertainty	Capital Allocation	ESG Risk Rating Assessment[1]
77.10 USD 19 Dec 2024	117.00 USD 3 Oct 2024 21:39, UTC	0.66	114.76 USD Bil 19 Dec 2024	Wide	Large Value	Medium	Exemplary	4 Dec 2024 06:00, UTC

ESG Risk Rating Breakdown

Exposure		
Company Exposure[1]	30.8
– Manageable Risk	27.6
Unmanageable Risk[2]	**3.1**
Management		
Manageable Risk	27.6
– Managed Risk[3]	12.3
Management Gap[4]	**15.3**
Overall Unmanaged Risk	**18.4**





- Exposure represents a company's vulnerability to ESG risks driven by their business model
- Exposure is assessed at the Subindustry level and then specified at the company level
- Scoring ranges from 0-55+ with categories of low, medium, and high-risk exposure

- Management measures a company's ability to manage ESG risks through its commitments and actions
- Management assesses a company's efficiency on ESG programs, practices, and policies
- Management score ranges from 0-100% showing how much manageable risk a company is managing

ESG Risk Rating

ESG Risk Ratings measure the degree to which a company's value is impacted by environmental, social, and governance risks, by evaluating the company's ability to manage the ESG risks it faces.

1. A company's Exposure to material ESG issues 2. Unmanageable Risk refers to risks that are inherent to a particular business model that cannot be managed by programs or initiatives 3. Managed Risk = Manageable Risk multiplied by a Management score of 44.6% 4. Management Gap assesses risks that are not managed, but are considered manageable 5. ESG Risk Rating Assessment = Overall Unmanaged Risk = Management Gap plus Unmanageable Risk

ESG Risk Rating Assessment[5]

ESG Risk Rating is of Dec 04, 2024. Highest Controversy Level is as of Dec 08, 2024. Sustainalytics Subindustry: Footwear. Sustainalytics provides Morningstar with company ESG ratings and metrics on a monthly basis and as such, the ratings in Morningstar may not necessarily reflect current Sustainalytics' scores for the company. For the most up to date rating and more information, please visit: sustainalytics.com/esg-ratings/.

Peer Analysis 04 Dec 2024

Peers are selected from the company's Sustainalytics-defined Subindustry and are displayed based on the closest market cap values

Company Name	Exposure		Management		ESG Risk Rating	
Nike Inc	30.8 | Low	0 — 55+	44.6 | Average	100 — 0	18.4 | Low	0 — 40+
Under Armour Inc	29.9 | Low	0 — 55+	50.0 | Average	100 — 0	16.3 | Low	0 — 40+
adidas AG	31.5 | Low	0 — 55+	55.4 | Strong	100 — 0	15.9 | Low	0 — 40+
Lululemon Athletica Inc	25.6 | Low	0 — 55+	49.6 | Average	100 — 0	14.1 | Low	0 — 40+
Puma SE	32.5 | Low	0 — 55+	51.6 | Strong	100 — 0	17.5 | Low	0 — 40+

Morningstar Equity Analyst Report | Report as of 20 Dec 2024 03:25, UTC | Reporting Currency: USD | Trading Currency: USD | Exchange: NEW YORK STOCK EXCHANGE, INC. Page 18 of 24

