

hardwood floors

THE MAGAZINE OF THE NATIONAL WOOD FLOORING ASSOCIATION

OCT/NOV 2018

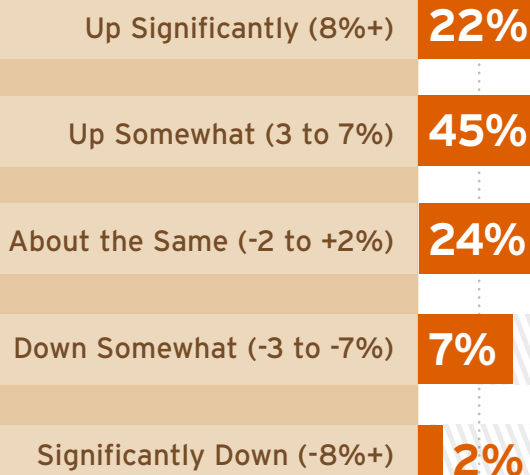
nwfa

EXTENDED

INDUSTRY OUTLOOK 2019



2019 EXPECTED SALES GROWTH (COMBINED PARTICIPANTS)



5% 10% 15% 20% 25% 30% 35% 40% 45%

Construction and remodeling markets are booming across the country, and NWFA members are optimistic that demand for wood flooring will remain strong going into 2019. More than two-thirds of respondents – including manufacturers, distributors, retailers, and contractors – expect sales growth of at least 3 percent in 2019, with 22 percent expecting sales will grow significantly (8 percent or more).

OUTLOOK 2019

By Lindsay Konzak

That's coming off a strong year in 2017 for NWEA members, most of whom said sales of their wood flooring products grew, according to NWEA's 2019 Industry Outlook survey. Halfway through 2018, most survey respondents were optimistic they'd end the year up.

National forecasts echo NWEA member sentiments, citing consumer confidence as one driver of demand.

The Leading Indicator of Remodeling Activity (LIRA), published by the Joint Center for Housing Studies of Harvard University, projects annual growth in homeowner remodeling expenditures may "taper somewhat" in the first half of 2019 but remain at a healthy 7 percent. The center expects annual spending on residential improvements and repairs by homeowners to reach nearly \$350 billion by the middle of 2019.

The National Association of Home Builders (NAHB) Remodeling Market Index (RMI) posted a reading of 58 in the second quarter 2018, up from the previous quarter; readings above 50 indicate more remodelers report positive market activity than not. NAHB also expects consumer demand for single-family housing to grow as the overall economy and labor market strengthen.

The American Institute of Architects' (AIA) Consensus Construction Forecast predicts 4.7 percent growth in nonresidential construction spending for the full year 2018 and 4 percent in 2019. If that pans out, it will result in nine years of consecutive growth, according to AIA, which also noted that total spending on nonresidential buildings will be 5 percent greater than the last market peak.

The positive outlook has been moderated somewhat by key concerns of NWEA members, including:

National forecasts echo NWEA member sentiments, citing consumer confidence as one driver of demand.

- The current market growth is unsustainable.
- Labor shortage is making it difficult to meet growing demand.
- Continuing price fluctuation from manufacturers, due to raw materials inflation, and concerns over potential tariffs. According to the U.S. Department of Labor, the prices of steel, aluminum, lumber, and plywood are all up by double digits.

These factors are driving uncertainty even as the wood flooring industry positions for ongoing growth. "Nobody knows what's going to happen when people are uneasy," said Kurt Vollstedt, with retailer New Dimension Hardwood. "They hold off on doing things that could cost them extra money. They might want to sit on their hands a little bit longer, wait to see how they're going to settle, and then move forward or choose not to move forward. The economy is hurt by that."

The upcoming midterm elections are also giving some members pause, as they wonder what the elections' impact will be on consumers' desire to move forward on major projects. "People pull back a little bit whenever they go through that," said David Williams of Horizon Forest Products, a distributor. "They want to wait and see what happens. My sense is that's going to be part of the reasoning that we might see a little softening going into next year." Building permit figures halfway through the summer indicated a potential softening in housing production, but that is from already-high

numbers compared with 2017, according to the NAHB.

The remodeling market is facing similar challenges: "Remodelers have to deal with rising material prices, especially lumber, and the continued shortage of labor to keep prices competitive. The labor shortage is also a factor contributing to the increasing backlog of remodeling jobs," according to NAHB's remodeling report.



Projected spending on residential improvements by mid-2019

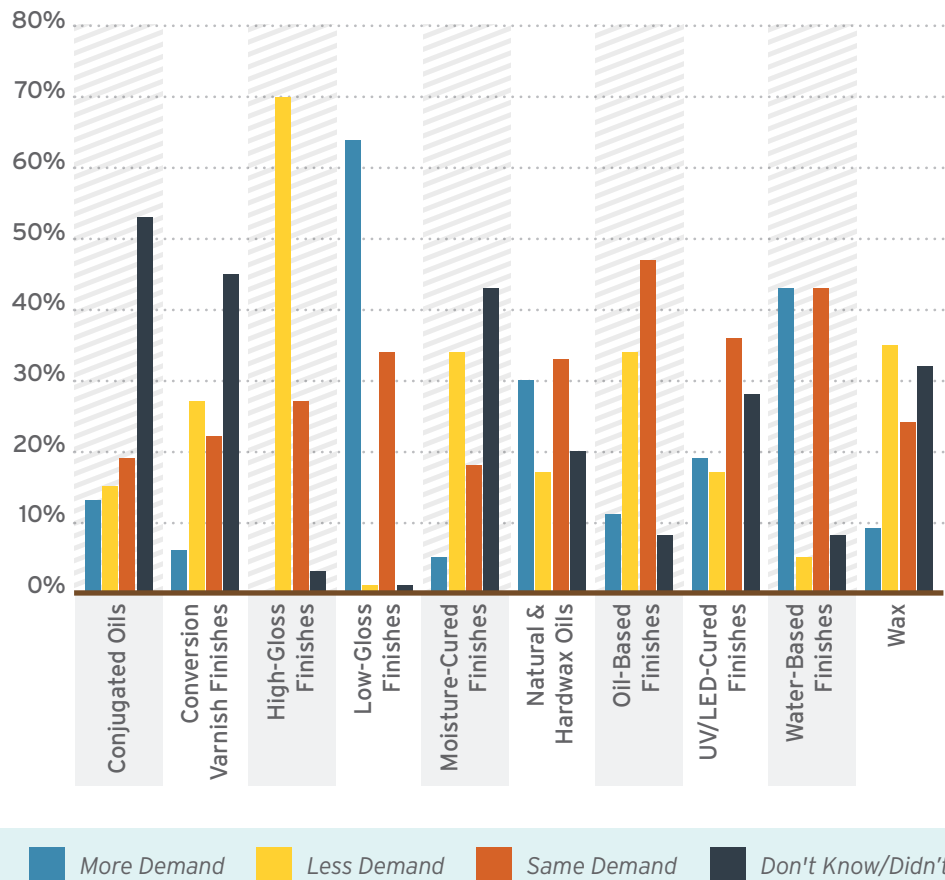
CONSTRUCTION MARKET INSIGHTS

NWFA members said white oak will continue to be the go-to species in 2019. Some respondents said this is in large part due to its wide availability, as countries like China have become better at sourcing it and manufacturing it relatively cheaply.

