Academy Sports & Outdoors [NASDAQ: ASO]

Initiate a BUY at 5% Weight| PT: $92.78

November 2nd, 2023

CIMG Investment Research

A Battered Stock

Academy Sports & Doors (NASDAQ: ASO) is down >30% from all time highs. Industry fears centered around increased shrink and a weaker consumer has led to a sell-off of the stock, even after ASO beat earnings and raised full year EPS guidance. We believe we have the chance to buy a high-growth retailer at an attractive valuation.

Investment Thesis

Supply-Chain Investments & Economies of Scale Will Increase Margins

Academy is strategically allocating resources to enhance its inventory management and supply chain operations, with the primary objective of bolstering its operating margins. The company's ongoing investments comprise the development of a scalable transportation system, which will harness real-time data for optimized goods movement from distribution centers to store locations. Additionally, there are plans to construct a new distribution center to cater to the expanding store network in new markets. Simultaneously, as new stores are established, the existing distribution centers, currently operating at approximately 50% capacity, are projected to achieve full capacity utilization. This synergy is expected to yield economies of scale, ultimately contributing to increased margins for ASO. ASO's management anticipates that these strategic investments will yield a substantial improvement of over 100 basis points in operating margins by the year 2027.

Aggressive Expansion Will Increase Store Count 50% by 2027

ASO plans to add between 120 to 140 new stores by the year 2027, constituting a 50% surge in its current store count. The company's new stores demonstrate exceptional year-one sales performance, with an average of $18 million in sales, while the upfront investment ranges from $5 to $6 million per store. These new outlets are EBITDA positive within a year and maintain an average return on invested capital (ROIC) of over 20%. Furthermore, ASO is proactively expanding its product offerings by entering into partnership agreements with new brands like LL Bean and Fanatics. This strategic move not only bolsters ASO's diverse product portfolio but also positions the company to tap into new customer bases in previously untapped markets. ASO's management predicts that these investments will result in a substantial revenue increase, with a target of reaching $10 billion in sales and a net income of $1 billion by the year 2027. These growth initiatives, backed by ASO's impressive new store performance and strategic partnerships, underscore the company's ambitious trajectory in the retail industry.

Industry Leading Metrics

ASO exhibits superior operational metrics that surpass industry benchmarks. Notably, ASO maintains top-tier margins and excels in store productivity, reinforcing its competitive edge. ASO's commitment to offering industry-low prices on name brand products through its price match guarantee positions the company favorably for market share capture as it expands into new geographical markets. Moreover, ASO boasts an impressive operating margin of approximately 13%, outpacing key competitors like Dick's Sporting Goods (DKS) at around 10% and Hibbett Sports (HIBB) at approximately 8%. This margin outperformance is chiefly attributed to ASO's

Consumer Staples

Cole Davis – Committee Head
cbdavis20@crimson.ua.edu

Will Guy – Committee Head
wmguy@crimson.ua.edu

Ethan Sneckenberger – Analyst
ebsneckenberger@crimson.ua.edu

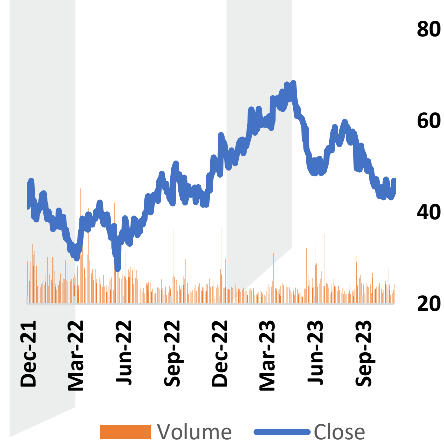
Caroline Egger – Analyst
coegger@crimson.ua.edu

