Q2 2022 Earnings Call

Company Participants

- Craig Menear, Chief Executive Officer
- Isabel Janci, Vice President-Investor Relations
- Richard McPhail, Chief Financial Officer & Executive Vice President
- Ted Decker, Chief Operating Officer

Other Participants

- Brian Nagel, Analyst
- Chris Horvers, Analyst
- Chuck Grom, Analyst
- David Belanger, Analyst
- Eric Bosshard, Analyst
- Greg Melich, Analyst
- Karen Short, Analyst
- Kate McShane, Analyst
- Laura Champine, Analyst
- Liz Suzuki, Analyst
- Michael Lasser, Analyst
- Simeon Gutman, Analyst
- Zach Fadem, Analyst

Presentation

Operator

Greetings and welcome to The Home Depot Second Quarter 2021 Earnings 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 {BIO 16473072 <GO>}

(technical difficulty) quarter 2021 Earnings Call. Joining us on our call today are Craig Menear, Chairman and CEO; Ted Decker, President and Chief Operating Officer 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 to your question during the call, please call Investor Relations at 770-384-2387.

Before I turn the call over to Craig, 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 presentations will also include certain non-GAAP measures, reconciliation of these measures is provided on our website.

Now let me turn the call over to Craig.

Craig Menear {BIO 15126612 <GO>}

Thank you, Isabel and good morning everyone. We appreciate you joining us on our call this morning. We were pleased with our performance in the second quarter, as we achieved over $40 billion in quarterly sales for the first time in our history. Sales for the second quarter were $41.1 billion, up 8.1% from last year. Comp sales were up 4.5% from last year, with US comps of a positive 3.4%. Diluted earnings per share were $4.53 in the second quarter, up from $4.02 in the second quarter last year.

The strong underlying demand across the business continues. During the second quarter, we did observe some changing consumer patterns in the US as the US economy opened up. This is manifested itself in several ways. We have seen a shift in pattern of sales within the week, as our weekday sales performance has actually strengthened relative to the weekend. We attribute this to consumers returning to travel and other recreational activities.

And while the consumers returning to pre-pandemic activities, we continue to see them engaged in home improvement projects. We also see customers more comfortable taking on larger projects is evidenced by the continued strength with our pro-customer, which outpaced the DIY customer for the second quarter in a row. We remained agile and flexible and we're pleased with our ability to respond to strong home improvement demand and comp-to-comp in the second quarter.

We had positive comps every week despite unprecedented compares last year and grew sales by $3.1 billion in the second quarter and more than $12 billion year-to-date. Over the last six quarters, we have grown the business by more than $34 billion, a level unmatched in our market. From a geographic perspective, 15 of our 19 US regions posted positive comps versus last year, on a two-year stack basis, all 19 regions saw strong double-digit comp growth.

However, unlike the past four quarters, the second quarter we did experience some variability in performance from a geographic perspective. The variability in our regional performance is driven by our Northern Division, where we saw a more pronounced shift in sales with stronger sales in outdoor seasonal categories during the first quarter. Mexico posted double digit positive comps and despite significant customer restrictions during the quarter due to COVID-19, Canada posted comps that were essentially flat in local currency.

We continue to effectively manage the strong demand for home improvement products despite significant industry disruptions in supply chains. We are leveraging the scale of our supply chain and partnership with our vendors to prioritize key SKUs and high demand categories. And while our in-stocks are not where we want them to be, they have improved from where they were a year ago and our network continues to flow goods remarkably well, thanks to the investments we have made in our supply chain over a number of years.

The team continues to make progress on building out our One Home Depot supply chain vision. We remain largely on track with our plans with the critical mass of building scheduled to come online this year and next. We believe that the network we are building is unique to the market. It will not only enhance the customer experience from a delivery standpoint, but also expand the breadth and depth of our current opportunity set, drive efficiency and leverage our scale to further extend our low cost position in home improvement.

In the near-term, we remain focused on being flexible and agile as we navigate this dynamic environment, but we also continue to leverage the momentum of our strategic investments to further enhance interconnected shopping experience and support of our goals to drive growth faster than the market in any environment, further strengthen our position as low cost provider in home improvement, with a relentless focus on productivity and efficiency and deliver exceptional shareholder value.

Throughout all events in the past 18 months, our culture has remained on North Star. In fact, I recently spent time with the number of new associates that we have hired in the past year and was struck by how engaged and connected these associates were to The Home Depot culture. They were on-boarded during a time when our stores and teams were busier than ever, but our associates took the time to get to know these new folks and share what it means to be part of the orange blended family.

Our ability to invest for the future while also managing the most fluid environment our Company history is a direct result of our associates and their extraordinary efforts. I want to close by thanking them for the many ways they continue to live our values, by serving our customers, communities and each other.

And with that, let me turn the call over to Ted.

Ted Decker {BIO 16614891 <GO>}

Thanks, Craig and good morning everyone. I want to start by also thanking all of our associates and supplier partners for their commitment to serving our customers and communities. As you heard from Craig, during the second quarter, we continue to see strong performance in our business particularly as we lapped the significant growth in the same period of last year. We were able to meet strong customer demand despite ongoing pressures throughout the supply chain.

Raw material shortages, production constraints and pressures across modes of transportation are creating a difficult supply chain environment. That being said, our performance would not be possible without the cross-functional efforts by our supply chain, merchandising store and MET teams as we continue to flow record volumes of goods week-after-week. Over the course of the pandemic, you've heard us talk about a number of initiatives we've implemented, many in concert with our suppliers to improve our in-stock positions and get product to our customers and our teams continue to use our culture and values to guide our decisions.

