Home Depot (HD) Earnings Report: Q1 2016 Conference Call Transcript

The following Home Depot conference call took place on May 17, 2016, 09:00 AM ET. This is a transcript of that earnings call:

Company Participants

- Diane Dayhoff; The Home Depot, Inc.; VP, IR
- Craig Menear; The Home Depot, Inc.; Chairman, CEO & President
- Ted Decker; The Home Depot, Inc.; EVP, Merchandising
- Carol Tome; The Home Depot, Inc.; EVP, Corporate Services & CFO
- Bill Lennie; The Home Depot, Inc.;EVP, Outside Sales & Service
- Mark Holifield; The Home Depot, Inc.;EVP, Supply Chain and Product Development
- Ann-Marie Campbell; The Home Depot, Inc.; Executive Vice President, U.S. Stores

Other Participants

- Seth Sigman; Credit Suisse; Analyst
- Simeon Gutman; Morgan Stanley; Analyst
- Michael Lasser; UBS; Analyst
- Kate McShane; Citi Research; Analyst
- Matthew McClintock; Barclays; Analyst
- Scott Mushkin; Wolfe Research; Analyst
- Chris Horvers; JP Morgan; Analyst
- Brian Nagel; Oppenheimer; Analyst
- Peter Benedict; Robert W. Baird; Analyst
- Dan Binder; Jefferies & Co.; Analyst
- Jaime Katz; MorningStar; Analyst
- Michael Baker; Deutsche Bank; Analyst
- Dennis McGill; Zelman & Associates; Analyst

MANAGEMENT DISCUSSION SECTION

Operator:

Good day and welcome to the Home Depot Q1 16 Earnings Call.

Today's conference is being recorded. If you'd like to ask a question during today's call, please press the star key followed by the number one on your touchtone phone. At this time, I would like to turn the conference over to Ms. Diane Dayhoff, Vice President of Investor Relations.

Please go ahead.

Diane Dayhoff (VP, IR):

Thank you. Good morning to everyone.

Joining us on our call today are Craig Menear, Chairman, CEO and President, Ted Decker, EVP of Merchandising, and Carol Tome, Chief Financial Officer and Executive Vice President, Corporate Services.

Following our prepared remarks, the call will be open to analyst questions. Questions will be limited to analysts and investors, and as a reminder we would appreciate it if participants would limit themselves to one question with one follow-up please. If we are unable to get your question during the call, please call our investor relations department at 770-384-2387.

Now before I turn the call over to Craig let me remind you that today's press release and the presentations made by our executives include forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. These statements are subject to risks and uncertainties that could cause actual results to differ materially from our expectations and projections. These risks and uncertainties include but are not limited to the factors identified in the release and in our filings with the Securities and Exchange Commission.

Today's presentations may also include certain non-GAAP measurements. Reconciliation of these measurements is provided on our website.

Now, let me the turn the call over to Craig.

Craig Menear (Chairman, CEO & President):

Thank you Diane and good morning everyone. Sales for the first quarter were $22.8 billion up 9% from last year, comp sales were up 6.5% from last year and our US stores had a positive comp of 7.4% diluted earnings per share, with $1.44 in the first quarter.

We were pleased with the start of the year. In the US all three of our divisions posted positive comps in the first quarter, led by our southern division, and all 19 US regions and top 40 markets saw single to low double digit comps in the quarter.

Internationally our Mexican and Canadian businesses had another quarter of solid performance. Mexico reported a positive double digit comps in local currency, making it the 50th consecutive quarter of positive comp growth. Our Canadian business also posted mid-single digit comps in local currency for a total of 18 consecutive quarters of positive comp growth.

(The weather) had somewhat of a positive impact on our business and certainly drove variability and demand. The first quarter was not an early spring story; it was an execution in the core of the store story. We continue to see broad-based growth across our store as both ticket and transactions grew in the quarter. All of our merchandising departments posted positive comps and we saw a healthy balance of growth among both our Pro and DIY categories, with Pro outpacing our DIY business in the US.

As Ted will detail, our customers continue to respond positively to our deep assortment of trusted brands, as we are the product authority for both our Pro and DIY customers.

The interline integration is progressing nicely. We continue to move forward on a number of exciting sales driving initiatives and we have outlined the path to truly realize the value of the interline acquisition and the total Pro opportunity over the next 18 to 24 months. We also continue to believe that blending the physical and digital channels into a seamless customer experience, which we call Interconnected Retail, provides a unique opportunity for us to expose the power of the Home Depot . This has been and will continue to be one of the central tenets of our company strategy and we will remain committed to the investments in our interconnected capabilities.

For the quarter, online traffic growth was double digits and our online sales grew 21.5%. Investing in interconnected capabilities goes beyond our .com business, as we are also continuing to further invest to more effectively meet customer's demands for increased fulfillment options. The role of (our .com), our new customer order management system is on track to be fully deployed in our US stores before year-end. Following behind, (the .com) rollout is the implementation of (BODFS or Buy Online, Deliver From Store). In certain markets were (BODFS) have been introduce, the demand has been much stronger than we anticipated. This is a good problem to have, but it is a challenging delivery capacity, which we will be working to address. We still expect (BODFS) to be fully rolled out by the end of the fiscal year.

For the spring season, we are focused on further connecting our in-store and online experiences. We offered a more expanded assortment of spring seasonal products online. We also leverage our digital assets to more effectively target customers with a personalized message pertaining to relevant products and special buys. Additionally, we used digital media to highlight local in-store assortments to drive footsteps to our stores.

