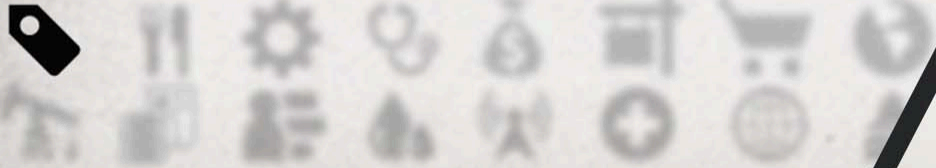


SECTOR SPOTLIGHT

RETAIL



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THIS DECK = CONCEPT CAR OF RETAIL

1

I WILL FLAT OUT REJECT THE 'IT CAN'T HAPPEN' PUSHBACK

Retail is deemed 'uninvestable', but it is very investable – if you can short, or pick the big winners as in the tech bubble. 20% of today's companies are likely to account for 90% of tomorrow's market cap. Bankruptcies should keep accelerating – both public and Private. Half of the winners will be companies you have never heard of. Returns are tee'd up to decline by 2,000bp – 4x the rate we saw in the Great Recession. And like it or not, there are plausible scenarios that tank content as powerful as Nike and Ralph Lauren if they don't invest.

2

SQUARE FOOTAGE MATH IS MORE BEARISH THAN BEARS THINK

We review the 5 #megacycles of retail back to the first Macy's store in 1858. One of the trends today is that the Strip Malls, Big Box Specialty and Off-Price centers – those that disintermediated Dept Stores from 1993-2010 – are now themselves being disintermediated. Like it or not, there's a 'square footage equivalent' associated with e-comm. By our math, 13.6bn in square footage today grows to 26bn by the end of #retail5.0. That implies square footage per capita goes from 43x to 76x.

3

A NEW KIND OF M&A

The 'no that deal can't happen' mindset is very JV. As in past periods of generational change, we see defensive generational deals. Content is key, but it's not King anymore. Now the 'Final Mile' wears that crown, and it will through #retail5.0. Next comes content, customer acquisition, vertical sourcing, and distribution. I'm completely 'valuation-agnostic' this climate – as will CEOs, Boards – and especially bankers. Valuation only matters when levered companies buy garbage at peak multiple on peak margins when a generational wave of deflation is over, and unit velocity declines – which will meaningfully take down margins.

RETAIL 4.0 = RISE OF STRIP CENTER, OFF PRICE

1995-2000

- 1994: Import Quotas start 10-year lift
- NAFTA
- 1997: AMZN IPO
- Strip Mall is born
- Ecomm 1% of retail sales. 2% of GAFO

2000-2005

- 2000: pets.com fails
- Regional mall growth slows to 1%
- DKS, HD, BBBY, KSS consolidate key categories & take mall traffic
- 'Off Price' concept grows

2005-2017

- 2007: Great Recession
- 9/2011: chewy.com born
- 2016 e-comm 12% of retail sales and 28% of GAFO
- 2017: Rise in Bankruptcies

