1982 ANNUAL REPORT

THE HOME DEPOT

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To Our Stockholders:

The management of The Home Depot is pleased and gratified to share with you our first published Annual Report as a public company. The Home Depot only recently completed its third operating year, commencing with the opening of the first two stores in June, 1979. That year marked the beginning of the downturn in the nation's economy, however, it was during this tight economy that The Home Depot successfully expanded from approximately 120,000 square feet to 500,000 square feet of retail selling space in eight stores in two of the southeast's most active markets, Atlanta and South Florida.

During fiscal year 1981, some very notable events in the life cycle of The Home Depot occurred:

September 3, 1981 — Two new stores opened in Lauderdale Lakes and Hollywood, Florida, generating customer counts and sales far beyond projections.

September 22, 1981 — The Company had a successful initial public offering and its shares are traded on the OTC market under the NASDAQ symbol HOMD.

November 3, 1981 — The Hialeah and South Dade stores had their very successful grand openings and all stores participated in the sales excitement and product movement.

January 19, 1982 — The Company had a three-for-two stock split-up effected in the form of a dividend in order to broaden its stockholder base.

After the close of the fiscal year ending January 31, 1982, we were pleased to announce record sales and profitability despite expensing almost three-quarters of a million dollars attributed to preopening costs for the four new Florida stores.

Sales for the year increased by 131% from $22,318,493 to $51,541,957. Earnings before extraordinary item increased 168% from $452,660 ($.11 per share) to $1,211,074 ($.29 per share) and from $855,913 ($.20 per share) to $1,445,339 ($.34 per share) after the extraordinary credit relating to the utilization of prior years' net operating loss carryforwards. Fourth quarter earnings before extraordinary item increased 159% from $246,198 ($.06 per share) to $638,211 ($.15 per share).

Results indicate that The Home Depot's do-it-yourself warehouse concept has been positively accepted by our customers, whether they be novice or veteran do-it-yourselfers, or small contractors and remodelers. Despite the economy, customers are coming in record numbers to our warehouse stores.

Our success has come from hard work and we credit our employees, suppliers and manufacturers, buyers, managers and our executives with a willingness to contribute more than their share. As the number of our employees grows and as more and more customers are attracted to our stores, the harder we work to deliver the kind of merchandise that is desired.

We should note that during the months that this company doubled its size, a tremendous burden was placed upon its employees in both markets. Top management efforts to establish the new Florida stores allowed the Atlanta team to demonstrate their ability to operate with less supervision. The Atlanta group was well prepared to meet this challenge and not only supplied the key employee base for the Florida stores, but maintained their sales and earnings momentum. We are pleased to acknowledge that each of the Atlanta stores registered significant sales and earnings increases over the prior year. Furthermore, we are pleased to report that the Florida stores, since opening in the fall of 1981, are all operating profitably.

This effort has resulted in THE HOME DEPOT being voted the 1982 RETAILER OF THE YEAR in the home center industry by Building Supply News. We thank the manufacturers and other retailers in our industry for their recognition.

Our plan for the future calls for expansion; site selection studies are in progress. Continued attention to astute buying, aggressive promotion, recruitment and training of capable personnel as well as stringent emphasis on overall cost control, we believe, will allow us to continue our profitable growth.

Finally, we want to thank you, our shareholders, who have demonstrated your confidence in our management team, a confidence we intend to maintain.

Respectfully yours,

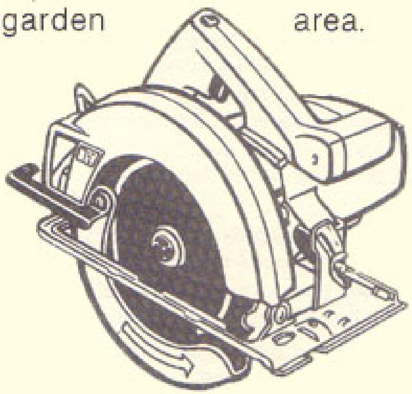
Bernard Marcus

Bernard Marcus
Chairman
Chief Executive Officer

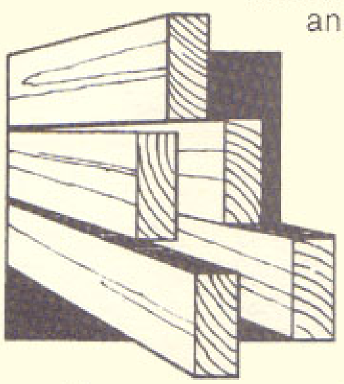
Arthur M. Blank
President
Chief Operating Officer

The Warehouse Concept

The Home Depot warehouse stores range from 63,000 to 82,000 square feet of enclosed floor space with an additional 4,000 to 10,000 square feet of outdoor garden area.



Each facility houses an indoor lumber yard, plumbing, paint, electrical, hardware, unfinished furniture, building material and seasonal departments, each larger than many free-standing specialty stores carrying just those products. Since almost every category in building materials and



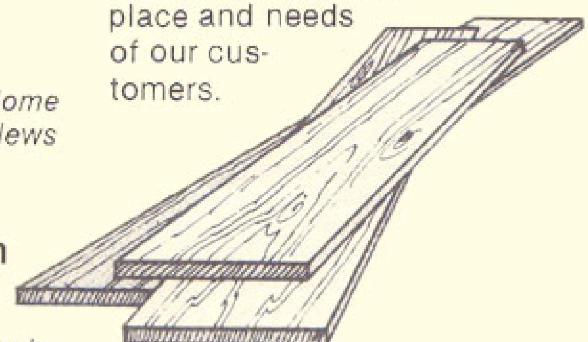
supplies can be found in great depth, it allows a do-it-yourselfer to essentially build an entire house from the store's inventory. The merchandise presentation is kept plain and simple — mass displays, open shelving, cartons stacked high and fork lifts operating on the selling floor.

