Burlington

MFIF
Minutemen Fixed Income Fund

Burlington Stores, Inc. (NYSE: BURL)

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We recommend a marketweight position on BURL's 6.25% Sr. Secured notes of 2025. Burlington, formerly known as Burlington Coat Factory, is an American off-price/discount department store, with 739 stores in 40 states and Puerto Rico. BURL is the smallest of the three major players in the off-price retail industry, joined by investment grade companies TJX and ROST. As with all retail stores, BURL has been under immense pressure amidst Covid-19 to offset losses and get back on track to pre-pandemic profitability. BURL's robust pipeline for new stores is set to stimulate growth in its topline. Additionally, strong inventory turnover and opportunistic expansion of pack-and-hold will offset 2Q20 sales declines. While we are confident in BURL's growth opportunities, we are wary of the company's inability to adapt to the changing retail environment, especially in the wake of Covid-19. As a result, we do not believe that the positive effects of their store growth and inventory management will tighten its notes to an attractive level and provide an enticing buying opportunity - thus we maintain the market's current valuation of these notes.

Figure 1: Capitalization Table

BURL Capitalization Table						
NTM adj. EBITDA			**828.2**	**2.79x**		
LTM adj. EBITDA			78.5			
Outstanding Debt Metrics & Leverage						
Type of debt	**Rate (%)**	**Maturity**	**Debt Outstanding ($MM)**	**xLTM Adj. EBITDA**	**Price**	**Yield**
REV A 1L USD	LIBOR + 150bps	6/29/23	250		-	-
TL B 1L USD	LIBOR +175bps	11/17/24	958		-	-
Total First Lien Notes			**1,208**	**15.39x**		
Sr. Secured Notes 25	6.250%	4/15/25	300		106.17	3.91%
Total Sr. Secured Notes			**1,508**	**19.21x**		
Sr. Unsecured Notes 25	2.250%	4/15/25	805		130.24	-3.94%
Total Sr. Unsecured Notes			**2,313**	**29.46x**		
Total Debt			**2,313**	**29.46x**		
Market Capitalization			13,286			
Less: Cash			1,077			
Enterprise Value			**14,522**			

**Source: Bloomberg*

Bond Data

Bond Maturity: 04/15/2025

Rank: Sr. Secured

Rating: Ba1/BB+

Price: $106.17

YTW: 3.907%

Coupon: 6.25%

Z-Spread: 383.39 bps

Call Date: 04/15/2022 @ $103.13

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Robust Pipeline for New Stores

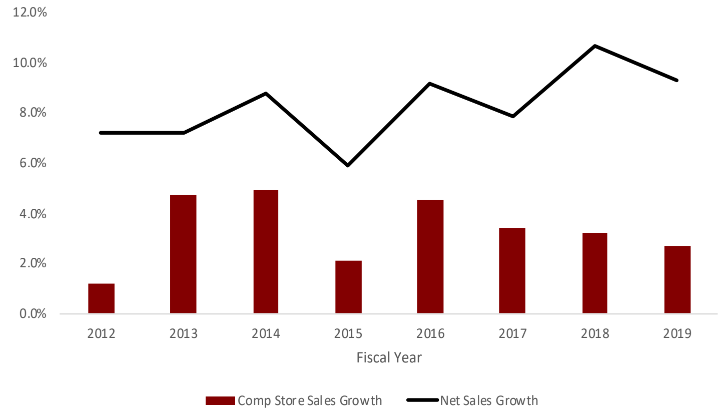
In 2015, BURL established its C-Point Strategy - the goal of which is to identify potential locations for new stores. BURL is working to take advantage of real estate opportunities especially from popular retail bankruptcies and increase its store fleet to 1,000+ stores (BURL currently operates 739 stores). Having opened/converted (through remodeling) ~400 net stores to its more productive "brand standard" sub-60K sq ft format since 2015, the next leg in its brand transformation involves saturating the market of the small store format (25K sq ft). BURL stores generate ~$200 sales/sq ft which is roughly half the level of TJX/ROST, however, BURL stores generate ~$10M in an avg year vs ROST/TJX at ~$9M. There is opportunity for P/L benefits especially as it pertains to store sales productivity. New stores of less than 60K sq. ft have shown sales productivity 20% higher than its fleet average. Smaller stores mean lower SG&A, lower rent, and fewer expenses as whole. As smaller stores open, BURL's focus remains on increasing sales growth and productivity. 4Q19 was BURL's 28th consecutive quarter of positive comp sales growth. BURL's off-price model will prove to be an advantage over other department store peers and will allow for positive comp sales growth to return post pandemic. BURL has reduced its net new store projections for FY 20 from 58 to 36 in order to preserve liquidity, but its long-term outlook to 1,000 stores remains. BURL is confident in its liquidity position, especially after its debt raise in April. CFO John Crimmins pointed to ending 2Q liquidity of $1,197 million, including $1,077 million in unrestricted cash and $120 million in availability on its ABL facility, when guiding that BURL had ample liquidity to last beyond the end of FY20 with all stores closed in a downside scenario. Thus, we remain confident in the growth opportunities tied to moving forward with its fleet expansion, which does not pose a concern from a liquidity perspective.

