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BIA Executive Insights

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

May 2021

Is This a Great Time to Sell? Perhaps. But First, Consider These 2 Factors ... and 1 Opportunity

By Michael Collins, Managing Director, BIA

It's human nature to regard whatever period you're in now as the best, worst, most amazing, or most unusual period in history. Such talk abounds these days, with claims this is the best time in recent memory to sell an LBM operation. I think current conditions certainly are the most favorable that I've seen in years, but I also would stress that the decision of when to sell shouldn't depend solely on whether the tide is high. Here are two other factors you need to think about, plus a potential alternative that you might not have considered.

The first factor is how good your company looks compared with what an acquirer wants. The superheated market we've experienced since last spring certainly will boost your performance numbers. But investors want to believe your company is going to do well in challenging times, so they also will examine your operations, your market, and your leadership team. If you fall short in those areas, interest will be limited, regardless of how hot conditions are.

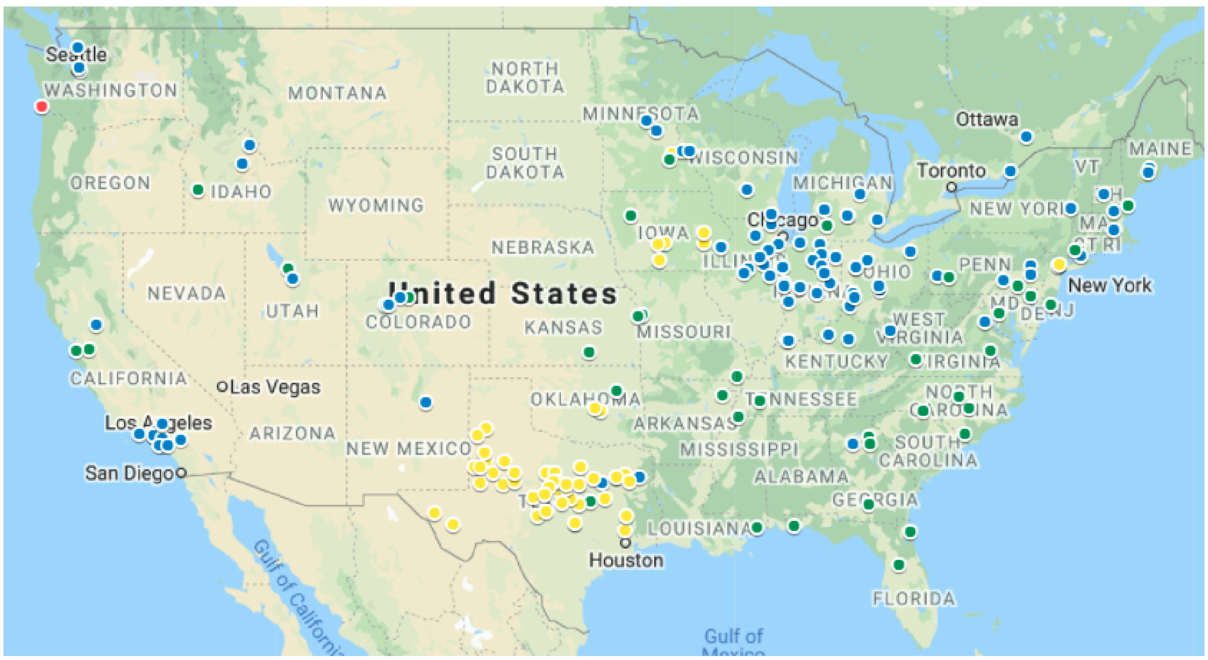
Remember, too, that potential investors are comparing you with other dealers that have caught their eye. If your net profits since last spring have remained modest, while a rival dealer's margin has increased, a potential buyer might regard that other dealer as being a better-performing vehicle over the long run.

A weak company can use a hot market to get a slightly higher valuation, it's true. But I believe a well-run, profitable company that's set up for the long term ultimately will prove more attractive, regardless of current market conditions.