One of our values is entrepreneurial spirit which is alive and well at The Home Depot. Our supply chain teams recently leveraged our scale and flexibility to arrange for several container vessels for our exclusive use. Yet another way, our teams found a creative solution to better serve our customers in this dynamic environment. Our in-stock levels are still not where we want them to be, we are maintaining the improvements we made over the last few quarters and building depth in key categories, as evidenced by inventory growing faster than sales compared to the same period last year.

Turning to our comp performance, during the second quarter 10 of our 14 merchandising departments posted positive comps, led by kitchen and bath and lumber. During the second quarter of this year, we saw single digit negative comps in paint, hardware, in indoor and outdoor garden. It is important to note that these were some of our strongest performing departments during the second quarter of last year. On a two-year stack basis, each of our departments posted healthy, double-digit comps.

Our comp average ticket increased to 11.3% and comp transactions decreased 6%. The growth in our comp average ticket was driven in part by inflation in certain categories, notably lumber. On a two-year stack basis both comp average ticket and comp transactions were healthy and positive. This was another historic quarter for lumber price volatility. During the first few weeks of the second quarter, prices for both framing and panel lumber reached all time highs for quickly falling from their peaks.

As an example, during the second quarter framing lumber peaked at approximately $1500 per 1000 board fee before falling over $1,000 to approximately $500, while pricing for both framing and panel has come down from the peaks, the average price during the second quarter was still significantly higher in the same period last year. Inflation from core commodity categories positively impacted our average ticket growth by approximately 420 basis points during the second quarter. Big-ticket comp transactions or those over $1,000 were up approximately 24% compared to the second quarter of last year. We saw the big ticket strength across many Pro heavy categories like lumber, vinyl plank flooring, gypsum, in pipe and fittings. During the second quarter, Pro sales growth outpaced DIY growth for the second quarter in a row, on a two-year stack basis growth with our Pro and DIY customers was consistent and strong.

We're encouraged by the momentum we are seeing with our Pros. Growth with our larger Pros continues to outpace that of our smaller Pros and they tell us that their backlogs are long in growing. In fact, the National Association of Homebuilders Remodeling Index hit all time highs during the second quarter and during the quarter we saw many of our customers turn to Pros to help them with larger renovation projects. This can be seen in the strength of several of our kitchen and bath categories like in-stock kitchens, tubs and showers and vanities, all of which posted one year and two-year comps above the company average. Sales leveraging our digital platforms were essentially flat during the second quarter as we lap digital sales growth of approximately 100% in the second quarter of last year. On a two-year stack basis, sales from our digital platforms increased approximately 100%.

We're thrilled with the customer engagement across our interconnected platforms. We know the vast majority of our customers engage with us in an interconnected manner, whether it be through project inspiration research, transacting, fulfillment or support, our customers' blend the physical and digital worlds. And while customers who've gotten more comfortable buying online, we've never been more confident in the importance of our physical stores as they they remain the center of our customer experience due to the project nature of our business.

For those customers that chose to transact with us online during the second quarter more than 55% of our online orders were fulfilled through our stores, a testament to the power of our interconnected retail strategy. As we look forward to the back half of the year, we know our Pros are busy and we are working hard to secure the best products to help our Pros get their jobs done. Last quarter, we highlighted several exclusive products for our Pro customers.

This quarter we're excited to announce a new big-box home improvement exclusive relationship with LP Building Solutions, a top provider of OSB panel boards. In addition, we are pleased with the momentum we are seeing with our Pro Xtra loyalty program. Several quarters ago we've relaunched Pro Xtra and we've been thrilled with the membership take up and engagement we are seeing.

Pro Xtra offers more frequent touch points with our pros and convenient services like purchase tracking and volume pricing along with other benefits. In addition, all Pro Xtra members are now able to access our B2B Pro online experience, offering Pros more personalization on homedepot.com. During the third quarter, we are also thrilled to announce the rollout of what we believe is the most innovative paint offering in years through our exclusive relationship with BEHR. BEHR DYNASTY is a brand new four-in-one interior paint that offers DIYers, pro painters and design professionals a unique product exclusively from The Home Depot, it is our most stain repellent, scuff resistant, fast drying, one coat coverage paint all in one can.

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

Richard McPhail {BIO 19175260 <GO>}

Thank you, Ted and good morning everyone. In the second quarter, total sales were $41.1 billion, an increase of $3.1 billion or 8.1% from last year. Foreign exchange rates positively impacted total sales growth by approximately $385 million. During the second quarter, our total company comps were positive 4.5%, with positive comps in all three months. During the quarter, we saw total company comps of 4.7% in May, 3.9% in June and 4.9% in July.

Comps in the US were positive 3.4% for the quarter, with comps of 3.1% in May, 2.7% in June and 4.3% in July. In the second quarter, our gross margin was 33.2%, a decrease of approximately 80 basis points from the same period last year. While there are many factors that impact gross margin, the year-over-year change during the second quarter was primarily driven by lumber, which accounted for approximately 60 basis points of pressure.

In addition, several other factors negatively impacted our gross margin including rising transportation costs, one supply chain investments and lapping a benefit from canceled events in the second quarter of last year. During the second quarter, operating expense as a percent of sales decreased approximately 100 basis points to 17.1%. Our operating leverage during the second quarter reflects significant COVID related expenses that we incurred in the second quarter of 2020 to support our associates.

