

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

Our View—

We rate Lululemon Athletica as a buy based upon growth potential in the athletic apparel industry. Strong consumer trends in the area of health and fitness advance the industry of which is further augmented by Lululemon's existing position in North American markets as a premium brand following strong expansion possibilities in Europe and into Asia.

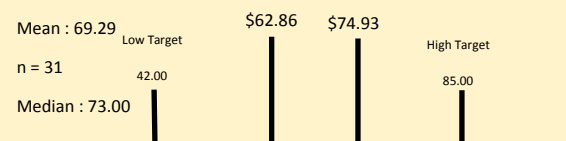
We base our opinion upon demonstrated management capacities in other ventures, and our view on existing regional market conditions and consumer preferences. Risks factored into our decision is the competitive nature of the fitness apparel industry, the low barriers to industry, and the relatively new nature of the company.

Key Points

- The growth in demand for health, fitness, and exercise, in our view, are strong upward trends which will propel further revenues. The emerging importance of millennials and aging baby boomers contribute to a growing concern regarding the longevity of individuals. This in addition the growth in health care costs and the rise of the athleisure style brings in considerable potential for growth.
- Lululemon's position in brand image and strategy for marketing its products take upon a differentiated style that connects to better target and engage its audience leading in turn to charging as a premium brand. Given Lululemon's strong technical and appealing products within yoga, Lululemon maintains a strong presence within the activity and associated lifestyles. It is able to further leverage this position in targeting similar associated "lifestyle activities" such as running.
- To further augment its brand image, the use of grassroots marketing efforts take form in a fashion many of its major competitors neglect. The use of genuine social media involvement, and community building through blogs and events, in addition to in-store hosted services/ programs appeal strongly to core fitness enthusiasts largely aging from 18-30.
- Strong management and, in our view, strong expansion environments in line with current plans offer good long term prospects. Lululemon plans to expand its current operations from North American and Australian markets into Europe, Asia, and the Middle East. Currently "testing the waters" through expansion in heavy traffic areas such as Hong Kong, the use of temporary retail locations and adequate but lackluster e-commerce options serve as a cautious step forward.
- The addition of notable senior management from global enterprises such as Toms shoes, Dell, and Apple offer experience in global expansion, e-commerce, and connection to a broader, yet similar "hip" audience.
- The significance of brand equity and regularly occurring controversy behind the brand pose undue risks moving further. In the 2013, stretching of Lululemon's luon fabric had shown to be have less than modest defects resulting in a product recall. Following, defensive remarks by company founder Chip Wilson aggravated the issue by inciting select members of the audience. In recent times another recall was announced on safety matters though deemed minor by company officials.
- Major Competitors are starting to react and engage audiences in similar fashion to Lululemon. Nike, a major competitor in the eyes of Lululemon, has started to offer similar product offerings and started in-store activities in select openings. Given the low barriers to entry, a major competitor with global logistical capacities present a challenge.

<BUY>

NASDAQ: LULU; USD 62.86



Key Statistics

Shares (000's)	143,935
Market Cap (000's)	8,923,970
Dividend:	0.00
P/E	33.62
Average Volume (000's)	2,003

Analyst Estimates

(000's)	2014	2015F	2016F	2017F	2018F	2019F
Revenue	1,797,213	2,039,837	2,315,215	2,627,769	2,982,517	3,385,157
Revenue Growth	12.95%	13.500%	13.500%	13.500%	13.500%	13.500%
Gross Margin	49.13%	49.63%	50.08%	50.47%	50.81%	50.23%
EBIT margin	20.92%	20.42%	19.98%	19.59%	19.24%	19.83%
EPS	1.66	2.23	2.43	2.67	2.94	3.42

Disclosure:

Any statements that we make, other than historical facts, contain forward-looking information based on our business assessment and assumptions at the time of disclosure. Such forward-looking information includes, but is not limited to expected growth strategies, projected operating results, anticipated timing for developments. Our business, as well as each product we analyze and market, is subject to various risks and uncertainties beyond our control. Risks and uncertainties that could affect the Company's future results and financial condition include, but are not limited to, the factors described after. Information disclosed is subject to addition, change or deletion without notice. The trading of stocks, futures, commodities, index futures or any other securities has potential rewards, and it also has potential risks involved. Trading may not be suitable for all users. Anyone wishing to invest should seek his or her own independent financial or professional advice. YOU SHOULD NOT MAKE ANY DECISION, FINANCIAL, INVESTMENTS, TRADING OR OTHERWISE, BASED ON ANY OF THE INFORMATION PRESENTED ON HERE WITHOUT UNDERTAKING INDEPENDENT DUE DILIGENCE AND CONSULTATION WITH A PROFESSIONAL BROKER OR COMPETENT FINANCIAL ADVISOR. You understand that you are using any and all information available here on YOUR OWN RISK.

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

Company Description and Highlights

Company Description

Lululemon offers a variety of fitness apparel marketed under the ath-leisure lifestyle. The corporation offers a variety of different apparel and accessories to the general public in addition to targeted groups under athletic pursuits such as yoga, running, and dance-inspired activities. The group markets with emphasis towards women and female youth, however are in the process of diversifying to men's athletic apparel and children's apparel. Their product line focuses upon technical and practical improvements with emphasis on fabric design.

News & Event Highlights

Jul 25, 2015— Lululemon branded beer announced

Lululemon announced through social media a limited run of 88,000 cans of "Curiosity Lager" in partnership with Stanley Park Brewing, a Canadian craft beer brewery. Some consider this introduction a stunt geared towards expanding the brand towards men in along with their expansion goals. Furthermore, a statement by global events manager, Travis McKenzie. "Our focus has always been to bring our event mantra — yoga.run.party — to life" The Guardian reports select social media users drew backlash to the graphic design of the product. Some call the "totem pole" design offensive towards native Americans.

Jun 29, 2015— Announced recall for select drawstring products.

Lululemon announced a joint recall with the U.S. Consumer Product Safety Commission and Health Canada. Consumers risk injury from drawstrings on 318,000 tops such as hoodies as they have the potential to lash faces. In the past Lululemon experienced a similar recall in 2013 for excessively transparent yoga pants under certain conditions. In a company statement, " We assessed and accrued for the financial impact ... and do not consider this to be material to our business".