To ensure stores are properly staffed for the busy spring selling season we hired over 80,000 associates to meet the demand of these increased footsteps. We continue to see great productivity from our supply chain. The flexibility and nimbleness of our supply chain was especially evident -- excuse me -- in the quarter, as we navigated spiky demand without sacrificing in stock levels.

We continue to see dividends from investments made in our supply chain, in our in stocks, inventory productivity, logistics costs, and service to our stores and customers. (Our BODFS RDC capability), which enables us to fulfill our Buy Online, Ship To Store orders through our RDC network leverages both our inventory and our fulfillment channels.

The cost savings of this initiative have been above our expectations in both our ship times and customer satisfaction scores continue to improve. We've made great strides with our supply chain over the past several years and we continue to optimize our network with initiatives like supply chain sync. While sync is in its early days of a multi-year roll-out, we are pleased with our initial results.

As it is early in the year, our view the macro-environment remains consistent. We believe that housing data indicates continued tailwinds for our business. As Carol will detail, because of our outperformance in the first quarter versus our plan, we are increasing our sales and earnings-per-share guidance for the year. We now expect fiscal 2016 sales growth of approximately 6.3% in diluted earnings per share of $6.27.

Today, we have over 400,000 associates and I want to close by thanking them for their hard work and dedication to our customers. In addition to serving our customers in our stores, through team Depot, our associate led volunteer force our associates donated their personal time to complete more than 1,000 projects and service to our local communities over the past 12 months.

And with that, let me turn the call over to thanks Ted.

Ted Decker (EVP, Merchandising):

Thanks Craig and good morning everyone.

We had a strong first quarter driven by continued strength across store, particularly with Pro customers.

An unseasonably warm February was followed by a more normal weathers of March and April. While weather positively impacted our sales performance in the first quarter, spring has not yet arrived in many of our markets.

In the first quarter, total comp transactions grew by 4%, while comp average tickets increased 2.5. Our average ticket increase was somewhat impacted by commodity price deflation mainly from lumber and copper. The total impact to ticket growth from commodity price deflation was approximately 15 basis points. Transactions for tickets under $50.00, representing approximately 20% of our US sales were up 2.7% per store. Transactions for tickets over $900.00, also, represent 20% of our US sales rep 9.5% first quarter.

The drivers behind increases in big-ticket purchases were appliances, roofing, sheds, and windows; all of which had double-digit comps. The departments that outperformed the company's average comps were appliances, tools, building materials, lumbar lighting, hardware, mill-work, and decor. Electrical paint, flooring, indoor garden, kitchen and bath plumbing and outdoor garden had positive comps although below the company average. Pro heavy categories continue to show great strength as we saw double-digit comps in fencing, pressure-treated decking, boards, fasteners, doors, and conduits.

In addition, the core of the store continues to perform well and we saw strength in maintenance and repair categories across the country. Tool storage, commercial and industrial lighting power, power tool accessories, and tools and wiring devices had double-digit comps across the quarter. The core categories including garage organization, laminate flooring, landscape lighting, vinyl plank, and wood flooring had comps above the company average.

Our store associates to great job executing our eighth annual Spring Black Friday event and creating excitement in our stores. In particular, special buys around appliances, outdoor power, and hard skates were well received by our customers, resulting in double-digit comps in those categories.

As Craig mentioned, the Home Depot is the product authority for both our professional and DIY customers. We have the deepest assortment of the leading programs in the marketplace. Many of these brands are billion-dollar categories for us. Our pros recognize our brand advantage and pro sales outpaced the company average in the first quarter.

We continue to use detailed analytics to help us balance the art and science of retail. In marketing, we maintain our best in class creative. We are also optimizing our ad effectiveness with targeted digital marketing. We remain focused on leveraging customer data to build the right message at the right time for the right customer. . As we made strategic moves away from print mass-marketing to more targeted digital marketing, we've seen great results. Since 2010, our return on advertising spend has nearly double

Now, let me turn our attention to the second quarter. We continue to be the leader of the marketplace for innovation and value that save our customers both time and money.

To maintain the momentum double-digit comps and Pneumatic category, we are introducing the Milwaukee's Pneumatic Framing Nailer, which the latest addition to the MA team fuel line-up. This high-powered mailer delivers fasteners much faster than competing battery-powered nailers, saving our pros time on the job site. And new from Dewalt is the 20V Max Brushless Finish Nailer. This compact and lightweight finish nailer has innovative features, including depth adjustments and multi-functional LED lights to illuminate work pieces. These are great examples of innovative and exclusive products from trusted best in class programs.

For our DIY customers, we are excited about the new exclusive launch of Pergo Outlast Plus Laminate Flooring. It is easy to install laminate, it is water resistant, and uses Spill Protect 24 Technology Proprietary Coating that prevents water from seeping into the floor. Outlast Plus Flooring allows customers to install laminate flooring in high traffic and water prone areas such as kitchens, bathrooms, and mud rooms.

In addition all the great new products, we are excited about our upcoming events. Our Thrill of the Grill, Memorial Day, Father's Day, and Fourth of July events are right around the corner and we have an incredible lineup of great values and special buys to help our customers enjoy this outdoor season to the fullest.

With that, I'd like to turn the call over to Carol.

Carol Tome (EVP, Corporate Services & CFO):

Thank you Ted, and good morning everyone.

