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A Financial Analysis and Valuation of Home Depot

Haolin Ma[1,a,*]

[1]*School of Statistics, Renmin University of China, Beijing, 100872, China*
a. mahaolin663@ruc.edu.cn
**corresponding author*

Abstract: This paper presents a detailed financial analysis and market evaluation of major players in the home improvement industry—Home Depot, Lowe's, Wayfair, and Floor & Decor Holdings. It assesses these companies based on their liquidity, solvency, and profitability to provide investors with actionable insights into their financial health and market position. The analysis reveals that Wayfair, despite its robust short-term liquidity, faces challenges with profitability. Home Depot and Lowe's both demonstrate strong financial stability with efficient operations that translate sales into profit effectively, though Lowe's exhibits some concerns related to its debt levels. Floor & Decor shows impressive growth but must improve its operational efficiency to enhance profitability. Additionally, the study explores industry trends impacting these businesses, including changes in consumer preferences and economic conditions affecting spending on home improvements. It also examines the companies' responses to these trends, such as adapting their business models and strategies to sustain growth and competitiveness. The paper concludes with investment considerations, highlighting Wayfair as a potentially high-reward but risky investment due to its growth prospects and operational challenges. Home Depot remains a relatively safe bet with stable financial returns, while Lowe's and Floor & Decor might require cautious evaluation due to their financial and market positions. This comprehensive analysis serves as a crucial tool for investors aiming to navigate the complexities of the home improvement sector and make informed decisions.

Keywords: The Home Depot, Financial Analysis, Valuation, Home Improvement Industry

1. Introduction

This paper aims to analyze several leading companies in the home improvement industry, including Home Depot, Wayfair, Lowe's, and Floor & Decor Holdings. Through a deep examination of these companies' business models, market performance, and recent developments, this paper aims to provide valuable insights and recommendations for investors.

Home Depot is a global leader in the retail of home improvement and construction products, primarily catering to builders, contractors, and do-it-yourself customers. With a vast network of physical stores and an expanding online presence, the company holds a substantial market share in the United States, Canada, and Mexico [1]. Over the past four years, the financial year 2024 marked a downturn in its rising trend, with revenues dipping to $152.669 billion. The company's impressive peak in the prior year could be attributed to strategic expansions and market demand.

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Lowe's is a major retailer of building materials and home improvement products, with a presence comparable to Home Depot across the United States and Canada. Targeting both DIY consumers and professional contractors, Lowe's focuses on offering high-quality products and excellent customer service [2]. With a steady increase in total revenue from $89.597 billion in 2021 to a high of $97.059 billion in 2023, The subsequent fall to $86.377 billion in 2024 could suggest a correction after an exceptional growth phase.

Wayfair operates as an online retailer specializing in furniture, home decoration, and household goods. Renowned for its extensive product selection and convenient shopping experience, the company serves customers primarily in North America and Europe. Wayfair's revenues have declined consistently from a high of $14.145 billion in 2020 to $12.003 billion in 2023, As an online retailer, Wayfair's dip could reflect the normalization of online shopping trends post a boom during certain events like the pandemic.

Floor & Decor Holdings specializes in flooring and related decor materials, offering a wide range of products including hardwood, tile, stone, and accessories. With numerous stores across various states in the U.S., the company caters to both residential and commercial customers. Floor & Decor Holdings had a remarkable growth trajectory, with revenues climbing from $2.426 billion in 2020 to $4.414 billion in 2023. This annual increase suggests a successful expansion strategy.

On the positive side, the industry seems to be bouncing back, with an anticipated improvement in the availability of raw materials, although prices are expected to be higher. Home improvement trends are shifting to focus on quick remodels that improve the quality of life and accessibility within homes. This includes adding features like grab bars, walk-in showers, and smart home upgrades. Another trend driven by the ongoing impact of the pandemic is the increase in remote work, which has led to sustained demand for home office renovations. Additionally, tax credits for energy-efficient home improvements are encouraging homeowners to invest in renovations that will bring long-term savings and environmental benefits. The industry is also facing challenges. The Harvard Joint Center for Housing Studies predicts a downturn in home remodeling, with spending expected to shrink for the first time since 2010, though the rate of decline may ease towards the end of the year [3]. This anticipated downturn is attributed to high prices, elevated interest rates, and weak home sales, which create uncertainty and may dampen remodeling activity.

2. Performance Evaluation

This section evaluates the liquidity, solvency, and profitability of Home Depot (HD) and its competitors Lowe's (LOW), Wayfair (W), and Floor & Decor Holdings (FND). These financial ratios provide insights into the ability of these companies to meet their short-term obligations, manage long-term debts, and generate profits. This comprehensive analysis highlights the strengths and potential challenges each company faces in maintaining financial stability and growth.