These expenses were partially offset by underspend in other expense items in the second quarter of last year, most notably payroll as we staffed up to meet strong demand. Our operating expenses during the second quarter of this year also include wage investments that we made at the end of 2020. Our operating margin for the second quarter was 16.1%, an increase of approximately 20 basis points from the second quarter of 2020.

Interest and other expense for the second quarter decreased by $16 million to $321million. In the second quarter, our effective tax rate was 23.9% down from 24.4% in the second quarter of fiscal 2020. Our diluted earnings per share for the second quarter were $4.53, an increase of 12.7% compared to the second quarter of 2020. At the end of the quarter, inventories were $18.9 billion, up $5.4 billion from last year and inventory turns were 5.7 times, compared with 6.1 times this time last year.

Turning to capital allocation. After investing in our business is our intent to return excess cash to shareholders in the form of dividends and share repurchases. During the second quarter, we invested approximately $520 million back into our business in the form of capital expenditures. And during the quarter, we paid approximately $1.75 billion in dividends to our shareholders and we returned approximately $3 billion to shareholders in the form of share repurchases.

Computed on the average of beginning and ending long-term debt and equity for the trailing 12 months, return on invested capital was approximately 44.7% up from 41.1% in the second quarter of fiscal 2020. As you heard from Craig, we are very pleased with the strong performance we saw during the second quarter, particularly as we lap the unprecedented growth we saw this time last year. And while these challenging compares continue through the back half of the year, we are encouraged by what we are seeing.

During the first two weeks of August, we've seen comps in the US consistent with the second quarter. Customer engagement and demand for home improvement is healthy, housing remained strong and we see a supportive environment for home improvement spending as we look out over the next several years. That said, there is still a significant amount of uncertainty in the broader environment as it relates to the evolution of the COVID-19 pandemic and the new and spreading variance.

As we've previously shared, we do not believe we can accurately predict how the external environment will evolve and how it will ultimately impact consumer spending. We will continue to execute with flexibility and focus and what has driven our successful performance. Longer-term, we remain committed to what we believe is the winning formula for our customers, our associates and our shareholders. We intend to provide the best customer experience in home improvement. We intend to extend our position as the low cost provider and we intend to be the most efficient investor of capital in home improvement. If we do these things, we believe we will continue to grow faster than our market and we will deliver exceptional value to our shareholders.

Thank you for your participation in today's call and Christine, we will now open the call for questions.

Questions And Answers

Operator

Thank you. (Operator Instructions) Thank you. Our first question comes from the line of Simeon Gutman with Morgan Stanley. Please proceed with your question.

Q - Simeon Gutman {BIO 7528320 <GO>}

Thanks, everyone. Good morning. Hi, Craig and Richard, I wanted to ask, maybe I'll ask this every quarter for now. I wanted to ask about home improvement demand whether it has to digest the next couple of years or we can keep compounding? And I think Richard just mentioned in his comments like expecting several years of healthy demand ahead, so curious if your thoughts have evolved on the next couple of years given the massive growth we've had over the past two?

A - Craig Menear {BIO 15126612 <GO>}

Simeon, when we look at overall backdrop for support in home improvement from a housing perspective, from the remodeling index, we feel pretty good about the long-term outlook for home improvement, hard to predict the short-term, but the longer-term outlook looks solid.

Richard, I don't know if you want to --

A - Richard McPhail {BIO 19175260 <GO>}

You just you look at the -- we believe that home price appreciation is a fundamental support of home improvement activity and demand as your home becomes more valuable, you are more likely to spend more on it. We are at a point now where the housing stock of the United States is over 20% more valuable than it was two years ago. And so as we look forward not only have we seen that home price appreciation, but the homeowner balance sheet is incredibly healthy, the state of mortgage-finance is incredibly healthy. And so that's why some of the reasons why we're optimistic.

Q - Simeon Gutman {BIO 7528320 <GO>}

That's helpful. And then one near-term question. The second half outlook for gross margin, does the dynamic that occurred in the second quarter, does it ease allowing the gross margin to improve in the back, not improve, but at least the rate of change improve from what happened in the second quarter.

A - Richard McPhail {BIO 19175260 <GO>}

I'd say we're focused on executing week-to-week here. There are certainly cost pressures in the environment and I think we're all dealing with that, but we've dealt with that throughout our history and we are comfortable with our ability to manage through the cost environment effectively.

A - Craig Menear {BIO 15126612 <GO>}

Simeon, I think there are some very unique scenarios, obviously in the quarter lumber being the one as Richard called out, unprecedented level of drop and unprecedented speed with which it drops. Normally the only impact you have is from mix, but with the rapid decline and the extent of the decline, we always have a philosophy that we want to lead the market down and lag going up to remain as competitive as possible for our customers and that actually created an impact which in this quarter was unique that we normally don't see.

A - Richard McPhail {BIO 19175260 <GO>}

And I'd make another comment which is the shape of the business given the volume that is coming through our system is not predictable, but we know we're confident that we are taking share and we're there to meet the demand that we see from our customer that, that mix may have an impact, but when we look at the operating profit dollar growth we're generating as a company we feel great about it. So, we're looking more at driving market share capture and driving that operating profit dollar growth.

Q - Simeon Gutman {BIO 7528320 <GO>}

Thank you.