Appendix
Historical Morningstar Rating

Nike Inc Class B NKE 19 Dec 2024 22:40, UTC

Dec 2024	Nov 2024	Oct 2024	Sep 2024	Aug 2024	Jul 2024	Jun 2024	May 2024	Apr 2024	Mar 2024	Feb 2024	Jan 2024
★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★	★★★★	★★★★	★★★★	★★★★
Dec 2023	Nov 2023	Oct 2023	Sep 2023	Aug 2023	Jul 2023	Jun 2023	May 2023	Apr 2023	Mar 2023	Feb 2023	Jan 2023
★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★	★★★	★★★	★★★
Dec 2022	Nov 2022	Oct 2022	Sep 2022	Aug 2022	Jul 2022	Jun 2022	May 2022	Apr 2022	Mar 2022	Feb 2022	Jan 2022
★★★★	★★★★	★★★★★	★★★★★	★★★★	★★★★	★★★★	★★★★	★★★	★★★	★★★	★★
Dec 2021	Nov 2021	Oct 2021	Sep 2021	Aug 2021	Jul 2021	Jun 2021	May 2021	Apr 2021	Mar 2021	Feb 2021	Jan 2021
★★	★★	★★	★★	★★	★★	★★	★★	★★★	★★	★★	★★
Dec 2020	Nov 2020	Oct 2020	Sep 2020	Aug 2020	Jul 2020	Jun 2020	May 2020	Apr 2020	Mar 2020	Feb 2020	Jan 2020
★★	★★	★★	★★	★★★	★★★	★★★	★★★	★★★★	★★★★	★★★★	★★★
Dec 2019	Nov 2019	Oct 2019	Sep 2019	Aug 2019	Jul 2019	Jun 2019	May 2019	Apr 2019	Mar 2019	Feb 2019	Jan 2019
★★★	★★★	★★★	★★★	★★★★	★★★★	★★★★	★★★★	★★★	★★★	★★★	★★★

Under Armour Inc Class A UAA 19 Dec 2024 22:41, UTC

Dec 2024	Nov 2024	Oct 2024	Sep 2024	Aug 2024	Jul 2024	Jun 2024	May 2024	Apr 2024	Mar 2024	Feb 2024	Jan 2024
★★★★	★★★★	★★★★	★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★
Dec 2023	Nov 2023	Oct 2023	Sep 2023	Aug 2023	Jul 2023	Jun 2023	May 2023	Apr 2023	Mar 2023	Feb 2023	Jan 2023
★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★	★★★★★	★★★★★	★★★★	★★★★	★★★★	★★★★
Dec 2022	Nov 2022	Oct 2022	Sep 2022	Aug 2022	Jul 2022	Jun 2022	May 2022	Apr 2022	Mar 2022	Feb 2022	Jan 2022
★★★★	★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★	★★★	★★★	★★★	★★
Dec 2021	Nov 2021	Oct 2021	Sep 2021	Aug 2021	Jul 2021	Jun 2021	May 2021	Apr 2021	Mar 2021	Feb 2021	Jan 2021
★★	★	★★	★★	★	★★	★★	★	★	★	★	★★
Dec 2020	Nov 2020	Oct 2020	Sep 2020	Aug 2020	Jul 2020	Jun 2020	May 2020	Apr 2020	Mar 2020	Feb 2020	Jan 2020
★★	★★	★★	★★★	★★★	★★★	★★★★	★★★★	★★★★	★★★★	★★★	★★
Dec 2019	Nov 2019	Oct 2019	Sep 2019	Aug 2019	Jul 2019	Jun 2019	May 2019	Apr 2019	Mar 2019	Feb 2019	Jan 2019
★★	★★★	★★	★★	★★★	★★	★★	★★	★★	★★★	★★★	★★★

Lululemon Athletica Inc LULU 19 Dec 2024 22:43, UTC

Dec 2024	Nov 2024	Oct 2024	Sep 2024	Aug 2024	Jul 2024	Jun 2024	May 2024	Apr 2024	Mar 2024	Feb 2024	Jan 2024
★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★	★★	★	★
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★	★	★★	★★	★★	★★	★★	★★	★★	★★	★★	★★
Dec 2022	Nov 2022	Oct 2022	Sep 2022	Aug 2022	Jul 2022	Jun 2022	May 2022	Apr 2022	Mar 2022	Feb 2022	Jan 2022
★★	★	★★	★★	★★	★★	★★	★★	★	★	★	★
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★	★	★	★	★	★	★	★	★	★★	★	★
Dec 2019	Nov 2019	Oct 2019	Sep 2019	Aug 2019	Jul 2019	Jun 2019	May 2019	Apr 2019	Mar 2019	Feb 2019	Jan 2019
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Dec 2024 ★	Nov 2024 ★★	Oct 2024 ★★	Sep 2024 ★	Aug 2024 ★★	Jul 2024 ★★	Jun 2024 ★★	May 2024 ★★	Apr 2024 ★★	Mar 2024 ★★	Feb 2024 ★★★	Jan 2024 ★★★
Dec 2023 ★★★	Nov 2023 ★★★	Oct 2023 ★★★	Sep 2023 ★★★	Aug 2023 ★★★	Jul 2023 ★★★	Jun 2023 ★★★	May 2023 ★★★	Apr 2023 ★★★	Mar 2023 ★★★	Feb 2023 ★★★	Jan 2023 ★★★★
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Dec 2021 —	Nov 2021 ★★	Oct 2021 ★★	Sep 2021 ★★	Aug 2021 ★	Jul 2021 ★	Jun 2021 ★	May 2021 ★	Apr 2021 ★★	Mar 2021 ★	Feb 2021 ★	Jan 2021 ★
Dec 2020 —	Nov 2020 ★	Oct 2020 ★	Sep 2020 ★	Aug 2020 ★	Jul 2020 ★★	Jun 2020 ★★	May 2020 ★★	Apr 2020 ★★★	Mar 2020 ★★★	Feb 2020 ★★	Jan 2020 ★
Dec 2019 —	Nov 2019 ★★	Oct 2019 ★	Sep 2019 ★	Aug 2019 ★★	Jul 2019 ★	Jun 2019 ★★	May 2019 ★★	Apr 2019 ★★	Mar 2019 ★	Feb 2019 ★★	Jan 2019 ★★