> **"The two (Atlanta) units were the prototypes for a national chain of no-frills, do-it-yourself warehouses . . ."**
>
> *National Home Center News*

Extensive Selection

Two of the major copy points in Home Depot advertising have been "ONE STOP SHOPPING FOR THE DO-IT-YOURSELFER" and "WORTH THE TRIP FROM MOST ANYWHERE". Selection, variety and depth of assortment that The Home Depot maintains are the basis of these claims. The selection within each de-

partment is abundant and always a quality product. The customer is assured of finding what he wants, when he wants it. The Home Depot is continually adding or deleting product lines, as well as introducing new product sizes, packaging and innovations. The merchandise mix is kept fluid and carefully adjusted to meet the changing marketplace and needs of our customers.



Name Brands

Nationally advertised brands are prominent throughout the store. The result is aisle after aisle of items that have product recognition and that a shopper can select with confidence and assurance.

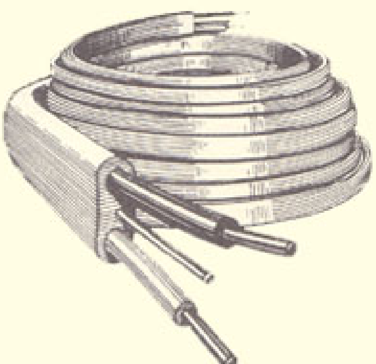
Promotional Pricing

The Home Depot stresses promotional pricing and prides itself on offering do-it-yourselfers outstanding value.

Five factors go into The Home Depot pricing formula:

(1) Direct buying;

(2) Buying at volume levels;

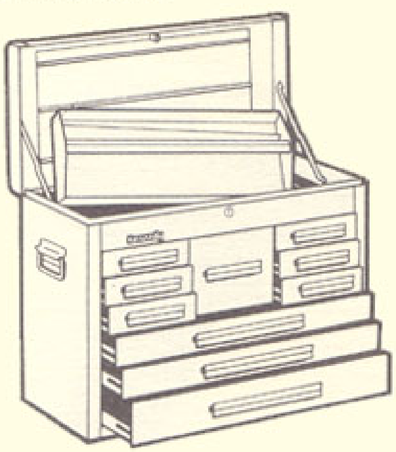


(3) Vendors shipping direct to stores;

(4) Cash and carry operation; and

(5) Selling at a lower gross margin.

This pricing formula has generated a high sales volume and rapid turnover of inventory.



Customer Service

At The Home Depot, service is paramount. Store personnel are trained to help the customer plan a project and select all of the necessary materials and supplies to finish it properly.

> **"The merchandising philosophy is clear . . . it's geared to high volume and high turnover at lower than normal margins."**
>
> *Hardware Retailing*

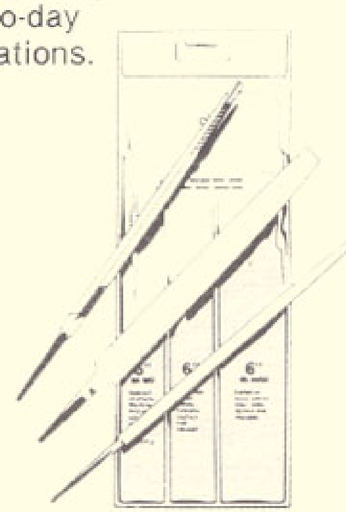
The stores contain many informational signs and working displays that show products and their applications.

To further enhance its image as headquarters for all do-it-yourself activity, The Home Depot schedules clinics, seminars, and show-and-tell sessions for the public.

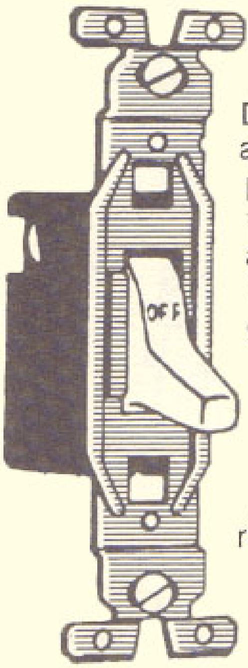
Employee Training

The Home Depot philosophy requires that store personnel be knowledgeable and capable of answering customer questions about products and their applications. Personnel are encouraged to expand their abilities so that they may grow with the Company. Management training seminars and product training sessions are held on a regularly scheduled basis.

In addition, store level meetings and critique sessions are held to encourage employee feedback and to keep management aware of day-to-day operations.



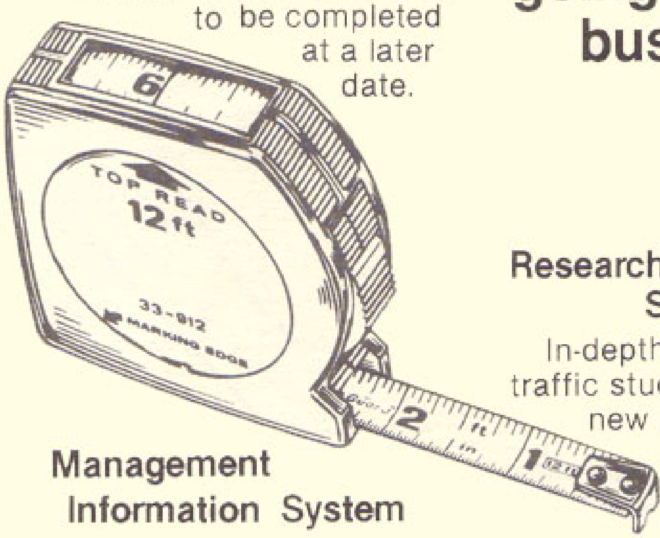
Advertising and Promotion



The Home Depot is a 52-week advertiser. Newspapers, radio, television, direct mail and in-store promotions are used aggressively. Author and personality, Super Handyman Al Carrell, is The Home Depot spokesman on radio and television.

