HOME DEPOT INC
Form 10-Q
August 27, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q
(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended August 3, 2014
- OR -
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission file number 1-8207
THE HOME DEPOT, INC.
(Exact name of Registrant as specified in its charter)

Delaware	95-3261426
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
2455 Paces Ferry Road N.W., Atlanta, Georgia	30339
(Address of principal executive offices)	(Zip Code)

(770) 433-8211
(Registrant's telephone number, including area code)
(Former name, former address and former fiscal year, if changed since last report)
Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨
Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes x No ¨
Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer ¨	Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x
APPLICABLE ONLY TO CORPORATE ISSUERS:
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.
1,345,921,559 shares of common stock, $0.05 par value, as of August 19, 2014

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

THE HOME DEPOT, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Unaudited)

amounts in millions, except share and per share data	August 3, 2014	February 2, 2014
ASSETS		
Current Assets:		
Cash and Cash Equivalents	$4,216	$1,929
Receivables, net	1,637	1,398
Merchandise Inventories	11,665	11,057
Other Current Assets	973	895
Total Current Assets	18,491	15,279
Property and Equipment, at cost	39,603	39,064
Less Accumulated Depreciation and Amortization	16,477	15,716
Net Property and Equipment	23,126	23,348
Goodwill	1,295	1,289
Other Assets	567	602
Total Assets	$43,479	$40,518
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts Payable	$7,165	$5,797
Accrued Salaries and Related Expenses	1,325	1,428
Sales Taxes Payable	583	396
Deferred Revenue	1,503	1,337
Income Taxes Payable	357	12
Current Installments of Long-Term Debt	34	33
Other Accrued Expenses	1,872	1,746
Total Current Liabilities	12,839	10,749
Long-Term Debt, excluding current installments	16,702	14,691
Other Long-Term Liabilities	1,953	2,042
Deferred Income Taxes	528	514
Total Liabilities	32,022	27,996
STOCKHOLDERS' EQUITY		
Common Stock, par value $0.05; authorized: 10 billion shares; issued: 1.766 billion shares at August 3, 2014 and 1.761 billion shares at February 2, 2014; outstanding: 1.346 billion shares at August 3, 2014 and 1.380 billion shares at February 2, 2014	88	88
Paid-In Capital	8,217	8,402
Retained Earnings	25,324	23,180
Accumulated Other Comprehensive Income	91	46
Treasury Stock, at cost, 420 million shares at August 3, 2014 and 381 million shares at February 2, 2014	(22,263)	(19,194)
Total Stockholders' Equity	11,457	12,522

Total Liabilities and Stockholders’ Equity	$43,479	$40,518

See accompanying Notes to Consolidated Financial Statements.

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THE HOME DEPOT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EARNINGS
(Unaudited)

amounts in millions, except per share data	Three Months Ended August 3, 2014	Three Months Ended August 4, 2013	Six Months Ended August 3, 2014	Six Months Ended August 4, 2013
NET SALES	$23,811	$22,522	$43,498	$41,646
Cost of Sales	15,650	14,801	28,452	27,246
GROSS PROFIT	8,161	7,721	15,046	14,400
Operating Expenses:				
Selling, General and Administrative	4,298	4,294	8,492	8,477
Depreciation and Amortization	415	409	829	811
Total Operating Expenses	4,713	4,703	9,321	9,288
OPERATING INCOME	3,448	3,018	5,725	5,112
Interest and Other (Income) Expense:				
Interest and Investment Income	(17)	(2)	(117)	(5)
Interest Expense	208	174	399	338
Interest and Other, net	191	172	282	333
EARNINGS BEFORE PROVISION FOR INCOME TAXES	3,257	2,846	5,443	4,779
Provision for Income Taxes	1,207	1,051	2,014	1,758
NET EARNINGS	$2,050	$1,795	$3,429	$3,021
Weighted Average Common Shares	1,346	1,434	1,358	1,452
BASIC EARNINGS PER SHARE	$1.52	$1.25	$2.53	$2.08
Diluted Weighted Average Common Shares	1,353	1,443	1,365	1,462
DILUTED EARNINGS PER SHARE	$1.52	$1.24	$2.51	$2.07
Dividends Declared per Share	$0.47	$0.39	$0.94	$0.78

See accompanying Notes to Consolidated Financial Statements.

