THE PARLIMENT PAGES

July, 2011

PROBLEM OR OPPORTUNITY –

Two shoe manufacturers sent sales reps to the interior of Africa to assess the market. The first sent a message back saying, “No one here wears shoes. It doesn’t look like there is a market. Coming home on next flight.” The second, sent a different message, “No one here wears shoes. I think the market is unlimited and will be staying indefinitely.”

PLEASE PAY THE DANG MORTGAGE –

Foreclosures continue to haunt the new home construction market. There are currently over 2.2 million vacant and foreclosed homes in the country. Let’s put that into perspective. Right now, single-family housing starts are hovering around the 400,000 per year. That means that the empty foreclosed inventory is over 5 times greater than all of the new homes that are expected to be built in the next 12 months. Pretty sobering thought. However, that is not the worst of it.

There are now over 4 million mortgages in default and over 90 days past due. Under normal circumstances, the mortgage holders would have taken action to seize these properties. However, with so much unsold inventory, the lenders are holding back, hesitant to put vast amounts of additional vacant properties on the market. Their hope is that prices will rebound and begin a flurry of buying activity. The big question is, can they hold out long enough? Or will they be forced to increase the inventory and therefore further erode the home value market?

I experienced this buildup of seized inventory in another industry about 20 years ago. What I learned from that experience is that the lenders will ultimately price their assets at whatever ridiculous low price is necessary to unload them from inventory. Until that happens, there just is not much of an upside market for new product.

ON THE OTHER HAND –

There is a new phenomena raising its ugly head that may help keep some life in the new housing construction market. Many homeowners are realizing that foreclosure is in the future for them. Either they can’t afford their payments, are facing mortgage resets, or are just so far upside down that it makes no sense for them to keep paying. Once this realization sets in, many of these people have stopped making their payments and they also have stopped maintaining their properties, living as squatters, rent-free. With the banks in no hurry to take the property, the condition of the homes is fast deteriorating.

While the property will ultimately sell for a lower price, there are buyers out there who will not settle for such worn down property and will pay the higher price for new construction. No one knows for certain the impact this will have on the overall housing starts, but it will definitely help some.

As an aside, there is a small, but fast growing market for the small remodelers and handy men who are contracted by the banks to bring the foreclosed properties up to a more saleable condition. A lot of work will be done over the next few years. If these contractors are not part of your customer base, we suggest you work hard at establishing relationships with them and the lending institutions that are contracting them. Many of these guys have been buying from the local big box. They need to buy from someone, why not you?

Remember, what is a problem to one person is an opportunity to someone else.

A CHANGE IN THE PARLIMENT PAGES –

Over the past couple of years, the content of our newsletter has subtlety changed. Instead of focusing specifically on our industry and the specific economics that drive housing, I have drifted off to a bigger

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picture and geo-political bits. I have decided to refocus this newsletter on our core message: what do we see happening in our industry and how can the building supply business improve their bottom line.

Not to be stilled, I plan on starting another newsletter, which will focus on the larger economic and political issues. In that newsletter, based on my research, I will give my conservative views on the overall economy, economic drivers and indicators, political trends and even some unsolicited social commentary. This new publication will be available only by email. If you are interested in joining the list of subscribers, it is necessary for you to send me an email addressed to: jbleech@no-excuses.com. Please put "subscription" in the subject column to avoid being spammed out. If I receive enough interest in this new publication, I will begin a bi-monthly issuance. The subscription list from the Parliment Pages will not be used for this publication. Remember, you must send an email with a request to be put on the new list.

THE WORLD OF TECHNOLOGY –

I have finally resigned myself to the fact that this Internet thing may be around for a while. There were many nights, as I labored in front of the computer screen, hoping that it would disappear and something more aligned to my talents would appear. Instead, in this world of simplification, things have continued to get more complex. Now please understand, these are the rantings of a 63- year-old. My 17-year-old daughter has a completely different take on it. She thinks things continue to get easier. Unfortunately, she is never there when I need her.

When we started Parliment about 9 years ago, most of our customer base was operating on what would today be seen as primitive technology. That technology seemed to do everything that we needed and was fairly simple to operate. Upgrades and changes were infrequent, inexpensive and truly optional. We basically ran our businesses from face-to-face contact and telephone. Cell phones increased efficiency and substantially increased the level of response. We had good inventory and financial analysis reports available and were able to utilize this information to better manage our business. In short, technology of 8 years ago helped us take our existing business and make it better.