2018-2020

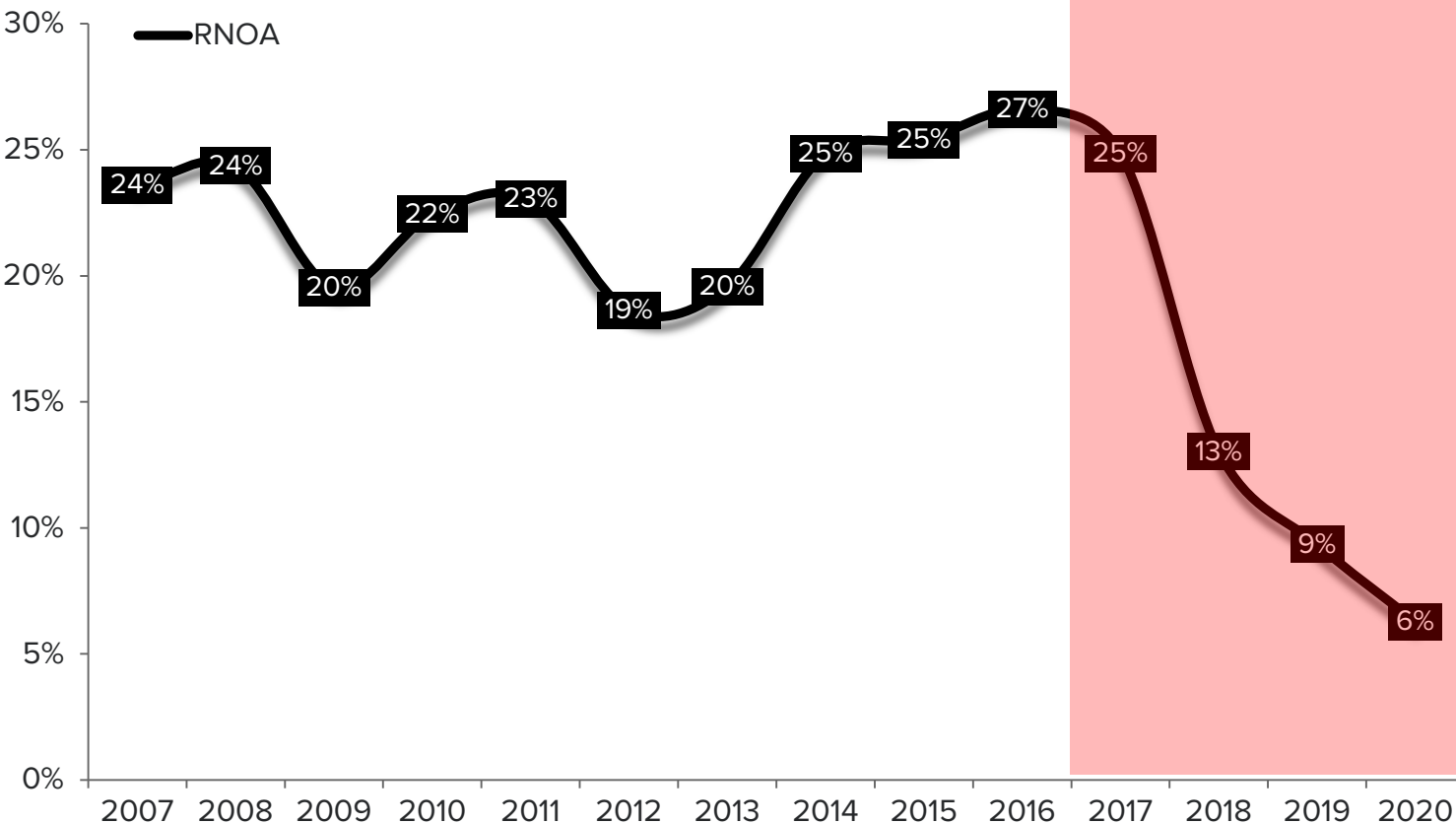
- 2018 Birth of the Amazon Store
- Sq ft goes from 14bn to 26bn



