



State of the Residential Construction Industry

Perspectives Spanning the Value Chain

SUMMARY

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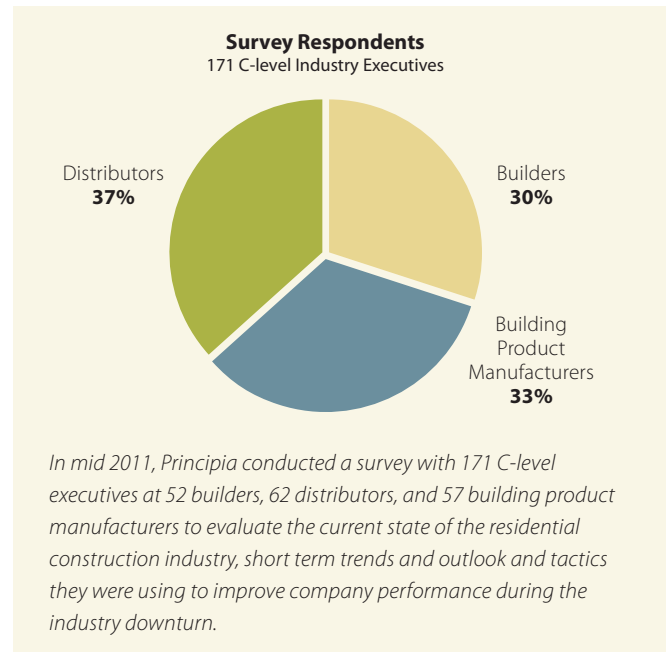
The residential construction industry remains in a state of flux. On one hand, survey respondents see 2011 shaping up to be no worse than 2010. Overall indications are that 1st half of 2011 was slightly below 1st half 2010 and the overall year looks to be flat.

However, all respondents (building product manufacturers, distributors and builders) expect next year to show a slight rebound of around 3% to 5%, which has been the perennial hope of the last few years.

Principia believes that industry executive's sentiment is mirroring consumer confidence, or lack thereof. There have been signs that the economy is stabilizing but lingering fears of a double-dip recession continue to undermine confidence in an imminent strong recovery. We do see pockets of expansion especially in the area of repair and remodeling activity and in the product categories typically associated within this sector.

Interestingly, for each time period surveyed builders were more positive in their outlook than distributors who in turn were more positive than building product manufacturers as shown on the subsequent figures. This is most likely a reflection of the margins achievable at each step of the value chain – with greater margins achievable closer to the property owner.

To a large extent, building products companies are looking to similar tactics that they have used in the past to weather the storm. The combination of the top three initiatives that industry participants are using indicate that they will hunker down with efforts focused on customer retention along with evaluations of which customer groups are profitable and which are less