Jun 25, 2015— Names Miguel Almedia Executive Vice President

Effective mid July Miguel Almedia will start his employment under the company subordinate to Laurent Potdevin, CEO. The press release claims Mr. Almedia's specialty is within the digital realm, focusing on e-commerce strategies. E-commerce discussed later is a fast growing source of revenues for the company. Miguel Almedia has served in similar roles before under Walgreens, Dell, and Appel and as a strategy consultant under the Boston Consulting Group.

Jun 09, 2015— Q1 2015 Earnings Call

Latest earnings call reflect momentum being built within growth areas such as men's apparel and the ivivva brand. Store expansion into Asia

They believe their market segment to be driven by the focus on longevity by aging Baby Boomers and Millennials. Products are largely sold through corporate-owned stores though e-commerce by direct to consumer channels are also present and growing. As of February 1st, 2015 Lululemon operates in total 302 retail stores, of which 211 reside within the United States and 57 reside within Canada. The group had opened 48 stores during fiscal 2014 and plans to expand largely into Non-North American markets.

continue. In along with the e-commerce focus, a website redesign is planned. Expenses following foreign exchange developments and west coast port delays in addition to unexpected airfreight expenses add pressures to margins.

Mar 26, 2015— Earnings Call w/ Outlook

Lululemon builds upon 2014 goals, developing supply chain with experienced management, building a third distribution center in Ohio, and launching a mobile shopping app. In the near future, the company expects gross margins of 49-50% and to open 60 new stores, 8 of which in Asia and Europe. In closing, company expectations of the long term are mid-single comp growth, a low to mid 50% gross margin.

Feb 02, 2015— Founder Chip Wilson resigns from board

After disagreements with other directors, Mr. Wilson is looking to sell his \$1.3 billion stake in the company. This move appears to follow the Wilson family's recent venture Kit and Ace, another Canadian apparel company. From the globe and mail, "according to sources familiar with the matter, Wilson left the board earlier this year after it failed to move forward on governance reforms that he had pushed for last year". In the past Chip Wilson has been the source of controversial comments that have been attributed to the company as offensive.

Jan 07, 2015— Names Stuart C. Haselden Chief Financial Officer

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

Qualitative Analysis

Marketing Differentiation

Lululemon engages in a variety of new marketing approaches. Emphasis is placed upon “grassroots” marketing in which Lululemon appeals to many however targets a relatively few number of people/places. A growing portion of revenues come from whole sale operations in targeted yoga studios, health clubs, and fitness centers. In addition the utilization of small showroom or temporary locations augmented with a community based approach to social media, in store community and brand ambassadorship .

Value Generation

The continued demand for this group’s technical product, style, and lifestyle is critical for the continued growth and basis of the company revenues. This is augmented by the strong customer relations Lululemon marketing strategy incorporating a “grassroots” and modern approach. From a technical perspective, Lululemon is driven by the demand for fitness apparel in the areas of yoga, running, sports wear and associated accessories. In addition, specialty exercise apparel further drive demand in product lines such as stink-free apparel, and mesh fabrics. In lieu of the athleisure lifestyle, most products and select lines design specifically fall under dual purpose clothing suitable for fitness though carrying a distinctive modern style suitable as casual wear. So long as current trends in fitness and athleisure continues driven by developments in culture, the Lululemon brand stands to gain from growth in technical demand and also their marketing positioning evident in the brand’s mention in social media.

Growth Drivers

Continued Trends in Fitness, Health, and Fashion

In a 2012 National Health Interview Survey, yoga became the top used mind and body practice within the United States. From past years, this marks a significant increase from 6.1% in 2007 and 5.1% in 2002. As reported by IBIS world, growth in time spent and participation in sports and exercise inherently drive product demand. In addition, in the realm of fitness and health clubs, an area Lululemon caters to through products but also in their “grassroots’ marketing strategy through product placement and partnerships.

Macroeconomic Factors

Consumer income and spending are of most importance. Lululemon could be considered a premium brand relative to most mass market offerings within its arena. Price points for its tops and pants are often within the 60-150 dollar range. Within North America, upper-middle income populations whom are most associated with this trend in fitness are a key driver of revenues. In light of Lululemon’s current store base and expansion goals, Australia shows a significant population in addition to most parts of Europe. Expansion into the Middle East and parts of Asia show significantly less persons in this income group. Spending and cultural preferences within these areas will also be a decisive factor, a question developed upon later will deal with how these markets will react to the growth in fitness and in particular the brand’s targeted activities and lifestyle.

Increase in consumer income, the growth of the middle class in emerging markets.

Studies in consumer income versus health and fitness trends show that as developments in this middle/upper-middle category continues, a greater demand of fitness clubs and apparel will being to emerge. In light of Lululemon’s current caution in not to over saturate North American markets the growth of the middle class in the emerging markets Lululemon targets, which includes Asia, will be severely blunted by these region’s income.

Growth in E-commerce business segment

Recent growth in revenues are largely attributed to growth in sales from the Lululemon website and mobile app.

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

Qualitative Analysis

Notable Risks

Diminished Brand Equity

Given the presence of the Lululemon brand within the athleisure, the promotion strategy, and positioning as a premium brand, Lululemon is at risk of severe downturn in lieu of bad public image. In recent controversies caused by Founder remarks, product recalls and concerns over the Lululemon limited beer production run, the brand is surprisingly resilient in face of its string of bad publicity.

Reliance on suppliers

Lululemon acknowledges that none of its products are manufactured in house. Given that the brand differentiates on a technical level through their promoted named fabrics, difficulties of sourcing what Lululemon considers relatively advanced textile products may be of issue. The dependences on five companies that source 63% of Lululemon's product and 40% of raw materials may come of concern in the long run. There is a special risk in light of campaigns towards environmentalism, emerging market labour concerns and the effect on brand equity.

Downturn on consumer spending

As discussed earlier, a downturn in economic factors and in consumer sentiment will result in more substitutable goods such as Lululemon branded apparel to be out of reach.