Deflation = Dept Store Disintermediation

RNOA WORSE THAN GREAT RECESSION

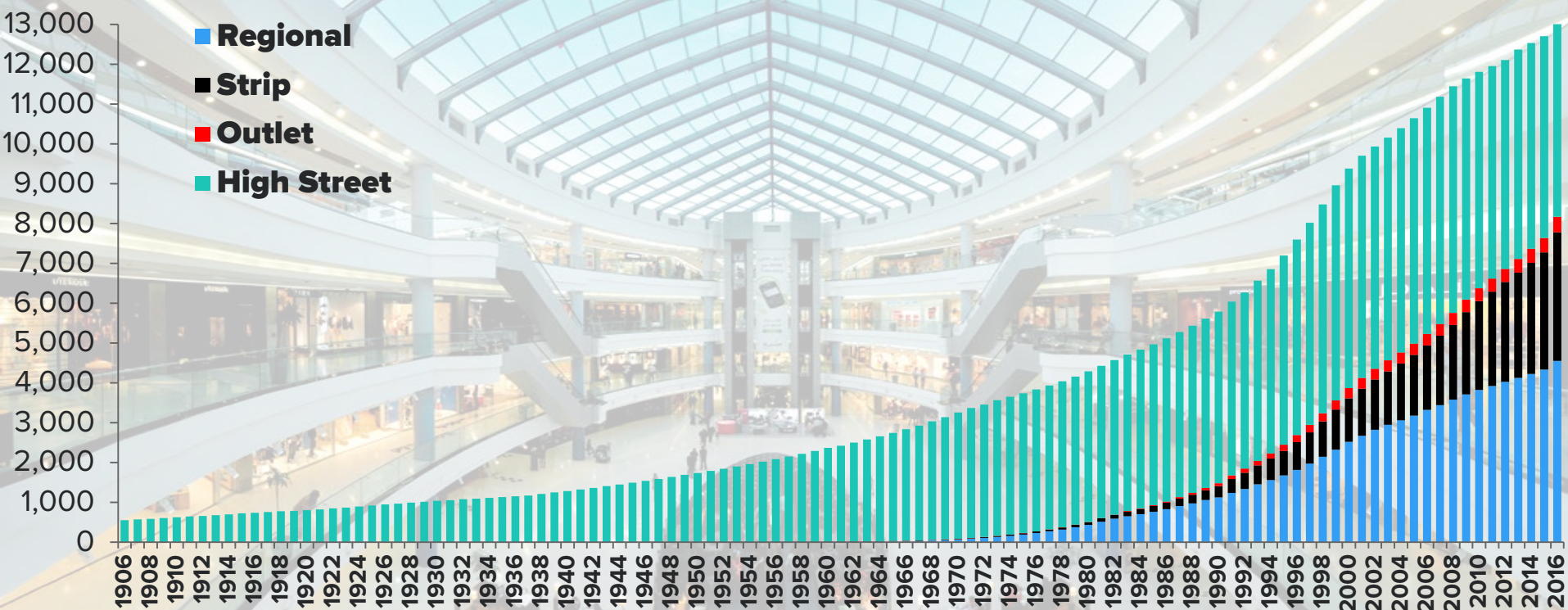
RETAIL INDUSTRY RNOA



NEWSFLASH

Stocks don't go up when this happens to returns – even the winners.

#FAKEESTATE 101 – THIS ALONE IS BEARISH



LONG TERM TRENDS IN REAL ESTATE

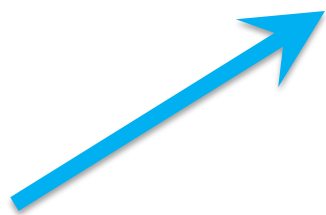
The proliferation in Strip Malls without declines in Regional Malls is the problem. I know, that's common sense. But there's your 'tough retail environment' and 'declining mall traffic'.

DOES ANYONE DISPUTE E-COM 12% - 34% IN 10-YEARS?

DIDN'T THINK SO....

