

THE GAP, INC	Ticker: BDC	Analyst: Lvovich	Today	7/31/22
Gap, Inc operates as a global apparel & retail company, offering clothing, accessories and personal care products for men, women, and children. The firm operates through following segments: Gap Global, Old Navy Global, Banana Republic Global, Athleta and Other.				
Company founded by Donald and Doris Fisher in 1969 and is HQ'd in San Francisco, CA. It runs operations via 2,800 co' operated and 550 franchised stores in Unites States, Canada, Japan, Italy, China, Taiwan and Mexico. Annual revenue reached over \$16.5bn in 2021. Nearly 40% of sales are done through online channel.				

CAPITAL STRUCTURE (\$mm) As of: December 2021 (4Q'21)															
Issue	Par Amount	Maturity	Coupon	Ratings	Price	YTW	YTC	CY	LTM Lvrg	Y+3 Lvrg	Next Call	Call Price	Fund A	Fund B	Fund C
Cash	845														
ST Investments	-														
RC, ABL \$1.8765bn, 05/23, L+200	350	May-23	4.780%									101.8	\$ -	\$ -	\$ -
Total Secured Debt	350														
'29 Sr Notes, 3.625%, 10/1/29	750	Oct-29	3.625%	Ba3 / BB	73.3	8.70%	20.05%	4.95%	1.1x	1.4x	Oct-24	101.8	\$ -	\$ -	\$ -
'31 Sr Notes, 3.875%, 10/1/31	750	Oct-31	3.875%	Ba3 / BB	72.0	8.29%	13.17%	5.38%	1.1x	1.4x	Oct-26	101.9	\$ -	\$ -	\$ -
Other	-														
Total Debt	1,850														
POSITION: RC, ABL \$1.8765bn: \$ - '29 Sr Notes: \$ - '31 Sr Notes: \$ - GPS: \$ -															
Net Debt	1,005								1.1x	1.4x					
Equity (Pref + Common)	3,277														
EV	4,282								4.8x	6.0x					
LIQUIDITY															
				Cash	Avail RC	Total									
				845	1,527	2,372									
LTM EBITDA	912														
LIBOR	2.78%			original corp rt:	B1/B										

INVESTMENT RATIONALE

I am HOLD on both '29 and '31 going into the 2Q'22 Earnings Call.
<p>YTW is >8.5% or about 50bps above HY market. Which is attractive on the surface provided very low leverage and LTV metrics.</p> <p>However, I do expect announcement of further operational weakness. That could put even more technical pressure on the notes. With further negative revisions the credit could trade lower toward double digit territory.</p> <ul style="list-style-type: none"> - I would like to see how much progress the company is making on decreasing its Inventory levels. - Upon further weakness in the trading levels, GPS notes could be upgraded to BUY later in August - September timeframe. - Overall leverage and LTV here are very manageable (sub 1.5x Net Leverage and 25%). '23 EBITDA multiples on stressed companies seem to be centering around 3.0 to 4.5x. Hence GPS leverage implied no impairment to the notes. - There is structural coverage (though not collateralized) from RE portfolio assets coupled with profitable Athleta and Banana Republic retailing brands. Ownership has proven to be conservative regarding leverage policy. - Long term, I can see return of success to Old Navy brand. It is a great value proposition and should do well attracting middle-income buyers looking to save in tougher economic times. Credit has plentiful liquidity to sustain itself as it is dealing with resolving current issues.

SEGMENT SUMMARY

	2018	2019	2020	2021	LTM	E'2022	E'2023
BRAND SEGMENTS							
Old Navy	7,840	7,983	7,536	9,082	8,643	8,538	8,111
Gap	5,160	4,634	3,388	4,063	3,968	3,979	3,899
Banana Republic	2,456	2,539	1,462	1,976	2,069	2,332	2,565
Athleta	-	978	1,135	1,447	1,460	1,505	1,580
Other	1,124	249	279	102	16	16	17
Total Sales	16,580	16,383	13,800	16,670	16,156	16,370	16,173
COGS & OccupancyX	(10,258)	(10,250)	(9,095)	(10,033)	(10,053)	(10,706)	(10,270)
Gross Profit	6,322	6,133	4,705	6,637	6,103	5,664	5,903
Cash OpX	(4,380)	(4,677)	(4,503)	(5,224)	(5,191)	(5,176)	(5,094)
adj EBITDA	1,942	1,456	202	1,413	912	491	809
YoY Δ in Sales by Brand							
Old Navy, YoY	8%	2%	-6%	21%		-6%	-5%
Gap, YoY	-3%	-10%	-27%	20%		-2%	-2%
Banana Republic, YoY	3%	3%	-42%	35%		18%	10%
Athleta & Other, YoY	22%	9%	15%	10%		4%	5%
YoY Δ in Sales	5%	-1%	-16%	21%		-2%	-1%
YoY in Merchandise Inventory							
	7%	1%	14%	23%		-15%	-10%
Gross Margin	38.1%	37.4%	34.1%	39.8%	37.8%	34.6%	36.5%
EBITDA margin	11.7%	8.9%	1.5%	8.5%	5.6%	3.0%	5.0%

THE GAP

CASH FLOWS

Net sales	15,855	16,580	16,383	13,800	16,670	16,156	16,370	16,173
COGS & OccupancyX	(9,789)	(10,258)	(10,250)	(9,095)	(10,033)	(10,053)	(10,706)	(10,270)
Gross Profit	6,066	6,322	6,133	4,705	6,637	6,103	5,664	5,903
OperatingX	(4,587)	(4,960)	(5,559)	(5,567)	(5,827)	(5,730)	(5,692)	(5,604)
OI	1,479	1,362	574	(862)	810	373	(28)	299
D&A	559	578	557	507	504	514	516	510
EBITDA	2,038	1,940	1,131	(355)	1,314	887	488	809
add Impairment of operating lease assets	-	-	239	391	8	3	-	-
add Impairment of store assets	28	14	98	135	1	4	3	-
add Impaiment of intangible asset	-	-	-	31	-	-	-	-
add back other	-	(12)	(12)	-	90	18	(3)	-
adj EBITDA	2,066	1,942	1,456	202	1,413	912	491	809
less Δ in NWC	(162)	(303)	310	(172)	(467)	(721)	392	79
less CapX	(731)	(705)	(702)	(392)	(694)	(798)	(700)	(725)
less IntX	(74)	(73)	(76)	(192)	(167)	(133)	(75)	(73)
less Taxes	(515)	(254)	(258)	300	(128)	(72)	21	(61)
FCF	584	607	730	(254)	(43)	(812)	129	29
less Debt Paydown	(67)	-	-	943	(1,046)	(696)	350	-
less Stock Repurchase	(315)	(398)	(200)	-	(201)	(255)	(279)	(300)
less Dividends	(361)	(373)	(364)	-	(226)	(191)	(221)	(205)
add back RE sale	-	-	(123)	-	-	333	333	-
NCF	(159)	(164)	43	689	(1,516)	(1,639)	312	(476)

CAPITAL STRUCTURE

Cash	1,783	1,081	1,364	1,988	877	845	1,175	699
ST Investments	-	288	290	410	-	-	-	-
RC, ABL \$1.8765bn, 05/23, L+200	-	-	-	-	-	350	350	350
'23 Sr Sec Notes, 8.375%, 5/15/23	-	-	-	500	-	-	-	-
'25 Sr Sec Notes, 8.625%, 5/15/25	-	-	-	750	-	-	-	-
'27 Sr Sec Notes, 8.875%, 5/15/27	-	-	-	1,000	-	-	-	-
Total Secured Debt	-	-	-	2,250	-	350	350	350
'21 Sr Notes, 5.95%, 4/21	1,249	1,249	1,249	-	-	-	-	-
'29 Sr Notes, 3.625%, 10/1/29	-	-	-	-	750	750	750	750
'31 Sr Notes, 3.875%, 10/1/31	-	-	-	-	750	750	750	750
Total Debt	1,249	1,249	1,249	2,250	1,500	1,850	1,850	1,850
Equity, Mkt Cap	12,864	9,560	2,096	11,523	5,472	3,277	2,273	3,701

shares	389	378	371	374	371	369	339	294
P, \$/sh	\$ 33.07	\$ 25.29	\$ 5.65	\$ 30.81	\$ 14.75	\$ 8.88	\$ 6.71	\$ 12.59

Net Debt	(534)	168	(115)	262	623	1,005	675	1,151
Equity	12,864	9,560	2,096	11,523	5,472	3,277	2,273	3,701
EV	12,330	9,728	1,981	11,785	6,095	4,282	2,948	4,852

