



THE BIG ORANGE

NEWS AND ANALYSIS OF HOME DEPOT REPORT

The Eco Option

Early last month, CTS Cement produced a press release announcing that several of its [Rapid Set](#) fast-setting cement products received the Home Depot Eco Option label.

There are hundreds of products with an [Eco Options](#) label on Home Depot shelves. And the retailer sold 354 million Eco Options items in 2006 alone. The stated purpose of the program is to help customers identify products that make a difference in the environment. They either — take your pick — conserve energy, conserve water, provide for a healthy home, promote clean air or support sustainable forestry.

The world's largest retailer doesn't just hand the label to all comers. Rapid Set's Cement All, Mortar Mix and Concrete Mix had to earn their way into the program. Here is a Q&A with Frank Senatore, VP packaged products sales of CTS Cement, who took us behind the scenes of the certification process.

Big Orange Report: When did you recognize you had a "green" product on your hands?



Frank Senatore: As a company, we've always strived to maximize our use of recycled materials and minimize

our environmental impact with our products. In that sense, our products
(see Eco Options, page 3)



Home Depot gets top billing at the Desert Palms Power Center in Phoenix. See "Walking the Aisles" on page 6.

HD plays in a new market

BY BILL ADDISON

For even the most experienced and enthusiastic DIYer, home improvement projects aren't a game, they're a job. A rewarding job, but a job nonetheless.

Apparently, nobody told that to Nintendo, as a new home improvement based game, "Our House: Party!," was released Sept. 22 for the Wii and DS systems. To celebrate the release, the world's largest home improvement retailer, Home Depot, teamed up with world's largest video game and entertainment software retailer, [GameStop](#), to come up with a unique marketing plan. Everyone who purchases the game at any of GameStop's retail locations, or online, will



Gamers can "shop" at Home Depot in "Our House: Party!"

receive a Home Depot Mystery gift card good for anywhere from \$1 to \$1,000.

"[Our House: Party!](#)" developed by Edison, N.J.-based game developer Majesco, allows players to build their own home and engage in home improvement projects virtually.

In the game, players race against each other and the clock to buy the best materials in a digital home improvement store. Players then construct
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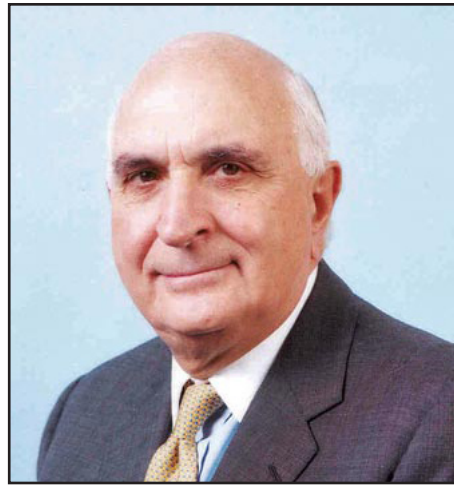


A word from the wise: Co-founder Langone speaks out

Home Depot co-founder Ken Langone has never been one to hold back his opinions on anything or anyone. The self-made investment banker and venture capitalist sat down on Oct. 2 with several reporters at *Bloomberg News* for a wide-ranging interview that touched on the early days of Home Depot, the current housing crisis and stock option rules, among other topics. Below are some excerpts.

• **On the founding of Home Depot in 1979:** “The world needed it. The circumstances of a home center industry were such that there was an enormous opportunity to create a national chain. Plus, we had two of the finest, smartest retailers in the world, especially Bernie Marcus. So, we had everything working for us.

“You need a little luck. The luck was that Bernie and Arthur [Blank] got fired [from a previous company]. Pat Farrah was working at a wine store company and was heading



Ken Langone, co-founder

into a store. So, you had the talent. You know, the stars have to be in alignment.”