Loss of market share

The market for athletic apparel is considered highly competitive and diversi-

fied. Competition may result in pricing pressures', the loss of profit margins, and lower growth. Competition comes from traditional athletic apparel companies and also similar "grass roots" companies. Traditional apparel companies will be able to expand or switch existing production and have existing distribution capacity as this market grows and becomes increasingly attractive. Companies such as Nike and Adidas, who are named major competitors of Lululemon, have longer operation histories, broader customer bases, and established consumer, retail, supplier, and distributor relationships. Smaller technical companies such as Under Armour, may nullify existing expansion opportunities such as the expansion into men's products given Lululemon's existing target individual.

Obsolescence

The nature of fashion and lifestyle trends may be of concern in the long term as the demand for the athleisure lifestyle and associated products / styles rotate out of fashion.

Lack of patents

Lululemon acknowledges that the intellectual property rights in technology, fabrics, and processes used to manufacture are owned or controlled by suppliers. The inability to obtain such rights leave greatly lowered barriers to entry. Risks include a vital supplier leaving Lululemon for one of their more mature competitors.

Notable Management

Given the current expansion strategy into Non-North American markets, and focuses in E-commerce opportunities. This analysis of management will focus upon key individuals with experience in expansion into emerging markets, European apparel markets, and the overall targeted individuals Lululemon pursues.

Michael Casey Independent Co-Chairman of the Board

He retired from Starbucks Corporation in October 2007, where he had served as Senior Vice President and CFO from August 1995 to September 1997, and Executive Vice President, CFO and Chief Administrative Officer from September 1997 to October 2007. Subsequent to retirement he served as a Senior Advisor to Starbucks Corporation from October 2007 to May 2008 and from November 2008 to January 2015.

Laurent Potdevin Chief Executive Officer

Mr. Potdevin previously worked at Toms Shoes, a socially-conscious shoe company, where he served as President from May 2011 to December 2013. From 1995 to 2010, he worked at Burton Snowboards, the world's largest and premier snowboarding company, serving in various capacities including as President and CEO from 2005 to

2010.

Scott (Duke) Stump Executive Vice-President

Mr. Stump was the Principal and Chief Architect at the Northstar Manifesto, a company committed to helping others become "bonfire" brands, emphasizing the role that a business conscience can play in propelling brands further on the road to growth and sustainability, where he had been since 2008. He also served as the SVP Culture, Creative and Brand Innovation at Easton Sports from January 2011 to April 2014. Prior to 2008, Mr. Stump worked at Seventh Generation as the Chief Marketing Officer and spent over 15 years at Nike in various roles in brand, product and sales.

Miguel Almedia Executive Vice President

Mr. Almeida's career spans over 15 years of operational and senior leadership with a keen focus on digital strategies. Most recently, he was the Group VP, Digital Commerce and Mobile solutions for Walgreens where he was responsible for omnichannel initiatives, mobile solutions, and online-to-consumer commerce across a variety of digital brands. Prior to joining Walgreens, Miguel held senior roles in the online groups of Apple and Dell where he drove global online expansion for both companies. Previously, he was a strategy consultant with The Boston Consulting Group where he worked across multiple countries in Europe and South America mainly in high technology, telecom, ecommerce, marketing and retail.

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

Industry Overview — Select Data Sourced from Mintel Academic

The Consumer

Mintel advises that in general higher household incomes out leads to healthier lifestyles which in turn leads to greater purchases in fitness apparel . Young men 18-34 are mentioned specifically by Mintel for higher tendencies for purchases and reporting that they are exercising more than a year ago. Furthermore their price tolerances are reported to be higher than average. One point worth mention is that 38% of consumers of the respondents to Mintel report purchases for fitness clothing for casual wear.

Nielsen Global reports that program offerings are increasingly relevant and the demand for quality and coaching are higher in women and millennials.

In addition, Mintel notes that in US markets the growth of the Hispanic population greatly benefits this fitness apparel industry as this population has “ a higher fitness clothing purchase incidence than other ethnicities due in part to the median age being younger, with 80% buying apparel in the past year. They are more willing to pay elevated prices for most items as well “.

Marketing Strategies of Significant Companies

Nike— Using traditional channels such as television Nike arguably focuses more-so upon the male population through it’s marketing statements in the area of performance and heroism. Nike has historically used athlete endorsements and sponsorships to great effect.

Adidas— Much like Nike Adidas promotes their brand through a mixture of traditional channels and sponsorship. Notable mentions go towards their World Cup efforts and popular youth icons such as Kanye West.

Under Armor— Under Armor is a similar company expanding into new markets and products. Originally marketing to men through a gritty industrial / urban theme now moving into women’s and children apparel.

Competition

Competition in the athletic apparel industry is principally on the basis of brand image and recognition as well as product quality, innovation, style, distribution and price. Lululemon focuses their efforts on their targeted niche of women’s apparel

largely by offering product quality, style, and leveraging their brand equity while charging accordingly to this “premium brand” image. Lululemon identifies three major competitors, Nike, Adidas, and Under Armor and three secondary competitors, The Gap, Lucy Activewear, and Bebe stores.

“Marketers can attempt to increase frequency of purchase and/or basket size among the avid purchasers, in particular young adults with high household incomes, recognizing insights about each group. Young adult men are brand loyal and prefer quality, durable items while young women are price conscious but are interested in being fashionable and stylish. Those with higher household incomes are more prone to purchase higher-ticket items with ancillary features like moisture-wicking, weatherproof, or smart technology.

Encouraging purchases as part of a larger reward or incentive program could be appealing, as 29% of consumers said they buy fitness clothing to treat themselves. Also, the idea of positioning fitness clothing as a gift appears to be an opportunity area for retailers to consider. Young men and affluent consumers are more likely to buy athletic apparel as a gift already. Perhaps this could be accelerated among less active or non-exercising shoppers.

Hispanic-focused initiatives should be included in marketing and branding efforts given the overall growth of this group coupled with their tendency to buy more fitness clothing overall versus the general population. They will also maintain loyalty to retailers and brands who they think are “for me.”

Porter’s Five Forces Summary (Less Competition)

Power of Suppliers

All of the named major competitors source the production of goods to third party supplies to some degree. Lululemon is of interest here in particular, it claims that given the high technical nature of it’s products there are fewer possibilities of adequate suppliers for its fabrics. A trend in Lululemon’s major competitors focuses upon “greenifying” their efforts in human rights, environmentalism, and safety in their sourcing operations.

