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Business Briefing

Woodworking Industry Demographics Continue To Shift

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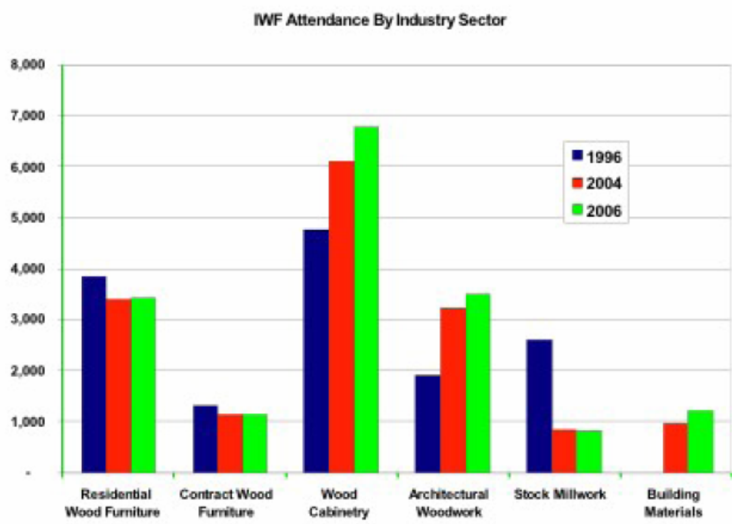
Attendance data from August's IWF 2006 allows the amendment of Business Briefing's February 2005 report on industry demographics. The adjacent chart shows attendance trends by major industry sector:

- Turnout from the residential wood furniture and contract wood furniture sector remained about level with 2004, after falling from 1996.
- Buoyed by a strong housing market, the audience from the cabinet sector jumped by 11 percent over 2004 and over 40 percent in 1996. This industry defends its market from foreign competitors by investing in technology that enhances speed to market and customization. Will the recent decline in housing starts cause this sector to pull in its horns?
- The architectural millwork sector, which produces to customer specifications, sent nearly 9 percent more attendees than in 2004 and over 80 percent more than 1996.



Importantly, small woodworking companies continue to be important customers of technology:

- Companies with less than 100 employees accounted for nearly 76 percent of attendees in 2006, up from 69 percent in 1996. Since 1996, attendance from companies with fewer than 10 employees grew by 19 percent.
- Companies with greater than 100 employees sent 19 percent fewer attendees.

Are Labor Unions On The Rise?

Today, only one out of eight U.S. workers is represented by organized labor. But every day the business news includes the story of labor unions' relentless attack on Wal-Mart, the world's largest retailer.

As the Wal-Mart situation confirms, manufacturers, whose ranks employ only 16 percent of the U.S. work force, are not their target. Instead, unions are going after the 42 percent of workers in the burgeoning service sector. Last July, the Service Employees International Union (SEIU) led a coup by leading 4.6 million workers out of the AFL-CIO, the largest U.S. labor organization. The SEIU is the fastest growing union in the U.S.

Most service employees work in jobs that are relatively protected from the threat of outsourcing. Unlike manufacturers, the service sector cannot easily replace U.S. workers with a lower cost Chinese. Union organizers understand the leverage that situation creates.

The globalization of business also enhances this leverage as the labor movement becomes more international in reach. More than ever businesses are dependent on foreign suppliers and complex supply chains to generate their product offerings. This dependence comes with a price - the risk of disruption from supply chain links beyond a company's control. A union like the SEIU with memberships around the world could outsource a strike against a U.S. company by paying Indian workers in its supply chain to walk out. This type of action is part of the SEIU's strategy.

To confront this threat, U.S. businesses must unite themselves. Labor-related problems like the cost of health care require the combined thinking and effort of every business operating in the U.S. Groups like NAM and the WMMA are good vehicles for this dialogue. Individually, every business must work to persuade workers and consumers alike that its objective is not short term profit at the expense of its work force.

The dynamics of your business and those of your customers' businesses are changing. With this change comes risk that you must work hard to mitigate. As a start, don't stick your head in the sand.

Economic Factoid
From 1980 to 2006, the U.S. trade deficit jumped from $19 billion, less than 1 percent of gross domestic product, to about $786 billion or about 6 percent of GDP. Employment in the U.S. during that period rose from 99 million to 145 million. Yes, every 3 months between 7 to 8 million jobs are lost, but the culprit is not just foreign trade. Domestic competition and improved productivity also contribute to these losses. Fortunately the job creating miracle that is the U. S. economy continues to make work available to those who want it.

Sector Report

Kitchen Cabinets
Cabinet sales rose only 0.8 percent in October versus the same month in 2005, according to the KCMA's Trend of Business Survey. For the year to date, sales were up 8.6 percent. Drilling into the numbers, October custom cabinet sales fell by 6.2 percent. Semi-custom cabinet sales rose by 1.8 percent; stock cabinet sales, by 1 percent.

After 120+ months of growth, the cabinet industry appears to be falling on a year-on-year basis. The drop in housing starts has hit this important wood products sector.

At the cabinetmakers...

- Masco reported 3Q2006 sales up one percent over the same period last year. Cabinet sales decreased as a double-digit decline in RTA cabinet sales offset a small gain in assembled cabinets. The company's performance continues to be adversely affected by the accelerating decline in housing activity.
- American Woodmark 2Q2007 sales fell two percent led by a decline in sales to homebuilders. In its core cabinet business the company continues to take market share at both Home Depot and Lowe's and expects to reach double-digit growth in the remodeling sector. Remodeling accounts for about 60 to 65 percent of the company's revenues. Gross margin improved to 20.3 percent

followed by an improvement in operating profit to 6.8 percent.

