

# THE PARLIMENT PAGES

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## WHAT WILL 2008 BE LIKE?

If I had to answer that question with one word, the word would be "better." Now if you want an expansion on that, it becomes a little fuzzier.

There is no doubt in our minds that we will see a gradual increase month over month throughout 2008. We think, starting in January, that our sales will increase about 1½ % each month on a 12 month rolling average basis. That will give us an overall increase of about 12% over 2007 results. It will be slow and methodical, and will not make the headlines, but it will definitely trend upward.

## WHAT IS OUR RATIONALE FOR THIS PREDICTION

Over and over we have preached the fundamentals of housing. To review, those 5 fundamentals are:

1. Interest rates
2. Job growth
3. Population growth
4. Population demographics
5. Foreign investment

Despite some argument from some economists, I believe that "affordability" has emerged as another fundamental.

As I have said repeatedly over the past couple of years, those 5 fundamentals still remain strong. Mortgage interest rates remain at historical lows. Job growth has remained strong, but more importantly, in the past couple of months, we are seeing real and dramatic wage increases. People are still moving into Florida at the rate of 1,000 people per day and South Georgia is seeing the biggest population increase in history. The most money spent on housing is in the 45 -54 age group and our market area continues to lead the country in that growth. The dollar continues its slide and European investment and second home money is still there. Affordability has been an issue, but it appears the wage gains combined with builder price reductions will make this a problem of the past.

These same fundamentals have driven the housing industry for the past 30 years and I just don't believe there has been a change in this buying motivation. These fundamentals have been there the last couple of years and will be with us long after the news headlines have stopped screaming about the housing problems. There, you have it. Read on.

## SO WHAT IS WRONG WITH OUR INDUSTRY?

Who in their right mind would buy a house now, when the media is talking about the depressed housing market and the falling prices? There is no shortage of stupid people out there, but very few that would sign on the dotted line for a house when the price is predicted to drop over the next couple of months. We see the house buying public like a vulture, perched on a wire, waiting for the last gasp of life before they swoop down and buy at a perceived bargain price.

As long as this mentality lasts, the outstanding inventory will not be absorbed and the housing market will remain depressed. And this mentality comes from the overabundance of press.

## WHAT IS GOOD FOR US MIGHT BE BAD FOR OTHERS

As of this print date, it is too early to say for certain, however, it appears retail holiday sales are going to come in substantially lower than prior years. In addition, there are some early and significant signs

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that the automobile industry may be hitting the skids. And the best news of all is that this is an election year. Put all of these together and the news hacks are not going to have to dig for headlines. In an effort to influence the election toward their bias, the newsies will have plenty of negative targets. Hopefully this is going to take the housing industry from the front page and put it back in the classifieds where it belongs.

When the public stops reading and hearing about further price reductions, they will fly off the wire and start gobbling up the excess inventories. That will happen quickly and the new permitting and starts will kick in immediately after that.

When will this take place? Don't know for sure, but with the elections just 10 months away and a hot and increasingly bitter primary season upon us, I think you can count on sooner rather than later.

### **BROAD ECONOMIC PICTURE**

It appears all but the very pessimistic have stopped predicting an overall recession. It seems that the consensus is that any recession, if it were to happen, will not happen before the 3<sup>rd</sup> quarter of 2010. On top of that, other economic indicators are extremely strong. As previously stated, job and wage growth are moving upward. Falling interest rates and economic stimulus packages are in place and working. Savings rates are actually moving up. Bankruptcies have slowed and new business formations are setting records. All of this bodes very well for a great overall economic environment.

Having said that, I continue to ask myself why it doesn't "feel" so good. Many of our customers are struggling. Accounts receivables and bad debts are growing. Fuel prices continue to escalate. I see retail stores shuttered. I see unfinished commercial and residential construction projects. How can things be so good and yet feel so bad?

### **WE NEED TO REDEFINE HOW WE SEE GOOD AND BAD**

My wife recently returned from a day of holiday shopping. She loves to shop in specialty stores with eccentric twists. To my great pleasure, the car was empty and the credit card unused. When I asked her why she had not filled the back seat, she replied, "Everybody seems to have the same thing. I saw the same items at the small stores as I saw at the big stores, just priced higher. And it is all Chinese made junk."

A couple of days later, I happened to run into a small retailer who was closing down his business. I asked him why and he told me that he was not big enough to buy goods directly from China and had to go through multiple step distribution. As a result, he was buying the same stuff as the big boys but at a higher price. He could not remain competitive. He said that looking back, he realized that he got away from his niche and tried to compete with the big box stores selling the same items. He couldn't do it and was nailing plywood across his doors.

This is a very common story. And it is a story that will gain considerable momentum. Business has changed and it has been a significant change. I believe this change has been a fundamental move towards a value driven economy driven by price and not quality. When was the last time you felt you purchased something of quality? It probably wasn't because you did not want quality but rather you could not find it.

I recently purchased a lawn sweeper with the intention of getting my yard cleaned up on a Saturday afternoon. Upon opening the box, I realized that the product, made in China, was unassembled and complete with an assembly instruction book in 13 languages none of which were the primary language of the writer. I spent the entire afternoon assembling the unit and had to put off all work until the following weekend. After 45 minutes of use, the unit broke and I had to spend another day finding replacement parts. This also is a common story.

I think these stories point to that fundamental shift in business today. Consolidation, cheap, commoditization, and big box domination are the rules of business today. If you are not a buyer of businesses or if you don't have a business model that allows you to compete for commodity buyers, or

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if you are not a big box retailer, you should understand that you had better be in a different business space.