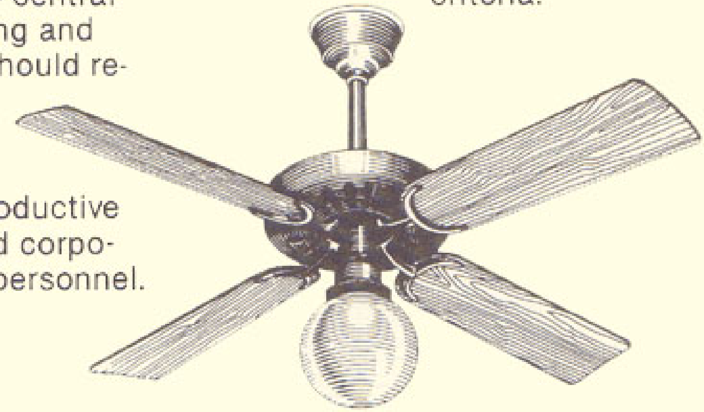
Atlanta Expansion Underway

Always working to improve its operations, The Home Depot is now in the process of enlarging its Atlanta retail warehouses. By April 30, 1982, three of the stores will have already completed their expansion to over 72,000 square feet, with the fourth scheduled to be completed at a later date.



Management Information System

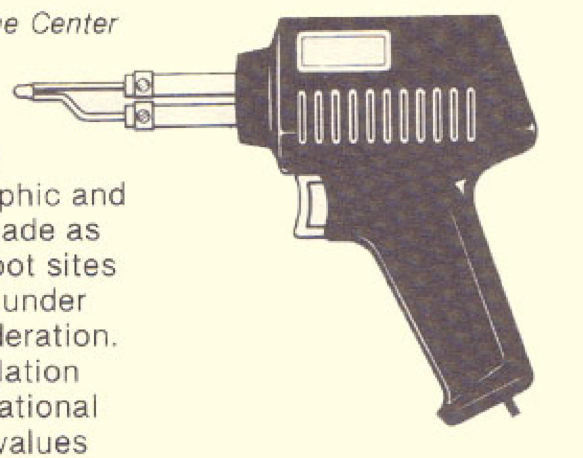
The Home Depot will be installing its pilot point-of-sale Management Information System program in a test store during the summer of 1982. The system should facilitate not only more efficient customer checkouts but also central control over ordering and distribution. This should result in improvement in merchandise inventory levels and more productive use of its store and corporate management personnel.



"In order to expand, we understand that we have to have the knowledge as to what is going on in our business."

Home Center

Researched Site Selection



In-depth demographic and traffic studies are made as new Home Depot sites come under consideration. Population shifts, income, educational levels, and housing values are all considered.

The Home Depot's plan is to continue an expansion program, but only into those communities that meet its specific demographic criteria.

Active Recruitment

Attracting qualified talent to the organization is something The Home Depot management actively pursues. By promoting from within and infusing the Company with new people with fresh ideas, The Home Depot is establishing itself within the do-it-yourself industry and the communities which it serves.

SELECTED FINANCIAL DATA

	Fiscal Years Ended January 31, 1982	Fiscal Years Ended February 1, 1981	Fiscal Years Ended January 27, 1980	Period From June 29, 1978 (Date of Inception) to January 28, 1979
Selected Statement of Earnings (Loss) Data:				
Sales	$51,541,957	$22,318,493	$7,025,499	$ —
Gross profit	$14,735,039	$ 6,855,391	$2,024,989	$ —
Earnings (loss) before income taxes and extraordinary item	$ 1,962,966	$ 855,913	$ (930,050)	$(354,188)
Earnings (loss) before extraordinary item	$ 1,211,074	$ 452,660	$ (930,050)	$(354,188)
Extraordinary item — reduction of income taxes arising from carry-forward of prior years' operating losses	$ 234,265	$ 403,253	$ —	$ —
Net earnings (loss)	$ 1,445,339	$ 855,913	$ (930,050)	$(354,188)
Per common and common equivalent share:[1]				
Earnings (loss) before extraordinary item	$ .29	$ .11	$ (.24)	$ (.12)
Extraordinary item	$ .05	$ .09	—	—
Net earnings (loss)	$ .34	$ .20	$ (.24)	$ (.12)
Weighted average number of common and common equivalent shares	4,210,017	4,299,251	3,861,256	2,989,059
Selected Balance Sheet Data:				
Total assets	$16,905,865	$ 4,506,720	$3,507,318	$ 231,893 [2,3]
Long-term debt	3,590,000	990,000	1,600,000	—
Non-current obligations under capital lease	147,736	22,575	34,708	—
Redeemable preferred stock — Series A	—	1,875,900	1,875,900	413,400 [2]
Series B	—	48,850	48,850	11,350 [2]
Stockholders' equity (deficit)	$5,203,663	$ (284,700)	$(1,141,413)	$(264,538)[3]

[1] Adjusted for the three-for-two stock split-up effected in the form of a dividend in January, 1982.

[2] Total assets and redeemable preferred stock are net of receivables aggregating $1,500,000 at January 28, 1979 representing $1,462,500 in Series A Preferred Stock and $37,500 in Series B Preferred Stock at par.

[3] Total assets and stockholders' equity are net of $33,600 in notes receivable from officers for purchase of Common Stock.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

The data below reflect the percentage relationship between sales and major categories in the Statements of Earnings (Loss) and selected sales data and the percentage change in the dollar amounts of each of the items.

