HD – Q3’24 Home Depot Earnings Call
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PRESENTATION

Operator

Greetings, and welcome to The Home Depot Third Quarter 2024 Earnings Conference Call. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Isabel Janci. Please go ahead.

Isabel Janci - *The Home Depot, Inc. - VP, IR & Treasurer*

Thank you, Christine, and good morning, everyone. Welcome to Home Depot's third quarter 2024 earnings call. Joining us on our call today are Ted Decker, Chair, President and CEO; Ann-Marie Campbell, Senior Executive Vice President; Billy Bastek, Executive Vice President of Merchandising; and Richard McPhail, Executive Vice President and Chief Financial Officer.

Following our prepared remarks, the call will be open for questions. Questions will be limited to analysts and investors, and as a reminder, please limit yourself to one question with one follow-up. If we are unable to get your question during the call, please call our Investor Relations department at 770-384-2387.

Before I turn the call over to Ted, 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 presentation will also include certain non-GAAP measures including, but not limited to, adjusted operating margin and adjusted diluted earnings per share. For a reconciliation of these and other non-GAAP measures to our corresponding GAAP measures, please refer to our earnings press release and our website.

Now, let me turn the call over to Ted.

Ted Decker - *The Home Depot, Inc. - President & CEO*

Thank you, Isabel, and good morning everyone.

Sales for the third quarter were $40.2 billion, an increase of 6.6 percent from the same period last year. Comp sales declined 1.3 percent from the same period last year, and our U.S. stores had negative comps of 1.2 percent. Adjusted diluted earnings per share were $3.78 in the third quarter, compared to $3.85 in the third quarter last year.

From a geographical perspective, storms and more favorable weather throughout the quarter drove a higher degree of variability in the performance across our divisions, and four of our nineteen U.S. regions delivered positive comps. In local currency, Mexico and Canada posted comps above the company average, with Mexico posting positive comps in the quarter.

In the third quarter, our associates and communities were impacted by two hurricanes. As you'll hear from Ann, our associates and supplier partners worked tirelessly under difficult circumstances to serve our customers and communities. Our thoughts continue to be with those impacted by Hurricanes Helene and Milton.

Excluding the impacts from the hurricanes, our third quarter performance exceeded our expectations. As weather normalized, we saw better engagement across seasonal goods and certain outdoor projects. But as Billy will detail, we continue to see pressure on larger remodeling projects, driven by the higher interest rate environment and continued macroeconomic uncertainty.

Today, we updated our guidance, primarily as a result of the better performance in the third quarter, as well as expected hurricane-related demand in the fourth quarter. For Fiscal 2024, we now expect our sales to grow approximately 4.0 percent, comps to decline approximately 2.5 percent, and adjusted diluted earnings per share to decline approximately 1%. Richard will take you through the details in a moment.

Despite the continued uncertainty in the macroeconomic environment, our focus remains on creating the best interconnected experience, growing Pro wallet share through a differentiated set of capabilities, and building new stores. Today, I would like to highlight where we are improving the interconnected experience.

Recall that over the last several years, we built a network of downstream supply chain facilities, including 19 Direct Fulfillment Centers, allowing us to reach 90% of the U.S. population with same or next day delivery. Recently, we expanded our assortment in these facilities to allow for faster delivery speeds across more products. And we made significant website enhancements to better communicate faster delivery options.

Many customers were not aware of our robust delivery options. In the third quarter, we launched a marketing campaign that builds awareness of our faster delivery speeds. And while this has just launched, we are seeing the intended results – greater customer engagement, higher conversion, and incremental sales.

This is also the first quarter that reflects a full period of SRS in our financials. SRS gives us the right to win with the specialty trade Pro customer, who needs specialized capabilities to complete their project. The SRS team did an exceptional job in the quarter and is on track to deliver $6.4B in sales for the approximately seven months we'll own them in Fiscal 2024. As you would expect, the immediate focus with SRS is supporting their growth – both organically and through acquisitions. However, we are also seeing incremental cross-sale opportunities from our distinct product catalogs and competitive advantages.

As you can tell, we remain excited about the growth opportunities in front of us, and we are committed to investing in our capabilities to continue growing share in any environment. Our merchants, store and MET teams, supplier partners, and supply chain teams did an outstanding job executing throughout the quarter, and I'd like to thank them for their dedication and hard work.

Before I turn the call over to Ann, I'd like to take a moment to reflect on the legacy of our co-founder Bernie Marcus. We owe an immeasurable debt of gratitude to Bernie. He was a master merchant and a retail visionary. But even more importantly, he valued our associates, customers, and communities above all. He's left us with an invaluable legacy and the backbone of our company: our values and culture. The entire Home Depot family is deeply saddened by his passing. He will be missed.

With that, let me turn the call over to Ann.

Ann-Marie Campbell - *The Home Depot, Inc. – Senior EVP*

Thanks Ted and good morning everyone.

First, I want to extend my deepest sympathy and support to all the residents and communities that have been impacted by Hurricanes Helene and Milton. One of the hallmarks of the Home Depot has always been to support our communities through natural disasters, and we are incredibly proud of the tireless efforts of our teams pre and post the storms to stage and deliver the needed products while ensuring the safety of our associates. In the aftermath of the storms, the efforts of both our field and Store Support Center teams have been extraordinary and demonstrate the culture and exceptionalism of our amazing associates who are committed to providing the necessary support and resources to help rebuild and restore their communities. Our thoughts and prayers continue to be with all of our affected associates and communities as they navigate this challenging time.

