Speaker 12
0s

Good morning, everyone. Welcome to Lowe's Company's third quarter 2025 earnings conference call. My name is Rob, and I'll be your operator for today's call. As a reminder, this conference is being recorded. I'll now turn the call over to Kate Perlman, Vice President of Investor Relations and Treasurer.

Speaker 8
17s

Thank you, and good morning. Here with me today are Marvin Ellison, Chairman and Chief Executive Officer; Bill Boltz, our Executive Vice President, Merchandising; Joe McFarland, our Executive Vice President, Stores; and Brandon Sink, our Executive Vice President and Chief Financial Officer. I would like to remind you that our notice regarding forward-looking statements is included in our press release this morning, which can be found on Lowe's Investor Relations website. During this call, we will be making comments that are forward-looking, including our expectations for fiscal 2025. Actual results may differ materially from those expressed or implied as a result of various risks, uncertainties, and important factors, including those discussed in the risk factors, MD&A, and other sections of our annual report on Form 10-K and our other SEC filings. Additionally, we'll be discussing certain non-GAAP financial measures. A reconciliation of these items to US GAAP can be found on the quarterly earnings section of our Investor Relations website. Now, I'll turn the call over to Marvin.

Speaker 7
1m 14s

Thank you, Kate, and good morning, everyone, and thank you for joining us today. Third quarter sales were $20.8 billion, with comparable sales increasing 0.4% year over year, despite a roughly 100 basis point headwind related to Hurricanes Helene and Milton. During the quarter, adjusted operating margin expanded approximately 10 basis points, leading to adjusted diluted earnings per share of $3.06, which is an increase of 6% versus last year. These results reflect continued operational discipline and strong execution across our Perpetual Productivity Improvement, or PPI, initiatives. Although sales results continue to be impacted by softer demand within an uncertain macro environment, we're encouraged to see improvement in DIY customer engagement and discretionary projects across many areas of the home. We're also pleased with our performance in the North and West divisions, which were not affected by storms in the prior year. We are seeing strength across all five key initiatives within our 2025 Total Home Strategy, which we launched at our Analysts and Investors Conference last year. Let me give you an update on the performance of our Total Home Strategy, beginning with the small to medium pro, where we once again delivered growth this quarter. We are enhancing our pro offering through our Pro Extended Aisle, which is a direct interface with our supplier systems.

Speaker 7
2m 46s

It allows our pro sales associates to sell directly from their product catalogs, with the suppliers opting for filling the orders directly to the job site. This expands our product assortment, inventory quantities, and delivery capabilities for larger orders. Second, when it comes to accelerating online sales, we delivered online sales growth of 11.4% this quarter, driven by increased traffic and continued strong conversion. We're also continuing to enhance the online experience across lowes.com and our mobile app to make it simpler and faster for DIY and pro customers to find all the products they need. Looking ahead, we're pleased with the ongoing build-out of our marketplace. This allows us to expand our product assortment to offer our customers everything they need for their homes across the price spectrum, from value to premium, without assuming the risk of owning the inventory. Third, we're leveraging our loyalty ecosystem to increase our customer preferences for Lowe's, so they choose us first and shop more often. In fact, our 30 million Milo's Rewards members shop twice as often and spend over 50% more than non-members. Through both our DIY and pro loyalty programs, we're gaining deeper customer insights, which help us tailor more personalized, value-enhancing offers through data-driven marketing.

Speaker 7
4m 13s

Fourth, we're really pleased with the strong results this quarter in home services, where we delivered double-digit comps. Later in the call, Joe will discuss the initiatives that are driving these gains. The fifth and final initiative in our total home strategy is increasing space productivity. We made great progress optimizing our selling space, and Bill will provide details on a couple of key initiatives later in the call. Overall, I'm very pleased with the progress that we have delivered through our total home strategy and the strategic alignment we're driving across the organization. Let me now discuss the importance of generative AI to improve how we sell, how we shop, and how we work. This is what we refer to as our AI framework. As we continue to make strategic investments in our AI capabilities, we're already seeing tangible results. Our virtual assistants, Milo and Milo Companion, which are built on an OpenAI platform, are answering nearly one million questions per month about everything from product specs to project know-how to the status of a customer order. In fact, when our customers engage with Milo online, the conversion rate more than doubles, which is clear evidence that AI is simplifying decision-making and driving sales.

Speaker 7
5m 32s

When our associates use Milo Companion to help customers shopping in our stores, we are seeing customer satisfaction scores increase 200 basis points. Every interaction with our virtual assistant is feeding our proprietary models, allowing us to continually improve accuracy and build a durable advantage in home improvement expertise. Within our technology team, engineers are using AI tools for development and code review, leading to double-digit productivity gains and accelerating our speed to market. In fact, Lowe's has just been recognized by OpenAI with their 100 billion token milestone award, as a reflection of the depth and breadth of AI adoption throughout the organization. Achieving this milestone places Lowe's in an elite tier of companies that are not just experimenting with AI, but operating at a true enterprise scale. Looking ahead, we have a detailed roadmap of several additional high-impact AI initiatives that will drive further enhancements to the pro and DIY customer experience, both in store and online. This will include our participation in organic commerce, so we can continue to meet our customers where and how they choose to shop. We also anticipate incremental productivity gains as we leverage AI to drive operating efficiency across the enterprise. Now, let me turn to our acquisition of Foundation Building Materials, or FBM, which we completed in October.