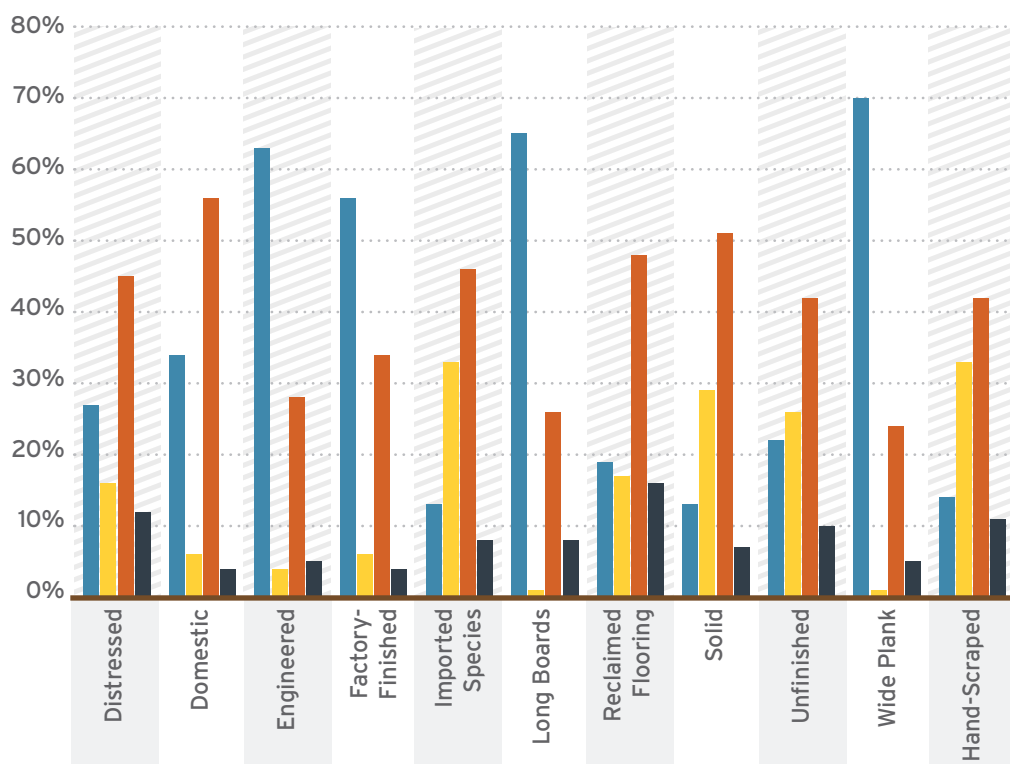
Members also kept wide-plank, long board, and low-gloss finishes in the strong-demand column for 2019. “This trend will probably last another two to five years,” said Leonard Hall of Endurance Floor Company, a contractor. “Right now, the wider planks are irresistible because you get more for a real fraction of the cost.” To meet some customers’ demand for lower-cost product, he said quality has fallen. “Because it’s so popular, everybody wants to have it but doesn’t always have the budget. Manufacturers are wedging themselves into a plank to get a margin share that doesn’t exist anymore.”

Factory-finished and engineered flooring are expected to continue to grow in demand in 2019, as well. On the color front, about 38 percent expect gray stains and finishes, as well as lighter colors, to be in higher demand in 2019; about