	Fiscal Years Ended			Percentage increase (decrease) of dollar amounts	
	Jan. 31, 1982	Feb. 1, 1981	Jan. 27, 1980	Fiscal Year 1981 v. 1980	Fiscal Year 1980 v. 1979
Selected Statement of Earnings (Loss) Data:					
Sales	100.0%	100.0%	100.0%	130.9%	217.7%
Gross profit	28.6	30.7	28.8	114.9	238.5
Costs and expenses					
Selling and store operating	19.0	20.6	24.7	112.8	164.3
Preopening	1.5	.2	4.0	1512.0	(82.8)
General and administrative	3.7	4.3	12.4	97.0	10.9
Interest, net	.6	1.8	.9	(19.3)	498.0
	24.8	26.9	42.0	112.9	103.0
Earnings (loss) before income taxes and extraordinary item	3.8	3.8	(13.2)	129.3	
Income taxes	1.5	1.8	—	86.5	
Earnings (loss) before extraordinary item	2.3	2.0	(13.2)	167.5	
Extraordinary item	.5	1.8	—	(41.9)	
Net earnings	2.8%	3.8%	(13.2)%	68.9%	
Selected Sales Data:					
Number of sales transactions	1,915,852	888,949	325,717	115.5% *	172.9% *
Average sale per transaction	$ 26.90	$ 25.11	$ 21.57	7.1	16.4
Weighted average weekly sales per operating store	$186,746	$107,300	$81,691	74.0	31.4

*Represents change in number of sales transactions, not dollar amount.

Results of Operations

Since the opening of the Company's first two stores in June 1979, advertising and promotions have been directed toward the retail do-it-yourself and home remodelers market. As a result of this orientation, the Company's sales have increased significantly despite high interest rates and reduced housing starts because these economic conditions encourage the expansion and improvement of existing homes. Management anticipates, based on its prior industry experience, that during a recovery in housing and economic activity, operating results should be favorably affected by a shift in purchasing patterns of homeowners to higher profit margin products.

Fiscal year ended January 31, 1982 compared to February 1, 1981.

Sales in fiscal 1981 increased 131% from $22,318,493 to $51,541,957. This growth was partially attributable to the opening of four stores in southern Florida (two in September 1981 and two in November 1981). Another major factor contributing to this increase was wider acceptance of the Company's merchandising concepts in the Atlanta market which resulted in significant increases in sales for the four Atlanta stores. The number of sales transactions increased 116% and the average sale per transaction increased 7%. During fiscal 1981, the other tenant at the Company's Atlanta locations commenced going out of business sales and these promotions attracted a significant number of customers to the Company's stores. The Company also took advantage of this opportunity by expanding its visibility through aggressive advertising and merchandising. This, together with the wider acceptance of the Company's merchandising concepts noted above, accounted for a significant increase in the store-for-store sales over the prior year.

Gross profit in fiscal 1981 increased 115% from $6,855,391 to $14,735,039 due to the increase in sales. The 2.1% reduction in the gross profit margin resulted from the Company's more aggressive pricing in the Atlanta market area as well as the promotional strategy that was adopted in order to obtain a market share in the new southern Florida market.

Earnings before income taxes and extraordinary item increased in fiscal 1981 from $855,913 to $1,962,966 due to the greater sales volume, related operating economies of scale and cost efficiencies realized by the Company. While costs and expenses increased 113% during fiscal 1981, they declined as a percentage of sales from 27% to 25%. Of the increase in costs and expenses, $726,666 (12.1% of the increase) represents an increase in preopening expenses resulting from the Florida expansion.

Net earnings in fiscal 1981 increased 69% from $855,913 to $1,445,339 as a result of greater sales and lower costs and expenses as a percent of sales. This increase resulted despite a higher effective income tax rate associated with utilization of all the remaining net operating loss carryforwards.

Fiscal year ended February 1, 1981 compared to January 27, 1980

Sales in fiscal 1980 increased 218% from $7,025,499 to $22,318,493, as a result of opening one additional store at the end of February 1980 and the three other stores' operating for a full year. The number of sales transactions in fiscal 1980 increased 173% from 325,717 to 888,949 and the average sale per transaction increased 16% from $21.57 to $25.11. The gross profit margin increased from 29% to 31% due to the promotion activities in the prior year associated with new store openings. Costs and expenses were reduced as a percentage of sales during fiscal 1980 because of the increased sales volume which enabled the Company to achieve certain operating economies of scale and cost efficiencies. These changes resulted in the increase in fiscal 1980 earnings.

Impact of Inflation and Changing Prices

Although the Company cannot accurately determine the precise effect of inflation, it has experienced higher costs of merchandise and increased operating expenses. The Company attempts to offset these higher costs by increasing selling prices in order to maintain desired profit margins.

Liquidity and Capital Resources

Cash flow generated from operations provides the Company with its most important source of liquidity since at least 97% of sales are on a cash-and-carry basis. In addition, a significant portion of the Company's inventory is financed under vendor credit terms. The Company supplements operating cash flow from time to time with bank credit. These sources of liquidity are used for payments on accounts payable for inventory and operating expenses.

The only significant scheduled capital expenditure for the balance of fiscal 1982 is the installation of in-store mini computers to support point of sale terminals. It is anticipated that such hardware for the Company's existing eight stores will cost approximately $500,000 and will be financed through capital leases.

