

Lululemon Athletica Inc. Investment Thesis
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Introduction

- (i) The report is part of the application for the 2022 Winter or Summer Co-op at BCI Public Markets department.
 - (ii) Readers can find my detail models on my **Github**:
<https://github.com/linhao142857/HAO-LIN>. The file name is **LULUUS** and has no password.
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1 Business Introduction & Assessment

- Headquartered in Vancouver, Lululemon Athletica Inc. designs and retails athletic clothing products. The company fitness pants, shorts tops, and jackets for yoga, dance, running, and general fitness.
- The stock (Ticker: LULU US) went public in 2007 and is traded on NASDAQ with a market cap of 51.5 billion. Its closing price was \$US 384.57 on Oct 12, with a 52-week range from \$US 269.28 to \$US 437.32. And its P/E and Current EV/LTM EBITDA were 60.6 and 37.8, respectively.

2 Absolute Valuation

- After conducting DCF analysis and comparable companies analysis for LULU, I issue an **SELL** recommendation for the stock. FCFE was used in my DCF models as the firm is not paying a dividend (so no DDM), and it has had virtually zero borrowing for the past few years (they now have some debts, but the cost of debt is hard to find).
- Since we are just a few months away from the end of LULU's fiscal 2022 and based on the Q2 result, the F2022 revenue growth rates I assigned for direct to customers, corporate-owned stores, and others were 50%, 30%, 40%. Then they will quickly converge to a long-term growth rate due to a boost from e-commerce during the pandemic. The COGS/Revenue ratio aligns with the historical level, with some improvement over time. SG&A was also estimated by the percentage of LULU's revenue. Working capitals days were aligned with the historical level. D&A expense was calculated by a percentage of gross PP&E.

- In my estimation of cost of equity, the adjusted-beta I used (1.122) was from the regression of LULU's price and SPX Index. The risk premium (10.19%) was from Bloomberg, and the risk-free rate (1.61%) is the 10 Year Treasury Rate. The CAPM gives the cost of equity of 11.24%.
- The target share price on Feb 1, 2022, was \$US 268.4, and this is significantly below the market value. So LULU is **OVERVALUED**.

3 Relative Valuation

- LULU US is trading at a level that is significantly above its peer average and its 5-year average. Based on the table below, I believe that LULU is **OVERVALUED**.

	P/E	EV/EBITDA	EV/Revenue	P/B
VF Corp	19.3	14.8	2.5	8.2
Adidas AG	27.4	14.2	2.3	7.2
Under Armour Inc.	33.7	13.9	1.6	5.2
Puma SE	37	15.9	2.1	7.5
Nike Inc.	37.9	28.1	4.8	16.8
Peer Group Average	31.06	17.38	2.66	8.98
Lululemon Athletica Inc.	46.5	28.4	7.3	19.3
Lululemon Athletica Inc. 5Y average	37.6	22.2	5.5	13.8

4 ESG

- Despite LULU has launched \$75 million plan and the Centre for Social Impact to solve "Inequity in Wellbeing", the firm has low scores on ESG factors on various sources¹.
- Lululemon only uses a low proportion of eco-friendly materials. While it has set an absolute target to reduce greenhouse gas emissions generated from its owned operations and supply chain by 60% by 2030. There is no evidence it has taken meaningful action to reduce or eliminate hazardous chemicals, nor does it have adequate policies or initiatives on water reduction.
- A few other concerns were Labour Conditions and Animal Welfare. The brand has made little to no progress toward the payment of a living wage, it sources its final stage of production from countries with extreme risk of labor abuse. While it does not use fur, angora, or exotic animal skin, there is no evidence it has an animal welfare policy. It uses down feathers accredited by the Responsible Down Standard, which is a plus, but it also uses leather, wool, and exotic animal hair without stating sources, so we can't be sure how the animals are treated.

¹e.g. Bloomberg ESG Disclosure Score, Yahoo Finance