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BIA Executive Insights

Analysis, strategy, and insights for decision makers in the building products industry.

March 2020

When You Contemplate Your Business Today, Put on Bifocals

By Michael Collins, Managing Director, BIA

Developments in the coronavirus pandemic are happening so quickly that, for once, the cable channels' ubiquitous "breaking news" alerts are actually delivering news that merits attention. It took only about 48 hours last week for dozens of state and local governments to issue stay-at-home decrees. Nervous dealers nationwide are scrambling to keep their businesses going even as social distancing, closed showrooms, the



occasional government shutdown of construction, and the constant need to sanitize are draining revenue. It's March Madness, indeed.

Amid such turmoil, succession planning and exit strategies may seem to be out of reach. But, even as traumatic as life is today, it's important to remember that COVID-19 is only a temporary visitor. Ultimately it will go away, leaving you feeling as if you were in a bad dream. You'll be eager to get back to your long-term plans.

And this makes me think of Tom Hanks.

You might remember Hanks' Oscar-nominated performance in *Cast Away* as a FedEx efficiency expert marooned for four years on a remote, uninhabited South Pacific island. Most of the movie chronicles his struggle to survive on and eventually sail away from the island, but it doesn't end with him getting off the island. Rather, it continues with his return to Memphis, TN, and his discovery that what he had—and who he was—before the ordeal had changed irrevocably, even if his long-term goals remained the same.

Like Hanks, you likely are operating most of the time in survival mode now. Just keep in mind that, ultimately, you also need to think about how to get off the island and what life will be like then.

These aren't contradictory notions. Truth is, the way you're shaping your business now to get through hard times will impress potential investors. They balance the current economic setbacks with the knowledge that America didn't build enough homes last decade, and thus will have a housing shortage for years to come. To meet that decade-long demand, they are looking now for companies that they believe will be able to thrive once the market rebounds. You can win their attention by doing a good job now.

If you've ever worn bifocals, you're familiar with how they enable both close-up and distance vision in a single pair of glasses. It takes time to get used to the jarring differences in perspective that bifocals provide, but ultimately using them can make you more efficient and effective than any alternative. As you thread your way across today's crisis-strewn landscape, remember to look up from time to time, take in the longer view, and spot your destination. Then look down again and figure out how best to get from here to there.



7 Takeaways from 3 Top LBM Executives at the ProSales 100 Conference M&A Panel

Three of the country's most prominent buyers of LBM operations shared their thoughts with fellow dealers Feb. 28 in Dallas at ProSales 100 Conference. I moderated the session, which featured L.T. Gibson, president and CEO of US LBM; Jim Drexinger, CEO of American Construction Source; and Chris Costello, president of Timberline Enterprises. Here are my highlights:

EBITDA Multiples and Other Purchasing Factors

Gibson said there hasn't been much change lately in how many times EBITDA (earnings before interest, taxes, depreciation, and amortization) buyers are paying for LBM operations, but the value of the companies being purchased is higher simply because they are nearer peak earnings for this business cycle.

Costello, meanwhile, cautioned attendees to not get fixated on EBITDA. "It's not as big a factor (in a decision to buy) as people think," he said. Drexinger said he looks closely at the strength of a dealer's local relationship, the company's culture, and how well the management has been running the company while it has been up for sale.

Greenfield Startups

We've noticed an increase lately in the number of brand-new locations being opened by some dealers, particularly those specializing in roofing. Gibson said US LBM sometimes will do a greenfield opening because it has found

there are fewer potential acquisition targets in a desired area, so if it wants to be there it needs to start from scratch.

Drexinger, notably, hasn't taken part. He said that's in part because ACS tends to be in smaller markets.

Do You Do Turnarounds?

Gibson and Drexinger both said they will look at a potentially complicated deal or one involving a troubled company, but neither has Costello's track record in this regard. The Massachusetts dealer has dealt with companies that were in so much trouble that he joked "About two weeks before they drag (the owner) off to prison is the best time to buy them."

In one case, he said, he took over a single-location yard staffed by an 84-year-old father and his son. In one year, he said, it went from \$500,000 in revenue to \$10 million. "It's daunting, but if you have the right formula, and the right people, it can be done."

