



## ANALYST QUICK NOTES

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**Home Depot Inc. (NYSE: HD: BUY)**

**Target Price: \$130**

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**7/13/2015**

### **A Potential Catalyst for HD and LOW**

- New research from Joint Center for Housing Studies, Harvard University researcher Abbe Will.
- “Aging Society and Inaccessible Housing Stock Suggest Growing Need for Remodeling.”
- The number and share of U.S. households age 65 and over will rise dramatically as the oldest members of the baby-boom generation reach retirement age.
- With age comes the growing presence of disability and problems using home fixtures and appliances without assistance.
- Much of the housing stock is ill-equipped. Less than 1/3 has even basic accessibility features.
- Of more than 25 million households 65 and over, 44% have need for basic accessibility features such as first-floor bedrooms and bathrooms, grab bars in showers, more accessible door handles.
- Many homeowners will “Age in Place” and they will need to retrofit their homes to continue to live there in comfort and safety.
- Construction of new housing is expected to fall considerably short of demand in Northeast and Midwest.
- Given the attitudes of today’s older homeowners, the remodeling industry
- Harvard cites significant retrofit spending on existing homes.
  - Total home improvement spending by older homeowners could surge by an additional \$17 billion annually over the next three years.

### **Comments Relevant to Home Improvement from 1Q earnings calls:**

#### **Home Depot:**

- The housing trends that we see in the market are positive ... in some cases above our assumptions overall. It’s certainly when home values go up, it gives customer confidence to drive into the project business, and when we see home turnover, that generally drives activity as well.”

**Toll Brothers:**

- “The economy and housing continue on parallel paths of recovery. It appears that the housing market is on firm footing and heading in the right direction. As pent-up demand is released, we envision a solid recovery for housing.”
- Yearley, Jr.: “We’ve always said that if the rates tick up slowly because of great economic news, which is why they should tick up, we’ll take it all day long. And right now, buyers don’t talk about rates. It’s not an issue. They’ve been sitting at this number for so long. So we don’t see it as an issue right now for our business.”

**Whirlpool:**

- “From a broader US market perspective, we believe the industry is on track for a multi-year recovery as evidenced by our recent increase in the existing home sales. In the first quarter, the industry was up 1% and we expect the full year industry to be up around 4%.”

**KB Home:**

- Mezger: “The national economy is continuing to improve with sustained job growth now occurring across the country. This improving employment and economic environment is in turn contributing to increased consumer confidence, which is currently at one of the highest levels reported since 2007.
- Meanwhile, the housing market also continues its measured recovery. Inventory levels remain well below normal, and while there is still price appreciation occurring in most markets, it is at a more moderate and sustainable pace. Even with the slight uptick in mortgage rates over the past week, affordability remains at compelling levels. The most encouraging statistical trend that bodes very well for future housing demand is the dramatic increase now occurring in household formation.”
- Kaminski: “If you think about it, over a 40-year period, the nation averaged 1.2 million household formations. From the period of 2008 to 2014, we averaged 500,000, well below normal.

**What differentiates HD and LOW from other retailers?**

- Less vulnerable to internet competition.
- Potential tail wind from a housing recovery.

**What is the case for additional upside for Home Improvement Retail?**

- Residential investment is still near a 66-year low, at 3.3% of GDP.
  - Well below the average of 4.6% since 1946.
- Home prices are still below 2006 peak levels and affordability is positive.
- Nearly two-thirds of U.S. homes are more than 25 years old and likely in need of upgrades and repairs.
- Lowe's is seeing:
  - Signs of modest home price appreciation in mid-sized markets.
  - An increasing customer willingness to invest in home improvement.
  - An uptick in big-ticket projects.
- The National Association of Home Builders Remodeling Index indicates improving conditions, particularly for maintenance and repair.
- Harvard University's Leading Indicator of Remodeling Activity also points to growth, but at a slower rate in the first three quarters of 2015 before accelerating again in 4Q.
- We believe that these factors point to sustainable growth for HD and Lowe's.

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