Over the last year, I have provided some key insights on the progress we are making with our Pro ecosystem capabilities that serve Pros working on larger, complex projects. We are pleased with the performance of this Pro Ecosystem, which is now in 17 U.S. markets.

Today I would like to take a moment to highlight some of the investments we are making in our stores to deliver the best experience for every Pro buying occasion. You've heard us talk about our focus on improving on shelf availability through multiple initiatives but we are also enhancing leadership oversight, processes, and systems to drive the overall in-store Pro customer experience. We recently introduced the Pro Customer Experience Manager to help drive a higher level of connectivity with our in-store pro and outside sales team in order to deliver a more seamless experience and exceptional service. This new leadership role with our existing teams enables us to focus more on the needs of the cash and carry Pro, with a focus on building relationships with our most important Pros, ensuring we have job-lot-quantities available for sale on critical SKUs, and allocating more labor hours to the Pro desk during peak shopping times. We also continue to improve My View with more robust insights to drive a deeper level of engagement and more actionable outcomes for our Pro customers. These tools, combined with process improvements, leadership engagement, and increased emphasis on service, are driving more customer engagement and improving the in-store shopping experience for our Pro customers.

I would also like to take a minute to share with you a bit more around the progress we have seen over the last few quarters as it relates to shrink. For us, our focus on mitigating shrink has been a continual and evolving process, leveraging our cross functional teams and investing in technology to test and learn the most effective methods of reducing shrink. While the external environment continues to be challenging, we are incredibly pleased with the positive momentum we are seeing and improved results through our shrink mitigating initiatives.

I could not be more excited about the progress we are making across the business to drive a best-in-class experience for our customers. Our stores are ready, and our associates stay engaged, and I would like to thank them for all that they do.

Lastly, as one of the hundreds of thousands of Home Depot associates inspired by Bernie's passion for giving back to our associates and our communities, I want to extend my deepest condolences to the entire Marcus family.

With that, let me turn the call over to Billy.

Billy Bastek - *The Home Depot, Inc. – EVP, Merchandising*

Thank you, Ann, and good morning everyone.

I want to start by also thanking all of our associates and supplier partners for their ongoing commitment to serving our customers and communities. As you heard from Ted, our performance during the third quarter exceeded our expectations as we saw better engagement in some seasonal related categories as a result of more favorable weather throughout the quarter. In addition, we also saw incremental sales as a result of the hurricanes. However, the higher interest rate environment and greater macro-economic uncertainty continues to pressure overall project demand.

Turning to our merchandising department comp performance for the third quarter… our power, outdoor garden, building materials, indoor garden and paint departments posted positive comps, while lumber, plumbing and hardware were all above the company average.

During the third quarter, our comp transactions decreased 0.6 percent, and comp average ticket decreased 0.8 percent. However, we continue to see our customers trading up for new and innovative products.

Big-ticket comp transactions, or those over $1,000 dollars, were down 6.8 percent compared to the third quarter of last year. We continued to see softer engagement in larger discretionary projects where customers typically use financing to fund the project such as kitchen and bath remodels.

During the third quarter, Pro sales were positive and outpaced the DIY customer. And those Pros engaging with elements of our pro ecosystem who also have a dedicated salesperson were our strongest performing Pros in the quarter.

Turning to total company online sales, sales leveraging our digital platforms increased 4 percent compared to the third quarter of last year and for those customers that chose to transact with us online during the third quarter, nearly half of our online orders were fulfilled through our stores. In addition, as you heard from Ted, we are focused on continuing to improve our interconnected retail experience. Whether it is our faster delivery speeds, our more relevant and personalized search results or our enhanced product review summaries powered by AI….All of which are leading to greater purchasing confidence for our customers.

During the third quarter, we hosted our annual Supplier Partnership meeting where we focused on how we will continue to work together to bring the best products to market, deliver innovative solutions that simplify the project and offer great value with best-in-class features and benefits. At the event, we recognized a number of vendors across categories who continue to transform the industry with the innovation they bring to our customers on a daily basis. This included: Starlink, Milwaukee, Ryobi, Wago, Glacier Bay, Henry Roofing and many more. We are proud of the innovation and partnership that our suppliers bring to The Home Depot, and the value we're able to offer both our Pro and DIY customers.

We also hosted our annual Labor Day and Halloween events and were pleased with the results. During our Labor Day Event, we were encouraged with the customer's engagement across a number of categories including grills which had positive comps for the quarter. And 2024 was another record sales year for our Halloween program both in-store and online as our customers continue to add to their collection with our unique and exclusive product assortment.

As we turn our attention to the fourth quarter, we plan to maintain our momentum with our annual holiday, Black Friday, and Gift Center events. In our Gift Center event we continue to lean into brands that matter most for our customers with our assortment of Milwaukee, Ryobi, Makita, DeWalt, Ridgid, Husky and more. We will have something for everyone whether it is our wide assortment of cordless Ryobi tools, Milwaukee M18 fuel tool kits, and our new Husky BITE tools. We are bringing more innovation in batteries with Ryobi Edge, DeWalt XR and the expansion of the Milwaukee Forge lineup with new 8 and 12 amp hour batteries, all designed to bring more power to our customers. And the innovative Husky BITE tool technology offers increased grip on new and rounded fasteners, better access, more torque and more leverage, making them a great addition to any toolbox at a great value. And they are exclusive to The Home Depot.