Research Methodology for Valuing Companies

Overview

At the heart of our valuation system is a detailed projection of a company's future cash flows, resulting from our analysts' research. Analysts create custom industry and company assumptions to feed income statement, balance sheet, and capital investment assumptions into our globally standardized, proprietary discounted cash flow, or DCF, modeling templates. We use scenario analysis, indepth competitive advantage analysis, and a variety of other analytical tools to augment this process. Moreover, we think analyzing valuation through discounted cash flows presents a better lens for viewing cyclical companies, high-growth firms, businesses with finite lives (e.g., mines), or companies expected to generate negative earnings over the next few years. That said, we don't dismiss multiples altogether but rather use them as supporting cross-checks for our DCF-based fair value estimates. We also acknowledge that DCF models offer their own challenges (including a potential proliferation of estimated inputs and the possibility that the method may miss shortterm market-price movements), but we believe these negatives are mitigated by deep analysis and our longterm approach.

Morningstar's equity research group ("we," "our") believes that a company's intrinsic worth results from the future cash flows it can generate. The Morningstar Rating for stocks identifies stocks trading at a discount or premium to their intrinsic worth—or fair value estimate, in Morningstar terminology. Five-star stocks sell for the biggest risk adjusted discount to their fair values, whereas 1-star stocks trade at premiums to their intrinsic worth.

Four key components drive the Morningstar rating: (1) our assessment of the firm's economic moat, (2) our estimate of the stock's fair value, (3) our uncertainty around that fair value estimate and (4) the current market price. This process ultimately culminates in our singlepoint star rating.

1. Economic Moat

The concept of an economic moat plays a vital role not only in our qualitative assessment of a firm's long-term investment potential, but also in the actual calculation of our fair value estimates. An economic moat is a structural feature that allows a firm to sustain excess profits over a long period of time. We define economic profits as returns on invested capital (or ROIC) over and above our estimate of a firm's cost of capital, or weighted average cost of capital (or WACC). Without a moat, profits are more susceptible to competition. We have identified five sources of economic moats: intangible assets, switching costs, network effect, cost advantage, and efficient scale.

Companies with a narrow moat are those we believe are more likely than not to achieve normalized excess returns for at least the next 10 years. Wide-moat companies are those in which we have very high confidence that excess returns will remain for 10 years, with excess returns more likely than not to remain for at least 20 years. The longer a firm generates economic profits, the higher its intrinsic value. We believe low-quality, no-moat companies will see their normalized returns gravitate toward the firm's cost of capital more quickly than companies with moats.

When considering a company's moat, we also assess whether there is a substantial threat of value destruction, stemming from risks related to ESG, industry disruption, financial health, or other idiosyncratic issues. In this context, a risk is considered potentially value destructive if its occurrence would eliminate a firm's economic profit on a cumulative or midcycle basis. If we deem the probability of occurrence sufficiently high, we would not characterize the company as possessing an economic moat.

