Updated thoughts on HIBB. 1Q results were pretty solid (all things considered) and 2Q is off to a "robust" start (digital strength continuing, stores comping positive with entire chain effectively re-opened). While stimulus checks have been supporting consumer spending in recent weeks, HIBB's improved suite of digital/omni-channel capabilities are helping fuel new customer acquisition/market share gains. Looking forward, sustainability of positive comps in a non-stimulus/high unemployment market remains the ultimate wildcard. Net, digital strength likely hits margins but helps the stock's multiple. Raising price target to $20. Maintain Neutral rating.

- **1Q recap.** Comps were in line with our expectations (-19.5% vs. our -20%E) as robust ecommerce sales (+110.5%) offset significant store declines (down 34%). That said, adjusted EPS of $0.31 lagged our $0.52E on more material GM compression. For more details on 1Q, see our early read note.

- **Digital fueling new customer acquisition.** A surge in traffic (>80%) and an increase in conversion (+26%) fueled 1Q's robust ecommerce performance (+110.5% y/y). With new customers accounting for ~40% of ecommerce sales across the 2H of 1Q, HIBB's suite of digital/omni-channel capabilities and decision to lean into advertising (while some competitors pulled back) clearly paid dividends from a market share standpoint.

- "Robust" trends QTD – sustainability remains a wildcard. Management noted "robust" comps QTD driven by continued strong digital sales and a return to positive brick-and-mortar comps as stores re-open. As of today, >1,000 stores are open (effectively the entire chain) vs. ~700 at the end of April, with many reporting "significant" comp increases upon their re-opening. While encouraging, HIBB's business is notoriously volatile, and a portion of the strength is clearly stimulus-related (provided additional support to recent Jordan shoe launches). Our new 2Q comp estimate of +3.2% (up from prior -10%) balances the strong start with some moderation across June/July as stimulus benefits fade and back-to-school timings may shift. Visibility, of course, is low.

- **Go-forward margin/expense dynamics.** While the mix shift to ecommerce will remain a structural GM headwind, the magnitude of pressure should moderate from 1Q as store sales recover. When combined with fixed cost leverage (occupancy/W&D) on positive comps, our model assumes 2Q GM -85bps (vs. 1Q's -550bps adjusted). SG&A will be more "normalized" going forward, but improved comps/GM trends have us raising our 2QE EPS to ($0.11) from ($0.27).

- **Estimates.** Despite our higher 2Q estimates, the 1Q shortfall vs. our model plus lower 2H EBIT margins (higher mix of digital sales) have us reducing FY20E/FY21E to $0.90/$1.70 (from prior $1.20/$2.00).

- **Raising price target to $20.** We are encouraged by the strong finish/start to 1Q/2Q and believe HIBB has ample liquidity to navigate this unprecedented environment. While we are comfortable raising our price target to $20 (~12x FY21E EPS) given HIBB's improved competitive position, uncertainty on the shape of the demand curve in a non-stimulus/high unemployment market keeps us Neutral-rated.

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Hibbett Sports operates stores specializing in athletic apparel, footwear, and equipment in small/mid-sized markets across the Southern, Mid-Atlantic, and lower Midwest regions of the US.

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1Q recap. While comps were in line with our model (-19.5% vs. our -20%E), this was better than feared given store closures (store fleet was closed for ~40% of the available selling days in the quarter). That said, adjusted EPS missed our forecast ($0.31 vs. our $0.52E) as gross margin pressure was more pronounced (down ~550bps on an adjusted basis vs. our -285bps estimate) and HIBB’s tax rate was higher than we had modeled (~$0.08 headwind). Importantly, inventory is in good shape exiting 1Q (-2.6% y/y), and the increase in reserves should mitigate markdown exposure going forward.

Strong digital growth a key positive. 1Q comps of -19.5% were in line with our expectations as robust digital growth (+110.5% y/y to ~22% of sales) offset significant store comp declines (down ~34%). 1Q’s digital performance was driven by a surge in traffic (up >80%) and increased conversion (up 26% y/y). In the second half of the quarter, 40% of digital sales were from new customers, reinforcing HIBB’s compelling suite of digital/omni-channel capabilities (including Klarna financing offers). Management also leaned into digital advertising at a time when some competitors pulled back, which contributed to market share gains during the quarter. Retaining these customers as other retailers re-open will be important to monitor going forward.

"Robust" trends QTD – sustainability remains a wildcard. Management noted "robust" comps QTD driven by continued strong digital sales and a return to positive brick-and-mortar comps as stores re-open. As of today, >1,000 stores are open (effectively the entire chain) vs. ~700 at the end of April, with many reporting "significant" comp increases upon their re-opening. While encouraging, HIBB’s business is notoriously volatile, and a portion of the strength is clearly stimulus-related (provided additional support to recent Jordan shoe launches). Our new 2Q comp estimate of +3.2% (up from prior -10%) balances the strong start with some moderation across June/July as stimulus benefits fade and the timing of back-to-school may shift across markets. Visibility, of course, is low.