Walt Shelton – Analyst
Whshelton1@crimson.ua.edu

Alex Nowicki – Analyst
Asnowicki1@crimson.ua.edu

Elle Schriver – Analyst
evschriver@crimson.ua.edu

Figure 1: 2-Year Stock Chart & Volume



Price	$48.84
Dividend Yield	0.74%
PT	$92.78
Upside	90%
52-Week Range	$40.67-69.02
Dil Shrs Outstand	78.09 M
Mkt Cap	$3.64 B
Ent Value	$4.94 B
NTM P/E	6.04x
NTM EV/EBITDA	4.50x

strategic emphasis on a diverse private brand portfolio, which constitutes a higher proportion of total sales compared to industry peers. Furthermore, ASO showcases industry-leading store performance metrics, including sales per square foot, sales per store, EBITDA per store, and cash flow as a percentage of sales, all of which surpass the standards set by other sports retailers. Despite ASO's outperformance across these key indicators, the company continues to trade at a significant discount relative to Dick's Sporting Goods.

Overreaction to Industry Headwinds

ASO has experienced a notable decline in its stock price, currently down by over 30% from its 2022 highs and more than 10% lower than its most recent earnings report. This drop has occurred despite ASO surpassing earnings expectations and raising its EPS guidance. One significant issue prevalent in the retail sector presently is theft, which has affected gross margins for companies like DKS and TGT, resulting in a decrease of over 100 basis points due to shrink. ASO, however, maintains industry-leading shrink rates, with their margins only contracting by approximately 30 basis points. Even though ASO's shrink management efforts have proven effective, the stock declined by nearly 10% on the same day DKS and TGT released their earnings reports. We view this as an overreaction, considering ASO's robust theft prevention investments are yielding positive results. Another prevailing concern within the retail space is sluggish consumer demand. Nonetheless, we believe that most of these concerns are already priced into ASO's stock. The consensus expectation on the street was an 8% year-over-year decrease in sales for ASO in their most recent earnings report, a projection that ASO surpassed. As the year-over-year comparisons start to ease off the elevated levels seen in 2022, same-store sales (SSS) should gradually turn positive. Furthermore, ASO's competitive pricing strategy, featuring the lowest price points in the industry, positions the company well to address the challenges associated with a weaker consumer environment.

Valuation

We arrive at a $92.78 price target for ASO, resulting in an upside of 90% based off their 11/3 close. We use a 5-year DCF and EV/EBITDA blended valuation. We have ASO building out 120 new stores in our projection period, which is the lower end of management guidance of 120-140. We also have them reaching 13% operating margins, which is also at the low end of management guidance of 13-13.5%. We model a SSS reflection point in 24Q2, with them reaching 2.5% SSS growth in 2027. We use a 10% discount rate, 2% long term growth rate, and a 4.00x EV/EBITDA (industry average) multiple.

Our bear case valuation has a price target of $64.05, representing an upside of 31% based off their 11/3 close. We have ASO building out only 70 new stores, roughly half of management guidance. We also have them declining to 10% operating margins, which is what DKS currently operates at. SSS projections remain the same as the base case.

Our super-bear case valuation represents what would happen if all Covid demand is completely reversed. We model the NTM revenue to be equal to their 2019 revenue. We also have them decreasing operating margins to 8%, which is what HIBB currently operates at and is the lowest in the industry. We reach a price target of $46.56, representing a downside of 5% based off their 11/3 close.

Industry Overview

The sports retailers industry encompasses a diverse and dynamic landscape, comprising prominent players such as Dick's Sporting Goods, Academy Sports and Outdoors, and Hibbett Sports. This sector caters to a wide range of sporting and recreational needs, from athletic apparel and footwear to sporting equipment and outdoor gear. Dick’s is the largest player in the space, with roughly $12 billion in revenue and over 700 stores across the US. ASO has roughly $6 billion in sales, with 275 stores mostly concentrated in the south. Hibbett is the smallest player by revenue, with roughly $1.7 billion in revenue. They operate over 1000 stores across the US; however they are much smaller and offer fewer products than Dick’s and ASO.