



## Calls Accumulate in HD Supply as 2H Outlook Looks Stronger

**Ticker/Price:** HDS (\$40.9)

### Analysis:

**HD Supply (HDS)** has seen 3,800 January \$37.50 calls bought to open over the past week for nearly \$2M and also has 3,000 August \$40/\$42.5 call spreads in open interest and 1,250 September \$40 short puts. The December \$42.50 calls have 1,740X in OI that were sold to open and January \$35 and \$32.50 puts each sold to open 1000X. HDS shares are working on a multi-week base just above YTD VPOC and key value areas and despite relative weakness are basing above the rising 144 week MA and 3.5 year trend support with weekly MACD showing potential for a bullish crossover. In December the CEO bought 50,000 shares of stock of \$1.85M at \$36.99/share. The \$6.87B Company trades 12.15X Earnings, 12.7X FCF and 10X EV/EBITDA. HDS is forecasted to see 4% EBITDA growth this year and 6-7% each of the next two years. Facilities Maintenance is 55% of sales and Construction/Industrial at 45%. It sees the target markets for these segments at \$55B and \$30B respectively. It sees a number of favorable tailwinds for the Facilities Maintenance industry that it only has a 5% share. The company has been building a leading position in the fragmented Living Space MRO market which has tailwinds from an aging apartment market, growth in rental demand, and expansion of assisted living facilities. Their product scope includes appliances, HVAC, plumbing/kitchen, as well as janitorial. Multi-Family is 65%, Hospitality 19% and Healthcare 8% for the facilities it services. Their specialty construction business is a potential \$30B market opportunity where they have scale to their advantage with over 450K SKUs and a solid 200K customer base. HDS beat estimates on 6-11 but lowered the Q2 outlook as the industry as seen some headwinds due to unfavorable weather, but reaffirmed FY20. HDS does have considerable exposure to the China tariffs. About 75% of its Facilities Maintenance brands are sourced from China with around 50% of those products included in the Section 301 tariffs. HDS has also been navigating through a weaker West Coast housing market where growth slowed. Analysts have an average target of \$47.50 on shares and short interest low at 1.8% of the float. BAML was positive after the quarter with a Buy rating and \$51 target noting the issues are transitory including the delays of the new Atlanta facility and cool weather. Longbow upgraded shares to Buy in June with a \$53 target noting "valuation does not reflect the outperformance we expect from HDS' defensive Facilities Maintenance (FM) business, while recent investments should drive additional sales growth and operating leverage. Improving pricing and leverage on the A.H. Harris acquisition should benefit the Construction & Industrial business (C&I). Finally, normalized debt and lower cyclicality vs. peers supports higher a valuation with cash deployment an upside earnings kicker." Hedge Fund ownership fell 10.6% in Q1 filings, Iridian and Oz Mgmt. concentrated holders while JANA Partners has a 10.05% weighting as its 4<sup>th</sup> largest holding but reduced in Q1.

### Hawk Vision:



**Hawk's Perspective:** HDS looks solid on a move above the 200 MA, liking the valuation, call accumulation, insider buying, and potential for a long runway of better than peer average growth.

**Confidence Ranking:** \$\$