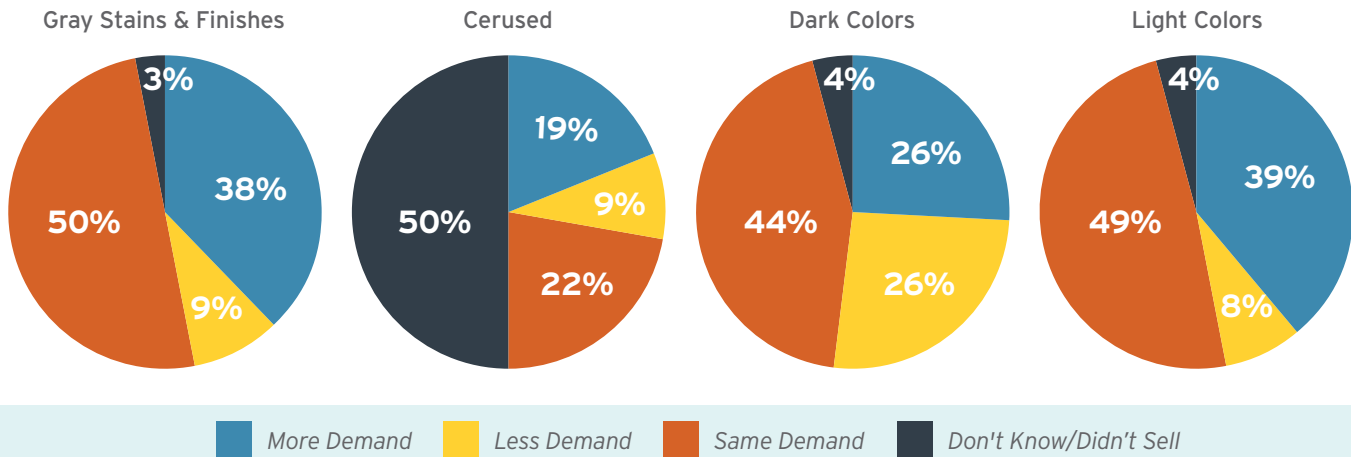
EXPECTED DEMAND BY FINISH IN 2019



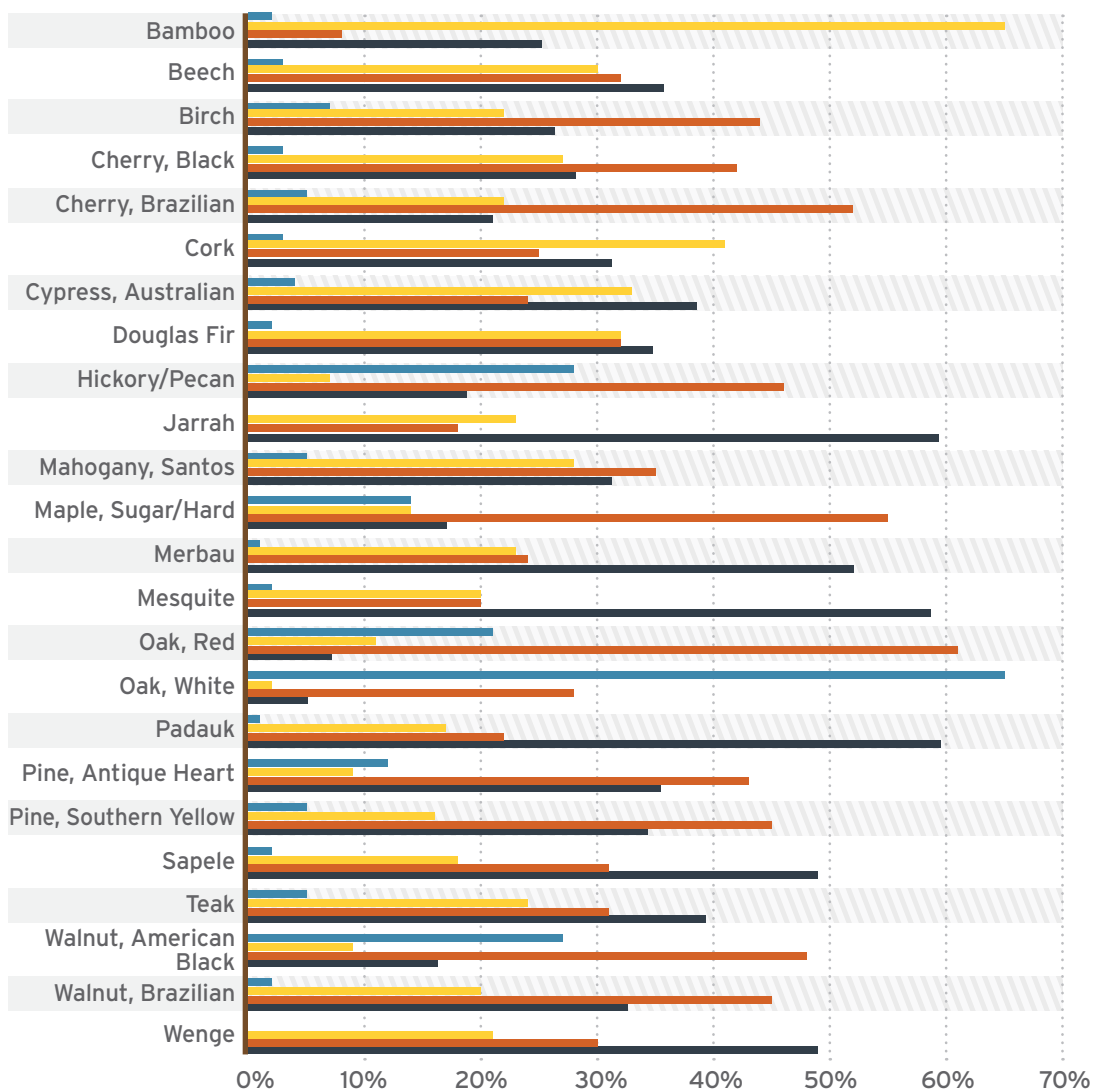
EXPECTED DEMAND BY TYPE IN 2019



EXPECTED DEMAND BY COLOR IN 2019



EXPECTED DEMAND BY SPECIES IN 2019



half expect demand for these shades to be the same as they are now. Low-gloss and scraped finishes are popular, some members said; in part, this is due to not showing the same wear and tear as a high-gloss finish. One respondent said that finishes that make the floor appear to be raw wood are increasing in popularity.

Demand for bamboo continues to decrease, with 65 percent of respondents expecting less demand in 2019. Cork and high-gloss or moisture-cured finishes also were expected to be lower in demand. "Exotics have fallen out of style due to pricing and poor availability in some markets," according to one respondent.

Despite the optimism in the industry, NWFA members noted several challenges moving into 2019:

Non-Wood/Wood-Look Competition

On top of these concerns, growing demand for resilient non-wood/wood-look floor coverings such as LVT, laminate, WPC and tile are taking market share from NWFA members. Contractors in the survey named LVT and laminate as the biggest threat to wood flooring. Half of survey-takers said that non-wood/wood-look floor coverings have had a negative impact on their real wood product sales. Another 17 percent were unsure.

“Everyone is trying to copy the wood look,” said Jim Gould, founder of the Floor Covering Institute, adding that the quality has improved, which has made LVT and other competing non-wood products a much bigger threat to NWFA members. He also said that there are no rules around marketing these products, and that some brands are misleading consumers.

Nearly half of retailers responding to the outlook survey said their wood flooring sales are growing more slowly than their non-wood flooring products. And about 64 percent of distributor respondents said the same. Consumers are attracted to waterproof options. And laminates hold an edge with builders, according to one NWFA member in the survey: “They are cheaper and less problematic in the building and move-in stage than solid hardwood.”

Some NWFA distributor and retailer members have diversified their product offering to include more non-wood/wood-look products in response to consumer demand for more water-

resistant options. One wrote on the survey: “We carry very few non-wood products. Just enough to offer to clients who request it. There is an interest in waterproof non-wood.” Another said: “It’s part of our overall plan to offer more products to the same customer base. It has allowed us not only to grow the new products that we’ve brought in, but it has allowed us to actually grow the product selection in sales that we’ve got. It’s a way of getting a bigger piece of the pie for us.”

Skilled Labor Shortage

NWFA members continued to report difficulty in finding skilled labor at every stage of the supply chain. However, contractors seem to be having the most trouble, with nearly 70 percent saying they are having problems finding the right people.

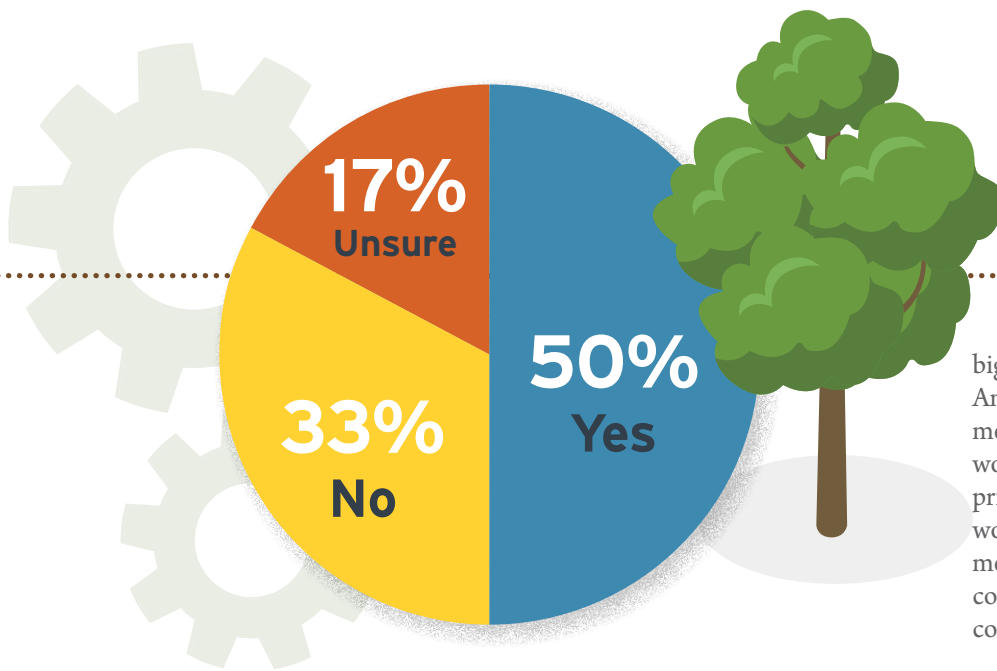
“Everybody’s struggling to find help at this point, but that’s what happens. Things gear up, and the labor is just not there, especially in our business,” Williams said. He said he’s having trouble finding talent for his distribution business, even for positions that don’t require strong technical expertise. “For us, it’s really looking out and trying to find people that are already working,” he said of their strategy.

One contractor wrote: “It’s one of our biggest struggles.” His strategy? “I have been training guys rather than looking for experienced guys. It just seems to work out better for me.”

Manufacturers continue to automate their operations, which is helping to ease the shortage. But some product lines, such as reclaimed wood, require work by hand. “There aren’t machines that can produce this or help us with that,” said Joe Pires of Northern Wood

Problems finding adequate skilled labor?





Has competition from wood-look products had a negative effect on real-wood product sales?

Plank, a Canadian manufacturer. “Up here, right now, it’s becoming more and more difficult to find.”

Another manufacturer said they are outsourcing some of their work: “We are outsourcing some of our production to another mill, that works just for us.”

Pricing Trends

More manufacturers said they expect to raise prices in 2019 than did in the 2018 NWFA Outlook. About 55 percent of manufacturers said they plan to increase pricing 3 percent or more in 2019 (compared with 37 percent that said the same in 2018). Another 45 percent plan to keep pricing about the same.

The jump is due in large part to the expectation that raw materials pricing will go up; 77 percent said they expect increases in raw materials costs. Members also noted that the cost of freight is putting pressure on margins.