Operator

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

Q - Michael Lasser {BIO 7266130 <GO>}

Good morning. Thanks a lot for taking my question. How should the trip -- the trend that you outlined with diverging performance on the weekdays versus the weekends inform how we think about the DIY business moving forward. Do you attribute that to more of a temporary condition where consumers had pent-up demand to go on vacation this summer and return to projects in the fall or alternatively as families return to traditional activities like U SPORTS watching college and pro sports and gradually returning the office, it's going to put accelerating pressure on the DIY business. And do you think there is enough strength and pent-up demand for the Pro segment that it can offset back?

A - Craig Menear {BIO 15126612 <GO>}

Hey, Michael, it's a great question is something we're watching carefully as the consumer gets back to more normal environments. What we did see is the consumers in our research would suggest this as well, consumers are taking on more projects, they are larger projects and have a tenancy to hire a Pro to do them. And as a result, we've seen our Pro business strengthen for several quarters in a row with the last two quarters where the Pro outperformed the DIY customers for the first time since the pandemic started.

And so we're very optimistic about where the Pro business goes and the strength of that Pro business and we're focused on making sure that we can take care of those Pros along with our DIY customers, but feel like there is solid opportunity to continue to grow. Pros tell us their backlogs are bigger than ever, consumers continue to tell us the home is more important than ever and that they have a laundry list of projects.

Q - Michael Lasser {BIO 7266130 <GO>}

That's all helpful, Craig and you're going to have this funky dynamic where maybe the Pro business is good, maybe the DIY business decelerates from here and how is that going to impact your labor model, which is activity based, so comps do turn negative in the back half, how quickly can you flex that and how well is it fine-tuned for this dynamic where you might have a decline in DIY transactions, you may actually not need as much labor, so you can save some SG&A dollars on that.

A - Craig Menear {BIO 15126612 <GO>}

Yeah, Mike, if you hit us on the head in terms of -- our labor model is an activity based model which has a component in their transaction. So we can adjust relatively quickly, it's a short cycle model and we'll make the appropriate adjustments as we go. It's -- we plan out a few weeks in advance.

Q - Michael Lasser {BIO 7266130 <GO>}

Okay. Thank you very much and good luck.

A - Craig Menear {BIO 15126612 <GO>}

Thank you.

Operator

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

Q - Chuck Grom {BIO 3937478 <GO>}

Hey, good morning. I was just wondering if you guys could elaborate a little bit more on some of the benefits you expect to see once the one HD Supply Chain gets built out sometime in 2022?

A - Ted Decker {BIO 16614891 <GO>}

Sure. The whole purpose of the supply chain is really our ability to deliver all of our products, parcel and big and bulky to 90% of the US population same and next day. And we're three plus years into this build out. We have multiple facilities up of each type that we're building, they're all performing well in fulfilling that expectation of being able to deliver and satisfy the customer speed and reliability is what's required particularly with our Pro customers.

In addition, it's allowing us to expand our assortments from what we carry in our stores. So not only can we get the product in a quicker more reliable fashion to our customers, we can get a broader assortment to our customers. And lastly, we're up to $660 a square foot of sales this past quarter in our stores and it's just a tremendous amount of activity in cube in that building, so to be able to get deliveries, particularly the big and bulky deliveries out of the store that helps our customer flow and our associate activities in the store. And we're just thrilled with that in particular as our FTCs have opened up, we're relieving tremendous amount of delivery activity in cube flow out of our stores and delivering directly out of the new facilities exactly the way the supply chain team had planned it.

Q - Chuck Grom {BIO 3937478 <GO>}

That's great and then just on lumber, I'm curious what you're seeing from a unit volume perspective as prices drop throughout the quarter.

A - Ted Decker {BIO 16614891 <GO>}

Well clearly when we hit $1500 plus a 1,000 board fee, people backed out of the market for sure and waited and it wasn't that we've got a tremendous amount of new supply in the marketplace, I think once you hit that tipping point where people backed off on the margin and prices started to fall and as Craig said it was falling so quickly $100, $150 even $200 a 1,000 board fee per week, people just stepped back even further. That's now settled at about $430 for framing lumber and for sure those high levels we saw an impact to units or units in turn negative and as prices have come down units are still negative, but on a sequential basis improving in responding to that lower price. So we're very pleased, supply and demand dynamics worked as expected.

Q - Chuck Grom {BIO 3937478 <GO>}

Thank you.

Operator

Our next question comes from the line of Karen Short with Barclays. Please proceed with your question.

Q - Karen Short {BIO 7215781 <GO>}

Hi. Thanks very much. Just wondering with respect to inventory, obviously you're up against your comparisons from last year, but looking at overall areas of inventory, is there any area where you think you're still lacking product? And then how to think about inventory growth in the second half of the year?

A - Craig Menear {BIO 15126612 <GO>}

Yeah, first of all, Karen, I'd say we're super pleased that we've been able to continue to build up, but yet at the same time have incredible inventory productivity at 5.7 turns. So we're very, very pleased with that. There is still -- we're in a situation still where we're not exactly where we want to be from an in-stock perspective, our suppliers are working hard, but our merchants have worked with our suppliers to kind of narrow the focus on key SKUs. And so there is opportunity still to continue to bring more product in across the breadth of assortment, but right now we're trying to stay focused on the things that really, really matter.

