Calgary Portfolio Management Trust

Lowe's Companies

Consumer Discretionary
NYSE: LOW
Market Outperform | Buy

LOWE'S

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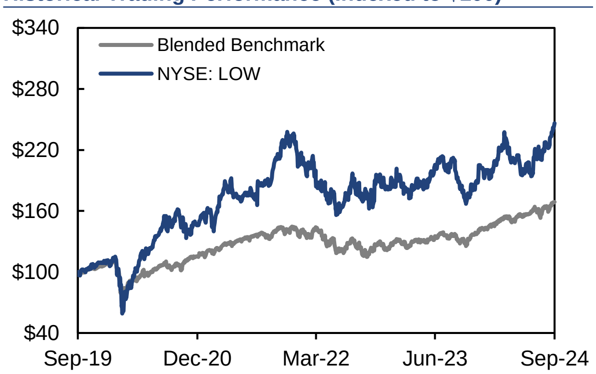
Return on Investment	
Current Share Price	$270.85
Target Price	$293.00
Dividend Yield	1.46%
Implied Return	10%
Conviction Rating	1

Market Profile	
52-Week Range	$181.85 - $270.85
Market Capitalization (US$B)	$152
Net Debt (US$B)	$36
Enterprise Value (US$B)	$188
Beta (5-Year Monthly)	1.06

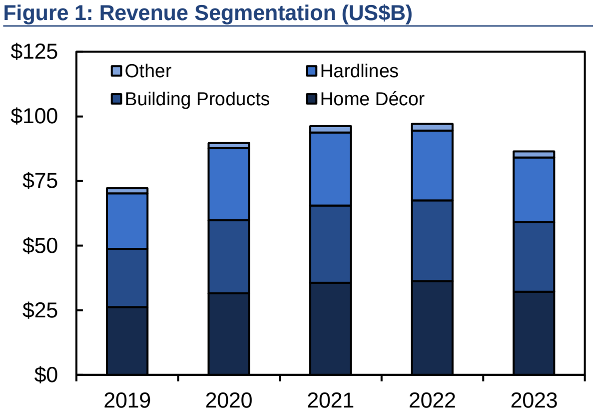
Metrics	2023A	2024E	2025E
Revenue (US$B)	$86.37	$91.23	$96.10
EBITDA (US$B)	$12.40	$13.27	$13.99
EPS (US$)	$13.20	$14.22	$15.66
EV/EBITDA	15.2x	14.2x	13.5x

Historical Trading Performance (Indexed to $100)



Source: S&P Capital IQ

Figure 1: Revenue Segmentation (US$B)



Source: Company Filings

Business Description

Lowe's Companies (NYSE: LOW) is the second largest home improvement retailer globally, operating 1,746 stores and outlets in the U.S. The Company offers a wide range of products for repair, remodel, home décor, and property maintenance. LOW operates through three main segments: (1) Home Décor, (2) Building Products, and (3) Hardlines. The Home Décor segment accounts for 37% of revenues and features a variety of products, including appliances, décor items, flooring, kitchen and bath essentials, and paint. The Building Products segment makes up 31% of revenues and encompasses a wide selection of materials, including building supplies, electrical components, lumber, millwork, and rough plumbing. The Hardlines segment represents 29% of revenues and includes hardware, lawn and garden products, seasonal and outdoor living items, and tools. LOW also provides installation services through independent contractors, as well as extended protection plans and repair services.

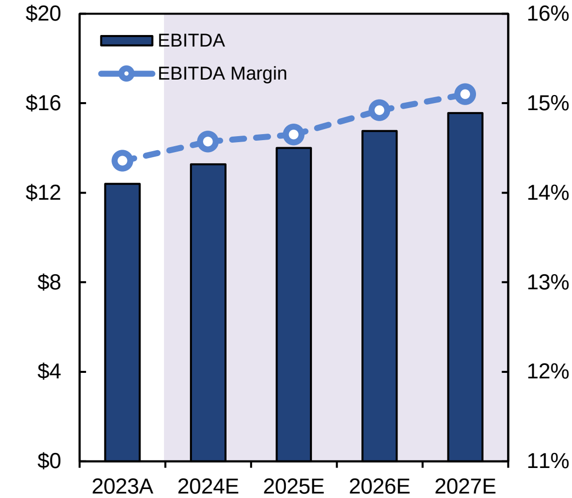
LOW sells its home improvement products through three channels: (1) In-Store, (2) Online, and (3) On-Site. The In-Store channel represents ~195mm square feet of retail space, with each location offering similar products and services. The Online channel offers buying guides and how-to videos designed to empower customers to undertake home improvement projects. Lastly, the On-Site channel features specialists available for retail and professional customers (Pro customers) in selecting the right products and services for their projects. LOW's Pro sales managers meet with Pro customers at their place of business or on their job sites to ensure the highest quality of service.