Speaker 7
7m 3s

I'd like to begin by extending a warm welcome to the entire FBM team. As a reminder, FBM is a leading distributor in interior building products, including drywall, metal framing, insulation, and ceiling systems. FBM's business mixes balance evenly between commercial and residential. While the housing market is currently under some pressure, we're pleased with the momentum we're seeing with FBM's commercial sales. Some recent highlights include several data center projects, a luxury 150-unit residential high-rise, and medical facilities. FBM leverages its strong reputation for reliability and technical expertise to win these contracts. When we consider the impact to Lowe's, this acquisition gives us a more comprehensive product portfolio, expands our revenue streams, and further enhances our offering to our pro customers. In fact, efforts are already underway to quickly connect FBM's product catalog to our Pro Extended Aisle. FBM customers will gain access to Lowe's complementary products like tools, safety gear, and fasteners, so they can more quickly and conveniently source everything they need for their jobs. FBM's 370 locations nationwide also strengthens our fulfillment capabilities, especially in high-density urban markets in California, the Northeast, and the Midwest, where Lowe's has less of a physical store presence. Our acquisition of FBM and Artisan Design Group, or ADG, creates comprehensive interior solutions for our home builders, with everything from drywall and insulation to doors, flooring, cabinets, and appliances.

Speaker 7
8m 48s

I look forward to updating you on the progress we're making with both acquisitions in the future. Now, let me transition to our view of the macro environment. Overall, the U.S. home owner remains healthy. Balance sheets are strong, and consumers continue to spend. However, affordability and uncertainty in the broader economy continue to weigh on consumer confidence, particularly when it comes to larger discretionary purchases, as borrowing costs have been elevated for longer than originally anticipated. Looking ahead, lower interest rates, including for home equity loans, could begin to spur demand, even as many homeowners remain reluctant to move and give up their historically low mortgage rates. This cycle is different from past housing slowdowns in a few important ways. First, homeowners today have record levels of equity, roughly $400,000 on average. At the same time, they are more likely to invest in the home they already own instead of giving up the low mortgage rate. This is referred to as the lock-in effect and could make home equity financing a more attractive solution. While the near-term macro backdrop reflects an anxious consumer, the combination of strong fundamentals, substantial home equity, and the potential for lower rates ahead gives us confidence in the long-term health of the home improvement sector.

Speaker 7
10m 12s

We remain confident that the continued execution of our total home strategy will position Lowe's to win in the short and in the long term. Before I close, I'd like to wish all of our associates a blessed and safe holiday season. Our associates are our competitive advantage, and I appreciate all they do to make Lowe's a great company. With that, I'll turn the call over to Bill.

Speaker 5
10m 33s

Thanks, Marvin, and good morning. This quarter, we delivered positive comps in 10 of our 14 merchandise divisions and solid performance across both DIY and pro, despite lapping hurricane activity last year. Starting with home decor, we delivered positive comps in appliances, flooring, paint, and kitchens and bath. We continue to strengthen our leadership position in appliances by providing customers with a value proposition that no other retailer in the industry can match. This includes the widest assortment of top brands and innovative products, all at a must-win price point. By leveraging our market delivery network, we are the only retailer who can deliver and install major appliances in virtually every zip code in the US next day. This capability is crucial for items like refrigerators or washing machines that often need to be replaced immediately. One example of our innovative product offering is an exclusive new Bosch hybrid tub dishwasher line, available only at Lowe's. These models combine the quiet operation Bosch is known for, along with the durability of stainless steel and the affordability of polymer. The result is a better, cleaner, and a better value with the most accessible price points in the industry. Turning to flooring, we saw a broad base strength across soft surfaces, vinyl, and tile flooring.

Speaker 5
11m 57s

In carpet, customers are enthusiastic about the benefits of StainMaster Pet Protect. Its leak defense backing helps prevent spills and pet accidents from seeping into the carpet pad or subfloor. StainMaster is the most trusted brand in carpet, and it is exclusive to Lowe's. Touching on paint, we drove broad-based growth across stains, primers, and paint, along with accessories and applicators. We are excited to announce the launch of Sherwin-Williams Pro Block Quick Dry Primers, an innovative product that blocks stains and provides outstanding coverage and dries in less than an hour. This new primer is available only at Lowe's and Sherwin-Williams locations, marking the first time that we have co-launched a product. This product provides Lowe's with true differentiation within the home center channel as we continue to build on our strong relationship with this key supplier. Lastly, in kitchens and bath, we recently completed a reset of our bathroom vanity showrooms, and these new sets are delivering results ahead of our expectations. The updated showroom provides a much better shopping experience for both pro and DIY customers because they can now see and interact with a larger number of products. The stock products are now much more accessible and readily available for quick take with.

Speaker 5
13m 17s

This is an important way we're driving space productivity and leveraging our larger stores as a competitive advantage. Turning now to building products, we drove positive comps across millwork, rough plumbing, lumber, and electrical. We're supplementing our already robust in-store pro offering in building products with our Pro Extended Aisle. As Marvin mentioned, this initiative expands our product offering, increases our inventory depth, and enhances our delivery capabilities. In millwork and rough plumbing, we've seen strong performance driven by higher installation sales and home services, which Joe will discuss shortly. Millwork is another area where we're seeing innovation, like the Larsen 60 MT Storm Door, with magnetic technology that keeps the door closed. It offers both performance and curb appeal, and it gives customers a reason to upgrade. Turning to hard lines, we delivered positive comps in lawn and garden with particular strength in live goods and hardscapes. Customers were inspired by the outdoor vignettes that showcased everything they needed to build their vertical gardens, along with upgrading a mailbox display and more. The mild weather gave customers more opportunities to tackle more outdoor projects, which helped drive extended demand. We're also pleased with a strong start to the holiday season in our tools, trimmetry, and decor categories.