Power of Buyers

Given the competitive nature of the industry, buyers are constantly pressuring for lower production costs and better shipment in quality and quantity.

New Entrants

As seen in the diverse competitors of Lululemon, the ease of entry is low especially for other entities already within the apparel space.

Substitute Product

Lululemon being what could be considered an industry leader may be able to stave off product substitution by leveraging it’s brand as many competitors do. However in practical terms, substitution is of ease.

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

Outlook

Short Term Outlook

E-commerce will continue to be the main driver of revenues.

Direct to consumer sales increased approximately 22% from 2014 to 2015 while traditional store retail sales increased 9.7%. Reported margins after general corporate expenses come out to be 41.4 % for e-commerce sales while retail is at 26.4%. The continued development on website sales and mobile applications show very favorable prospects domestically within North America and also abroad into emerging markets. As of the current, Lululemon offer's its mobile shopping app and training / social media app on iOS devices however not its shopping app on android devices. Its website store already allows shipment to the vast majority of the globe including all of western Europe, Scandinavia, China, Korea, India, Japan, Turkey, UAE, Israel, Saudi Arabia, the Caribbean, and south America.

Long Term Outlook

Growth of the Middle and Upper Classes in Asia and in particular China.

Given the growth of the middle class and dispositions in trends regarding environmentalism, fitness and health, and in addition American culture, Lululemon products, in our view, seem to be well received in this market. As reported by IBIS world, The Gym, Health and Fitness Clubs industry in China has been developing rapidly in recent years, largely due to increasing disposable incomes and health awareness among Chinese consumers". IBIS world statistics report that in the last five years, the annual growth rate of this industry comes to be approximately 13.7%. Going further, "The combined market share of the top four players in the industry – Haosa Group, Wellness Group, Impulse Total Fitness, and Powerhouse Gym – is estimated at about 17.1% in 2015. There are a large number of regional fitness clubs in the industry. Many clubs only establish chain establishments in a specific city so as to maximize their influence. These fragmented clubs provide similar fitness services and make a relatively small contribution to industry revenue. The low industry concentration level is also attributed to the industry being in the growth phase of its life cycle". In our view, bringing the same level of community engagement firstly to these key industry players through strategic partnerships then followed suit by smaller regional players will allow Lululemon to secure a great deal of future revenues.

Consumer sentiment and spending will be dampened given recent developments in the oil price plunge and markets in Asia and Europe.

Despite savings on gasoline and related oil and gas expenditures, Q1 personal consumption in the areas of recreational goods and vehicles, clothing and footwear have remained largely steady towards past quarterly figures. From the start of 2015, the consumer confidence index had remained largely steady on average near 100 (1985 =100) levels. From the most recent release of July 28, 2015, the consumer index has dropped by 8.9 points from 99.8 to 90.9. The release shows that while consumers show that current situations are largely favorable, short-term expectations are less optimistic regarding employment, and financial markets likely due to developments in China and Greece. If conditions continue, dampened spending within the Fall and Winter seasons will have a great impact on the revenues of Lululemon.

Physical Activity still an issue in North America.

Despite increased awareness in light of over all health and longevity concerns, North Americans are still showing trends towards an increasingly obese population. In recent years, the demographic of fitness orientated individuals has changed from the 18-30 range to a more dispersed level amongst all age groups. As the centers for Disease Control and Prevention says, "some Americans are getting enough, but too many are not" . Key findings by the Outdoor foundation show that running and jogging staying at the most popular outdoor activity. In addition, young women and teenage girls are collectively adding five percentage points more in terms of overall outdoor activity participation, in our view a proxy for overall physical activity engagement. In our view the trends in North America paint two divergent outlooks. As the effects of obesity within the general population comes about the trend towards a healthier lifestyle could accelerate or become increasingly irrelevant. With specific focus on women's products, Lululemon stands to gain from a larger participation population.

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

Key Questions

Q1. How will Lululemon cater to / adapt its current operations to better fulfill its expansion into European and Emerging Markets?

Firstly the use of the temporary and showroom store model mitigates early concerns regarding the lack of traction with foreign markets. In the notable management panel, we discussed how select members of senior management have the global expansion experience within other companies such as CEO Laurent Potdevin. Mr. Potdevin brings experience from Toms shoes and Burton brand. In our view, Lululemon could benefit from additional website overhauls and as Mr. Potdevin says, the company will have to adapt to Asia and not the other way around. Upon inspection of the e-commerce site despite the wide range of shipping options the current selection of nationality appears to only affect pricing and presumably shipping matters. The website is still in English and additional brand community measures such as the blog and education section follow suit. In Europe, a greater sense of health and exercise exists and will likely propel the brand though this may be offset given the perceived stigma of a “yogi” American brand. In terms of Asia, we’ve discussed the brand ambassadorship and the opportunities in partnership with the growing fitness clubs present in Asia. The company will likely have to drastically adapt it’s product line in suit for Asian styles and fitness goals.

Q2. Given the nature of this industry, how will major players such as Nike reacts as Lululemon expands into other markets and gain traction domestically.

We’ve named Nike in particular given their recent movements into this athleisure lifestyle area. On November 21, 2014, Nike opened a 6,000 sq-ft store in Newport Beach, California. Matching Lululemon’s initiative on building communities around the brand and store, Nike’s new opening serves as a retail location but also as a service for yoga classes and pant hemming services both offered by Lululemon for years now. Nike has expanded it’s product line directly in competition of Lululemon’s product offerings. Traditionally, Nike has a large presence in the realm of running equipment, now it appears to be coping the move into yoga through it’s own branded leggings and pants. Nike does not maintain a in-house e-commerce store while relying on third parties such as Amazon while Lululemon offers an in-house and third party Amazon option. On the mobile front, Nike has various training apps however not a mobile store application. In our view, a expansion into these areas of e-commerce will likely be well received by the Lululemon demographic though we are unsure of its financial viability overall for Nike.