Figure 3: Comps Cash Conversion Cycle

	DSO	DIO	DPO	CCC
BURL	3 days	59 days	50 days	**12 days**
KSS	0 days	89 days	25 days	63 days
JWN	5 days	63 days	41 days	27 days
DDS	2 days	130 days	43 days	89 days
TJX	5 days	53 days	25 days	33 days
ROST	3 days	67 days	34 days	36 days

**Source: Company Filings, MFIF Analysis*

Figure 2: Comp and Net Sales Growth



**Source: Company Filings*

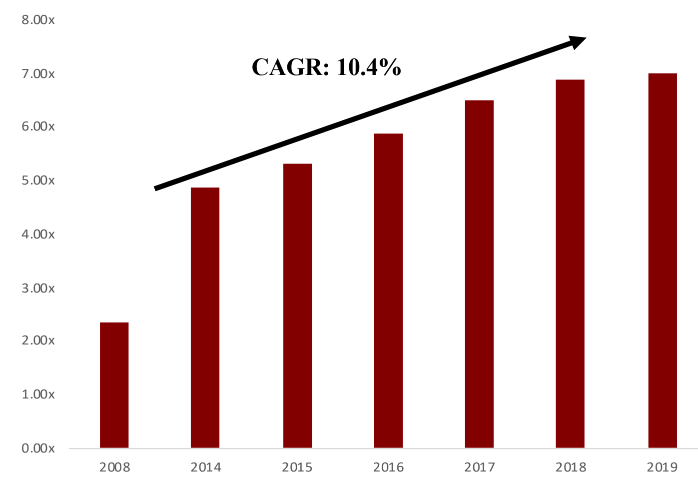
Strong Inventory Turnover and Opportunistic Expansion of Pack-and-Hold to Offset 2Q20

In response to the ongoing pandemic, BURL has shifted its focus to aggressively slim its inventory, especially during the shutdown period. They succeeded in doing so and created lean inventory numbers. The first half of 2Q20 started off extremely successful, as pent up demand from the lockdowns drove consumers back to BURL stores. Replenishment delays in 2H left BURL with depleted inventory. Demand dropped as a result and open store sales decreased 14%. We believe this misstep is attributable to the overall uncertainty of Covid - but BURL has plenty of opportunities to counteract these losses. BURL's comparable store inventory turnover has improved 198% since 2008 and is on track to continue. Reducing aging stockpiles has contributed to this growth - BURL's inventory aged 91 days or older has significantly decreased in the years since 2008 ($551M down to $34M today). As an off-price retailer, BURL is in a unique position to take advantage of attractive buying opportunities compared to its department store peers. Off-price retailers have greater flexibility to chase opportunistic buys due to the fact that they are not contractually obligated to brands like other department stores. The off-price business model employs the "pack-and-hold" strategy, where items are bought out of season and stored for later use. Store closings and supply chain disruption as a result of Covid create a perfect opportunity for BURL to purchase inventory at a discount. Spring and Summer merchandise is sitting stale in warehouses and stores due to the depressed retail environment, creating a great buying opportunity for BURL to increase pack-and-hold inventory. While the pandemic has impacted BURL's sales as evidenced by 2Q20, BURL remains at a strategic advantage to other big-box retailers. BURL has expanded its warehousing storage capacity to support its new pack and hold expansion strategy which will be pivotal in the months to come. We believe its recent improvements in managing inventory will lead to a decrease in DIO, contributing to an improved CCC, especially when compared to peers.