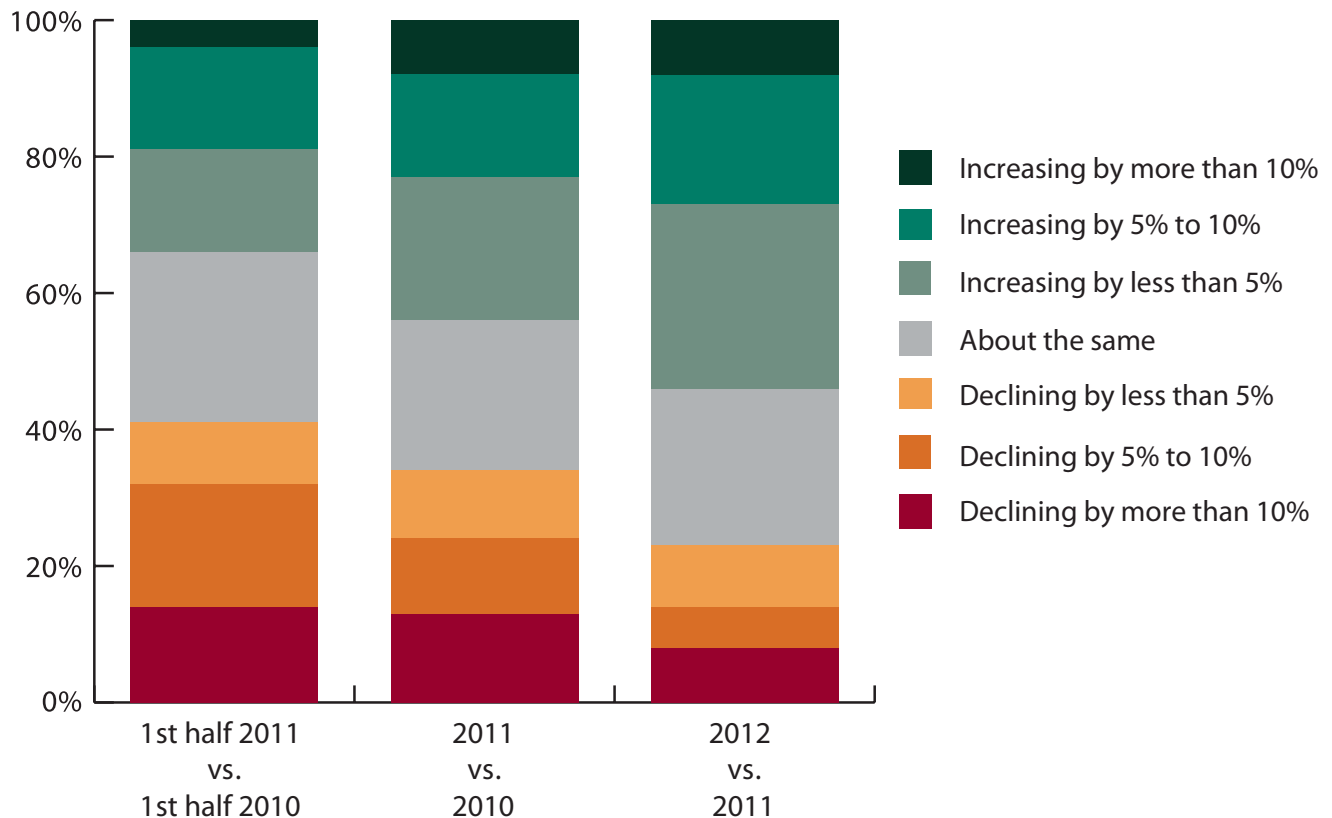


profitable. An active customer management program enables building products companies to cultivate the most beneficial relationships and fiscally manage lesser profitable accounts.

On the operation side of the ledger, we see cost efficiency and pricing and margin management as concurrent activities with customer relationship management. Many of our clients either systematically or manually scrutinize every opportunity for the value it may bring to the company. Finally, the fourth factor, increasing share, reflects the fact that in stagnant markets better performing companies are active, not passive.