2.1. Liquidity

Table 1: Liquidity ratios of Company HD and its competitors.

	HD	LOW	W	FND
Current Ratio	135.25%	122.50%	84.97%	114.29%
Quick Ratio	39.97%	13.98%	81.54%	18.27%
Cash Ratio	17.08%	7.89%	61.89%	2.98%

Data Source: Nasdaq.

According to the current ratio shown in Table 1, it can be concluded that HD has the highest current ratio of 135.25%, indicating that it has sufficient current assets to cover current liabilities and has very strong liquidity. LOW and FND also have high current ratios of 122.50% and 114.29%, respectively, indicating good short-term solvency. W's current ratio is relatively low, at 84.97%, which means that its current assets are less than its current liabilities and may face some liquidity pressure.

For quick ratio, the quick ratio of W is extremely high, reaching 81.54% and indicating that even without relying on slow-moving assets such as inventory, the company can still meet short-term liabilities well. HD also has a high quick ratio of 39.97%, demonstrating good debt-paying ability. The quick ratio of FND and LOW is relatively low, at 18.27% and 13.98% respectively, which may indicate that these two companies rely on a larger proportion of inventory or other assets that are not easily liquidated quickly.

For Cash Ratio, W exhibits a very high cash ratio of 61.89%, demonstrating that it has ample liquid assets to cover its current liabilities. HD's cash ratio is also relatively strong at 17.08%, suggesting a comfortable cash and equivalents position. LOW and FND have lower cash ratios at 7.89% and 2.98%, respectively, indicating higher short-term liquidity risk.

In conclusion, W exhibits very strong debt repayment capabilities in the short term, which could be attributed to its business model heavily reliant on direct-to-consumer sales online, minimizing physical inventory needs compared to traditional retailers; HD shows good overall liquidity across all three indicators, it has maintained a focus on enhancing customer experience and operational efficiency, which helps sustain its financial health. LOW and FND, while having adequate current ratios, their lower quick and cash ratios suggest potential reliance on slower-to-convert assets or future income to meet short-term liabilities. FND has been opening new stores and entering new markets, such as the flagship store in New York City. Such expansions require significant capital outlays, which could tie up cash that otherwise might bolster liquidity measures; LOW has also demonstrated commitment to expanding its market share, particularly in the professional contracting space [4].

For W and HD, such liquidity metrics may be more attractive to investors, whereas LOW and FND might need strategic adjustments or improvements to enhance their liquidity positions.

2.2. Solvency

Table 2: Solvency ratios of Company HD and its competitors.

	HD	LOW	W	FND
Total Debt Ratio	98.64%	136.01%	177.92%	58.59%
Long-term Debt Ratio	55.85%	84.66%	89.00%	4.18%
Interest Ratio	11.25	8.36	-	32.48

Data Source: Nasdaq.

For total debt ratio shown in Table 2, W has the highest total debt ratio at 177.92%, indicating that it has significantly more debt than assets; LOW follows with a total debt ratio of 136.01%, also indicating substantial reliance on debt and HD has a lower yet substantial total debt ratio at 98.64%; FND presents a much healthier picture with a total debt ratio of 58.59%, showing a more balanced approach between debt and assets.

For long-term debt ratio, W again shows a high long-term debt ratio at 89.00%, suggesting a significant amount of its debt is long-term; LOW also has a high long-term debt ratio at 84.66%; HD has a moderate long-term debt ratio of 55.85%, reflecting a more conservative debt structure; FND has a very low long-term debt ratio of 4.18%, indicating minimal reliance on long-term debt, which may imply greater financial flexibility and less risk of long-term financial commitments.

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For Interest Coverage Ratio, FND stands out with an exceptionally high-interest coverage ratio of 32.48, highlighting its strong earnings ability to cover interest expenses comfortably; HD and LOW, with interest ratios of 11.25 and 8.36, still maintain adequate coverage, though it is less robust compared to FND; W had negative earnings before interest and taxes, which would make this ratio irrelevant for the period.

In summary, HD's solvency ratios show a balanced approach to debt management, with a relatively moderate total debt and long-term debt ratio; LOW shows higher total and long-term debt ratios compared to HD, indicating a more aggressive debt position. However, LOW has faced challenges such as a significant decline in comparable-store sales and has been downgraded by analysts due to performance concerns compared to its competitors; W has an aggressive growth strategy, primarily funded through debt. W operates in the e-commerce space, which requires substantial upfront investment in technology and market expansion. Its negative earnings before interest and taxes could suggest potential challenges in generating sufficient earnings to cover interest expenses; FND has very low long-term debt ratios and a high interest coverage ratio, indicating strong earnings relative to its debt obligations.

2.3. Profitability

Table 3: Profitability ratios of Company HD and its competitors.

