



■ *MDM Interview*

HD Supply Repositions for Growth

HD Supply's leadership talks about investments as they emerge from recession

HD Supply, Atlanta, GA, will appear on four of the five major sector lists that MDM will publish in its MDM Market Leaders report. Though a leader in many of its markets, HD Supply recorded steep losses in the past year.

HD Supply CEO Joe DeAngelo and Executive President John Stegeman recently spoke with MDM about the plans to reposition and prime HD Supply for growth in 2010 and 2011. Stegeman, former CEO of Ferguson Enterprises, is a new addition to the HD Supply team.

MDM: How is the year going so far for HD Supply?

Joe DeAngelo: I think it's going really well. All our businesses are delivering on their commitments, and that's really the result of our associates' continued dedication and passion for serving our customers. And I think we've made some awesome additions to our team, with John (Stegeman) coming on board as executive president, Joe Izganics as the senior vice president, and Ronald Domanico as our CFO.

It allows us to continue to focus all of our associates on growing profitably faster in our markets, saving as we grow, and generating cash to reduce our debt.

But the bottom line is growth, and now I have three other individuals along with myself who all share an intense passion for customers, but also have significant relevant experience in areas of our business and a track record of significant success in those areas. We're really turbo-charging around how we grow profitably faster in our markets.

John leads our branch-based businesses that serve our construction industry. So those would be our Canadian operations, our electrical business, our plumbing and HVAC business, our Waterworks business

and our White Cap business.

Joe Izganics will be leading our retail and installation services businesses, which is our Crown Bolt business, our interior service business, and our repair/remodel business. And Ron Domanico has really been brought in as our quarterback for value accretion across the portfolio. On top of being a very accomplished CFO, he was the CEO of Nabisco Asia.

MDM: Sounds like you are going through a lot of change right when the markets are starting to turn positive.

DeAngelo: For me, it is an exceptionally exciting change. We invested throughout the downturn, so we felt very good about the core investments we were putting in, in terms of digitization, in terms of expanding our markets, and really the last phase of that is just pounding in the talent at the top of the organization to be able to catch the wave of growth, but more importantly, lead the wave of growth, whether the markets are growing or not.

MDM: How do you believe the recession has had an impact on the way HD Supply and other distributors do business?

John Stegeman: Following more than a decade of incredible expansion, distributors were faced with market conditions that were really difficult to forecast. We didn't know how much business was going to be out there for us to grab. In most cases, every distributor was forced to take incredible action to hold onto market share in a declining market.

Significant cost-cutting was paramount and became the order of the day to stay relevant, and the cost reductions covered

continued on next page



all areas of the business. So in many respects, we had a chance to look at our businesses from the inside out for really the first time in a long time.

You think about companies that invested in new green-field investments that were absolutely stalled or abandoned completely as the investments just wouldn't provide a return in a fast enough period of time. And in addition, you think about larger companies like HD Supply, Ferguson, and some of the big competitors out there that were making acquisitions.

A lot of those companies made acquisitions at the absolute peak of the market, and naturally the expectation with those acquisitions is that they're going to continue to grow. And unfortunately, when they're bought at the peak, in some respects the revenues from some of those companies may represent 50 or 60 percent today of what they were when they were actually acquired. So it's very challenging.

But I think in the long run for large and small distributors who survive this, it will change the way we run our businesses in the future. Things like managing cash and being profitable is I think now much better understood, as is inventory investment, relationships with key vendors that are critical, and the customers' ability to pay for material that they purchase. In many respects businesses will be better because of what we've gone through. Our customers, our key vendors, our associates and our investors will certainly be more cautious, and perhaps a little smarter, as we invest in the future with the decisions that we have to make.

Everyone's learned that business and the investments we make must be sustainable in all market conditions. I still don't think we've seen all the fallout that we actually will see, quite honestly. And I don't think we're out of the woods yet. But I think we'll look back on these last three years as a great learning experience for the industry.

MDM: Looking forward, hopefully those changes that you mention will be sustainable, if we hit a boom again.

Stegeman: If you're not a proactive company and take a little risk in these times where we think we're running along a little bit of a bottom, I believe you'll miss out on a significant opportunity to grab additional market share as the markets come back. You don't want to sit back and wait for the market to just simply improve.