Speaker 5
14m 40s

Shifting gears to tools, where we also delivered positive comps, we saw strong performance in hand tools and tool storage. Customers responded to our value offerings and improved assortments like the Cobalt 46-inch workstation available in a wide range of colors. During the quarter, we leaned into value and drove strong online engagement during our DeWalt Days event, supported by a homepage takeover and a compelling free tools battery offer. Now, let me give you an update on one of our key Total Home Strategy initiatives, increasing space productivity, which is all about driving incremental sales opportunities by optimizing our sales footprint. This quarter, we completed the rollout of our rural format in 150 additional stores, bringing the total to nearly 500. We're also on track to complete rollouts of workwear and pet to more than 1,000 stores, giving us an opportunity to drive these assortments beyond our rural stores. In line with our pet expansion, which is focused on grab-and-go items like toys and treats, we're pleased to announce our new private brand, Heart & Herd. It offers pet owners high-quality, value-priced products for dogs and cats just in time for holiday gifting. As part of our space productivity efforts, we've made significant progress on our SKU rationalization initiative, designed to improve our inventory productivity.

Speaker 5
16m 5s

By the end of 2025, we're set to achieve our multi-year goal of reducing our in-store SKU count by 15%. As we head into the holiday season, we're delivering new, exciting products both in-store and online through our Black Friday build-up event. We're giving customers an early start on their holiday shopping with great deals, including several that are already available now. In closing, I'd like to thank our merchants, inventory and supply chain teams, along with our MST associates and our supplier partners for their continued efforts to deliver results for our customers ahead of the busy holiday season. Now, I'll turn the call over to Joe.

Speaker 13
16m 45s

Thank you, Bill. Good morning, everyone. Let me begin by recognizing our store and supply chain associates who show up every day with energy and commitment to serve our customers. Quarter after quarter, through changes and challenges, they've proven themselves to be our company's greatest asset. That is why I'm particularly pleased to share that the investments we're making to support our frontline associates are truly paying off. New training programs are better equipping our store teams to sell complete customer projects, including featured seasonal products and services. By enabling our associates to deliver more comprehensive solutions, these programs are boosting their knowledge, confidence, and effectiveness at driving sales. As Marvin mentioned, they can also rely on our AI-powered Milo Companion for product details and for help answering customers' questions. Add it all up, and we're empowering our associates with the tools they need to sell more effectively across all departments in the store. Additionally, a few weeks ago, we concluded our associate annual engagement survey, a critical component of our proactive listening strategy, which supports our efforts to become the employer of choice in retail. Scores across the key measures of engagement and associate well-being, as well as leadership effectiveness, have all continued to improve, and our 95% participation rate continues to be industry-leading.

Speaker 13
18m 12s

All told, our better-trained and highly engaged associates are elevating the Lowe's shopping experience, which is reflected in improved customer satisfaction scores for both the DIY and pro. To focus now on the pro, enrollments in our MyLowe's Pro Rewards program continue to grow as our core small to medium pro customers experience firsthand the benefits of our easier-to-use loyalty platform, which allows them to start earning rewards immediately and achieve higher rewards with lower levels of spending. We're also pleased to see pros taking advantage of our enhanced digital capabilities as they shift to more shopping online. Looking ahead, we're encouraged that our recent pro survey overall sentiment improved for small to medium pros as they remain confident in their job prospects and report stable backlogs. Shifting now to performance in home services this quarter, we're pleased with our double-digit growth in this key initiative within our Total Home Strategy. The team delivered broad-based strength across a number of product categories, including windows and doors, HVAC, water heaters, kitchens and bath, and window treatments. These strong results were driven in part by tech-enabled solutions, which have enhanced the experience of customers, installers, and associates alike. For our customers, we've accelerated the process from inquiry to completed installation by providing intuitive solutions for scheduling, quoting, and payment.

Speaker 13
19m 44s

These enhancements have transformed what was a time-consuming process by removing friction and pain points along the customer journey. Turning now to our focus on operating efficiency, I'd like to thank our asset protection teams for continuing to deliver one of the best inventory shrink results in big box retail. Despite the challenging environment, these results are driven by a combination of outstanding leadership and industry-leading technology. We also focused this year on a number of perpetual productivity improvements, or PPI, initiatives in our stores, including our front-end transformation, streamlining our BOPUS fulfillment, and the freight flow optimization. We are already working on our PPI roadmap for 2026 for store operations as we leverage AI-enabled solutions to further enhance the customer experience while also driving labor productivity. Before I close, let me take a moment to discuss one of our new initiatives to support veterans as part of our long-standing commitment to the military community and in support of our objective to deliver 10 million sq ft of impact in 2025. As a Marine who served in combat, I'm particularly proud to share that in partnership with Building Homes for Heroes and our hometown of Mooresville, North Carolina, we have just broken ground on Freedom Hill.

Speaker 13
21m 4s

This first-of-its-kind community will provide mortgage-free housing and support services for up to 15 households of injured veterans and first responders. As the executive sponsor of Lowe's philanthropic support of our military communities, it will be an honor for me to see lives changed through this initiative. With that, let me turn the call over to Brandon.

Speaker 14
21m 25s

Thank you, Joe, and good morning. Starting with our third quarter results, we generated GAAP-diluted earnings per share of $2.88. In the quarter, we closed on our acquisition of Foundation Building Materials, or FBM. We recognized $105 million in pre-tax transaction costs, including the fees associated with $9 billion in bridge financing. To finance the $8.8 billion purchase price, we issued $5 billion of bonds with a competitive weighted average coupon of 4.38% and borrowed $2 billion under a three-year term loan. Given our better-than-expected cash flow generation, we financed the remaining $1.8 billion with cash on hand. We also recognized $24 million in non-GAAP adjustments associated with Artisan Design Group, or ADG. Keep in mind that in the third quarter of last year, we recorded a pre-tax gain of $54 million associated with the 2022 sale of our Canadian retail business. Excluding these impacts, we delivered adjusted diluted earnings per share of $3.06, exceeding our expectations. This is a 6% increase compared to adjusted diluted earnings per share in the prior year quarter. My comments from this point forward will include certain non-GAAP comparisons that exclude these impacts where applicable. Third quarter sales were $20.8 billion, with comparable sales up 0.4%, driven by DIY engagement across project-related categories, as well as another quarter of growth in pro, online, and appliances.