Balance Sheets

January 31, 1982 and February 1, 1981

ASSETS	1982	1981
CURRENT ASSETS:		
Cash (note 2)	$ 1,617,907	$ 112,045
Accounts receivable, less allowance for doubtful receivables of $56,992 at January 31, 1982 and $16,666 at February 1, 1981	415,272	171,823
Merchandise inventories	11,263,474	2,881,331
Prepaid expenses	77,264	87,851
TOTAL CURRENT ASSETS	13,373,917	3,253,050
PROPERTY AND EQUIPMENT, AT COST (notes 2 and 7):		
Furniture and fixtures	1,291,456	541,772
Automotive equipment	59,882	37,529
Leasehold improvements	2,299,857	800,844
Capital leases, principally computer equipment at January 31, 1982	186,510	50,202
	3,837,705	1,430,347
Less accumulated depreciation and amortization	334,436	184,168
NET PROPERTY AND EQUIPMENT	3,503,269	1,246,179
OTHER ASSETS	28,679	7,491
	$ 16,905,865	$ 4,506,720

LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)	1982	1981
CURRENT LIABILITIES:		
Current portion of long-term debt (note 2)	$ 340,000	$ 110,000
Current portion of capital lease obligations (note 7)	29,003	12,133
Accounts payable	6,315,193	1,321,099
Accrued salaries and related expenses	377,090	166,972
Accrued interest	89,689	121,976
Accrued property taxes	295,864	121,915
Income taxes payable (note 5)	424,627	—
TOTAL CURRENT LIABILITIES	7,871,466	1,854,095
Long-term debt, excluding current installments (note 2)	3,590,000	990,000
Capital lease obligations, excluding current installments (note 7)	147,736	22,575
TOTAL LONG-TERM DEBT AND CAPITAL LEASE OBLIGATIONS	3,737,736	1,012,575
Deferred income taxes (note 5)	93,000	—
REDEEMABLE PREFERRED STOCK OF $50 PAR VALUE. Authorized: 40,000 Shares at February 1, 1981, issuable in series (note 3):		
Series A nonvoting, redeemable at par. Issued 37,518 shares	—	1,875,900
Series B nonvoting, redeemable at par. Issued 977 shares	—	48,850
TOTAL REDEEMABLE PREFERRED STOCK	—	1,924,750
STOCKHOLDERS' EQUITY (DEFICIT)—(notes 2, 3, 4, and 6):		
Common stock, par value $.05. Authorized: 4,000,000 shares; issued and outstanding 3,995,394 shares at January 31, 1982 and 2,872,500 shares at February 1, 1981	199,770	143,625
Paid-in capital	3,986,879	—
Retained earnings (accumulated deficit)	1,017,014	(428,325)
TOTAL STOCKHOLDERS' EQUITY (DEFICIT)	5,203,663	(284,700)
Commitments and contingent liabilities (notes 2, 6, 7, and 8)		
	$ 16,905,865	$ 4,506,720

See accompanying notes to financial statements.

Statements of Earnings (Loss)

Years Ended January 31, 1982, February 1, 1981, and January 27, 1980

	1982	1981	1980
SALES	$51,541,957	$22,318,493	$ 7,025,499
COST OF SALES	36,806,918	15,463,102	5,000,510
GROSS PROFIT	14,735,039	6,855,391	2,024,989
OPERATING EXPENSES:			
Selling and store operating expenses	9,780,382	4,597,079	1,739,070
Preopening expenses	774,725	48,059	279,589
General and administrative expenses	1,903,655	966,313	871,489
TOTAL OPERATING EXPENSES	12,458,762	5,611,451	2,890,148
OPERATING INCOME (LOSS)	2,276,277	1,243,940	(865,159)
OTHER INCOME (EXPENSE):			
Interest expense	(334,213)	(388,027)	(89,928)
Interest income	20,902	—	25,037
	(313,311)	(388,027)	(64,891)
EARNINGS (LOSS) BEFORE INCOME TAXES AND EXTRAORDINARY ITEM	1,962,966	855,913	(930,050)
INCOME TAXES (note 5)	751,892	403,253	—
EARNINGS (LOSS) BEFORE EXTRAORDINARY ITEM	1,211,074	452,660	(930,050)
EXTRAORDINARY ITEM — Reduction of Income Taxes arising from carryforward of prior years' operating losses (note 5)	234,265	403,253	—
NET EARNINGS (LOSS)	$ 1,445,339	$ 855,913	$ (930,050)
EARNINGS (LOSS) PER COMMON AND COMMON EQUIVALENT SHARE (note 4):			
Earnings (loss) before extraordinary item	$ .29	$ .11	$ (.24)
Extraordinary item	.05	.09	—
NET EARNINGS (LOSS)	$ .34	$ .20	$ (.24)
WEIGHTED AVERAGE NUMBER OF COMMON AND COMMON EQUIVALENT SHARES (note 4)	4,210,017	4,299,251	3,861,756

See accompanying notes to financial statements.

Statements of Stockholders' Equity (Deficit)

Years Ended January 31, 1982, February 1, 1981, and January 27, 1980

	Common stock			Retained earnings	Notes receivable	
	Shares	Amount	Paid-in capital	(accumulated deficit)	from officers for common stock	Total stockholders' equity (deficit)
BALANCE, JANUARY 28, 1979	2,465,000	$123,250	$ —	$ (354,188)	$ (33,600)	$(264,538)
Shares sold under employee stock purchase plan (note 6)	124,000	6,200	—	—	—	6,200
Shares sold to existing stockholders (note 2)	147,500	7,375	—	—	—	7,375
Shares sold to officer under employment agreement	120,000	6,000	—	—	—	6,000
Collection of notes receivable	—	—	—	—	33,600	33,600
Net loss	—	—	—	(930,050)	—	(930,050)
BALANCE, JANUARY 27, 1980	2,856,500	142,825	—	(1,284,238)	—	(1,141,413)
Shares sold under employee stock purchase plan (note 6)	16,000	800	—	—	—	800
Net earnings	—	—	—	855,913	—	855,913
BALANCE, FEBRUARY 1, 1981	2,872,500	143,625	—	(428,325)	—	(284,700)
Shares contributed to the Company	(3,125)	(156)	156	—	—	—
Shares shold to existing stockholders through exercise of warrants (note 2)	24,000	1,200	118,800	—	—	120,000
Sale of common stock under initial public offering, net of expenses of sale	400,000	20,000	4,073,435	—	—	4,093,435
Redemption of common stock (note 3)	(629,764)	(31,488)	(138,548)	—	—	(170,036)
Three-for-two stock split, net of redemption of fractional shares (note 4)	1,331,783	66,589	(66,964)	—	—	(375)
Net earnings	—	—	—	1,445,339	—	1,445,339
BALANCE, JANUARY 31, 1982	3,995,394	$199,770	$3,986,879	$1,017,014	$ —	$5,203,663