What Has Changed in the Past Five Years?

Gibson said one of his goals has been to expand US LBM operations' ability to sell specialty products like roofing and wallboard in addition to its traditional strength in lumber. It's one reason why its Universal Supply division has added several new locations in the past year, sometimes co-locating in places already occupied by other US LBM divisions.

Drexinger, meanwhile, said he's been looking at adding manufacturing capability, such as components plants.

Costello remains focused on the Boston area, but he's trying to identify places where he serves customers but could be more effective. He also said he's looking to serve a more urban audience.

Why Sell to a Bigger Company?

"We like to say we bring culture to an acquisition," Costello said. "The target (company being acquired) probably is family owned with a tight culture. We're equally tight-knit. That's an option vs. (being in a company with) the feel of Goliath ... It's one of the biggest edges we get."

Drexinger said ACS tries "to be the best of both worlds. We respect the local brand and want to keep local people. We promote from within. At the same time, we get the benefit of scale." For instance, in ACS' recent purchase of Homewood Holdings from Building Industry Partners, Homewood operations near Sacramento, CA, can take advantage of rail service.

Gibson said that whenever US LBM ponders an acquisition, it asks itself, “How do we make this company better?” While retaining a close-knit, entrepreneurial culture. That desire to improve long-term, even after the sale, has to be part of the company’s mindset, Gibson said, declaring: “We’re not interested in people who want a financial exit and wash their hands and walk away.”

Which Metrics Matter Most? And How Long Must the Previous Owner Stay?

Gibson said he looks closely at the quality of an acquisition target’s team, including how long they’ve been together and how much they want to move ahead. Drexinger sounded a similar note, saying ACS digs deep into the second and third layers of management to see what kind of talent is there. It’s important that the next level of leadership for the Nos. 2, 3, and 4 slots is apparent, he said. The executive selling the company is welcome to stay, particularly to help with potential future M&A, but it’s not vital.

Costello, the smallest of the three operators, has a much more specific target. He’s looking for a company with two to four acres of land, 10- to 20 employees, \$9 million to \$16 million in revenue, and four to six vehicles. All that, plus strong core values, make for the best candidate, he said.

As for how long the seller should remain, Costello remarked: “Sometimes you do get handed the keys. Sometimes there’s a padlock.” What matters is the strength of the culture, he said. In one recent case, he said, the team already in place at the acquired company was so good that he only needed to parachute in one person who know how Timberline likes to operate.

At US LBM, meanwhile, “We’ve walked away from deals where the transition was short,” Gibson said. “And we’ve done deals where the manager wasn’t really there.”

What Should a Dealer Do to Get Ready for a Sale?

Gibson’s No. 1 piece of advice is “eliminate addbacks,” those elements that complicate valuing a company and/or determining a sale price. [As I wrote for ProSales in 2018](#), addbacks can boost EBITDA when an item that’s part of current operating costs won’t continue under the new ownership. For example, the payroll may include a seller’s relative who doesn’t do any work. Addbacks can also be negative. If the selling company pays rent to an affiliated entity at below-market rates, the rent increase for the buyer constitutes a negative addback. Virtually all deals have addbacks of some sort, and some can create big changes in the EBITDA multiple.

Drexinger urged dealers to organize “voice of the buyer” and “voice of the customer” calls in which they can get honest, direct views regarding the value their operation provides to contractors and manufacturers. ACS does this with every purchase, and Drexinger said the results could be enlightening—as well as discomfiting—for sellers.



Lansing's Purchase of Harvey Building Products Continues 2020's Northeastern M&A Focus

Coronavirus news has pushed aside most of the headlines in LBM these days, but one story from March 16 bears noting: **Lansing Building Product's** acquisition of **Harvey Building Products**. The deal unites the 13th- and 15th-biggest companies on the current ProSales to create construction supply's newest billion-dollar company.

The combined business will operate 113 branches in 35 states and bolster Lansing's status as one of the nation's biggest specialty dealers. Aside from providing new distribution facilities to the Lansing network, Harvey also will continue to make its own branded doors and windows. Given that Harvey operated mainly in New York and New England, the deal particularly boosts Lansing's presence in the Northeast. The deal also continues New England's status as an M&A hotspot, as it follows a flurry of deals last month in Vermont.