A - Ted Decker {BIO 16614891 <GO>}

And I'd say it's been a category-by-category story and as Craig said, we're trying to build depth in our highest philosophy SKUs. We're trying to build up in job lot quantities for our Pro customers and that tends to be heavy on the building material side of the business, the lumber building materials and electrical and plumbing fixtures. And we've recovered nicely in all of those departments. But again, it can be category-by-category, there is a COVID outbreak in a factory, there is a shipping constraint, there is a domestic transportation capacity constraint.

So it's been the story of two steps forward one step back, but we are making progress. And that's why we're happy to lean into inventory, we're blessed with the financial strength and liquidity. Our goods tend to be non-perishable, not a lot of obsolescence particularly in our core product. So if -- lot of this is who has the product is going to sell the product and I think our supply chain and merchants responding as well as they have is one of the reasons we've taken so much market share in this environment.

Q - Karen Short {BIO 7215781 <GO>}

Okay, that's helpful. And I just was wondering on the Pro Xtra loyalty, I was wondering if you'd be willing to give a little update on the number of members in the program. And then any color if you can provide on average spend of members versus non-member Pro or just any metrics that you could provide?

A - Ted Decker {BIO 16614891 <GO>}

Yeah, I won't get into details, but you know our rough dynamic about 4%, 5% of our customer base being the Pro makes up 45% of our sales. So this is a number in the mid-millions of our core Pros, very strong number of those percentage of those are in the Pro Xtra program. And now as I mentioned in my prepared remarks, we're building a B2B website and all of our Pro Xtra members now have been transferred over to that B2B experience.

So the combination of the benefits that you're getting with Pro Xtra, we've stood up with separate Pro Xtra app that those pros are using and the ability to engage on the B2B website which has all sorts of functionality build out specifically for the Pro. So think of bills material for jobs, tracking jobs, quotes building quotes reorder capability, tracking all receipts, preferred pricing in certain instances, all of that is coming together, as well as personalization in building relevance on that Pro B2B website.

So think of something like search results. If you are I would put in players. We have 1000 suppliers that could be returned in that search result. We're getting to the point now that we know an electrician is performing that search. So we're going to provide relevance and we're going to provide our electrical players as the first results in that search query. So this is just another great add to our Pro ecosystem and just been tremendous engagement with the Pro loyalty app, the Pro Xtra program and now B2B website.

Q - Karen Short {BIO 7215781 <GO>}

Great. Thanks very much for all the color.

Operator

Our next question comes from the line of Brian Nagel with Oppenheimer. Please proceed with your question.

Q - Brian Nagel {BIO 6638066 <GO>}

Good morning. Thank you for taking my question. A couple of questions with regard to sales and pretty quick ones, but first just with respect to lumber. I know you talked about it in your prepared comments and in response from the questions, but could you say to what extent lumber was a benefit to comps this quarter?

A - Ted Decker {BIO 16614891 <GO>}

About $1.3 billion.

Q - Brian Nagel {BIO 6638066 <GO>}

Okay. And then that was weighed more towards the first the way laid out as you know was weighed much more towards the first half of the quarter or early in the quarter (inaudible).

A - Craig Menear {BIO 15126612 <GO>}

Yes, Brian, for sure it was a unbelievable fast fall. But yes, it was -- that was heavily geared towards the first part of the quarter.

Q - Brian Nagel {BIO 6638066 <GO>}

Okay. And then the second question I have, I know this is off of nuance but as you talk about the strength in the Pro business in your conversations, your connections with your Pro customers, do you think that the jobs are being taken on now, were those jobs that were started during the pandemic and are only now being able to be fulfilled because the

Pros have -- Pros are available to work or these projects are actually sort of starting right now?

A - Craig Menear {BIO 15126612 <GO>}

I think you probably have a combination would be my best guess. I don't know that for sure, but we know for example when we talk to Pros they've had a backlog for some time. And so I think clearly there is probably some that have been in the works where they've been waiting to -- customers have been waiting for Pro to start a job and then I think there is probably scenarios where it's a quicker cycle, but we don't really have a way of knowing that.

A - Richard McPhail {BIO 19175260 <GO>}

The National Association of Homebuilders Index has a lot of interesting survey data within it. One of the survey components is consumer optimism in intent around projects and we have actually seen intent tick up for small projects, medium-size projects and large projects really sort of sequentially through the year. So I think if you kind of take the question off of the backlog and you say what's the intent, it does seem like that homeowners are leaning into projects and you -- whether it's a Pro or consumer customer at all essentially at the same customer demand. So it looks like the trend is strengthening in project demand.

A - Ted Decker {BIO 16614891 <GO>}

And I think if you look at our services business is a proxy, we're certainly seeing that as well as our service business think of these are large projects, carpet installation, cabinet installation, rephase bath HVAC, those all are strong and accelerating.

Q - Brian Nagel {BIO 6638066 <GO>}

Appreciate all the color. Thank you.

Operator

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

Q - Zach Fadem {BIO 18911015 <GO>}

Hey, good morning. So you're lapping a period of very low promotional activity as you know and given the three major holiday events in Q2 with Memorial Day, Father's Day, July 4th, could you talk about to what extent these events were a material top line driver in the quarter? And then with respect to gross margin, to what extent that this has unimpacted in Q2 and how should we think about the promotional impact as that mix is into the gross margin line in the second half.

A - Ted Decker {BIO 16614891 <GO>}

I would say our promotions were up from last year, but only because we canceled so many last year we were on the margin less promotional say then going back to '19. So while we're very happy with our events in our sell-through, we had record sell-through in virtually all of our programs. The events were not a huge driver of our comp and it wasn't the things Richard called out on our margin impact, it wasn't particularly meaningful.