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

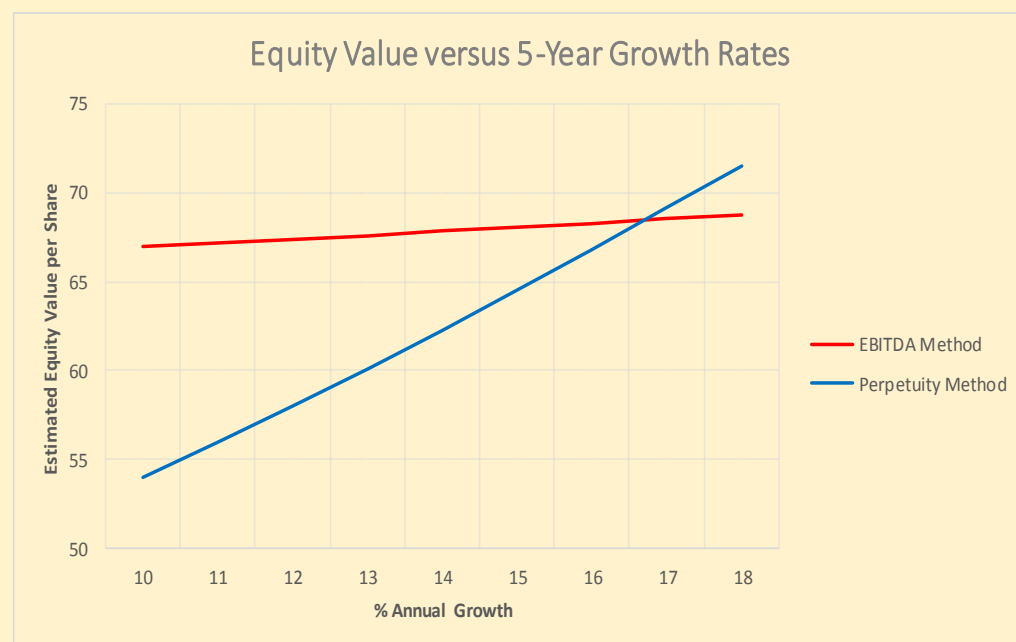
Scenario Analysis

Base Case (See Attached) 67.52 / 59.07

In the base case we model a neutral view largely based upon industry outlook and statements made in earnings calls by company officials. We predict an expected growth rate of 13.5% annually, larger than the 2014 FY period though smaller compared to the 2013 FY period (16.11%) in which the Luon fabric recall and controversial statements by Chip were made. In line with their targeted gross margin goals, for year 2015 the margin will come to be 49.63%. Under current circumstances, incorporating Q1 data, our EPS estimates for 2015 FY and 2016 FY are 2.23 and 2.43. These are higher than the 1.93 and 2.32 average estimates polled by Yahoo Finance. However our yearly revenue estimate of 2.03 B is on par with the average analyst estimate. This difference is likely due to the expected share repurchases under Lululemon's share buyback program within the coming year. Our terminal value is based upon earnings call and estimates for industry growth, and company consensus estimates at 7.00%. In the Q1 2015 earnings call, company officials stated that the long term outlook would incorporate a low-mid single digit growth. In consensus analyst estimates provided by Thompson one, the lowest polled estimate out of 31 is 11.90.

Aggressive Case 68.1 / 74.41

If Lululemon were to maintain the growth rate experienced for 2013 FY and 2012 FY, a growth rate of 16.12% and a long term growth rate of 7.50% given its focus on expanding abroad and through e-commerce channel then a price increase up to 74.41 by terminal value. Expectations here see a smooth transition abroad and in following a strong initiative to revamp North American stores which see a significant increase in revenues.



Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

Comparables Analysis

Key Financials & Effectiveness

Name	Sales TTM	Sales Year/Year	EBITDA Year/Year	EBIT Year/Year	Net Margin TTM	Net Margin FY1	EPS TTM	EPS Year/Year	EPS FY1	ROA TTM	ROE TTM
LULULEMON ATHLETICA INC.	1,745.84	1.22	1.06	1.02	14.46%	13.51%	1.76	1.17	2.06	19.90%	22.84%
THE GAP, INC.	16,318.00	1.01	1.00	0.98	7.61%	7.06%	2.86	1.10	2.77	17.17%	41.96%
UNDER ARMOUR, INC.	3,421.63	1.29	1.26	1.23	5.94%	6.14%	0.92	0.66	1.08	9.37%	15.91%
NIKE, INC.	30,601.00	1.10	1.16	1.18	10.70%	11.14%	3.70	1.24	4.18	18.11%	27.82%
BEBE STORES, INC.	411.28	0.95	0.75	0.77	(13.84%)	(5.07%)	(0.72)	0.95	(0.28)	(22.06%)	(30.33%)
adidas	16,200.19	1.06	0.93	0.88	3.36%	4.41%	2.63	0.75	3.74	4.74%	8.53%
URBAN OUTFITTERS, INC.	3,375.78	1.08	0.90	0.86	6.75%	6.99%	1.68	0.92	1.90	12.33%	16.41%
ABERCROMBIE & FITCH CO.	3,631.02	0.89	0.93	0.88	0.34%	1.40%	0.13	0.27	0.73	1.35%	0.86%
L BRANDS, INC.	11,575.00	1.06	1.14	1.16	9.81%	9.35%	3.81	1.23	3.75	21.88%	(186.68%)
COACH, INC.	4,323.72	0.88	-	-	10.78%	12.65%	1.68	0.51	1.91	-	18.91%
AMERICAN EAGLE OUTFITTERS, INC.	3,336.26	1.02	1.45	1.87	3.16%	5.45%	0.54	1.77	0.97	6.39%	9.20%
Mean	8,630.88	1.05	1.06	1.08	5.37%	6.64%	1.73	0.96	2.07	8.92%	(4.96%)
Median	3,631.02	1.06	1.03	1.00	6.75%	6.99%	1.68	0.95	1.91	10.85%	15.91%
High	30,601.00	1.29	1.45	1.87	14.46%	13.51%	3.81	1.77	4.18	21.88%	41.96%
Low	411.28	0.88	0.75	0.77	(13.84%)	(5.07%)	(0.72)	0.27	(0.28)	(22.06%)	(186.68%)