	HD	LOW	W	FND
Gross Margin	33.38%	33.39%	30.55%	42.10%
Operating Margin	14.21%	13.38%	-6.77%	7.28%
Net Profit Margin	9.92%	8.94%	-6.15%	5.57%
Asset Turnover	2.00	2.02	3.40	0.98

Data Source: Nasdaq.

For gross margin shown in Table 3, FND stands out with the highest gross margin of 42.10%, indicating its ability to retain a larger percentage of each dollar of sales as profit before accounting for certain expenses; HD and LOW show very similar gross margins, around 33.38% and 33.39% respectively; W has a slightly lower gross margin at 30.55%, which could be due to its e-commerce business model that might involve higher logistics and operating costs.

For operating margin, HD has the highest operating margin at 14.21%, LOW follows closely at 13.38%, suggesting that they have efficient management of operational costs relative to sales; FND shows a moderate operating margin of 7.28%; While W has a negative operating margin of -6.77%, indicating that there are extremely high operating expenses compared to total revenue.

For net profit margin, HD and LOW again lead with net profit margins of 9.92% and 8.94%, demonstrating its ability to translate sales into net income effectively; FND has a reasonable net profit margin of 5.57%, lower than HD and LOW, indicating that it retains less net income from each dollar of revenue; W shows a negative net profit margin of -6.15%, reflecting significant challenges in achieving profitability under its current operating model.

According to asset turnover, W has the highest asset turnover ratio at 3.40, indicating that it generates significantly more revenue per dollar of assets compared to the others. This high ratio is typical for e-commerce platforms, which typically require less physical asset investment; HD and LOW have similar asset turnovers, around 2.00 and 2.02 respectively, suggesting efficient use of assets to generate revenue; FND has the lowest asset turnover at 0.98, indicating less revenue generation per dollar of assets, which could be due to a heavy investment in physical stores and slower turnover of inventory.

In conclusion, HD demonstrates strong performance across all margins and decent asset utilization, reflecting efficient operations and effective cost management; LOW follows closely but shows slight variations that could imply room for improvement in cost control or operational efficiencies; FND, despite its strong gross margin, needs to enhance its operational efficiency and asset utilization to boost its bottom line; W faces significant challenges in terms of profitability and operational efficiency, although it excels in generating revenue relative to its asset base. Strategies to convert this revenue efficiency into profitability would be crucial for W's sustainable growth.

3. Valuation

Next, this paper will conduct a valuation for four companies, judging their expected performance through some of their financial indicators, and analyze the strategies and risks of the companies and related industries [5].

3.1. Forecast

As Table 4 shown, HD's TTM P/E is 23.09 and its NTM P/E is 22.73 (indicating stable earnings expectations); LOW TTM P/E is 18.08 (lower, suggesting better valuation compared to HD), its NTM P/E is 19.43; W's TTM P/E is Negative (due to negative EPS), its NTM P/E is 69.67 (suggesting significant growth expectations or high risk); FND Holdings' TTM P/E is 54.00 (indicating potentially overvalued status), its NTM P/E is 64.18 (increasing, suggests worsening valuation). HD and LOW have P/E ratios indicating higher investor expectations compared to FND. W's negative TTM P/E is due to its negative EPS, but its high NTM P/E suggests that improvements in profitability are expected.

For revenue growth rate, Both W (5.8%) and FND (5.8%) show significantly higher revenue growth rates than HD (1.1%) and LOW (-2.3%). For the EPS growth rate, there is negative growth for LOW (-7.0%) and FND (-15.9%); HD shows slight positive growth (1.6%). W currently has negative TTM EPS but is expected to turn positive in the next twelve months [6].

HD's PEG ratio of approximately 14 is significantly high, which suggests that the stock may be overvalued given its relatively low growth rate of 1.6%. This high PEG ratio implies that the current price is steep relative to the rate at which the company's earnings are expected to grow [7]. While the other companies are not available.

W has the highest GP/A ratio (105.6%) among the four, indicating it is most effective at generating gross profit from its assets despite its current net loss. This could be a sign of potential if the company manages to control other costs or increase efficiency further; LOW (69%) also shows a strong GP/A ratio, slightly higher than HD's (66.6%), suggesting efficient asset utilization; FND Holdings has the lowest GP/A ratio (39.9%), indicating less efficiency in converting assets into gross profits compared to the others.