Inability to Adapt to the Changing Retail Environment

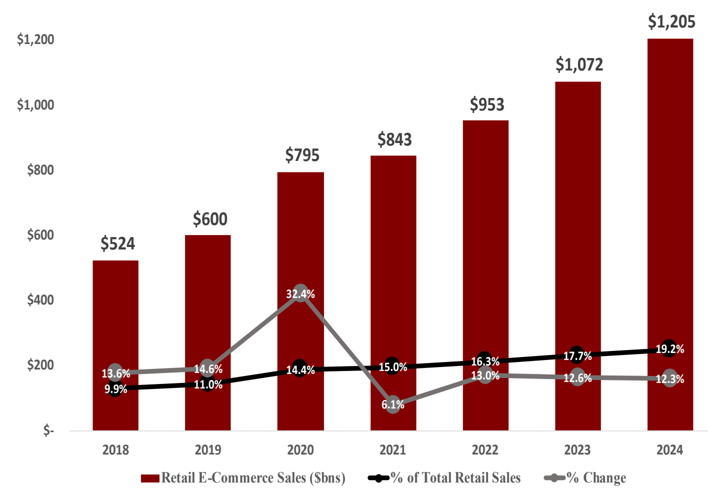
During pre-pandemic times in the retail industry, off-price retail stores were somewhat less susceptible to the growing threat of e-commerce operations compared to other department stores. Off-price retailers have argued that the "treasure hunt" experience is less replicable by online shopping. CEO Michael O'Sullivan decided to cease e-commerce operations in 4Q2019, citing that it only contributed to 0.5% of BURL's revenue and therefore was no longer worth pursuing. Expedited changes relating to the digitization of retail commerce amidst the Covid-19 pandemic make O'Sullivan's move seem questionable. When non-essential businesses shut down across the nation, BURL was in a zero-revenue environment. On the other hand, department store peers like KSS, and JWN, saw spikes in their digital penetration upwards of 58%. E- commerce sales are expected to account for about 15% of total retail sales in 2021 and this number is only expected to increase. We believe BURL's decision to exit the e-commerce market will not yield favorably in the future, given current competitor's success in the e-commerce space. In addition to its lack of digital sales, BURL has also failed to adapt to retail trends on the loyalty front. All of BURL's peers in both the off-price and department store industry have established loyalty and rewards programs which aid in keeping its customers devoted during downturns. BURL only just rolled out a private label credit card after a pilot in 2H2019. Management has not provided much color regarding its success, and it will take time for this loyal customer base to materialize. As a result, BURL is unable to capitalize on the benefits of loyalty and rewards programs. Had BURL maintained its e-commerce presence and shifted its focus to make its expansion a priority, as well as introduced a loyalty program much earlier than it did, we would have been more confident in an overweight position, however we believe its inability to adapt to a changing retail industry will keep it from reaching its full growth potential.