Market Data & Price Multiples

Name	Dividend Yield TTM	Total Return 1 Yr	Market Cap - Consolidated	Enterprise Value	P/E TTM	P/E FY1	Price/ Cash Flow TTM	Price/ Cash Flow FY1	Price/ BV Tangible
LULULEMON ATHLETICA INC.	0.00%	55.04%	9,557.97	8,873.64	38.32	32.75	33.01	24.94	8.21
THE GAP, INC.	2.56%	4.51%	15,045.65	15,064.65	12.61	13.03	8.50	9.83	5.12
UNDER ARMOUR, INC.	0.00%	40.26%	21,455.54	22,000.04	107.39	91.70	56.99	92.49	28.91
NIKE, INC.	0.99%	33.60%	98,440.00	92,140.00	31.08	27.52	22.99	23.37	8.02
BEBE STORES, INC.	0.00%	(40.82%)	149.71	78.16	NEG	NEG	NEG	-	0.96
adidas	2.10%	(4.27%)	16,648.53	16,477.77	30.25	21.30	15.55	16.36	4.48
URBAN OUTFITTERS, INC.	0.00%	12.30%	4,228.33	3,954.77	19.65	17.35	11.81	11.20	3.13
ABERCROMBIE & FITCH CO.	3.94%	(38.92%)	1,384.42	1,338.48	159.01	27.23	5.15	5.11	1.01
L BRANDS, INC.	2.41%	70.68%	23,748.38	27,810.38	21.36	21.72	15.67	18.07	NEG
COACH, INC.	4.43%	(14.11%)	8,647.79	7,517.79	18.59	16.43	10.14	10.79	3.90
AMERICAN EAGLE OUTFITTERS, INC.	2.85%	43.04%	3,392.50	3,065.59	32.20	17.93	10.99	11.22	3.12
Mean	1.75%	14.66%	-	-	42.53	25.46	16.94	22.34	5.15
Median	2.56%	12.30%	-	-	30.25	21.30	11.81	13.79	3.90
High	4.43%	70.68%	98,440.00	92,140.00	159.01	91.70	56.99	92.49	28.91
Low	0.00%	(40.82%)	149.71	78.16	12.61	13.03	5.15	5.11	0.96

Data from Thompson One Academic

We note that Under Armour, Nike, and Adidas are the three primary competitors here with other brands largely fitting with the area of general apparel and/ or expanding their own fitness apparel line. Lululemon maintains a well above average year on year sales growth in comparison to its competitors while holding the highest net margins for TTM and FY1. This is offset by its low growth in EBITA and EBIT of which it's competitors such as Nike and Under Armour show values more fitting for their year to year sales. Presumably Nike has the logistical capacity to handle a growth in sales. Presumably the expansion into foreign markets and foreign exchange considerations in recent times have had more of an effect on Lululemon given it's strong net margin, ROA, and ROE figures. In our view, it is natural to consider Under Armour as a suitable alternative investment choice to Lululemon however the given Under Armour's lower yearly return and abnormally high P/E, price to cash flow and price to book ratios, this investment alternative is overvalued.

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

CONSOLIDATED STATEMENTS OF OPERATIONS AND INCOME

(Amounts in thousands)

Period Ending January 31st.

	2013A	2014A	2015A	2016F	2017F	2018F	2019F	2020F
Revenue								
Net Sales	1,370,358	1,591,188	1,797,213	2,039,837	2,315,215	2,627,769	2,982,517	3,385,157
% Growth		16.11%	12.95%	13.500%	13.500%	13.500%	13.500%	13.500%
Cost of goods sold (Adjusted)								
Cost of goods sold	564,532	702,044	824,669	935,999	1,062,359	1,205,778	1,368,558	1,553,313
COGS as a % of revenue	41.20%	44.12%	45.89%	45.89%	45.89%	45.89%	45.89%	45.89%
Gross profit	805,826	889,144	972,544	1,103,837	1,252,855	1,421,991	1,613,960	1,831,844
Gross profit margin (%)	58.80%	55.88%	54.11%	54.11%	54.11%	54.11%	54.11%	54.11%
Gross profit margin (%) (including de- preciation)	44.33%	47.20%	49.13%	49.63%	50.08%	50.47%	50.81%	50.23%
Operating expenses								
Selling, general and administrative	386,387	448,718	538,147	610,797	693,254	786,844	893,068	1,013,632
SG&A as a % of revenue	28.20%	28.20%	29.94%	29.94%	29.94%	29.94%	29.94%	29.94%
EBITDA (Adjusted)	419,439	440,426	434,397	493,041	559,601	635,147	720,892	818,213
EBITDA margin (%)	30.61%	27.68%	24.17%	24.17%	24.17%	24.17%	24.17%	24.17%
Depreciation and amortization	43,000	49,068	58,364	76,405	97,010	120,396	146,939	146,939
EBIT	376,439	391,358	376,033	416,635	462,591	514,751	573,953	671,273
EBIT margin (%)	27.47%	24.60%	20.92%	20.42%	19.98%	19.59%	19.24%	19.83%
Interest								
Other Income (Expense)	4,957	5,768	7,102	7,102	7,102	7,102	7,102	7,102
Taxation								
Income tax expense	109,965	117,579	144,102	127,206	141,002	156,660	174,433	203,648
Deferred Taxes				13,469	9,345	5,480	1,688	311
Net Taxation				113,737	131,657	151,181	172,745	203,338
Tax rate (%)	28.83%	29.61%	37.61%	30.02%	30.02%	30.02%	30.02%	30.02%
Minority Control								
Net income attributable to non- controlling interest	875.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Net Income (Adjusted)	270,556	279,547	239,033	310,000	338,037	370,673	408,310	475,038
Net Income (Reported)	270,556	279,547	239,033					
Earnings Per Share (EPS)								
Basic	1.88	1.93	1.66	2.23	2.43	2.67	2.94	3.42
Diluted	1.86	1.91	1.66	2.22	2.42	2.66	2.93	3.41
Average Shares Outstanding								
Basic	144,000	144,913	143,935	139,055	139,055	139,055	139,055	139,055
Diluted	145,806	146,043	144,298	139,418	139,418	139,418	139,418	139,418

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in thousands)

