

The Home Depot Inc. (HD)

\$245.03 (As of 02/14/20)

Price Target (6-12 Months): **\$257.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 01/11/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: C

Growth: C

Momentum: B

Summary

Although Home Depot has underperformed the industry in past three months, its robust earnings beat streak drives optimism. The company's earnings gained from progress on strategic investments. Its efforts to provide an interconnected shopping experience to customers, with innovative products and improved productivity, also position it for growth. However, lower-than-expected sales results in third-quarter fiscal 2019 and a slashed view for fiscal 2019, followed by a soft view for fiscal 2020 is hurting investors' sentiment. Though it is on track with its One Home Depot strategy, it expects investments under the plan to weigh on margins in fiscal 2020. Also, it expects margins to be hurt by product mix due to outsized growth in categories like appliances, power tools and outdoor power equipment, with higher shrink due to product theft.

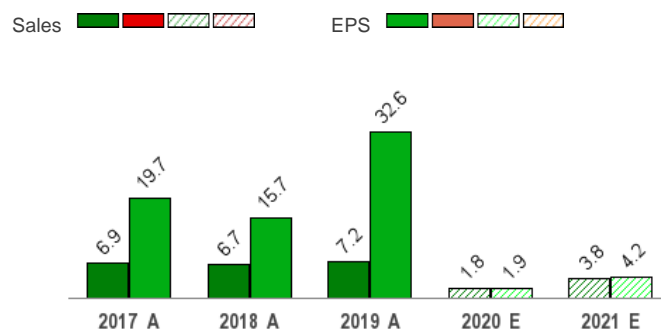
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$245.20 - \$179.52
20 Day Average Volume (sh)	3,796,192
Market Cap	\$267.3 B
YTD Price Change	12.2%
Beta	1.01
Dividend / Div Yld	\$5.44 / 2.2%
Industry	Building Products - Retail
Zacks Industry Rank	Top 36% (92 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	0.0%
Last Sales Surprise	-0.9%
EPS F1 Est- 4 week change	0.1%
Expected Report Date	02/25/2020
Earnings ESP	-0.1%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	27,537 E	32,097 E	28,241 E	26,611 E	114,442 E
2020	26,381 A	30,839 A	27,223 A	25,765 E	110,200 E
2019	24,947 A	30,463 A	26,302 A	26,491 A	108,203 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.36 E	\$3.29 E	\$2.62 E	\$2.23 E	\$10.50 E
2020	\$2.27 A	\$3.17 A	\$2.53 A	\$2.10 E	\$10.08 E
2019	\$2.08 A	\$3.05 A	\$2.51 A	\$2.25 A	\$9.89 A

*Quarterly figures may not add up to annual.

P/E TTM	24.0
P/E F1	23.3
PEG F1	2.2
P/S TTM	2.4

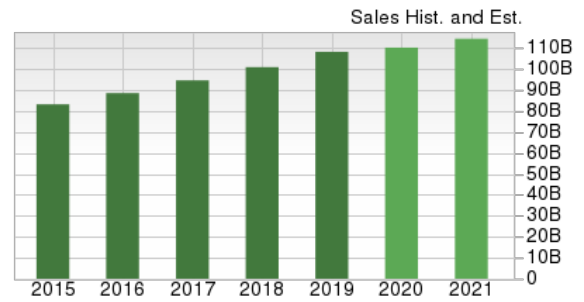
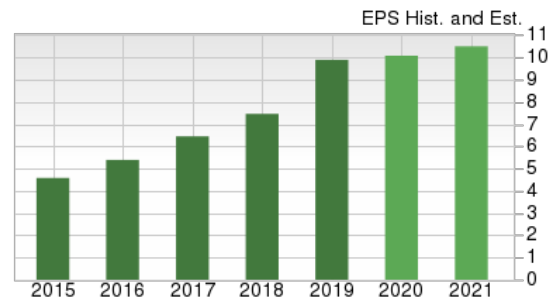
The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 02/14/2020. The reports text is as of 02/17/2020.

Overview

Based on net sales, The Home Depot Inc. is the world's largest home improvement specialty retailer with over 2,200 retail stores across the globe, offering a diverse range of branded and proprietary home improvement items, building materials, lawn and garden products, and related services.