CREDIT METRICS

LTM EBITDA	2,066	1,942	1,456	202	1,413	912	491	809
Leverage	0.6x	0.6x	0.9x	11.1x	1.1x	2.1x	3.8x	2.3x
Net Leverage	-0.3x	0.1x	-0.1x	1.3x	0.4x	1.1x	1.4x	1.4x
EV/EBITDA	6.0x	5.0x	1.4x	58.3x	4.3x	4.8x	6.0x	6.0x

LTV	-4%	2%	-6%	2%	10%	23%	23%	24%
Interest Coverage	27.9x	26.6x	19.2x	1.1x	8.5x	6.7x	6.6x	8.1x

Land, buildings, building improvemnts * 1,037 1,123 1,408 1,452 1,416 1,036 1,001

* - before depreciation (up to 39 yrs on RE). All else sub 10yrs

The Gap, Inc - model by Jerry Lvovich

5/4/19	8/3/19	11/2/19	2/1/20	5/2/20	8/1/20	10/31/20	1/30/21	5/1/21	7/31/21	10/30/21	1/29/22	4/30/22	7/31/22	10/31/22	1/31/23
1Q'19	2Q'19	3Q'19	4Q'19	1Q'20	2Q'20	3Q'20	4Q'20	1Q'21	2Q'21	3Q'21	4Q'21	1Q'22	E'2Q'22	E'3Q'22	E'4Q'22
3,706	4,005	3,998	4,674	2,107	3,275	3,994	4,424	3,991	4,211	3,943	4,525	3,477	4,010	4,094	4,789
(2,362)	(2,449)	(2,439)	(3,000)	(1,839)	(2,126)	(2,374)	(2,756)	(2,361)	(2,388)	(2,282)	(3,002)	(2,381)	(2,647)	(2,661)	(3,017)
1,344	1,556	1,559	1,674	268	1,149	1,620	1,668	1,630	1,823	1,661	1,523	1,096	1,363	1,433	1,772
(1,028)	(1,274)	(1,338)	(1,919)	(1,512)	(1,076)	(1,445)	(1,534)	(1,390)	(1,414)	(1,508)	(1,515)	(1,293)	(1,416)	(1,397)	(1,586)
316	282	221	(245)	(1,244)	73	175	134	240	409	153	8	(197)	(53)	36	186
138	139	140	140	130	126	125	126	120	124	128	132	130	133	128	125
454	421	361	(105)	(1,114)	199	300	260	360	533	281	140	(67)	80	164	311
-	-	-	239	360	1	-	30	5	1	-	2	-	-	-	-
-	-	-	98	124	3	-	8	-	1	-	-	3	-	-	-
-	-	-	-	-	-	-	31	-	-	-	-	-	-	-	-
7	3	(3)	(19)	3	(3)	-	-	69	4	7	10	(3)	-	-	-
454	421	361	232	(630)	203	300	329	365	535	281	142	(64)	80	164	311
(199)	198	(345)	656	(602)	793	191	(554)	(78)	14	(390)	(13)	(332)	423	93	208
(165)	(159)	(199)	(179)	(122)	(86)	(80)	(104)	(124)	(145)	(217)	(208)	(228)	(157)	(157)	(157)
(20)	(19)	(19)	(18)	(19)	(58)	(55)	(60)	(54)	(51)	(44)	(18)	(20)	(18)	(18)	(18)
(52)	(80)	(73)	(53)	286	(105)	25	94	(3)	(91)	7	(41)	53	19	(5)	(46)
18	361	(275)	638	(1,087)	747	381	(295)	106	262	(363)	(138)	(591)	346	76	298
-	-	-	-	500	443	-	-	-	-	(1,046)	-	350	-	-	-
(50)	(50)	(50)	(50)	-	-	-	-	-	(55)	(73)	(73)	(54)	(50)	(75)	(100)
(92)	(91)	(91)	(90)	-	-	-	-	(91)	(46)	(45)	(44)	(56)	(55)	(55)	(55)
(123)	-	-	-	-	-	-	-	-	-	-	333	-	-	-	-
(247)	220	(416)	498	(587)	1,190	381	(295)	15	161	(1,527)	(255)	(18)	241	(54)	143

1Q'19	2Q'19	3Q'19	4Q'19	1Q'20	2Q'20	3Q'20	4Q'20	1Q'21	2Q'21	3Q'21	4Q'21	1Q'22	E'2Q'22	E'3Q'22	E'4Q'22
941	1,177	788	1,364	1,028	2,188	2,471	1,988	2,066	2,375	801	877	845	1,086	1,033	1,175
272	294	294	290	51	25	178	410	475	337	275	-	-	-	-	-
-	-	-	-	500	-	-	-	-	-	-	-	350	350	350	350
-	-	-	-	500	500	500	500	500	500	-	-	-	-	-	-
-	-	-	-	750	750	750	750	750	750	-	-	-	-	-	-
-	-	-	-	1,000	1,000	1,000	1,000	1,000	1,000	-	-	-	-	-	-
-	-	-	-	2,750	2,250	2,250	2,250	2,250	2,250	-	-	350	350	350	350
1,249	1,249	1,249	1,249	-	-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-	750	750	750	750	750	750
-	-	-	-	-	-	-	-	-	-	750	750	750	750	750	750

1,249	1,249	1,249	1,249	2,750	2,250	2,250	2,250	2,250	2,250	1,500	1,500	1,850	1,850	1,850	1,850
6,883	6,373	6,069	2,096	4,502	6,552	8,135	11,523	11,913	9,968	6,253	5,472	3,277	3,628	2,080	2,273
378	378	373	371	373	374	374	374	377	376	374	371	369	363	356	339
\$ 18.21	\$ 16.86	\$ 16.27	\$ 5.65	\$ 12.07	\$ 17.52	\$ 21.75	\$ 30.81	\$ 31.60	\$ 26.51	\$ 16.72	\$ 14.75	\$ 8.88	\$ 9.99	\$ 5.85	\$ 6.71

308	72	461	(115)	1,722	62	(221)	262	184	(125)	699	623	1,005	764	817	675
6,883	6,373	6,069	2,096	4,502	6,552	8,135	11,523	11,913	9,968	6,253	5,472	3,277	3,628	2,080	2,273
7,191	6,445	6,530	1,981	6,224	6,614	7,914	11,785	12,097	9,843	6,952	6,095	4,282	4,392	2,898	2,948

1Q'19	2Q'19	3Q'19	4Q'19	1Q'20	2Q'20	3Q'20	4Q'20	1Q'21	2Q'21	3Q'21	4Q'21	1Q'22	E'2Q'22	E'3Q'22	E'4Q'22
2,039	1,922	1,775	1,468	384	166	105	202	1,197	1,529	1,510	1,323	894	439	322	491
0.6x	0.6x	0.7x	0.9x	7.2x	13.6x	21.4x	11.1x	1.9x	1.5x	1.0x	1.1x	2.1x	4.2x	5.7x	3.8x
0.2x	0.0x	0.3x	-0.1x	4.5x	0.4x	-2.1x	1.3x	0.2x	-0.1x	0.5x	0.5x	1.1x	1.7x	2.5x	1.4x
3.5x	3.4x	3.7x	1.3x	16.2x	39.8x	75.4x	58.3x	10.1x	6.4x	4.6x	4.6x	4.8x	10.0x	9.0x	6.0x

4%	1%	7%	-6%	28%	1%	-3%	2%	2%	-1%	10%	10%	23%	17%	28%	23%
26.5x	24.3x	23.1x	19.3x	5.1x	1.5x	0.7x	1.1x	5.3x	7.0x	7.2x	7.9x	6.7x	4.4x	4.3x	6.6x

1,408 1,452 1,416 1,036

THE GAP

DRIVERS

YoY Δ in Sales by Brand

Old Navy, YoY	8%	2%	-6%	21%		-6%	-5%
Gap, YoY	-3%	-10%	-27%	20%		-2%	-2%
Banana Republic, YoY	3%	3%	-42%	35%		18%	10%
Athleta & Other, YoY	22%	9%	15%	10%		4%	5%
YoY Δ in Sales	5%	-1%	-16%	21%		-2%	-1%

YoY in Merchandise Inventory	7%	1%	14%	23%		-15%	-10%
Merchandise Inventory	2,131	2,156	2,451	3,018		2,565	2,206

YoY Δ in Sales	725	(197)	(2,583)	2,870
Δ in NWC	(303)	310	(172)	(467)
Δ in NWC / YoY Δ in Sales	-42%	-157%	7%	-16%