Period Ending January 31st.	2013A	2014A	2015A	2016F	2017F	2018F	2019F	2020F
Cash flows from operating activities								
Net income	270,556	279,547	239,033	310,000	338,037	370,673	408,310	475,038
<i>Items not affecting cash</i>								
Depreciation and amortization	43,000	49,068	58,364	76,405	97,010	120,396	146,939	146,939
Deferred income taxes	(6,445)	820	2,087	13,469	9,345	5,480	1,688	311
Working Capital Changes (From Balance Sheet)								
Accounts receivable		(5,552)	(1,843)	(810)	(1,965)	(2,230)	(2,531)	(2,873)
Inventories		(33,568)	(19,326)	(19,169)	(30,684)	(34,826)	(39,527)	(44,863)
Prepaid expenses and other current assets		(10,896)	(18,474)	(8,731)	(9,909)	(11,247)	(12,765)	(14,489)
Accounts payable		11,602	(3,308)	3,138	1,684	1,912	2,170	2,463
Accrued inventory liabilities		(14,617)	6,881	8,000	4,090	4,642	5,269	5,980
Accrued compensation and related expenses		(8,085)	10,487	2,039	4,316	4,899	5,560	6,311
Income taxes payable		(38,868)	19,304	(4,545)	1,684	1,911	2,169	3,566
Unredeemed gift card liability		3,230	7,909	(3,955)	5,710	6,481	7,356	8,349
Other accrued liabilities		29,595	2,394	2,960	4,718	5,355	6,078	6,899
Net cash provided by operating activities	307,111	262,276	303,508	378,802	424,037	473,445	530,716	593,630
Cash flows from investing activities		v	v					
Purchase of property and equipment	Hardcoded	(106,408)	(119,733)	(136,154)	(154,535)	(175,397)	(199,075)	(225,950)
Other non-current assets				(82)	(73)	(57)	(44)	(58)
Other non-current liabilities				11,554	8,842	8,454	8,014	12,145
Net cash used in investing activities		(106,408)	(119,733)	(124,681)	(145,765)	(166,999)	(191,105)	(213,863)
Purchase of property and equipment % of Revenues		6.69%	6.66%	6.67%	6.67%	6.67%	6.67%	6.67%
Cash flows from financing activities								
Proceeds from exercise of stock options	11,014	8,171	2,913	0	0	0	0	0
Taxes paid related to net share settlement of equity awards	(393)	(5,721)	(4,972)	(5,812)	0	0	0	0
Repurchase of common stock	0	0	(147,431)	(302,569)	0	0	0	0
Net cash (used in) provided by financing activities	10,621	2,450	(149,490)	(308,381)	0	0	0	0
Shares Repurchased @ 64.00	62			(4,880)	0	0	0	0
Effect of exchange rate changes on cash (Decrease) increase in cash and cash equivalents	(651)	(72,368)	(79,809)	(65,000)	(65,000)	(32,500)	(16,250)	(8,125)
		85,950	(45,524)	(119,260)	213,272	273,946	323,361	371,642

[illegible]

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

Depreciation								
(Amounts in thousands)								
Period Ending January 31st.	2013A	2014A	2015A	2016F	2017F	2018F	2019F	2020F
Property and equipment (Beg of Year)	214,639	255,603	296,008	355,757	413,282	468,282	520,418	599,429
Capital expenditures (Beg of Year)			119,733	136,154	154,535	175,397	199,075	225,950
Book (GAAP) depreciation								
Useful Life								
PP&E			7					
CAPEX			8	8	8	8	8	8
Depreciation (Level Method , End of Year)								
Existing PP&E			42,287	42,287	42,287	42,287	42,287	42,287
CAPEX 2015			15,964	15,964	15,964	15,964	15,964	15,964
CAPEX 2016				18,154	18,154	18,154	18,154	18,154
CAPEX 2017					20,605	20,605	20,605	20,605
CAPEX 2018						23,386	23,386	23,386
CAPEX 2019							26,543	26,543
CAPEX 2020								30,127
Total			58,251	76,405	97,010	120,396	146,939	146,939
Book (MACRS) depreciation								
Useful Life								
Depreciation (Half Year % , 7- year)								
Existing PP&E			14.29%	24.49%	17.49%	12.49%	8.93%	8.92%
CAPEX 2015			14.29%	24.49%	17.49%	12.49%	8.93%	8.92%
CAPEX 2016				14.29%	24.49%	17.49%	12.49%	8.93%
CAPEX 2017					14.29%	24.49%	17.49%	12.49%
CAPEX 2018						14.29%	24.49%	17.49%
CAPEX 2019							14.29%	24.49%
CAPEX 2020								14.29%
Depreciation (Half Year)								
Existing PP&E			42,300	72,492	51,772	36,971	26,434	26,404
CAPEX 2015			17,110	29,323	20,941	14,955	10,692	10,680
CAPEX 2016				19,456	33,344	23,813	17,006	12,159
CAPEX 2017					22,083	37,846	27,028	19,301
CAPEX 2018						25,064	42,955	30,677
CAPEX 2019							28,448	48,754
CAPEX 2020								32,288
Total			59,409	121,271	128,140	138,649	152,562	147,974
Deferred Tax Liability				13,469	9,345	5,480	1,688	311

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

Operating Working Capital								
(Amounts in thousands)								
Period Ending January 31st.	2013A	2014A	2015A	2016F	2017F	2018F	2019F	2020F
Current Assets								
Accounts receivable	6,351	11,903	13,746	14,556	16,521	18,751	21,283	24,156
Receivable days		2	3	3	3	3	3	3
Inventories	155,222	188,790	208,116	227,285	257,969	292,795	332,322	377,186
Inventory days		89	88	89	89	89	89	89
Prepaid expenses and other current assets	35,301	46,197	64,671	73,402	83,311	94,558	107,323	121,812
Prepaid expense days		38	44	44	44	44	44	44
Current liabilities								
Accounts payable	1,045	12,647	9,339	12,477	14,161	16,073	18,243	20,706
Payable days		4	5	5	5	5	5	5
Accrued inventory liabilities	30,032	15,415	22,296	30,296	34,386	39,028	44,297	50,277
Payable days		12	8	12	12	12	12	12
Accrued compensation and related expenses	27,530	19,445	29,932	31,971	36,287	41,186	46,746	53,057
Payable days		19	17	19	19	19	19	19
Income taxes payable	39,637	769	20,073	15,528	17,212	19,124	21,293	24,860
Payable Days		63	26	45	45	45	45	45
Unredeemed gift card liability	35,113	38,343	46,252	42,298	48,008	54,489	61,845	70,194
Payable Days		8	9	9	9	9	9	9
Other accrued liabilities	0	29,595	31,989	34,949	39,667	45,022	51,100	57,999
Payable Days		3	6	6	6	6	6	6