A - Richard McPhail {BIO 19175260 <GO>}

Wasn't meaningful.

Q - Zach Fadem {BIO 18911015 <GO>}

Got it, that's helpful. And then Richard, could you talk about how your Pro versus DIY trends performed through the quarter? And if there is any variability in trend from one versus the other and then for Q3, does the commentary that trends are in line during the first two weeks of August, does that also hold for both Pro versus DIY?

A - Richard McPhail {BIO 19175260 <GO>}

Well, so we're not going to break out intra-quarter, it was the second quarter where we saw our Pro customer grow faster than our DIY customer. I'd say in the first two weeks of the quarter not much has changed with respect to the direction of our business.

Q - Zach Fadem {BIO 18911015 <GO>}

Got it, appreciate the time.

Operator

Our next question comes from the line of Liz Suzuki with Bank of America. Please proceed with your question.

Q - Liz Suzuki {BIO 16142563 <GO>}

Great, thank you. Could you just give an update on the MRO market and the trends you're seeing there, I mean you mentioned that your big Pros were outpacing small Pros, so with MRO growth even above that of those big Pros given relatively easier comparisons against last year?

A - Craig Menear {BIO 15126612 <GO>}

Liz, we're very pleased actually with our MRO business and the acquisition of HD Supply. Yeah, the business there is very, very solid. What we're excited about candidly with that business is the opportunity to much better serve 50 million households in the multi-family space. Not only can we serve them with MRO products, but obviously as we have relationships and build that through our MRO business, the opportunity to then participate in capital refreshes for those property owners on those 50 million households that are in the multi-family is a huge opportunity for Home Depot going forward. So we're super pleased with the business and the progress that we're making there.

Q - Liz Suzuki {BIO 16142563 <GO>}

Great. And I'm just checking on to Zack's question a little bit, I mean it may be early to be thinking about this, how are you approaching the holiday season this year from a procurement standpoint and a promotional standpoint, should we expect it to look more like last year or marketing started early and extended longer, but promotions were bit shallower than a normal year, do you think it will go back to kind of a shorter and deeper promotional cadence like pre-pandemic seasons?

A - Ted Decker {BIO 16614891 <GO>}

Well, Liz, as you can imagine with the international supply chain involved in those types of events, the merchants and supply chain teams made the bulk of those buy decision some time ago. So it's a fixed buy, we're not expecting huge growth in those programs, but to your point it's deeper buys, stronger values, fewer items and we think we have great programs. In terms of marketing early, I think we're going to follow all our normal trends, we had a sneak peak of opening up Halloween online and just sold out our sort of pre-release Halloween product almost immediately. So that's a very strong indication that people are still going to engage in decorating and we look forward to setting our decorative holiday later in October.

Q - Liz Suzuki {BIO 16142563 <GO>}

Great, thank you.

Operator

Our next question comes from the line of Christopher Horvers with J.P. Morgan. Please proceed with your question.

Q - Chris Horvers {BIO 7499419 <GO>}

Thanks, good morning everybody. It's been long time since the weather was a potential question, but during the second quarter do you think it was a net headwind the major DIY holidays had record rain in some of the northern geographies and so was it beyond just the effect of 1Q versus 2Q?

A - Craig Menear {BIO 15126612 <GO>}

I wouldn't say it was beyond it, but we certainly saw it. So we think that it may have accounted for low single-digit comp impact call 1 to 200 basis points of comp, a pull-forward from Q1, sorry from Q2 into Q1 particularly in the Northern division. So as Craig called out, while we did see a difference in regional performance that really was the primary driver in our view.

Q - Chris Horvers {BIO 7499419 <GO>}

Got it. And then on the lumber side as prices stand now, would lumber be a modest headwind comp for the balance of the year? And is that reflected in the quarter-to-date commentary?

A - Ted Decker {BIO 16614891 <GO>}

So yeah, lumber just the market pricing of lumber, Chris, right now framing is approaching 40% under LY in panel is 10% under LY. So neutral units, there would be a negative comp impact, as I said unit progression is going in the right direction with these lower prices and that all speaks to project nature, but from a price perspective not expecting any tailwind in lumber.

Q - Chris Horvers {BIO 7499419 <GO>}

Got it. And then the last question, Richard, as you think about how transportation costs I assume some of that gets hung up in inventory. So do you think the transportation cost pressure actually gets worse as you look in the back half? So as much as the rate pressure from lumber doesn't repeat itself, you could have higher transportation cost pressures on gross margin?

A - Richard McPhail {BIO 19175260 <GO>}

You know, the back half is a long period of time, I'm not going to speculate on what transportation cost might look like. I'll just tell you that I would bet on our team every single day to be able to manage through that dynamic. Our supply chain team is exceptional and creative and I think that they have reinforced our position as the low cost provider in the market. So regardless of where the market goes, I think we'll be in advantaged position.

Q - Chris Horvers {BIO 7499419 <GO>}

I'm sorry, one last quick one. In July, how would you characterize sort of the competitive promotional environment, there are some questions out there that maybe some of your competitors got more promotional, although it was for you just more of a comparison to a low level last year?

A - Craig Menear {BIO 15126612 <GO>}

Did you see anything majorly different?

A - Ted Decker {BIO 16614891 <GO>}

Didn't notice that much, Chris.