Margins

COGS & Occupancy X, % of Sales	-61.7%	-61.9%	-62.6%	-65.9%	-60.2%	-62.2%	-65.4%	-63.5%
Gross Margin	38.3%	38.1%	37.4%	34.1%	39.8%	37.8%	34.6%	36.5%
OpX cash, % Sales	-25.2%	-26.4%	-28.5%	-32.6%	-31.3%	-32.1%	-31.6%	-31.5%
EBITDA margin	13.0%	11.7%	8.9%	1.5%	8.5%	5.6%	3.0%	5.0%

D&A, % of Sales	-3.5%	-3.5%	-3.4%	-3.7%	-3.0%		-3.2%	-3.2%
adj OI margin (mngt guidance)	9.5%	8.2%	5.5%	-2.2%	5.5%		-0.2%	1.8%

CapX	(731)	(705)	(702)	(392)	(694)			(725)
Tax Rate	-40%	-24%	-34%	-40%	-21%		-23%	-27%
Stock Repurchase	(315)	(398)	(200)	-	(201)			(300)
Dividend	(361)	(373)	(364)	-	(226)			(205)

SEGMENTS

Channel

Store Sales			12,294	7,522	10,239	9,992	10,131	10,027
Online Sales			4,089	6,278	6,431	6,164	6,239	6,146
Total Sales			16,383	13,800	16,670	16,156	16,370	16,173
			25%	45%	39%		38%	38%

Brand Sales

Old Navy	7,238	7,840	7,983	7,536	9,082	8,643	8,538	8,111
Gap	5,318	5,160	4,634	3,388	4,063	3,968	3,979	3,899
Banana Republic	2,380	2,456	2,539	1,462	1,976	2,069	2,332	2,565
Athleta			978	1,135	1,447	1,460	1,505	1,580
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OperatingX	(4,587)	(4,960)	(5,559)	(5,567)	(5,827)	(5,730)	(5,692)	(5,604)
OI	1,479	1,362	574	(862)	810	373	(28)	299
loss extinguishment of debt	-	-	-	(58)	(325)	(325)	-	-
IntX	(74)	(73)	(76)	(192)	(167)	(133)	(75)	(73)
Interest Income	19	33	30	10	5	5	4	1
Income before income taxes	1,424	1,322	528	(1,102)	323	(80)	(98)	227
Income taxes	(576)	(319)	(177)	437	(67)	8	22	(61)
Net income	848	1,003	351	(665)	256	(72)	(76)	165

The Gap, Inc - model by Jerry Lvovich

5/4/19	8/3/19	11/2/19	2/1/20	5/2/20	8/1/20	10/31/20	1/30/21	5/1/21	7/31/21	10/30/21	1/29/22	4/30/22	7/31/22	10/31/22	1/31/23
1Q'19	2Q'19	3Q'19	4Q'19	1Q'20	2Q'20	3Q'20	4Q'20	1Q'21	2Q'21	3Q'21	4Q'21	1Q'22	E'2Q'22	E'3Q'22	E'4Q'22
3%	-1%	0%	5%	-42%	-5%	15%	5%	120%	27%	-6%	-3%	-19%	-10%	2%	4%
-13%	-11%	-10%	-8%	-50%	-28%	-14%	-19%	69%	24%	5%	7%	-11%	-7%	2%	5%
1%	2%	3%	7%	-49%	-54%	-38%	-32%	35%	75%	24%	22%	24%	20%	15%	15%
6%	25%	7%	1%	-11%	-1%	36%	37%	70%	7%	-14%	-4%	-17%	2%	5%	5%
-2%	-2%	-2%	1%	-43%	-18%	0%	-5%	89%	29%	-1%	2%	-13%	-5%	4%	6%

10%	6%	2%	1%	-1%	-4%	1%	14%	7%	2%	-1%	23%	34%	25%	10%	-15%
2,242	2,326	2,720	2,156	2,217	2,242	2,747	2,451	2,370	2,281	2,721	3,018	3,169	2,851	2,993	2,565

-63.7%	-61.1%	-61.0%	-64.2%	-87.3%	-64.9%	-59.4%	-62.3%	-59.2%	-56.7%	-57.9%	-66.3%	-68.5%	-66.0%	-65.0%	-63.0%
36.3%	38.9%	39.0%	35.8%	12.7%	35.1%	40.6%	37.7%	40.8%	43.3%	42.1%	33.7%	31.5%	34.0%	35.0%	37.0%
-24.0%	-28.3%	-30.0%	-30.9%	-42.6%	-28.9%	-33.0%	-30.3%	-31.7%	-30.6%	-35.0%	-30.5%	-33.4%	-32.0%	-31.0%	-30.5%
12.3%	10.5%	9.0%	5.0%	-29.9%	6.2%	7.5%	7.4%	9.1%	12.7%	7.1%	3.1%	-1.8%	2.0%	4.0%	6.5%
-3.7%	-3.5%	-3.5%	-3.0%	-6.2%	-3.8%	-3.1%	-2.8%	-3.0%	-2.9%	-3.2%	-2.9%	-3.7%	-3.3%	-3.1%	-2.6%
8.5%	7.0%	5.5%	2.0%	-36.1%	2.4%	4.4%	4.6%	6.1%	9.8%	3.9%	0.2%	-5.6%	-1.3%	0.9%	3.9%

(165)	(159)	(199)	(179)	(122)	(86)	(80)	(104)	(124)	(145)	(217)	(208)	(228)	(157)	(157)	(157)
-24%	-27%	-29%	-34%	-22%	-23%	-24%	-40%	26%	1%	24%	-21%	-10%	-27%	-27%	-27%
(50)	(50)	(50)	(50)	-	-	-	-	-	(55)	(73)	(73)	(54)	(50)	(75)	(100)
(92)	(91)	(91)	(90)	-	-	-	-	(91)	(46)	(45)	(44)	(56)	(55)	(55)	(55)

1Q'19	2Q'19	3Q'19	4Q'19	1Q'20	2Q'20	3Q'20	4Q'20	1Q'21	2Q'21	3Q'21	4Q'21	1Q'22	E'2Q'22	E'3Q'22	E'4Q'22
2,823	3,166	2,992	3,313	1,108	1,642	2,379	2,393	2,384	2,828	2,456	2,571	2,137	2,486	2,538	2,969
883	839	1,006	1,361	999	1,633	1,615	2,031	1,607	1,383	1,487	1,954	1,340	1,524	1,556	1,820
3,706	4,005	3,998	4,674	2,107	3,275	3,994	4,424	3,991	4,211	3,943	4,525	3,477	4,010	4,094	4,789
24%	21%	25%	29%	47%	50%	40%	46%	40%	33%	38%	43%	39%	38%	38%	38%

1,799	1,972	1,947	2,265	1,038	1,881	2,242	2,375	2,280	2,390	2,105	2,307	1,841	2,151	2,147	2,399
1,052	1,086	1,158	1,338	524	783	993	1,088	886	974	1,039	1,164	791	906	1,060	1,222
568	616	618	737	289	283	386	504	389	495	479	613	482	594	551	705
	-	-	978	-	267	292	576	347	341	320	439	360	348	336	461
287	331	275	(644)	256	61	81	(119)	89	11	-	2	3	11	-	2
3,706	4,005	3,998	4,674	2,107	3,275	3,994	4,424	3,991	4,211	3,943	4,525	3,477	4,010	4,094	4,789

1Q'19	2Q'19	3Q'19	4Q'19	1Q'20	2Q'20	3Q'20	4Q'20	1Q'21	2Q'21	3Q'21	4Q'21	1Q'22	E'2Q'22	E'3Q'22	E'4Q'22
3,706	4,005	3,998	4,674	2,107	3,275	3,994	4,424	3,991	4,211	3,943	4,525	3,477	4,010	4,094	4,789
(2,362)	(2,449)	(2,439)	(3,000)	(1,839)	(2,126)	(2,374)	(2,756)	(2,361)	(2,388)	(2,282)	(3,002)	(2,381)	(2,647)	(2,661)	(3,017)
1,344	1,556	1,559	1,674	268	1,149	1,620	1,668	1,630	1,823	1,661	1,523	1,096	1,363	1,433	1,772
(1,028)	(1,274)	(1,338)	(1,919)	(1,512)	(1,076)	(1,445)	(1,534)	(1,390)	(1,414)	(1,508)	(1,515)	(1,293)	(1,416)	(1,397)	(1,586)
316	282	221	(245)	(1,244)	73	175	134	240	409	153	8	(197)	(53)	36	186
-	-	-	-	-	(58)	-	-	-	-	(325)	-	-	-	-	-
(20)	(19)	(19)	(18)	(19)	(58)	(55)	(60)	(54)	(51)	(44)	(18)	(20)	(18)	(18)	(18)
6	8	7	9	4	2	1	3	1	1	1	2	1	1	1	1
302	271	209	(254)	(1,259)	(41)	121	77	187	359	(215)	(8)	(216)	(70)	19	169
(75)	(103)	(69)	70	327	(21)	(26)	157	(21)	(101)	63	(8)	54	19	(5)	(46)
227	168	140	(184)	(932)	(62)	95	234	166	258	(152)	(16)	(162)	(51)	14	123