In the first quarter, sales were $22.8 million, a 9% increase from last year, driven primarily by positive comp sales as well as the impact of interline brands versus last year, a stronger US dollar negatively impacted total sales growth by approximately $196 million, 4.9%. Our total company comps or same-store sales were positive, 6.5% for the quarter with positive comps of 10.2% in February, 6.7% in March and 4.3% in April. Comps for US stores were positive 7.4% for the quarter with positive comps, of 11.8% in February, 7.7% in March and 4.6% in April. We estimate weather driven demand positively impacted our US sales growth by approximately $250 million. The variability in our comp sales performance during the quarter was due in large part to whether adjutant timing at Easter this year versus last year.

Our total company gross margin was 34.2% for the quarter, a decrease of 13 basis points from last year. The change in our gross margin is explained largely by the following factors; first as expected we had 25 points of gross margin contraction due to the impact of interline; second, we had 12 basis points of gross margin expansion in our supply chain driven by lower fuel cost and increased productivity.

For fiscal 2016, we continue to expect our gross margin rate the same as what we reported in fiscal 2015. In the first quarter, operating expenses as percent of sales decreased by 122 basis points to 20.7%, our expense leverage reflects the impact of positive comp sales growth along with great expense control. For this year, we now expect our expense to grow at approximately 35% of our sales growth rate. Our operating margin for the quarter was 13.5% increase of 109 basis points from last year.

Interest and other expenses for the first quarter are $237 million, up $44 million last year, due primarily to higher long-term debt balances. In the first quarter, our effective tax rate was 36.5% compared to 34.3% in the first quarter of fiscal 2015. We call that the effective tax rate in the first quarter as last year it was favorably impacted by the settlement of a tax audit. For fiscal 2016, we expect our income tax provision rate be approximately 37%. Our diluted earnings per share for the first quarter were $1.44, an increase of 19% from last year.

Now moving to some additional highlights, during the first quarter we opened one new store in Mexico and we ended the quarter with a store count of 2275, a selling square footage of 237 million. Total sales per square foot for the first quarter, were $377.00 up 6.5% last year.

Now turning to the balance sheet, at the end of the quarter inventory was $13.2 billion, up $913 million from last year, reflecting both the impact of interline and the seasonality of our business. Inventory turns were 4.8 times up one tenth from the first quarter of last year. In the first quarter we repurchased $1.25 billion, or approximately 9.45 million shares of outstanding stock. For the remainder of the fiscal year, we intend repurchased approximately $3.75 billion of outstanding stock using excess cash, bringing total anticipated 2016 share purchases to $5 billion. Computing on the average from the beginning and ending long-term debt and equity for the trailing four quarters, return on invested capital with 29.2%, at 300 basis points higher than the first quarter of fiscal 2015.

Now, turning our attention to the full year, while US GDP forecasts has pulled back slightly as we built our 2016 sales plan, we continue to see strength in the housing market with home price appreciation, housing turnover, and household formation trending where we thought they would. Sales in the first quarter exceeded our expectations, not just because of the weather but because of higher demand for many of our core product categories.

While we ordinarily don't ordinarily rate our sales growth guidance so early in the year, we're going to roll forward some of our first quarter out-performance to give the underlying strength of the business. Further, the US dollar had weakened, such that the current spot rate of exchange is now in line with the FX rates we used to build our plan. Because of that, we are going to a single point estimate of a range for our 2016 guidance. From the high-end of the guidance range we provided in February, today we are raising our sales and earnings per share growth guidance. We now expect our 2016 sales to grow by approximately 6.3%, with comps of approximately 4.9%.

For earnings-per-share, remember that we guide office gap. We now expect fiscal 2016 diluted earnings per share to grow approximately 14.8%, to $6.27.

We thank you for your participation in today's call. And Derek, we are now ready for questions.

QUESTIONS & ANSWERS

Operator:

Absolutely.

And if you would like to ask a question please signal by pressing star one on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again press star one to ask a question.

Seth Sigman, Credit Suisse. Please go ahead.

Seth Sigman (Analyst - Credit Suisse):

All right, thanks. Good morning.

Nice quarter guys.

Ted Decker (EVP, Merchandising):

Thank you.

Seth Sigman (Analyst - Credit Suisse):

Just a follow-up there, does that $250 million consider that spring weather hasn't arrived in some markets as you alluded to and would that be factored into that number?

Carol Tome (EVP, Corporate Services & CFO):

That's right, we think we pulled forward true spring related categories -- $40-$50 million.

And as you know -- I don't know where you're sitting Seth, but as you know, in certain parts of the country spring has not yet arrived. So we're still anticipating a bang up spring quarter.

Seth Sigman (Analyst - Credit Suisse):

Yes, don't we know it all right.

Then just one follow-up on the on the Pro initiatives here, the extension of credit earlier in the quarter, can you talk about how that's going it and you know, how incremental to the numbers this quarter that may have been?

Carol Tome (EVP, Corporate Services & CFO):

Yes, we were very pleased with the new value proposition that were offering our private label card for pros. You'll recall that we are now offering 60 days to pay, 365 day returns, and discount at the fuel pump.

What we're seeing with our pros reciprocity, new accounts, our head of our sales plan, which is great news. But Seth, remember, we just rolled this out to all stores in January. So there was no measurable impact to the top line because but we anticipate that to come.

Seth Sigman (Analyst - Credit Suisse):

Great, thanks very much.

Operator:

Simeon Gutman, Morgan Stanley .

Simeon Gutman (Analyst - Morgan Stanley):

Thanks and good morning.