See accompanying notes to financial statements.

Statements of Changes in Financial Position

Years Ended January 31, 1982, February 1, 1981, and January 27, 1980

	1982	1981	1980
SOURCES OF WORKING CAPITAL:			
Earnings (loss) before extraordinary item	$ 1,211,074	$ 452,660	$ (930,050)
Items which do not use working capital:			
Depreciation and amortization of property and equipment	175,655	126,513	54,939
Deferred income taxes	93,000	—	—
Other	8,830	6,764	4,210
WORKING CAPITAL PROVIDED (USED) BY OPERATIONS EXCLUSIVE OF EXTRAORDINARY ITEM	1,488,559	585,937	(870,901)
Extraordinary item — utilization of net operating loss carryforwards	234,265	403,253	—
WORKING CAPITAL PROVIDED (USED) BY OPERATIONS	1,722,824	989,190	(870,901)
Proceeds from sale of property and equipment, net	54,978	—	—
Increase in long-term debt and capital lease obligations	3,173,959	—	1,634,708
Sale of preferred stock, including collections of receivables	—	—	1,500,000
Sale of common stock, net — including collections of receivables	4,213,435	800	53,175
Other, net	—	—	1,239
	$ 9,165,196	$ 989,990	$ 2,318,221
USES OF WORKING CAPITAL:			
Additions to property and equipment	$ 2,487,723	$ 186,408	$ 1,222,134
Current installments and repayments of long-term debt and capital lease obligations	448,798	622,133	—
Repurchase of common stock	170,411	—	—
Redemption of preferred stock	1,924,750	—	—
Other, net	30,018	—	—
Increase in working capital	4,103,496	181,449	1,096,087
	$ 9,165,196	$ 989,990	$ 2,318,221
CHANGES IN COMPONENTS OF WORKING CAPITAL:			
Increase (decrease) in current assets:			
Cash	$ 1,505,862	$ (3,072)	$ (64,484)
Accounts receivable, net	243,449	100,777	71,046
Employee relocation advances	—	—	(10,000)
Merchandise inventories	8,382,143	800,948	2,080,383
Prepaid expenses	(10,587)	47,618	36,734
	10,120,867	946,271	2,113,679
Increase (decrease) in current liabilities:			
Current portion of long-term debt and capital lease obligations	246,870	112,055	10,078
Accounts payable	4,994,094	406,399	852,743
Accrued salaries and related expenses	210,118	82,876	74,372
Accrued interest	(32,287)	71,617	50,359
Accrued property taxes	173,949	91,875	30,040
Income taxes payable	424,627	—	—
	6,017,371	764,822	1,017,592
INCREASE IN WORKING CAPITAL	$ 4,103,496	$ 181,449	$ 1,096,087

See accompanying notes to financial statements.

Notes to Financial Statements

(1) Summary of Significant Accounting Policies

(a) Basis of Presentation

The Home Depot, Inc. (Company) was incorporated in Delaware on June 29, 1978 for the purpose of establishing retail do-it-yourself home improvement stores. During the fiscal year ended January 27, 1980, the Company began store operations by opening three retail stores. A fourth retail store was opened in February 1980 and four additional stores were opened during the latter part of 1981. The Company's fiscal year ends on the Sunday closest to the last day of January and usually consists of 52 weeks. Every five or six years, however, there is a 53-week year, as was the case with the year ended February 1, 1981.

(b) Inventories

Merchandise inventories are stated at the lower of cost (first-in, first-out) or market, as determined by the retail inventory method.

(c) Depreciation and Amortization

Furniture, fixtures, and equipment are depreciated using the straight-line method over the estimated useful lives of the assets. Improvements to leased premises are amortized on the straight-line method over the life of the lease or the useful life of the improvement, whichever is shorter. Equipment obtained under capital leases is amortized by the straight-line method over the lease term.

(d) Investment Tax Credits

Investment tax credits are recorded as a reduction of Federal income taxes in the year the credits are realized.

(e) Store Preopening Expenses

Preopening costs related to new store openings are expensed as incurred.

(f) Earnings Per Common and Common Equivalent Share

Earnings per common and common equivalent share are based on the weighted average number of shares and common equivalents outstanding after adjustment for the three-for-two stock split in 1982.

(2) Financing

The Company has an agreement in effect for the following borrowings:

A $1,700,000 revolving line of credit at February 1, 1981 at prime plus 1½%, interest paid quarterly. The balance outstanding under this line of credit at July 31, 1981 ($1,700,000) was converted to a term loan, payable in 20 equal quarterly installments beginning October 31, 1981. As of January 31, 1982 and February 1, 1981, the Company had $1,530,000 and $1,100,000, respectively, outstanding under this line of credit, of which $340,000 and $110,000, respectively, was classified as current. At January 31, 1982, the interest rate was prime plus 1%.