That said, some increases in the market are due to government moves, including tariffs on lumber. “The majority of the lumber that we purchase, which is white oak, comes from the U.S.,” Pires said. “We manufacture it here and send it back to the U.S. There’s a lot of border crossing, and we’ve already noticed it doesn’t flow as easily as it used to.”

77%
of manufacturers
said they expect increases
in raw materials costs

Educating Consumers

Once again, NWFA members are struggling to sustain adequate margins as they compete against liquidators,

big-box stores, and cheaper imports. And, as noted last year, some members say competition from wood-look products is also driving pricing down in some categories of wood flooring. But, very few NWFA members surveyed mentioned online competition as a contributor to commodity-level prices.

The impact of the internet, for now, seems to be limited to the need to educate the consumer, who is doing more research online. “The internet has a lot of bad or misleading information,” said one NWFA member. “We try to correct this by using our expertise or directing them to the manufacturer’s site.”

Another wrote that sometimes the information is just not specific enough to that buyer’s needs. “Most of the information out there is not specific enough to the area in which we live.” And consumers tend to think they know more than they do, considering how infrequently they buy the products they are seeking from NWFA members, said another. “They are not immersed in all the variables that make for either superior or inferior items. The belief that the information they acquire on the internet is sufficient to understand a category only leads to misunderstandings.”

Many members said they are focused on education in the coming year, connecting more with the consumer to guide them through the buying process. “I don’t avoid it; I take it head on,” said Hall. “Certainly, the access to the Internet content, as

well as other sources for information, cannot guarantee the information's validity. Consumers usually cannot differentiate good from bad."

More than half of retailers in the survey said they had experienced challenges in educating consumers on the differences between floor covering products and materials.

Other Findings

Claims: Just 10 percent of manufacturers in the survey said that claims had increased in 2018; about 30 percent said they had decreased. The rest said they had stayed the same from the prior year. "Our moisture control systems have almost eliminated moisture complaints," said one. Another wrote: "Scaling and splintering is the most common and difficult to deal with from the production standpoint."

Commodity-level pricing: Companies are still experiencing margin pressure; to counter that, some are focused on higher-end markets or eliminating their focus on commodity-level products. "Too many in this business are in a race to the bottom in profit and quality," one manufacturer said. "You can always buy cheaper, but not always better!" Another wrote: "When the largest players in the segment (volume) are losing money, at least on the solid product line, then the pricing is artificially low... we look for alternate ways to use raw materials." Distributors attributed ongoing margin pressure to big-box stores, lower consumer budgets, low-cost imports and competitors that are offering product at lower cost to "steal business."

Top callback reasons: Contractors said the top callback issues included damage done by other service companies, such as movers or appliance installers. Seasonal gaps, unrealistic customer expectations, and finishes were the other reasons noted by contractors in the survey.

Wood flooring sources: The value of the distributor in the supply chain was highlighted, as all contractors said they bought from wood flooring distributors in 2017 and 38 percent said they bought from general floor covering distributors. "I like having my suppliers as business partners," a contractor said. "Most distributors will do jobsite delivery, and if we have an issue with a product, it's easier dealing with a distributor than a direct manufacturer." Their regional knowledge is also an asset. About 41 percent of contractors in the survey also said they installed wood flooring that was purchased by the client directly.

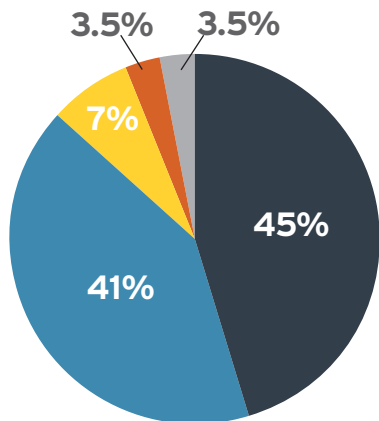


"I like having my suppliers as business partners," a contractor said. "Most distributors will do jobsite delivery, and if we have an issue with a product, it's easier dealing with a distributor than a direct manufacturer."

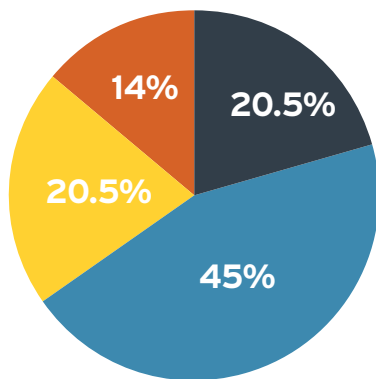


**CHALLENGES
& CONCERNS**

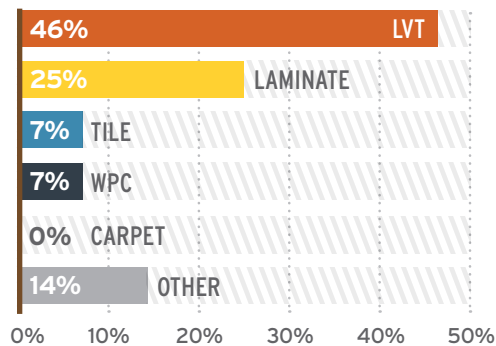
CONTRACTORS



2016 VS 2017 SALES CHANGE



2019 EXPECTED SALES GROWTH



BIGGEST LONG-TERM THREAT TO REAL WOOD PRODUCTS

Up Significantly (8%+)
 Up Somewhat (3 to 7%)
 About the Same (-2 to +2%)
 Down Somewhat (-3 to -7%)
 Significantly Down (-8%+)

Nearly 45 percent of NAWFA contractors – the greatest percentage of the four groups surveyed – saw significant sales growth (more than 8 percent) in 2017, and another 41 percent saw sales increase somewhat (3 to 7 percent). In 2019, two-thirds of contractors expect wood-flooring sales to continue to grow by at least 3 percent.

Labor shortages are once again expected to be the top challenge for contractors in 2019. Nearly 70 percent said they have had problems finding adequate skilled labor this year to keep up with the demand. “Proper training doesn’t exist in this area,” wrote one. Another said: “We are passing on several (jobs) per year.”

Long-term, 46 percent of contractors see LVT as the biggest threat to real wood products, slightly down from last year’s report. Another 25 percent said laminate was the biggest threat to real wood products. Some wood flooring-exclusive installers have come to embrace water-resistant options for use in select locations such as basements, bathrooms, or kitchens. “I suggest it sometimes to our customers rather than have them be unhappy with our wood floors,” said one.

Others said it has hurt their business. “We are losing some kitchen and bath projects to LVT.”

All of the contractors in the survey said they installed wood purchased from wood-flooring distributors in 2017. Just 3 percent said they installed flooring bought through online-only sources, though 41 percent said the client provided the wood.

The most common cut of flooring was plainsawn (90 percent), and the most common installation method in 2017 among those who answered the survey was nail down over wood subfloors. Water-based finishes were most common, used by 50 percent of respondents, followed by oil-modified finishes, used by about a third.