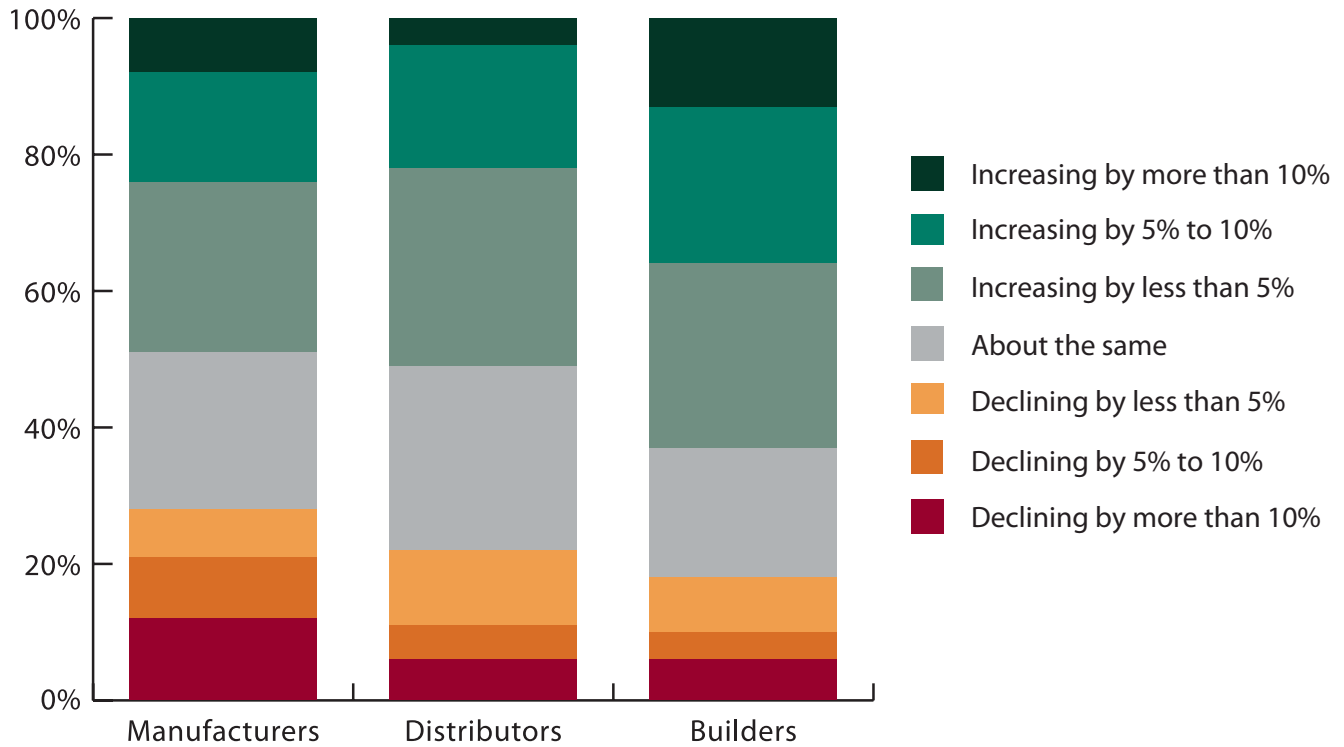
Identifying where and how to grow business in this environment is critical to success and separates leaders from the rest of the pack.

How do you see building products demand changing in the near term?



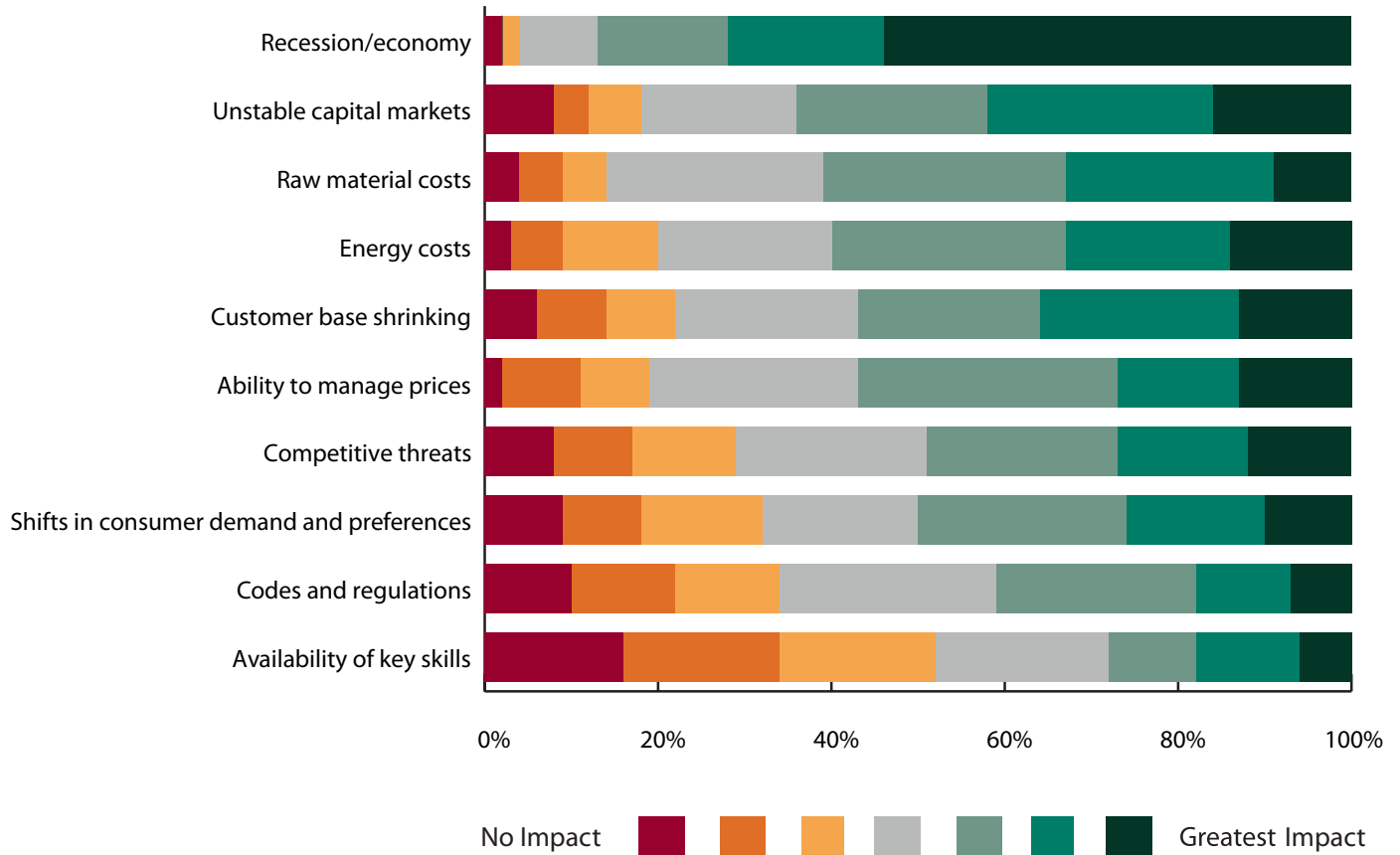
- Overall, building industry executives viewed the first half of the 2011 results being slightly below the first half 2010 with only slight improvement for 2011 as a whole. In both cases approximately 20% of executives saw 2011 business improving by more than 5% compared to 2010.
- As expected, 2012 is looked upon as a rebound year as more than 50% of respondents see the year as a growth year and only 20% expect to see a decline next year.
- The rebound is projected to more tempered that most economists might envision with overall growth in the 3% to 5% ranges.
- Interestingly, for each time period asked builders were more positive in their outlook than distributors who in turn were more positive than building product manufacturers as shown on the subsequent slides.