2. Estimated Fair Value

Combining our analysts' financial forecasts with the firm's economic moat helps us assess how long returns on invested capital are likely to exceed the firm's cost of capital. Returns of firms with a wide economic moat rating are assumed to fade to the perpetuity period over a longer period of time than the returns of narrow-moat firms, and both will fade slower than no-moat firms, increasing our estimate of their intrinsic value.

Our model is divided into three distinct stages:

Stage I: Explicit Forecast

In this stage, which can last five to 10 years, analysts make full financial statement forecasts, including items such as revenue, profit margins, tax rates, changes in workingcapital accounts, and capital spending. Based on these projections, we calculate earnings before interest, after taxes (EBI) and the net new investment (NNI) to derive our annual free cash flow forecast.

Stage II: Fade

The second stage of our model is the period it will take the company's return on new invested capital—the return on capital of the next dollar invested ("RONIC")—to decline (or rise) to its cost of capital. During the Stage II period, we use a formula to approximate cash flows in lieu of explicitly modeling the income statement, balance sheet, and cash flow statement as we do in Stage I. The length of the second stage depends on the strength of the company's economic moat. We forecast this period to last anywhere from one year (for companies with no economic moat) to 10–15 years or more (for wide-moat companies). During this period, cash flows are forecast using four assumptions: an average growth rate for EBI over the period, a normalized investment rate, average return on new invested capital (RONIC), and the number of years until perpetuity, when excess returns cease. The investment rate and return on new invested capital decline until a perpetuity value is calculated. In the case of firms that do not earn their cost of capital, we assume marginal ROICs rise to the firm's cost of capital (usually attributable to less reinvestment), and we may truncate the second stage.

Stage III: Perpetuity

Once a company's marginal ROIC hits its cost of capital, we calculate a continuing value, using a standard perpetuity formula. At perpetuity, we assume that any growth or decline or investment in the business neither creates nor destroys value and that any new investment provides a return in line with estimated WACC.

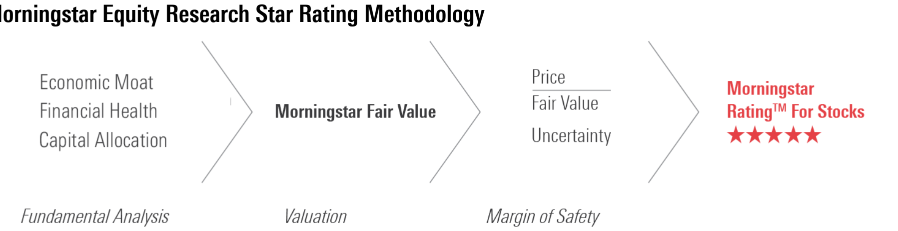
Because a dollar earned today is worth more than a dollar earned tomorrow, we discount our projections of cash flows in stages I, II, and III to arrive at a total present value of expected future cash flows. Because we are modeling free cash flow to the firm—representing cash available to provide a return to all capital providers—we discount future cash flows using the WACC, which is a weighted average of the costs of equity, debt, and preferred stock (and any other funding sources), using expected future proportionate long-term, market-value weights.

3. Uncertainty Around That Fair Value Estimate

Morningstar's Uncertainty Rating is designed to capture the range of potential outcomes for a company's intrinsic value. This rating is used to assign the margin of safety required before investing, which in turn explicitly drives our stock star rating system. The Uncertainty Rating is aimed at identifying the confidence we should have in assigning a fair value estimate for a given stock.

Our Uncertainty Rating is meant to take into account anything that can increase the potential dispersion of future outcomes for the intrinsic value of a company, and any-

Morningstar Equity Research Star Rating Methodology



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thing that can affect our ability to accurately predict these outcomes. The rating begins with a suggested rating produced by a quantitative process based on the trailing 12-month standard deviation of daily stock returns. An analyst overlay is then applied, with analysts using the suggested rating, historical rating data, and their own knowledge of the company to inform them as they make the final Uncertainty Rating decision. Ultimately, the rating decision rests with the analyst. Analysts take into account many characteristics when making their final decision, including cyclical factors, operational and financial factors such as leverage, company-specific events, ESG risks, and anything else that might increase the potential dispersion of future outcomes and our ability to estimate those outcomes.