The most common callback issues were damage by another service company, like a moving company or an appliance installer, seasonal gaps, and unrealistic customer expectations. “Customers order No. 2 floors and expect us to make it look like select.” Another wrote that price competition is very real. But while it remains a challenge, many said that

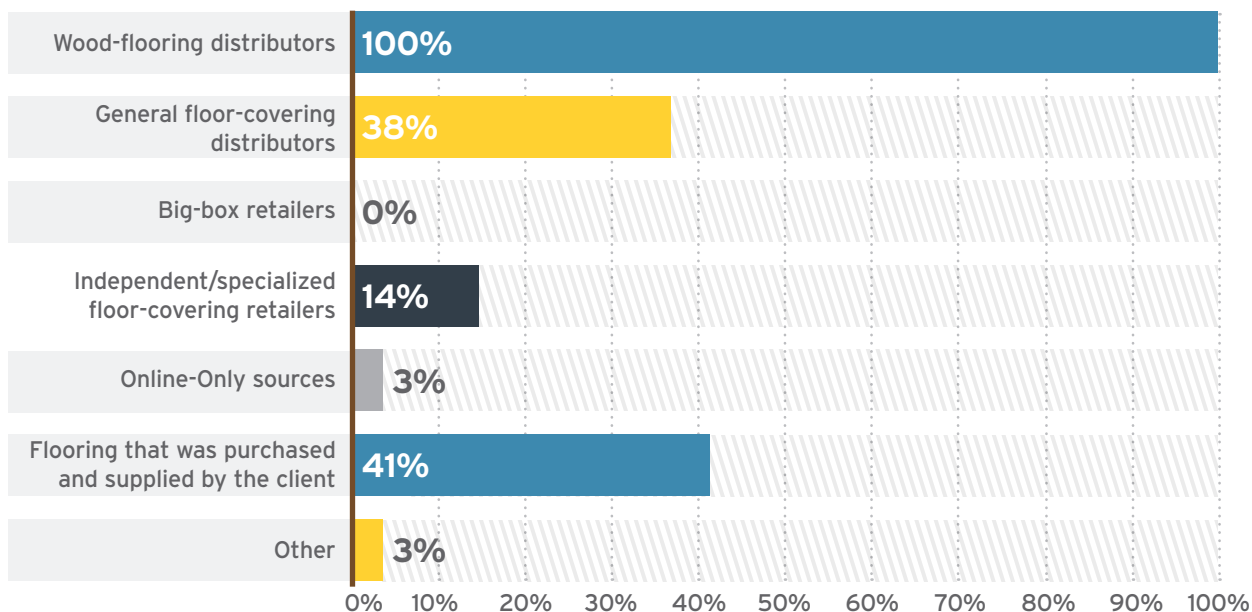
they would not resort to the lowest price. “We will never be the cheapest around,” a contractor said. Another reinforced their value to customers: “We are the go-to experts here.”

Contractors are optimistic for the next year, hoping to ride the booming construction and remodeling markets. Top opportunities going into the second half of 2018 and into 2019 include expanding in prefinished flooring and other flooring surfaces; establishing new lines of business, such as flooring maintenance programs; selling more high-end products; and raising prices. Others are looking to work with new customer types, such as architects and designers.

TOP CONCERNS IN 2019

1. Finding/Hiring Skilled Labor
2. Time Involved to Install
3. Pricing
4. Online Retailers

SOURCES OF WOOD FLOORING (2017)

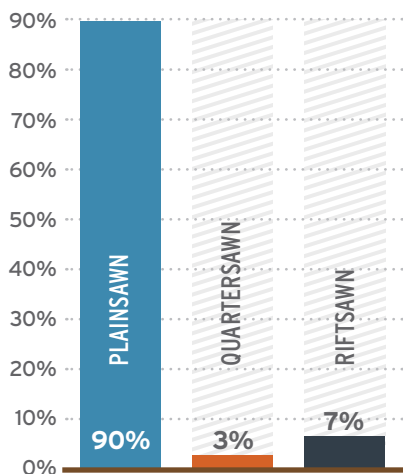


MOST COMMON INSTALLATION METHOD

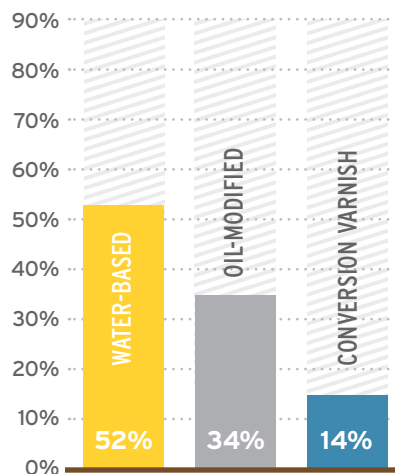
Nail down over wood subfloors	86%
Glue down over concrete substrate	7%
Floating	3%
Other	3%

MAIN CALL-BACK ISSUES

- Damage by other service company
- Seasonal gaps
- Unrealistic customer expectations
- Finishes

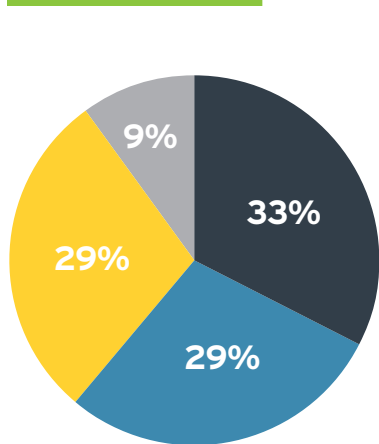


MOST COMMON CUT OF FLOORING (2017-2018)

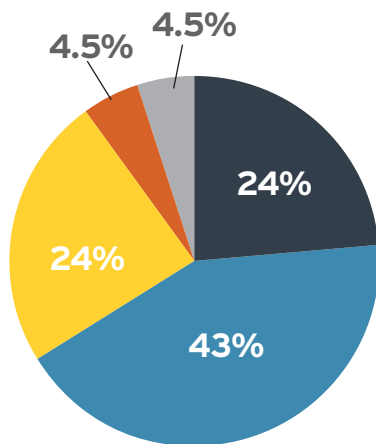


MOST FREQUENTLY USED FINISH (2018)

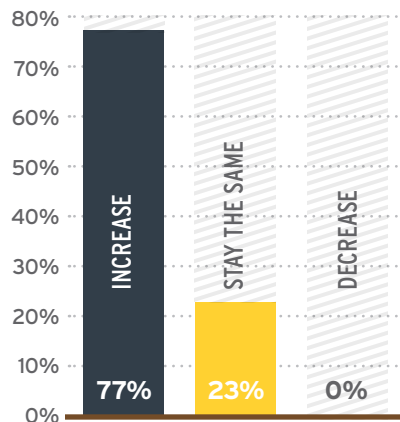
MANUFACTURERS



2016 VS 2017 SALES CHANGE

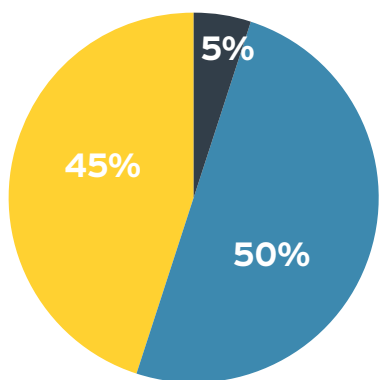


2019 EXPECTED SALES GROWTH



2019 RAW MATERIALS PRICING EXPECTATION

Up Significantly (8%+)
 Up Somewhat (3 to 7%)
 About the Same (-2 to +2%)
 Down Somewhat (-3 to -7%)
 Significantly Down (-8%+)



2019 PRICING EXPECTATIONS

About two-thirds of NWFA manufacturers saw wood flooring products sales grow in 2017. A third experienced growth of 8 percent or more, and another 29 percent said sales were up 3 to 7 percent. Manufacturers are optimistic about 2019, with about 43 percent expecting modest growth (3 to 7 percent) and a quarter forecasting significant growth (more than 8 percent). Few expect declines.