THE GAP

SCF

OCF

	2/3/18	2/2/19	2/1/20	1/30/21	1/29/22	4/30/22	1/31/23	1/31/24
	2017	2018	2019	2020	2021	LTM	F'2022	F'2023
Net Income	848	1,003	351	(665)	256	(72)	(76)	165
D&A	559	578	557	507	504	514	516	510
Amortization of lease incentives	(60)	(61)				-	-	-
Share-based compensation	87	91	68	77	139	104	1	-
Impairment of operating lease assets	-	-	239	391	8	3	-	-
Impairment of store assets	28	14	98	135	1	4	3	-
Impaiment of intangible asset	-	-	-	31	-	-	-	-
Loss on extinguishment of debt	-	-	-	58	325	325	-	-
Loss on disposal of P&E	11	4	70	-	-	-	-	-
Amort of debt issuance costs	8	2	2	12	14	12	2	-
Non-cash and other items	-	(12)	(12)	-	31	15	(3)	-
Loss on divestiture activity	-	-	-	-	59	3	-	-
Gain on sale of building	-	-	(191)	-	-	-	-	-
Deferred income taxes	61	65	(81)	(137)	(61)	(80)	(1)	-
Δ in NWC	(162)	(303)	310	(172)	(467)	(721)	392	79
Merchandise inventory	(142)	(154)	4	(305)	(593)	(828)	438	359
Other current assets and other LT assets	33	(18)	105	64	(42)	5	42	(45)
Accounts payable	(90)	(78)	66	564	186	55	(236)	(125)
Accrued Expenses & other CL	34	(196)	110	(14)	172	(104)	(101)	25
Income taxes payable, net of receivable	(52)	113	86	(304)	(85)	302	369	-
Other LT liabilities	55	30	-	12	(3)	(24)	25	(10)
Operating lease assets & liabilities	-	-	(61)	(189)	(102)	(127)	(145)	(125)

OCF

ICF

Purchases of P&E	(731)	(705)	(702)	(392)	(694)	(798)	(700)	(725)
Purchase of building	-	-	(343)	-	-	-	-	-
Proceeds from sale of building	-	-	220	-	-	333	333	-
Purchases of ST investments	-	(464)	(293)	(508)	(753)	(455)	-	-
Proceeds from ST investments	-	177	293	388	1,162	929	-	-
Payments for acquisition activity	-	-	(69)	-	(135)	(135)	-	-
Net cash for divestiture activity	-	-	-	-	(21)	(49)	-	-
Insurance proceeds re loss of P&E	66	-	-	-	-	-	-	-
Other	(1)	(9)	-	2	(5)	(5)	-	-

ICF

FCF

Proceeds from RC		-	-	500	-	350	350	
Payments for RC		-	-	(500)	-	-	-	
Proceeds from LTD		-	-	2,250	1,500	1,500	-	
Payments for LTD	(67)	-	-	(1,307)	(2,546)	(2,546)	-	
Debt Issiance Costs	-	(1)	-	(61)	(16)	(16)	-	
Proceeds from issuance of share-based comp plans	30	46	25	22	54	36	7	
Withholding tax payments on vested stock	(18)	(23)	(21)	(9)	(36)	(18)	(14)	
Repurchases of common stock	(315)	(398)	(200)	-	(201)	(255)	(279)	(300)
Cash dividends paid	(361)	(373)	(364)	-	(226)	(191)	(221)	(205)

FCF

FX effect

NCF

	(731)	(749)	(560)	895	(1,471)	(1,140)	(157)	(505)
	19	(10)	4	13	(6)	(12)	(7)	-
	2	(379)	(39)	635	(1,114)	(1,225)	302	(475)

The Gap, Inc - model by Jerry Lvovich

5/4/19	8/3/19	11/2/19	2/1/20	5/2/20	8/1/20	10/31/20	1/30/21	5/1/21	7/31/21	10/30/21	1/29/22	4/30/22	7/31/22	10/31/22	1/31/23
1Q'19	2Q'19	3Q'19	4Q'19	1Q'20	2Q'20	3Q'20	4Q'20	1Q'21	2Q'21	3Q'21	4Q'21	1Q'22	F'2Q'22	F'3Q'22	F'4Q'22
227	168	140	(184)	(932)	(62)	95	234	166	258	(152)	(16)	(162)	(51)	14	123
138	139	140	140	130	126	125	126	120	124	128	132	130	133	128	125
-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
24	23	17	4	18	17	20	22	36	36	25	42	1	-	-	-
-	-	-	239	360	1	-	30	5	1	-	2	-	-	-	-
-	-	-	98	124	3	-	8	-	1	-	-	3	-	-	-
-	-	-	-	-	-	-	31	-	-	-	-	-	-	-	-
-	-	-	-	-	58	-	-	-	-	325	-	-	-	-	-
-	-	-	70	-	-	-	-	-	-	-	-	-	-	-	-
-	-	-	2	-	4	4	4	4	4	3	3	2	-	-	-
7	3	(3)	(19)	3	(3)	-	-	13	1	7	10	(3)	-	-	-
-	-	-	-	-	-	-	-	56	3	-	-	-	-	-	-
(191)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
23	23	(4)	(123)	(41)	(84)	51	(63)	18	10	(56)	(33)	(1)	-	-	-
(199)	198	(345)	656	(602)	793	191	(554)	(78)	14	(390)	(13)	(332)	423	93	208
(83)	(83)	(393)	563	(79)	(12)	(499)	285	69	87	(444)	(305)	(166)	318	(142)	428
25	4	(21)	97	126	8	(97)	27	10	(108)	(70)	126	57	5	(50)	30
(100)	247	(18)	(63)	(203)	670	653	(556)	(205)	37	49	305	(336)	75	150	(125)
(37)	23	42	82	(86)	46	138	(112)	40	43	156	(67)	(236)	45	140	(50)
36	7	46	(3)	(322)	90	26	(98)	(18)	(37)	(39)	9	369	-	-	-
14	10	(5)	(19)	(18)	19	53	(42)	41	16	(8)	(52)	20	15	30	(40)
(54)	(10)	4	(1)	(20)	(28)	(83)	(58)	(15)	(24)	(34)	(29)	(40)	(35)	(35)	(35)
29	554	(55)	883	(940)	853	486	(162)	340	452	(110)	127	(362)	505	235	456
(165)	(159)	(199)	(179)	(122)	(86)	(80)	(104)	(124)	(145)	(217)	(208)	(228)	(157)	(157)	(157)
(343)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
220	-	-	-	-	-	-	-	-	-	-	-	333	-	-	-
(69)	(81)	(85)	(58)	(59)	-	(178)	(271)	(298)	(129)	(207)	(119)	-	-	-	-
86	60	85	62	297	28	23	40	233	267	268	394	-	-	-	-
(69)	-	-	-	-	-	-	-	-	-	(135)	-	-	-	-	-
-	-	-	-	-	-	-	-	28	(49)	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	2	-	-	-	-	-	(5)	-	-	-	-
(340)	(180)	(199)	(175)	116	(56)	(235)	(335)	(161)	(56)	(291)	62	105	(157)	(157)	(157)
-	-	-	-	500	-	-	-	-	-	-	-	350	-	-	-
-	-	-	-	-	(500)	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	2,250	-	-	-	-	1,500	-	-	-	-	-
-	-	-	-	-	(1,307)	-	-	-	-	(2,546)	-	-	-	-	-
-	-	-	-	-	(61)	-	-	-	-	(16)	-	-	-	-	-
10	7	5	3	6	6	4	6	25	16	7	6	7	-	-	-
(19)	(1)	(1)	-	(7)	(1)	-	(1)	(32)	-	(2)	(2)	(14)	-	-	-
(50)	(50)	(50)	(50)	-	-	-	-	-	(55)	(73)	(73)	(54)	(50)	(75)	(100)
(92)	(91)	(91)	(90)	-	-	-	-	(91)	(46)	(45)	(44)	(56)	(55)	(55)	(55)
(151)	(135)	(137)	(137)	499	387	4	5	(98)	(85)	(1,175)	(113)	233	(105)	(130)	(155)
-	(2)	2	4	(8)	9	3	9	(1)	-	(2)	(3)	(7)	-	-	-
(462)	237	(389)	575	(333)	1,193	258	(483)	80	311	(1,578)	73	(31)	242	(53)	144

