LOWE'S SECURITY ANALYSIS

TERRY ASANTE

THE OUTLINE

1. Theme
2. Business Analysis
3. Financial Analysis
4. Stock Valuation
5. The moat
6. Risk
7. Bulls vs. . Bears
8. Investing Strategies

THE THEME

- Lowe’s the nation world’s second largest home Improvement retailer and fortune 50 company
- Creates value by identifying and providing home improvement solutions to the customers
- Objective is to break down the complex home improvement process
- Lowe’s commitment to Everyday low prices
- A typical Lowe's stores stocks approximately 40,000 items

THEME

- U.S employment remaining persistently high at 9%, Lowe’s will put pressure on Lowes bottom numbers and margins.
- Home Depot Continues to dominate the Home Improvement market with $70 billion annually in sales
- U.S home improvement housing market decreased approximately 11% in 2009

BUSINESS ANALYSIS

- Orchestrated in 1952 in North Carolina Lowe is committed to being full service home improvement retailer who's objective is to be the first choice for home improvement
- By providing a wide assortment of products ranging from home decorating , maintenance, repair, remodeling, and property maintenance in addition to knowledgably employees Lowes is able to simplify the complex process of home improvement

- Lowes objective is to offer competitive prices and help the customer accomplish their home improvement projects.

BUSINESS ANALYSIS

- Management structure
- **Robert A. Niblock**
  Chairman, President and Chief Executive Officer
- **Robert F. Hull, Jr.**
  Executive Vice President and Chief Financial Officer
- **Michael K. Brown**
  Executive Vice President and Chief Information Officer
- **Robert J. Gfeller, Jr.**
  Executive Vice President of Merchandising

BUSINESS: PROFILE OF THE COMPANY

Customers

- Homeowners
- Renters
- Commercial Business owners
- Do it Yourself
- Do it for Me

Products

- Appliances
- Lumber
- Paint
- Millwork
- Building materials
- Lawn& Landscape
- Flooring
- Seasonal living
- Home organization
- Outdoor power equipment

MACROECONOMIC AND INDUSTRY ANALYSIS

MACROECONOMIC FACTORS

- 3 major macroeconomic factors affecting Lowe's

1. Unemployment
2. Real disposable income
3. Home ownership levels

UNEMPLOYMENT AND REAL DISPOSABLE.

"Real disposable personal income growth is forecasted to be 2.6% for calendar 2011, compared with 1.45 for calendar 2010, based on data from March 2011 Blue chip Economic indicators'"

HOME OWNERSHIP AND HOME PRICES

PHOTO: SCOTT OLSON/GETTY IMAGES

- On August CNN money stated that Home ownership hits lowest level since 1965
- “Homeowner ship is important to our business because it established customer base for home maintenance and repair projects” (2010 Annual Report)
- the Census Bureau reported that the percentage of people who owned a home had dropped to 65.9% during the second quarter in 2011 -- its lowest level since the first quarter of 1998

HOME VALUES

According to Fiserv (FISV), a financial analytics company, home values are expected to fall another 3.6% by next June, pushing them to a new low of 35% below the peak reached in early 2006 and marking a triple dip in prices.