Lansing's purchase also marks the arrival of **Markel Ventures**, a financial holding company that has acquired a majority interest in family-owned Lansing. President and CEO Hunter Lansing noted that Markel is a buy-and-hold company, not having sold a single business in its portfolio in over 15 years. "Today, we have the opportunity to create the next generation of success--where what it means to be a family business remains at our core," Hunter Lansing wrote in a [company announcement](#).

With the deal, we now have a total of 104 locations that have (or in the case of four locations, will) change hands, close, or open as a greenfield side so far this year. That's almost exactly the same pace as in the first quarter of 2019, and is way ahead of the 61 locations listed on the M&A chart in 2018.

In other action since mid-February:

- **Hartville Hardware** expanded to a third location with its acquisition of **Centerra Hardware & Lumber Center** of Middlefield, OH.
- **TAL Holdings** bought **Lake Chelan Building Supply** in Washington state. TAL plans to close its **Marson & Marson** yard in Chelan, WA, and merge it with the Lake Chelan Building Supply facility in the same city.
- **Galliher & Huguely** of Washington, DC, closed. Its yard in Washington closed permanently, while its Chevy Chase, MD, showroom was taken over by Baltimore-based **National Lumber**.
- **Drexel Building Supply** acquired **Blenker Cos.** and will merge Drexel's **Truss Systems** subsidiary to create a new venture called **Drexel Systems**. Blenker Construction will remain separate.
- **Nation's Best Holdings** bought **Bridgeport Building Centers**, which has yards under various names in Bridgeport, Springtown, Alvord, Jacksboro, and West Tawakoni, TX.
- **ABC Supply** bought **Exterior Building Supply** of Meridian, ID.
- **Mans Lumber** acquired **Legendary Millwork**, based in Troy, MI.
- **Anawalt Lumber** plans to open a new location in Pacific Palisades, CA, that previously was occupied by the now-closed **Norris Hardware**.
- **Bloedorn Lumber** closed its North Platte, NE, location.

Curbside Available

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**Morrison Terrebonne Hardware
St Charles....223-6370**



Painful as This Has Been, the Pandemic Could Be a Catalyst to Improve LBM Operations

By Craig Webb

President, Webb Analytics

Seemingly within days, the coronavirus drastically slowed parts of the U.S. economy, forcing dealers to abandon their usual springtime ramp-up of business and instead scramble and improvise in ways they haven't experienced for a dozen years. And just as the Great Recession altered how building material dealers operate, I believe it's already possible to see the coronavirus' long-term impact on how we do business. You could argue the news is encouraging.

Take **curbside pickup**. Basically, dealers across the country are embracing a variation of BOPIS—Buy Online, Pickup in Store—that The Home Depot and restaurants have been promoting for quite a while: The order arrives via phone, text, email or online; the order is processed while the customer comes to the store; and the handover takes place in just minutes. Technology speeds the process, and staff time is reduced. What's not to like?

Likewise, the buildup of **remote communication** setups that previously had been used mainly by the sales team will give rise to contemplation about whether everyone truly needs to do their work in the office. And once you get used to having teleworkers, it becomes less important that they live nearby. There's a big remodeling company in Virginia whose human resources officer lives in San Diego, while another remodeling company serves Southern California with a receptionist located in Florida. If you're short of workers in your area, telework expands your reach.

Technology is an obvious example of how this pandemic will produce change. I wouldn't be surprised if SRS Distribution wins customers during the crisis because it had created Roof Hub, an app that provides real-time information on order status, when the delivery truck will arrive, and invoice history. You also can order materials online and pay bills. Customers increasingly will be expecting these services from dealers, if only because Amazon and the big box stores are offering them. Dealers with old systems and no easy way to communicate via smartphone are less able to evolve with the changing business climate. Falling behind on technology is an existential threat, so I expect that tech vendors will be hearing lots of requests once the pandemic ends.