THE GAP

BS

ASSETS

Cash	1,783	1,081	1,364	1,988	877	845	1,175	699
ST Investments	-	288	290	410	-	-	-	-
Merchandise inventory	1,997	2,131	2,156	2,451	3,018	3,169	2,565	2,206
Other current assets	788	751	706	1,159	1,270	991	1,006	1,051
Total current assets	4,568	4,251	4,516	6,008	5,165	5,005	4,747	
P&E, net	2,805	2,912	3,122	2,841	3,037	2,791	-	
Operating lease assets	-	-	5,402	4,217	3,675	3,587	-	
Other LT assets	616	886	639	703	884	874	-	
TOTAL ASSETS	7,989	8,049	13,679	13,769	12,761	12,257	-	

LIABILITIES

RC Facility	-	-	-	-	-	-	-	
Accounts payable	1,181	1,126	1,174	1,743	1,951	1,599	1,699	1,574
Accrued expenses & other CL	1,270	1,024	1,067	1,276	1,367	1,127	1,262	1,287
Current operating lease liabilities	-	-	920	831	734	717	-	
Income taxes payable	10	24	48	34	25	29	-	
Total current liabilities	2,461	2,174	3,209	3,884	4,077	3,472	-	
RC Facility	-	-	-	-	-	350	350	350
LT Debt	1,249	1,249	1,249	2,216	1,484	1,485	1,500	1,500
LT operating lease liabilities	-	-	5,508	4,617	4,033	3,921	-	
Other LT liabilities	1,135	1,073	397	438	445	575	-	
TOTAL LIABILITIES	4,845	4,496	10,363	11,155	10,039	9,803	-	

EQUITY

common stock par value	19	19	19	19	19	19	-	
Additional paid-in capital	8	-	-	85	43	-	-	
Retained Earnings	3,081	3,481	3,257	2,501	2,622	2,389	-	
Accumulated other comprehensive income	36	53	40	9	38	46	-	
TOTAL EQUITY	3,144	3,553	3,316	2,614	2,722	2,454	-	

A - (L + E)	-	-	-	-	-	-	-	
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The Gap, Inc - model by Jerry Lvovich

5/4/19	8/3/19	11/2/19	2/1/20	5/2/20	8/1/20	10/31/20	1/30/21	5/1/21	7/31/21	10/30/21	1/29/22	4/30/22	7/31/22	10/31/22	1/31/23
1Q'19	2Q'19	3Q'19	4Q'19	1Q'20	2Q'20	3Q'20	4Q'20	1Q'21	2Q'21	3Q'21	4Q'21	1Q'22	F'2Q'22	F'3Q'22	F'4Q'22
941	1,177	788	1,364	1,028	2,188	2,471	1,988	2,066	2,375	801	877	845	1,086	1,033	1,175
272	294	294	290	51	25	178	410	475	337	275	-	-	-	-	-
2,242	2,326	2,720	2,156	2,217	2,242	2,747	2,451	2,370	2,281	2,721	3,018	3,169	2,851	2,993	2,565
757	770	770	706	920	882	966	1,159	1,091	1,201	1,410	1,270	991	986	1,036	1,006
4,212	4,567	4,572	4,516	4,216	5,337	6,362	6,008	6,002	6,194	5,207	5,165	5,005	4,924	5,062	4,747
3,129	3,141	3,225	3,122	2,945	2,895	2,846	2,841	2,839	2,897	2,924	3,037	2,791			
5,732	5,807	5,796	5,402	4,851	4,689	4,460	4,217	4,060	3,975	3,788	3,675	3,587			
547	528	525	639	698	795	705	703	703	693	861	884	874			
13,620	14,043	14,118	13,679	12,710	13,716	14,373	13,769	13,604	13,759	12,780	12,761	12,257			
-	-	-	-	500	-	-	-	-	-	-	-	-			
994	1,246	1,241	1,174	971	1,629	2,284	1,743	1,530	1,583	1,630	1,951	1,599	1,674	1,824	1,699
882	908	974	1,067	1,051	1,124	1,283	1,276	1,294	1,252	1,414	1,367	1,127	1,172	1,312	1,262
929	946	934	920	886	856	823	831	798	789	746	734	717			
26	34	43	48	23	40	41	34	16	27	33	25	29			
2,831	3,134	3,192	3,209	3,431	3,649	4,431	3,884	3,638	3,651	3,823	4,077	3,472			
-	-	-	-	-	-	-	-	-	-	-	-	350	350	350	350
1,249	1,249	1,249	1,249	1,250	2,212	2,214	2,216	2,218	2,220	1,484	1,484	1,485	1,500	1,500	1,500
5,597	5,644	5,650	5,508	5,331	5,179	4,899	4,617	4,449	4,348	4,163	4,033	3,921			
372	391	393	397	381	423	458	438	493	520	523	445	575			
10,049	10,418	10,484	10,363	10,393	11,463	12,002	11,155	10,798	10,739	9,993	10,039	9,803			
19	19	19	19	19	19	19	19	19	19	19	19	19			
-	-	-	-	17	39	60	85	118	114	71	43	-			
3,495	3,551	3,573	3,257	2,235	2,173	2,268	2,501	2,667	2,879	2,681	2,622	2,389			
57	55	42	40	46	22	24	9	2	8	16	38	46			
3,571	3,625	3,634	3,316	2,317	2,253	2,371	2,614	2,806	3,020	2,787	2,722	2,454			
-	-	-	-	-	-	-	-	-	-	-	-	-			

	1/31/23	1/31/24	4/30/22	7/31/22	10/31/22	1/31/23
DRIVERS	E'2022	E'2023	1Q'22	E'2Q'22	E'3Q'22	E'4Q'22
SET CASE: 2 / 3		2				
YoY Δ in Sales by Brand						
Old Navy, YoY		-5%		-10%	2%	4%
Gap, YoY		-2%		-7%	2%	5%
Banana Republic, YoY		10%		20%	15%	15%
Athleta & Other, YoY		5%		2%	5%	5%
YoY Δ in Sales						
Working Capital						
YoY in Merchandise Inventory		-10%		25%	10%	-15%
Accounts Payable		(125)		75	150	(125)
Accrued Expenses & other CL		25		45	140	(50)
Margins						
COGS & Occupancy X, % of Sales		-63.5%		-66.0%	-65.0%	-63.0%
Gross Margin		36.5%		34.0%	35.0%	37.0%
OpX cash, % Sales		-30.0%		-32.0%	-31.0%	-30.5%
EBITDA margin		6.5%		2.0%	4.0%	6.5%
CAPITAL ALLOCATION						
CapX		(725)		(157)	(157)	(157)
Stock Repurchase		(300)		(50)	(75)	(100)
Dividend		(205)		(55)	(55)	(55)
VALUATION						
EV/EBITDA		6.0x		10.0x	9.0x	6.0x

BASE CASE	2	E'2022	E'2023	1Q'22	E'2Q'22	E'3Q'22	E'4Q'22
YoY Δ in Sales by Brand							
Old Navy, YoY		-5%		-10%	2%	4%	
Gap, YoY		-2%		-7%	2%	5%	
Banana Republic, YoY		10%		20%	15%	15%	
Athleta & Other, YoY		5%		2%	5%	5%	
YoY Δ in Sales							
Working Capital							
YoY in Merchandise Inventory		-10%		25%	10%	-15%	
Accounts Payable		(125)		75	150	(125)	
Accrued Expenses & other CL		25		45	140	(50)	
Margins							
COGS & Occupancy X, % of Sales		-63.5%		-66.0%	-65.0%	-63.0%	
Gross Margin		36.5%		34.0%	35.0%	37.0%	
OpX cash, % Sales		-30.0%		-32.0%	-31.0%	-30.5%	
EBITDA margin		6.5%		2.0%	4.0%	6.5%	
CAPITAL ALLOCATION							
CapX		(725)		(157)	(157)	(157)	
Stock Repurchase		(300)		(50)	(75)	(100)	
Dividend		(205)		(55)	(55)	(55)	
VALUATION							
EV/EBITDA		6.0x		10.0x	9.0x	6.0x	