Ceo Robert Niblock told Reuters in a telephone interview

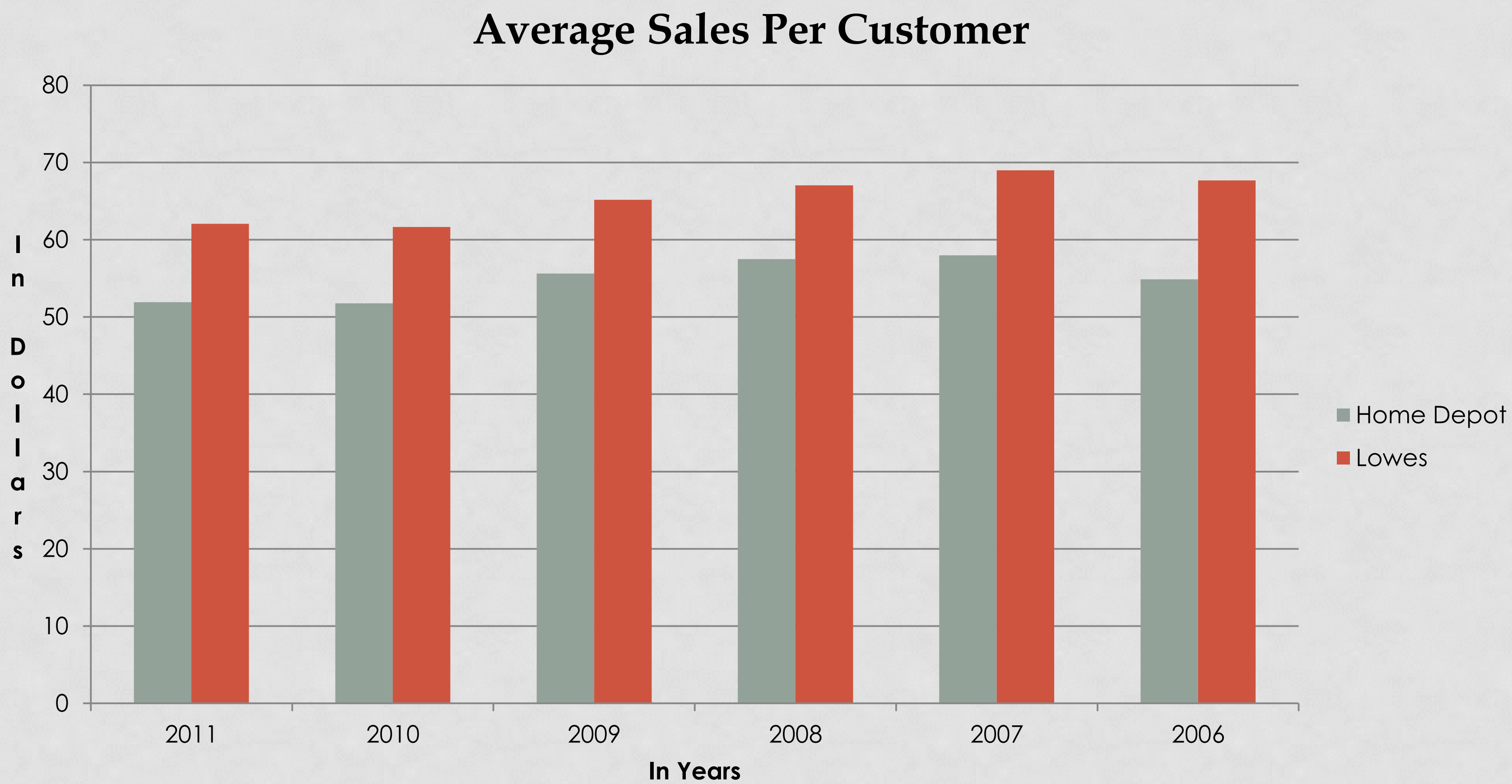
- Demand for expensive renovations is still weak
- Home prices need to appreciate to see consumers purchasing big ticket items
- U.S. consumers still have a fragile mindset due to high unemployment and economic uncertainty.

INDUSTRY ANALYSIS

#1 Home improvement retailer in the world

 # 2 Home improvement retailer in the world

	Home Depot	Lowes
Markets	Asia, North America, Mexico, Canada	North America , Mexico, Canada
# of Stores operated	2246	1729
# Of Customers in 2011	1,306,000,000	786,000,000
Brand Equity	**Powerful**	Strong
Return on Equity in 2011	17.439%	10.812
Return on Invested capital 2011	11.10%	9.1271%
Current P/E ratio	16.4	15.3
Economic value added	**707.87**	**-143.87**



- This is the **cost** to the customer but a **benefi**t to the firm
- Home Depot Generates greater consumer surplus by achieving a lower cost
- This could drastically hurt their Lowe's existing client base as consumer switch over lower cost firm and from benefit from savings