I think quite honestly there's competition out there that's probably doing that, that isn't investing, probably still downsizing, and just

waiting for something to happen. I'm excited to be part of a team that is proactive and has a leadership team here that is willing to make investments in tough times, to be able to make sure that we're looking five to 10 years down the road.

MDM: What steps has HD Supply taken to reduce cost and improve profitability? Are there challenges that you face after making these adjustments in trying to meet demand going forward?

DeAngelo: I think over the past two years, we've certainly invested a considerable amount of time and energy in consolidating our operations, automating our processes and really tightening our belt so that there's no unnecessary cost in the business. And I think a prime example of that is a process that we put in place. That process resulted in savings of over \$100 million across categories like rent, freight, postage, travel, professional fees, and telephone utilities. Everything that was non-customer-facing, we really made sure that we took the cost and waste out. We're in great shape for a bounce-back.

MDM: A lot of distributors and suppliers have cut inventory in the past. In some channels, distributors and manufacturers are facing some challenge in meeting demand again. What have you seen and how did you approach inventory management over the past year?

DeAngelo: We work very hard to align our inventory investment to the needs of the marketplace. We had an intense focus on reducing our aged inventory so we could free up funding for the inventories our customers need. We come into this period with great inventory positions. Meaning, we held enough inventory to be able to satisfy our customers' needs, and we were very thoughtful in terms of making sure that we didn't dig too deep.

We'll continue to focus on automating this area, because for us, it's about having the right product in the right place at the right time. That's our game. That's what we do. And when you look at the supply chain overall, their ability to be able to meet our needs, the capacity is there with the folks that we're working with, and we're very close to those suppliers. So we don't think that there's going to be a gap, because we've done our homework, and we'll make sure there isn't a gap.

MDM: What do you feel has been your biggest

accomplishment in the past year despite the recession?

DeAngelo: In spite of the recession, the team's done a wonderful job working with our 450,000 customers to service their needs and to continue to earn that business every day. ... Also we were able to restructure our corporate debt so our debt now matures in 2014, which is really deep into the economic recovery and at a time when all our businesses will be at peak efficiency and effectiveness. That was a big deal for us.

And then we continued to invest heavily, as we discussed, in critical growth areas for our businesses throughout the downturn. So I believe we're uniquely positioned to grow faster than the markets as they recover.

MDM: Which markets do you consider to be growth opportunities for you?

DeAngelo: Our four larger businesses are the ones that we drive growth through, in two areas. One is the core businesses that we have. So we have great core businesses in Waterworks, Facilities Maintenance, Utilities, and White Cap. We've also invested very heavily in adjacencies associated with those businesses. So a natural adjacency for our core Waterworks underground business is plant works – the water treatment plants. And that's one where we really made a name for ourselves in a short period of time in the treatment plant business, and Waterworks is a natural adjacency and extension.

Another natural adjacency would be in Facilities Maintenance. We're the No. 1 provider in multi-family housing. We're a growing player in hospitality. The adjacency there is the vertical adjacency of hotel/motel, and then a products adjacency of textiles. The linens and towels that you have in a hotel, we've got an individual who's leading our hospitality segment.

He grew up in that industry, and he has made a tremendous leap forward into how we address not only the hard side of servicing a hotel room, such as replacing the lights and the telephones. We are entering into the market supplying the people who service that room. Textile in this regard would be a new product segment. That's the way we grow.

MDM: You recently added 4,000 products to your facilities maintenance catalog. What opportunity do you see in continuing to add products to your offering?

DeAngelo: The launch of the new catalog has

been tremendous. For us this is just a natural progression. Every year we will add new products, and those products will fit existing customers' needs, and allow us entry into new customers. Those will be in the key verticals of the multi-family housing, the hospitality, and healthcare.

MDM: Are customers asking you to supply them with more products than they have in the past? Are they looking to consolidate suppliers?

DeAngelo: All the time. Our model, if you look at Facilities Maintenance, is a high service-oriented model. So you call us today, we'll deliver it to your doorstep tomorrow. That keeps the Facilities Maintenance professionals in the facility, working on the facility, and solving issues they have. And to be able to do that with more products so they don't have to get in the truck and go grab something – that is our value proposition.