More than 80 percent of manufacturers saw raw material prices increase in the first half of 2018, significantly more than the 30 percent who said the same last year at this time. Increases were seen in red and white oak, walnut, hickory, cherry, maple, ash, packaging, and freight. No manufacturers said raw material prices fell, and just 18 percent said they remained the same.

Despite ongoing pressures from lower in the supply chain to keep pricing lower, more than half of manufacturers said they increased prices in the first half of 2018, more than last year, and nearly half have kept prices the same. No one lowered prices.

Inflation is expected to continue in 2019, with more than half expecting to increase prices in 2019. Some of those price increases are connected to tariffs enacted on various raw materials, or in response to the possibility of tariffs, which has introduced some uncertainty into manufacturers' forecasts for 2019.

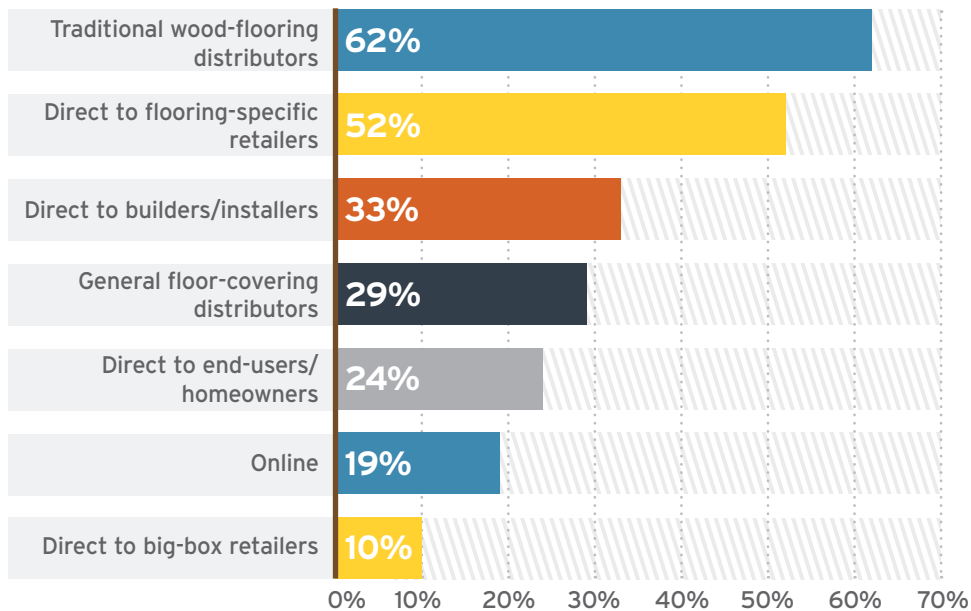
Government regulation and non-wood floor covering competition from laminate, LVT, and WPC topped manufacturers' main concerns for 2019, followed by the economy and the political climate.

Manufacturers are concentrated on introducing or focusing on product lines such as engineered, which is in high demand, to position for 2019. Others are doubling down on higher-end products. "We are a small manufacturer that makes a high-end product," said one. "If you want our quality, you will have to pay our price; we do not do cheap. Too many in this business are in a race to the bottom, for profit and quality."

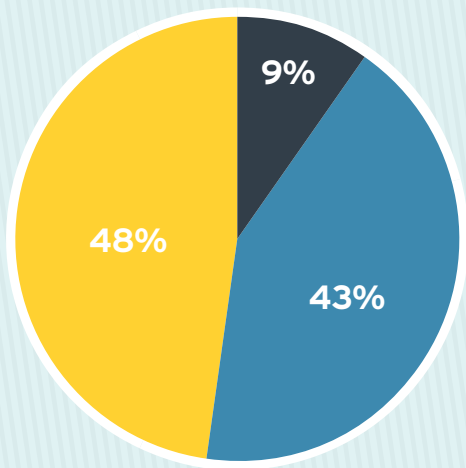
TOP CONCERNS IN 2019

1. Government Regulation
2. Non-Wood Floor Covering Competition
3. Commodity-level Pricing
4. Economy/Political Climate

MAIN SALES CHANNELS FOR MARKET

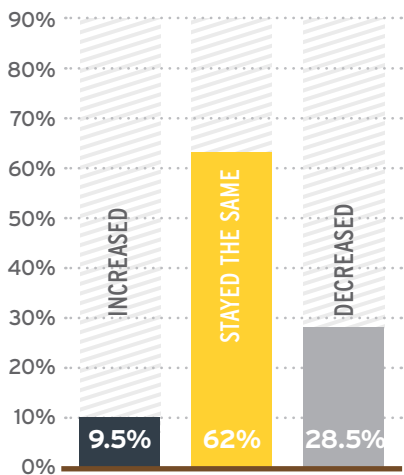


86%
don't expect to shift business among channels in 2019

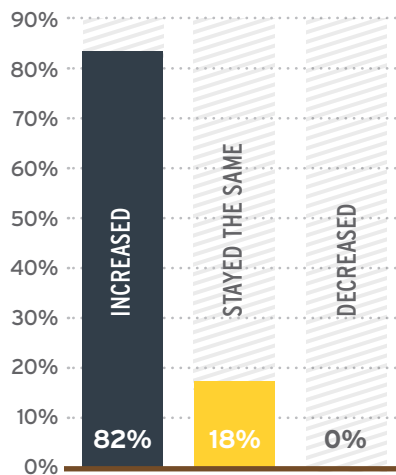


PRICING (2018 SO FAR)

- Up Significantly (8%+)
- Up Somewhat (3 to 7%)
- About the Same (-2 to +2%)
- Down Somewhat (-3 to -7%)
- Significantly Down (-8%+)

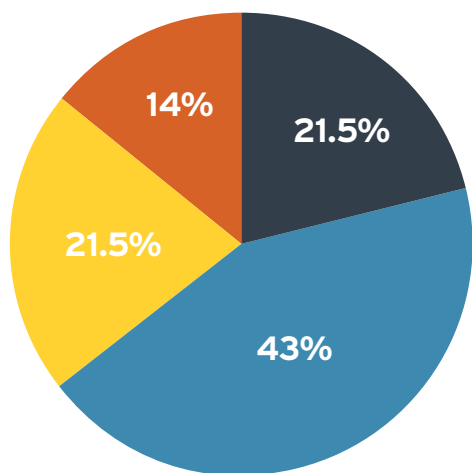


CLAIMS (2018 SO FAR)

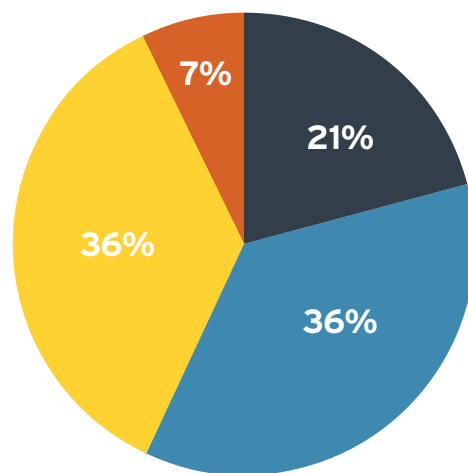


RAW MATERIALS PRICING (2018 SO FAR)

DISTRIBUTORS



2016 VS 2017 SALES CHANGE



2019 EXPECTED SALES GROWTH

Up Significantly (8%+)
 Up Somewhat (3 to 7%)
 About the Same (-2 to +2%)
 Down Somewhat (-3 to -7%)
 Significantly Down (-8%+)

Two-thirds of NWEA distributors saw sales increases in 2017, according to the 2019 Industry Outlook survey. About 57 percent expect sales growth in 2019 of at least 3 percent.