• **On the recovery:** “I have no idea when it’s going to recover, all right? I’m not smart enough to say. I do know this — that this

economy with automobiles in the tank, and home building in the tank, these are huge industries as a percentage of our economy. I do know that people will continue to live some place. I haven’t seen any tent cities cropping up out on Long Island or anywhere. People end up living in apartments or homes, and wear and tear takes its toll.”

• **On the company’s health:** “This year [Home Depot] will pay off \$1.8 billion in debt, will maintain our dividend, will reinvest back into the business significantly in distribution, IT, new stores, remodeled, the whole bit and not borrow a nickel.”

• **On accounting rules:** “... If we tried to [start] Home Depot today, we couldn’t for one simple reason. One of the things that drove the passion in the stores were the options that we gave out. The accounting rules today regarding options make it impossible because we never would have been in the black.” ■

Do your Retail *Product Demos* Measure up?



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Eco Options

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have always been green. Since they have so many other advantageous features and benefits, we have been primarily educating people on these characteristics of our products. As people become more aware and concerned about the impact that products have on the environment, it is important that we educate people on the environmental benefits of our products.

BOR: How can you quantify the value of the HD Eco Options endorsement?

Senatore: Since the HD Eco Options program is new to us, it is difficult to quantify the value. However, we respect the Home Depot and value our relationship with them. The Home Depot has a great reputation, and having their [Eco Options endorsement](#) lends even more credibility to our “green” products.

BOR: How did you approach Home Depot initially, and what was its response?

Senatore: We initially approached Scientific Certification Systems (SCS). They are the company asked by Home Depot to



Eco Options isn't just for lawn and garden — it also helps guide buyers of fast-setting cement.

conduct independent evaluations of products to determine whether they meet the environmental performance criteria needed to qualify for participation in the program. We completed the questionnaire and submitted it to SCS in mid-June of 2008. They were very good to work with, and our interactions were positive.

BOR: Was acceptance harder or easier than you thought? What surprised you, if anything, about the process?

Senatore: Acceptance was neither harder nor easier than we thought. We know our products are “green,” and it was just a mat-

ter of making sure the information we submitted conveyed this information. We were pleasantly surprised at how thorough and rigorous SCS was in evaluating our submitted information. They were very good about asking questions and follow-up questions to clarify information so that they fully understood the criteria they used in evaluating our products. It was a nine-month process from the time we submitted our questionnaire to the time when SCS recommended us for the Eco Options Program. From there, Home Depot had the final say in whether or not our products were placed in the program. One month later,

Home Depot accepted our products into the program.

BOR: What kind of results do you expect now? And how else are you trying to promote the product?

Senatore: Rapid Set cement products are different from Portland cement products ... We have a strong base of loyal end users and continue to attract new users. We believe our loyal end users will continue using our products, and as consumers become more environmentally conscious, we expect the Eco Options to enhance our appeal to new end users. ■

Gaming

(from page 1)

their dream house with the purchased materials. Using the Wii remote, players actually hammer, saw, paint and perform many of the actual tasks involved with home improvement projects.

Ultimately, through building know-how and design prowess, players compete to create the most valued house in the community.

It's not hard to see why Home Depot would want a part of this. Throughout the games, players will see The Home Depot brand in weekly tabs with new lower prices and their “More Saving. More Doing.” tagline. They'll also get tips from Home Depot's [Home Improvement 1-2-3](#) books.

“We are always looking at new and emerging marketing techniques, and gaming certainly fits into that,” said Jean

Niemi of Home Depot's public relations team. “This game incorporates home improvement in a playful way and is great exposure for our brand.”

But it goes further than just branding throughout the game. Players literally shop at Home Depot for all their supplies.

“Wii players build their dream home by shopping at [Home Depot] to collect tools and supplies before competing in more than 175 mini-games. The

players interact in various store scenes and with [Home Depot] associates as they work on DIY projects,” said Niemi.