MDM: It seems like M&A is picking up again. Do you think consolidation will pick up, and start once again to become a much bigger part of the market?

Stegeman: I think there are going to be significant opportunities. One of the issues we'll have is that a lot of companies that are good, or were good three or four years ago at the peak, will still consider themselves worth what they were worth four years ago. We're going to have to see some corrections in the market from a value perspective to clearly understand what a company is worth today versus what they were worth when their revenues were perhaps double what they are right now.

But I think in every type of situation there's going to be opportunities where perhaps there are business owners that don't have good succession plans that are looking for somebody to perpetuate their business. There will be synergistic opportunities, from a competitive perspective, to be able to bolt on businesses to the core businesses that we have. So you have to be active in all times, and I know that HD Supply has been active in talking with a lot of different business owners during the recession, and those communications will continue as we move forward.

MDM: Will HD Supply remain privately held, or is there a public future for the company?

DeAngelo: For us, how we capitalize the corporation is really dependent on external events. ...

As you look at the configuration of the company, it is a large company, and so therefore sometime in the future it will most likely become a public company.

But for us, the timing of that is really dependent on what happens externally relative to those capital markets. We're very comfortable running it privately forever. We're comfortable

becoming a public company. We don't think about that too much on a daily basis.

What we think about is how we're going to energize the best associates in the industry to do the absolute best job for our customers, and we've done a good job of getting our capital structure right, and that gives us flexibility to do whatever we want in the future.

Executive President John Stegeman on New Role with HD Supply

MDM: What are your goals in your new position at HD Supply, and how did you get to this position?

John Stegeman: Shortly after leaving Ferguson, I had an opportunity to sit back and think about what I wanted to do next. I wanted to understand which options would be available to really challenge me as a professional. I'm a driven individual. I wanted to pursue something that would naturally complement the skill sets that I developed over 24 years with Ferguson, and most importantly, be able to take care of my family for the future.

A friend in the vendor community put me in touch with one of the three private equity owners of HD Supply, which led to an initial interview with Joe (DeAngelo). I remember the meeting here with Joe very well. I was impressed with what I heard. As I was looking at other opportunities, this is the one that continued to come back to me, that stood out, that really complemented my skill sets.

MDM: What's your role in the organization?

Stegeman: When Joe and I met, we thought that it made sense for me to really dial in on the branch-based businesses, and certainly I'm very familiar with most of those. I want to be able to complement Joe where I can, and more importantly, I want to make the businesses that I'm responsible for extremely successful financially. So I try to keep goals relatively simple. In the short term, I want to get to know the leadership teams in the field. I've done that in the first three weeks. I've traveled extensively, spent time with the core leadership teams and discovered that we've got some extremely passionate individuals in the field. I'm looking forward to mentoring and coaching them and providing guidance for the group.

Longer term, I think we have some good opportunities in our business to be better. I'm born thinking that we have opportunities to im-

prove every day regardless of how much market share we have. There's still significant opportunity even in declining markets to be better at what you do. And most importantly, I'm very customer-oriented, and I know that all customers have choices in terms of who they want to do business with. Fielding the best teams supported by the best process and systems is going to be critical to HD's long-term success.

MDM: What have you learned in the past from Ferguson and other places you've worked that you'll bring into HD Supply in your new position?

Stegeman: As a general comparison, Ferguson is in five major businesses, and is supported by a centralized system. HD is more diversified, in 10 different businesses. So we service more customer segments with each business, and each business runs pretty autonomously. I recognized that very quickly, and I think there are advantages and challenges to both models. Certainly Ferguson has invested millions and millions of dollars in their distribution network, which works well in a rapidly growing market, and quite honestly doesn't work as well when the market is declining, because throughput through those operations is critical. So being autonomous can be advantageous; it allows you to be a little bit more flexible. But I don't think at this point I can tell you what is right or what is wrong.

In many respects, the companies are very similar. We focus on developing the best people to put in front of customers to drive the business in the construction industry. We have a lot of similarities from business to business. I think the key is profitable growth. It's critical to the lifecycles of all companies that are out there and a key element in providing those growth opportunities for our associates. I almost feel that this position was almost customized for me. And what I've seen so far is an energized organization that is walking down the right path. I'm excited to be a part of that.