With the help of its stores, the company operates throughout the United States (including the territories of Puerto Rico and the Virgin Islands), Canada and Mexico and employs more than 300,000 associates. The company's average store area is almost 105,000 square feet with approximately 23,000 square feet of additional outside garden area. The company typically serves three primary customer groups: Do-It-Yourself (D-I-Y), Do-It-For-Me (D-I-F-M), and Professional Customers.

- **D-I-Y Customers:** These customers are usually home owners, who prefer purchasing products and completing installations on their own.
- **D-I-F-M Customers:** These customers are usually home owners, who purchase products on their own and employ third-parties to complete the projects and installations.
- **Professional Customers:** This customer segment mostly comprises professional remodelers, general contractors, repairmen, small business owners, and tradesmen.



Reasons To Buy:

▲ **Earnings Trend:** Home Depot continued with its positive earnings streak in third-quarter fiscal 2019. Earnings surpassed the Zacks Consensus Estimate and improved year over year. Earnings were fueled by significant progress on strategic investments and 3.5% top-line growth. The company's overall comps grew 3.6%, with 3.8% improvement in the United States. Comps were aided by 1.9% rise in average ticket and 1.5% increase in customer transactions. Further, the company reiterated the earnings per share view of \$10.03 for fiscal 2019 (suggesting 3.1% growth from the year-ago quarter's reported figure), while it cut the sales view.

The Pro segment is gaining from Home Depot's efforts to simplify the Pro shopping experience and expand engagement through services like tool rental, delivery and the new B2B online experience.

▲ **Integrated Retail Strategy:** Home Depot is witnessing significant benefits from the execution of its "One Home Depot" investment plan, focused on delivering an interconnected shopping experience for customers. In-store investments under the plan mainly focus on easy customer navigation through the stores and increased speed to checkout. The company has enhanced navigation through the introduction of way-finding sign and store refresh package. These along with front-end store investments to optimize labor and merchandise space productivity led to improved customer satisfaction scores and improved conversion rates in stores. Further, the introduction of digital price labels in the appliance department brought the ratings and reviews of the digital world into its store shopping experience. Though physical stores are the key to its business, the company identifies that many of in-store purchases are the result of online visits. Additionally, nearly 50% of the online orders in the United States are picked up from stores, reflecting the relevance of stores amid the growing popularity of e-commerce. The blended customer engagement across both channels forms the basis for the company's integrated retail strategy that connects offline and online channels.

On the digital front, the company is investing in its website and other applications to further enhance online customer experience. It is witnessing higher traffic, better conversion and continued sales growth in the digital business through improved search capabilities, site functionality, category presentation and product content. Moreover, the company continues to roll out automated lockers in stores to make picking-up of online orders easier and convenient. Currently, automated lockers are available in about 1,300 stores. Notably, stores with these lockers witnessed an increase of 280 basis points (bps) in checkout scores. The company is also making efforts to leverage the digital business to boost sales for adjacent categories like HD Home, Cool and Workwear. These investments across the digital and physical assets are likely to drive the company's productivity growth, apart from boosting customer experience.

▲ **Long-Term Financial Targets:** With the "One Home Depot" investment plan on track, the company is nearing the financial goals that were outlined in December 2017. It is benefiting from efforts to provide an interconnected shopping experience to customers, with localized and innovative products, and improved productivity. The company reiterated its targets for fiscal 2020, anticipating total sales of nearly \$115-\$120 billion. This represents compounded annual sales growth of nearly 4.5-6%. Operating margin is expected to be 14.4-15%. Moreover, the company expects annual average capital spending to be about 2.5% of sales. Alongside achieving these targets, the company plans to accelerate investments in the next three years to enhance customer experience and shareholder value.

▲ **Focus on Pro Customers:** Home Depot's Pro segment is a key growth driver, with Pro sales outpacing DIY (do-it-yourself) sales for the past several quarters. Sales for Pro customers, which represent 45% of overall sales, continued to outpace DIY sales in the United States in the fiscal third quarter. Strong growth in Pro-heavy categories like fasteners, pneumatics, concrete and installation mainly aided Pro customer sales. The Pro segment is benefiting from the company's efforts to enhance service capabilities for the Pros. The company is focused on simplifying the Pro shopping experience and expanding engagement through services like tool rental, delivery and the new B2B website. The B2B platform brings a more personalized experience for Pro customers based on customer feedback. The company expects to roll out the new Pro online experience to more than a million Pros by 2019. Additionally, the company equipped store personnel with several tools to better understand Pro customers. The latest among these tools is the My View system, which enables associates to access customer data, allowing them to work proactively to better serve Pro customers.