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THE HOME DEPOT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

amounts in millions	Three Months Ended August 3, 2014	Three Months Ended August 4, 2013	Six Months Ended August 3, 2014	Six Months Ended August 4, 2013
Net Earnings	$2,050	$1,795	$3,429	$3,021
Other Comprehensive Income (Loss):				
Foreign Currency Translation Adjustments	15	(153)	55	(109)
Cash Flow Hedges, net of tax	(13)	1	(11)	3
Other	1	—	1	(10)
Total Other Comprehensive Income (Loss)	3	(152)	45	(116)
COMPREHENSIVE INCOME	$2,053	$1,643	$3,474	$2,905

See accompanying Notes to Consolidated Financial Statements.

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THE HOME DEPOT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

amounts in millions	Six Months Ended August 3, 2014	August 4, 2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Earnings	$3,429	$3,021
Reconciliation of Net Earnings to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	896	877
Stock-Based Compensation Expense	119	116
Changes in Assets and Liabilities, net of the effect of acquisition:		
Receivables, net	(239)	(153)
Merchandise Inventories	(589)	(419)
Other Current Assets	(111)	(51)
Accounts Payable and Accrued Expenses	1,366	1,278
Deferred Revenue	164	114
Income Taxes Payable	446	140
Deferred Income Taxes	54	(78)
Other	(250)	(127)
Net Cash Provided by Operating Activities	5,285	4,718
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital Expenditures	(631)	(599)
Proceeds from Sales of Investments	112	—
Payments for Business Acquired, net	—	(13)
Proceeds from Sales of Property and Equipment	16	16
Net Cash Used in Investing Activities	(503)	(596)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from Long-Term Borrowings, net of discount	1,981	1,994
Repayments of Long-Term Debt	(21)	(17)
Repurchases of Common Stock	(3,500)	(4,346)
Proceeds from Sales of Common Stock	148	150
Cash Dividends Paid to Stockholders	(1,285)	(1,143)
Other Financing Activities	181	154
Net Cash Used in Financing Activities	(2,496)	(3,208)
Change in Cash and Cash Equivalents	2,286	914
Effect of Exchange Rate Changes on Cash and Cash Equivalents	1	11
Cash and Cash Equivalents at Beginning of Period	1,929	2,494
Cash and Cash Equivalents at End of Period	$4,216	$3,419

See accompanying Notes to Consolidated Financial Statements.

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THE HOME DEPOT, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying Consolidated Financial Statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and footnotes required by generally accepted accounting principles ("GAAP") for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. These statements should be read in conjunction with the Consolidated Financial Statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended February 2, 2014, as filed with the Securities and Exchange Commission.

Business

The Home Depot, Inc. and its subsidiaries (the "Company") operate The Home Depot stores, which are full-service, warehouse-style stores averaging approximately 104,000 square feet of enclosed space, with approximately 24,000 additional square feet of outside garden area. The stores stock approximately 30,000 to 40,000 different kinds of building materials, home improvement supplies and lawn and garden products that are sold to do-it-yourself customers, do-it-for-me customers and professional customers. The Company also offers over 700,000 products through its websites, including Home Depot, Home Decorators Collection and Blinds.com.

Valuation Reserves

As of August 3, 2014 and February 2, 2014, the valuation allowances for Merchandise Inventories and uncollectible Receivables were not material.

2. LONG-TERM DEBT

In June 2014, the Company issued $1.0 billion of 2.00% senior notes due June 15, 2019 (the "2019 notes") at a discount of $4 million and $1.0 billion of 4.40% senior notes due March 15, 2045 (the "2045 notes") at a discount of $15 million (together, the "June 2014 issuance"). Interest on the 2019 notes is due semi-annually on June 15 and December 15 of each year, beginning December 15, 2014. Interest on the 2045 notes is due semi-annually on March 15 and September 15 of each year, beginning September 15, 2014. The net proceeds of the June 2014 issuance were used for general corporate purposes, including repurchases of shares of the Company's common stock. The $19 million discount associated with the June 2014 issuance is being amortized over the term of the notes using the effective interest rate method. Issuance costs associated with the June 2014 issuance were approximately $14 million and are being amortized over the term of the notes.