Q - Chris Horvers {BIO 7499419 <GO>}

Got it. Thanks so much. Best of luck.

A - Ted Decker {BIO 16614891 <GO>}

Thank you.

Operator

Our next question comes from the line of Kate McShane with Goldman Sachs. Please proceed with your question.

Q - Kate McShane {BIO 7542899 <GO>}

Hi, good morning. Thanks for taking my question. Just a couple of housekeeping type questions. I wondered if you could address at all the trend of trading up by the customer that was something you continue to see during the quarter. And any commentary you can give specifically around appliances and what you saw in Q2?

A - Ted Decker {BIO 16614891 <GO>}

I would say yes, we continue to see the trading up, it's not as clear as I used to report on it, just because of the inventory situation, we're seeing lots of substitution of goods depending on what's in stock on the shelf that particular day. But if you look at power tools for example, outdoor power equipment, the appliance category, grill category, riding lawn mower and zero turn category, just as a few examples, Kate, people are trading up to innovation in all those categories. So just more powerful longer run time on batteries that's moving over to outdoor power equipment, the design esthetic and the features of modern appliances, people are happily trading up to quite strong price points in appliances, LED lighting it's going through, not just slight balls, but integrated in ceiling fans and fixtures that trade up is innovation and newness driven and we are seeing that as strong as ever.

Operator

Does that complete your question?

Q - Kate McShane {BIO 7542899 <GO>}

Yeah, sorry. Thank you.

Operator

Our next question comes from the line of Greg Melich with Evercore. Please proceed with your question.

Q - Greg Melich {BIO 1507344 <GO>}

Hey, thanks. Had a follow-up on comps and then SG&A, I guess I'd start with SG&A. So you had 100 bps of leverage in the first half and you guys talked about getting back to leveraging the way that Home Depot did in the past. Should we expect the second half to have similar type leverage or is there something unique about what happened last year that means that would be less?

A - Craig Menear {BIO 15126612 <GO>}

Well, Greg, 2020 was such a unique year and comparisons from 2021 to 2020 are difficult for a number of factors, you think about the amount of COVID expense that we -- that we put in place in support of our associates last year, you think about expense underspend as we worked to bring staffing up to levels to meet demand. And then you think about the wage investment that we made towards the end of 2020, all these make comparisons difficult. We are committed to generating operating expense leverage over the long-term.

We feel great about the operating expense leverage that we delivered in Q2 and in the first half. You're always going to see fluctuations quarter-to-quarter, leverage is a function of top line sales, it can be a function of seasonality and other factors. So in any given quarter, you may see volatility, but over a period of quarters you're going to see from us operating expense leverage. And again, we're very happy with how the quarter in the half played out.

Q - Greg Melich {BIO 1507344 <GO>}

And my follow-up may be linked to that is on comps. So if the trend I just want to make sure I got it right, if the trend is similar in the second quarter, but there is no inflation in lumber, is it fair to say that that two-year comp is stable in the mid 20s without inflation, am I interpreting that correct?

A - Ted Decker {BIO 16614891 <GO>}

Well, two-year comp is sort of similar in its consistency to one-year comp in the first couple of weeks of the month.

Q - Greg Melich {BIO 1507344 <GO>}

Got it. All right. Appreciate it, thanks a lot and good luck.

A - Ted Decker {BIO 16614891 <GO>}

Thanks, Greg.

Operator

Our next question comes from the line of David Belanger with Wolfe Research. Please proceed with your question.

Q - David Belanger {BIO 17201127 <GO>}

Hey, good morning and thanks for taking my question. I want to ask in regard to first supply chain, so you alluded in the prepared comments working through a difficult environment. So, are you seeing incremental pressures now versus just a few months ago, is there some level of sales that you missed out on in the Q2 period? And maybe a bigger picture question, through all the recent supply chain issues across the industry, is there anything now that you're reevaluating or making some type of change within the One Home Depot build out?

A - Craig Menear {BIO 15126612 <GO>}

Yeah, I'd say the first comment that I have is, as it relates to the potential sales impact really, really hard to tell. And the reason it's so hard to get a gauge on that is the fact that there is a high level of willingness of substitution on the customer's part since this pandemic began, much more so than pre-pandemic. Is there some level of impact? The logic tells you there probably was, but it's really hard to gauge and we think we captured most as a result of substitution.

Q - David Belanger {BIO 17201127 <GO>}

And then any change in regard to you are the larger build-out plans of One Home Depot?

A - Craig Menear {BIO 15126612 <GO>}

No, not at all, no, we're -- that build, I'm sorry that build out is focused on where the customer has taken us and how they want to engage with The Home Depot. So it has no impact at all.

Q - David Belanger {BIO 17201127 <GO>}

Got it. And just my follow-up, you mentioned a new exclusive relationship with LP Building Solutions. Can you expand upon that any further, does that reflect some type of shift in the business where maybe you lean more into Pros tied to more new home construction is the next level of Pro sales growth just give the company more exposure on the new home construction side. Can you just expand upon that any further?

A - Ted Decker {BIO 16614891 <GO>}

No, I mean the intent was not to be any different position in regards to new home construction. It's not a market we play in or consciously go after. LP is similar to what we did last quarter with Carlon electrical boxes, there is -- as Carlon is the largest provider particularly for the Pro in PVC electrical boxes, LP is one of the top couple OSB providers very strong brand. And this is a matter The Home Depot making arrangements with top suppliers, so that they can focus their supply chain into serving us and we can focus on having that depth of inventory in these critical Pro categories on our shelves. So the likes of exclusives with Carlon and LP is all about taking care of our Pro customer.