A $3,500,000 revolving line of credit at prime plus 1%, interest paid quarterly. The line of credit will convert to a term loan on July 31, 1983, the then outstanding balance of which will be payable in 20 equal quarterly installments beginning October 31, 1983. At January 31, 1982, the Company had $2,400,000 outstanding under this line of credit, all of which is classified as long-term debt.

A $1,500,000 line of credit (increased from $1,000,000 effective June 22, 1981) for working capital purposes at prime plus ½%, interest paid quarterly until April 30, 1982. The Company had no borrowings outstanding under this line as of January 31, 1982 and February 1, 1981.

The above borrowings are secured by a lien on all present and future furniture, fixtures, and equipment. Under the terms of the credit agreement dated June 22, 1981, the Company is required among other requirements to:

a. Maintain tangible net worth of not less than $1,600,000 plus 80% of cumulative net earnings beginning with the fiscal year ending January 31, 1982.

b. Not exceed ratios of total debt to tangible stockholders' equity of amounts ranging from a high of 700% during the current fiscal year to a low of 250% subsequent to January 30, 1983.

c. Maintain a current ratio of not less than 1.4 to 1.

d. Maintain working capital of at least $1,900,000.

e. Not declare or pay any dividends (other than dividends payable in common stock of the Company).

The Company is also required to pay a commitment fee of ½% per annum (payable quarterly) on the unused portion of the $3,500,000 line of credit. Additionally, the Company is required to maintain collected bank balances amounting to 5% of the total commitment plus 5% of the amounts outstanding.

Maturities during the next five years of the amounts outstanding under the $1,700,000 term loan and the $3,500,000 line of credit (assuming the maximum amount available is outstanding at the conversion date) at January 31, 1982 are as follows:

1983	$ 340,000
1984	690,000
1985	1,080,000
1986	1,080,000
1987	870,000

As an inducement for issuing letters of credit under the Company's original bank financing in May 1979, the participating stockholders were allowed to purchase 147,500 shares of common stock at par value. Additionally, 47,500 of the aforementioned 147,500 shares were subject to mandatory repurchase provisions (note 3).

In connection with the renegotiation of the Company's credit agreement, effective June 22, 1981, the then existing letters of credit were cancelled and new letters of credit aggregating $1,000,000 were issued. As an inducement for issuing the letters of credit, the participating shareholders received and exercised warrants to purchase 24,000 shares of common stock at $5 per share. The letters of credit were cancelled by the bank subsequent to the Company's initial public offering in September 1981.

The following information is provided with respect to the short-term borrowings under the working capital line of credit:

	Fiscal years ended		
	January 31, 1982	February 1, 1981	January 27, 1980
Maximum amount outstanding during period	$1,400,000	$700,000	$500,000
Average daily amount outstanding	$ 370,000	$153,000	$172,000
Daily weighted average interest rates on borrowings	20%	16%	14%

(3) Redeemable Preferred Stock

Series A preferred stock was redeemable at par at any time at the Company's option. However, redemption was mandatory when the Company's stockholders' equity and redeemable preferred stock at the end of its fiscal year equaled or exceeded $10,000,000. Upon redemption of the Series A preferred, certain investors were required to sell to the Company 39½% of the shares of common stock (an aggregate of 582,264 shares) owned by such investors for the then book value. Additionally, 33⅓% of the common shares (an aggregate of 47,500 shares) sold to the participating shareholders at the time of the issuance of the original letters of credit (note 2) were required to be sold to the Company at such time and on the same basis. Series B preferred stock was redeemable at par value plus accrued dividends at any time subsequent to the redemption of Series A preferred stock at the investor's option.

Subsequent to the initial public offering of the Company's common stock in September 1981, the Company redeemed the Series A and Series B preferred stock at par value and all of the redeemable shares of common stock, aggregating 629,764 shares, at the August 2, 1981 book value of $.27 per share. The redemption was made pursuant to a modification to the Shareholders' Agreement dated July 23, 1981 between the Company and the holders of such shares.

The following is a summary of the changes in the redeemable preferred stock:

	Series A		Series B		
	Shares	Amount	Shares	Amount	Total
Shares issued	37,518	$ 1,875,900	977	$ 48,850	$ 1,924,750
Less receivables for preferred stock	—	(1,462,500)	—	(37,500)	(1,500,000)
Balance — January 28, 1979	37,518	413,400	977	11,350	424,750
Collections of receivables for preferred stock	—	1,462,500	—	37,500	1,500,000
Balance — January 27, 1980 and February 1, 1981	37,518	1,875,900	977	48,850	1,924,750
Redemption of preferred stock	(37,518)	(1,875,900)	(977)	(48,850)	(1,924,750)
Balance — January 31, 1982	—	$ —	—	$—	$ —

At January 31, 1982, there are no preferred shares authorized for issuance.

(4) Common Stock

The authorized common stock was increased from 3,000,000 to 4,000,000 shares in August 1981.

On December 23, 1981, the Board of Directors authorized a three-for-two stock split of the Company's common stock effected in the form of a dividend with the par value remaining at $.05 per share. Such distribution on January 19, 1982 resulted in the transfer of $66,589 to common stock from paid-in capital. All per share amounts and other share information have been adjusted to reflect this transaction.

(5) Income Taxes

The provision for income taxes consists of the following:

	Fiscal years ended					
	January 31, 1982			February 1, 1981		
	Current	Deferred	Total	Current	Deferred	Total
Federal	$512,623	93,000	605,623	351,069	—	351,069
State	146,269	—	146,269	52,184	—	52,184
TOTAL	$658,892	93,000	751,892	403,253	—	403,253

The provisions for income taxes represent the amounts that would be provided were net operating loss carryforwards not available. The above provisions were offset by $234,265 and $403,253 of available carryforwards for the fiscal years ended January 31, 1982 and February 1, 1981, respectively. Such carryforwards are included as an extraordinary item in the accompanying statement of earnings (loss).

