Words of Wisdom
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Modern Woodworking's publisher, Chip Wisdom, noticed a woman seated next to him at the airport looking at furniture advertisements in the newspaper. He asked her if she was in the market for some new furniture. She replied that she was and named her favorite brands. Chip then asked her if it would make a difference to her that her favorite U.S. manufacturers actually were having their furniture made in China. She replied, "Absolutely. I wouldn't pay as much for it."

That mindset hasn't been such a good thing for the profitability of U.S. furniture retailers. Their gross margin is no more for an import than it is for a U.S.-made product. Art Raymond, president of wood industry consulting firm A.G. Raymond & Co. gives this scenario: "The mark-up on furniture is about 100%. On a U.S.-made bedroom suite that costs him $2,500, a retailer will set his “list price” at $4,999. If he replaces that group with one made in China that costs $1,800, its “list price” will be $3,599. The gross profit on the imported group is only $1,799 vs. $2,499, a decrease of $700. In the meantime that retailer’s rent, advertising costs, and other overhead costs remain the same. At the end of the day, that retailer’s net profit is lower. And furniture is price inelastic. A consumer won’t buy two bedroom suites just because the price is less.”

For the last four years deflation has been prevalent in the retail furniture industry primarily due to the lower prices of imports. "That retailer is unable to maintain his gross profit because of competition," says Raymond. "He isn’t operating in a vacuum, he’s not a monopoly. He would like to mark up that $1,800 imported group by the full $2,499 so that his net profit in absolute dollars remains the same. But his competitor down the street and that lady in the airport with Chip won’t let him.

But retailers continue to favor the imported furniture in High Point showrooms because they consider it a better value. As a result U.S. furniture manufacturers continue to take their designs to Chinese manufacturers or buy from Chinese manufacturers who have their own design talent. To cope with this change in their supply chains these manufacturers are closing U.S. plants and opening import warehouses.

But once the Chinese manufacturer has the skill to manufacture a well-designed, quality product, there's nothing to prevent selling directly to the retailer and cutting out the U.S. furniture manufacturer.

“Leading Chinese furniture producers have set up distribution here in the U.S. complete with sales forces and warehouses,” says Raymond. “American retailers are also buying directly from Chinese plants and cutting out the U.S. furniture manufacturer who previously sourced imported products for those same buyers. Economists call this elimination of the middleman ‘disintermediation’, a natural strategic action driven by the desire to streamline the value chain, reduce its costs. There’s a 25 and 40 percent mark-up on imports that is up for grabs.”

So the furniture value chain has changed and will continue to change. U.S. furniture makers have seen their roles move from design/produce/distribute to design/

source/distribute. This shift has brought the need for new business skills. “The battle for a part of furniture’s future is and will be fought in logistics”, says Raymond. “If you want a piece of that action, you better identify and execute a fast, low cost delivery chain. U.S. producers will only be able to leverage their existing retail relationships if they invest in properly located distribution centers, systems to forecast and control their supply chains, and the people who can make product flow.”

So if you have thrown in the towel on American furniture manufacturing, there’s a new game in town – distribution.