Home Furniture

Soft business persisted for domestic furniture producers as shipments in August fell 1 percent behind the same month last year. Companies interviewed at the October High Point Furniture Market indicated that the higher sales levels seen during the Labor Day selling period have not continued. In contrast, retail furniture sales data reported by the U.S. Department of Commerce have shown steady strength for the full year. Could retailers now be relying more heavily on direct imports, a channel that cuts out U. S. furniture makers?

News at the company level is correspondingly gloomy...

- Ethan Allen reported a 3.4 percent decline in its 1Q2007 sales, as continued retail weakness impacted performance. Gross margin, however, increased to 52 percent while operating profit fell from 12.9 percent to 11.6 percent.
- Stanley Furniture announced an 11.3 percent decline in its 3Q2006 sales. Gross margin followed suit by falling to 19.7 percent from 23.9 percent. Operating profit also fell from 11 percent to 6.5 percent.
- La-Z-Boy reported an increase of 1.4 percent in its 2Q2007 sales and turned a small 1.4 percent operating profit. For the quarter, upholstery sales which account for 70 percent of revenues, rose while casegoods fell. The company continues to reorganize its retail operations, a segment that analysts believe is key to long-term success. For the quarter, retail sales rose 6.7 percent, but this operation generated an $8.8 million loss.
- Furniture Brands reported a 2 percent increase in its 3Q2006 revenues while gross margin improved to 21.6 percent and operating margin fell to 2.3 percent. Inventory rose by $84 million as the longer supply chain from offshore manufacturers combined with an inaccurate forecast of retail sales. Earlier this month, management slashed its forecast for 4Q sales.
- Chromcraft Revington reported a 13.4 percent decline in its 3Q2007 sales and a $640,000 operating loss.

Some good news was reported among industry participants...

- Swedwood, the manufacturing arm of the world's largest furniture retailer Ikea, announced the construction of an 810,000 square foot factory in Danville, VA. The plant will employ 740 workers, open in early 2008, and support Ikea's 28 U.S. and 11 Canadian stores.
- Linwood Furniture continues to expand production at its Lexington, NC, plant. The company purchased Lexington Home Brands' Plant No. 2 in March 2006 to produce a collection of furniture designed by Bob Timberlake, a well-known local designer. Employment has expanded from 50 to 90 as production grows.

Meanwhile, more plant closures and restructurings were announced by other U.S. producers...

- Broyhill Furniture, a division of Furniture Brands, is closing its last remaining casegoods plant in the U.S. The facility, located in Lenoir, NC, employed 390 workers. Earlier this year the company shuttered another casegoods plant and its particleboard mill also located in Lenoir along with a frame plant in Marion, NC. The company now operates only two plants in North Carolina, both producing upholstery.
- Good Cos. has ceased production at its Carson, CA, plant as sales of its particleboard-based casegoods declined.
- Chromcraft Revington said its Warrenton, NC, wood processing plant will close in early December. The 166,000 square foot facility employed 58 workers. The company will source the parts manufactured at the Warrenton plant from overseas suppliers.
- SLF, recently created by the merger of Samuel Lawrence Furniture and Pulaski Furniture, is closing its Plant 12 in Pulaski, VA. The curio products made there will be shifted to its Plant 1 also located in Pulaski. The closure will affect 119 workers and will leave the company with a single domestic production facility.
- Davis Furniture is shifting production of its fully finished upholstery furniture line to China from its plant in Houlka, MS. That plant will be converted into a distribution center employing about 20 workers. The closure will affect about 130 production workers.

Office Furniture

BIFMA reported that October orders grew by seven percent and shipments by 7 percent. Trailing 12-

month shipments was $10.7 billion, the highest level since January 2002 and well above the $8.46 billion experienced in the late 2003 bottom. While orders and shipments over the last six months have shown an average growth rate of seven percent, this performance must be compared with the 11 percent average growth in the prior six months. Analysts believe these numbers show that the industry is reverting to its long-term growth rate of three to six percent

At the company level...

- HNI Corporation reported a 13 percent jump in 3Q2006 office furniture sales, a product segment that accounts for 78 percent of total sales. Operating margin in that segment was 8.7 percent. Profitability was negatively impacted by higher materials and transportation costs.
- Kimball International reported a 1.9 percent decline in furniture revenues in its 1Q2007 as it continued to exit the contract sector of that business. The furniture segment generated a 4.2 percent net margin, up from a small loss year-on-year.

Wood Flooring

October 2006 shipments of strip flooring declined to 34.805 million square feet, down 27 percent compared with the same month in 2005. Year to date, the industry has shipped 413.746 million square feet, a 4 percent decrease for the first ten months of 2006.

At the company level...

- KKR, a major private equity investor, has acquired a 50 percent interest in Tarkett, one of the largest U.S. flooring manufacturers.

Softwood Lumber

With new home construction accounting for 75 percent of demand for softwood lumber, the recent 30 percent decline in housing starts has translated into shorter hours and layoffs at many softwood mills. Production at Western mills was off 6 percent in the first nine months of this year and continues falling. Southern mills, which saw about one third of the U.S. softwood supply, are also curtailing production. Softwood demand in the U.S. is forecasted to fall from a record high 64 billion board feet to 57 million next year. As a result, the U.S. Forest Service is extending logging contracts by one year to minimize mill shutdowns.