Our recommended margin of safety—the discount to fair value demanded before we'd recommend buying or selling the stock—widens as our uncertainty of the estimated value of the equity increases. The more uncertain we are about the potential dispersion of outcomes, the greater the discount we require relative to our estimate of the value of the firm before we would recommend the purchase of the shares. In addition, the Uncertainty Rating provides guidance in portfolio construction based on risk tolerance.

Our Uncertainty Ratings are: Low, Medium, High, Very High, and Extreme.

	Margin of Safety	
Qualitative Analysis Uncertainty Ratings	★★★★★Rating	★Rating
Low	20% Discount	25% Premium
Medium	30% Discount	35% Premium
High	40% Discount	55% Premium
Very High	50% Discount	75% Premium
Extreme	75% Discount	300% Premium

Our uncertainty rating is based on the interquartile range, or the middle 50% of potential outcomes, covering the 25th percentile–75th percentile. This means that when a stock hits 5 stars, we expect there is a 75% chance that the intrinsic value of that stock lies above the current market price. Similarly, when a stock hits 1 star, we expect there is a 75% chance that the intrinsic value of that stock lies below the current market price.

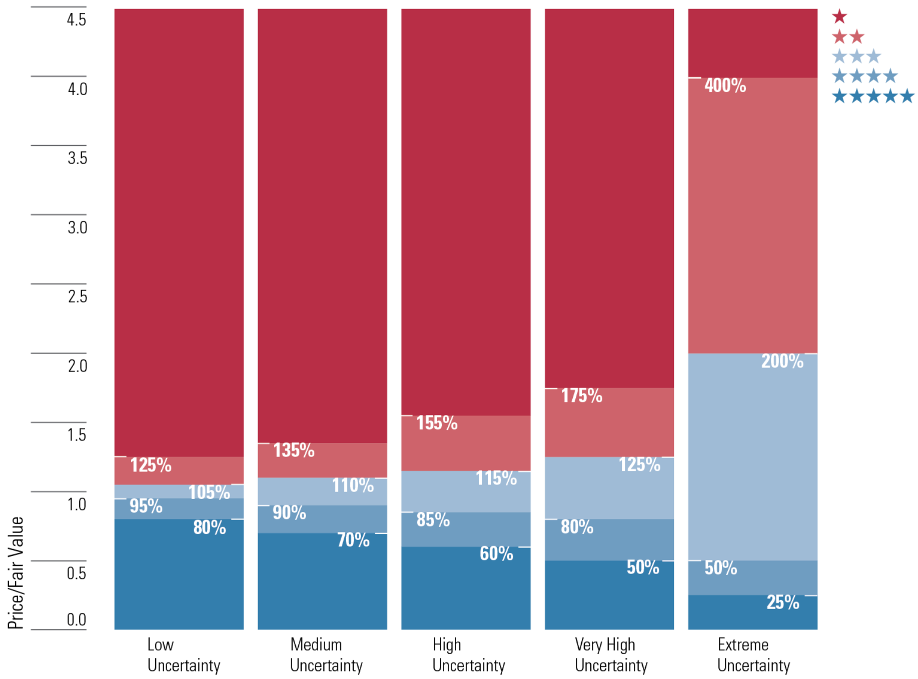
4. Market Price

The market prices used in this analysis and noted in the report come from exchange on which the stock is listed which we believe is a reliable source.

For more details about our methodology, please go to https://shareholders.morningstar.com

Morningstar Star Rating for Stocks

Morningstar Equity Research Star Rating Methodology



Once we determine the fair value estimate of a stock, we compare it with the stock's current market price on a daily basis, and the star rating is automatically re-calculated at the market close on every day the market on which the stock is listed is open. Our analysts keep close tabs on the companies they follow, and, based on thorough and ongoing analysis, raise or lower their fair value estimates as warranted.

Please note, there is no predefined distribution of stars. That is, the percentage of stocks that earn 5 stars can fluctuate daily, so the star ratings, in the aggregate, can serve as a gauge of the broader market's valuation. When there are many 5-star stocks, the stock market as a whole is more undervalued, in our opinion, than when very few companies garner our highest rating.

We expect that if our base-case assumptions are true the market price will converge on our fair value estimate over time generally within three years (although it is impossible to predict the exact time frame in which market prices may adjust).