The second factor lies entirely inside your mind: Are you ready to make a transition? A golden handshake at your post-sale goodbye party can be fun if you have something attractive to do once you exit. But if you've never imagined life beyond LBM, if you find guiding a team much more fulfilling than hitting a golf ball, then you need to think about your future while—or better yet, before—you entertain bids for your company's future.

If you still need to make those plans but want to take advantage of buying interest, I suggest you consider taking a half-step: Sell controlling interest in the company but keep a significant minority stake. Most investors want a dealer's leadership to remain in place after a deal, either in the president's chair or in a position where you can still wield influence. If you still have a little skin in the game, the investors will know that you're not going to be indifferent to the company's fate. It also might be possible to adjust your total valuation based on how the company performs during this transition period.

Reducing your stake without leaving could also give you a different perspective about your company, one that could help you improve its operations even as you start imagining life beyond LBM. With that new-found mental preparation, odds are you'll be much more likely to say—regardless of when you actually sold—that it happened at the best possible time.



US LBM, SRS Spring Forward to Lead Recent M&A, Openings Charge

The number of M&A deals, openings, and closures activity through the first days of May is running 50% ahead of last year's pace, thanks in big part to **US LBM**'s just-announced purchase of Texas-based **Higginbotham Bros.**

That deal combines with US LBM's acquisition of Iowa's **Gilcrest/Jewett** in January and the opening of yet another **Universal Supply** branch in New Jersey in April to increase

US LBM's total number of dealers by 50 this year alone. It now claims more than 320 locations nationwide.

US LBM also has topped **SRS Distribution** for the title of most active company in 2021, but it's not because SRS has gone dormant. SRS recently announced the greenfield opening of eight new roofing outlets and one new hardscaping store in April, bringing to 42 its total additions for the year.

Through May 3, there have been 179 deals, openings, or closures year-to-date. There were only 121 such actions by this point in 2020. Last year's market didn't start heating up until late in the year.

In other activity since late March:

* **L&W Supply**, a division of **ABC Supply**, opened a new branch in Palm Springs, CA, and bought **Starr's Building Supply** of Sacramento, CA.

* **American Construction Source** purchased **Foley (MN) Lumber** and **Milaca (MN) Building Source**.

* **TAL Holdings** acquired **Mount Vernon (WA) Building Center**.

* **Hancock Lumber** bought **Lapointe Lumber,** a two-unit operation based in central Maine.

* **Kodiak Building Partners** bought **Alpine Appliance**, which has stores in Avon and Basalt, CO.

* Utah's **Sunpro** bought **Columbia Millwork**, a specialty firm based in Vineyard, UT.

* **Costello's Ace Hardware** bought and renamed **Rankin's True Value** hardware in Warrenton, VA.

* Specialty dealer **Beach Building Products** started up in Jacksonville Beach, FL.

* **E.C. Barton's** newest Home Outlet center is in Tulsa, OK.

* **Westlake Ace Hardware** opened a new store in Livermore, CA.

* **Professional Builders Supply** opened a distribution center in Charlotte, NC, to serve that region.

* **Aker's True Value** hardware opened in Brushfork, WV.

* **Teton Lumber & Do it Best Center** in Choteau, MT, remains on sale for $1.3 million, including $700,000 in real estate but excluding $250,000 in inventory.

* An unidentified lumberyard in western Pennsylvania that claims annual gross revenue of $2.7 million is on sale for $1.9 million. The price includes $925,000 in real estate, $675,000 in inventory, and $300,000 in FF&E.

* A lumberyard in Yucaipa, CA, that claims gross revenue of $2 million and cash flow of $375,000 is for sale for $4.45 million. That may seem high, but the yard is in Riverside County, where there's huge demand for space to build warehouses to handle imports through Southern California from Asia.

* In Cherokee County, NC, a lumberyard that claims annual gross revenue of $5 million is for sale for $3.55 million. The price includes $950,000 in real estate, $450,000 worth of inventory, and $420,000 in equipment.

* There's a hardware and lumber store in rural Jefferson County, AL, for sale for $635,000. It claims gross revenue of $1.25 million.

Here's How Ward Lumber's New Co-Op Works

Most announcements from last week about **Ward Lumber** becoming a co-op omitted details about how the co-op works and why CEO Jay Ward did it. Here is some background.