Speaker 14
23m 10s

As Marvin mentioned, we also lapped storm-related demand, which was a roughly 100 basis point headwind to sales this quarter. While we continue to manage through an uncertain macro environment, we are pleased that we delivered positive comps in 10 of 14 product categories. Monthly comps were up 2.5% in August, up 0.9% in September, and down 2.6% in October when storm-related demand was most concentrated last year. For the quarter, comparable average ticket increased 3.4%, driven by ongoing strength in pro and appliances, mixed shift into larger ticket purchases, and modest price increases, while comparable transactions declined 3%. Gross margin was 34.2% in the quarter, up 50 basis points as we cycle a number of storm-related pressures in the prior year. We also saw improvements in credit revenue and better sell-through of inventory as we drive our SKU rationalization efforts. Adjusted SG&A was 19.6% of sales, deleveraging 36 basis points as we cycled lower bonus attainment in the prior year and also invested in sales-driving actions. Adjusted operating margin rate of 12.4% was up 10 basis points versus prior year, and the adjusted effective tax rate of 24% was in line with prior year results. Inventory ended Q3 at $17.2 billion, down approximately $400 million versus prior year.

Speaker 14
24m 51s

This net decrease also reflects the inclusion of inventory from recent acquisitions of approximately $600 million and higher tariffs. These results were driven by several inventory productivity initiatives across the company as we leverage advanced AI inventory solutions to enhance our demand planning, allocation, and replenishment, while also driving our SKU rationalization efforts. ADG operating results were accretive to EPS on a non-GAAP basis for the third quarter and pressured operating margin by approximately 15 basis points, in line with expectations. Turning now to capital allocation. In Q3, we generated $687 million in operating cash flow, inclusive of the payment of federal and state taxes of roughly $900 million that had been deferred under a provision related to Hurricane Helene. Capital expenditures totaled $597 million as we continue to invest in our strategic growth imperatives. In the quarter, we paid $673 million in dividends at $1.20 per share. Adjusted debt to EBITDA was 3.36 times at the end of the quarter after we repaid $1.75 billion in debt maturities and borrowed $7 billion to finance the acquisition of FBM. The structure of this financing, in conjunction with the timing of our existing bond maturities, will allow for steady deleverage to our 2.75 times target, which is expected by mid-2027.

Speaker 14
26m 26s

We ended the quarter with $621 million of cash and cash equivalents and delivered a return on invested capital of 26.1%. Turning to our financial outlook, which we are updating to include our year-to-date results and our expectations for FBM. We are seeing a cautious consumer amid ongoing uncertainty in the macro environment, and the timing of an inflection in the home improvement and housing markets remains unclear. We're now expecting comp sales to be roughly flat for the year, which is at the bottom end of our previous guidance. When we include FBM sales of approximately $1.3 billion in the fourth quarter, we are expecting sales of approximately $86 billion for the year. We also now expect full-year adjusted operating margin of approximately 12.1%, which includes 20 basis points of dilution from FBM and ADG. We're expecting adjusted diluted earnings per share of approximately $12.25, which represents a 2% growth over the prior year. Please note that this includes the impact of FBM, which is roughly neutral to adjusted EPS, and we expect capital expenditures of up to $2.5 billion for the year. On an annualized basis, we expect FBM and ADG to negatively impact consolidated adjusted operating margin by approximately 50 basis points.

Speaker 14
28m 3s

We are already working collaboratively with the FBM and ADG teams on cross-selling opportunities as we expand the offering for our pro customers. We have also begun the efforts to extract cost synergies from our overlapping areas of spend. Taken together, we remain confident that there are compelling long-term EBITDA synergies from both revenue growth and lower operating expense. These investments in our pro growth initiative, along with the other investments in our total home strategy, will position us to capitalize on the expected recovery in housing and home improvement and continue to deliver long-term sales growth and shareholder value. With that, we will open it up for your questions.

Speaker 12
28m 50s

Thank you. We are now ready for questions. If you'd like to ask a question, press star one on your telephone keypad. To withdraw your question, press star two. In order to allow us questions from as many individuals as possible, please limit yourself to one question and one follow-up. Our first question comes from the line of Chris Horvers with JP Morgan. Please proceed with your question.

Speaker 2
29m 12s

Thanks, and good morning. My first question is about just how you're thinking about the trend in the business in light of the performance that you've seen over the past six months and a harder compare and then into 2026. You noted that quarter-to-date is positive. Is there anything you could elaborate on that? Is the flat guide for the fourth quarter simply just like, "Hey, there's uncertainty and there's a harder compare"? As you think to 2026, if the home improvement market is flat to slightly down this year and you're putting up a flat comp, if you take a look at the sum total of everything, a little bit of lower rates, a little bit of replacement cycle, a little bit of innovation in what you're doing on the self-help side, should the market and should Lowe's comp accelerate in 2026 relative to 2025?

Speaker 7
30m 16s

Hey, Chris, this is Marvin. Bill and I will talk about November, then we'll let Brandon share a tiny bit about how we think about '26 because, as you can respect, we're not going to get into a ton of detail about that until our February call where we'll provide guidance for the year. Relative to November, look, we're very pleased with the positive comp performance to start the quarter in spite of storm overlaps from last year. We've seen improvements in the top line since exiting October, and we just believe that some of the key elements of our total home strategy are working. We're excited about November because there's some great things untapped. I'm going to let Bill talk a bit about November, but also talk about appliances, which we think is really key to our performance, not only for the quarter, but what we're seeing in November.