Industry Overview

The U.S. home improvement industry is highly fragmented. LOW holds the second largest market share at 12%, behind The Home Depot (NYSE: HD), which leads at 17%. These companies compete on product offerings, market focus, pricing strategies, and store locations. The home improvement industry serves a diverse range of customers, including Pro customers, individual homeowners, and renters. Pro customers encompass three primary categories: (1) tradespeople, (2) repaid and remodelers, and (3) property managers. These customers complete a variety of projects, including do-it-yourself (DIY) and do-it-for-me (DIFM). DIY projects require staff who can provide advice on minor project execution details, whereas DIFM projects prioritize personalized services and expert specialist assistance. DIY projects are more price sensitive, while DIFM projects demand professional quality. LOW's focus is on DIY customers, and accounts for ~75% of the Company's revenue. Additionally, LOW faces competition from online retailers such as AMZN, where pricing strategies are more competitive because of the convenience of direct price comparisons.

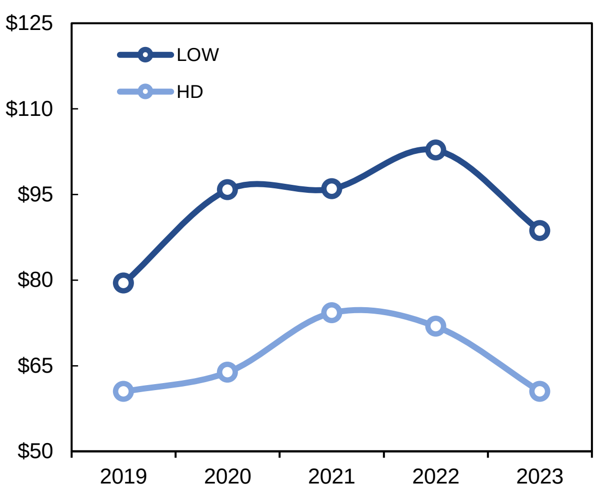
The home improvement industry is strategically positioned to capitalize on a surge in consumer spending on maintenance and remodeling, driven by the aging housing stock. Currently, U.S. housing stock has a median age of 42 years, with 13% of remodeling spending for homes aged between 35 and 44. Additionally, home-improvement retailers are positioned to benefit from a 5% (cont.)

Figure 2: LHS EBITDA (US$B) vs RHS EBITDA Margin



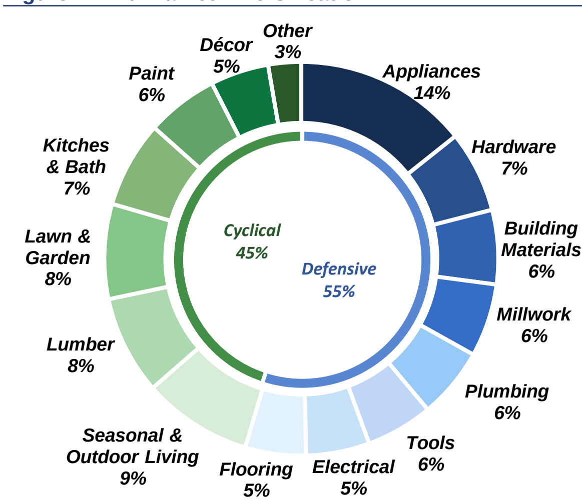
Source: Company Filings

Figure 3: NOI per Retail Square Foot vs HD (US$)



Source: S&P Capital IQ

Figure 4: End Market Diversification



Source: Company Filings

YoY increase in real disposable income. With Fed rate cuts underway, home-related names should soon see a fundamental recovery with 30-year fixed mortgage rates approaching the 6% threshold for the first time in 30 months. The industry is expected to benefit from a record of US$32.5T home equity, which may support a recovery in big-ticket remodeling early into 2025.

