



Home Depot (HD)

Updated May 26th, 2019 by Quinn Mohammed

Key Metrics

Current Price:	\$194	5 Year CAGR Estimate:	10.5%	Volatility Percentile:	27.6%
Fair Value Price:	\$190	5 Year Growth Estimate:	8.0%	Momentum Percentile:	52.9%
% Fair Value:	102%	5 Year Valuation Multiple Estimate:	-0.3%	Growth Percentile:	76.0%
Dividend Yield:	2.8%	5 Year Price Target	\$280	Valuation Percentile:	47.9%
Dividend Risk Score:	C	Retirement Suitability Score:	C	Total Return Percentile:	57.5%

Overview & Current Events

Home Depot was founded in 1978 and since that time has grown into a juggernaut home improvement retailer with almost 2,300 stores in the US, Canada and Mexico that generate around \$108 billion in annual revenue. The stock has a market value of \$214 billion, making it one of the larger companies by market capitalization in the US.

Home Depot reported Q1 earnings on May 21st, 2019 and recorded sales of \$26.4 billion, a 5.7% increase from the same period one year ago. Comparable sales increased by 2.5% while comparable sales in the U.S. increased by 3.0%. The difference between sales growth and comparable sales performance is to provide a more accurate picture of the company's performance since fiscal 2018 contained 53 weeks of sales while the current fiscal 2019 is made up of 52 weeks.

Net earnings for the quarter came in at \$2.5 billion, compared to \$2.4 billion in the first quarter of last year. The company earned \$2.27 per diluted share, a 9.1% increase over the \$2.08 earned last year.

Management reaffirmed their previous guidance for fiscal 2019, including 5% comparable sales growth, 3.3% total sales growth, and diluted earnings-per-share of \$10.03, representing growth of just 3.1% against 2018. Keep in mind the company's tax rate is expected to rise ~2% against 2018 and that the calendar for 2019 contains the standard 52 weeks against the 53 weeks from 2018. In other words, while the headline growth number looks low, it isn't when these factors are adjusted out. We believe the company's long-term growth is well intact.

Diluted Shares outstanding for the first quarter of 2019 were down 4.5% from the last year, as Home Depot continues to buy back shares and lower the overall float of the company.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$1.66	\$2.03	\$2.47	\$3.10	\$3.76	\$4.56	\$5.34	\$6.45	\$7.46	\$9.73	\$10.03	\$14.74
DPS	\$0.90	\$0.95	\$1.04	\$1.16	\$1.56	\$1.88	\$2.36	\$2.76	\$3.56	\$4.12	\$5.44	\$8.00
Shares	1,698	1,623	1,537	1,484	1,380	1,307	1,252	1,203	1,158	1,121	1,100	1,000

Home Depot's earnings momentum has been enormous in the past decade as it has been able to fully capitalize on the housing and construction boom that ensued following the Great Recession. We see five-year annual earnings growth of 8%, consisting of comp sales in the mid-single digits, a low single digit tailwind from buybacks and a steady, low single digit tailwind from operating margin improvements. This is down from our prior estimate of 10% growth simply due to the lateness of the cycle Home Depot is in today; 10% annual growth looks difficult to maintain given where its margins are today in the mid-teens as well as its very high rate of comparable sales growth over the years.

In addition, the company's streak of meaningful dividend growth should continue as we see the payout rising at the rate of earnings, reaching \$8 per share in five years. Home Depot's recent increase has turned it into an income stock with a nearly-3% yield and it has plenty of room to continue raising the payout in the years to come. Further, as it matures it may institute a higher payout ratio target for the dividend, further boosting its dividend growth prospects.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	15.3	15.6	15.0	17.9	20.2	19.1	22.1	20.3	21.6	19.4	19.3	19.0
Avg. Yld.	3.5%	3.0%	2.8%	2.1%	2.1%	2.2%	2.0%	2.1%	2.2%	2.2%	2.8%	2.9%

Shares have moved slightly higher since our last report, but the stock still trades roughly at fair value. Shares trade for 19.3 times our earnings estimate for this year, which is almost exactly where we see fair value, at 19 times earnings.

As a result, we see a small decline of 0.3% in the valuation multiple over the next five years. The yield should remain about where it is in the years to come given that earnings and the dividend should expand at roughly congruent rates.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	54%	47%	42%	37%	42%	41%	44%	43%	48%	42%	54%	54%