Speaker 14
31m 11s

Yeah. Thanks, Marvin. Chris, we're excited about kind of the early start to the quarter, obviously, coming off of October. Strength for us, really broad-based across the store, but particular strength within our seasonal categories, holiday, trimmetry, tools, appliances, and other gift-related businesses that are getting off to an early start. Our stores look great. We're starting to see live trees show up now. Poinsettias showing up now as we get ready for next week. We're seeing some early excitement around some key areas of the store. Whether it's buy now and install by the holidays within our flooring and cooking areas, or you look at Cobalt and some of the strength that we're seeing there with some new products in workstations, the buy-and-get offers within our tool business driven by DeWalt, Craftsman, Cobalt. We've got just a lot of strength going on right now that we'll carry into next week with Black Friday. We are excited about how things are progressing. In our appliance business, we've had, really since last year, four straight quarters now of comp growth and unit growth, which is telling us the health of that business and that consumer responding to the offers and the innovation and the new products that the team has put out there.

Speaker 7
32m 23s

Chris, this is Brandon. I think when I step back and look at the totality of the year, we're now three quarters of the way through, obviously navigating a lot of factors, a very choppy macro. When I look at just the trends of the business, I think a lot for us to be cautiously optimistic about as we look ahead to 2026. We're seeing acceleration on one-year comps when you exclude storm-related activity for Q3 and what's implied in our Q4. Also, two-year comps accelerating nicely as we've moved through the year. Ongoing strength in pro online. Bill just spoke to appliances. Some early signs of life in our home services business, which is really positive. We cited broad-based performance across categories with 10 of 14 categories, geographies broad-based. Really excited about FBM and ADG as we start the integration efforts. Obviously, just really pleased with the bottom-line performance and the ongoing operational discipline that the company has been able to show. Pleased through three quarters. As we look ahead into 2026, as Marvin mentioned, we'll have more to come in February, but those are early thoughts.

Speaker 2
33m 35s

On a related question, I mean, kitchen and bath, I think you said it was positive. Looking back, it seems like you'd have to go all the way back to 1Q 2023. What's changed there? As you think about it, Marvin, you've talked about we have a lot of big ticket. We have a lot of remodel, the kitchen and bath, the appliances, and we sort of need lower rates to improve that sort of big-ticket remodel category. You are seeing signs of life. Is there sort of a misperception around sort of how remodel-oriented you are amongst investors, or how do you think about maybe that category showing signs that it will inflect to the positive?

Speaker 7
34m 19s

Chris, I think it's two things. I'll take the first part and I'll let Bill just talk about some of the work in resets and new products. I really believe that this is more about Lowe's taking share in this space. If you can go back to 2018 at our first analyst and investor conference, I presented how we were managing this install business with binders and whiteboards. It's taken us a while, candidly, to get this business digitized with a technology platform that makes this entire process easy for the associate, the installer, and most importantly, the customer. We think now we have a best-in-class tech stack for this space. We have central selling. What you're looking at outside of kitchen and bath, which Bill will speak to, you're seeing categories like windows and doors and HVAC and water heaters. These are more replacement categories for customers who are living in the oldest housing stock in the history of the U.S. Because we have a better go-to-market strategy, Bill's team's given us great pricing, Brandon's team's given us a great credit portfolio. We're taking share in this area. We're also seeing, to your point, signs of life in areas that make us cautiously optimistic that maybe there are brighter days ahead.

Speaker 7
35m 44s

Now let Bill talk about some of those categories.

Speaker 14
35m 47s

Yeah. Chris, I mentioned in my prepared remarks that during the quarter, we had completed our vanity reset across the stores. That's one of the nice bright spots driving our kitchen and bath business. We're also seeing broad-based strength, toilets, bathing, faucets, disposal of kitchen sinks, bath repair. It's really kind of broad-based across the categories. We're excited about that. It really boils down to the strength I think we're also seeing within our central selling organization where the store associates take the lead. We turn it over to our central selling team, and they're helping to close the deal on a kitchen cabinet. The strength of what Joe's team's doing in the store to take good care of the customer. There's just a lot of things that are adding up to the strength of the kitchen and bath business, but those are just a few highlights.

Speaker 2
36m 35s

Thanks so much. Have a great holiday.

Speaker 14
36m 38s

Thanks, Chris.

Speaker 12
36m 41s

Our next question is from the line of Zach Fadum with Wells Fargo. Please proceed with your questions.

Speaker 10
36m 47s

Hey, good morning. I wanted to follow up on your comments around improving pro survey sentiment. I am curious if there is any extra color you can talk through in terms of how that has trended through the year, to what extent you think this is a good leading indicator for your business. What do you think is driving the recent improvement?

Speaker 7
37m 7s

Zach, thanks for the question. Just to hit it at a high level, our small to medium pro business remains very stable. Roughly 75% of our pros are very confident in their job prospects. Also, this segment of the pro consumer continues to work on smaller ticket repair and maintenance projects. That has been very consistent with what we have been saying all year long. When we look at our pros, when we talk to our pros, they feel very confident in their business. They feel confident in their access to credit and even feel a little bit more confident about their ability to hire and attract labor. We feel great about what our pros are telling us. Let me hand it over to Joe to just talk about some of the things we're doing in the store to drive this continued growth and, in my opinion, market share gain with the specific customer segment.

Speaker 13
38m 5s

Zach, thanks for the question. We're really pleased with the flywheel effect that we're seeing from the Transform Pro offering. When you think about where we've been headed with the loyalty through Milo's Pro Rewards, our relaunch there, we have just a wonderful enhanced digital experience, that pro extended aisle. We have made investments in fulfillment. The last three years, our pro inventory investments are really beginning to pay off. The order modifications, the fulfillment flexibility, and the in-store experience. We're excited to see this flywheel effect all come together with the great product offerings that we have. We have good confidence that when this does bounce back, we're well-positioned to capture the share.