I just to clarify something, when we when we use the word, "pull forward" and if we take the $40 million out that, that's seasonal; just thinking about the other part that quote, unquote was pulled forward -- maybe other projects getting done a little earlier; do we know if that's typically a one the three-month pull forward? I mean, these are projects that presumably could get done in other parts of the year. Where I'm going is trying to think about, how that could impact the second quarter versus others later in the year.

Carol Tome (EVP, Corporate Services & CFO):

Well, here's how we've looked at this, we think there was about $250 million-ish of weather driven demand, if not all seasonal than this is just activity because of great weather earlier in the quarter. We're not rolling that forward because we anticipated that these were projects that would be completed later in the year and just got done earlier in the year. So we're not rolling that forward, it will bleed into Q2, Q3, maybe even Q4.

Simeon Gutman (Analyst - Morgan Stanley):

Yes, to your point. I mean, if somebody was doing a concrete project that maybe that planned for the summer, and they said, "Hey look, the grounds not frozen in the North. I can do it now." And they do it, that's -- it's hard to tell which quarters its come from, but it certainly probably the next couple quarters.

Carol Tome (EVP, Corporate Services & CFO):

So as we think about the shape of the year and this might help the modeling, we now think that the first quarter will be the highest growing quarter.

As a result, the first half will be slightly higher than the back half of the year. And if you look at the comps that we are projecting for Q2, Q3 and Q4, we expect them to be in the similar range, not a lot of difference in those comps numbers.

Simeon Gutman (Analyst - Morgan Stanley):

Okay, that's helpful.

My follow-up on the online business, I think that you mentioned growth of about 20.5%, anything different about the pickup in store percentage that's changed? And then your comment on the deliver strain maybe from delivering from store, is that because Home Depot is offering the customer the option of where they want the product from or is that your system that is choosing to deliver from store?

Craig Menear (Chairman, CEO & President):

So first of all, a comment on the percentage of pickup, it is around 40% to where the customer is choosing the option to pick up their items from Home Depot.com in our stores. And as a relates to the delivery, we have piloted the delivery program for a while we saw, mid single-digit growth in deliveries with the pilot when we went into additional markets, markets like Atlanta, for example, we saw a pretty substantial increase in the customer option to choose that delivery and were seen double digit growth in deliveries.

Simeon Gutman (Analyst - Morgan Stanley):

Okay, thanks.

Operator:

Michael Lasser, UBS.

Michael Lasser (Analyst - UBS):

Good morning and thanks for taking my question.

Carol, as you mentioned, it is not typical for the company to raise it's guidance after the first quarter, and you have strong first quarters in the past; so what is different about what you're witnessing in the business right now that it inspires so much confidence for you to move that rate higher?

Carol Tome (EVP, Corporate Services & CFO):

It's really the strength across the store.

As you know, when we build our sales plan, we use our directionally correct but imperfect sales forecasting model, which is an economic driven model. We do not build market share gains into our forecast. As we look at the performance in the first quarter, clearly there was some share shift. Look at appliances, Ted called it out, appliances contributed 50 basis point of our comp growth in the first quarter. So we are confident with what we saw in the first quarter and what we're seeing early in May to roll forward the outperformance of the first quarter.

Michael Lasser (Analyst - UBS):

So you mentioned that GDP forecast was a little lower, housing was about where you thought it was, but what's changed is you're getting a little more market share than you originally thought?

Carol Tome (EVP, Corporate Services & CFO):

We don't plan market shares as you know. So then, wee believe there were some share shifts and confirmed by (Nasdaq data that came out to show from a census perspective anyway), we did grow share.

The other thing that we must look at, is housing and just some other things that are happening within the housing market that we haven't built into our plan but we find to be of interest.

Here's a statistic, we have seen home equity values increase 94% since 2011. How is that possible? -- Because home prices are up 25% and people have continued to pay down their mortgages. So there's a wealth effect that's occurring with homeowners. This wealth effect as we've talked at length, if you feel like your home is as an investment and not an expense, you spend differently in your home and you get set in our big ticket category.

Michael Lasser (Analyst - UBS):

And then my following up question is on the Expense Outlook.

You know, you're now expecting to grow 35% at a rate of sales, is that all due to what's happening in the first quarter or do you expect it to be some expense good guys in the remainder of the year? Thank you so much.

Carol Tome (EVP, Corporate Services & CFO):

Yes, well despite our sales plan considerable in the first quarter, our total expenses are actually $13 million under our plan. That was driven by lower utilities as you would expect because of warmer weather in February. But also, we're not seeing the kind of pressure on medical as we had anticipated.

So now for the full year, we anticipate that our expenses will be lower than our original plan, which is helping take our expense growth factor down from what we had set that at 40% to now 35%.

Michael Lasser (Analyst - UBS):

Okay, good luck with the rest of spring.

Carol Tome (EVP, Corporate Services & CFO):

Thank you.

Operator:

Kate McShane, Citi Research

Kate McShane (Analyst - Citi Research):

Thanks for taking my question.

I wanted to follow-up on the other question that was just asked, just given some of the earnings that we've seen so far for Q1, that the health of the US consumer, I think is being called into question somewhat. So I wondered if you could, beyond Craig, what you have already mentioned, just talk about the DIY business and if there is any read through there to the overall take of the consumer? And just how much of the out-performance of Pro versus DIY is driven versus maybe to housing logistics versus your initiatives?

Craig Menear (Chairman, CEO & President):

I would say that you when you look at the strength of the business, it really comes across the board.