Figure 4: Comparable Store Inventory Turnover



**Source: Company Filings*

Figure 5: US Retail E-Commerce Sales 2018-2024



**Source: eMarketer, MFIF Analysis*

Risks

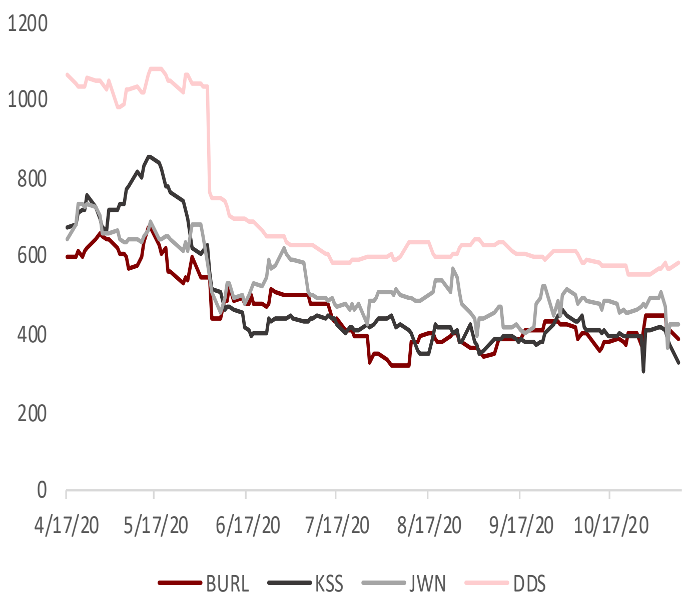
- **Renewed store lockdowns through 2021 would threaten BURL's liquidity – especially as it continues to open new stores**
- **Warehouse and vendor inability to replenish inventory demand can lead to lengthier inventory turnover, DIO, and ultimately increased CCC**
- **Lack of inventory availability within the closeout channel or brands pulling out of the off-price channel could negatively impact comp sales**
- **Inability to maintain historically lean inventory numbers and high inventory turnover**

Figure 6: Competitor Financial Performance and Health

COMPS ($MM)	BURL	KSS	JWN	DDS
Market Cap	13.29B	4.1B	2.6B	1.1B
EV	14,522	8,700	6,847	1,779
LTM Revenue	5,804	17,292	12,191	5,158
FY19 EBITDA	886	2,025	1,455	402
FY19 EBITDA Margin	15.3%	11.7%	11.9%	7.8%
FCF	48	673	-730	-15
Debt	2,313	3,467	4,164	796
Debt/ FY19 EBITDA	2.6x	1.7x	2.9x	2.0x
FCF/Debt	2%	19%	-18%	-2%
Individual Security	**BURL**	**KSS**	**JWN**	**DDS**
Bond Maturity	4/15/25	7/17/25	5/15/25	7/15/26
Credit Rating	Ba1/BB+	Baa2/BBB-	Baa2/BBB-	Baa3/BB-
Price	106.2	102.3	110.3	109.3
Yield	3.907%	3.659%	4.478%	5.824%
Z-Spread	383.4bps	328.2bps	426.3bps	584.0bps
Spread per Turn of Leverage	146.86	191.70	148.96	295.17

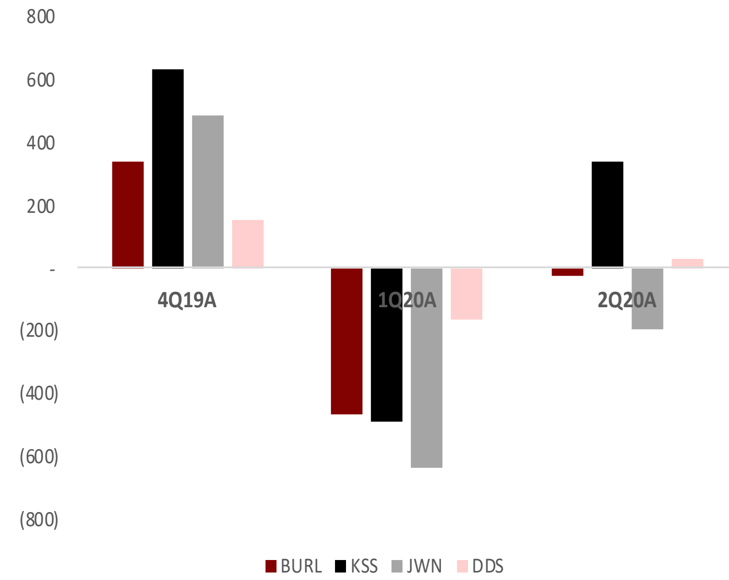
**Source: Company Analysis, MFIF Analysis*