WORST CASE	3	E'2022	E'2023	1Q'22	E'2Q'22	E'3Q'22	E'4Q'22
YoY Δ in Sales by Brand							
Old Navy, YoY		-8%		-10%	-5%	-2%	
Gap, YoY		-5%		-7%	-2%	-2%	
Banana Republic, YoY		7%		15%	10%	10%	
Athleta & Other, YoY		3%		0%	-2%	-2%	
YoY Δ in Sales							
Working Capital							
YoY in Merchandise Inventory		-15%		25%	5%	-20%	
Accounts Payable		75		75	175	(85)	
Accrued Expenses & other CL		65		45	150	(35)	
Margins							
COGS & Occupancy X, % of Sales		-66.5%		-67.0%	-66.0%	-65.0%	
Gross Margin		33.5%		33.0%	34.0%	35.0%	
OpX cash, % Sales		-32.0%		-32.0%	-31.0%	-31.5%	
EBITDA margin		1.5%		1.0%	3.0%	3.5%	
CAPITAL ALLOCATION							
CapX		(650)		(157)	(157)	(157)	
Stock Repurchase		-		(50)	(50)	-	
Dividend		-		(55)	(55)	-	
VALUATION							
EV/EBITDA		7.0x		10.0x	12.0x	8.5x	

THE GAP, INC		The Gap, Inc - model by Jerry Lvovich	
NOTES			
INVESTMENT THESIS		7/30/22	
<p>I am HOLD on both ’29 and ’31 going into the 2Q’22 Earnings Call. I do expect announcement of further operational weakness. That could put even more technical pressure on the notes. With further negative revisions the credit could trade lower toward double digit territory.</p> <p>- However, I would like to see how much progress the company is making on decreasing its Inventory levels.</p> <p>- Upon further weakness in the trading levels, GPS notes could be upgraded to BUY later in August -September timeframe.</p> <p>- Overall leverage and LTV here are very manageable (sub 1.5x Net Leverage and 25%). ’23 EBITDA multiples on stressed companies seem to be centering around 3.0 to 4.5x. Hence GPS leverage implied no impairment to the notes.</p> <p>- There is structural coverage (though not collateralized) from RE portfolio assets coupled with profitable Athleta and Banana Republic retailing brands. Ownership has proven to be conservative regarding leverage policy.</p> <p>- Long term, I can see return of success to Old Navy brand. It is a great value proposition and should do well attracting middle-income buyers looking to save in tougher economic times. Credit has plentiful liquidity to sustain itself as it is dealing with resolving current issues.</p> <p>FUNDAMENTAL BASIS FOR CONCLUSION:</p> <p>Highly negative operating sentiment. It seems GPS made a huge strategic mistake at exactly the wrong time. Previous CEO and senior management team invested heavily in inventory (up 25 – 35%) from previous year’s highs. The strategy is getting slammed in 3 different ways:</p> <p>1) Styles ordered are not in consumer demand (stay at home / active leisure vs going out). Sentiment shifted and GSP missed it. Now stock with inventory which would have to be sold at tiny to zero margins.</p> <p>2) Bodequality – great ESG initiative proven to be hard to execute... SKU count is through the roof, but the consumer they are seeking did not show up.</p> <p>3) Low-end consumer is feeling the pinch of inflation in every day life. Tightening of belts means trimming down on clothes purchases.</p>		<p>Also it is too early for a step-down consumer from higher price points to show up.</p> <p>Hence GSP is entering a very challenging operating environment. Sales should under pressure.</p> <p>- Former CEO (fired a few weeks ago) had a terrifying anecdote about two different stores with \$50k and \$100k customer demographics.</p> <p>- Carter’s came out with (8%) sales comp in 2Q and negative outlook based weakening consumer sentiment.</p> <p>- VF Corp is showing great numbers in North Face, Timberland and Vans... but negative comps in Dickies... singling out low-income consumer’s weakness.</p> <p>- Seems fair to expect another revision down in 2Q EC.</p> <p>However, the notes are in low 70’s already. YTW is >8.5% or about 100bps above HY market.</p> <p>Some structural credit support counter-balances operational negativity:</p> <p>- The company spent heavily on inventory. At 1QE’22 inventory was at record high levels a whopping 34% above Apr’21 levels. That’s \$800m!!! Over next 18 months inventory levels should be brought down significantly. Hence Working Capital will be net source of cash.</p> <p>- Should be sufficient to overcome negative cash flow from EBITDA less CapX and IntX</p> <p>- GPS ownership proved prudent in its capital allocation policy. Cut cash to shareholders entirely in all 4Q’s of 2020. I’d expect the same should operating environment begin to resemble my Worst case scenario.</p> <p>- Co’ owns over \$1bn on RE and is ready to liquidate it to supplement cash flow needs.</p> <p>- Liquidity is ample base on cash levels and RC availability.</p> <p>- Athleta and Banana Republic are smaller but well-functioning brands. Monetization is an option... though only theoretically.</p>	
CRI & VFC 2Q’22 EC update		7/29/22	
<p>CRI, 2Q’22 Earnings Call; 7/29/22</p> <p>- In addition to slow start in April (retail sales down 1%), sales weakened in May and June.</p> <p>- Correlating to consumer confidence. Inflation of gas prices was sited first. Retail sales were down 8%!!!</p> <p>- Unlike GPS they are planning on margin expansion. Prices increases have been successful and cost (freight) have been coming down.</p>		<p>VFC, 2Q’22 Earnings Call, 7/29/22</p> <p>- Timberland and North Face have shown 11% and 14% growth in all geographies outside of China.</p> <p>- But Dickies was down 13% - reflecting contracting low-end consumer in the Americas (!!!)</p>	
NET WORKING CAPITAL		7/29/22	
<p>- Typically The Gap is spending NWC on inventory in 1Q (ahead of spring/summer) and 3Q (ahead of holidays);</p> <p>- Similarly, The Gap is selling the inventory and raising NWC in 2Q (spring/summer) and 4Q (holidays shopping);</p>		<p>- However in 4Q’21 and 1Q’22 GPS was amassing inventory: up 23% and 34% (nothing seen in last 6 years). Hence 4Q’21 NWC was a slight use of capital while 3Q’21 and 1Q’22 were huge uses of capital.</p> <p>- The co’ is bound to discount existing inventory for remainder of the year.</p> <p>- For the year, I’s expect NWC to be a use of capital... but potentially</p>	
SELLSIDE SOURCE #4 (HY)		7/29/2022	
<p>Comps:</p> <p>- HY Comps: Abercrombie; Bath Body Works; Foot Locker; Rent-a-Center</p> <p>- Rent: use EBITDAR vs Debt + Leases</p> <p>- VFC & CRI just reported showing weakness from the consumer</p> <p>Capital Structure:</p> <p>- Downside on the notes is protected by RE ownership and Athleta’s valuation.</p>		<p>- Fisher family (owns 40% of GPS) has historically been very conservative with balance sheet.</p> <p>- In ’20 refi’d existing ’21 notes with Sr Secured debt by providing liens on IP and real estate</p> <p>- RC: yes, it does have some sort of ABL borrowing formula</p> <p>Liquidity:</p> <p>- Trading: very few incremental buyers... HF’s are playing this via CDS.</p>	

SELL-SIDE SOURCE #6 (equity)

7/13/2022

- 1) Low Visibility re: recovery at Old Navy

2) Elevated promotional environment – negative impact on margins at Gap & Old Navy

3) Further risk to 2H’22 numbers / guidance

4) C-suit changes add to near term uncertainty.
- BODEQUALITY: Old Navy extended size initiative

- 2Q’22 sales to be up but due to promotions!

- GPM in 2Q’22 down 905bps. It was down 930bps in 1Q’22

- Valuation: EV/EBITDA 4.0x on ’23 EBITDA \$978mm (vs prior est \$1,161mm vs street est \$1,026mm) = \$9/sh
- Old Navy visibility is pushed out to spring ’23 (new lineup arrival)

- Longer then average transit times

- Lower then anticipated demand in active / fleece / kids & baby

SELLSIDE SOURCE #5 (equity)

7/11/2022

- Announce c-suit changes

Downgraded guidance: inline w street expectations: down 9%, adjoin margin zero to slightly negative (street +3%).
- 1) Mngt is siting: more aggressive approach to assortment balancing. Result: increased promotion activity!!!

- 2Q’22 sales decline in double-digits. Problem in Old Navy: not increase in demand since new product has arrived!!!

- Sharp consumer shift into fashion/dress-up categories.

- Consumer discretionary spend is squeezed by inflation.

- New fashion designs won’t hit the stores until 1Q’23

- Inventories are building: will require aggressive promotions!!! Margins will decrease.

- Getting this message from URBN (urban outfitters), M
- (Macy’s), AEO (American Eagle), GPS

2) Increased promos + airfreight & raw materials inflation:

- \$50m increased airfreight costs

- 2Q’22 gross margin could be down 910bps from to 34.2% (!!!)

- EBIT margins should be zero! Everyone has taken down their expectations.