We are really pleased with the mix of both transactions and ticket growth that we had. That's something we look for in terms of balance in the business. We see the consumer continuing to engage in big-ticket sales with transactions above $900.00, you know, growing at 9.5% in the quarter.

So while our pro business was strong and were pleased to see that you're also very pleased to see the growth in our DIY business. So the balance is what really is what were striving to achieve and we're seen that balance across the store.

Carol Tome (EVP, Corporate Services & CFO):

And again, I go back housing data.

That data suggest that homeowners feel like they have more value than they did before. Look at negative equity, homes with negative equity have dropped from 22% at the beginning of 2012 to now

8.5%.

Kate McShane (Analyst - Citi Research):

Thank you. That's very helpful.

And then my second follow-up question -- it's unrelated -- I know you've spent some time in the prepared comments talking about, why Online Ship From Store -- which I think you're rolling out by the end of the year. I wanted more detail in terms of how much of that program -- how much of your merchandise will that program address? Is it going to be eligible for everything that's online and in the store? How will we expect that to work by the end of the year?

Ted Decker (EVP, Merchandising):

It pretty much is almost everything we sell, whether it's online or in store, it will be eligible for delivery. And we will leverage the supply chain network that we build up to do that in the most cost-effective way using our RDC as flow-through points for product that will come from our distribution points that a customer chooses to have delivered. So it's definitely a broad approach to the assortment that we carry.

Kate McShane (Analyst - Citi Research):

Thank you.

Operator:

Scott Mushkin, Wolfe Research.

Scott Mushkin (Analyst - Wolfe Research):

Thanks guys. Thanks for taking my questions.

So I just wanted to go back to the buy online and deliver from store economics, I'm trying to understand a little bit more. Our research that suggests that particularly millennials really want to do that, they don't necessarily really want to pick up in store. I was just wondering in looking at the uptake is exceeding expectations, what would the margins attached that business be?

Craig Menear (Chairman, CEO & President):

First of all, I would say that in our business, we have a lot of project businesses. We have a lot of things that are big and bulky. And so, I think that's why in many ways we are seeing in a significant portion of our customers choose to pick up their product in store and then potentially have it delivered from store.

We also have pros who are interested in having the product delivered from store to their jobsites. It saves them time. It saves their runners from having to come in to the stores overall. And then you know, candidly we've been doing delivery from store for quite some time for years.

Carol Tome (EVP, Corporate Services & CFO):

Yes, we have.

Craig Menear (Chairman, CEO & President):

And you know it's that's just part of the overall operating cost of doing business. And so you know, we approach that the on a day in day out basis as part of operating the business and you know, our value proposition for the customer across product takes that into account.

Scott Mushkin (Analyst - Wolfe Research):

I just want to remember, please refresh my memory, do you guys charge for that or is that not charged for?

Craig Menear (Chairman, CEO & President):

Yes, we do. We charge for it and there's options for tighter windows where it's a premium paid.

Scott Mushkin (Analyst - Wolfe Research):

Okay, perfect.

And I want to go into the credit changes extending from 30 to 60 days, and just try to understand a little bit more about the credit limits attached. I know you guys are using a bank to help you with that. What are what are your upper credit limits and is there thought of expanding that out and maybe just a little tutorial on that that would be great? And that's my last question.

Carol Tome (EVP, Corporate Services & CFO):

Sure our private-label credit card is underwritten by a third party.

I'll do averages then I'll talk to you about outliers. So for our commercial customers, these would be our pros. The average line of credit $6600.00, which seems to adequately meet their needs but we do have some higher spend pros. So the third part underwriter will extend larger lines, and we have six figure lines, too many of our customers ask for those lines.

Furthermore, if there is a situation where the credit lines tighten up a bit, we have a second look program with another third person provider that will take a second look at the request and up the line of credit. So we have a number of tools in our toolkit to adequately provide the financing requirements for our Pros. The biggest tool is moving to 60 days because if you think about it we are providing working capital support for them. They're going to get paid by their customers before they have to pay us back.

Scott Mushkin (Analyst - Wolfe Research):

So you said, I think there are some six figures out there. With the mix of the business, are you anticipating in all that $6,600.00, I think that referenced, going up meaningfully and would you guys ever think of taking this on your own balance sheet, or no?

Carol Tome (EVP, Corporate Services & CFO):

No. We will let the customer take us where they take us.

We want to grow the Pro and if they need more credit, we're happy to support them in that effort. In terms of taking it onto our balance sheet, we love the arrangement that we have with our third-party underwriter today.

Scott Mushkin (Analyst - Wolfe Research):

Perfect, thanks guys. Thanks for taking my questions.

Operator:

Chris Horvers, JP Morgan.

Chris Horvers (Analyst - JP Morgan):

Thanks. Good morning everybody.

I wanted to just ask at the risk of beating a dead horse, sort to speak, to follow-up on California and the oil markets. We've seen someone like Costco -- we've seen some variability in California, and you know, they sell a lot of food, so is a bit surprising to us. Are you seeing anything different in these markets that alert you or cause any concern?

I also understand you have done some analysis, so can you talk about any research that you've done around millennials and household formation, are they are they coming to form households? Now will -- do you think they'll act like Gen X did before them? And how do you think and impact the long-term outlook of the box and in the online business?

Ted Decker (EVP, Merchandising):

We've actually done a fair amount of research here and it was part of our strategic planning.