The two companies have also teamed up with Joe Gibbs racing to give Joey Logano's No. 20 GameStop NASCAR car a custom “Our House: Party!” paint scheme. Home Depot is also promoting the game on social media vehicles such as Twitter and [YouTube](#), Niemi told *HCN*. ■

Wall Street Chatter

Excerpts from analyst and conference calls

BY BRAE CANLEN

A Home Depot-style casino, inside the battle for the paint pro and the missing piece in the big ticket average — all this can be found in this month's Wall Street Chatter.



Capturing more sales in the pro paint channel has been on the minds of executives at both Sherwin-Williams and Masco, the maker of Behr paint. Much of this has to do with Behr's "pro initiative," launched at Home Depot last July, which offers deliveries to job sites, factory tinting and other perks.

But in order to capture more sales from the professional painter, both manufacturers have to define exactly who he is. Do they want to target the guy in the white overalls who paints houses for a living? Or the handyman who offers painting along with his other services? And more to the point, does he buy his paint at Home Depot or go somewhere else?

[Masco Investors Day Meeting](#) Sept. 17, 2009

Karen Mendelsohn, VP sales and marketing, explained Masco's strategy of "intelligent brand extension."

"The next example that I'm going to use is going to really speak to the idea of needs assessment: understanding the needs of your target. I'm going to use Behr as an example for this. There is no argument that Behr is a very well known, very well established, very successful brand in the DIY space. They have been partnering with the Home Depot since 1978, and they never stopped understanding the needs of this DIY consumer. But collectively, Behr and the Home Depot noticed that there was an opportunity. There was about 55% of the total paint market that is not DIY; that's pro. And, it was a target that was very consistent with Home Depot's strategy of 'Own the Pro' and their frequent



Cabinets sales have taken a hit since consumers have pulled back on remodeling projects.

and loyal purchasers. And a lot of these pros were shopping at the Home Depot for building materials but maybe not paint; so [it's] a sizable growth opportunity for both of us, both the Home Depot and for Behr.

"But who were these people, and what were their needs? So we again, Behr, did a very deep drill-down into this pro target, and we actually found that a pro is not a pro. We found that there were really two separate groups of pros, one the repair, remodeling and property maintenance professional who was going to shop in-store because they had other needs in the store, and then a second target audience, more of a general contractor, who really needed a job-site delivery solution. So, we addressed both.

"We presented a program — we are executing on a program in-store — and we've trained over 9,000 of the professional account sales associates at the Home Depot.

"We work closely with the Pro desk to develop programs and promotions for those contractors that are in-store. We have 29 of our own sales associates dedicated to the professional contractor who work hand-in-glove with the other over 400 sales associates

that Behr has working in-store to provide that really optimal in-store solution. And then, to address the general contractors who are really looking for more of a job-site solution, we just launched Behr Direct to Pro, and that is where we actually deliver paint directly to the job site. We will guarantee 72-hour order fulfillment. We do factory tinting for color accuracy, and we have a team of highly qualified experts and technical professionals to support the whole operation. So again, understanding the needs of the customer, Behr wins, Home Depot and the pro wins."

[Sherwin-Williams at Credit Suisse Group Chemical Conference](#) Sept. 17, 2009

Analyst: "In the contractor markets, Lowe's and Home Depot continue to try to court the contractors. What's the risk in your mind that they get that right? And how would you actually defend your position then?"

Sean Hennessy, senior VP finance and
(see Wall Street, next page)

Wall Street

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CFO: “I think that for many years we’ve watched this. I don’t think this is a new phenomenon. I think that if you look back at Home Depot, I think that they’ve courted the contractor for many years. They have had separate entrances. They’ve brought Glidden Paint in. Prior to that, regionally, they felt that they needed a brand. On the West Coast [they] had Frazee Paint; on the East Coast they had Duron. They found the strongest brands in the region and actually brought them in.

“So we’ve continually watched this. I think that they’ve done a lot of interesting things. The chances are, when you take a look at that [power point] slide that shows 92% of the architectural [market], the painting contractors buy from paint stores. That continually remains the same.