▲ **Capital Strategy:** Home Depot has a disciplined capital allocation strategy, supported by solid free cash flow generation capability. This allows management to undertake shareholder-friendly moves. Clearly, the long-term targets of dividend payout ratio of about 55% of earnings and return on invested capital (ROIC) of more than 40% highlight its focus on this strategy. Based on the average of beginning and ending long-term debt and equity for the trailing 12 months, ROIC at the end of third-quarter fiscal 2019 improved 290 bps year over year to 45.1%. In the first nine months of fiscal 2019, the company reinvested about \$1,891 million in its business through capital expenditure. In the fiscal third quarter, it bought back 5.2 million shares for \$1.25 billion. In the first nine months of fiscal 2019, it paid out \$4,477 million in dividends and repurchased shares worth \$3,909 million.

Reasons To Sell:

- ▼ **Stock Performance & Valuation:** Shares of Home Depot have declined 0.8% in the past three months, against the industry's growth of 1.4%. The stock was hurt by the lower-than-expected sales performance in third-quarter fiscal 2019 and a lowered sales view fiscal 2019, followed by a soft view for fiscal 2020 in the recent analyst meet. Considering Price-to-Earnings (P/E) ratio, Home Depot looks overvalued when compared with the S&P 500. The stock has a trailing 12-month P/E of 22.79x compared with 20.83x for S&P 500. The company's trailing 12-month P/E ratio is above the median level of 20.91x but below the high level of 23.37x scaled in the past year. These factors profess that the stock's valuation is quite stretched.
- ▼ **Q3 Sales, Guidance Cut:** Home Depot's top line missed the Zacks Consensus Estimate in second-quarter fiscal 2019 despite witnessing year-over-year growth. Lower-than-expected sales resulted from timing issues related to the receipt of some benefits from its One Home Depot investments. Though these investments are delivering positive results, some of the benefits from these initiatives will take longer than originally planned to be realized. Based on the delays, the company slashed its sales and comparable sales (comps) view for fiscal 2019. It now expects sales growth of 1.8% for fiscal 2019 compared with 2.3% rise stated earlier. The company now anticipates comps (for the comparable 52-week period) growth of 3.5% compared with 4% improvement mentioned previously.
- ▼ **Higher Investments to Hurt Fiscal 2020 Margins:** Home Depot outlined its preliminary guidance for fiscal 2020 in an analyst meet held to provide updates on its "One Home Depot" plan. Though the company is on track with its planned targets, it expects investments for the One Home Depot strategy to weigh on margins in fiscal 2020. The company's total investment in the plan is estimated to be \$3.9 billion in 2020 versus \$3.6 billion in 2019 and \$3.3 billion last year. Additionally, the company expects margins in fiscal 2020 to be hurt by product mix due to outsized growth in categories like appliances, power tools and outdoor power equipment. Further, it expects margins to be hurt by increased shrink due to product theft. For fiscal 2020, Home Depot expects sales and comparable sales (comps) growth of 3.5-4% each. Operating margin is expected to be 14%.
- ▼ **Copper & Lumber Prices:** Although Home Depot put up a great show in the fiscal third quarter, commodity deflation in lumber and copper partly hurt sales and comparable sales (comps) in the quarter. Notably, U.S. comps included negative impacts of nearly 35 bps. Particularly, lumber price deflation hurt comp sales growth by \$175 million (or more than 65 bps). All departments witnessed comps growth, except for electrical and lumber. While lumber reported low-single-digit comps decline, electrical was essentially flat. The decline in lumber is attributed to continued lumber price deflation, offset by unit growth. Meanwhile, electrical was impacted by deflation in copper. Commodity deflation in lumber and copper also hurt average ticket growth by 80 bps.
- ▼ **Soft Q3 Margins:** While Home Depot has been posting splendid results, its margins look troubled. Evidently, the company's gross margin contracted 31 bps in second-quarter fiscal 2019 due to impacts of changes in the mix of products sold and higher shrink. Meanwhile, operating expenses declined 10 bps, owing to efficient expense control and continued productivity in the business along with investments in strategic initiatives. However, expenses related to the strategic investment plan of \$277 million were up about \$44 million year over year, resulting in 13 bps of operating expense deleverage. Moreover, operating margin declined 21 bps mostly due to soft gross margin.