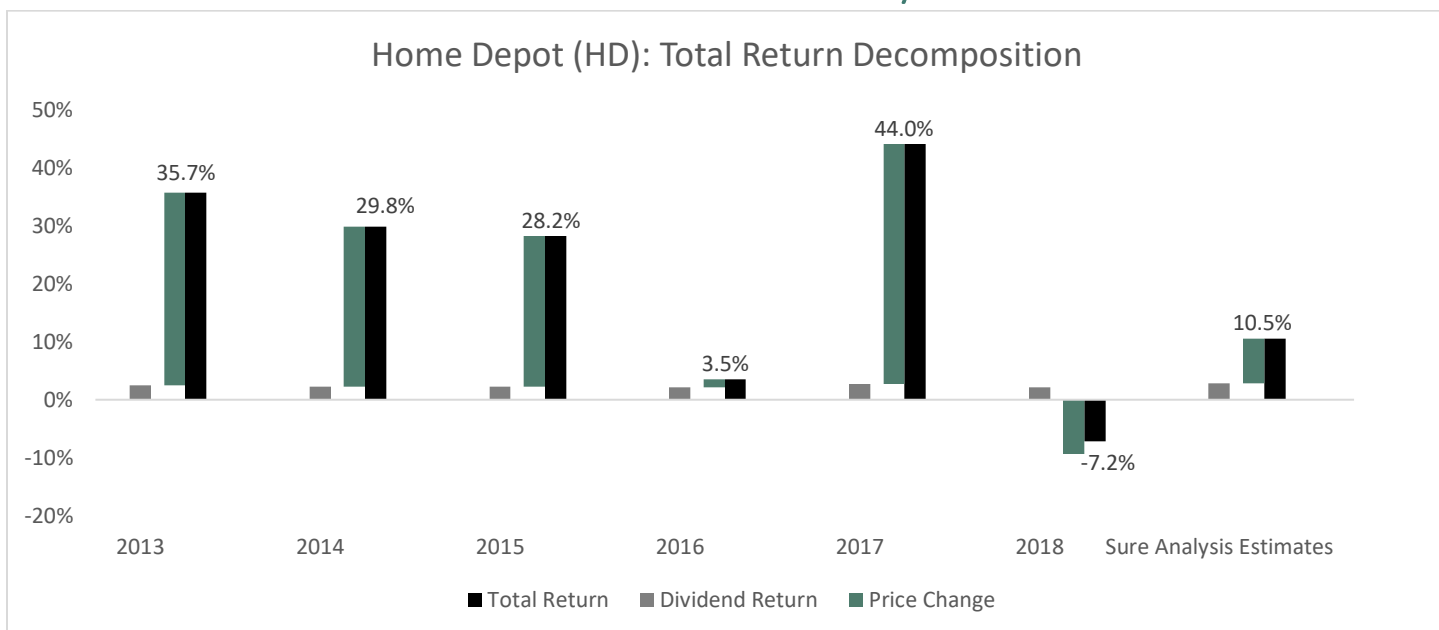
Home Depot's payout ratio is just over half of earnings and we expect it will stay there for the foreseeable future. That means the dividend is not only safe, but it has lots of room to grow in the future as well as earnings expand.

Home Depot's competitive advantage is in its enormous footprint, strong brand recognition and inventory variety. Supplanting its dominant position in home improvement will be extremely difficult for all comers, including rival Lowe's. The company is likely to suffer during a recession, but weakness would be a buying opportunity for long-term investors.

Final Thoughts & Recommendation

Home Depot currently trades roughly at fair value, but the growth prospects and dividend make up for this, and we continue to like the stock. We expect total annual returns of 10.5% going forward, consisting of the current 2.8% yield, a 0.3% headwind from the valuation and 8% earnings-per-share growth. Home Depot's fundamentals and growth catalysts are intact, and we rate the shares a buy despite trading near fair value. Home Depot offers investors the chance to own a stock that is dominant in its industry with terrific earnings and dividend growth outlooks for a reasonable price.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue (\$B)	66.18	68.00	70.40	74.75	78.81	83.18	88.52	94.60	100.90	108.20
Gross Profit	22412	23304	24262	25842	26915	28389	30265	32313	34356	37160
Gross Margin	33.9%	34.3%	34.5%	34.6%	34.2%	34.1%	34.2%	34.2%	34.0%	34.3%
SG&A Exp.	15902	15849	16028	16508	16122	16280	16801	17132	17864	19513
D&A Exp.	1806	1718	1682	1684	1757	1786	1863	1973	2062	2152
Operating Profit	4803	5839	6661	7766	9166	10469	11774	13427	14681	15777
Op. Margin	7.3%	8.6%	9.5%	10.4%	11.6%	12.6%	13.3%	14.2%	14.5%	14.6%
Net Profit	2661	3338	3883	4535	5385	6345	7009	7957	8630	11121
Net Margin	4.0%	4.9%	5.5%	6.1%	6.8%	7.6%	7.9%	8.4%	8.6%	10.3%
Free Cash Flow	4159	3489	5430	5663	6239	6800	7870	8162	10134	10596
Income Tax	1362	1935	2185	2686	3082	3631	4012	4534	5068	3435

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	40877	40125	40518	41084	40518	39946	41973	42966	44529	44003
Cash & Equivalents	1421	545	1987	2494	1929	1723	2216	2538	3595	1778
Acc. Receivable			1245	1395	1398	1484	1890	1570	1604	1936
Inventories	10188	10625	10325	10710	11057	11079	11809	12549	12748	13925
Goodwill & Int.	1171	1187	1120	1170	1289	1353	2102	2093	2275	2252
Total Liabilities	21484	21236	22620	23307	27996	30624	35657	38633	43075	45881
Accounts Payable	4863	4717	4856	5376	5797	5807	6565	7000	7244	7755
Long-Term Debt	9682	9749	10788	10796	14724	17197	21216	23601	27028	29202
Total Equity	19393	18889	17898	17777	12522	9322	6316	4333	1454	N/A
D/E Ratio	0.50	0.52	0.60	0.61	1.18	1.84	3.36	5.45	18.59	N/A

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	6.5%	8.2%	9.6%	11.1%	13.2%	15.8%	17.1%	18.7%	19.7%	25.1%
Return on Equity	14.3%	17.4%	21.1%	25.4%	35.5%	58.1%	89.6%	149%	298%	N/A
ROIC	9.1%	11.6%	13.5%	15.8%	19.3%	23.6%	25.9%	28.7%	30.6%	N/A
Shares Out.	1,698	1,623	1,537	1,484	1,380	1,307	1,252	1,203	1,158	1,121
Revenue/Share	39.11	41.01	44.84	49.47	54.96	61.79	68.99	76.66	85.22	94.67
FCF/Share	2.46	2.10	3.46	3.75	4.35	5.05	6.13	6.61	8.56	9.27

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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