

Monitor

Building Materials



VOLUME
384

SLUGGISHNESS PREVAILS

STAGNANT ACTIVITY

High mortgage rates and lingering inflation have left the residential construction market limping into 2024

BEARISH PRICING

Cautiousness continues to characterize the softwood market, resulting in a downward price trajectory

LACKING URGENCY

Ample supply up and down the supply chain has limited most hardwood purchases to immediate needs

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Deals are a moving target with a constantly shifting mix of people, numbers and timing. We are here to simplify this process for you. Our associates are experts at analyzing situations and quantifying values you need on the most complex deals, so you can leverage our extensive industry knowledge to close the deal.

Trend Tracker - Inventory

	Lumber	Building Materials
NOLVs	Decreasing ▼	Mixed ⬆
Sales Trends	Decreasing ▼	Mixed ⬆
Gross Margin	Decreasing ▼	Mixed ⬆
Inventory	Consistent —	Mixed ⬆

	Market Prices	
	Three Months	Year
Softwood	Decreasing ▼	Decreasing ▼
Hardwood	Decreasing ▼	Decreasing ▼

NOLVS

- **Lumber:** A slowdown in the housing market and sluggish demand, combined with stronger indicators during the comparative period of 2022, have led to declines in lumber prices and NOLVs.
- **Building materials:** A slow housing market has negatively impacted sales for building materials and has led to cautious buying, negatively impacting NOLVs. However, some companies have benefitted from higher pricing locked in last year, positively impacting gross margins and NOLVs.

SALES TRENDS

- **Lumber:** High interest rates and lingering inflationary factors have led to cautious buying in the lumber market.
- **Building materials:** A slowdown in construction activity has negatively impacted demand, but some companies were able to keep inflation-based price increases intact from 2022 into 2023, positively impacting sales dollars.

GROSS MARGIN

- **Lumber:** High log prices, which typically lag behind lumber prices, combined with production inefficiencies to drive down margins at mills. Distributors continued to sell through previously purchased, higher-cost inventory that drove down margins.

- **Building materials:** Similar issues have plagued the building materials market, though favorable locked-in pricing and lower freight costs benefitted margins in some cases. The sales mix between end-use markets has also played a role in margin performance.

INVENTORY

- **Lumber:** Mills have curtailed production, while other companies have sought to align inventory levels with stagnant demand, resulting in a generally flat trend.
- **Building materials:** Companies continued to sell-through a buildup of inventory stemming from supply chain issues last year, resulting in a declining trend. However, demand for certain products, such as drywall, remains strong, leading to continued purchasing and elevated levels.

PRICING

- **Lumber:** A sluggish construction market has led to slower demand and more cautious purchasing, resulting in flat to lower pricing.
- **Building materials:** A lower level of building activity has driven prices for some products down, but demand for certain goods, such as drywall and roofing, remains strong, keeping pricing afloat.

Trend Tracker - M&E

	Woodworking Sawmills / Furniture
Used Pricing	Consistent —
Used Trade Movement	Consistent —
OEM Pricing	Consistent —
Technology Advancement	Consistent —
Auction Activity	Increasing ▲



- **Used Pricing:** A limited amount of good quality used equipment exists on the market, keeping prices steady despite declines in construction activity and, in turn, lumber prices.
- **Used Trade Movement:** Used trade movement remains healthy, which is consistent with trends from 2022. There has been limited availability of equipment on the market.
- **OEM Pricing:** OEM pricing continues to stabilize, especially in the U.S. and Europe. However, as noted in prior *Building Materials Monitors*, Asian machinery continues to put pressure on OEM pricing, especially with regard to European manufacturers. Imports from China and Taiwan appear to be increasing, but it is expected that businesses will look to reduce reliance on foreign suppliers in the future.
- **Technology Advancement:** Consistent with recent trends, many companies continue to spend investment dollars to automate with upgraded CNC controls and software, as well as more affordable 3D prototyping, to maximize efficiency returns.



Overview

According to the U.S. Census Bureau, the seasonally adjusted annual rate for privately owned housing starts reached 1.37 million units in October 2023, 1.9% above the revised September estimate of 1.35 million units but 4.2% below the October 2022 rate of 1.56 million.