Home Depot slashed its sales and comps guidance for fiscal 2019 based on anticipated delay in the realization of benefits from some of its initiatives. It expects sales growth of 1.8% for fiscal 2019.

Last Earnings Report

Home Depot Q3 Earnings Beat, Sales Miss

Home Depot posted better-than-expected earnings results for third-quarter fiscal 2019, retaining its positive earnings trend. However, the company's top line lagged the Zacks Consensus Estimate but improved year over year. The top line lagged primarily due to timing issues related to the receipt of certain benefits from the One Home Depot investments. Based on the delays, the company slashed its sales and comparable sales (comps) view for fiscal 2019.

Quarter Ending **10/2019**

Report Date	Nov 19, 2019
Sales Surprise	-0.91%
EPS Surprise	0.00%
Quarterly EPS	2.53
Annual EPS (TTM)	10.22

Q3 Highlights

Adjusted earnings of \$3.53 per share grew 0.8% from \$2.51 registered in the year-ago quarter. The bottom line also surpassed the Zacks Consensus Estimate of \$2.52.

Net sales rose 3.5% to \$27,223 million from \$26,302 million in the year-ago quarter but missed the Zacks Consensus Estimate of \$27,472.2 million. Lower-than-expected sales resulted from timing issues related to receipt of some benefits from its One Home Depot investments. Though these investments are delivering positive results, some of the benefits from these initiatives will take longer than planned to be realized. The company's overall comps grew 3.6%, with a 3.8% improvement in the United States.

In the reported quarter, comps were aided by 1.9% rise in average ticket and a 1.5% increase in customer transactions. Moreover, sales per square foot rose 3.5%.

In dollar terms, gross profit improved 2.6% to \$9,387 million from \$9,151 million in the year-ago quarter, primarily driven by higher sales. However, gross profit margin contracted 30 basis points (bps) to 34.5%.

Operating income rose 2% to \$3,947 million, while operating margin contracted 20 bps to 14.5%.

Balance Sheet and Cash Flow

Home Depot ended the quarter with cash and cash equivalents of \$2,193 million, long-term debt (excluding current maturities) of \$26,597 million, and shareholders' deficit of \$1,082 million. In the first nine months of fiscal 2019, it generated \$10,664 million of net cash from operations.

Further, the company paid out cash dividends of \$4,477 million and repurchased shares worth \$3,909 million in the first nine months of fiscal 2019.

Outlook

Driven by the aforementioned delay in realizing benefits from the One Home Depot investments, the company lowered sales and comps guidance for fiscal 2019. It now expects sales growth of 1.8% for fiscal 2019 compared with 2.3% rise stated earlier. It now anticipates comps (for the comparable 52-week period) growth of 3.5% compared with 4% improvement mentioned previously.

However, the company reiterated earnings view for fiscal 2019. It continues to project earnings per share of \$10.03 for fiscal 2019, suggesting 3.1% growth from the year-ago reported figure.

Recent News

Home Depot Prepares for Spring by Hiring 80K Workers – Feb 11, 2020

Home Depot started hiring associates for spring, which is its busiest season. Notably, it announced plans to hire 80,000 workers for full-time and part-time positions. Interested candidates may visit careers.homedepot.com for applying for suitable jobs.

According to sources, it recruited the same number of employees last year. Furthermore, Home Depot is likely to recruit 1,400 associates in Atlanta alone, driven by solid demand, per sources.

The part-time employees will be posted in Home Depot's garden center as it will enable them to be hands-on and help neighbors with their spring projects. Further, the company is looking to fill up positions related to overnight freight, merchandising, and other customer service in stores, warehouses and distribution centers. With 90% of the U.S. population living within 10 miles of a Home Depot store, these positions are lucrative opportunities for people looking to work close to their homes.