As much as I hate to say this, and I will go kicking and screaming the whole way, *technology of today has the ability to significantly change the very manner in which we do business.* It is no longer just seeing how we can use the digital world to assist, but instead we now can use this new world to redefine some of our basic business models. Some will look at this as a problem while others will see it as an opportunity. However, let's remember that you cannot outrun change. It will eventually overtake you if you don't run fast enough. So instead of looking with fear at this impending change, we need to see it as an opportunity. After all, when there is no change, the mediocre can still win the race.

David Houle is a futurist who has spent years studying the growth and multiple uses of technology. He believes the introduction of the smart phone is probably the single biggest change to ever impact the human race and, in particular, the world of commerce.

I was recently returning from a business trip and was waiting patiently in the gate area of Delta Airlines. Bored, with nothing to do but wait for the already late plane to become even later, I decided to do some people watching. As this was a Friday night flight back home, the gate area was jammed with business people. As I gazed around the area, I counted over 90% of the people in that area using smart phones, I- Pads, or similar tablets. Very few were talking and most were texting or responding to emails. I was sitting next to one businessman who told me that he was ordering the materials he would need to meet next week's production schedules. Another contractor was carrying on a conference call with one of his subs and the manufacturer of the equipment the sub was installing.

As I pondered what I was seeing, I realized that, with Internet access almost everywhere at anytime, combined with email, anyone could contact anyone in the world almost instantaneously. The following week, I was on vacation on my boat in the Caribbean and upon arrival discovered that my air-conditioning was not working. The boat is European and so naturally the air unit was of German manufacture. The smart digital control unit, quickly told me that the problem was a defective sensor. Accessing the German website from the wireless connection on my boat, I was able to order a replacement sensor and have it Fed Exed to me for 2 day delivery from Germany.

Prior to this technology, I would have had to employ a technician from a local boat yard, wait for his schedule to allow him to come to the boat, have him research the issue, fax or maybe call in an order and wait for it to arrive. Instead of a 2 day process, this could easily have become a two week, hot and humid suffering waiting for the part.

Houle, the futurist, has a term for this. He calls it “disintermediation.” In short, this means that distribution channels are being bypassed, aided by technology. This concept has profound meaning to our industry, which is an industry full of distribution channels. Will contractors be able to order something direct from the manufacturer thereby eliminating the need to visit the lumberyard or building supply house? Will lumberyards and building supply houses be able to order directly from the factory and eliminate the need for the distributor? With today’s smart phones, a customer can access vendor inventories, place an order, choose a shipping method and even authorize a payment. This can be done on the job site, from a car, or from the kitchen table. This potential situation has caused us and a number of our customers to better evaluate their role in the future of their customer’s business.

It has been a curious surprise to me that more of this has not already taken place. In fact, despite the logic of this strategy, the exact opposite seems to be taking place. At the time when manufacturers should be increasing customer service, lowering shipping minimums and working closely with credit issues, they are, in fact, doing just the opposite. Because of this, dealers and distributors alike have a window of opportunity to further cement precious relationships all the while exploring how to best employ this new technology in their future.

To figure the strategy, it is important to understand the role of disintermediation. In theory, disintermediation should allow for immediate access to information, smaller purchases, and quicker delivery. To believe that the manufacturers will not eventually see the picture is to bury our heads in the sand. So, those of us in the distribution channel must play this game but play it better than ever before.

At Parliment, we realize this threat. As a result, we have continued with our policies of no minimum orders, no cut-off times for the next truck delivery and set delivery schedules regardless of order size. We continue to be the best in the industry for sourcing hard to find items. We will not hesitate to purchase from our competitors if it will help our customers make a tough deadline. We are driven more by relationships than policy when credit is determined. We ensure our phones are always answered promptly by a real person who can immediately take an order or answer a question.

The most important word in the Parliment vocabulary is “agility.” We are exploring how technology can help with that agility, but regardless, we know that the bottom line is that we must perform better than anyone else.