Online
Penetration

12%

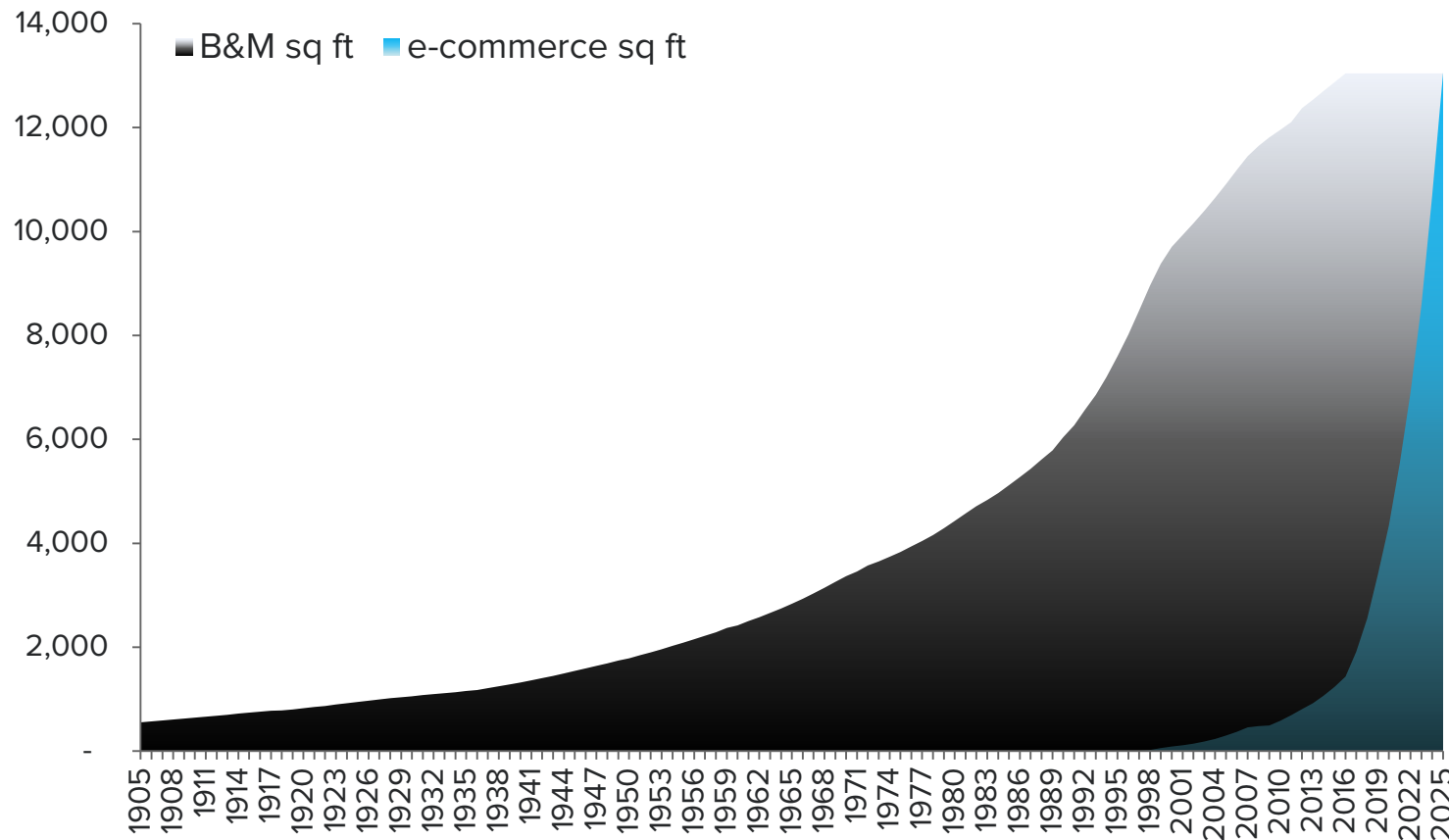


34%



...ENTER RETAIL 1.0—5.0

E-COMM SQ FT IN 10-YEARS

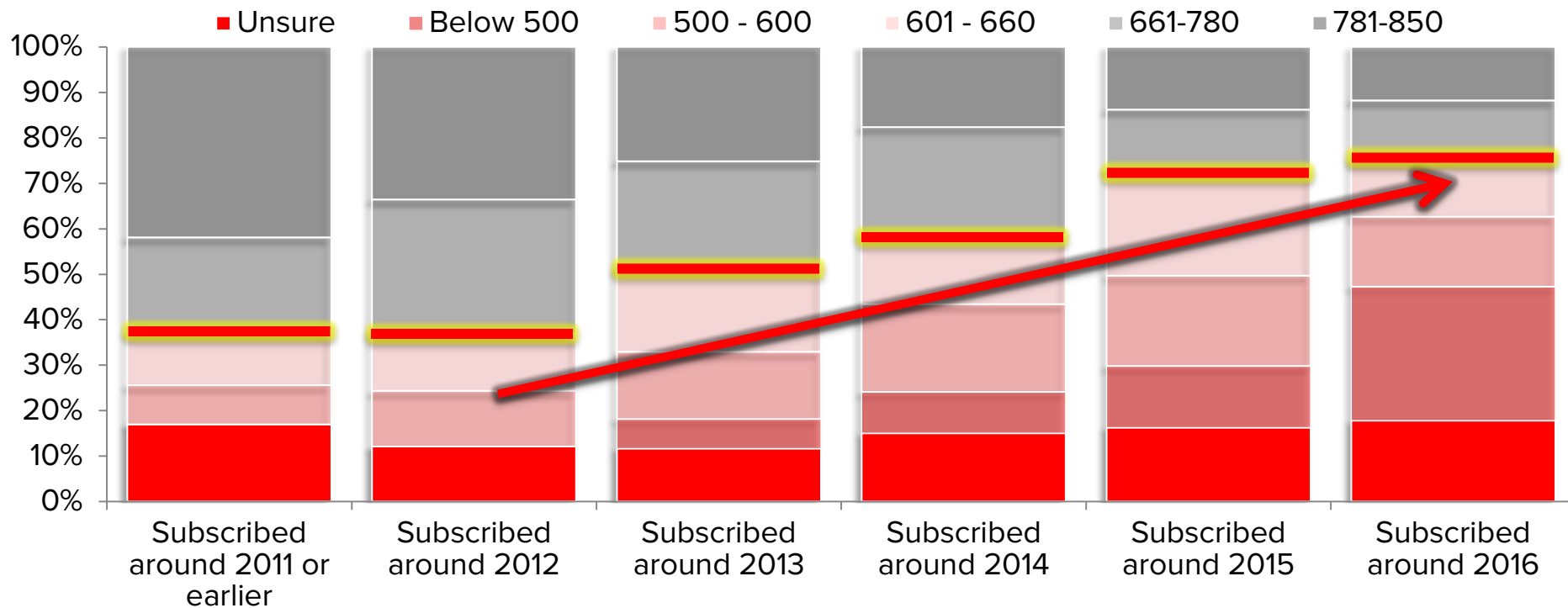


That blue area should scare every CEO out there.

But they probably have not done this math.

If they have, they think their Brands are better than they are – which means they're not closing stores fast enough.