- More risk for markdowns to move the inventory – hence more risk of margin compression in 2H’22
- Valuation: 4x ’23 EV/EBITDA = 3x for Old Navy / Banana / Gap + 8x for Athleta Equity = \$5/sh!

SELLSIDE SOURCE #4 (HY)

7/11/2022

- CEO, Sonia Syngal (former Old Navy CEO), leaving after 18 years at the company.

- 2Q guidance is revised down

- FYE’22 leverage 2.5-3.0x
- assortment miss in Old Navy.

- 35% lower-end consumer weakness... could be getting worse

- Supply chain is 6 mo’s or longer: no improvement until ’23
- Co’s issues:

- 65% miss on execution (Old Navy)... \$250M air freight; 4Q’21
- New CEO for Old Navy, Horatio Berbeito, x-CEO OF Walmart Canada.

- Board Chairman, Bob Martin, is interim CEO – X-Dillards, Walmart Intl;

INDUSTRY EXPERT VIA ThirdBridge

6/10/2022 Ben Stefacic (former SVP & CFO, Global Supply Chain Ops at The Gap Inc)

- Key Takeaways:

1) Negative growth in all but BR brands!

2) Old Navy has had a product problem for at least 3 quarters... only now it is being acknowledged.

3) Old Navy does 700mm units a year – supply chain gets very delicate

4) Whenever Old Navy has inventory problem – it becomes ugly really fast. Can only mark down to get rid off it.
- Inflation is a huge problem: squeezing retailer from every direction: raw materials, transportation, wages... all the while apparel has been in deflationary environment for a long time.

- Retail apparel is a negative growth story in ’22 but reversion to the mean in ’23-26 of 2-4%... investors should have been cautious of inventory levels this year.

- Gap will do worse than others in ’22. They planned for aggressive ’22 and stacked up. 34% inventory comp at 1QE’22.

- It’ll take at least through ’22 to work through it... only via promotions.

- Why? Management was arrogant to think ’21 will be repeated and lapped. Senior team not listening to their people on the ground.
- Old Navy runs 75% of units of all of Gap Inc.

- Athleta has greatly benefited from staying at home trend. Lulu is still doing very well... Athleta is showing negative growth but it should reverse.

- Old Navy – been explained already. Bodequality added to the problem with increasing SKU’s. Women’s line was completely wrong. Gave example a brand new store in Hawaii – in 6 mo’s entire women’s line went on clearance. Nancy Green firing – scape goat.
- Old Navy’s problem: women’s line is not compelling. Hence when mom is going to shop for the kids and a little bit for herself... she won’t want to go back there.
- Gap – struggling for last 15 years. Launched home line w Walmart... who is a discount retailer. Gap lost its way.

- Banana Republic – benefiting from people being sick of staying home (same as Nordstrom and Macy’s). Hired former exec from Restoration Hardware. Found a unique look. Cut back inventory – (mb cut SKU’s – JL)
- Problem with moving not sold items to off-price retailers (TJX or Ross)... you can do that with Gap/Banana... problem w Old Navy is you can’t move 100,000 units... you need to move 10 million! Reverse logistics is also a nightmare... so instead GPS just puts it on clearance and sells it close to cost.
- Old Navy’s peers: Walmart, Target, Costco (latter does \$7bn in apparel). All are struggling with inflation and weakening demand from value-driven and low income bracket consumer.

- Consumer with under \$50k income will ask – “what am I spending my money on?... period.”
- Gap moved production to Vietnam from China over last 10 years.
- Best case: low demand will drive restructuring... SG&A is overinflated and needs to be cut. But management team is not focused on this at all.

- Worst case: inflation will continue... especially on raw materials, wages (at stores, distribution centers, corporate). Spring lockdowns in China will play a role in product availability in 2H’22.

SELLSIDE SOURCE #3 (equity)

6/8/2022

- Mix shift toward Old Navy and Athleta should improve margin structure

- Old Navy: >50% of revenue and even more profits (higher margin!!!)

- Athleta is not large enough to drive investment case.

SELLSIDE SOURCE #2 (equity)

5/30/2022

- Gap brand seeing pressure in Asia (lockdowns)
 - Supply chain / raw material costs inflation
 - Old Navy turnaround execution
 - Lower income consumer is struggling
 - Shift in demand toward going out categories vs athleisure / active
- Promotional levels are increasing
 - Banana Republic comps up 27% as brand change is working
 - Athleta – near term shift in demand
 - Searching for new Old Navy leadership

EARNINGS CALL, 1Q'22

5/26/2022

Sonia Sygnal, CEO; Katrina O'Connell, CFO

- Underperformed expectations for Q1 and took guidance down for '22
 - Sales of \$3.5bn down 13% YoY, due to Old Navy, down 19%; Athleta comp sales down 7%. Gap down 11%. BR comp sales up 27%. Instore sales down 10%, online sales down 17%.
 - Gross Margin 31.5% (“deleveraging” 930bps... what is that? Window dressing verbiage for worsening margins???) \$170m of incremental air freight was 480 bps.
 - Merchandise Margins down 760bps... 280 due to discounting at Old Navy.
 - SG&A \$1.3bn or 37.2% of sales

- Old Navy weakness will have negative impact on '22 EPS by \$1/sh due to:

 - Soft demand in active, fleece, kids & baby. Consumer pivoted to dresses and tops (these are underrepresented in Old Navy’s women’s line mix). When product did arrive – “there is an acceptance issue”. Invested in Bodequality... overestimated that demand in stores.
 - Inflation is impacting costs – fuel costs, labor. Also inflation impacted lower-income consumer’s demand. Cutting down growth expectations as a result.
 - Gap – slowdown in Asia due to COVID related shutdowns.
- Seen improved trends in May. But taking more conservative view on low-income consumer to guide down for '22.

- Two stores: \$100k vs \$50k consumer... the former showed no effect, the latter had baskets down, cash frequency down!!!!

Capital Usage:

 - paid \$0.15/sh dividend and repurchased 3.7m shares... for \$110m.

2Q'22 divie: \$0.15/sh

 - Inventory: up 34% YoY
 - OCF: (\$362m); FCF (\$590m) – well worse then historic norms.
 - Sold Mission Bay property in SF for \$330m + \$428m in NOL carryback tax refunds on CARES Act.

'22 Guidance:

 - Sales down low-mid single digits.
 - Gross Margin: 36.5-37.5%.
 - Operating Margin: 1.8% - 2.8%; adj Operating Margin 1.5% - 2.5%;
 - IntX \$80m;
 - Taxes 27%

SELLSIDE SOURCE #1 (HY)

3/4/2022

- '22 Guidance:

 - Co’ expected 20-25% lower air freight expenses (pressured margins in '21).
 - LSD sales growth
 - Management expected 1Q TO be soft and turn around thereafter (clearly which never happened - JL)
 - Old Navy: '21 sales flat to '19. 1H'22 – continued weakness. Miss on dresses and tops as consumers pivoted way from casualwear/athleisure.
 - Gap: global '21 sales up 3% from '19, US +12%
 - Banana Republic comp sales down -2% vs '19. Should improve to more high end rebranding.
 - Athleta comp sales up 42%. On track to reach \$2bn in '23.
 - Supply chain disruptions persist. '21 air freight costs: \$430mm... '22 should be >\$300mm...
- Capital allocation:

 - CapX \$700M
 - Dividend is increasing (1Q'22 up 25% from 4Q'21)
 - GPS paid \$400m to shareholders!
 - Will open 30-40 stores (Old Navy / Athleta)
 - Will close 50-60 stores (Gap / Banana part of 350 store closure plan)
 - Diversifying from port concentration on west coast: south and eastern seaboard.
 - Lockdowns in China impacting Gap’s performance.