Figure 7: Z -Spread



**Source: Bloomberg, Company Analysis, MFIF Analysis*

Figure 7: Covid Impact on Retail EBITDA



**Source: Company Analysis, MFIF Analysis*

Relative Value

It is important to note that the "off-price" subdivision of the department store industry is small. BURL is 1 of 3 major off-price retailers, along with TJX and ROST (Investment Grade). For the purposes of this relative value valuation, BURL is compared to department stores KSS, JWN, and DDS. BURL and its comparisons have traded similarly in the past. The most notable comparison in terms of z-spread similarity is KSS, which for the past 6 months, has alternated between trading tighter or wider than BURL. KSS is currently trading at 328 bps, with BURL trading ~55bps wider, followed by JWN and DDS which are trading ~98 and ~255 bps wider respectively.

JWN's notes tightened over 130bps at the end of last week, as the company announced a major clearance sale, amounting to upwards of 90% off. The market's initial reaction was unjustified, as JWN's credit profile is weak, and its segments are consistently underperforming. JWN's high exposure to malls as opposed to BURL and KSS (both of which focus on stand-alone store locations) also put it at risk, thus justifying its eventual widening back out to ~584bps. When comparing credit metrics, BURL's leverage of 2.6x is similar to JWN and DDS. KSS is ~1x less levered than BURL and has a significantly higher FCF/Debt ratio than BURL and its peers.

We are confident in BURL's potential to grow given its new store fleet strategy, as well as its significant advantage, inventory wise, over department stores in the wake of the pandemic. KSS may not have access to discounted inventory at the same levels as BURL, but its online presence has grown over 58% y/y since the start of the pandemic, and it has the industry leading loyalty program. KSS' superior credit profile and online presence justifies its spread to BURL.

Figure 11: Summary Model

BURLINGTON STORES, INC (NYSE: BURL)

Fiscal year	FY18A	FY19A	1Q20A	2Q20A	3Q20P	4Q20P	FY20P	FY21P	FY22P
Fiscal year end date	*2/2/19*	*2/1/19*	*5/2/20*	*8/1/20*	*11/30/20*	*2/28/21*	*2/28/21*	*2/28/22*	*2/28/23*
INCOME STATEMENT ($MM)									
Net Sales	6,643.1	7,261.2	798.00	1,009.88	1,384.84	2,090.93	5,283.64	7,134.42	7,633.83
Other Revenue	25.4	25.2	3.53	2.45	4.80	7.24	18.01	24.71	26.44
Total Revenue	**6,668.5**	**7,286.4**	**801.5**	**1,012.3**	**1,389.6**	**2,098.2**	**5,301.7**	**7,159.1**	**7,660.3**
Cost of Sales	(3,868.12)	(4,228.74)	(782.18)	(547.55)	(751.63)	(1,134.86)	(3,216.22)	(3,872.25)	(4,143.30)
Gross Profit	**2,800.36**	**3,057.66**	**19.34**	**464.78**	**638.01**	**963.31**	**2,085.43**	**3,286.89**	**3,516.97**
Selling, General, Administrative	(2,018.74)	(2,228.18)	(485.09)	(491.60)	(474.42)	(716.31)	(2,167.41)	(2,444.11)	(2,615.20)
Depreciation and Amortization	(217.88)	(210.72)	(54.29)	(54.40)	(54.34)	(59.57)	(222.61)	(251.31)	(264.88)
Operating Profit (EBIT)	**554.40**	**614.82**	**(526.32)**	**(82.30)**	**109.25**	**187.42**	**(311.95)**	**591.47**	**636.89**
Interest Expense	(55.99)	(50.83)	(14.69)	(28.36)	(24.03)	(5.60)	(72.69)	(56.04)	(54.97)
Income Before Tax	**507.58**	**580.53**	**(539.09)**	**(109.84)**	**89.54**	**184.73**	**(374.65)**	**548.00**	**595.02**
Income Tax (Benefit) Expense	(92.84)	(115.41)	205.36	63.06	(22.38)	(46.18)	199.85	(137.00)	(148.75)
Net (loss) Income	**414.75**	**465.12**	**(333.73)**	**(46.78)**	**67.15**	**138.55**	**(174.81)**	**411.00**	**446.26**