Last summer, we had several group millennial actually work on what Home Depot looks like 8 to 10 years out as well. What our research tells us is that basically this is a delayed cycle, that the the millennial generation has many of the same desires that generations prior to them have. We're seeing as household formation goes up, roughly a third or so of those formations are happening with millennial at the tail end of that age group. It appears there's about a six year delayed cycle here, but our research indicates that in many ways they lack the same as previous generations.

Carol Tome (EVP, Corporate Services & CFO):

You know, the average age of new home buyers last year was 33 years old. That's the edge of the millennial. So that's another proof point that at some point, they want to own a home.

Chris Horvers (Analyst - JP Morgan):

Yes.

Then one last -- just a clarification question, was there any impact of the month -- sort of to the Easter shift?

Carol Tome (EVP, Corporate Services & CFO):

Yes so, if we look how we reported comps, and I'm talking to the US now, March was reported at 7.7.

If you shifted to -- like for April that comp would've been a 9.2. April was reported at 4.6. It would've been like for like 3.6.

Chris Horvers (Analyst - JP Morgan):

Understood. Thank you very much.

Operator:

Matthew McClintock, Barclays.

Matthew McClintock (Analyst - Barclays):

Yes, good morning everyone.

I was wondering if we could ask a question on appliances. You know, thinking about the longer-term opportunity within that category, particularly now that you're seeing on other channels of retail that are maybe more challenged right now, the department stores, etc -- looking at that is also a new growth opportunity. Can you maybe just update us on your thoughts and maybe how that's starting to change now that you're seeing more competition in that category?

Craig Menear (Chairman, CEO & President):

We haven't seen the impact of any increased competition. Our appliances business is extremely strong again in the first quarter, in fact, it accelerated as we exited the quarter. We've been leading into that space as you know, and we're going to expand the appliance square footage in another hundred stores again this year. So were very happy with the results. In fact, certain markets that some others entered the space, we saw significantly higher performance than the rest of the country

Matthew McClintock (Analyst - Barclays):

Perfect. Thank you very much.

Operator:

Brian Nagel, Oppenheimer.

Brian Nagel (Analyst - Oppenheimer):

Good morning. Congratulations on a nice quarter.

So my first question which was market share, anything as you look at the data to suggest -- maybe comment on market share one way or the other -- and particularly, with what seemed to be somewhat of a volatile weather through the period; did that impact market share trends that you're seeing within the channel through the quarter?

Craig Menear (Chairman, CEO & President):

I don't think we have any way of knowing if weather really impacted shares.

We are really focused on making sure that were driving everyday great value for our customers and trying to bring innovative products that solve problems for them.

Ted, I don't know if you have any additional comments?

Ted Decker (EVP, Merchandising):

No again, with the weather, whether it has been normal or in fact good, our seasonal businesses of all stores been outperforming. And then the things that are tied more heavily to the consumer in outdoor garden, that is been extremely strong where we have good weather. So don't know yet if we would take any share there. And then right now, April in the north -- and even now with a day like today with a lot of rain -- again, we don't see great consumer outside sales but again, you don't know the relative performance at this point.

Brian Nagel (Analyst - Oppenheimer):

Got it, that's helpful.

The second question I have, I guess a bigger picture in nature, but a lot of questions I get a lot from our client is, "here's Home Depot -- they've put up great numbers now for a while, how much longer does this persist?" I know an analysis -- and you talked about it -- your analysts reviewed such like this to look at the productivity of the store -- you know, particularly by category -- maybe its more of a quick update there -- as you look around the store, and relative to historic peak -- where are the biggest opportunities in the categories to drive to drive increased productivity from here?

Ted Decker (EVP, Merchandising):

You know, I would say that as we look at that business -- first of all, my starting comment would be, "you know, we're planning a $550 billion market all in now with the addition of interline and playing in the MRO space for multi family hospitality and institutional. And we own less than 20% of that, so we think there's lots of opportunity to grow.

We have several initiatives underway. I have both Ann-Marie and

Mark Holifield here, so I'll let them comment. But there are several initiatives underway to drive productivity as we move forward -- and coordinated effort between our supply chain in our store operations team.

Mark Holifield (EVP, Supply Chain and Product Development):

Yes, we're very pleased, this is Mark Holifield.

We are very pleased with the supply chain sync initiative. We've got that rolled pretty much in the southern tier of RDC's with a good deal of our dollar flow on that. One of the things that's going along with sync is the floor load process, where we are loading up product on the floor. We were previously loading it on pallets and this is driving tremendous productivity just filling trucks much more full as they depart for stores. You know, we're still rolling, so still lots of opportunity.

Ann-Marie Campbell (Executive Vice President, U.S. Stores):

In conjunction with that, there is a tremendous opportunity in the store.

So as Mark talked about Project Sync, we are also focused on getting that product to the shelf. And as we manage the flow of product in the stores, we then really engineered the back end to create a better streamlined process to get the product on the shelf much quicker as well. So, there's a ton of opportunity there.

In addition, we talked about Buying Online, Deliver From Store and also talked about Buy Online, Ship to Store, and all those are convenient experiences for the customer. And we want to make sure that we ensure that we organize all labor around where the customer is going and create an efficient and effective process for them.

Carol Tome (EVP, Corporate Services & CFO):

And if I could jump in, there's a sales productivity opportunities too.

As Craig said, it's a huge market plan with lots of room for growth. But if you think about it from peak to trough, we still haven't fully recovered some of our category. So when I look at productivity still to be recovered; special order kitchens, some of our building material category still have room to recover from the peak.