Nearly 70 percent of NWEA distributors do not offer services – including design, repair, and training. And 84 percent say that the percentage of sales from services will stay in the same in 2019. About 8 percent had sales of services that made up between 11 percent and 25 percent of revenues. Fifteen percent of distributors said services were less than 10 percent of sales.

Accessories, however, make up a much bigger percentage of distributors’ top lines, with a little less than a third saying accessories are between 11 percent and 25 percent of revenues. Distributors expect their 2019 accessories sales to be consistent with 2018.

Much like last year, uncertainty about the economy and manufacturers selling direct were top-of-mind for distributors looking to 2019. “Two of our existing (sampled) manufacturers have removed their products from distributors and are going direct this year,” a distributor said. Competition from wood-look and non-wood floor coverings was also a top concern. Nearly two-thirds of distributors said that wood-flooring sales are growing more slowly than non-wood/wood-look sales. “LVT is taking a lot of market share,” said one distributor.

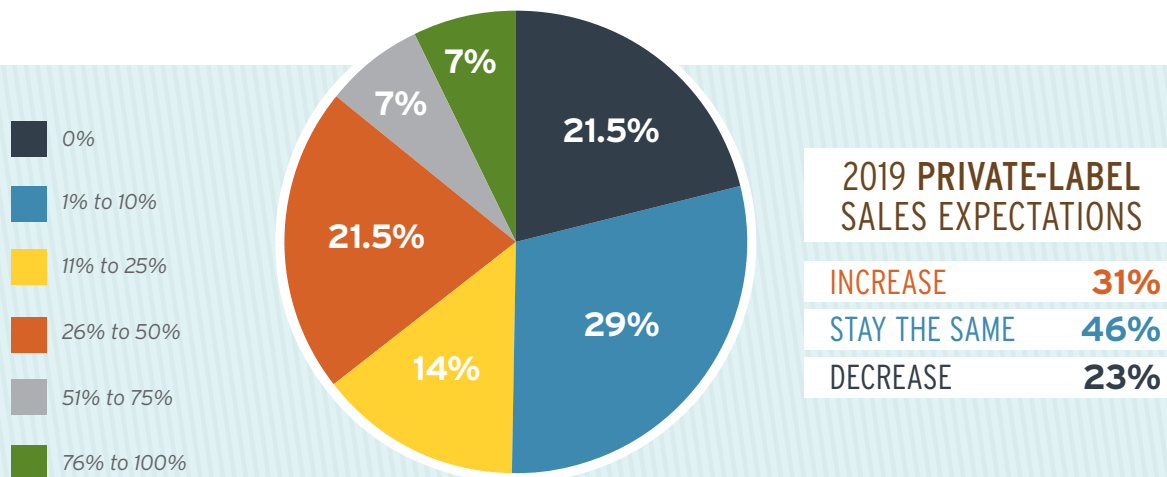
Pricing competition is a top challenge, as always. “Small ‘wholesalers’ are driving pricing down on all commodity flooring and accessories,” wrote one in the survey, “just to take share.” Another said they are facing “issues with other distributors selling products for at or below cost to steal business.” In response to pricing pressures, distributors currently offering private-label products plan to increase or

keep volume the same for those offerings in 2019. Other opportunities for 2019 include selling more high-end flooring, working more with designers that are less focused on price and selling more prefinished flooring.

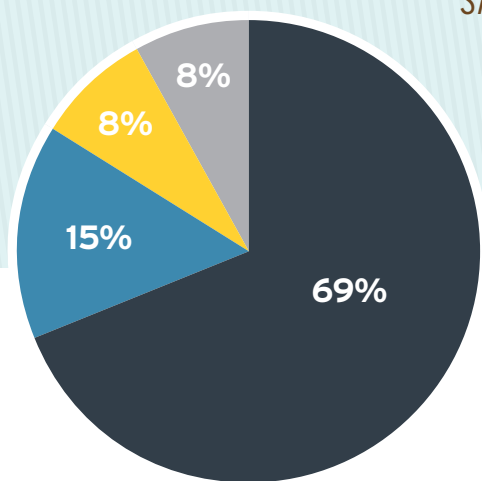
Most distributors are hosting training for customers, with nearly a third saying they are “extremely important” and that they host several schools a year. About half said they view them as “somewhat important.”

TOP CONCERNS IN 2019

1. Manufacturers Selling Direct
2. Economy
3. Commodity-Level Pricing
4. Competition from Big Box Stores
5. Competition from Non-Wood Floor Coverings

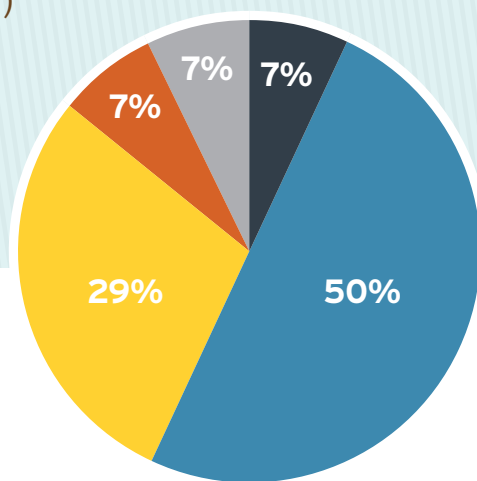


% PRIVATE-LABEL SALES (2017)



% SERVICE SALES (2017)

84% EXPECT SALES TO **STAY THE SAME** IN 2019



% ACCESSORIES SALES (2017)

79% EXPECT SALES TO **STAY THE SAME** IN 2019

IMPORTANCE OF CUSTOMER TRAINING

29% **Extremely important**
We host several schools every year.

50% **Somewhat important**
We have hosted schools in the past and would host in the future.

14% **Minimally important**
It takes away from our business focus.

7% **Not at all**

GROWTH OF FLOORING SALES WOOD VS. NON-WOOD

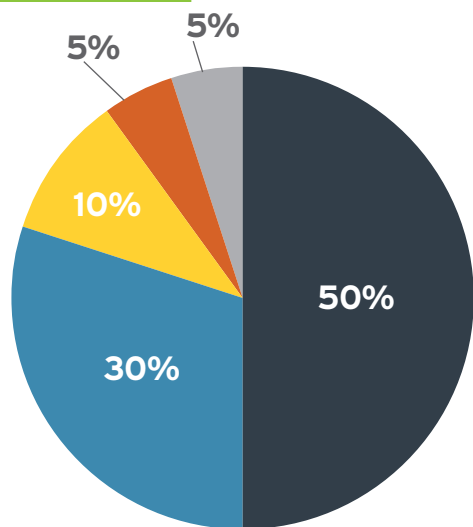
My wood flooring sales are growing more quickly than non-wood flooring products. **14.5%**

About the same growth rate as non-wood flooring products. **14.5%**

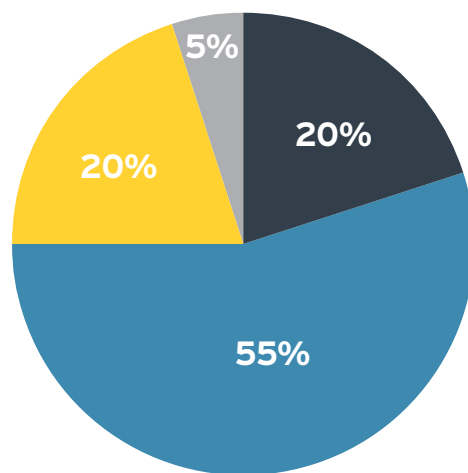
My wood flooring sales are growing more slowly than non-wood flooring products. **64%**

We only sell wood flooring. **7%**

RETAILERS



2016 VS 2017 SALES CHANGE



2019 EXPECTED SALES GROWTH

Up Significantly (8%+)
 Up Somewhat (3 to 7%)
 About the Same (-2 to +2%)
 Down Somewhat (-3 to -7%)
 Significantly Down (-8%+)

About 80 percent of NWEA retailers reported either modest or significant growth in 2017. A similar number expect growth of at least 3 percent in 2019, with a fifth looking forward to more than 8 percent growth.