Speaker 7
38m 52s

In fact, the only thing I'll add to that, I mentioned in my prepared comments that we're in the process of adding FBM to our Pro Extended Aisle platform. That's going to be a huge deal for us because it is very challenging for us today to fulfill a large order of something, let's say, drywall to a customer's job site and do it efficiently. We now are working to just transition that entire fulfillment process to a company that's best in class at it, and that's FBM. We think this is going to be great for FBM. It's going to be great for Lowe's, but more importantly, it's going to be great for the customer. Again, we see this as a sustainable growth strategy, and we feel great about the work we've done thus far.

Speaker 10
39m 43s

Appreciate that. I know we aren't guiding for 2026 yet, but since the model is different with FBM and ADG, could we talk through early margin scenarios in both a status quo environment as well as a scenario where perhaps we see some benefits from tax stimulus and lower rates?

Speaker 14
40m 4s

Yeah, Zach, I'll just hit briefly what we're looking at in terms of margins on the FBM and ADG transactions. When you look at 2025, taking an isolation, I mentioned in my remarks, we're roughly 20 basis points on 2025. That's coming roughly split even, 10 from FBM and 10 ADG. When you look at as we wrap the year for 2026, that's going to be 50 basis points on the year. Think 30 basis points of wrap into 2026. The majority of that 50 basis points, when you think of 2026, is going to be weighted towards gross margin on that. I'm not going to get into any more details as it relates to base business or run rate, but that's just some early views of geography and impact from the transactions in 2026.

Speaker 10
40m 59s

Thanks for the color.

Speaker 14
41m 1s

Thanks, Zach.

Speaker 12
41m 4s

Our next question is from the line of Simeon Gutman with Morgan Stanley. Please proceed with your questions.

Speaker 4
41m 10s

Hey, good morning, everyone. I wanted to ask to put the macro hat on again. There's a, I don't know if it's a bear case, but there's a housing scenario that it just stays in this treading water position for longer. You have new prices that are lower than existing homes, and the age of homeowners is pushing close to 40 years old. I think affordability is the issue. It sounds like you may reject that premise, Marvin, given some of the bright spots, but I wanted to hear how you react to it.

Speaker 7
41m 42s

No, Simeon, it's a good question. I'll give you my thoughts, and I'll let Brandon provide any additional comments. The way we see it is this. I think that mortgage rates obviously are elevated longer than any of us anticipated. The one thing that's different, as I said in my prepared comments, is the fact that you have a healthy homeowner financially, and you have $33 trillion in equity that is in the system. We think anywhere between $11-$13 trillion of that is tappable. We think this lock-in effect is real because at some point, customers are going to be looking at these sub-3% 30-year fixed mortgage rates. They like the neighborhood that they live in. They have excess equity in their home. We think HELOCs are going to become the next opportunity for us to drive discretionary remodel big-ticket projects. We think that is a strong possibility in the future. Now, we're not going to try to time it. We're not going to try to build it in our forecast. I think that would be reckless. We do think that that is a very plausible hypothesis that takes you away from the bear case. I'll pass it on to Brandon to see if he has any other thoughts.

Speaker 14
43m 6s

Yeah, Simeon, I'll add, as Marvin mentioned, the mortgage rates, we're looking at those remaining elevated, at least as of now, 6-6.5%, tied more to the longer-term yields. That's continuing to pressure both existing home sales and new home starts. I think as we start to look ahead into 2026, we're not anticipating meaningful near-term improvement there. We are potentially excited about what could happen with the funding coming from home equity. We've seen 150 basis points of rate cuts from the Fed here over the last 18 months. The consensus would suggest we're going to see more. We've seen these HELOC rates go from a neighborhood of 10-12% down to 8-10%. That's creating, I think, some opportunity as we look at project backlog. When we look at the data, about $50 billion of projects that have been delayed or deferred with the equity now with the potential to be a significant funding mechanism. If we do see further near-term rate reductions, that could act ongoing as an additional stimulus. We are investing in the business through our Total Home Strategy to be prepared for that type of environment and excited about the potential upside related to that into 2026.

Speaker 4
44m 25s

Okay. My follow-up, it's on the medium to larger pro. Can you, Marvin, set up what Lowe's strategy is there? We've talked about pieces of it. Will you keep supply chain separate? Are there categories that you think are essential to addressing that customer, whether it's an existing home remodeler or even a new home builder? Will you cross-sell that customer using the rest of the Lowe's asset base?

Speaker 7
44m 54s

Yes. Simeon, I would say we feel great about the current strategy with the small to medium pro is working. We've had quarter-over-quarter growth. We think it hinges on our Milo's Pro Rewards loyalty platform. It's resonating well with our customers. We think it hinges well on the products that Bill's team brings to the table every day. That was a huge gap and deficit for us seven years ago, and that is no longer the case. We also think it's important that we maintain a very competitive credit portfolio. We have a best in class, 5% off every day for our Lowe's credit cardholders. That also extends to the pro customer. That resonates exceptionally well. We have every intention on leveraging FBM for fulfillment and every intention on taking the roughly 40 million FBM pro customers and getting them connected to complementary projects, product, and projects at Lowe's. We see a very specific void in the marketplace for serving the small to medium pro. That is why we have been so intentional about focusing on that customer. We think we can focus on that customer in the brick-and-mortar stores and Lowe's.com. We can have a very robust strategy and platform with FBM and ADG, and we can do both concurrently.

Speaker 7
46m 25s

One of the reasons we talk about the importance of FBM's commercial business is because it is countercyclical. When housing is down, that commercial business tends to outperform. That is what we are seeing right now. Overall, we think we can do both. The data has proven that we have a very effective strategy with the small to medium pro.

Speaker 4
46m 48s

Okay. Thank you. Good luck.

Speaker 14
46m 51s

Thanks, Simeon.