PRIME MOVING MORE INTO SUBPRIME



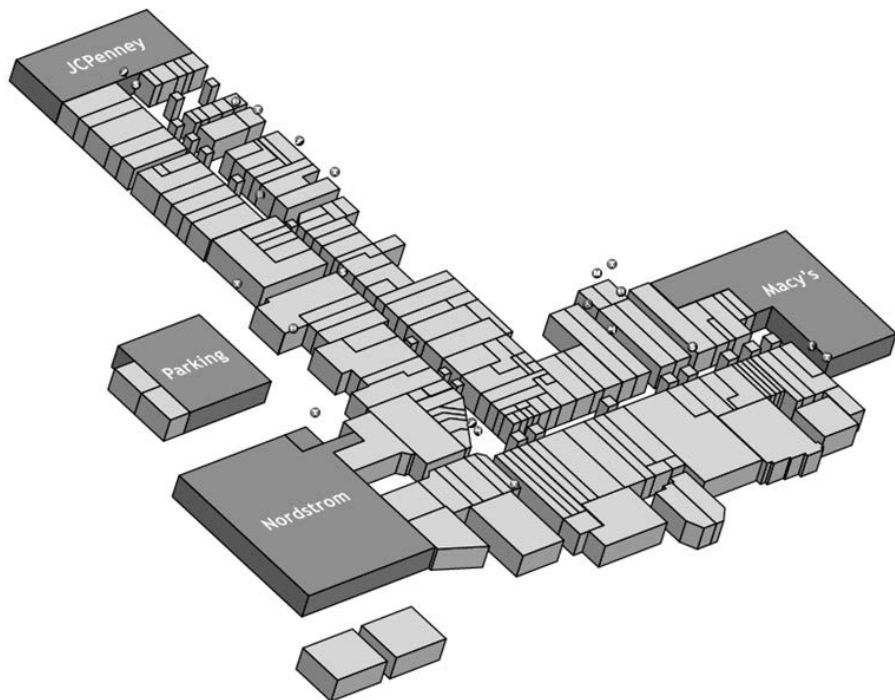
INCREMENTAL PRIME CUSTOMERS BY FICO SCORES

As Prime subscribers are added, Credit Scores get worse. Perhaps commonsensical, but this is a bigger trend than we thought we'd see. This is TGT bullish, and 'middle-America -retail' (WMT, TGT, KSS, JCP, BBBY, WSM, Rx front-end, Dollar Stores, etc...) bearish.