Our merchandising organization remains focused on being our customers' advocate for value. This means continuing to provide a broad assortment of best-in-class products that are in-stock and available for our customers when they need it. We will also continue to provide innovative product solutions that simplify the project, saving our customers time and money. That's why I'm so excited about the innovation we continue to bring to the market.

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

Richard McPhail - *The Home Depot, Inc. - EVP & CFO*

Thank you Billy and good morning everyone.

In the third quarter, total sales were $40.2 billion dollars, an increase of approximately 6.6% percent from last year.

During the third quarter, our total company comps were negative 1.3 percent, with comps of negative 3.3 percent in August, negative 2.3 percent in September, and positive 1.0 percent in October. Comps in the U.S. were negative 1.2 percent for the quarter, with comps of negative 3.5 percent in August, negative 2.2 percent in September, and positive 1.4 percent in October. The progression of our monthly comps reflects, in large part, hurricane related sales. Our results for the third quarter include a net contribution of approximately $200M in hurricane related sales, which positively impacted total company comps by approximately 55 basis points for the quarter and approximately 120 basis points for October.

In the third quarter, our gross margin was approximately 33.4 percent, a decrease of approximately 40 basis points from the third quarter last year, primarily driven by mix as a result of the SRS acquisition, partially offset by benefits from lower shrink.

During the third quarter, operating expense as a percent of sales increased approximately 45 basis points to 19.9 percent compared to the third quarter of 2023. Our operating expense performance was in line with our expectations.

Our operating margin for the third quarter was 13.5 percent, compared to 14.3 percent in the third quarter of 2023. In the quarter, pre-tax intangible asset amortization was $138 million dollars, including $86 million dollars related to SRS.

Excluding the intangible asset amortization in the quarter, our adjusted operating margin for the third quarter was 13.8 percent, compared to 14.5 percent in the third quarter of 2023.

Interest and other expense for the third quarter increased by $157 million dollars to $595 million dollars, due primarily to higher debt balances than a year ago.

In the third quarter, our effective tax rate was 24.4 percent, compared to 23.3 percent in the third quarter of fiscal 2023.

Our diluted earnings per share for the third quarter were $3.67, a decrease of approximately 4 percent compared to the third quarter of 2023. Excluding intangible asset amortization, our adjusted diluted earnings per share for the third quarter were $3.78, a decrease of approximately 2 percent compared to the third quarter of 2023.

During the third quarter, we opened 5 new stores bringing our total store count to 2,345. Retail selling square footage was approximately 243 million square feet.

At the end of the quarter, merchandise inventories were $23.9 billion dollars, up approximately $1.1 billion dollars compared to the third quarter of 2023, and inventory turns were 4.8 times, up from 4.3 times last year.

Turning to capital allocation…

- During the third quarter, we invested approximately $820 million dollars back into our business in the form of capital expenditures.
- And during the quarter, we paid approximately $2.2 billion dollars in dividends to our shareholders.

Computed on the average of beginning and ending long-term debt and equity for the trailing twelve months, return on invested capital was approximately 31.5 percent, down from 38.7 percent in the third quarter of fiscal 2023.

Now I will comment on our updated outlook for fiscal 2024.

As you heard from Ted, while macro uncertainty remains and continues to pressure home improvement demand, our performance in the third quarter was better than expected. Our performance reflects hurricane related sales in the third quarter, and we expect some hurricane related sales in the fourth quarter. Given the better than expected performance in the third quarter and incremental hurricane related sales, we are updating our Fiscal 2024 guidance.

- We now expect total sales growth of approximately 4% percent including SRS and the 53rd week
    - The 53rd week is projected to add approximately $2.3 billion dollars to total sales
    - SRS is expected to contribute approximately $6.4 billion dollars in incremental sales
- Comparable sales are expected to decline approximately 2.5% percent for the 52-week period
- We expect to open approximately 12 new stores
- Our Gross Margin is expected to be approximately 33.5% percent.
- We expect operating margin to be approximately 13.5% percent.
- And adjusted operating margin to be approximately 13.8% percent.
- Our effective tax rate is targeted at approximately 24% percent.
- We expect net interest expense of approximately $2.1 billion dollars.
- We expect our diluted earnings per share to decline approximately 2% percent compared to fiscal 2023, with the extra week contributing approximately $0.30 cents per share.
- And we expect our adjusted diluted earnings per share to decline approximately 1% compared to fiscal 2023, with the extra week contributing approximately $0.30 cents per share.

We believe that we will grow market share in any environment. We are continuing to invest to strengthen our competitive position with our customers, and leverage our scale and low-cost position to drive growth faster than the market and deliver shareholder value.

Thank you for your participation in today’s call, and Christine, we are now ready for questions.

QUESTION AND ANSWER

Operator

[Operator Instructions] Our first question comes from the line of Scott Ciccarelli with Truist. Please proceed with your question.