Mandate Fit

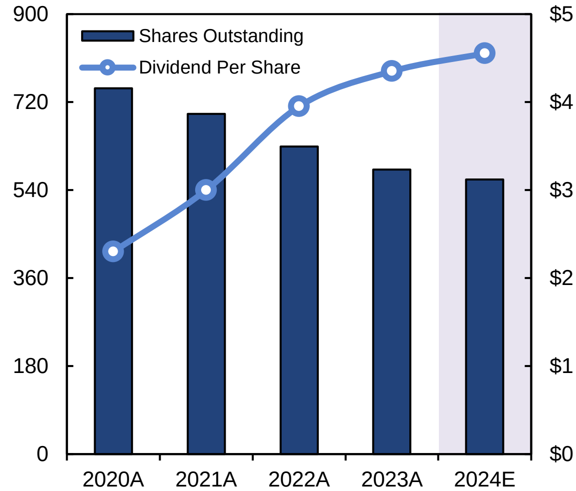
Quality Management: LOW is led by its Chairman and CEO, Marvin Ellison. Ellison has more than 35 years of retail leadership and operational experience, most recently serving as CEO of J.C. Penny Co. Since joining the Company in 2018, Ellison increased LOW's ROIC from 19% to 30%, and its operating margin from 9% to 13%. This improvement has been driven by Ellison's divestment from Canada and Mexico, increasing focus on the U.S. business. He also emphasized improving customer service through Pro sales managers, installed services, and introduction of omnichannel retailing. The Company's CEO compensation consists of 77% long-term incentives, 8% base salary, and a 15% annual target incentive. NEO compensation consists of, 68% long-term, 16% base salary, and a 16% annual target incentive.

Competitive Advantage: LOW's competitive advantage stems from its strong DIY and DIFM market positioning, operational strategies, and customer-focused initiatives. The Company benefits from its economies of scale, which provides significant pricing power for bulk material purchases and streamlined supply chain operations across the U.S. LOW serves as a one-stop-shop for DIY homeowners and professional contractors, which allows for cross-selling opportunities with its diverse assortment of products. The Company has also invested in enhancing customer experience, providing omnichannel capabilities such as same-day delivery partnerships. LOW's higher mix of DIY customers in comparison to HD makes the Company more responsive to housing turnover improvements and early-stage recovery for home projects. LOW's strategic focus on its Pro customer base has driven substantial growth, with the segment now accounting for ~25% of sales. Customers with ongoing business activities who rely on the Company's products benefit from competitive bulk pricing and improved job-site delivery, which helps establish strong brand loyalty. These factors enable LOW to maintain a competitive edge in the home improvement sector. The Company also owns and operates more than 120 supply chain facilities in its network. This allows LOW to efficiently serve its stores and meet customer expectations for fast fulfillment and delivery. In contrast, HD leases 97% of its warehouses and distribution centers, leading to higher fixed costs.

Strong Balance Sheet: LOW has a Net Debt/EBITDA ratio of 2.7x, slightly above HD at 2.4x. HD's slightly lower ratio is attributed to its maturity in the market, which limits growth opportunities and results in a more conservative approach to leveraging debt. The Company also holds credit ratings of Baa1 and BBB+ from Moody's and S&P, respectively. LOW has US$4.0B in available credit capacity and is currently undrawn with a weighted average interest rate of 4.8%. Additionally, the Company has no imminent debt maturities, with ~45% of long-term debt due post-2034, and has US$4.6B in cash to cover short-term liquidity needs.

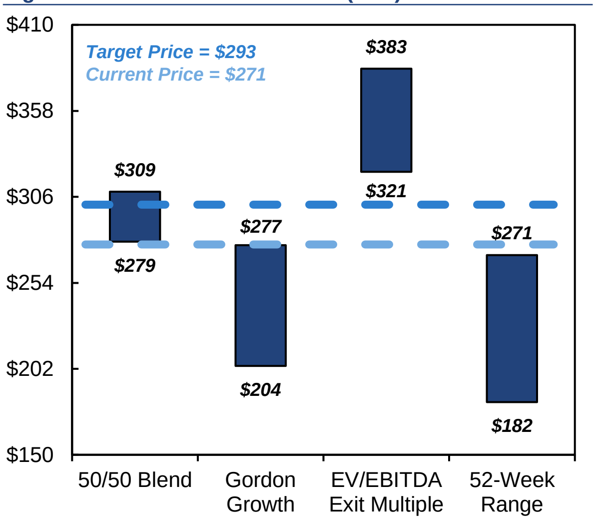
Growing Free Cash Flow: LOW has a five-year FCF CAGR of 9.2%, and in 2023, the Company generated US$5.7B in FCF. LOW has paid a cash dividend every quarter since going public in 1961. The Company has also increased its dividend for over (cont.)