Further, the company will provide innovative training programs and tools, including a gamified mobile app, e-learning and on-the-job coaching. It will also offer employee benefits such as tuition reimbursement, backup dependent care for children and elders, and discounts on items such as cell phones and laptops. Also, employees will be eligible for paid family leaves after a year of service.

Home Depot Updates Transformation Plan, Gives Soft Fiscal 2020 View – Dec 11, 2019

Home Depot outlined its preliminary guidance for fiscal 2020 in an analyst meet held to provide updates on its "One Home Depot" plan. Home Depot's "One Home Depot" investment plan, which was announced in 2017, focuses on delivering an interconnected shopping experience for customers. Investments under the plan include leveraging the convenience of stores, enhancing digital experience, expanding product offerings into new categories, extending its leadership position with the Pro and allowing customers to receive their goods in the way they choose.

Notably, Home Depot expects its investments for the One Home Depot strategy to weigh on margins in fiscal 2020. The company outlined that it expects investments under the \$11 billion-One Home Depot program to be the highest in fiscal 2020. It envisions to have invested \$5 billion in its stores, \$2.5 billion in technology and remain on track to invest \$1.2 billion in its supply chain network by the end of fiscal 2020. Beyond 2020, Home Depot expects the level of investments to decline, while it will start realizing benefits from the investments made under the plan.

The company's total investment in the plan is estimated to be \$3.9 billion in 2020 versus \$3.6 billion in 2019 and \$3.3 billion last year. Home Depot stated that its guidance for margin reflects the increased investments planned for 2020. Additionally, the company expects margins in fiscal 2020 to be hurt by product mix due to outsized growth in categories like appliances, power tools and outdoor power equipment. Further, it expects margins to be hurt by increased shrink due to product theft.

For fiscal 2020, Home Depot expects sales and comparable sales (comps) growth of 3.5-4% each. The Zacks Consensus Estimate for sales for fiscal 2020 is pegged at \$114.7 billion, suggesting a growth of 4.1% year over year. Operating margin is expected to be 14%. Further, the company expects to continue returning value to its shareholders through dividends and share repurchases.

Notably, the company expects to return more than \$35 billion, in the form of dividends and share repurchases, over the three years ending in 2020. Further, it expects return on invested capital to be nearly 45%.

Moreover, the company reaffirmed its guidance for fiscal 2019. It expects sales growth of 1.8% for fiscal 2019, with comps (for the comparable 52-week period) growth of 3.5%. Home Depot continues to project earnings of \$10.03 per share for fiscal 2019, suggesting 3.1% growth from the year-ago reported figure.

Home Depot Declares Dividend – Nov 21, 2019

Home Depot declared third-quarter cash dividend of \$1.36 per share, payable on Dec19 to shareholders with record as of Dec 5.

Valuation

Home Depot shares are up 12.2% in the year-to-date period and 27.4% for the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Retail-Wholesale sector are up 9.7% and 5.6%, respectively in the year-to-date period. Over the past year, the Zacks sub-industry and the sector is up 23.9% and 19.5%, respectively.

The S&P 500 index is up 5% in the year-to-date period and 21% in the past year.

The stock is currently trading at 23.25X forward 12-month earnings, which compares to 21.36X for the Zacks sub-industry, 26.17X for the Zacks sector and 19.36X for the S&P 500 index.

Over the past five years, the stock has traded as high as 27.11X and as low as 15.52X, with a 5-year median of 20.18X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$257 price target reflects 24.39X forward 12-month earnings.

The table below shows summary valuation data for HD

Valuation Multiples - HD					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	23.25	21.36	26.17	19.36
	5-Year High	27.11	21.61	26.2	19.36
	5-Year Low	15.52	16.02	19.07	15.18
	5-Year Median	20.18	19.2	23	17.47
P/S F12M	Current	2.33	1.57	1.09	3.57
	5-Year High	2.36	1.57	1.11	3.57
	5-Year Low	1.5	1.06	0.8	2.54
	5-Year Median	1.81	1.27	0.91	3
EV/EBITDA TTM	Current	16.46	12.51	15.71	11.36
	5-Year High	16.46	12.51	15.71	12.85
	5-Year Low	11.1	8.95	10.79	8.47
	5-Year Median	13.33	10.78	12.4	10.7