Scot Ciccarelli - *Truist, Analyst*

Good morning, everyone. [Technical Difficulty]

Isabel Janci - *The Home Depot, Inc. - VP, IR & Treasurer*

Scot, you're breaking up. Can you repeat your question, please?

Scot Ciccarelli - *Truist, Analyst*

Sorry for that. Sales were better than [Technical Difficulty] I know you guys outlined [Technical Difficulty] because obviously, it was quite [Technical Difficulty]

Isabel Janci - *The Home Depot, Inc. - VP, IR & Treasurer*

Scot, sorry to cut you off. We can't really hear you. So we're going to go to the next question, and we'll come back to you.

Operator

Our next question comes from the line of Zack Fadem with Wells Fargo. Please proceed with your question.

Zack Fadem - *Wells Fargo, Analyst*

Hey. Good morning. So, starting with the hurricane impact, Richard, you called out about 55 basis points in Q3. Any color on category impacts? And if those sales skewed more DIY versus Pro?

And then as you think about Q4, how would you characterize the implied down 2.5% comp guide between hurricane-driven and the underlying business?

Billy Bastek - *The Home Depot, Inc. – EVP, Merchandising*

Hey, Zach, it's Billy, and then I'll turn it over to Richard to answer the back half of that question. Just in terms of the hurricane piece, obviously, pretty similar to all events. Think about generators, think about cleanup – you think about obviously lumber as it relates to what we do to help our communities get ready for those events. So pretty similar from a product assortment standpoint. And obviously, all that's consumer-driven as customers ready themselves for that event.

And I'll flip it to Richard to answer the back half of that.

Richard McPhail - *The Home Depot, Inc. - EVP & CFO*

Yes. So, Zack, just talking about the guide of 2.5% for the year, our guidance really principally reflects the outperformance that we saw in Q3, driven by hurricane-related sales, as well as reflecting the fact that we just saw exceptional weather across the entire country for most of the quarter. So, the full year view is basically the flow-through of that Q3 performance with some Q4 impact of hurricane-related sales.

Zack Fadem - *Wells Fargo, Analyst*

Got it. Appreciate the color. And just taking a step back, how much of your business would you categorize as needs base versus discretionary today. And is it still fair to say that the larger and bigger ticket projects are being deferred, while needs-based brake fix type projects are getting done? And also, any color on how those two buckets have been trending through the year?

Ted Decker - *The Home Depot, Inc. - President & CEO*

Yes. Zack, that's always difficult to parse out needs based versus discretionary project. We would say your needs based projects are getting done. We've talked about there being strong engagement in home improvement and certainly with our Pros, but the larger, more discretionary projects are the ones that are being deferred, and that balance has been consistent throughout this year.

Operator

Our next question comes from the line of Chuck Grom with Gordon Haskett. Please proceed with your question.

Chuck Grom - *Gordon Haskett, Analyst*

Hey. Good morning. Thanks very much. Can you discuss SRS and the progress you've made in cross-selling products and services across the two businesses? And then can you also touch on the volume contribution specifically in the third quarter?

Ted Decker - *The Home Depot, Inc. - President & CEO*

Sure. So, we're very pleased with our progress with SRS, as I said in my prepared remarks. Job one is to support them executing their play of growing their business, which they do with what we would call comp growth through their existing branches, opening up new branches and then doing tuck-in M&A. They've continued to do that through the third quarter. They opened a number of branches. They grew the business, and they even made a couple small tuck-in acquisitions. So, the strategic game plan for SRS is proceeding as expected.

On the cross-sell opportunity, the initial things we're working on is to make their catalog available to our customers largely through the Pro desk and through our outside sales resources. And we're seeing terrific take-up on that. The comp sales of SRS product through The Home Depot ecosystem, while obviously, a very small base is accelerating an incredible sort of triple-digit comp growth with those specific sales. And then we're also beginning to quote our product into their customer base.

Now remember, their specialty trade and they're focused on roofers, landscapers, folks putting down, hardscapes and backyards and then working on repairing and maintaining pools and irrigation. However, those customers do engage in some broader home improvement activity, and we've already begun to actively quote our broader catalog into their customer base. Very, very early days, but the sales teams are working together incredibly well, getting to know each other, going on some joint customer calls together. So early days on that. But again, the strategic thesis is playing out exactly how we had hoped.

Richard McPhail - *The Home Depot, Inc. - EVP & CFO*

And Chuck, you asked for specifics. They contributed $2.9 billion in the third quarter. They're on track to deliver the expected $6.4 billion in sales contribution for the roughly 7 months that we'll own them.

Chuck Grom - *Gordon Haskett, Analyst*

Okay. Great. Thanks very much. And then one for you, Richard on gross margins, down 40 basis points. It sounds like SRS was the lion's share. Is there any way to double-click on that and just unpack? I think it was about 35 basis points of pressure last quarter?

And then just looking out, can we think about broader puts and takes for gross margins? I mean, relative to where you were pre-COVID, which was north of 34%. How do we think about the gross margin trajectory over the next few years? Thanks.

Richard McPhail - *The Home Depot, Inc. - EVP & CFO*

Sure. Well, so specifically, look, when you look year-over-year, the major impact in gross margin versus last year was simply the mix impact from SRS. And – so that was actually an 80-basis point impact for the quarter. So let's just – let's talk about gross margin.