Mark Holifield (EVP, Supply Chain and Product Development):

The building material categories in lumber mill work; those were still as Carol said, off for our 06 peak as we exited last year. And it was nice to see those were some of our strongest departments in the first quarter 2016. So it's nice to see larger project business underway.

Brian Nagel (Analyst - Oppenheimer):

Thank you. It was very helpful.

Operator:

Peter Benedict, Robert W. Baird.

Peter Benedict (Analyst - Robert W. Baird):

Hi guys. Thanks for taking the question.

In the past you've spoken to --I think it's roughly 25% of your sales mix as being in a bucket that you've considered at risk of online competition, obviously that's a big topic right now. Is that still the right way to think about it and can you give us any color maybe on how the products in that bucket have performed relative to rest the box or how you have been merchandising against that bucket?

Craig Menear (Chairman, CEO & President):

I say in general, it is still good way to think about it. If you think about those things that carry the highest level risk would be those that are you know, small package, reasonably high value, easy to ship product. So when you think about categories like power tools, faucets, and so on.

You know as Ted called out, we had a tremendous quarter is related to tool sales. Quite candidly we're seeing both channels grow in these categories that represent that 25%. We're staying very focused on driving great value for customers everyday.

Peter Benedict (Analyst - Robert W. Baird):

Okay good, that's helpful.

Carol, maybe just on leverages, is there is a scenario where you would be comfortable revisiting that two times leverage guardrail? What would need to happen for you to even consider something like that?

Carol Tome (EVP, Corporate Services & CFO):

Peter, as you know, our targeted debt adjusted EBITDA ratio is 2, we're slightly under that, were about at 1.9 today. We like 2 as a guardrail, it provides financial flexibility, but more importantly we can sleep at night because we don't have too much leverage as a company. So we like it.

So it's not, our goal to let that leverage ratio decline and it will as we earn more.

So as you've seen us in the past, as the leverage point gets to a certain inflection point and if interest rates are subtracted so on and so forth, we will raise incremental debt in our share repurchase program.

Peter Benedict (Analyst - Robert W. Baird):

Okay, fair enough. Thanks so much.

Operator:

Dan Binder, Jefferies & Co.

Dan Binder (Analyst - Jefferies & Co.):

If we look at the comps per sales for the quarter, there was a little bit of deceleration which I suspect was weather related. I was just curious if you could comment on whether May has picked back up or has seen trends similar to April?

Carol Tome (EVP, Corporate Services & CFO):

Yes, as I said earlier, one reason that we were confident with our ability to lift our sales for the year, is what we're seeing in May.

Dan Binder (Analyst - Jefferies & Co.):

Okay, good enough.

And then on the pro, I know that you said that it was above the company average and is somewhat of an estimate. But just curious, is the gap between the DIY and the Pro business widening, stable, or, narrowing?

Ted Decker (EVP, Merchandising):

It's not that dramatically different.

It was slightly stronger in the first quarter. I think we saw more outdoor project business which you can have a tendency to be pro related if you doing things like concrete.

Dan Binder (Analyst - Jefferies & Co.):

Lastly, on the overtime proposal that's out there being reviewed, can you just comment on how Home Depot would be able to digest if it becomes law?

Craig Menear (Chairman, CEO & President):

I mean we do look at all factors when we put together our plans.

Clearly we are aware that this was ill possible to come. That's factored into our guidance.

Dan Binder (Analyst - Jefferies & Co.):

Great, thank you.

Operator:

Jaime Katz, Morningstar .

Jaime Katz (Analyst - MorningStar):

I'm curious about lending standards. You guys have mentioned them in the past. I'm wondering if there have been any changes particularly if you have them by any sort of demographic? There have been a few articles out recently saying that millennials have had more difficult accessing the credit markets.

Carol Tome (EVP, Corporate Services & CFO):

Well, you can look it through two lenses.

First is just, call it consumer credit which may come through a bankcard or in our case through a private label card. We see consumer credit asked, being approved 71% of the time. So it's a pretty good approval rate.

Now, I'll tell you the cycle is pretty high, it's over 700, but that's a pretty good approval rate. It also speaks to the type of customers who are shopping at our store. The approval rates for our pro-cards or pro applicants is about the same, it's approved about 70% of the time. Then you need to look at lending standards, and for mortgages; and lending standards are changing ever so slowly, it's like glacier melting.

And you can appreciate why, because financial institutions have higher capital ratios, it's very hard to make a buck in this global environment. So you can understand why it's slow to move, but we've factored that in as we think about where our business may go. And if it were to be easy on underwriting standards for mortgages, that would be good news because the affordability index is something like 170, that's awesome. So if you can get approved, that's great.

Jaime Katz (Analyst - MorningStar):

Okay, and then can you guys offer any commentary on any lessons you may have learned so far for interlined brands or shared best practices you've adopted into the Home Depot model?

Craig Menear (Chairman, CEO & President):

So I think lessons learned would be that our anticipation that we have a customer who has common need across both businesses would be a clear learning. You know, the desire for the customer whether it's an interlined customer to fill in and shop at the Home Depot and or customers who are shopping at the Home Depot to have a desire to buy through interline is there.

We're pleased with the start of it. Bill, you do have any other comments?

Bill Lennie (EVP, Outside Sales & Service):

Jaime, Bill Lennie.