Our customers need to feel the same. You are not only faced with the obvious threats of a depressed market place, but you will begin to feel the impact of how technology could be used against you. We urge you to take a look at how the younger generations are conducting their business and make certain that you are making their purchasing style congruent with how you sell.

Oh, and by the way, the sensor that I received was the wrong one. One week later, and I still had no air conditioner. I now have a $150 part that I have to figure out how to return to Germany with the weak hopes of somehow being credited for the return. You see, the big boys haven’t quite got it figured out yet. But rest assured, it won’t be long before I can plug right into the a/c unit and have the diagnostics sent directly to the manufacturer to make sure I get the right part. We are faced with disintermediation. Please prepare for it.

HOUSING STARTS –

Watching for a change in the housing start projections is as boring as the old phrase “watching grass grow.” For over 18 months the projections have ranged from a low of 275,000 to a high of 950,000. In retrospect, the actual starts have been very consistent in the 400,000 range. Despite the political promises and misleading information, we believe that historic number of 400,000 will probably continue through the balance of 2011 and well into 2012.

PRODUCT AVAILABILTY –

A large portion of the building products used in this country are imported, primarily from the Far and Middle East. Over the past few months, we have noticed a substantial extension in the amount of time that it takes to get product into our warehouse. Because of the world economic slow-down, many shipping companies

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have mothballed big portions of their fleets in an effort to increase capacity loads and keep freight rates up. To compensate, we are increasing our inventory commitment to ensure we are not caught without product because of these delays. We are hearing of increasing shortages throughout the distribution channels. Make sure of inventory status and exact delivery date before you place your order.

PRODUCT PRICING –

Aside from a few minor ups and downs in certain products, we see very stable pricing for the next few months. If a recovery were to start to pick up some velocity, there will certainly be shortages, which will have an immediate upward pressure on pricing. We don't foresee that happening for much of the remainder of the year.

INTEREST RATES –

Short-term rates are almost certain to remain pretty much where they are presently. We do not see any substantial increase in these rates before the middle of 2012 at the earliest. Mortgage rates however, could be a different story. If the dollar continues its present strength, bond rates will remain low and mortgage rates will stay pretty much the same. However, if the dollar weakens and treasury auctions start to run into some resistance, one of two things will happen. Either the Fed Reserve will step in with more quantitative easing (printing of money) or the bonds will be sold on the open market. If they are sold on the open market with a weak dollar, bond rates are sure to rise, pulling long-term mortgage rates up as well. We will keep you posted on this, but for the next quarter or so, there is little need to worry about any sudden escalation.

GAS PRICES –

We have believed for a long time that the normal price for gas would be between $3.50 and $5.00 per gallon. We are presently on the low range of that estimate and the prices will probably hold to that low range barring significant economic recovery. However, if a recovery takes place, especially in China, gas will easily be at the high end of that range. Long-term gas in the $5 gallon range will start to have an impact on housing. More homeowners will realize the need for shorter commutes and will be looking for housing closer to the workplace. Beware of the "out-in-the-country" developments. With an extra burden of a couple hundred bucks in transportation cost, some of those attractive homes are going to become less affordable.

NEW PRODUCTS –

One of the biggest benefits we can bring to our customers is the advance notice of new and exciting products. Sometimes it will be new and innovative methods or products while at other times it could be a change in distribution allowing for easier purchasing. We have several products in each of these categories and would like to address one in this issue.

We have picked up the Prosoco (Sure Klean) line of stone, brick and block cleaners and preservatives. Prosoco is easily the most recognized name in this product line and will have instant brand recognition with your customers. Like so many of our new products, this product not only has residential construction uses but is also well known by the commercial contractors. Yet another opportunity for you to further penetrate other avenues of revenue production.

ONE LAST JAB AT OUR POLITICAL LEADERSHIP –

In 1960, the spending of the US Government amounted to about 3% of our economy. Today that number has reached 24% and is set to further increase exponentially based on the course that we presently have set. Every increase in this percentage is a decrease in the free markets of this country. Every dollar of spending that moves from the free markets to government results in waste, fraud and incredible inefficiency.

It is the concept of free markets and capitalism that have been the very foundation of the incredible growth and strength of this country. If we allow this trend of government spending to continue, we will, in short order, fail to continue as the leader of the free world and the economic powerhouse that has contributed so much to the prosperity of this country.