Ward Lumber, a fourth-generation company based in the towns of Jay and Malone in New York’s North Country, has always been a Chapter C corporation. Jay Ward has been the sole owner of that operation since 2017. That’s the same year Jay and brother Jeff Ward spun off the company’s manufacturing division, Ward Pine Mill. The mill isn't involved in the co-op deal.

The co-op's organizing documents permit each of the company’s more than 40 workers to buy one share of the company for $1,000 apiece for full-time and salaried employees and a $500 half share for part-timers working up to 1,000 hours per year.

The worker-shareholders make up the entire community eligible to vote on major issues. Up to seven employees and two outsiders (neither of whom will have shares) will sit on a board of directors, and Jay Ward will remain as CEO and as the person who makes day-to-day decisions. Salaries will continue to vary based on the job and on the worker's performance.

As you would imagine, Ward Lumber is worth far more than the $40,000 represented by those shares. In fact, aside from a grant from New York State, most of the money paid to Jay Ward came from the Co-Op Fund of New England, and so the company's books now include a debt to the Fund that it will pay just as if it had gotten a bank loan. Notably, the co-op owners are not required to make personal guarantees for repaying the Co-Op Fund's money.

The shareholders' money is held in what is referred to as a "capital account." Profits will be distributed into this account and shared equally. At retirement, the employee owner presumably will have a capital account that has grown in wealth. The employee can request a payout from that account, and the board will decide on a payout schedule that typically will last several years.

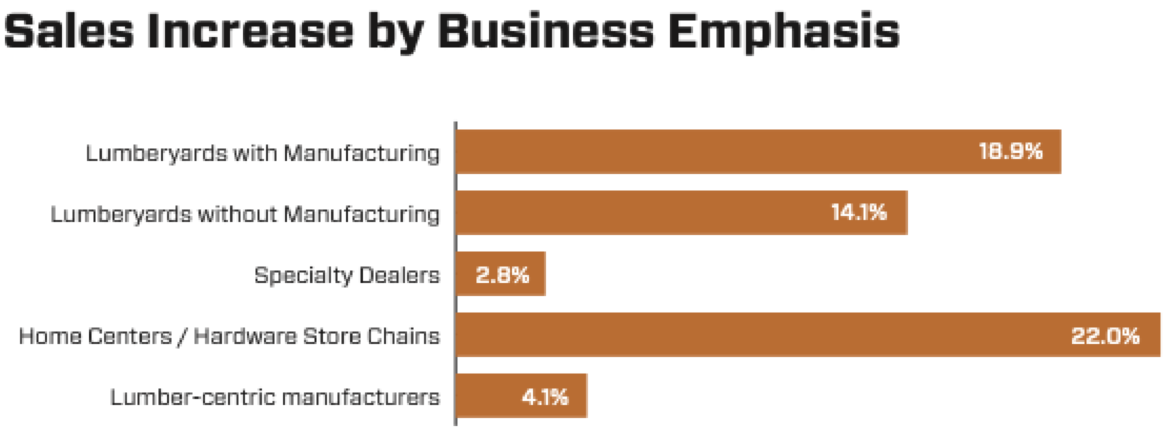
Jay Ward said he has been thinking about an employee ownership structure for 25 years, but was told it was too complicated and expensive. "I found information about co-ops through the North Country Association," he said. "Ultimately, I found the Cooperative Development Institute. CDI and the Co-Operative Fund of New England were really core to this. CDI's Rob Brown handles the business ownership solution part of this. They know the process. When I met Rob, this idea that sounded exciting, but I don't know how to do this became more tangible. The expertise exists and the lender exists."

Other LBM operations have decided to create Employee Stock Ownership Plans, but Jay Ward believes a Ward Lumber-style co-op is easier, simpler, and less expensive.

"An ESOP requires a valuation of the business every year," he said. "Valuations can be expensive, and this is typically not a high-margin industry. ESOPs also are highly regulated. Co-ops aren't gruesome. The big thing is that, with an ESOP, there's a trustee who makes the big decision. In an employee co-op, the owners make the decision—they vote directly. I really wanted to vest control in this business in the team that runs this business every day." And to help assure the business runs well, he plans to add even more financial training beyond what he has done for decades.