Speaker 12
46m 53s

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

Speaker 6
47m 0s

Hi, good morning. Thanks for taking our question. We wanted to ask a little bit more about the marketplace, just in terms of what the initial performance has been, what you've seen with regards to seller onboarding, product expansion, and customer adoption, and just when you expect to scale this platform to a point where it could start to contribute more meaningfully to margin.

Speaker 7
47m 24s

No, Kate, thank you for the question. We are really excited about the launch of our marketplace. The caveat is it's really early, and we are not going to get into a lot of conversation relative to performance other than to say it's exceeding expectations relative to financial performance. It's exceeding expectations relative to the number of sellers and the quality of sellers. Every seller that we've approached, and we are literally looking at four-star plus rated sellers, are required to get on this platform. We, again, had great adoption with Merkle's technology, and they actually awarded Lowe's as the fastest launch partner they've ever had. We were able to get that done quickly, and we feel incredibly excited. One of the unique characteristics that we have is that virtually everything purchased as a marketplace item can be returned in a physical Lowe's store because Joe and his team partnered with technology some years back to create the technology rails to make that happen. It creates incredible convenience for the customer when they need to return something. Again, I'll let Bill talk about how the merchants are playing a role to make sure that we have a really balanced approach to how we're thinking about this.

Speaker 14
48m 45s

Yeah, thanks, Marvin. Kate, the only thing I would add is obviously early, but we're learning a lot as we progress with marketplace. We're finding that it's an opportunity to expand programs that our current vendors are providing in our stores to provide stuff that would be found on Lowes.com. We're also entering in and finding new products, products that, quite honestly, we didn't think that could be available on Lowes.com that now is available, and the consumers are engaging and buying them. We are excited about that learning and what that can do. At the forefront of when we put this together based on being a closed system is that we wanted it to complement what we were doing with what was happening inside of our stores. That's exactly what we're seeing early on here.

Speaker 6
49m 32s

Thank you.

Speaker 14
49m 35s

Thanks, Kate.

Speaker 12
49m 36s

Our next question is from the line of Seth Sigmund with Barclays. Please proceed with your questions.

Speaker 9
49m 41s

Hey, good morning, everyone. I wanted to ask about operating leverage going forward. You've been delivering really strong operating margin improvement this year on pretty low comps. I guess it's been mostly driven by gross margin this year. How do you think about the sustainability of gross margin as the primary driver of that, or does the composition of margin expansion change over time? I guess, in general, if you could speak to how you are thinking about the leverage point in the business, that would be helpful. Thank you.

Speaker 14
50m 13s

Sure, Seth. This is Brandon. Thanks for the question. I think as it relates to margin, very focused at this point on delivering the 12.1% operating margin that we communicated as part of our guide. Just as a reminder, ex the dilution from the acquisitions, that's at 12.3%, consistent with the flat bottom end of our range that we communicated at the beginning of the year. The team's done a really great job balancing flow through the balance between gross margin, SG&A, managing the tariff pressure that we've been dealing with. Honestly, the PPI initiatives continuing to deliver a billion dollars split roughly between SG&A and gross margin, that has been the primary driver in our ability to deliver mid-softer sales. I think as we look ahead into 2026, a few things I would highlight. We're continuing to look at FBM and ADG, what we think housing and commercial markets are going to be looking like and the business performance there in 2026. I mentioned earlier new home starts, both single-family and multi-family remain under pressure, but confident with these businesses that we can gain share in a down market. Marvin also mentioned the nice balance that we have on the commercial side.

Speaker 14
51m 31s

Looking at that and how that impacts the margin profile into 2026. The last thing I'll mention, just as we continue to look at tariffs, those ramp here in Q3, we're expecting that also to continue ramping in Q4 and the wrap to affect the first half of the year. Managing through that and trying to understand how that impacts both sales margin and operating margin going forward. All that will be weighed. We'll look at that in terms of our previous rule of thumb, and we'll have more on that as we get into our call in February for 2026.

Speaker 9
52m 7s

Okay. Got it. That's helpful. I guess a related follow-up would be on the gross margin specifically. The gains this quarter really stepped up. Can you just unpack that a little bit more? Are there any timing considerations? I mean, you mentioned tariffs starting to flow through. Was there a benefit from raising prices relative to the cost coming through, or anything else you can tell us about the mixed dynamics that seem to be supportive this quarter? Thank you.

Speaker 7
52m 31s

Yeah, I would say, Seth, on Q3 margin, really nothing related to pricing or tariffs. I would say that's playing out very much in line with our expectations just in terms of estimating when the cost is going to be flowing through margin. The great work that Bill and team have done on the merchandising side with our suppliers. It really is the themes that I outlined in my remarks. We're lapping storm pressure from last year, so that is serving as a benefit this year. The credit portfolio has outperformed our expectations on better-than-expected losses. Then Bill referenced the SKU rationalization initiative. We've seen really good sell-through results thus far on the inventory that we're exiting there. That really was the core of the composition of the 50 basis points that we saw in Q3.

Speaker 9
53m 21s

Okay. Great. Thanks so much.

Speaker 7
53m 24s

Thanks, Seth.

Speaker 12
53m 26s

Our next question is from the line of Greg Mellick with Evercore ISI. Please proceed with your questions.

Speaker 3
53m 32s

Hey, thanks. I'd love to follow up on the traffic and ticket breakdown. If you look at the ticket expansion, it's accelerated, I think, each quarter this year. How much of that 150 basis points of acceleration is related to some of the early tariffs going through? How much of it is mixed? How's sort of the basket evolving in terms of items in it and the size?