Just - I think Craig's exactly right, we're encouraged by the customer feedback and the advantages they see when we combined interline at Home Depot . And then, the second thing that we're pleased with is the collaboration we're seeing within our outside sales organizations and our ability to join forces and sell across all markets.

Jaime Katz (Analyst - MorningStar):

Thank you.

Operator:

Michael Baker, Deutsche Bank.

Michael Baker (Analyst - Deutsche Bank):

Thanks I wanted to - maybe even three follow ups.

One, just to be clear, are you raising the full year guidance because of currency being less burdensome then what you saw in first quarter? Are you also changing and I guess - raising the second, third, or fourth quarter guidance or is all the increase because of what we saw in the first quarter and currency?

Carol Tome (EVP, Corporate Services & CFO):

Mike, the increase is solely related the outperformance we saw in the United States.

The reason that we are no longer providing a range is that the exchange rates that we use for our plan are now about the same as the current (spotlight), so no need to provide a range. But we're just rolling forward outperformance except for weather driven demands, we're rolling over the zest of the outperformance.

Michael Baker (Analyst - Deutsche Bank):

Okay, so no real change in how you would have thought about the second, third, and fourth quarter?

Carol Tome (EVP, Corporate Services & CFO):

That's right.

Michael Baker (Analyst - Deutsche Bank):

Okay, thank you.

Two others. One, Easter as I understand it - so Easter hurt March, helped April, I guess that's because of the store as people don't really shop on Easter but I would've thought that would've been outweighed by people shopping before Easter to do some outdoor projects. I guess that's not the case as Easter hurt March and it helped April. Is that correct?

Carol Tome (EVP, Corporate Services & CFO):

Easter is not a big selling day for Home Depot .

Michael Baker (Analyst - Deutsche Bank):

Right, but again, sales are around Easter don't offset that I suppose?

Carol Tome (EVP, Corporate Services & CFO):

No, they don't.

Craig Menear (Chairman, CEO & President):

You lose a weekend effectively.

Carol Tome (EVP, Corporate Services & CFO):

Yes, because it's a weekend in Spring.

Craig Menear (Chairman, CEO & President):

Okay.

Carol Tome (EVP, Corporate Services & CFO):

Again, it doesn't impact the store.

Michael Baker (Analyst - Deutsche Bank):

Right understood.

And then one last, this is may be a bigger picture question but it sounds like you think some of the housing trends are favorable and we agree with that. One thing I think you look at as an important metric and we agree again -- is that of home price appreciation, but home prices are now pretty close to where they were in 2006 if we think of that as the peak year. So do you think - how do think about that? Are we concerned that is to be less on home price appreciation and then therefore less of a driver to your business?

Craig Menear (Chairman, CEO & President):

I think the way we look at it and the important factor is when home values are positive, it's a good thing for our business.

Truly, the customer knew to recover the value of their homes. We've seen that recovery - you know, obviously take place and improve for a large portion of customers. As long as home values stay positive, it's a good thing.

I mean, for years and years home values grew on average in the low single digit 1%, 2%, 3%.

Michael Baker (Analyst - Deutsche Bank):

I see your view, as we are now back towards peak year, your view is that home price appreciation can continue?

Carol Tome (EVP, Corporate Services & CFO):

We've factored that into our longer term forecast.

Now this year, we believe home prices will be up around 5%. It's important to note that it's not fully recovered even with that 5%, and its certainly different in other parts of the country. So we think 5% this year and we think next year maybe 3%, the year on after that 2%, so it continues to Craig's point - there is just ongoing home price appreciation.

Michael Baker (Analyst - Deutsche Bank):

Okay thank you. Great color, I really appreciate the time.

Craig Menear (Chairman, CEO & President):

Thank you.

Carol Tome (EVP, Corporate Services & CFO):

Derek, we have time for one more question.

Operator:

Dennis McGill, Zelman & Associates.

Dennis McGill (Analyst - Zelman & Associates):

Hi good morning, thank you. Just a couple of quick ones.

Carol, on the cash flow, could you just refresh how we should think about cash flow drop down for the year and working capital as you work through the year?

Carol Tome (EVP, Corporate Services & CFO):

Yes, so we think we generate around $10 billion of cash from the business this year. That includes a slight improvement in working capital principally in inventory turnover. We're planning to take our inventory turnover up by a tenth in 2016.

Dennis McGill (Analyst - Zelman & Associates):

And then the share transaction is greater than 900, I think you talked about that it's around 20% of late. Where did that peak out in the last cycle?

Carol Tome (EVP, Corporate Services & CFO):

Where did it peak out in 2006?

Dennis McGill (Analyst - Zelman & Associates):

Yes, just a sign of a big ticket share.

Carol Tome (EVP, Corporate Services & CFO):

I don't know. I would have to go look at it. I'm not even sure we did that barbell analysis back in 2006.

Craig Menear (Chairman, CEO & President):

No, I don't know if we did in 2006. I can tell you that for the last seven or eight - maybe seven years, it's been pretty comparable to that.

I think the other factor to consider is when we look at 2006 and look at kind of peak performance, in our own minds, we're not sure what the peak really was. In 2006, we actually have negative transaction, we were firing customers. And so, we don't know that we actually - we assume we didn't actually peak in 2006 the way we should have.

Dennis McGill (Analyst - Zelman & Associates):

Okay, that's fair. Thank you guys.

Diane Dayhoff (VP, IR):

Well, thank you for joining us on our call today. And we look forward to discussing our second quarter earnings in August.

Operator:

That does conclude today's conference. We appreciate your participation.

END