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Home Depot dives as Lowe's thrives

Steady management a key to Mooresville firm's success

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When Home Depot Inc.'s former chief executive, Robert Nardelli, resigned earlier this month, industry insiders rushed to question all that had gone wrong at the nation's No. 1 home improvement retailer.

Among them: Management blunders, shaky customer service and a plummeting stock price.

Meanwhile, Mooresville-based Lowe's Companies Inc., Home Depot's fiercest competitor, has found itself the sudden recipient of Wall Street's accolades.

Analysts point out that Lowe's stock price has soared 185 percent in the last five years, compared to a 7 percent drop at Home Depot, even though profits doubled at both companies during that time.

And while Home Depot is still about twice as big as Lowe's in terms of revenues, Lowe's is continuing to gain ground on its competitor by expanding into international markets. Last week, Lowe's announced it will expand into Mexico, where Home Depot already owns stores.

At home, studies show Lowe's customer service ratings are at record levels, Home Depot's have tanked to their worst in years.

"The issues with Home Depot just got highlighted, and when you look at them under broad daylight, you realize, 'Wow, Lowe's has a pretty tight ship,'" said Joe Feldman, senior research analyst for New York-based Telsey Advisory Group, which holds no shares with either retailer.

How did Lowe's put itself ahead of the competition in the eyes of investors?

Some retail experts say it's the result of stable management and a steady focus on goals that matter most to customers. Others, however, say the rivalry between the two companies is exaggerated, and that such comparisons are unfair.

Officials at both companies even try to avoid discussing each other directly or using each other's name in company filings and conversations with reporters. Instead, they opt to refer to each other generally as "our competitors" or "biggest competitor."

"There's room for both companies to exist and be healthy," said Stephanie Hoff, a senior analyst with Edward Jones, which holds no shares with either retailer. "One doesn't always have to assume that one company's success is the result of the other doing poorly."

Lowe's wasn't always so warmly regarded.

In the early 1990s, investors were high on Home Depot, which had rapidly expanded across the country with its large, warehouse-style stores pushing "do it yourself" home improvements. Meanwhile, Lowe's had relatively small stores that still focused on hardware.

Many experts agree that the biggest initial key to Lowe's success was being the first to capitalize on a critical potential customer: women, who were rapidly becoming the primary home improvement decision-makers in their families.

Lowe's built stores close to Home Depot locations (70 percent of Lowe's stores are within a 10 mile radius of them) but

more comfortable to shop in. Lighting was brighter, aisles were wider and displays made it easier for customers to visualize how the merchandise would look in their homes.

More importantly, analysts say, Lowe's continued to reinvest in the look and feel of its stores as profits grew. While many retailers typically remodel stores every five to six years, Lowe's was revamping more regularly, Feldman said.

"Home Depot would make a big deal about how much they were reinvesting in the store base during a given year, but Lowe's does it all the time -- it's standard business practice," Feldman said.

That type of investment also likely propped up Lowe's stock price, said Sherry Jarrell, assistant professor of finance and economics at Wake Forest University's Babcock Graduate School of Management.

"Even if earnings are going up, those earnings mean nothing if it's just sitting in a corner," Jarrell said. "It's what you do with that money that matters."

Net income at Lowe's has been increasing at an average rate of about 28 percent a year, compared to about 18 percent at Home Depot. Between 2001 and 2006, that has meant Lowe's has seen a total profit increase of about 241 percent to \$2.8 billion. Home Depot's profits increased 126 percent to \$5.8 billion.

Then there's customer service.

According to a University of Michigan survey, shoppers rated Home Depot and Lowe's equally in 2001, when both were above the industry average.

Since then, Lowe's has consistently ranked above average and has been improving. Home Depot, however, has seen its ratings fall below average, hitting an all-time low in 2005.

Lowe's has also sustained a healthy number of full-time positions, a factor that some experts think boosts customer service levels. About 75 percent of Lowe's workers are full time, compared to about 68 percent at Home Depot, a decrease from 74 percent in 2001.

"You just can't do that and survive," Jarrell said.

Wachovia senior analyst Peter Benedict and Bank of America analyst David Strasser said in recent research notes that during recent meetings, Home Depot managers said their key priorities this year include improving store appearance and freeing employees up to interact with customers more.

For their part, Lowe's officials are steering clear of the debate. The company declined to comment on analyst speculation about the company's success. Company spokeswoman Karen Cobb said Lowe's has just continued to try to focus on what customers want.

CEO Pay

Analysts say shareholders have been relatively happy with the pay Lowe's Chief Executive Robert Niblock receives compared to that of former Home Depot Chief Executive Robert Nardelli. Home Depot shareholders grumbled that the company's shares tumbled during Nardelli's reign, and that his compensation should have been more closely tied to company performance.

According to Home Depot's most recent proxy filing, Nardelli's 2005 pay totaled \$31.7 million plus stock options that compensation firm Equilar valued at \$10.6 million, using a standardized calculation. Niblock's package was worth \$9.6 million plus stock options Equilar valued at \$1.7 million. now a Wall street darling

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