How do you see building products demand changing in 2012 compared to 2011?



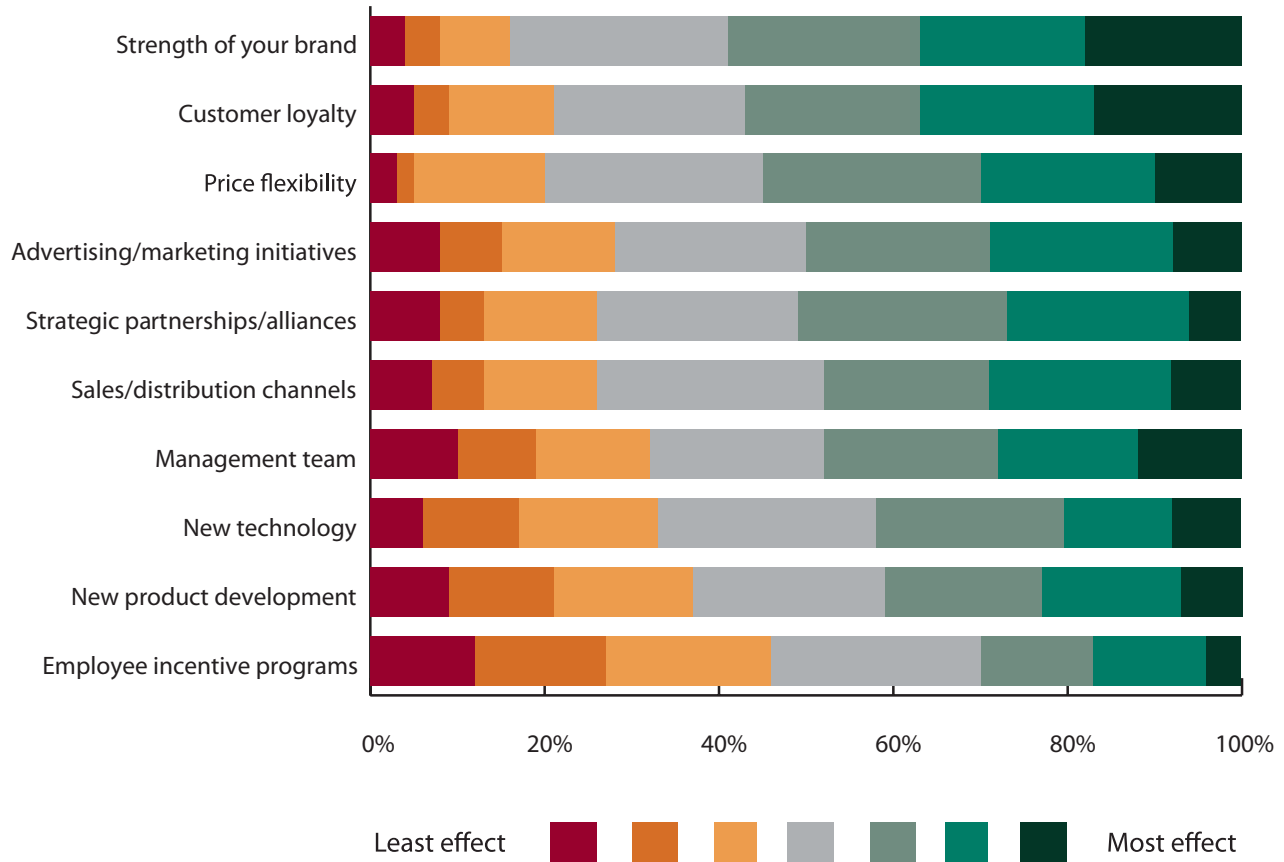
- All three respondents groups view 2012 as the rebound year with optimism increasing closer to the consumer, with builders expecting nearly 5% growth next year on average.
- Of significance is that across all respondent groups, at least 70% view 2012 as stable or growing, a dramatic shift from the prognostications for 2011.

What external factors will have the greatest overall impact on your business growth prospects?