A reconciliation of income taxes from Federal statutory rates to actual tax rates for the applicable periods follows:

	Fiscal years ended	
	January 31, 1982	February 1, 1981
Income taxes at Federal statutory rate, net of surtax exemption	$883,714	$375,074
State income taxes, net of Federal income tax benefit	78,985	28,179
Investment tax credits, including $79,400 carried forward from prior years	(220,695)	—
Other, net	9,888	—
	$751,892	$403,253

No provision for income taxes was recorded for the fiscal year ended January 27, 1980 since the Company had an operating loss for that year and for the period from June 29, 1978 (date of inception) to January 28, 1979.

Deferred income tax expense results from timing differences between depreciation expense computed for financial reporting purposes and deductions computed for income tax purposes in accordance with "The Economic Recovery Tax Act of 1981" for property and equipment acquired after December 31, 1980.

(6) Employee Stock Plans

The Company had in effect an Employee Stock Purchase Plan for officers and key employees. Under this plan, options aggregating 140,000 shares were granted at the discretion of the Board of Directors and were exercisable at par value within 60 days from the date of grant. The agreement was terminable at any time by the Board of Directors. Options for 124,000 shares ($6,200) were granted and exercised during the fiscal year ended January 27, 1980 and 16,000 shares ($800) during the fiscal year ended February 1, 1981. Par value was determined to be equivalent to fair value at the dates of the grants due to the start-up phase of the Company's operations and the resulting stockholders' deficit. At January 31, 1982 and February 1, 1981, there were no additional shares available for future grants.

The Company's Board of Directors adopted an Employee Incentive Stock Option Plan on August 4, 1981 (as amended September 21, 1981) under which 187,500 shares of common stock (as restated for the three-for-two stock split — see note 4) were authorized for future grants at fair market value at date of grant. Such options may be exercised at the rate of 25% per year commencing with the first anniversary date of the grant and expire after five years. At January 31, 1982, options for 115,680 shares had been granted at $8.00 to $14.25 per share and 71,820 common shares were available for future grants under the plan. The plan is subject to stockholder approval within twelve months of adoption by the Board of Directors.

(7) Leases

The Company leases retail, office, and distribution space, equipment, and vehicles under operating leases. All leases will expire within the next 22 years; however, it can be expected that in the normal course of business, leases will be renewed or replaced. Total rent expense for the fiscal years ended January 31, 1982, February 1, 1981, and January 27, 1980 amounted to approximately $1,096,000, $698,000, and $300,000, respectively. The lease for office space provides that the lessor pay real estate taxes, insurance, maintenance, and certain other operating expenses applicable to the leased property. Under the store leases, real estate taxes, insurance, maintenance, and operating expenses applicable to the leased property are obligations of the Company.

The Company leases a computer and transportation equipment under capital leases that expire in 1987 and 1984, respectively. Future minimum lease payments under operating leases and the present value of future minimum capital lease payments as of January 31, 1982 are as follows:

	Capital leases	Operating leases
1983	$ 54,605	$ 1,820,000
1984	51,685	1,809,000
1985	50,225	1,853,000
1986	50,225	1,843,000
1987	46,040	1,801,000
1988 - 2003	—	21,325,000
	252,780	$30,451,000
Less amount representing interest (at rates varying from 15.5% to 18.3%)	76,041	
Present value of net minimum capital lease payments	176,739	
Less current installments of obligations under capital leases	29,003	
Long-term obligations under capital leases	$147,736	

During February 1982, existing leases on certain retail stores were modified to provide additional retail space. The modifications thereto will result in additional annual lease payments approximating $173,000. In conjunction with the expansion of these stores, the Company has committed to spend approximately $300,000 for capital improvements.

(8) Commitments and Contingent Liabilities

The Company has been named as a defendant in certain legal actions. In the opinion of management and legal counsel, the ultimate liability to the Company, if any, not covered by insurance will not have a material effect on the financial position or results of operations.

At January 31, 1982, the Company is contingently liable for bank letters of credit aggregating $1,816,000 issued for purchases of merchandise.

Accountants' Report

Peat, Marwick, Mitchell & Co.

Certified Public Accountants

2100 Peachtree Center South
Atlanta, Georgia 30303

The Board of Directors
The Home Depot, Inc.:

We have examined the balance sheets of The Home Depot, Inc. as of January 31, 1982 and February 1, 1981, and the related statements of earnings (loss), stockholders' equity (deficit), and changes in financial position for each of the years in the three-year period ended January 31, 1982. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned financial statements present fairly the financial position of The Home Depot, Inc. at January 31, 1982 and February 1, 1981, and the results of its operations and the changes in its financial position for each of the years in the three-year period ended January 31, 1982, in conformity with generally accepted accounting principles applied on a consistent basis.

Peat, Marwick, Mitchell & Co.

March 24, 1982

Directors

Bernard Marcus, *Chairman of the Board*
Arthur M. Blank, *President and Director*
Patrick G. Farrah, *Executive Vice President and Director*
Berry R. Cox, *Director*
Frederick DeMatteis, *Director*
Milledge A. Hart, III, *Director*
Kenneth G. Langone, *Director*

Executive Officers

Bernard Marcus, *Chairman of the Board*
Arthur M. Blank, *President*
Patrick G. Farrah, *Executive Vice President*
Ronald M. Brill, *Vice President-Finance and Treasurer*

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ANNUAL REPORT ON FORM 10-K
A copy of the Company's Annual Report on Form 10-K is enclosed as a supplement to this Annual Report to Stockholders.