Services – including installations, refinishing, design, repair, and training – accounted for up to half of 2017 sales for most retailers, and most survey respondents expect this percentage to stay the same in 2019. Retailers also expect accessories sales, which made up less than 10 percent of 2017 sales for most, to hold steady in 2019. Just as

with distributors, private-label sales are expected to grow in importance in 2019 for a little less than half of the retailers in the survey.

Nearly half of retailers in the survey said that wood flooring sales were growing more slowly than non-wood flooring products. Most retailers named manufacturers’ selling direct, the economy, and the political climate as their top three challenges going into 2019. Online sales and competition from big-box and liquidator stores were also top of mind. “Manufacturers and big-box stores drive commodity pricing,” one retailer said. Another said: “End-users and contractors... frequently confuse low selling prices with value and often buy inferior products in order to finalize the purchasing process and proclaim mission accomplished.”

More than half of retailers said they face challenges in educating consumers on

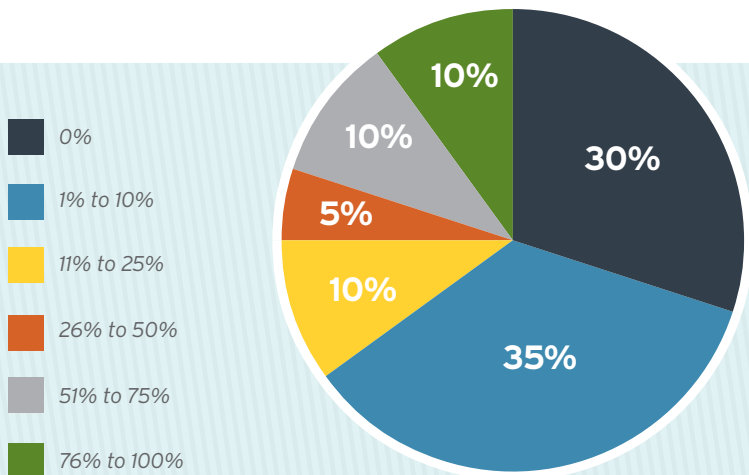
TOP CONCERNS IN 2019

1. Manufacturers Selling Direct
2. Economy
3. Political Climate
4. Online Sales
5. Competition from Big Box/ Liquidators

the differences among floor covering products and materials. “Customers buy our products infrequently and are not immersed in all the variables that make for either superior or inferior items,” wrote one retailer. In response, retailers said they are focused on better staff training, hiring more specialists, and positioning themselves with “proprietary products and stellar service,” while avoiding the price-driven parts of the market in 2019.

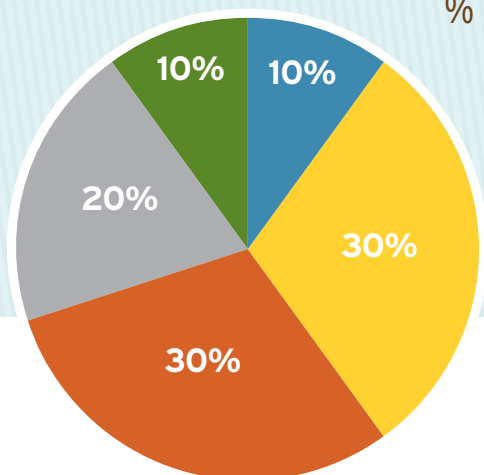
Is it challenging to educate consumers on the differences among floor covering products/materials?

YES 55% | NO 45%



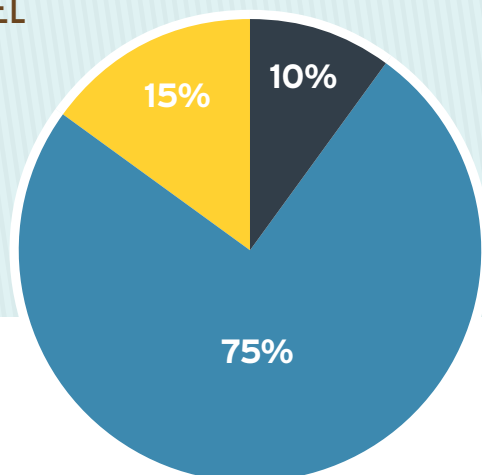
2019 PRIVATE-LABEL SALES EXPECTATIONS	
INCREASE	42%
STAY THE SAME	58%
DECREASE	0%

% PRIVATE-LABEL SALES (2017)



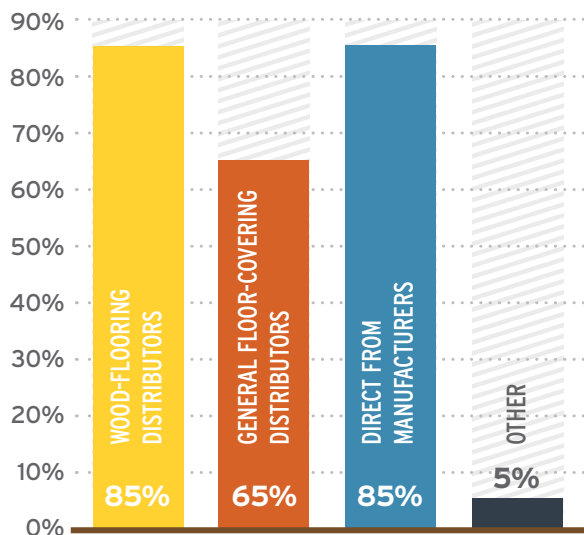
% SERVICE SALES (2017)

2019 EXPECTATION:
INCREASE **32%** | STAY THE SAME **68%** | DECREASE **0%**



% ACCESSORIES SALES (2017)

2019 EXPECTATION:
INCREASE **21%** | STAY THE SAME **79%** | DECREASE **0%**



SOURCES OF WOOD FLOORING (2017)

GROWTH OF FLOORING SALES WOOD VS. NON-WOOD

My wood-flooring sales are growing more quickly than non-wood flooring products. **11%**

About the same growth rate as non-wood flooring products. **21%**

My wood-flooring sales are growing more slowly than non-wood flooring products. **47%**

We only sell wood flooring. **21%**

LOOKING FORWARD

While optimistic for ongoing growth into 2019, the industry probably “won’t get back to the 2008 bubble,” said Gould.

Overall, most members who responded to the NWEA survey expect positive results, despite some uncertainty. But in response to challenges, they are adjusting product lines to ensure ongoing profitability in line with consumer demand. For some, that means more engineered or prefinished flooring, or adding some non-wood and wood-look product to their mix. And for others, it just means their previous strategy of going high-end has been reaffirmed.

Lindsay Konzak is a researcher with 3 Aspens Media, an industrial and construction markets-focused content production and marketing firm. 3 Aspens Media partnered with NWEA to survey its members and produce the 2019 Outlook report. Learn more about 3 Aspens Media at 3aspensmedia.com.