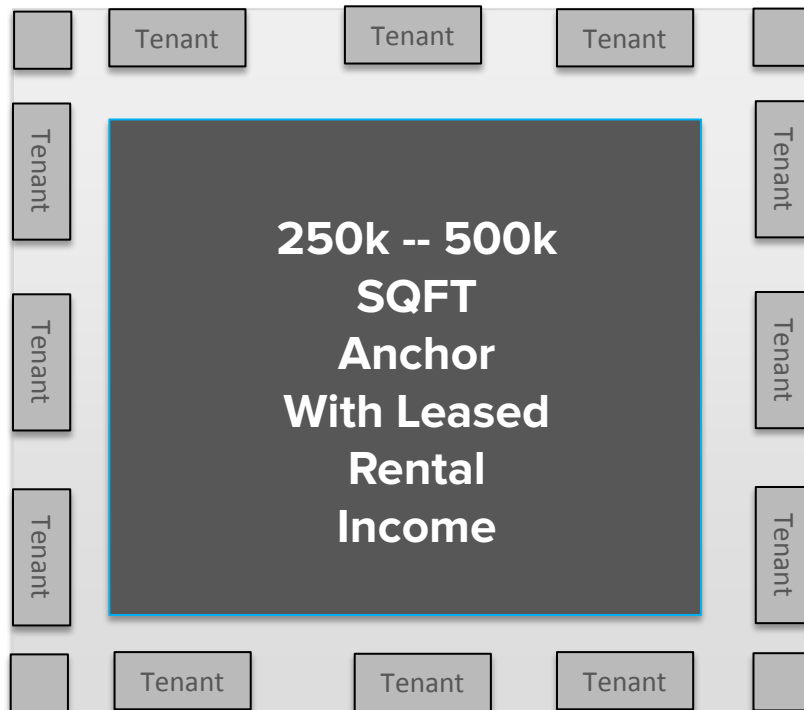
SHOW A RETAIL 5.0 CENTER

SQUARE FOOTAGE IS NOT A ZERO SUM GAME

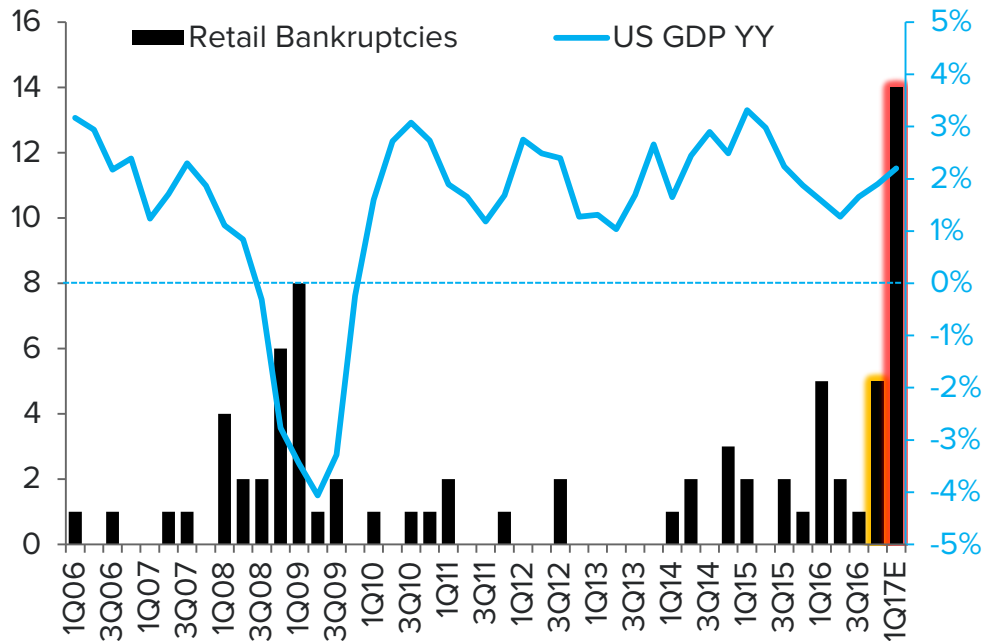
3.0 Shopping Center



5.0 Shopping Center



BANKRUPTCIES AND GROWTH #ACCELERATING?



RETAIL VS MACRO BIFURCATION

Retail Bankruptcies are accelerating to all time high levels, while US GDP growth is strengthening. Something isn't right.

CONFLUENCE

- Brands going direct
- AMZN investing on one end
- WMT on the other
- Lower profitability Survivors (TGT, COST) in the middle – but surviving
- Marginals left out in the cold
 - KSS
 - Claires
 - Party City
 - Etc...
- Deflation stalling at a minimum. That's your Bullish case. And that's Bearish.

MORE BANKRUPTCIES TO COME

Bankrupt



At Risk of \$0 Equity

| | |
|------|----------------|
| SSI | CBK |
| GNC | HBI |
| ICON | BONT |
| SPWH | PIR |
| RCII | SHLD |
| TPX | Claires |
| TLRD | Sears |
| TCS | J Crew |
| BOOT | True Religion |
| PRTY | Gymboree |
| JCP | Academy |
| KSS | Neiman |
| ASNA | Nine West |
| FRED | David's Bridal |

High Risk



THE BANKRUPTCY SPECTRUM

'Stuck in the middle' + Leverage – Cash Flow = Bad

The 'junk company short call that didn't work for the past decade should finally start working.'