“It’s incumbent upon us not to be arrogant. To say, ‘Well, that’s the way it’s always going to be.’ I think that we’re concerned. We’re concerned to the point — which is a good concern, because we’re out there — we look at all their different initiatives, and we’re out there watching it.

“Home Depot has [a] person inside the store basically trying to sell the whole paint job for the house. We are watching that very carefully. So you know, it is a risk, but as you can see from that slide, that [market] hasn’t changed much in 10 years.

Bob Wells, senior VP corporate communication and public affairs, Sherwin-Williams: “Let me add something to that, Sean. The other thing that’s important to keep in mind is when the home centers talk about attracting the pro market, oftentimes

they’re talking about a different professional. The slide that Sean showed that broke down the painting contractors’ preferences by channel, those contractors are defined as companies that derive more than 75% of their revenues applying paint.

“The home centers have been very successful attracting remodelers who will remodel your basement. They’ll do a little electrical work, a little plumbing, they’ll put up drywall, they’ll put down floor covering. And as the last step in the process, they will apply paint.

“Oftentimes, when [Home Depot] refers to growing their pro business, that’s the pro they’re talking about. And they definitely have a natural run to market with that customer, because they are a one-stop shop. When we talk about pros, we talk about the dedicated painting contractors.”



Cabinets are a major component of any kitchen makeover, and the category has taken a beating as consumers pull back on remodeling projects. **Masco**, one of Home Depot’s main cabinet suppliers, is analyzing price points and pushing promotions in an effort to boost sales. But the best remedy may be to simply wait out the recession, judging from a Sept. 17 discussion at the company’s Investors’ Day meeting.

Analyst: “Where within your priorities is the development of an opening price point product for retail cabinets?”

Donny DeMarie, executive VP, chief operating officer, Masco: “Yes. It’s a really good question. It’s very high on our list of priorities. I think you’re

aware we make the ready-to-assemble products that still flow through Home Depot. And so we have that ultra opening price point. We also have some in-store assembled product that runs through our [Distinction] brands in retail, so we have that product as well.

“But a true opening price point on the retail side, I’d say that’s a gap and one we need to think about how [to] close. The problem we really have [to face] is that we really don’t want to take the KraftMaid brand into that price segment, because the KraftMaid brand is really above it. We do have the Distinction line, but I think we could have a more robust offering, and we’re talking about it all the time.

“On the builder side ... we do very, very well. Quality [Cabinets] does a nice job of really reaching into that middle space with Merillat, but actually comes down a little below where Merillat’s at. So I feel we’re fine on the builder side. I’d like to have a little bit more robust offering on the retail side.”

Analyst: “If you look at the comps in home retail in the second quarter, traffic had really picked up. And that is reflective in your results, and Behr Paint is doing pretty well, but there’s still a very profound weakness in ticket at Home Depot and Lowe’s. And there’s a fear, I think, that it’s going to have a pretty long tail to it. So [with] the product mix that you have, what [will] you do to kind of mitigate that impact going forward into 2010? Basically, what can you do to try and drive up the ticket or drive up demand for the bigger ticket products that you sell?”

DeMarie: “Are you talking more on the cabinets with the high-

ticket items?”

Analyst: “Yes.”

DeMarie: “And how that’s impacted the average ticket? I think that the problem with talking real specific about retail is it’s very, very different by category. And I know when we report by segment, you have a hard time seeing that. But, yes, if we talk specifically the weakness at retail, the weakness at retail is cabinets; it’s the high-ticket items on the retail side.

“And you’re seeing that the consumer responds very favorably to promotional activities. And where our American [Classics] wood market ran that promotion at the end of last year that carried into the first quarter of this year. Yes, it picked up a lot of business, but as soon as the promotion [ended], the market share went back to its traditional splits.

“We’ve done some things. We’ve done some promotional activities that have spurred some upticks in volume, but you just find the consumer really waiting for that deal. You know what I think is the key metric we’ve got to watch? Is there confidence and [an] ability to finance a kitchen — a home-improvement project? So until that changes, I don’t think you’re going to see a lot in that cabinet segment. I think the rest of our segments are far better on the retail than we have on the cabinets.”