OPERATING METRICS	FY18A	FY19A	1Q20A	2Q20A	3Q20P	4Q20P	FY20P	FY21P	FY22P
Gross Margin	42.0%	42.0%	2.4%	45.9%	45.9%	45.9%	39.3%	45.9%	45.9%
SG&A/Sales	30.4%	30.7%	60.8%	48.7%	34.3%	34.3%	41.0%	34.3%	34.3%
Operating Margin	8.3%	8.4%	-65.7%	-8.1%	7.9%	8.9%	-5.9%	8.3%	8.3%
Tax Rate	18.3%	19.9%	38.1%	57.4%	25.0%	25.0%	53.3%	25.0%	25.0%

EBITDA RECONCILIATION	FY18A	FY19A	1Q20A	2Q20A	3Q20P	4Q20P	FY20P	FY21P	FY22P
Net Income	414.7	465.1	(333.7)	(46.8)	67.2	138.6	(174.8)	411.0	446.3
(+) Interest	56.0	50.8	14.7	28.4	24.0	5.6	72.7	56.0	55.0
(+) Taxes	92.8	115.4	(205.4)	(63.1)	22.4	46.2	(199.8)	137.0	148.8
(+) Depreciation & Amortization	217.9	210.7	54.3	54.4	54.3	59.6	222.6	251.3	264.9
EBITDA	**781.5**	**842.1**	**(470.1)**	**(27.1)**	**167.9**	**249.9**	**(79.4)**	**855.3**	**914.9**
(+) Stock Based Compensation	35.5	43.9	17.4	12.7	9.9	9.4	30.0	40.6	43.4
Adj. EBITDA	**816.9**	**886.0**	**(452.8)**	**(14.4)**	**177.8**	**259.3**	**(49.3)**	**895.9**	**958.3**

FCF RECONCILIATION	FY18A	FY19A	1Q20A	2Q20A	3Q20P	4Q20P	FY20P	FY21P	FY22P
(+) EBIT*(1-Tax Rate)	(171.3)	(193.7)	199.8	46.8	(28.4)	(47.6)	75.5	(151.0)	(162.5)
(+) Depreciation & Amortization	217.9	210.7	54.3	54.4	54.3	59.6	222.6	251.3	264.9
(-) Capital Expenditure	(295.8)	(328.4)	(62.5)	(71.3)	(81.1)	(122.4)	(337.2)	(417.8)	(447.0)
(-) Change in NWC	60.0	(43.6)	(199.5)	214.0	63.8	(55.7)	22.6	(24.2)	(19.2)
FCF	**254.4**	**363.6**	**(133.3)**	**(265.5)**	**(5.4)**	**135.6**	**(363.7)**	**310.8**	**324.6**

CREDIT METRICS	FY18A	FY19A	1Q20A	2Q20A	3Q20P	4Q20P	FY20P	FY21P	FY22P
Cash	112.27	403.07	596.61	1,230.55	3,487.55	2,712.39	1,230.55	920.92	1,068.22
Debt	983.64	1,001.72	2,304.09	2,161.17	2,313.03	2,313.03	2,313.03	2,063.03	2,063.03
Debt/EBITDA	1.3x	1.2x	10.8x	84.7x	253.5x	-29.1x	-29.1x	2.4x	2.3x
Net Leverage	1.1x	0.7x	8.0x	36.5x	-128.7x	5.0x	-13.6x	1.3x	1.1x
EBITDA/Interest	14.0x	16.6x	4.1x	0.4x	0.1x	-1.1x	-1.1x	15.3x	16.6x

**Source: MFIF Analysis, SEC Filings*