Years	2011	2010	2009	2008	2007	2006
Home Depot	51.93	51.76	55.61	57.48	57.98	54.89
Lowes Companies	62.07	61.66	65.15	67.05	68.98	67.67

ANALYSIS OF THE COMPANY AND ITS MAJOR PRODUCT LINES

- **Lowe's creates value by providing more services at a lower cost than smaller competitors**
- Approximately 4000 products to choose from to meet the needs of any customer
- One stop shop for the Customer home-improvement solutions which saves on time and money
- On site specialist to help customers to simply the complex process of home improvement
- Sacrificing low profit to build customer traffic and loyalty to drive sales

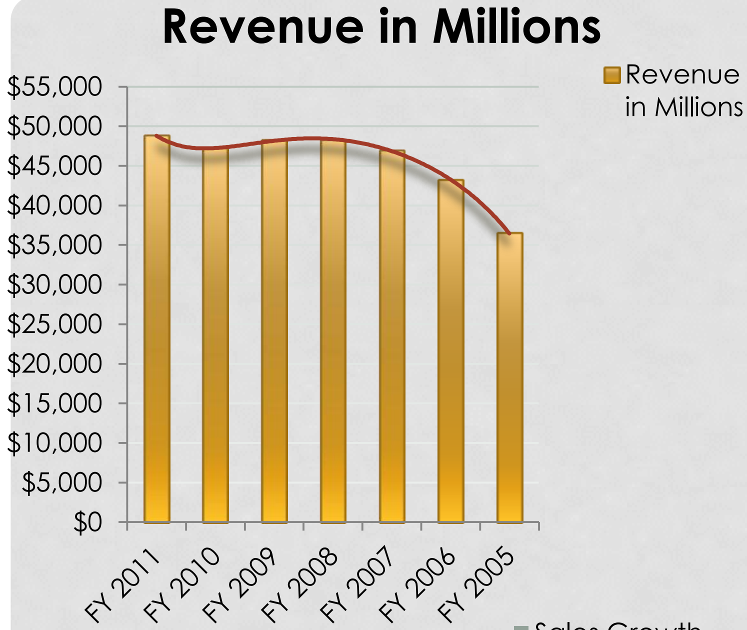
ANALYSIS OF THE COMPANY AND PRODUCTS CONTINUED

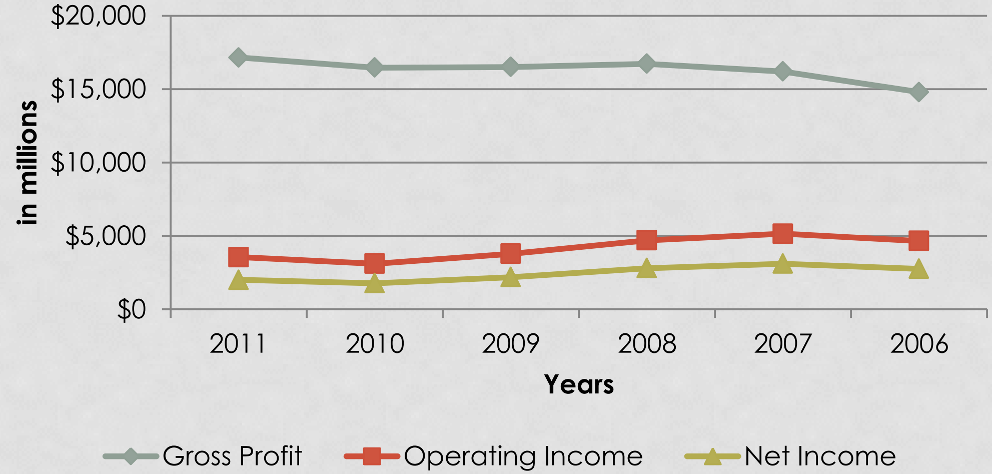
Brand Name Merchandise	Private Brands
• Samsung • Dewalt power tools • John Deere • Whirlpool appliances	• Kolbalt tools • allen+roth home décor products • Aqua source faucets and sinks