THINK BIG FOLKS, CROSS SECTOR DEALS = NEW REALITY



URBAN OUTFITTERS



The
Washington
Post

News Corp



RETAIL IDEA LIST

LONGS

BEST LONG IDEAS

| | | TRADE | TREND | TAIL |
|-------------|-----------------------|-------|-------|------|
| NKE | Nike, Inc. | ✓ | ✓ | ✓ |
| *RH | Restoration Hardware | ✓ | ✓ | ✓ |
| DKS | Dick's Sporting Goods | ✓ | ✓ | ✓ |
| KATE | Kate Spade | ✓ | ✓ | ✓ |

OTHER ACTIVE LONGS

| | | | | |
|------------|----------|---|---|---|
| WMT | Wal-Mart | ✓ | ✓ | ✗ |
|------------|----------|---|---|---|

AMZN Amazon.com

LONG VETTING BENCH

| | |
|-------------------|---------------------------|
| ORLY | O'Reilly Automotive, Inc. |
| MIK | Michael's Stores |
| BBY | Best Buy |
| ETH | Ethan Allen Interiors |
| ABF-GB | ABF/Primark |
| FINL | Finish Line |
| MALL REITS | |
| | GGP, TCO, SPG, VNO |
| | CBL, MAC, SRG |

*Hedgely has temporarily suspended coverage, effective March 5, 2017.

SHORTS

BEST SHORT IDEAS

| | | TRADE | TREND | TAIL |
|------------|--------------|-------|-------|------|
| HBI | HanesBrands | ✗ | ✗ | ✗ |
| KSS | Kohl's | ✗ | ✗ | ✗ |
| CRI | Carters Inc. | ✗ | ✗ | ✗ |
| TGT | Target | ✗ | ✗ | ✗ |

OTHER ACTIVE SHORTS

| | | | | |
|-------------|--------------------|---|---|---|
| VFC | VF Corp | - | ✗ | ✗ |
| PVH | PVH Inc | - | ✗ | ✗ |
| TJX | TJX, Inc | - | ✗ | ✗ |
| JILL | J Jill | ✓ | ✓ | ✗ |
| RL | Ralph Lauren | - | ✗ | ✗ |
| UA | Under Armour | ✗ | ✗ | ✗ |
| W | Wayfair | - | ✗ | ✗ |
| LULU | Lululemon | - | - | ✗ |
| HIBB | Hibbett Sports | ✗ | ✗ | ✗ |
| JCP | JC Penney | ✗ | ✗ | ✗ |
| PRTY | Party City | ✗ | ✗ | ✗ |
| BBBY | Bed, Bath & Beyond | ✗ | ✗ | ✗ |
| WSM | Williams-Sonoma | ✗ | ✗ | ✗ |
| M | Macy's | - | ✗ | ✗ |
| JWN | Nordstrom | - | ✗ | ✗ |

SHORT VETTING BENCH

| | |
|---------------|----------------|
| FL | Foot Locker |
| TIF | Tiffany |
| DG | Dollar General |
| DLTR | Dollar Tree |
| FRED | Fred's |
| ROST | Ross Stores |
| DOL-CA | Dollarama |
| GOOS | Canada Goose |

The Vault -- Vetted in the Past Six Months, But No Call Today

| | | | |
|--------------|---------------------|---------------|---------------------|
| GIL | Gildan | COH | Coach |
| GME | Gamestop | KORS | Michael Kors |
| COLM | Columbia Sportswear | ADS-DE | Adidas |
| CTC.A | Canadian Tire Corp | ANF | Abercrombie & Fitch |
| GCO | Genesco | DECK | Decker's |
| LB | L Brands | FRAN | Francesca's |
| HOME | At Home | GIII | GIII Apparel |
| GPS | Gap, Inc | ICON | Iconix |
| TLRD | Tailored Brands | HD | Home Depot |
| SKX | Skechers | LOW | Lowe's |
| ELY | Callaway Golf | LUX | Luxxotica |
| GNC | GNC Inc | OLLI | Ollie's |
| VSI | Vitamin Shoppe | TSCO | Tractor Supply |
| FOSL | Fossil Group, Inc | WWW | Wolverine Worldwide |
| GPRO | GoPro | HBC | Hudson's Bay |
| ULTA | Ulta Salon | | |