The notes may be redeemed by the Company at any time, in whole or in part, at the redemption price plus accrued interest up to the redemption date. The redemption price is equal to the greater of (1) 100% of the principal amount of the notes to be redeemed, and (2) the sum of the present values of the remaining scheduled payments of principal and interest to the Par Call Date, as defined in the respective notes. Additionally, if a Change in Control Triggering Event occurs, as defined in the notes, holders of the notes have the right to require the Company to redeem those notes at 101% of the aggregate principal amount of the notes plus accrued interest up to the redemption date. The Company is generally not limited under the indenture governing the notes in its ability to incur additional indebtedness or required to maintain financial ratios or specified levels of net worth or liquidity. Further, while the indenture governing the notes contains various restrictive covenants, none are expected to impact the Company's liquidity or capital resources.

3. INVESTMENT IN HD SUPPLY HOLDINGS, INC.

At the end of fiscal 2013, the Company owned 16.3 million shares of HD Supply Holdings, Inc. ("HD Supply") common stock, which represented approximately 8% of the shares of HD Supply common stock outstanding. This investment is accounted for using the cost method, as there are significant restrictions in place on the Company's ability to sell or transfer its HD Supply shares. The restrictions are controlled by the three largest shareholders of HD Supply (the "Principal Shareholders"). The carrying value of the HD Supply shares was impaired by the Company to a zero cost basis in fiscal 2009. During the first quarter of fiscal 2014, the Principal Shareholders elected to sell shares in a secondary public offering of HD Supply common stock. Under the terms of a registration rights agreement among the Company, HD Supply and the Principal Shareholders, the Company had the right to include a portion of its shares in the offering, and the Company elected to do so. As a result, the restrictions on 3.9 million shares were lifted so that they could be sold in the offering. The Company received $97 million of proceeds from the sale of these shares and recognized a corresponding gain in the first quarter of fiscal 2014.

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(Unaudited)

In the second quarter of fiscal 2014, the underwriters of the secondary public offering exercised their overallotment option to sell additional shares of HD Supply common stock to the public. As a result, the Company sold 600 thousand additional shares of HD Supply common stock and received $15 million of proceeds from the sale of these shares and recognized a corresponding gain in the second quarter of fiscal 2014. The total gain of $112 million is included in Interest and Investment Income in the accompanying Consolidated Statements of Earnings for the six months ended August 3, 2014. The remaining 11.8 million shares owned by the Company, which represent approximately 6% of the shares of HD Supply common stock outstanding, continue to be accounted for using the cost method as the restrictions on these shares remain in place.

4. ACCELERATED SHARE REPURCHASE AGREEMENTS

In the first quarter of fiscal 2014, the Company entered into an Accelerated Share Repurchase ("ASR") agreement with a third-party financial institution to repurchase $950 million of the Company’s common stock. Under this agreement, the Company paid $950 million to the financial institution and received an initial delivery of 9.5 million shares in the first quarter of fiscal 2014. The transaction was completed later in the first quarter of fiscal 2014, at which time the Company received 2.6 million additional shares. The final number of shares delivered upon settlement of the $950 million ASR agreement was determined with reference to the average price of the Company's common stock over the term of the agreement. The $950 million of shares repurchased is included in Treasury Stock in the accompanying Consolidated Balance Sheets as of August 3, 2014.

In the second quarter of fiscal 2014, the Company entered into an ASR agreement with a third-party financial institution to repurchase $1.75 billion of the Company’s common stock. Under this agreement, the Company paid $1.75 billion to the financial institution and received an initial delivery of 16.9 million shares in the second quarter of fiscal 2014. The fair market value of the 16.9 million shares on the date of purchase was $1.32 billion and is included in Treasury Stock in the accompanying Consolidated Balance Sheets as of August 3, 2014. The remaining $430 million is included in Paid-In Capital in the accompanying Consolidated Balance Sheets as of August 3, 2014. The final number of shares delivered upon settlement of the $1.75 billion ASR agreement will be determined in the third quarter of fiscal 2014 with reference to the average price of the Company's common stock over the term of the agreement.