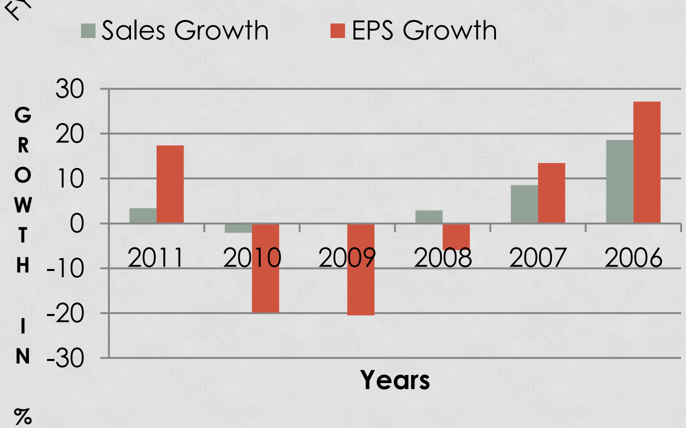
Financial Analysis

- The Analysis of Profitability and ROIC
- The Analysis of Credit risk
- Efficiency ratios

Lowes Companies



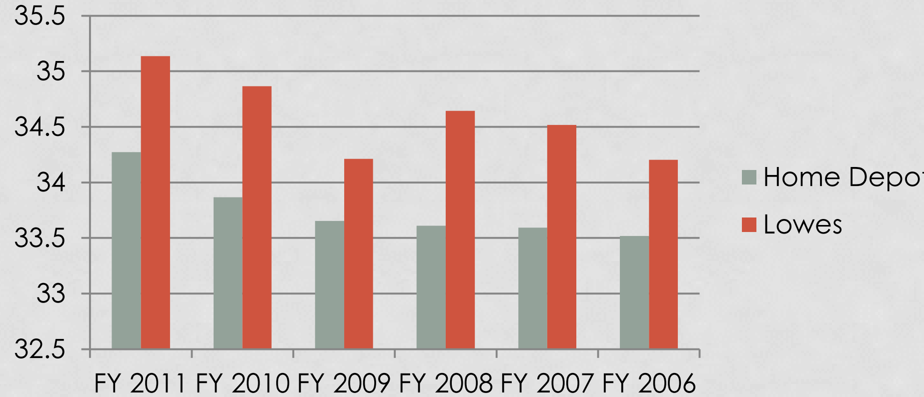




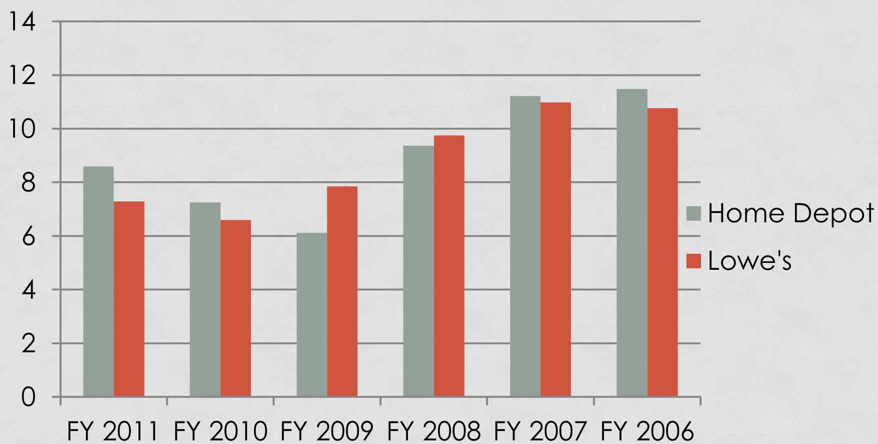
Years	**2011**	**2010**	**2009**	**2008**	**2007**	**2006**
Revenue	48815	47220	48230	48283	46927	43243
Gross Profit	17152	16463	16501	16727	16198	14790
Operating Income	3560	3112	3786	4705	5152	4654
Net Income	2010	1783	2195	2809	3105	2765
Sales Growth	3.3778	-2.0941	-0.1098	2.8896	8.5193	18.5909
Basic EPS Before XO Growth	17.3554	-19.8675	-20.5263	-5.9406	13.4831	27.1429