It was in line with our expectations. In fact, our guidance for gross margin for the full year has not changed. So again, in Q3, the impact was around 80 basis points from SRS, so you can do the math and see that the remainder of the business was up significantly and was in line with our expectations. And that also reflected benefits from shrink that Ann had mentioned.

And just to remind you, SRS will be for the year 2024 – it will have about a 45-basis point impact on the year because remember, we will have only owned them for about seven months. But an annualized number, for SRS, impacted gross margin is about 70 basis points. So if you just allow me a second to make sure everyone got that, that's 70 basis points of expected shift in our gross margin profile from adding them to our business. Our gross margin, again, was right where we expected it to be.

Transportation expense or rather benefits from decreasing transportation expense were a dynamic in the first half of the year, but that's largely sort of going away as year-over-year comparisons are flat now. And so we were very pleased with our margin performance. And as I said, we have not changed our guidance for the full year gross margin. And then look, as far as long-term goes, in June of 2023, at our investor conference, we laid out a base case that in essence said, look, we anticipate flat gross margin as part of our operating model.

There's a ton of productivity that our amazing supply chain team drives every single year that we reinvest in that gross margin. But that's reflective of our position as the sharpest value in the market for our customers, and that's our intention. But again, the acquisition of SRS does present a shift in our margin base for the business.

Chuck Grom - *Gordon Haskett, Analyst*

Makes sense. Thank you.

Operator

Our next question comes from the line of Seth Sigman with Barclays. Please proceed with your question.

Seth Sigman - *Barclays, Analyst*

Hey, good morning, everyone. Nice progress in the quarter. My main question is around market share. Obviously, macro and housing matters a lot here, but you're also doing a lot to better serve your customer and all the different types of customers.

I guess in that context, it does seem like Home Depot's performance improved relative to the industry this quarter. Can you speak to that? And any specific categories you would call out where you do think you're gaining more share? Thanks.

Ted Decker - *The Home Depot, Inc. - President & CEO*

I'll hit on the broader topic and pass over to Billy. As we've always said it is tough to parse out market share. But if you look at PC expenditures in home, in furnishings, those were deeper negative as reported in government statistics than our results.

So, if you look at that broader macro, we would – the highest level macro, we would say we took share. And then we obviously look at reported results from competitors who are functioning in certain product categories that we operate in. And again, in most of those, we see our businesses outperforming those of publicly traded companies' results. And Billy, if you want to hit on some categories?

Billy Bastek - *The Home Depot, Inc. – EVP, Merchandising*

Yeah. As we said in our prepared remarks, certainly, our seasonal performance, we saw increased grade engagement across our seasonally related categories and that includes Halloween. Paint continues to be a great story for us. And while we did see some exterior business just related on the weather that we called out, we're certainly making great progress with the Pro the Paints, our partnerships with Bayer and PPG, our in-store service model enhancements, our job site delivery expansion has really helped us grow share in that segment and really pleased with the performance of the team there.

And then we talk about building materials, continue to see really strong performance in our building materials. That's multiple quarters on top of multiple quarters. So, as Ted mentioned, pretty hard to kind of parse that out. We look at a lot of different data sets, but feel very confident that in any market, we're going to continue to take share. But that's a few of the areas that we've seen great, continued acceleration and as I mentioned, in building materials specifically, ongoing terrific improvement there.

Seth Sigman - *Barclays, Analyst*

Okay. That's helpful. I guess a follow-up question would be around big ticket more specifically. It does seem like it took a step down this quarter, even in light of hurricanes, certain categories you mentioned like generators. How do you categorize that? And you mentioned interest rates, do you think there was some election noise? I mean, I guess, ultimately, we're trying to think about what needs to change in your view to really get those categories inflecting?

Ted Decker - *The Home Depot, Inc. - President & CEO*

What – maybe I'll just step back on how we look at this overall environment and what we're seeing. I mean, clearly, our sales during the quarter, as we said, were more favorable than we expected a lot with weather and hurricane-related demand. And don't forget on weather, it's not just that you're doing garden because the weather is nice. Think of limited days loss from a Pro because they can be out of the job site through virtually every day in October, it was dry throughout the country.

The issue we continue to watch are the macroeconomic uncertainties and the higher rate environment that continues to pressure larger remodeling projects. So, we look at the reversion of personal consumption from goods to services. That's largely worked its way out. And we've largely navigated our way through the pull forward of demand that we saw during the pandemic. So again, today, this higher rate environment is pressuring the larger normally debt-financed remodeling projects, as well as existing home sales.

So, we all know that the Feds cut interest rates, two cycles here. But from the cut in September, mortgage rates has actually increased about 60 basis points. So, two rate cuts of combined 75 basis points, yet the 10-year and then therefore, the mortgage rates were up about 60 basis points. That continues to impact housing turnover which were just about 3% of homes turning over, which is a 40-year low at this point. And you might say that the worst is behind us, how much lower are we going to go? Usually, we're at about 4.5%, 5% turnover. I think we actually touched on sort of 2.99%. So, one could argue we're near the low there.