Figure 5: LHS Shares Outstanding (mm) vs RHS DPS (US$)



Source: S&P Capital IQ, CPMT Estimates

Figure 6: Valuation Football Field (US$)



Source: CPMT Estimates

25 consecutive years, achieving a CAGR of 17% from 1998 to 2023. LOW now maintains a dividend payout ratio of 35%. Share repurchases are also projected to amount to ~US$4.0B in FY2024. Since 2020, the Company has implemented two buyback programs, collectively amounting to US$15.3B. In 2020, LOW conducted its first buyback program valued at ~US$8.6B worth of shares. The second buyback program was announced in 2022, and over FY2023 the Company repurchased 47mm shares, representing ~US$6.7B.

Risks

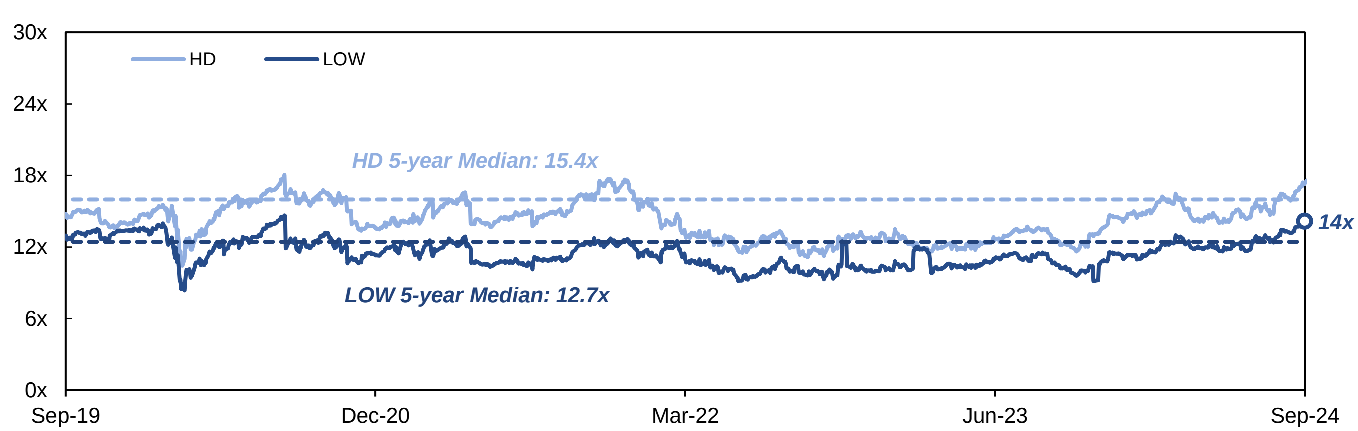
Macroeconomic factors such as inflation, rising interest rates, and housing market fluctuations can significantly impact discretionary consumer spending on home improvement, which is core to the Company's business. LOW's is also susceptible to supply chain disruptions and material shortages due to its reliance on global suppliers. Geopolitical tensions, natural disasters, or shipping delays can directly impact the Company's ability to meet customer demand. Additionally, the home improvement industry is heavily saturated through both e-commerce and brick-and-mortar operators. Constant innovation from HD poses a risk to LOW's position, forcing the Company to continually adapt to differentiate itself against HD.

Investment Thesis and Valuation

LOW was valued at US$293 using a five-year DCF with a WACC of 8.1%. The target price was derived using a 50/50 blend of (1) the Gordon Growth method, using a 1.5% terminal growth rate, and (2) an EV/EBITDA exit multiple of 14.0x.

LOW has historically traded at a discount to its closest peer, HD. The Fund views this discount as an attractive entry point due to LOW's growing operating margins, increasing net operating income per retail square-foot, and a peer leader in customer service. The Company's divestiture of its Canadian business in 2023 shifted LOW's store strategy to concentrate on its U.S. footprint. LOW's emphasis is on improving the productivity within its existing asset base and same-store sales that have grown at a five-year CAGR of 7.4%. The Fund views slowing DIY discretionary spending as a short-term headwind mitigated by Pro customer growth with a focus on small and midsize contractors. While LOW remains committed to its capital return program through share buybacks and quarterly dividends, the CPMT believes its return to shareholders will surpass those anticipated from HD. The Fund views a focus on customer service and DIY customers in an omnichannel environment as a resilient business model for the Company.

Figure 7: NTM EV/EBITDA vs HD



Source: S&P Capital IQ