Speaker 14
53m 57s

Yeah, Greg, I can speak to ticket and transaction. When we look at ticket growth, it's really similar when we look at Q3 performance as to what we've seen in previous quarters in terms of the drivers. It's to strengthen our pro business, also appliances. I will reference that in Q3, we did have some modest price increases. When we look at like-for-like inflation, again, modest, it's very consistent with our expectations and also the year-to-date trends that we've seen as we continue to watch tariffs move through the system. The offset is transactions, and that has been pressured by the lower DIY demand. I'll also call out the bulk of the 100 basis points of storm-related pressure with the DIY is affecting the transactions. That's really the driver of the offset when we look at Q3. I think when we look ahead to Q4, a lot of those same drivers are expected lift from pro appliances. There will be some modest like-for-like inflation. Just as a reminder, we also have 100 basis points of hurricane pressure that we're cycling in Q4 that will also pressure comps and pressure DIY transactions in Q4.

Speaker 3
55m 8s

Got it. Maybe just a clarification on before, the 50 basis points is the full annualized effect on the margins of the two acquisitions, right? We have basically 15 basis points that show up this year and then 35 basis points next year?

Speaker 14
55m 26s

Yes, Greg, it's 20 on the year for 2025, and then 30 of wrap for a total annualized run rate into 2026 of 50 basis points.

Speaker 3
55m 37s

Got it. Thank you. If I take the guide for Q4, it seems like margin should be down around 60 basis points, and it's fair to say that's the two of those sort of rolling in.

Speaker 14
55m 46s

Yeah, I would say when you isolate Q4, the bulk of the operating margin decrease is going to be driven by layering in the transactions. We have $1.3 billion of sales for FBM. That will pressure operating margin or dilute it down as well as ADG. So that's driving the bulk of the change in Q4.

Speaker 3
56m 7s

That's great. Thanks and good luck.

Speaker 14
56m 9s

Thanks, Greg.

Speaker 12
56m 11s

Our next question is from the line of Jihyun Mott with Bernstein. Please proceed with your questions.

Speaker 11
56m 17s

Great. Thank you for taking my question. I wanted to ask about the FBM-ADG integration that you are doing. Can you just help us understand to what extent you're maybe onboarding ADG onto the FBM-ERP system? How does that integration work in the near term?

Speaker 7
56m 34s

No, thank you for the question. It's early days. The first rule that we have is to do no harm to the performance of either business platform, including Lowe's. We are in the early stages of the integration. The big advantage we have is FBM's current IT platform is the same platform that we are transitioning ADG to. That is not by accident. Also, it's an existing platform that we have in our Lowe's Pro Supply businesses. We feel like we're going to have the ability to accelerate the IT integration between the companies. As you can respect, we're in the early stages of that. We feel really good about the plan. We feel really good about the timetable, and we have the best IT team in retail working on it. I am very confident we'll be able to make it happen.

Speaker 11
57m 34s

Great. Then just a longer-term follow-up. You mentioned a plan to de-level to the 2.75 by mid-2027. Is the longer-term plan to resume share buybacks by then, or should we expect additional acquisitions from here?

Speaker 14
57m 51s

Yeah, I would say Jihyun, still very focused on the integration activities, as Marvin mentioned. That's going to be our focus here over the next two years. We're pausing share repo and very much expect to get back down to that 2.75 times leverage target by 2027. That's our focus. FBM is going to continue to run their existing play in the meantime, expanding through Greenfield expansion, organic growth. There could be potentially some small tuck-in M&A, but that would only be what we could self-fund with additional cash flow. I think that's the best way to think about how we're going to be operating here over the next two years.

Speaker 11
58m 33s

Great. Thank you.

Speaker 12
58m 37s

Hey, yes. Thank you. Our last question comes from the line of Robbie Ohmes with Bank of America. Please proceed with your question.

Speaker 1
58m 45s

Oh, thanks for squeezing me in. I'll be quick here because we all have to jump, I think, to other calls. Just two follow-ups. Just on the fourth quarter, the way you're planning it for seasonal and given a little bit more probably tariff prices coming through, any changes in the timing of promos? Are you doing any promos earlier related to holiday and things like that?

Speaker 14
59m 7s

Not, Robbie. I mean, the promotional cadence remains relatively consistent to prior years. We started the quarter off with kind of the early pre-Black Friday type stuff that we've been doing. Obviously, Black Friday next week, and then post-Black Friday when you get into Cyber Monday events for dot com, and then you get into that leading up to the holiday timeframe. We've got offers out there for both the Milo's Rewards members as well as all of our consumers, both online and in store. Relatively consistent with what we've done.

Speaker 1
59m 36s

That's helpful. Just to follow up on flooring and the strength you guys are seeing there, you guys called out soft surfaces. Is there a trade-down going on? How do you think you're doing relative to industry? Is there something changing in flooring, or is it something about your positioning in good, better, best, or maybe a little more color there?

Speaker 14
59m 58s

Yeah. It's nice to be able to give a shout-out to the flooring team and all the work that they've been doing. Last quarter, we announced the acquisition and being able to get Dow Tile into our assortment. That's starting to roll in now. Specifically to soft surface, it's really the strength of Stainmaster. We called that out as one of our strongest brands. Now we've got leak defense being able to be offered. That is not a trade-down. That's a trade-up offering in the assortment. I think the team's done a really nice job of offering value out there every single day. I'd stack our soft surface offer out there every single day against what's going on in the marketplace. You could go into luxury vinyl. You can go into resilient hybrid, and then you can go into hard surface tile. The teams have offers out there every single day to close that consumer that's now making the decision to do a flooring project.

Speaker 7
1h 0m

Robbie, I would just add that the investments we've continued to make in our services business, flooring was one of our first to go central selling, where we removed that complexity of the design from the store. We shortened the time to close the customer and take them off the market. I think all in all, the products, the service level, we're really seeing some green shoots.

Speaker 1
1h 1m

Really helpful. Thanks so much.

Speaker 14
1h 1m

Thanks, Robbie.

Speaker 12
1h 1m

Thank you all for joining us today. We look forward to speaking with you on our fourth quarter earnings call in February. Thank you. This concludes the Lowe's third quarter 2025 earnings call. You may now disconnect.