But then the larger projects often require financing, whether it's cash out financing or home equity lines of credit, those are down. So, our HELOCs, those track more directly the drop in short-term rates. So, those are down 75 basis points, but still historically high at over 8%. So with that, we're encouraged with certain green shoots, if you will, in the business with the pull forward working its way through, the categories that Billy just went through.

But what we're looking for is just one is the timing of homeowners starting those larger remodeling projects. So, we remain super bullish on the outlook for home improvement. We'll have to work our way through this current macro uncertainty and the interest rates pressuring home improvement demand. But this is a market after all and markets return to equilibrium and remodeling will as well. We just don't think we're quite there yet.

Seth Sigman - *Barclays, Analyst*

Got it. Thank you so much.

Operator

Our next question comes from the line of Steve Zaccone with Citi. Please proceed with your question.

Steve Zaccone – *Citi, Analyst*

Hey. Good morning. Thanks very much for taking my question. I wanted to follow up on gross margin briefly. So, in the quarter, was there any mixed pressure on gross margin from the higher hurricane-related sales? And then just to follow up on the longer term, there's a good amount of discussion around shrink. You've made a lot of progress there. Can you help us understand how much of an opportunity that is over the medium term? Is this something that's in the 10 to 20 basis points? Or could it be something more meaningful over time?

Richard McPhail - *The Home Depot, Inc. - EVP & CFO*

Right. Yeah. So, as far as gross margin goes, for the quarter, there was a slight amount of mix pressure to margin. And just think about how Billy characterized it, at the beginning of hurricane prep and then through cleanup, you're just selling higher volumes of lower gross margin goods.

And so there was some slight pressure there. And as far as shrink goes, look, we are, frankly, just head down and the teams are working so hard every single day. They have made major investments, not just financially, but also in the amazing number of initiatives they have brought forward to combat in essence the results of organized retail theft and other crime.

This is a problem for all of retail. It's hard to quantify. What we can tell you is that our investments are paying off. They've led now to multiple quarters of benefits year-over-year. Tangible results from investments we've made. That does not mean that the operating environment is getting any easier. In fact, it's getting harder and harder. So our hats are off to our teams, and it's an everyday initiative that our teams are fighting every single day.

Steve Zaccone – *Citi, Analyst*

Yeah. Understood. My follow-up question, I know there's no 2025 guidance today. But I think as we – I'm curious like as you look at the backdrop, right, the view for 2024 was like housing was going to be net neutral. As you sit here today, it's tough to kind of call rates, but as you think about 2025, would you think the housing backdrop turns a little bit more favorable for you? Or is it still like think about housing as net neutral as kind of the base case scenario?

Ted Decker *- The Home Depot, Inc. - President & CEO*

Well, Steven, I'd repeat the comments I just made. One could argue that the rate environment is settling down in turnover, certainly even under 3% last reported period would be at a low. But just don't know and not obviously ready to talk about 2025 and not ready as we sit here today to call that this is a turn on larger remodeling projects.

Steve Zaccone – *Citi, Analyst*

Okay. Fair enough. Thank you.

Operator

Our next question comes from the line of Scot Ciccarelli with Truist. Please proceed with your question.

Scot Ciccarelli *- Truist, Analyst*

Thanks, guys. I apologize for the tech issues. Richard, I know you outlined the impact of hurricane-related sales, but is there a broader estimate for the weather impact in quarter? And then second, can you guys give us an idea of the magnitude of difference in performance in the 17 markets where you've rolled out incremental Pro capabilities versus the rest of the base, just so we can better understand the impact that those capabilities are having? Thanks.

Richard McPhail *- The Home Depot, Inc. - EVP & CFO*

So, for the first part of your question, Scot, look, we had outstanding weather across the country. So, it becomes harder to parse out what the weather impact is when you literally don't have a control group. However, we know when the sun was shining, our customers were engaged, and that's a huge testament to our merchants and our operators for inspiring them to do outdoor projects and the like. So, it's hard to parse out weather. And therefore, we're cautious with respect to extrapolating Q3 just given how favorable the weather truly was across the country. And Ann, Chip, maybe you can talk about some more.

Ann-Marie Campbell *- The Home Depot, Inc. – Senior EVP*

I'll jump in, and I'll turn it over a little to Chip, and Hector. But as we mentioned, just tremendous opportunity as we think about greatest share of wallet with the Pro – Complex Pro. And we invest in across the end-to-end experience. We have talked about previously of what we're doing with capabilities on the complex side of the business. And today, I highlighted a lot of great work that Hector and his team is doing with the in-store Pro.

And when we think about it across the entire ecosystem, we want to have a great experience outside the stores, and we want to have a great experience inside the stores. So we have to be working on these initiatives simultaneously.

To your point, the more they engage with our capabilities, we are seeing tremendous upside. And it's important for us, as we think about the 17 markets to ensure that we're delivering an excellent experience where we build the level of confidence. So Chip, I know you continue to work on some key capabilities. And if you then turn it over to Hector on some of the things he's doing in-store.

Chip Devine - *The Home Depot, Inc. – SVP, Outside Sales*

Yeah. Thanks, Ann. And Scot, we're very encouraged in what's going on in the 17 investment markets where we've been building out the ecosystem that Ann referenced. The investment in our foundational capabilities, breadth and depth of inventory, supply chain, delivery and importantly, our sales force has led to share gains and outperformance in all those markets, low single-digits in those markets. So very, very pleased.