Profit Margin

Gross Margin



Operating Margin

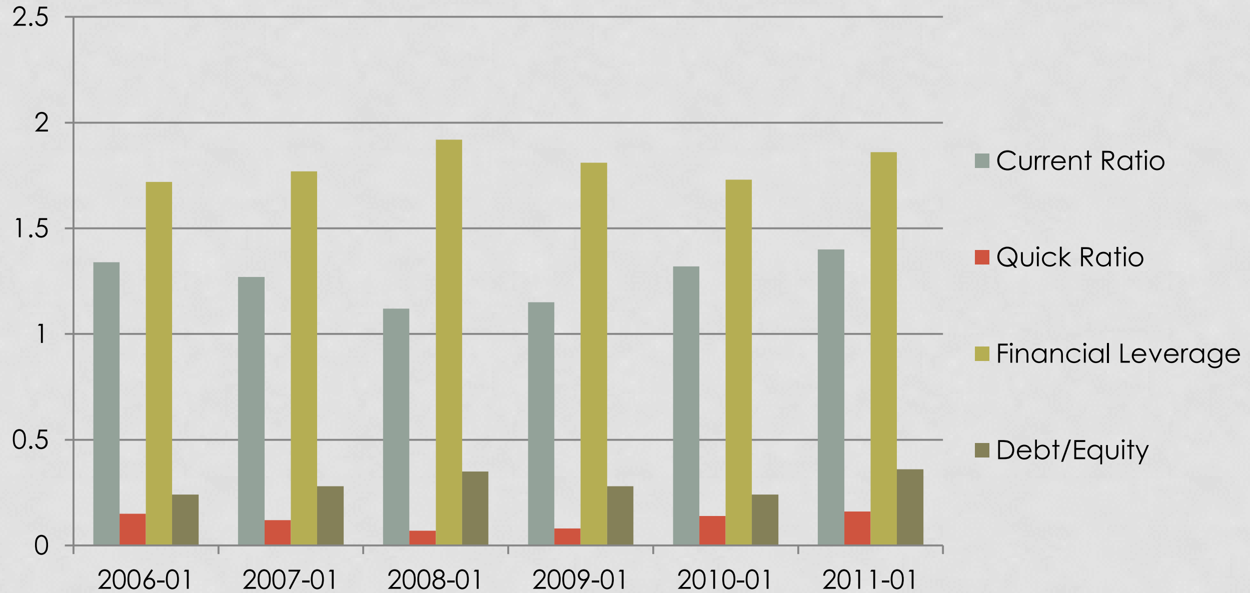


Return On Common Equity

Years	2011	2010	2009	2008	2007	2006
Gross Margin	35.1367	34.8645	34.2131	34.6437	34.5174	34.2021
Operating Margin	7.2928	6.5904	7.8499	9.7446	10.9788	10.7624
Profit Margin	4.1176	3.7759	4.5511	5.8178	6.6167	6.3941
Return On Common Equity	10.812	9.6056	12.8539	17.6539	20.6855	21.4084

The rate of return on invested capital (ROIC) is the single most important value driver. A company creates value for its shareholders only when it earns rates of return on new invested capital that exceed its cost of capital. Return on invested capital and the proportion of its profits that the company invests for growth drive free cash flow, which in turn drives value – Valuation Measuring and Managing the Value of Companies Mckinsey and Company Inc.