Analyst: “Is that promotional activity a risk going forward? Is there a chance that consumers just won’t come back, [and] your margins wouldn’t recover because they want that deal?”

DeMarie: “I don’t think so. I think as long as you continue *(see Wall Street, page 7)*



BY KEN CLARK

PHOENIX — Somebody forgot to tell Home Depot store #477 that Phoenix is suffering from a housing market slowdown.

When two visitors from *Home Channel News* approached the Central Phoenix store here on Thomas Road on a weekday morning, it was hard to get a picture of the exterior — too



many contractor vehicles were obscuring the view.

Shopping activity was brisk inside, as well, particularly in the lumber department, where we met Toni Mayorga, operations manager, and Becca Garcia, manager in training.

“Business is not like it was four or five years ago, but we’re still a major hub for construction,” Mayorga said. “And we get a lot of the downtown business.”

The Home Depot on Thomas Road is part of the Desert Palm shop-

Selling in the Valley of the Sun

ping center and shares top billing with a Wal-Mart Supercenter. Another geographic advantage for store #477 is the resurgence of old town Phoenix, where stately old homes have been somewhat rediscovered in a city where the norm for years has been new construction in an ever-expanding outer-perimeter.

“It’s about 10-years old, but it’s shopped hard. Very hard. Because we’re busy, as you can see,” Mayorga said.

Walking around the store revealed some traditional sights and sounds. A “Cashier Appreciation Month” banner hangs proudly at one of the checkout aisles. The Ryobi Tek4 display, promoting an environmentally smart, reusable power source for cordless electric tools, is front and center in the tools section, and various homemade Homer signs are sprinkled around the store.

The store has its local focus. Case in point: [winter grass](#). In Phoenix, October is winter grass-planting season, and many customers are inquiring about this topic. The store is providing answers through customer clinics, Mayorga said.

Look a little closer at the signs, and a special Spanish-language initiative is revealed. The Clinic/Clinica sign gives equal billing to Spanish language. And back in the



Becca Garcia, left, manager in training, and Toni Mayorga, operations manager, in Phoenix

aisles, visitors can read that Roger and Miguel — whose pictures are smiling at customers — are among those employees who “hablan español.”

According to Mayorga, about half the store’s customers speak Spanish, and the store is showing its character by aggressively reaching out to them.

But a lot of this store’s character is not visible to the visitor in the aisles. Mayorga sang the praises of the store’s pro depart-

ment — “We’re still doing double what any other pro department is doing. It’s a huge business here,” she said. And part of that is the aggressiveness of the store’s sales staff. “They get out in the field, they pull permits and visit sites, and let the pros know what we can do for them,” she said.

Another example of store character is revealed in its partnership with the City of Phoenix and the [Latino Institute](#) to participate in “El Día de

los Niños” earlier this year. More than 3,000 kids participated, painting tiles and orange aprons supplied by Home Depot. The store was recognized with an “Orange Embrace” award, a corporate program designed to promote diversity and inclusion.

And then there’s the case of the customer whose dedication to riding her neighborhood of crime was rewarded with a Home Depot-sponsored home makeover.

(see *Aisles*, next page)

Aisles

(from previous page)

Looking around the busy pro-oriented Home Depot, this seems a world away from one of Mayorga's previous retail jobs with the department store Macy's. "There it was: 'How do you like working with Donna Karan?' as opposed to

here, where you're working with nuts and bolts," she said. "But you know, selling is selling."