HD's annual gross margin shows fluctuation but is generally stable at around 33.5%. Net profit margin has a slight decline to 9.9%; For its quarterly margins, gross margin slightly fluctuates between 33.0% and 33.8%. Net profit margin has varied from 10.4% down to 8.1%; For LOW annual margins, gross margin is stable at around 33.3%. Net profit margin increased from 6.5% to 8.9%; But its quarterly net profit margin shows a consistent decrease from 10.1% to 5.5%; For W's annual margins, the gross margin has increased from 28.4% to 30.6%. Net Profit Margin has shown volatility, improving from -10.9% to -6.1%; For its quarterly margins, gross margin increased slightly from 29.6% to 30.3%. Net profit margin shows fluctuating negative margins, showing signs of improvement but remaining negative; FND Holdings' annual gross margin has slightly increased. Net profit margin shows a decreasing trend from 8.0% to 5.6%; Its quarterly net profit margin has declined significantly from 6.4% to 3.5%.

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HD and LOW show stable gross margins with varying degrees of net profit margin stability. W exhibits increasing gross margins but continues to struggle with negative net margins, though there is an improving trend. FND Holdings shows very stable high gross margins but a concerning decrease in net margins both annually and quarterly [8].

Table 4: Financial analysis of Company HD and its competitors.

	HD	LOW	W	FND
Share Price	$348.67	$236.08	$71.06	$122.59
TTM EPS	15.1	13.06	-1.16	2.27
NTM EPS	15.34	12.15	1.02	1.91
EPS Growth Rate	1.6%	-7.0%	N/A	-15.9%
Revenue Growth Rate	1.1%	-2.3%	5.8%	5.8%
TTM P/E	23.09	18.08	(61.26)	54.00
NTM P/E	22.73	19.43	69.67	64.18
PEG	14.53	N/A	N/A	N/A
GP/A	66.6%	69.0%	105.6%	39.9%

Data Source: Nasdaq & Estimize.

3.2. Strategy & Risks

HD is focusing on modest growth through new store openings despite a general downturn in the market. This strategy is aimed at capturing more market share and maintaining revenue streams even as same-store sales decline. The company is responding to changing consumer preferences by focusing on quick home remodels that improve quality of life and accessibility, such as smart home features and more accessible bathroom fixtures. This reflects an adaptation to ongoing trends accelerated by the pandemic, like remote work and energy efficiency. Like W, HD also focuses on the enhancement of Online Capabilities: HD continues to develop its online presence to cater to the surge in e-commerce, aiming to provide a seamless shopping experience that integrates its physical stores and online platforms.

HD recently reported a slight decline in sales, with fourth-quarter revenue falling by 2.9% to $34.8 billion. This drop was better than expected, but same-store sales still fell by 3.5% globally and 4% in the U.S. The decrease in "big ticket" transactions, those over $1,000, suggests that both builders and homeowners are undertaking smaller projects instead of significant remodels. HD projects only a modest 1% sales increase for the next fiscal year, primarily from new store openings, with same-store sales expected to decline by 1%. As the market becomes more competitive, particularly with the rise of online alternatives, Home Depot needs to continually innovate and improve its service offerings to maintain its market lead. There are other risks for HD: Like many others in the retail sector, Home Depot is potentially vulnerable to disruptions in the supply chain, which could affect inventory availability and cost structures.

LOW reported a 6.2% drop in comparable store sales for Q4 2023. Despite this, it managed to beat analyst forecasts. The company noted that its Pro segment held up better than its DIY segment, which still constitutes the majority of its revenue. FND plans to continue expanding, with up to 35 new stores expected to open, which might boost their overall sales. FND's strategy to open new stores could be doubted to help drive revenue growth. W started a physical store this year, profit margins are often slim for physical retail, their revenue on it is still doubtful and it can also influence its NTM EPS. W, despite the potential for revenue growth, faces challenges in turning this into profit.

The home improvement industry overall is facing a tough market with weak consumer spending and a subdued housing market. Factors like inflation, slow housing sales, and a shift in consumer

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spending toward experiences rather than goods have contributed to this downturn [9]. However, segments like DIY and new home construction are slightly less impacted but are still experiencing slower growth compared to previous years [10].

4. Conclusion

Home Depot and Lowe's show stable gross margins with varying degrees of net profit margin stability. Home Depot has more variability in net margins quarterly, while Lowe's shows improvement annually. Wayfair exhibits increasing gross margins but continues to struggle with negative net margins, though there is an improving trend. Floor & Decor Holdings shows very stable high gross margins but a concerning decrease in net margins both annually and quarterly.

Based on the analysis above, Wayfair is more likely to be expected by investors. Considering that both Lowe’s and Floor & Decor Holdings have negative EPS growth rates, choosing them might be a value trap. Although Home Depot has a relatively stable performance and a positive EPS growth rate, because it has a high PEG ratio, it is expensive per unit of growth rate. Moreover, both its net profit margins and gross margins are declining according to quarterly and annual data. Moreover, Wayfair performs exceptionally in terms of GP/A, and the NTM EPS performance is promising. There is also hope that reductions in operating expenses could lead to a rebound in its net profit. It is a risky but promising stock.

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