As Billy mentioned, these customers that are interacting with our ecosystem are some of our very best performing customers. Just as an example, we've launched our trade credit offering where its early days, but it is really resonating with our customers, and we've been able to take share in some of their projects that we normally cannot participate in. So very pleased with what's happening. Hector?

Hector Padilla - *The Home Depot, Inc. – EVP, U.S. Stores and Operations*

Yeah. And Scot, I would just add that we are super pleased with the engagement of our teams in-store to drive just a great experience for that in-store Pro. Ann mentioned some of the strategic adjustments that we made going into the second half of the year to drive that engagement from our leaders.

We're laser-focused on driving speed and ease for checkout for our Pros, making sure that we are driving in-stock on large quantities of the products and customers needs, and integrating the tools and resources and features that Chip and team are developing for the outside Pro, that are also adding value to the in-store Pro experience. So we just like how the ecosystem is coming together in those markets and beyond.

Operator

Our next question comes from the line of Michael Lasser with UBS. Please proceed with your question.

Michael Lasser - *UBS, Analyst*

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Ted Decker ***- The Home Depot, Inc. - President & CEO***

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Operator

Our next question comes from the line of Michael Lasser with UBS. Please proceed with your question.

Michael Lasser ***- UBS, Analyst***

Good morning. Thank you so much for taking my question. Ted, are you looking at the multiyear home improvement outlook as the longer that rates remain elevated, the more that homeowners are deferring projects? And as soon as rates come down, that will lead to a more robust recovery. So there's a relationship between what's happening right now and the magnitude of the recovery? And I guess as part of that, if rates don't come down next year, can the home improvement industry grow in 2025?

Ted Decker ***- The Home Depot, Inc. - President & CEO***

Yes, Michael. We think about that quite a bit, as you can imagine. And certainly rates have been high. They've pressured turnover most specifically but even HELOC extraction. HELOC extraction is something like 25% right now of more recent period extractions. So clearly, rates are impacting. But I'm not sure that we've talked about when rates came down towards the 6% we immediately saw activity in housing. And we were seeing that just a matter of weeks, months ago, before this latest change when rates actually went up.

I think there's a little bit of so much discussion about where rates are going and that the certainty of that they were going down has caused people to wait for that lower rate. But if you get stability at sort of any rate might be more important at this point. So once rates settle and there's probably a gradual easing of rates, but I don't think we need a dramatic drop. We just need the talk of the big drops are coming and market equilibrium will set in.

Either that or people simply get used to the higher rates, which historically are still pretty decent rates and life cycles will continue. New household formation, increasing size of home, decreasing size of home, second homes, that normal equilibrium of housing activity will be reestablished.

We've just had such a dramatic increase in value, increase in rates followed by this expectation of a meaningful short-term drop in rates over a very short period of time that has changed that stable turnover rate that we've seen for years and years to be what now you would argue could be a low.

So I don't think, again, to answer your question, that they have to drop quickly and meaningfully. They just need to stabilize and all the talk of what the Fed is going to do sort of gets out of the national conversation.

Michael Lasser - ***UBS, Analyst***

Got you. That's very helpful. My follow-up question is, I want to get the team's perspective on tariffs. So as part of that, what percentage of sales for The Home Depot could be subject to tariffs in China? And what about from other countries?

And is the bigger risk from tariffs related to the sheer increase in merchandise cost or the indirect impact of potentially reaccelerating inflation and that impact on consumer spending? Thank you.

Ted Decker - ***The Home Depot, Inc. - President & CEO***

Sure. And I'll let Billy and John Deaton, who runs our supply chain comment on tariffs. I would say, first and foremost, whatever happens in tariffs will be an industry-wide impact. It won't discriminate against different retailers and distributors who are importing goods.

The type of product as an industry is generally sourced from the same countries. There has been some diversification of those sources, but clearly, a bit of concentration in Southeast Asia and China in particular. We source well more than half of our goods domestically and in North America, but there certainly will be an impact.

But again, given our scale, our experience going through the previous tariffs on – 25% on, I guess, it was couple of hundred billion dollars of industry import goods going back a number of years ago, I'd bet on this team's ability to work with the type of suppliers we have to work through this in a differentiated manner than others in the industry.

But Billy and John, why don't you give some input?

Billy Bastek - ***The Home Depot, Inc. – EVP, Merchandising***

Yeah, Michael, it's Billy. Thanks. As Ted mentioned, I mean, our teams have been through this before. We anticipate we'll manage through any new tariffs similarly to how we've done this in the past.

As Ted mentioned, the majority of our goods are sourced in North America. And listen, we've been focused on diversifying sourcing for several years. And we'll continue to assess that going forward. And I'll hand it to John. I mean we're focused on that. But frankly there's some other things that John and the team are also focused on.

John Deaton - *The Home Depot, Inc. – EVP, Supply Chain & Product Development*

Yeah. More near-term, we're focused on the resolution of the East Coast port situation and any implications that might have on our ability to move product through our supply chain is – as Billy and Ted said, we have a lot of experience in this area in terms of being able to manage through these types of disruptions and these types of changes in terms of trade policy. And we feel very confident with our ability to manage through whatever is to come in the future.