Our star ratings are guideposts to a broad audience and individuals must consider their own specific investment goals, risk tolerance, tax situation, time horizon, income needs, and complete investment portfolio, among other factors.

The Morningstar Star Ratings for stocks are defined below:

★★★★★ We believe appreciation beyond a fair risk adjusted return is highly likely over a multiyear time frame. Scenario analysis developed by our analysts indicates that the current market price represents an excessively pessimistic outlook, limiting downside risk and maximizing upside potential.

★★★★ We believe appreciation beyond a fair risk-adjusted return is likely.

★★★ Indicates our belief that investors are likely to receive a fair risk-adjusted return (approximately cost of equity).

★★ We believe investors are likely to receive a less than fair risk-adjusted return.

★ Indicates a high probability of undesirable risk-adjusted returns from the current market price over a multiyear time frame, based on our analysis. Scenario analysis by our analysts indicates that the market is pricing in an excessively optimistic outlook, limiting upside potential and leaving the investor exposed to Capital loss.

Other Definitions

Last Price: Price of the stock as of the close of the market of the last trading day before date of the report.

Capital Allocation Rating: Our Capital Allocation (or Stewardship) Rating represents our assessment of the quality of management's capital allocation, with particular emphasis on the firm's balance sheet, investments, and shareholder distributions. Analysts consider compan-

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ies' investment strategy and valuation, balance sheet management, and dividend and share buyback policies. Corporate governance factors are only considered if they are likely to materially impact shareholder value, though either the balance sheet, investment, or shareholder distributions. Analysts assign one of three ratings: "Exemplary", "Standard", or "Poor". Analysts judge Capital Allocation from an equity holder's perspective. Ratings are determined on a forward looking and absolute basis. The Standard rating is most common as most managers will exhibit neither exceptionally strong nor poor capital allocation.

Capital Allocation (or Stewardship) analysis published prior to Dec. 9, 2020, was determined using a different process. Beyond investment strategy, financial leverage, and dividend and share buyback policies, analysts also considered execution, compensation, related party transactions, and accounting practices in the rating.

Capital Allocation Rating: Our Capital Allocation (or Stewardship) Rating represents our assessment of the quality of management's capital allocation, with particular emphasis on the firm's balance sheet, investments, and shareholder distributions. Analysts consider companies' investment strategy and valuation, balance sheet management, and dividend and share buyback policies. Corporate governance factors are only considered if they are likely to materially impact shareholder value, though either the balance sheet, investment, or shareholder distributions. Analysts assign one of three ratings: "Exemplary", "Standard", or "Poor". Analysts judge Capital Allocation from an equity holder's perspective. Ratings are determined on a forward looking and absolute basis. The Standard rating is most common as most managers will exhibit neither exceptionally strong nor poor capital allocation.

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Sustainalytics ESG Risk Rating Assessment: The ESG Risk Rating Assessment is provided by Sustainalytics; a Morningstar company.

Sustainalytics' ESG Risk Ratings measure the degree to which company's economic value at risk is driven by environment, social and governance (ESG) factors.

Sustainalytics analyzes over 1,300 data points to assess a company's exposure to and management of ESG risks. In other words, ESG Risk Ratings measures a company's unmanaged ESG Risks represented as a quantitative score. Unmanaged Risk is measured on an open-ended scale starting at zero (no risk) with lower scores representing less unmanaged risk and, for 95% of cases, the unmanaged ESG Risk score is below 50.

Based on their quantitative scores, companies are grouped into one of five Risk Categories (negligible, low, medium, high, severe). These risk categories are absolute, meaning that a 'high risk' assessment reflects a comparable degree of unmanaged ESG risk across all subindustries covered.

The ESG Risk Rating Assessment is a visual representation of Sustainalytics ESG Risk Categories on a 1 to 5 scale. Companies with Negligible Risk = 5 Globes, Low Risk = 4, Medium Risk = 3 Globes, High Risk = 2 Globes, Severe Risk = 1 Globe. For more information, please visit sustainalytics.com/esg-ratings/

Ratings should not be used as the sole basis in evaluating a company or security. Ratings involve unknown risks and uncertainties which may cause our expectations not to occur or to differ significantly from what was expected and should not be considered an offer or solicitation to buy or sell a security.

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