Q - David Belanger {BIO 17201127 <GO>}

Got it. Appreciate the color.

Operator

Our next question comes from the line of Laura Champine with Loop Capital. Please proceed with your question.

Q - Laura Champine {BIO 4748805 <GO>}

Thanks for taking my question. I just wanted to get some context around the commentary that you should be able to lap the difficult comparisons given the strong macro drivers in home prices and comparing that to the outcome in Q2 of transactions that were down, is the thought there that the transactions were down largely because of lumber inflation and another sort of one-time issues in the transaction should tick back up as we move through the rest of this year and next?

A - Craig Menear {BIO 15126612 <GO>}

Laura, first comment would be, we didn't really provide any outlook going forward. We don't believe we can take past performance and project that forward due to the uncertainty in the environment that exist today. As it relates to the transactions, I mean huge transactions last year as a result of PPE. Ted, I don't know if you want to comment?

A - Ted Decker {BIO 16614891 <GO>}

Yeah, I mean that was one of our single biggest drivers of the fall-off is people coming in for masks and hand sanitizers and the four departments that we did see negative sales hardware, outdoor and indoor garden and paint, those are can tend to be more consumer oriented, lots of units in mulch and soil and things in paint is that DIY wire was home not doing other activities on the weekends.

So we're not alarmed by that fall off at all, we'll get through that, I'd say that take a category like paint. In paint had been a one or two unit grower for several years up until the pandemic. And painting is one of the initial home improvement projects that a customer engages in and starts to build confidence in home improvement. And while we saw a dip in Q2 the levels in unit volume that we're seeing in paint is well above 2019 and I've talked about the millennials before and the millennials are engaged in housing, they are engaging in home improvement, they've done that first project which is painting and some gardening work generally. So we're just thrilled that they're engaged in the category and moving on to bigger projects.

Q - Laura Champine {BIO 4748805 <GO>}

Got it. And then as a follow-on, do we have a better sense now on where digital should be in terms of a longer-term sustainable growth rate and/or as a percentage of sales hopefully things are settling out there?

A - Craig Menear {BIO 15126612 <GO>}

I mean we really look at this as an interconnected experience. Our customers are clearly blending the physical and digital worlds together because of the project nature of our business. Certainly from pre-pandemic levels, we've seen an accelerated rate of engagement in terms of sales through our digital channels, but that's not how we focus on that or look at it, we view it as a capability for our customer to engage with The Home Depot.

Q - Laura Champine {BIO 4748805 <GO>}

Got it. Thank you.

A - Isabel Janci {BIO 16473072 <GO>}

Christine, we have time for one more question.

Operator

Thank you. Our final question comes from the line of Eric Bosshard with Cleveland Research. Please proceed with your question.

Q - Eric Bosshard {BIO 1647410 <GO>}

Thanks. Two things. First of all, perhaps for Richard, some clarity on lumber, you talk about leading on the way down with price to do what's best for the customer, does that necessitate more gross margin pressure from lumber in 3Q or am I thinking about that wrong?

A - Richard McPhail {BIO 19175260 <GO>}

By and large the pressure from lumber at least what the prices we've seen in the market have been recognized to date. So no, now it depends on future lumber price, right? But at the moment the precipitous decline had its impact in Q2 for the most part.

A - Craig Menear {BIO 15126612 <GO>}

Yeah, Eric, the key for that normally you don't see any pressure from gross margin as a result of lumber, it's all because of mix. The reason that we thought this time was the steep decline that happened in price in a very compressed timeframe. And again we weren't going to change our approach to the market, we want to be incredibly focused on driving the best value for our customer. So we always try to lag the market when it's going up and lead it when it's coming down.

Q - Eric Bosshard {BIO 1647410 <GO>}

Perfect. That makes sense. And then secondly, the sales growth over the last couple of years now is exceptional like you pointed out, you've obviously invested to take care of your associates and take care of your customers, the margin leverage has been less than what we would have expected with nearly a $50 billion 50% increase in sales in the last three years. Is there some embedded operating margin improvement that can get released over the next couple of years if things return to normal or is the cost of doing business and other investments you've made taken some of that away, trying to figure out if the operating margin of the enterprise could lift incrementally in the next couple of years or it's more of the focus is on sales growth and a little bit less on releasing operating margin?

A - Richard McPhail {BIO 19175260 <GO>}

I think so -- I think that we have to go back to the central focus that we have from a financial performance perspective, which is growing operating profit dollars as fast as possible and generating an exceptional return on investment on those dollars. And so we feel very pleased with the market share that we've captured over the last three to four years and we feel exceptionally pleased with the shareholder value that we've created as well. We think that the formula of having the best experience in home improvement retail, being the lowest cost provider and being the best investor of capital in the market is a formula that can't be beat and that's what we're going to continue to do.

Q - Eric Bosshard {BIO 1647410 <GO>}

Great. Thank you very much.

A - Richard McPhail {BIO 19175260 <GO>}

Thank you.

Operator

Ms. Janci, I would now like to turn the floor back over to you for closing comments.

A - Isabel Janci {BIO 16473072 <GO>}

Thanks, Christine and thank you everyone for joining us today. We look forward to speaking with you on our third quarter earnings call in November.

Operator

This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation and have a wonderful day.