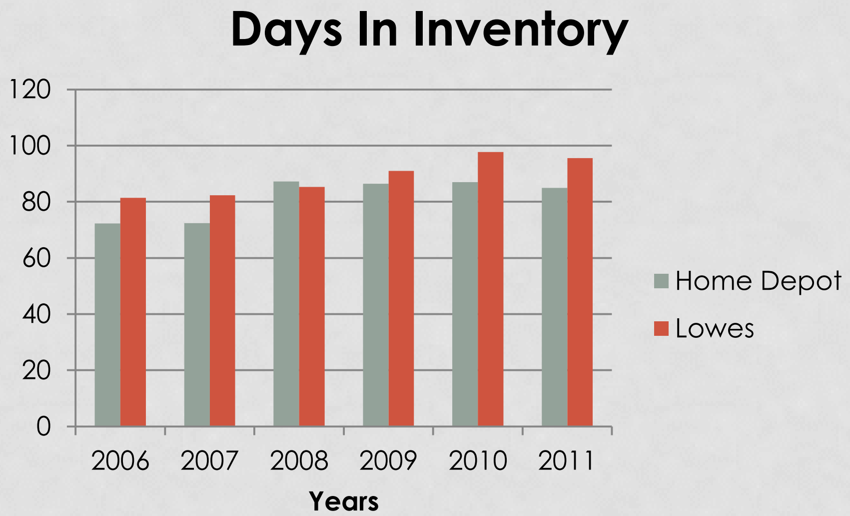
The Analysis of Credit risk

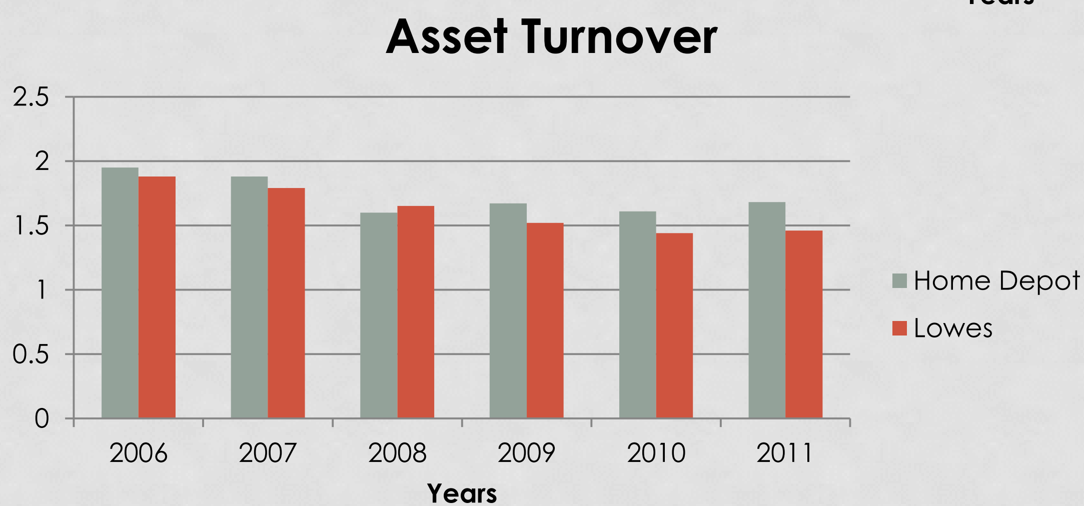


Liquidity/Financial Health	2006-01	2007-01	2008-01	2009-01	2010-01	2011-01
Current Ratio	1.34	1.27	1.12	1.15	1.32	1.4
Quick Ratio	0.15	0.12	0.07	0.08	0.14	0.16
Financial Leverage	1.72	1.77	1.92	1.81	1.73	1.86
Debt/Equity	0.24	0.28	0.35	0.28	0.24	0.36

Year	2011	2010	2009	2008	2007	2006
Total Current Assets	9967	9732	9190	8686	8314	7788
Total Long-Term Assets	23732	23273	23435	22183	19453	16851
Total Current Liabilities	7119	7355	7560	7751	6539	5832
Total Long-Term Liabilities	8468	6581	7010	7020	5503	4511
Total Equity	18112	19069	18055	16098	15725	14296

Efficiency Ratios





Efficiency	2006-01	2007-01	2008-01	2009-01	2010-01
Days Inventory	81.41	82.26	85.33	90.99	97.66
Inventory Turnover	4.48	4.44	4.28	4.01	3.74
Asset Turnover	1.88	1.79	1.65	1.52	1.44

