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Home Depot Makes Progress on Ambitious Supply Chain Transformation

One Inventory Turn Equals $1.5 billion in Cash Flow; 35 Years of John Deere Inventory at One Store

SCDigest Editorial Staff

In the first quarter of 2007, Home Depot announced ambitious plans to transform many elements of its supply chain. **Mark Holifield**, a respected supply chain executive from Office Depot, was hired in 2006 to lead the effort at Home Depot.

In a presentation to financial industry analysts in February, 2007, Holifield outlined several key elements of the retailer's supply chain strategy. A key element was a transition from a logistics model that favored direct store delivery from suppliers to a model that moved most products first through Home Depot distribution centers. In the past, as much as 80% of products went direct to store; the goal is to cut that number to just 25% by 2010.

Home Depot, in fact, is the country's largest Less-than-Truckload (LTL) shipper – a crown not many companies would like to wear, given the relative expense of LTL shipping.

The move to DC/flow through shipment will result in a variety of inventory, transportation and store labor efficiencies, Holifield said, and was necessary in part due to store expansion, which ultimately led to lower sales at each individual store location.

"The inventory strategy for a $40 million store is different than the one that worked for an $80 million one," he said. Some Home Depot Stores now have just $10-20 million in annual sales – still a huge number for most retailers, but well down from the levels of the 1990s.

"Our stores, candidly, have way too much inventory in them," Holifield recently told the Atlanta Journal-Constitution. "A common reaction here to something being out of stock is to look up. But nothing good happens in 'top stock," referring to merchandise high up in store racking locations.

For every one tenth improvement in inventory turns, the company will free up about $150 million in working capital. Improving inventory management by just one full turn per year can therefore generate that $1.5 billion in annual cash flow.

Holifield also said back in 2007 that the company would improve its supply chain technology in several areas:

- Implement supply chain analytics
- Install improved demand forecasting tools
- Improve central replenishment
- Improve merchandise financial planning processes
- Improve transportation management

An anecdote from current CEO **Frank Blake** illustrates the retailer's supply chain challenges. A couple of years ago, while visiting a store in Prescott, AZ, he saw a pyramid of John Deere tractors.

As told at a recent Cobb County, GA Chamber of Commerce meeting, Blake said he looked around the desert landscape and thought to himself, "It doesn't look like [Prescott] has seen a blade of

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grass, ever."

He asked the store manager whether he sold a lot of tractors.

"I sold one last year," the manager told Blake.

"Well, you've got 35 years of supply then," the CEO replied.

The cost of the transformation effort and new technology is not trivial, even by Home Depot standards. Blake said the bill will be as much as $118 million this year and some $260 million through 2010.

But the payoff may be huge – the planned reductions in inventory levels can free up as much as $1.5 billion (with a "B") in working capital, Home Depot says. That's because for every one tenth improvement in inventory turns, the company will free up about $150 million in working capital.

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Mark Holifield
Home Depot

In 2007, Home Depot had an inventory turn level of 4.9. That's up slightly from the 4.8 turns in 2006, in a year when turns were probably under pressure from the massive slowdown in the housing industry in 2007.

Home Depot is taking a page out of the traditional retail playbook, including the supply chains of competitors such as Wal-Mart and Lowes, building large, flow-though type facilities that will each serve approximately 100 stores. A prototype of this new DC was built in Braselton, GA last year, as was another Regional Distribution Center (RDC). But since then, additional DCs have been pushed back a bit, as Home Depot absorbs the lessons of managing the first two and corresponding supply chain processes.

Holifield is simultaneously working a range of other issues. "The root of the problem has been poor forecasts, late shipments and inaccurate "perpetual inventory" at the stores, he told the Atlanta paper.

The challenge is substantial. Although less than the 100,000 SKUs Wal-Mart Supercenters handle, Home Depot stores typically carry a still massive 35,000 items.