Cleaning the store likely will drop in importance once COVID-19 ceases to be a common phrase, but the truth is that a lot of construction supply companies are pretty grungy places. Keeping things spruced up could help dealers retain customers—particularly female customers—who had felt grossed out by what they saw in the past. Those same folks might have been pleasantly surprised when they visited a cleaner version of your place during the outbreak. Keep it up.

Finally, there's the concern you show for **your team's health**. Lots of dealers promote safety, but that often is motivated by the desire to reduce worker's comp costs. The future is likely to have you doing much more to promote workers' mental health and general physical well-being. We're seeing dealers reduce stress by telling people to not worry about their jobs or their PTO quotas when they feel ill; just go home and the job will be there when they get healthy again. Naturally, it's in your financial interest to suggest that, but it also shows you've made a commitment to the employee. In today's age of "at will" employment, what you're doing promotes worker loyalty.

Years from now, thinking back to these days, what will you remember? Hopefully, you'll mark this as the time your business didn't just survive—it became even better.

Is there something that you would like to see covered in a future issue of BIA Executive Insights? [Write to us](#) with your request.

Dealer/Distributor LTM Scorecard

All \$ in 000's All companies' fiscal years end 12/31 except for GMS, which ends 4/30, and Beacon, which ends 9/30

	BMC	BFS	Beacon	GMS	Foundation	BlueLinx	Huttig
Revenue	\$3,626,593	\$7,280,431	\$7,058,596	\$3,250,606	\$2,154,530	\$2,637,268	\$812,000
Rev Change YOY	-1.5%	-5.3%	0.6%	9.4%	5.4%	-7.9%	-3.3%
Gross Profit	\$951,304	\$1,976,829	-\$1,711,684	\$1,068,547	\$656,609	\$356,915	\$162,000
GM % margin	26.2%	27.2%	-24.2%	32.9%	30.5%	13.5%	20.0%
EBIT (Operating Income)	\$156,062	\$392,306	\$129,427	\$169,153	\$88,300	\$35,154	\$12,400
EBIT % Margin	4.3%	5.4%	1.8%	5.2%	4.1%	1.3%	1.5%
Net Income	\$109,845	\$221,809	-\$33,129	\$81,462	\$40,239	-\$17,656	-\$21,300
Net Income % margin	3.0%	3.0%	-0.5%	2.5%	1.9%	-0.7%	-2.6%
Adjusted EBITDA	\$259,433	\$516,100	\$448,621	\$304,663	\$176,838	\$80,430	\$5,300
EBITDA % margin	7.2%	7.1%	6.4%	9.4%	8.2%	3.0%	0.7%
Stock Price	\$28.69	\$25.41	\$31.98	\$27.08	\$19.35	\$32.33	\$1.54
Market Cap	\$1,959,527	\$2,948,881	\$2,200,224	\$1,145,755	\$831,876	\$302,803	\$40,721
Enterprise Value (EV)	\$2,145,640	\$4,226,058	\$4,665,487	\$2,176,800	\$1,253,243	\$751,775	\$175,321
Valuation Multiple (EV/Adj. EBITDA)	8.27	8.19	10.40	7.14	7.09	9.35	33.08
Total Debt/ Adjusted EBITDA	1.36	2.50	5.59	3.52	2.48	5.73	25.81

Before Coronavirus Struck, Here's How the Public LBM Operations Were Doing

Once upon a time--that is, in 2019--the biggest challenges to the financial statements of publicly traded LBM operations involved commodity prices, a relative lack of roof-damaging storms, corporate debt, and shifting the business model. Given what's happening now, these company's results ending Dec. 31 (Jan. 31 for GMS) serve mainly to give a sense of how the companies were doing before coronavirus struck. Anecdotal reports from the lumber side indicate that good weather across most of the U.S. boosted construction and remodeling activity far above 2019 levels, so odds are that 1Q financials will look good.

We Can Answer Your Most Pressing M&A Questions

- * How do the most active buyers in today's market value my company?
- * What parts of the business should I change to improve its valuation?
- * When is the right time to sell?

These are questions that are commonly asked by the owners of building

products manufacturers and distributors. Our work in selling and raising capital for companies puts us in a unique position to help answer these important questions. Regardless of when you might decide to approach the market, please contact me to have a confidential discussion about your company and ways to maximize its value for the owners.

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