Lululemon Athletica Inc.	Target Price: \$74.93 USD	Fair Price: \$59.07 USD (Low Est.)	Shouyang Zhou
LULU	Company Analysis Report		Friday, July 24, 2015

Discounted Cash Flow Analysis

(Amounts in thousands)

Period Ending January 31st.	2013A	2014A	2015A	2016F	2017F	2018F	2019F	2020F
Unlevered Free Cash Flow								
EBIT				416,635.5	462,591.4	514,751.3	573,952.8	671,273.2
Depreciation & Amortization				76,405.1	97,009.7	120,395.9	146,939.3	146,939.3
Deferred Taxes				13,468.8	9,345.4	5,479.6	1,687.9	310.7
Other non-current liabilities				11,554.5	8,842.5	8,454.5	8,014.1	12,145.3
Changes in Working Capital				(21,071.9)	(20,354.9)	(23,102.9)	(26,221.7)	(28,657.7)
Capital Expenditures				(136,153.8)	(154,534.6)	(175,396.7)	(199,075.3)	(225,950.4)
Taxes				(127,206.0)	(141,002.0)	(156,660.4)	(174,432.6)	(203,648.2)
Total Unlevered Free Cash Flow		0.0	0.0	233,632.2	261,897.5	293,921.4	330,864.5	372,412.2
Net Present Value Calculation								
Period				0.7	0.7	0.7	0.7	0.7
Discounted Cash Flow				217,978.2	244,349.6	274,227.8	308,695.6	347,459.5
			1,392,7					
Total Net Present Value			10.8					
Terminal Value								

Cost of Capital by CAPM			
Risk Free Rate	1.70%	Debt YE 2015	0
Market Risk Premium	5.81%	Stock Price	62.00
Beta	1.50	Shares Outstanding	143,935,000
Cost of Equity	100.00%	Equity Value	8,923,970,000.0
Cost of Debt			
WACC	10.415000%		

EBITDA Method		
Exit Year EBITDA		818,212.5
Multiple		10.91x
Terminal Value		8,923,970.0
Net Present Value		8,326,039.1
Perpetuity Method		
Unlevered Free Cash Flow		398,481.1
Growth Rate		7.00%
Terminal Value		11,668,552.0
Net Present Value		7,110,114.3
Discounted Cash Flow Total Valuation		Perpetuity Method
Total of Present Value of Cash Flows	1,392,710.8	1,392,710.8
Present Value of Terminal Value	8,326,039.1	7,110,114.3
Total Enterprise Value	9,718,750.0	8,502,825.1
Net Debt, Non-controlling interests, preferred securities	0.0	0.0
Equity Value	9,718,750.0	8,502,825.1
Share Count	143,935,000.0	143,935,000.0
Estimated Equity Value per Share	\$67.52	\$59.07

Note:

12 Month Target Price is a measure of our assessment on the prevalent market price based upon P/E ratios at that time. Our figure is based upon our estimated EPS and the current market P/E ratio for this stock.

Sources and Further Reading

Nielsen Global Consumer Exercise Trends Survey 2014	http://www.slideshare.net/Bryankorourke/nielsen-global-consumer-exercise-trends-survey-2014
Jul 25, 2015— Lululemon branded beer announced	http://www.thestar.com/life/2015/07/21/from-duds-to-suds-lululemon-going-into-beer-business.html http://www.cbc.ca/news/canada/british-columbia/lululemon-branded-beer-hits-store-shelves-this-summer-1.3161000 http://www.theguardian.com/business/2015/jul/24/lululemon-branded-beer-can-cartoon-totem-pole
Jun 29, 2015— Announced recall for select drawstring products.	http://www.theglobeandmail.com/report-on-business/lululemon-recalls-drawstrings-from-hoodies-after-they-lash-faces/article25112115/ http://www.fool.com/investing/general/2015/07/08/lululemon-athletica-inc-issues-another-product-rec.aspx
Jun 25, 2015— Names Miguel Almedia Executive Vice President	http://investor.lululemon.com/releasedetail.cfm?ReleaseID=919574
Mar 26, 2015— Earnings Call w/ Outlook	http://files.shareholder.com/downloads/LULU/4156765498x0x818138/EC275B0E-84B6-4AE7-8136-50FB05287D15/LULU-4Q14_Transcript.pdf
Feb 02, 2015— Founder Chip Wilson resigns from board	http://www.theglobeandmail.com/report-on-business/founder-chip-wilson-looking-at-sale-of-entire-lululemon-stake/article24913579/
North America, Europe Are the Principal Domains of the Upper-Middle Income	http://www.pewglobal.org/2015/07/08/a-global-middle-class-is-more-promise-than-reality/pg-2015-07-08_globalclass-10/
Ancient practice of yoga now a growth industry	http://www.usatoday.com/story/news/nation/2015/03/01/yoga-health-fitness-trends/23881391/
Most Used Mind & Body Practices NHIS	https://nccih.nih.gov/research/statistics/NHIS/2012/mind-body/yoga
IBISWorld Industry Report 71394	- University Subscription —
Table 2.3.5. Personal Consumption Expenditures by Major Type of Product	http://www.bea.gov/iTable/iTable.cfm?reqid=9&step=1&acrdn=2#reqid=9&step=3&isuri=1&903=65
Fitness for Foreigners	http://www.slate.com/articles/life/fitness/2011/01/fitness_for_foreigners.html
How people exercise in China, Pakistan, Sudan, and Sweden	
Outdoor Participation Report	http://www.outdoorfoundation.org/pdf/ResearchParticipation2014.pdf
Health And Wellness A European Consumer Obsession?	http://www.marketresearchworld.net/content/view/2201/77/
Nike Just Launched A Direct Threat To Lululemon	http://www.businessinsider.com/nike-just-launched-a-threat-to-lululemon-2014-11
Facts about Physical Activity	http://www.cdc.gov/physicalactivity/data/facts.html