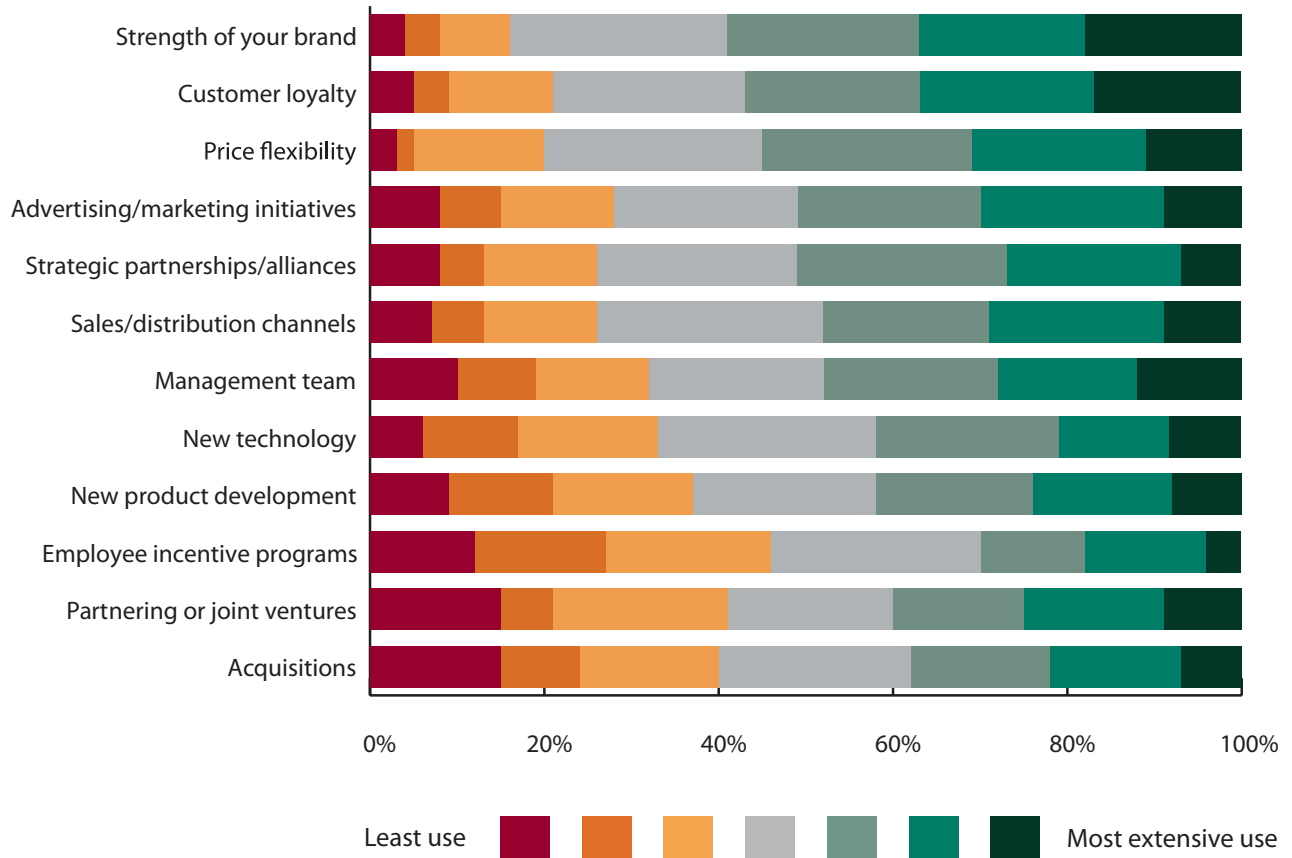
- Construction spending is down across the board in both the residential and commercial sectors. Many forecasts at the start of 2011 projected this as a rebound year with significant growth in housing starts but the most recent indications are that the year end total will be between 550,000 and 600,000 starts – essentially flat compared to 2010. This is reflected across the responses from our executive panel.
- The general lack of confidence in economic growth weighs heavily on the overall business outlook. However, the repair and remodeling segments in both residential and commercial construction, along with infrastructure do show signs of modest growth.
- Raw material and energy cost increases weigh heavily in a times where margins are tight, growth is stagnant, and customer bases are shrinking based on lower production levels and business insolvencies.

What internal factors will have the most effect on your revenue and margin growth over the next two years?



- Internal factors overall appear to be much lower in impact than external factors. All groups considered their legacy of customer equity (strength of brand and customer loyalty) as the key determinants of growth this year.
- Coupled with price flexibility, the willingness to cut a deal in this environment, presents a perspective of “hanging on.” Building products companies are using their relationships and price flexibility to retain existing customers at a time when there’s limited optimism for growth.

What initiatives will you use to drive revenue and margin growth over the next two years?



- To a large extent, building products companies are relying on familiar tactics to weather the storm. The top three initiatives show that companies remain focused on customer retention, and are evaluating which customer groups based on profitability. Some customers are more profitable, some less. An active customer management program enables building products companies to cultivate the most beneficial relationships and fiscally manage lesser profitable accounts.
- On the operations side of the business, we see cost efficiency and pricing and margin management as concurrent activities with customer relationship management. Many of Principia's clients either systematically or manually scrutinize every opportunity for the value it may bring to the company.
- Finally, the fourth factor, increasing share, reflects the fact that in stagnant markets, suppliers are not relying on a wait and grow mentality where waiting for the market rebound to grow sales is good enough. Identifying where and how to gain share in this environment is critical success and separates the eventual leaders from the rest of the pack.



About Principia

Principia, founded in 1995, is a marketing consulting firm focused on building materials and chemicals. We help our clients increase market share, grow revenues and improve margins.

Our industry focus translates into the knowledge and market access needed to have visibility up and down the value chain. Our end to end coverage, from raw materials through the final user, delivers the acute Voice of Customer insights required to best evaluate market realities.

Our actionable recommendations for better decision making have led to a long track record of client performance improvement based on the foresight delivered in every Principia engagement

Mailing Address:
101 Lindenwood Drive
Suite 225
Malvern, PA 19355

Phone/Fax:
610-363-7815 Main
484-252-2118 Fax

Email:
info@PrincipiaConsulting.com

PrincipiaConsulting.com