Operator

Our next question comes from the line of Simeon Gutman with Morgan Stanley. Please proceed with your question.

Simeon Gutman - *Morgan Stanley, Analyst*

Hi. Good morning, everyone. First, a short-term question on Q3 to Q4, you mentioned Q3 exceeded expectations, ex the hurricanes. There was weather, and you mentioned that weather helped as well.

In thinking about the movement to Q4, it looks like it's a decel on stacks, and obviously, the absolute number. So is the assumption that weather is less helpful? Or is there some conservatism or any other thing that changed into the fourth quarter?

Richard McPhail - *The Home Depot, Inc. - EVP & CFO*

Hey. Thanks, Simeon. It's Richard. Look, bottom-line, we don't expect the fundamentals of our business to decelerate. We're just being cautious about extrapolating Q3 results that saw a significant benefit from weather. And also, just as a reminder, the guide is for approximately negative 2.5% comp sales.

Simeon Gutman - *Morgan Stanley, Analyst*

Okay. Fair enough. And second, on the macro, this is trying to get a sense of how you're thinking. And I know a lot of it in this call was helpful in that regard. The weight that you're thinking about in terms of tappable equity, which we've talked about recently, versus something like housing turnover, both are impacted by rates. But could this tappable equity idea become like a lock-in effect at some point, when does that kick in? Can it kick in even with rates being higher?

Ted Decker - *The Home Depot, Inc. - President & CEO*

Yeah. The question is often posed to us, hey, with housing turnover, there's obviously more spend. And if you don't move, then you remove the place. And while we haven't – we've seen the decrease in moving, when does the repair or the remodel in place take effect. And clearly, that has been delayed and we would point to the higher rates. But even more importantly, our surveys over the prior several months, more than cost of project and higher rates, the number one issue that people were citing in our surveys were general macroeconomic and even political uncertainty.

So as those dissipate, I think you'll see people, again, with the lower rates, HELOCs are variable. So those are down 75 basis points since the cuts. And assuming we're going to get another cut here in December, huge amount of tappable equity. That's nearly doubled since the end of 2019. It went from just under $6 trillion to $11.5 trillion. I mean trillion with a T, so tremendous amount of tappable equity.

Recall back in the housing boom, I think folks were taking out as much as $120 billion a quarter. That was more recently $60 billion, $80 billion a quarter, and now we're down to $20 billion a quarter. So I don't think it goes much lower. When people get some confidence back in macro and political dynamic, it's a big project. And for someone to make that decision to pull the trigger on the $25,000, $50,000, $75,000 project, there's a certain amount of confidence that goes into that. And one would hope that we're headed toward a change in overall confidence levels.

Isabel Janci - *The Home Depot, Inc. - VP, IR & Treasurer*

And Christine, we have time for one more question.

Operator

Thank you. Our final question comes from the line of Steven Forbes with Guggenheim. Please proceed with your question.

Steven Forbes - *Guggenheim, Analyst*

Good morning. Ted, I appreciate the color around cross-selling opportunities at SRS. But I wanted to explore maybe sort of the learnings you're gaining from monitoring the sales force over there. So can you remind us on how large the sales force is today at SRS and what you're tracking to maybe inform your decision on how you're thinking about scaling the sales force at HD?

Ted Decker - *The Home Depot, Inc. - President & CEO*

Right. So, their outside sales force is about 2,500 people. They also have inside sales force capabilities and account managers. It's observing what they do and how they do it, has given us confidence in what our approach is in terms of variable compensation, in terms of management structure and how we go to market. So clearly, we're in the hundreds of outside sales folks. They are multiples of that and the way they're compensated, managed, the tools they use to go-to-market. All that is reinforcing what we're doing.

Chip mentioned the credit. Credit is a huge unlock for these larger projects and almost all their sales are on open account, house account. And as we've introduced, and again, it's just hundreds of customers at this time, we're seeing much, much larger purchases, the type of purchase that you just wouldn't get from putting it on a credit card at a Pro desk at a Home Depot store. So yeah, great learnings. Chip and his team are in contact regularly with the SRS sales team and just going really, really well.

Steven Forbes - *Guggenheim, Analyst*

And then maybe just a quick follow-up on that. Can you maybe just update us on the current timeline or thinking behind the full rollout of bill upon delivery capabilities within the order management system?

Chip Devine - *The Home Depot, Inc. – SVP, Outside Sales*

Yeah. Hi, Steve, it's Chip. We plan to roll out order management by the end of 2025. There's elements of order management that are being turned on as we speak, including inventory reservation, which is a key win for us as Pros manage larger projects to be able to reserve that inventory for future delivery is a big win. So we'll light that up through the course of 2025 with completion at the end of the year.

Steven Forbes - *Guggenheim, Analyst*

Thank you.

Operator

Thank you. Ms. Janci, I'd like to turn the floor back over to you for closing comments.

Isabel Janci - *The Home Depot, Inc. - VP, IR & Treasurer*

Thanks, Christine. Thank you all for joining us today. We look forward to speaking with you on our fourth quarter earnings call in February.

Operator

Ladies and gentlemen, this does conclude today's teleconference. You may disconnect your lines at this time. Thank you for your participation, and have a wonderful day.