24-232
Revised June 20, 2026

Five Below, Inc.

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As he approached his one-year anniversary at Fidelis Capital Investments, a boutique hedge fund specializing in fundamental value investing, research analyst Kyle McLaren noticed that discount retailer Five Below had filed its annual report for the fiscal year ended February 3, 2024. The filing reminded him of his interview with Fidelis nearly a year earlier.

As part of the interview process, Fidelis required candidates to complete a financial statement forecasting and valuation exercise. McLaren was assigned Five Below and provided with a brief company overview, Five Below's annual report for the fiscal year ended January 28, 2023, and a spreadsheet containing the company's historical financial statements. He was asked to forecast the company's financial statements over the next seven years using assumptions provided by Fidelis and then estimate the company's intrinsic value. At the time McLaren completed the exercise, Five Below's stock price was approximately $200 per share.

Now that Five Below's results for the fiscal year ended February 3, 2024 were available (**Exhibit 1**), McLaren was curious to see how accurately his model had performed during its first year.

Company Overview

Five Below carved out a unique niche in the retail industry by targeting preteens, teens, and young adults with a wide range of trendy products priced primarily at $5 or less. Founded in 2002 by David Schlessinger and Tom Vellios, the company opened its first store in Wayne, Pennsylvania.[1] The founders were no strangers to the retail business, having previously co-founded the successful toy

[1] "Zany Brainy execs to open discount chain," *Philadelphia Business Journal*, September 23, 2002, https://www.bizjournals.com/philadelphia/stories/2002/09/23/daily3.html (accessed September 2024).

This case was prepared by 2024 MBA Justin Morris and Senior Lecturer Christopher Noe.

retailer Zany Brainy.[2] Their vision for Five Below was to create an environment that encouraged exploration and surprise, similar to that of retailers like Marshalls or TJ Maxx. In 2018, then-CEO Joel Anderson described the shopping experience at the company's stores, commenting, "When you walk into one of our stores, you'll discover things you didn't know you wanted. It's like a treasure hunt."[3]

Five Below distinguished itself among brick-and-mortar retailers through its resilience against the rise of online shopping. The company created a protective moat around its business by offering products often described as "unamazonable" – items priced so low that selling them profitably was challenging even for e-commerce giant Amazon. A key factor drawing customers into Five Below's physical locations was the lack of viable home delivery options for these low-cost goods.

Five Below rapidly expanded across the U.S., reflecting its strategic success. By early 2023, the company operated 1,340 stores in 42 states.[4]

[2] Ibid.

[3] Suzanne Kapner, "Five Below, the Amazon-Proof Store," *The Wall Street Journal*, November 2, 2018, https://www.wsj.com/articles/five-below-becomes-the-amazon-proof-store-1541151001 (accessed September 2024).

[4] Five Below, Inc. 10-K, January 28, 2023.

Exhibit 1 Five Below, Inc. Income Statements ($ Thousands)

	Fiscal Year Ended		
	February 3, 2024	**January 28, 2023**	**January 29, 2022**
Net sales	3,559,369	3,076,308	2,848,354
Cost of goods sold	2,285,544	1,980,817	1,817,910
Gross profit	1,273,825	1,095,491	1,030,444
Selling, general and administrative expenses	888,254	750,448	650,564
Operating income	385,571	345,043	379,880
Interest/other income (expense), net	15,530	2,491	(13,177)
Income before income taxes	401,101	347,534	366,703
Income tax expense	99,995	86,006	87,893
Net income	301,106	261,528	278,810

Exhibit 1 (cont.) Five Below, Inc. Balance Sheets ($ Thousands)

	Fiscal Year Ended	
	February 3, 2024	**January 28, 2023**
Current assets:		
Cash and cash equivalents	179,749	332,324
Short-term investment securities	280,339	66,845
Inventories	584,627	527,720
Prepaid income taxes and tax receivable	4,834	8,898
Prepaid expenses and other current assets	153,993	130,592
Total current assets	1,203,542	1,066,379
Property and equipment, net	1,134,312	925,530
Operating lease assets	1,509,416	1,319,132
Other assets	24,767	13,870
Total assets	3,872,037	3,324,911
Current liabilities:		
Accounts payable	256,275	221,120
Income taxes payable	41,772	19,928
Accrued salaries and wages	30,028	25,420
Other accrued expenses	146,887	136,316
Operating lease liabilities	240,964	199,776
Total current liabilities	715,926	602,560
Other long-term liabilities	6,826	4,296
Deferred income taxes	66,743	59,151
Long-term operating lease liabilities	1,497,586	1,296,975
Total liabilities	2,287,081	1,962,982
Shareholders’ equity:		
Common stock	551	555
Additional paid-in capital	182,709	260,784
Retained earnings	1,401,696	1,100,590
Total shareholders’ equity	1,584,956	1,361,929
Total liabilities and shareholders’ equity	3,872,037	3,324,911

Exhibit 1 (cont.) Five Below, Inc. Cash Flow Statements ($ Thousands)

	Fiscal Year Ended		
	February 3, 2024	**January 28, 2023**	**January 29, 2022**
Operating activities:			
Net income	301,106	261,528	278,810
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	130,747	105,617	84,831
Share-based compensation expense	17,859	23,583	25,787
Deferred income tax expense	7,592	22,995	7,245
Other non-cash expenses	351	409	708
Changes in operating assets and liabilities:			
Inventories	(56,907)	(72,616)	(173,837)
Prepaid income taxes and tax receivable	4,064	2,427	(4,975)
Prepaid expenses and other assets	(26,651)	(39,379)	(26,287)
Accounts payable	35,133	24,891	61,559
Income taxes payable	21,844	(8,168)	26,071
Accrued salaries and wages	4,608	(28,119)	10,094
Operating leases	51,515	30,022	13,131
Other accrued expenses	8,358	(8,264)	24,775
Net cash provided by operating activities	499,619	314,926	327,912
Investing activities:			
Purchases of investment securities and other investments	(416,649)	(56,459)	(477,082)
Sales, maturities, and redemptions of investment securities	195,364	304,473	299,652
Capital expenditures	(335,050)	(251,954)	(288,167)
Net cash used in investing activities	(556,335)	(3,940)	(465,597)
Financing activities:			
Cash paid for Revolving Credit Facility financing costs	0	(248)	0
Net proceeds from issuance of common stock	980	824	828
Repurchase and retirement of common stock	(80,541)	(40,007)	(60,011)
Proceeds from exercise of options to purchase common stock and vesting of restricted stock units	288	777	390
Common shares withheld for taxes	(16,586)	(4,981)	(7,332)
Net cash used in financing activities	(95,859)	(43,635)	(66,125)
Net increase (decrease) in cash and cash equivalents	(152,575)	267,351	(203,810)
Cash and cash equivalents at beginning of year	332,324	64,973	268,783
Cash and cash equivalents at end of year	179,749	332,324	64,973

Source: Five Below, Inc. 10-K, February 3, 2024.