5. FAIR VALUE MEASUREMENTS

The fair value of an asset is considered to be the price at which the asset could be sold in an orderly transaction between unrelated knowledgeable and willing parties. A liability’s fair value is defined as the amount that would be paid to transfer the liability to a new obligor, rather than the amount that would be paid to settle the liability with the creditor. Assets and liabilities recorded at fair value are measured using a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers are:

- Level 1 – Observable inputs that reflect quoted prices in active markets
- Level 2 – Inputs other than quoted prices in active markets that are either directly or indirectly observable
- Level 3 – Unobservable inputs for which little or no market data exists, therefore requiring the Company to develop its own assumptions

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The assets and liabilities of the Company that are measured at fair value on a recurring basis as of August 3, 2014 and February 2, 2014 were as follows (amounts in millions):

	Fair Value at August 3, 2014 Using			Fair Value at February 2, 2014 Using		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Derivative agreements - assets	$—	$30	$—	$—	$30	$—
Derivative agreements - liabilities	—	(25)	—	—	(10)	—
Total	$—	$5	$—	$—	$20	$—

The Company uses derivative financial instruments from time to time in the management of its interest rate exposure on long-term debt and its exposure on foreign currency fluctuations. The fair value of the Company’s derivative financial instruments was measured using level 2 inputs.

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THE HOME DEPOT, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

Long-lived assets were analyzed for impairment on a nonrecurring basis using fair value measurements with unobservable inputs (level 3). Impairment charges related to long-lived assets in the first six months of fiscal 2014 and 2013 were not material.

The aggregate fair value of the Company’s senior notes, based on quoted market prices, was $17.8 billion and $15.6 billion at August 3, 2014 and February 2, 2014, respectively, compared to a carrying value of $16.2 billion and $14.2 billion at August 3, 2014 and February 2, 2014, respectively.

6. BASIC AND DILUTED WEIGHTED AVERAGE COMMON SHARES

The reconciliation of basic to diluted weighted average common shares for the three and six months ended August 3, 2014 and August 4, 2013 was as follows (amounts in millions):

	Three Months Ended		Six Months Ended	
	August 3, 2014	August 4, 2013	August 3, 2014	August 4, 2013
Weighted average common shares	1,346	1,434	1,358	1,452
Effect of potentially dilutive securities:				
Stock plans	7	9	7	10
Diluted weighted average common shares	1,353	1,443	1,365	1,462

Stock plans consist of shares granted under the Company’s employee stock plans. Options to purchase 2 million and 1 million shares of common stock for the three months ended August 3, 2014 and August 4, 2013, respectively, and options to purchase 2 million and 1 million shares of common stock for the six months ended August 3, 2014 and August 4, 2013, respectively, were excluded from the computation of Diluted Earnings per Share because their effect would have been anti-dilutive.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
The Home Depot, Inc.:

We have reviewed the Consolidated Balance Sheet of The Home Depot, Inc. and subsidiaries as of August 3, 2014, the related Consolidated Statements of Earnings and Comprehensive Income for the three-month and six-month periods ended August 3, 2014 and August 4, 2013, and the related Consolidated Statements of Cash Flows for the six-month periods ended August 3, 2014 and August 4, 2013. These Consolidated Financial Statements are the responsibility of the Company’s management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the Consolidated Financial Statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the Consolidated Balance Sheet of The Home Depot, Inc. and subsidiaries as of February 2, 2014, and the related Consolidated Statements of Earnings, Comprehensive Income, Stockholders’ Equity, and Cash Flows for the year then ended (not presented herein); and in our report dated March 27, 2014, we expressed an unqualified opinion on those Consolidated Financial Statements. In our opinion, the information set forth in the accompanying Consolidated Balance Sheet as of February 2, 2014, is fairly stated, in all material respects, in relation to the Consolidated Balance Sheet from which it has been derived.