Too many businesses have tried to compete against this bigness in business by going head to head. That was the frustration of the small retailer who felt that his personalized service and loyal customer following alone would make up for the fact that he was selling an identical product for more money. It didn't work for him. Will it work for you?

### **IS THERE A SPACE FOR THE INDEPENDENT LUMBER DEALER AND REDI-MIX YARD?**

The answer to that is a resounding YES. At Parliment, we have over 600 customers. These customers reach across broad geographic areas with a wide variety of operating models. When times are good, virtually everyone makes money. The really successful business models are those that can prosper when times are not so good. Fortunately, most of our 600 customers are handling these bad times well. Because the market is so putrid, we have had a front row seat in seeing why part of the customer list will succeed while another part of the list will succumb during a market downturn.

### **WHAT ARE THE COMMON THREADS OF SUCCESS?**

The most prominent success factor that sticks out is profitable sales. That sounds basic but what it means is a strong focus towards gross profit and not just top line sales. The solid gross profit has come from an established customer base, focused primarily on custom homes. The custom builders seem to have a higher appreciation for service and are willing to pay for quality. In addition, they will typically lean towards branded products that yield higher margins and tend to shy away from the commoditized items.

Another success factor in our profitable customer category has been total product coverage. While it is not possible for most independent dealers to carry everything, we found the profitable ones had figured out how to meet their entire customer needs either through inventory stocking or reliable distribution on non-inventoried items. This success factor was getting everything the builder needed in his hands within a day or two.

Along with that success factor is the related aspect of knowledge. Our top tier customers have an infinite amount of knowledge and experience and spend an inordinate amount of time with their customers helping the customer to better understand new products and techniques. The custom builder is not building a "cookie cutter" and therefore has lots of opportunities to learn and build profit into his job.

We also noticed that guys still in the profit column were not turning employees over. They had a stable of sales and support people who had been with them for years. The dealers with high turnover, are almost all, struggling through this downturn.

However, the biggest success factor of all boils down to relationships. Relationships with customers, influencers and suppliers are tantamount to success. Loyalty up and down the chain seems to trump all other bad news. A real business relationship can add so many dimensions to a transaction.

So, as you enter 2008, ask yourself how you are doing with these success factors. If you can fix the ship now, you will reap huge rewards as the market turns and the tide rolls back in.

### **INDUSTRY CONSOLIDATION AND CHANGES**

In 2007, we saw a lot of changes take place in the industry. Further consolidations were happening at the same time as the Home Depot - HD Supply meltdown. Lots of transactions. We see an increased pace of change in 2008. It is likely at least 1 or 2 of the big national lumber yards will fail while others will continue to buy up independents. A lot of marginal independents will throw in the towel and cease business in the final seconds of the 10<sup>th</sup> round, unable to hold out. There will be more vertical integration as manufacturers buy up distribution and fabrication. Distributors are closing down and/or

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limiting and revising product offerings. National builders will continue to yield market share to local builders, many of whom sold out to the nationals a few years ago and are now back in business.

*The most important role of a business owner is to navigate his business through change. You are about to face the year of biggest industry change in history.* Please make sure that you have established the right strategies to best cope with this change. How your business looks 5 years from now may very well be a reflection of the decisions you make today.

### **INTEREST RATES**

*The FED will continue to stimulate the economy through rate reductions.* We have already experienced a couple of major cuts and we can count on a few more throughout 2008. *The general consensus is that short-term rates will probably be about a full point lower this time next year.* There doesn't seem to be a lurking threat of inflation to change this outlook and the FED seems to be taking a more proactive political approach to monetary policy.

### **FUEL COSTS**

Gasoline seems to have settled at that \$3 per gallon threshold. We expect that it will stay there on a semi-permanent basis with very little likelihood of any kind of sustained reduction. To the contrary, we think pressure will build by next summer to slowly begin ratcheting it up further. *We projected over a year ago that you had better get used to \$4 per gallon gas and we still think that will happen over the next 24 – 30 months.*

### **SPECIFIC PRODUCT PRICING NEWS**

Throughout the year, the industry has some pretty spectacular swings in the price of scrap steel which is a major component in the manufacturing of so many building products. We see some of the fluctuations abating during 2008, but we also see pricing inching up throughout the year. *There is no doubt that most steel products will be more expensive at the end of the year than it is now.*

A couple of issues ago, we discussed the issue of duties and subsidies and the impact they could have on the pricing of imported fasteners. As predicted, pricing has increased and it appears, as the final hearing date approaches this month, that between price increases and an anticipated tariff, *the price increases of over 25% over the past couple of months will hold and become permanent.*

There is also some uncertainty in the market with several products, however, it doesn't seem extreme enough yet to warrant any major market concerns.

*Overall, it looks like 2008 will be a year of steady pricing with marginal increases throughout the year reflecting inflation and dollar devaluations.*

### **PRODUCT SPECIALIST**

With so many new products continually coming on line, we have made the strategic decision to bolster our product specialist role. Kyle Christopher has been named to that role and as such, he will be contacting our entire customer base to help you better understand new products, the benefits of them and how you and your customer can profit from them. Remember the small retailer. *Look for something not found on the shelves of the big boys.* Kyle can help you with collateral support, training and even working directly helping you with your contractors. Again, this is one more opportunity to differentiate yourself.

*There is tremendous opportunity out there for the savvy operator.* Have faith in the market, understand lineal thinking, execute your niche better than anyone else and most important, count on your business partners.