Successful Danger Zone Pick Continues to Outperform

Sears Holdings Corp (SHLD: $3/share) – down 79% vs. S&P up 74%

Sears Holdings Corp was originally selected as a Danger Zone pick on 4/22/13. At the time of the report, the stock received a Very Unattractive rating. Our short thesis highlighted four main issues:

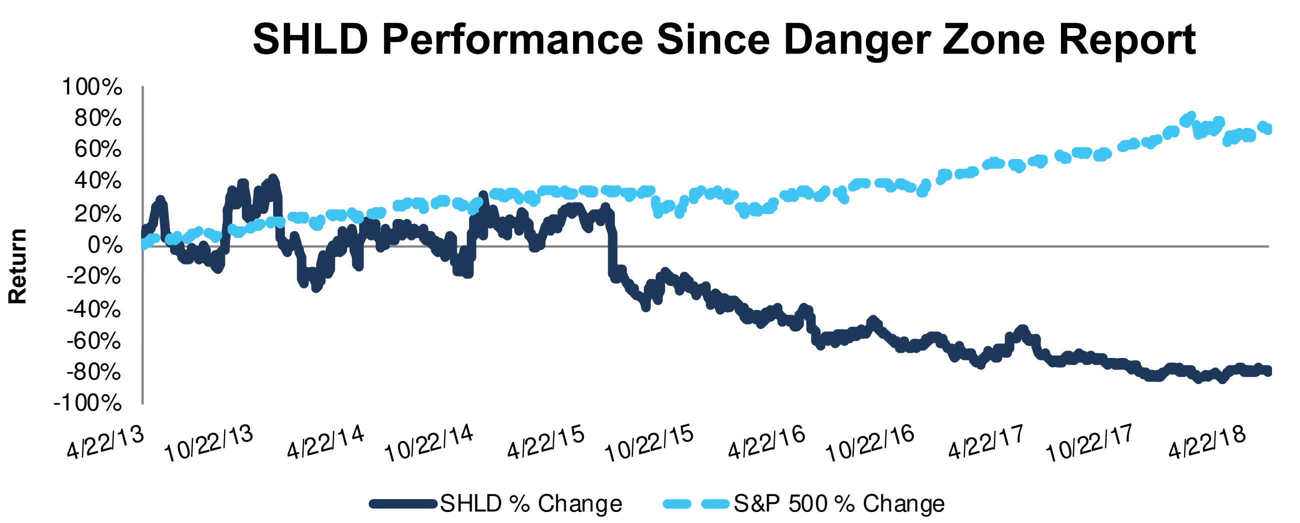
1. Hidden liabilities (underfunded pensions, off-balance sheet debt, and deferred tax liabilities) that lowered the reported value of the firm
2. Declining revenue and after-tax operating profit (NOPAT)
3. A weak competitive position relative to big-box and online retailers
4. Overly optimistic expectations baked into the stock price

We added the stock to our Focus List – Short Model Portfolio on 11/3/17, and it is down 38% vs S&P up 5%.

Sears' struggles have been widely documented. The company struggled to compete with low price retailers (such as Walmart (WMT)) and failed to adapt to e-commerce. While the combined Sears once had 3,500 stores (after it merged with K-Mart in 2005), it now has less than 900. SHLD recently announced plans to close more stores after reporting its 26th consecutive quarter of declining sales.

Since our original Danger Zone report, SHLD has significantly outperformed as a short position, falling 79% (after adjusting for the spin-off of Lands' End (LE) in 2014) compared to a 74% gain for the S&P 500.

Figure 1: SHLD vs. S&P 500 – Price Return: Successful Short



Sources: New Constructs, LLC and company filings
Note: Gain/Decline performance analysis excludes transaction costs and dividends.

SHLD still earns a Very Unattractive rating and has a Bankruptcy Threat analyst note, as noted in its 2017 10-K: "our historical operating results indicate substantial doubt exists related to the Company's ability to continue as a going concern."

We hope readers have been able to protect their portfolios from this stock while it fell in a strongly rising market.

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Disclosure: David Trainer, Kyle Guske II, and Sam McBride receive no compensation to write about any specific stock, style, or theme.

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