Current Stock Price	23.76
Shares outstanding (bil)	1.26
Next Year's Cash Flow (mil)	
Perpetuity growth grate (g)	3.00%
Discount Rate (Wacc)	8.49%

10-year Valuation Model for Lowe Companies

Step 1: Forecast Free Cash (FCF) For the Next 10 years

Assume constant 4% growth rate in free cash flow, free cash flows in $ millions

YEAR	1	2	3	4	5	6	7	8	9	1
Free cash Flow	2886	3001.44	3121.4976	3246.3575	3376.2118	3511.2603	3686.8233	3834.2962	3987.6681	4147.174

Step 2 : Discount these free cash Flows to Reflect the present Value

Discount Factor= (1+R)n where (WACC= discount rate and N=year being discounted)

Free Cash Flow	2886	3001.44	3121.4976	3246.3575	3376.2118	3511.2603	3686.8233	3834.2962	3987.6681	4147.174
÷ Discount Factor		1.0849^2	1.0849 ^3	1.0849^4	1.0849^5	1.0849^6	1.0849^7	1.0849^8	1.0849^9	1.0849^1
Equal Discounted FCF		($2,550.06)	($2,444.52)	($2,343.35)	($2,246.37)	($2,153.40)	($2,084.13)	($1,997.87)	($1,915.19)	($1,835.9

Step 3 : Calculate the Perpetuity value and discount it to the present

Perpetuity value = Yr 10 FCF x (1+g) ÷ (R-g) (where g = perpetuity growth rate and R= WACC)

Perpetuity value→ $4271.59 x 1.03 ÷ (.0849-.03)=77806.74

Step 4: Calculate total equity value

Add the discounted perpetuity value to the sum of the 10 discounted cash flows

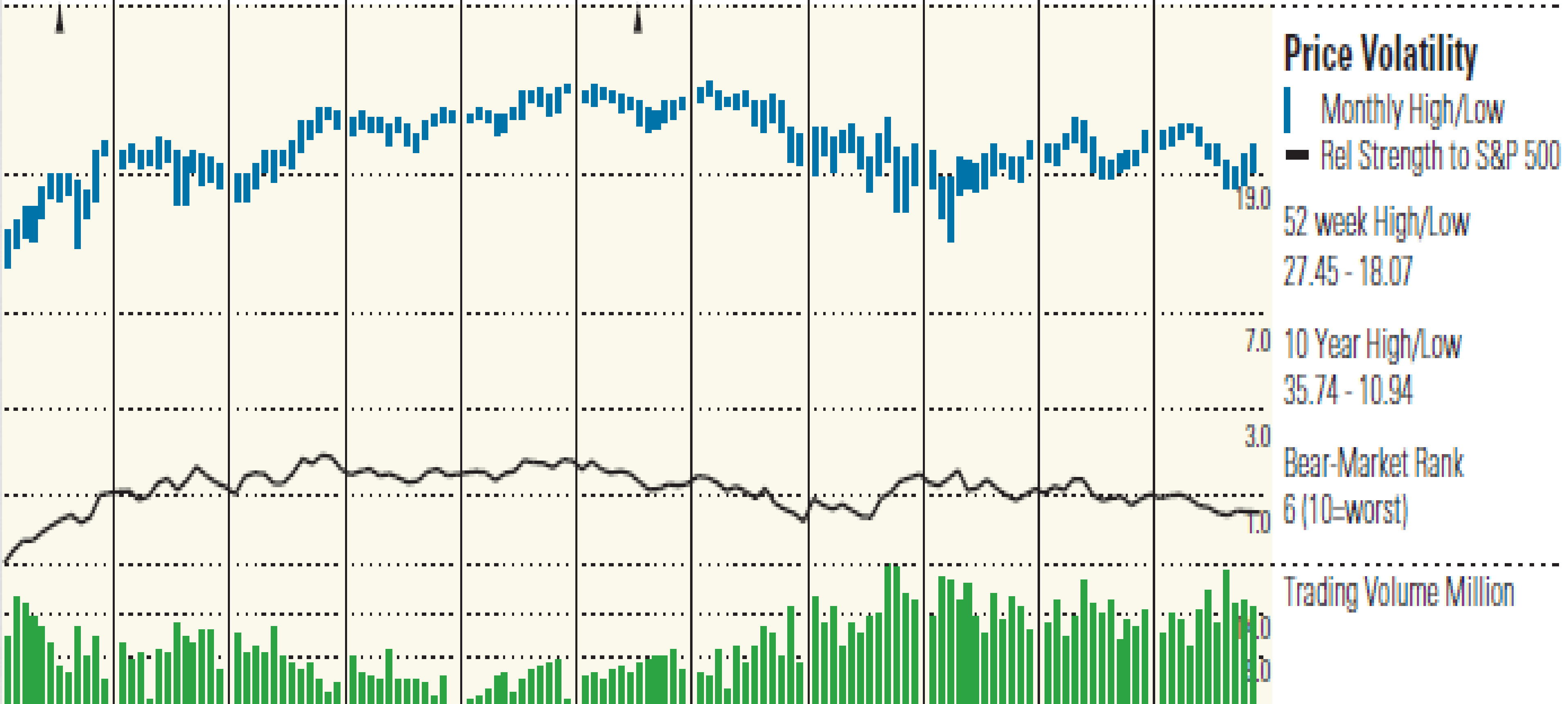
Total Equity value → $34444 + $17734 = 52178