As of 02/14/2020

Industry Analysis Zacks Industry Rank: Top 36% (92 out of 255)



Top Peers

Beacon Roofing Supply, Inc. (BECN)	Neutral
Builders FirstSource, Inc. (BLDR)	Neutral
Fastenal Company (FAST)	Neutral
Lowes Companies, Inc. (LOW)	Neutral
RH (RH)	Neutral
Travis Perkins PLC (TVPKF)	Neutral
Walmart Inc. (WMT)	Neutral
Lumber Liquidators Holdings, Inc (LL)	Underperform

Industry Comparison Industry: Building Products - Retail				Industry Peers		
	HD Neutral	X Industry	S&P 500	BLDR Neutral	LL Underperform	LOW Neutral
VGM Score	C	-	-	A	F	A
Market Cap	267.29 B	2.05 B	24.61 B	3.15 B	227.10 M	96.13 B
# of Analysts	13	6	13	5	3	13
Dividend Yield	2.22%	0.00%	1.78%	0.00%	0.00%	1.75%
Value Score	C	-	-	B	D	B
Cash/Price	0.01	0.03	0.04	0.02	0.03	0.01
EV/EBITDA	16.71	9.64	14.06	9.45	-11.41	17.60
PEG Ratio	2.17	1.34	2.09	NA	0.69	1.34
Price/Book (P/B)	NA	1.74	3.29	4.04	1.58	39.11
Price/Cash Flow (P/CF)	20.57	10.17	13.65	9.64	6.50	14.99
P/E (F1)	23.34	14.71	19.21	12.41	19.06	18.74
Price/Sales (P/S)	2.41	0.50	2.70	0.43	0.21	1.34
Earnings Yield	4.29%	6.81%	5.19%	8.05%	5.18%	5.33%
Debt/Equity	-29.31	1.49	0.71	1.73	1.24	8.37
Cash Flow (\$/share)	11.91	1.77	6.92	2.82	1.22	8.37
Growth Score	C	-	-	A	F	B
Hist. EPS Growth (3-5 yrs)	19.59%	14.07%	10.85%	77.74%	-25.41%	16.26%
Proj. EPS Growth (F1/F0)	4.19%	7.88%	7.17%	7.42%	122.32%	17.45%
Curr. Cash Flow Growth	23.53%	17.66%	8.56%	31.45%	-273.34%	28.26%
Hist. Cash Flow Growth (3-5 yrs)	13.51%	12.59%	8.36%	64.23%	-17.13%	11.67%
Current Ratio	1.08	2.11	1.23	1.66	1.48	1.04
Debt/Capital	NA%	59.97%	42.91%	63.42%	55.31%	89.33%
Net Margin	10.01%	2.78%	11.81%	3.17%	-5.85%	4.11%
Return on Equity	-721.00%	11.24%	16.86%	37.03%	2.90%	146.62%
Sales/Assets	2.22	1.89	0.54	2.31	1.97	1.81
Proj. Sales Growth (F1/F0)	3.85%	3.85%	3.85%	4.81%	3.42%	3.13%
Momentum Score	B	-	-	D	D	D
Daily Price Chg	1.10%	0.79%	0.06%	-1.84%	2.86%	0.52%
1 Week Price Chg	4.03%	0.00%	2.47%	-1.09%	-4.73%	4.51%
4 Week Price Chg	7.08%	-0.13%	0.59%	0.59%	-15.04%	5.16%
12 Week Price Chg	12.12%	6.45%	6.98%	9.37%	-7.81%	7.18%
52 Week Price Chg	30.54%	22.88%	16.62%	101.11%	-29.56%	23.55%
20 Day Average Volume	3,796,192	304,682	2,020,569	1,083,906	1,381,335	3,240,533
(F1) EPS Est 1 week change	0.09%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.07%	0.00%	-0.05%	0.52%	-6.74%	0.00%
(F1) EPS Est 12 week change	-3.97%	-0.07%	-0.17%	0.35%	-8.07%	0.51%
(Q1) EPS Est Mthly Chg	0.05%	0.00%	-0.24%	0.00%	-17.95%	-0.09%

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	C
Growth Score	C
Momentum Score	B
VGM Score	C

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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