/s/ KPMG LLP
Atlanta, Georgia
August 27, 2014

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Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

FORWARD-LOOKING STATEMENTS

Certain statements contained herein regarding our future performance constitute "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements may relate to, among other things, the demand for our products and services; net sales growth; comparable store sales; effects of competition; state of the economy; state of the residential construction, housing and home improvement markets; state of the credit markets, including mortgages, home equity loans and consumer credit; inventory and in-stock positions; implementation of store, interconnected retail and supply chain initiatives; management of relationships with our suppliers and vendors; continuation of share repurchase programs; net earnings performance; earnings per share; capital allocation and expenditures; liquidity; return on invested capital; expense leverage; stock-based compensation expense; commodity price inflation and deflation; the ability to issue debt on terms and at rates acceptable to us; the effect of accounting charges; the effect of adopting certain accounting standards; store openings and closures; and financial outlook.

Forward-looking statements are based on currently available information and our current assumptions, expectations and projections about future events. You should not rely on our forward-looking statements. These statements are not guarantees of future performance and are subject to future events, risks and uncertainties – many of which are beyond our control or are currently unknown to us – as well as potentially inaccurate assumptions that could cause actual results to differ materially from our expectations and projections. These risks and uncertainties include, but are not limited to, those described in Item 1A, "Risk Factors" and elsewhere in our Annual Report on Form 10-K for the fiscal year ended February 2, 2014 as filed with the Securities and Exchange Commission ("SEC") on March 27, 2014 ("2013 Form 10-K") and in Item 1A of Part II and elsewhere in this report. You should read such information in conjunction with our Consolidated Financial Statements and related notes and "Management’s Discussion and Analysis of Financial Condition and Results of Operations" in this report. There also may be other factors that we cannot anticipate or that are not described in this report, generally because we do not currently perceive them to be material. Such factors could cause results to differ materially from our expectations.

Forward-looking statements speak only as of the date they are made, and we do not undertake to update these statements other than as required by law. You are advised, however, to review any further disclosures we make on related subjects in our periodic filings with the SEC.

EXECUTIVE SUMMARY AND SELECTED CONSOLIDATED STATEMENTS OF EARNINGS DATA

For the second quarter of fiscal 2014, we reported Net Earnings of $2.1 billion and Diluted Earnings per Share of $1.52 compared to Net Earnings of $1.8 billion and Diluted Earnings per Share of $1.24 for the second quarter of fiscal 2013. For the first six months of fiscal 2014, we reported Net Earnings of $3.4 billion and Diluted Earnings per Share of $2.51 compared to Net Earnings of $3.0 billion and Diluted Earnings per Share of $2.07 for the first six months of fiscal 2013.

The results for the first six months of fiscal 2014 included a $112 million pretax gain related to the sale of a portion of our equity ownership in HD Supply Holdings, Inc. ("HD Supply"), of which $97 million was recognized in the first quarter of fiscal 2014 and $15 million was recognized in the second quarter of fiscal 2014. This gain contributed $0.05 to Diluted Earnings per Share for the first six months of fiscal 2014, of which $0.04 was recognized in the first quarter of fiscal 2014 and $0.01 was recognized in the second quarter of fiscal 2014.

Net Sales increased 5.7% to $23.8 billion for the second quarter of fiscal 2014 from $22.5 billion for the second quarter of fiscal 2013. For the first six months of fiscal 2014, Net Sales increased 4.4% to $43.5 billion from $41.6 billion for the first six months of fiscal 2013. Our total comparable store sales increased 5.8% in the second quarter of fiscal 2014, driven by a 4.1% increase in our comparable store customer transactions and a 1.7% increase in our comparable store average ticket. Comparable store sales for our U.S. stores increased 6.4% in the second quarter of fiscal 2014. For the first six months of fiscal 2014, our total comparable store sales increased 4.3%, and comparable store sales for our U.S. stores increased 5.0%.

In the second quarter and first six months of fiscal 2014, we continued to focus on the following key initiatives:

Customer Service – Our focus on customer service is anchored on the principles of creating an emotional connection with customers, putting customers first, taking care of our associates and simplifying the business. In the first six months of fiscal 2014, we continued to make enhancements to our FIRST phone, an associate and customer service tool. These enhancements include plans to introduce the next generation of our FIRST phone in the second half of fiscal 2014, which will allow for internet access to assist with questions and online orders and will be equipped to complete the check-out process in the aisle for our customers.