I've long said that our employees have owned Ward Lumber in their hearts for a long time," Jay Ward said. "Now there's ownership in the pocketbook."

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



New Report Could Reset Your Expectations of How Much Dealers' Sales Grew in 2020

You might have heard that my colleague, Craig Webb of Webb Analytics, has published a new report on 150 of the biggest construction supply companies. His **Construction Supply 150** report (available here for free) covers the businesses that accounted for 82% of America's retail building material and supplies sales last year. The average company's sales rose 18.6%, but the gains certainly weren't shared equally.

As the chart above (also taken from the CS150 report) shows, revenue gains varied dramatically based on the type of construction supply company. Home centers and hardware stores scored highest, with some companies recording sales gains topping 40%. In contrast, most of the companies with tepid or negative results are firms that specialize in serving the multifamily and commercial parts of construction—two sectors depressed by the pandemic.

These group results differ markedly from past years, when specialty dealers showed much stronger results and home centers and hardware stores didn't have a tailwind from DIY sales. Having these numbers available could help you decide whether the strong sales gains of a dealer you're eyeing put them at the front of the pack or merely in the middle.

How Long Will the Demand for Lumber Last? Possibly into 2023, this Expert Believes

The sky-high lumber prices we're seeing aren't a temporary phenomenon, Russ Taylor believes. This timber expert says the combination of COVID-exaggerated demand for new housing and a long-term shortage of lumber means the conditions we're seeing today could linger as long as into 2023.

Lumber producers were caught flat-footed when softwood consumption that had been relatively flat between 2016 and 2019 suddenly shot up around last July, the head of Russ Taylor Global said in a presentation last month during the Timber & Technology Conference. That surprise came following a period in which 40 sawmills in British Columbia alone were closed, mainly because an infestation of mountain pine beetles last decade laid waste to enough trees to fill New York State.

Plants with the capacity to produce roughly 3.2 billion board feet of lumber have been cranking up since 2018, and another 2.4 billion board feet of capacity is expected to come on through 2023, But the consumption rate is growing even faster.

Taylor predicts U.S. sawn softwood demand will rise by 4.5% in 2021, 4% in 2022 and “remain favorable” to 2023. Meanwhile, Canadian output will continue to be constrained, and imports from Europe won’t come in big enough volumes to ease the strain.

Prove You're Not as Rich as They Think. Invest in Financial Literacy for Your Team

By Craig Webb, President, Webb Analytics

When I first heard about Ward Lumber’s plan to create a co-op (see story above), I immediately saw trouble ahead. The reason for that concern came out of a conversation in which I was trying to persuade a dealer to provide his revenue numbers for my just-published Construction Supply 150.

“We don’t like to give out our numbers,” the dealer said, “because whenever we do that, our people see how big our revenues are and they decide all us owners must be millionaires."

You'd think Ward Lumber's employees might think the same now that they've become owners. But that's unlikely to happen because of something Jay Ward started 30+ years ago.

"Back in 1988-89, I had taken on some management responsibility," Jay Ward told me. "I took a P&L out and had a meeting with my managers and asked them the net profit. The answers weren't realistic. I then went through the financial statement and show really small numbers go to the bottom line. … If i hadn't, the perception would have been that we're taking home half of every dollar."

Ever since, Jay Ward has continued to practice open-book management a couple of times per year. "I'll write it all out and everybody's got a copy," he said. "Reality is usually a lot slimmer than what folks think. It was just part of my culture."

That work has paid dividends now in achieving Jay Ward's goal of creating a co-op. "When we were being assisted, we were told this was an easier transition because it wasn't totally out of the realm of knowledge," he said.

We've just finished Financial Literacy Month. Typically, it's a period in which various groups call for programs to educate young people. But those programs will come too late for your and everyone else's employees. Thus, if you want them to understand what a low-margin business construction supply is, you'll need to do it yourself. I recommend you do so. It could help give them a bit more motivation to turn a profit, maybe get a bonus, and help assure your construction supply business thrives.

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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