Go-forward margin/expense dynamics. 1Q gross margin declined >700bps on a GAAP basis, with adjusted gross margin (excluding higher inventory reserves) down ~550bps. The decline in adjusted gross margin was driven by the mix shift to digital, as well as fixed cost deleverage on occupancy and warehouse/distribution. While the mix shift to digital will remain a structural headwind going forward, the magnitude of pressure should moderate from 1Q as store sales recover. When combined with leverage
on occupancy and warehouse/distribution in a positive comp environment, our model assumes 2Q gross margin down ~85bps. Shifting down the P&L, SG&A growth will be more normalized going forward (we model 2Q up slightly y/y vs. 1Q’s ~11% decline), but improved comps/gross margin have us raising our 2Q EPS estimate to ($0.11) from ($0.27).

**Strong liquidity position.** HIBB ended the quarter with $106M in cash on hand, which includes a $50M draw on the company’s $75M secured credit facility. In short, we continue to believe HIBB has ample liquidity and financial flexibility to navigate through these unprecedented times.

**Estimate revisions.** Despite our higher 2Q EPS estimate, the 1Q shortfall vs. our model plus lower 2H EBIT margins (higher mix of digital sales) have us reducing FY20E/FY21E to $0.90/$1.70 (from prior $1.20/$2.00).

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**Investment Thesis**

- **Key vendor actions suggest ongoing support.** Concerns over vendor direct selling efforts continue to weigh on sentiment around sporting goods retailers (including HIBB). While we agree a sale on Nike or Under Armour’s website represents a lost sale for retail partners, these vendors’ support for HIBB appears to remain strong. Given HIBB’s unique small market distribution footprint and track record of strong sell-through, we believe key vendors like Nike view HIBB as an important long-term partner. As such, we are not overly concerned about HIBB losing incremental allocations from key vendors anytime soon.

- **Entering the omni-channel payback phase.** HIBB’s multi-year modernization journey began back in 2014 and has included a variety of infrastructure, systems, and personnel investments. Several key deliverables occurred in 2017, including the rollout of a new store POS system and the launch of HIBB’s first transactional ecommerce website. The introduction of BOPIS/ROPIS capabilities and a mobile app followed in 2018, with Klarna financing launched in 2019. HIBB’s ecommerce business has quickly scaled ($125M in FY19 or ~10% of sales), and we expect momentum to continue in FY20.

- **Thoughts on City Gear.** HIBB’s acquisition of City Gear in 2018 bolstered the company’s presence among the younger fashion-forward/“sneakerhead” customer in urban areas. While HIBB sees an opportunity to grow the footprint in new and in-fill markets, management has also been focused on improving City Gear’s omni-channel capabilities. Some brands within City Gear’s assortment have proven additive to HIBB’s ~350 fashion specialty stores. In addition to improved buying power with key vendors, other potential long-term synergies include systems integration and leveraging expertise in customer loyalty.

- **Margins finding a floor?** HIBB’s small market strategy (less big box competition, more favorable lease terms) historically supported the company’s premium EBIT margin profile. While EBIT margins declined to ~4.4% in 2018 (from FY12’s peak of 14.2%), adjusted EBIT margins increased ~50bps in FY19 as comps returned to MSD% levels. We were optimistic HIBB’s EBIT margin profile was starting to find a floor; however, demand destruction from COVID-19 and an accelerated shift to digital channels seems likely to pressure EBIT margins in FY20.

- **Price target rationale.** Our $20 price target assumes shares trade at ~12x FY21E EPS, a premium to the stock’s three-year average of ~11x given HIBB’s improved competitive positioning.

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**Risks & Caveats**

- **High vendor concentration.** Nearly 80% of HIBB’s COGS are concentrated among three primary vendors, with Nike alone representing 68% of purchases in 2019. The loss of key vendor support or decline/discontinuation of vendor incentives could have a material adverse effect on business.
- **Systems investments.** Any potential disruptions associated with the implementation of recent (and future) IT systems could negatively impact HIBB's financial results.

- **Increased competition.** HIBB competes against a wide variety of retailers, including other full-line sporting goods stores, specialty shops, mass merchants, and catalog and internet retailers. Increased competitive pressures could require HIBB to reduce prices or increase ad/promo spending, which could have an adverse effect on sales and profitability.

- **Regional concentration of store base.** HIBB is particularly exposed to consumer spending trends in the South, Midwest, and Mid-Atlantic.

- **Economic conditions.** A contraction in consumer spending resulting from macroeconomic factors such as higher interest rates, rising fuel and energy costs, prolonged weakness in the housing market, increased unemployment levels, and lack of credit availability could impact sales.

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**Company Description**

Hibbett Sports operates sporting goods stores specializing in athletic apparel, footwear, and equipment. Hibbett offers a core selection of high-quality, branded products, primarily related to team sports. Stores are located in small and mid-sized markets in the South, Mid-Atlantic, and lower Midwest regions of the U.S.
1 Robert W. Baird & Co. Incorporated makes a market in the securities of HIBB.

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