Step 5: Caluclate per Share value

Divide total equity value by shares outstanding

Intrinsic value Per share → $52178÷ $1260 = 41.39

24.44	25.00	30.21	30.27	34.85	34.83	35.74	28.49	24.50	28.54	27.45	Annual Price High
10.94	16.25	16.76	22.95	25.36	26.15	21.01	15.76	13.00	19.35	18.07	Low
2:1					2:1						Recent Splits



2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	YTD	**Stock Performance**
108.9	-19.0	48.0	4.2	16.1	-6.1	-26.6	-3.4	10.3	8.9	-7.6	Total Return %
121.9	4.4	21.6	-4.8	13.1	-19.7	-30.1	35.1	-13.1	-3.9	0.3	+/- Market
83.4	25.9	-1.0	-11.2	13.7	-4.3	2.9	4.8	-11.9	-9.2	-8.1	+/- Industry

THE MOAT

- Strong brand product portfolio
- Able to meet diverse needs of many customers
- Cost advantage over mom and pop home improvement stores
- Size

RISK

- Dismal consumer spending
- Sustained high rates of unemployment
- Declining home sales
- Slower rate of growth in real disposable personal income consumer
- Slower Home Renovations(Higher Revenue activities)
- Price cuts due to the competitive nature for retail and the economy(even lower decreased margins)
- Home Depot will continue to be benefit due to its massive client base and economies of scale.

BULLS AND BEARS

Bulls

- The second largest home improvement store
- Size and efficiency allows them to keep cost a low price which passes on savings to the end consumer
- Once the economy picks up, the demand for home improvement will increase due to increase in disposable income
- 4000 products available at a typical which saves time and cost for the consumer

Bears

- Home depot is the Number 1 home improvement stores with annual revenues of 70 billion
- Prolong unemployment rates will hurt eat into Lowes gross margin as they will have to lower their prices to spur demand
- Internal cash flow will grow at a slow rate due to less borrowing for home ownership and major home improvements
- Weak consumer spending, inability of customers to tap home-equity lines of credit

INVESTING STRATEGY

- Bought it at $23.69
- Hold until march and liquidate 100 shares of Lowe’s
- Invest in company's who have the ability to produce sustainable economic profits with barriers of entry and monopoly characteristics in the future.

NOTES

- During 2009 Lowe’s Entered into a joint venture agreement with Australian retailer, To develop a chain of home improvement stores.
- In 2010 opened 8 Canadian stores and their first two stores in Mexico
- One-third of their anticipated store growth over the next five years will be in Canada and Mexico
- October 17, 2011 - Lowe’s Companies, Inc. (NYSE:LOW) announced today the company is closing 20 underperforming stores in 15 states

REFERENCES

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