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Product Authority – Our focus on product authority is facilitated by our merchandising transformation and portfolio strategy, which is aimed at delivering product innovation, assortment and value. As part of this effort, we are implementing new merchandising assortment planning and pricing tools to better assort products within stores with similar attributes based on local preferences, regulations and demographics.

We also continued to introduce innovative new products and great values to our customers. This includes plans to launch a new light bulb reset, which will add 26 new SKUs to our assortment, and introduce new products for the connected home, such as garage door openers, thermostats and water heaters.

Disciplined Capital Allocation, Productivity and Efficiency – Our approach to driving productivity and efficiency is advanced through continuous operational improvement in the stores and our supply chain, disciplined capital allocation and building shareholder value through higher returns on invested capital and total value returned to shareholders in the form of dividends and share repurchases. During the first six months of fiscal 2014, we introduced our new Customer Order Management system. This system is designed to provide greater visibility into and improved execution of special orders by our associates and a more seamless experience for our customers. We intend to roll this system out to all U.S. stores by the end of fiscal 2014.

During the second quarter of fiscal 2014, we entered into a $1.75 billion Accelerated Share Repurchase (“ASR”) agreement and received an initial delivery of 16.9 million shares of our common stock. Also in the second quarter of fiscal 2014, we repurchased 6.2 million shares of our common stock through the open market. During the first six months of fiscal 2014, we repurchased a total of 38.9 million shares of our common stock for $3.5 billion through ASR agreements and the open market.

We opened one new store in Mexico during the second quarter of fiscal 2014, for a total store count of 2,264 at the end of the quarter. As of the end of the second quarter of fiscal 2014, a total of 287 of our stores, or 12.7%, were located in Canada and Mexico.

We generated $5.3 billion of cash flow from operations in the first six months of fiscal 2014. This cash flow, along with $2.0 billion of long-term debt issued in the second quarter of fiscal 2014, was used to fund $3.5 billion of share repurchases, pay $1.3 billion of dividends and fund $631 million in capital expenditures.

Our return on invested capital (computed on net operating profit after tax for the trailing twelve months and the average of beginning and ending long-term debt and equity) was 21.9% for the second quarter of fiscal 2014 compared to 19.1% for the second quarter of fiscal 2013.

Interconnected Retail – Our focus on interconnected retail, which connects our other three key initiatives, is based on building a competitive and seamless platform across all commerce channels. During the first six months of fiscal 2014, we continued to enhance our website and mobile experience, resulting in improved customer satisfaction scores and online sales conversion rates. Sales from our online channels increased over 38% for the second quarter and first six months of fiscal 2014 compared to the same periods last year and represented approximately 4.2% of our total Net Sales at the end of the quarter.

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We believe the selected sales data, the percentage relationship between Net Sales and major categories in the Consolidated Statements of Earnings and the percentage change in the dollar amounts of each of the items presented below are important in evaluating the performance of our business operations.

	% of Net Sales				% Increase (Decrease) in Dollar Amounts	
	Three Months Ended		Six Months Ended			
	August 3, 2014	August 4, 2013	August 3, 2014	August 4, 2013	Three Months	Six Months
NET SALES	100.0 %	100.0 %	100.0 %	100.0 %	5.7 %	4.4 %
GROSS PROFIT	34.3	34.3	34.6	34.6	5.7	4.5
Operating Expenses:						
Selling, General and Administrative	18.1	19.1	19.5	20.4	0.1	0.2
Depreciation and Amortization	1.7	1.8	1.9	1.9	1.5	2.2
Total Operating Expenses	19.8	20.9	21.4	22.3	0.2	0.4
OPERATING INCOME	14.5	13.4	13.2	12.3	14.2	12.0
Interest and Other (Income) Expense:						
Interest and Investment Income	(0.1)	—	(0.3)	—	N/M	N/M
Interest Expense	0.9	0.8	0.9	0.8	19.5	18.0
Interest and Other, net	0.8	0.8	0.6	0.8	11.0	(15.3)