Home Depot will get an infusion of Macy's-like merchandising when Martha Stewart, who for years has had a relationship with Macy's, brings her brands to Home Depot in 2010. "Very excited about that," said

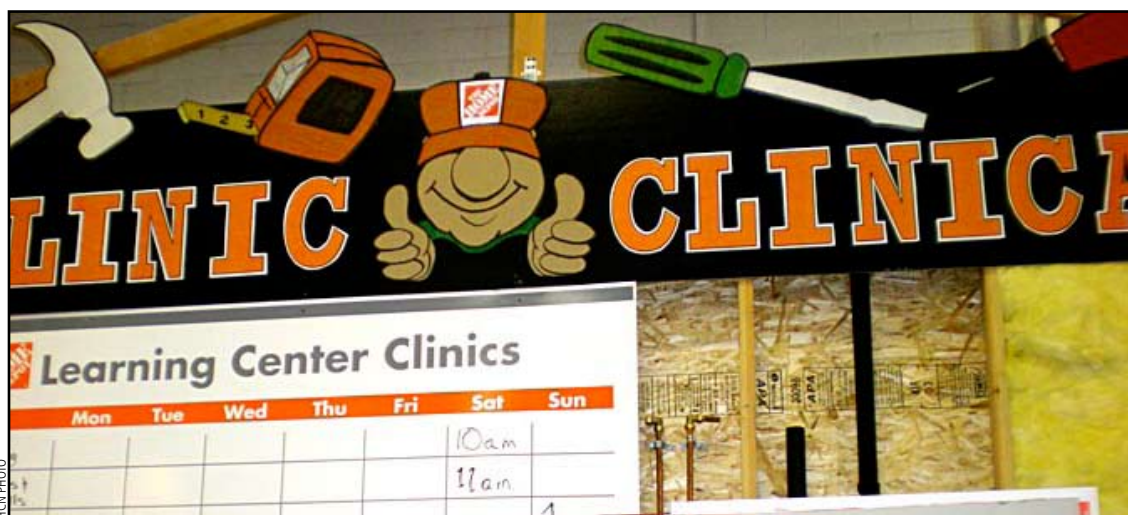
Mayorga.

Mayorga was transplanted here from a different Home Depot in the upscale Scottsdale area about three years ago.

"In Scottsdale, people really wouldn't blink at spending five grand on patio furniture," she said. "Here it's a little bit different. We always have to make sure we get

the right product for the customer we're selling to. Maybe a little more middle line, but we always get surprises. We have the Arizona Biltmore Hotel nearby. I've seen Bentleys in the parking lot."

Then she added, philosophically: "I never judge a book by its cover. People are going to buy." ■



Store #477 has embraced the company's Hispanic initiative — with bilingual balance in its signage.

Wall Street

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to innovate and be true to your brands, the consumer will be there. I think what you have to do right now is ... stimulate them to do something different. I also think you have a significant amount of pent-up demand. If I look at the number of foreclosed homes that are going through the system, at some point people are going to go in and start having confidence and invest in their home again. Right now, I think we're seeing some

of that volume come through in paint; it's a real easy do-it-yourself project. I think it makes the house look good for a relatively low cost. But at some point, I think you'll see the confidence go out and start doing the bigger-ticket items again.

But to overly promote — we're promoting pretty aggressively now. And certainly, we're having the matched competitor promotions that are pretty aggressive right now. So I'm not sure that there's a number that would make sense for us and our retail partners that would really do

anything other than pull forward some people sitting on the fence." ■ ■ ■ ■ ■

No one would ever accuse William Clifford, the CFO of [Penn National Gaming](#), of aggrandizing the decor of his firm's gambling establishments. At the Deutsche Bank Securities Leveraged Finance Conference on Sept. 30, Clifford updated analysts on gaming referendums in various states, showed photos of Penn's existing casinos and talked about upcoming projects. A

1,500-slot facility in the Baltimore area is still two years from completion, Clifford said.

William Clifford, CFO, Penn National Gaming: "It is very minimalist. It kind of looks like a Home Depot with some nice — no disrespect to Home Depot, but generally very conservative on the spend. I think the building itself, land wasn't that cheap. We had some other things, but it is really nothing more than a box. Once you are inside, it will look very nice, but it is definitely Hollywood Lite." ■

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