Classification of Expenses

- COGS & Occupancy X:

 - cost of merchandise
 - inventory shortage & valuation adj
 - freight charges
 - online shipping and packaging costs;
 - cost assoc w sourcing
 - gains & losses associated FX derivatives for hedging
- OpX:

 - payroll, benefits, admin for store ops, field mngt, distribution centers;
 - payroll, benefits, admin for corp functions, marketing, design and development;
 - IT expenses;
 - lease less sepreciation on corporate offices;
 - R&D;
 - gains/losses on FX derivatives not for hedging
 - third party credit card processing;

Issue Symbol	Issuer	Issue Date	Maturity Date	Coupon	Issue Curren	Amount Outstand	Yield Price	to Maturity	OAS to LIBOR	Moody's Issue Rating	Net Debt	Market Cap	EV	Est '22 EBITDA	EV EBITDA	Net Leverage
364760AP	Gap, Inc.	27-SEP-2021	01-OCT-2029	3.625%	USD	750.0	73.35	8.70	599.20	Ba3	990.0	3,666.0	4,656.0	536.0	8.7x	1.8x
Average						436.8	91.02	7.56	463.81							
Median						475.0	90.28	7.95	519.38							
926400AA	Victoria's Secret & Co.	15-JUL-2021	15-JUL-2029	4.625%	USD	600.0	82.50	7.95	519.38	B1	747.0	3,229.0	3,976.0	1,015.0	3.9x	0.7x
926400AB	Victoria's Secret & Co.	15-JUL-2021	15-JUL-2029	4.625%	USD	600.0	82.50	7.95	519.38	B1	747.0	3,229.0	3,976.0	1,015.0	3.9x	0.7x
U9223QAA	Victoria's Secret & Co.	15-JUL-2021	15-JUL-2029	4.625%	USD	600.0	82.50	7.95	519.38	B1	747.0	3,229.0	3,976.0	1,015.0	3.9x	0.7x
501797AR	Bath & Body Works, Inc.	20-JUN-2019	15-JUN-2029	7.500%	USD	500.0	99.16	7.66	441.54	Ba2	4,080.0	8,275.0	12,355.0	1,453.0	8.5x	2.8x
778296AD	Ross Stores, Inc.	06-APR-2020	15-APR-2030	4.800%	USD	133.9	101.93	4.50	177.16	A2	-1,574.0	28,892.0	27,318.0	2,484.0	11.0x	-0.6x
918204AR	V.F. Corporation	30-APR-2004	15-OCT-2033	6.000%	USD	276.7	107.78	5.08	232.28	Baa1	4,874.0	17,477.0	22,351.0	1,852.0	12.1x	2.6x
96926JAC	William Carter Company	14-MAR-2019	15-MAR-2027	5.625%	USD	500.0	98.75	5.94	240.51	Ba2	387.0	3,337.0	3,724.0	521.0	7.1x	0.7x
003000AA	Abercrombie & Fitch Managen	02-JUL-2020	15-JUL-2025	8.750%	USD	307.7	98.06	9.51	630.87	Ba2	-146.7	959.0	812.3	346.0	2.3x	-0.4x
344849AA	Foot Locker, Inc.	05-OCT-2021	01-OCT-2029	4.000%	USD	400.0	77.75	8.16	543.64	Ba2	-162.0	2,748.0	2,586.0	835.0	3.1x	-0.2x
76009NAL	Rent-A-Center, Inc.	17-FEB-2021	15-FEB-2029	6.375%	USD	450.0	79.32	10.87	813.97	B1	1,305.0	1,619.0	2,924.0	506.0	5.8x	2.6x

Gap, Inc. (GPS)

The Gap, Inc - model by Jerry Lvovich

\$9.62

Comps Tables - FactSet Industry - Apparel/Footwear Retail

Selected Financials

Company Name	Ticker	Fiscal Period	Market Data (\$)			Financial (\$)					Valuation (x)		
			Price	Mkt Cap (M)	EV (M)	Shares (M)	Shares Out (M)	Sales (M)	EBIT (M)	EBITDA (M)	EV/EBIT	EV/EBITDA	EV/EBITDA FY2 (x)
Gap	GPS-US	04/30/2022	9.62	3,539.9	9,167.9	368.0	370.0	16,156.0	334.0	848.0	27.45x	10.81x	4.58x
Carters	CRI-US	07/02/2022	81.48	3,283.0	4,210.9	40.3	39.4	3,434.7	412.1	491.4	10.22x	8.57x	7.18x
Victoria's	VSCO-US	04/30/2022	36.96	3,070.6	5,444.6	83.1	87.0	6,714.4	738.2	1,031.2	7.38x	5.28x	3.69x
Ralph Lauren A	RL-US	03/2022	98.63	6,877.3	7,669.2	44.8	74.3	6,218.5	853.8	1,083.5	8.98x	7.08x	5.50x
Foot Locker	FL-US	04/30/2022	28.37	2,681.3	5,461.3	94.5	97.2	8,980.0	969.0	1,175.0	5.64x	4.65x	3.38x
American Eagle	AEO-US	04/30/2022	12.04	2,039.6	3,685.4	169.4	219.7	5,031.2	511.5	692.0	7.21x	5.33x	4.41x
Urban Outfitters	URBN-US	04/30/2022	20.48	1,897.8	2,779.5	92.7	96.3	4,673.3	381.3	682.0	7.29x	4.08x	3.45x
Boot Barn Holdings	BOOT-US	06/25/2022	62.30	1,852.6	2,216.6	29.7	30.4	1,547.8	257.1	327.5	8.62x	6.77x	6.24x
Bath & Body Works	BBWI-US	04/30/2022	35.54	8,129.3	13,517.3	228.7	243.0	9,476.4	2,169.2	2,614.2	6.23x	5.17x	7.50x
Buckle	BKE-US	04/30/2022	30.20	1,512.9	1,526.1	50.1	49.5	1,304.5	332.8	351.1	4.59x	4.35x	3.21x
Tapestry	TPR-US	04/02/2022	33.63	8,468.1	10,651.5	251.8	265.5	6,675.0	1,231.5	1,431.1	8.65x	7.44x	6.36x
Burlington Stores	BURL-US	04/30/2022	141.13	9,324.8	13,264.3	66.1	66.6	9,058.7	596.8	851.2	22.22x	15.58x	9.26x
Caleres	CAL-US	04/30/2022	24.82	911.8	1,760.3	36.7	36.7	2,874.1	258.8	309.9	6.80x	5.68x	4.44x
Abercrombie & Fitch A	ANF-US	04/30/2022	17.81	898.5	1,601.3	50.4	52.1	3,744.1	271.6	411.6	5.90x	3.89x	2.05x
Designer Brands A	DBI-US	04/30/2022	14.43	1,015.2	2,025.2	62.6	76.9	3,324.0	238.0	316.8	8.51x	6.39x	4.29x
Genesco	GCO-US	04/30/2022	56.05	769.5	1,152.8	13.7	13.4	2,404.1	135.9	178.5	8.48x	6.46x	2.95x
Chico's FAS	CHS-US	04/30/2022	5.02	628.2	1,129.4	125.1	123.3	1,962.9	127.4	357.8	8.86x	3.16x	3.38x
Shoe Carnival	SCVL-US	04/30/2022	21.81	601.7	751.2	27.6	28.3	1,319.5	187.9	250.6	4.00x	3.00x	2.74x
Children's Place	PLCE-US	04/30/2022	43.34	571.0	1,030.4	13.2	13.8	1,842.2	233.8	383.4	4.41x	2.69x	3.99x
Poshmark A	POSH-US	03/31/2022	10.79	843.0	259.4	53.6	77.6	336.5	-39.5	-35.8	-	-	-
Zumiez	ZUMZ-US	04/30/2022	26.00	505.9	610.3	19.5	19.5	1,125.5	126.1	213.6	4.84x	2.86x	2.72x
Stitch Fix A	SFIX-US	04/30/2022	5.97	645.8	587.1	82.8	108.8	2,162.1	-88.7	-54.1	-	-	-
Ross Stores	ROST-US	04/30/2022	81.26	28,435.0	30,064.5	349.9	348.8	18,733.3	2,157.4	2,522.7	13.94x	11.92x	9.89x
Lands' End	LE-US	04/29/2022	12.75	426.0	812.7	33.4	33.2	1,619.0	71.8	110.7	11.32x	7.34x	6.41x
Destination XL Group	DXLG-US	04/30/2022	4.14	259.3	407.2	62.6	68.4	521.2	63.4	80.1	6.42x	5.08x	4.31x
Cato A	CATO-US	04/30/2022	12.35	259.2	280.4	19.2	20.1	762.9	25.0	37.0	11.22x	7.57x	-
Citi Trends	CTRN-US	04/30/2022	24.58	206.4	395.5	8.4	8.4	914.4	45.2	117.1	8.74x	3.38x	2.61x
Tillys A	TLYS-US	04/30/2022	7.57	227.4	364.9	22.7	31.0	758.3	74.0	90.0	4.93x	4.05x	2.37x
TJX Cos	TJX-US	04/30/2022	61.16	71,657.2	80,070.7	1,171.6	1,189.3	49,869.8	4,878.7	5,750.9	16.41x	13.92x	10.88x
J.Jill	JILL-US	04/30/2022	16.02	161.9	506.8	10.1	14.2	613.2	74.9	103.3	6.77x	4.91x	3.16x
Average											9.14x	6.34x	4.85x
Median											7.93x	5.30x	4.29x

-23%

-19%