October's rate reflected a slight increase over the previous month, but activity remains uninspiring as the nation continues to experience elevated mortgage rates. Although homebuilding faces challenges, an acute shortage of available houses on the market has managed to underpin at least some new construction. Per the U.S. Commerce Department, permits for future single-family homebuilding rose to their highest level in nearly one and a half years in October. Furthermore, residential investment recovered in the third quarter of 2023, bringing a streak of nine straight quarters of declines to a close.

Despite these glimmers of hope, lackluster demand and an underwhelming pace of new construction and remodeling projects resulted in year-over-year softwood price declines over the past few months. Remodeling activity has also stagnated, and reports suggest that activity could remain low in 2024. Prices have generally exhibited more stability in 2023 compared to the years during and immediately following the COVID-19 pandemic, during which price volatility was prevalent.

However, factors such as potentially more attractive mortgage rates and a shortage of available homes could present demand for lumber heading into 2024. Furthermore, the aged state of many homes in the U.S. may feed demand for remodeling and repair activity, which could bolster demand for lumber.

On July 27, 2023, the U.S. Department of Commerce announced the final results of its fourth administrative review of duties on imports of Canadian lumber; the fourth administrative review occurred in January 2023. The new duties from the review will take effect at an overall rate of 8.05% once they are published in the U.S. Federal Register. The most recent review affirmed the previous conclusions put forth by the U.S. Department of Commerce that countervailing and anti-dumping duties are necessary and their revocation would likely result in the recurrence of an imbalanced trade market. As has been the case throughout Canadian softwood tariff saga, the new rates have garnered discontentment north of the border, where producers seek the abolishment of all tariffs.

KEY FACTORS

Negative indicators from the first half of 2023 were realized more fully in the second half of the year, as construction activity slowed further.

Unimpressive demand and cautious buying have drawn lumber prices down to lows not witnessed since the height of the pandemic.

Softwood Lumber and Panels

Softwood lumber and panels are produced from gymnosperm trees, such as Pine and Spruce, and are typically used for structural building purposes, as well as millwork.

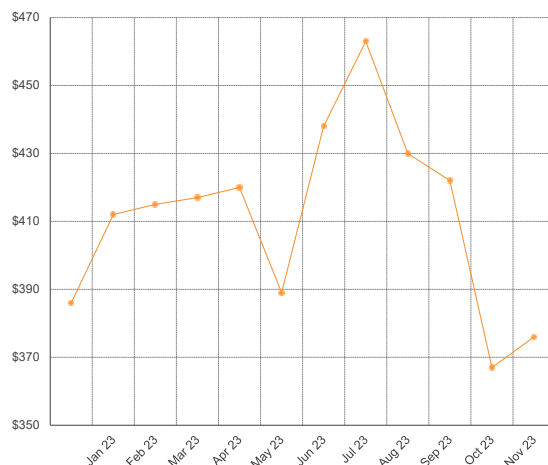
The second half of 2023 was characterized by trepidation continuing from the first half of 2023, as persistent high interest rates and inflationary factors have led to flat to mostly downward pricing. With lack of demand, and new construction and remodeling projects moving at a modest pace, composite prices dropped approximately 15% to 25% in October and November 2023 compared to the same time period in 2022.

With prices mirroring the lows witnessed at the onset of the pandemic, pessimism has emerged at the distributor level, resulting in cutbacks on purchases and a supply that continues to outpace demand at the mill level. While mills have curtailed production in an effort to mitigate downward pricing, concerns over potential labor shortages in the event of shutdowns have prompted mills to keep running in some cases, leading to a continuous oversupply environment. While it is not unusual for prices to trend downward in the second half of the year due to the approaching winter season, prices tend to pick up towards the end of the year or at the turn of the year as distributors look to hedge in preparation for the spring. However, as inflation

and high interest rates show few signs of letting up, prices could continue to stay relatively flat, with most buyers entertaining the possibility of skipping their annual round of winter buying. Conversely, as distributor inventories have been thinning for months now and prices have reached their lowest levels in years, modest gains are still possible.

Appraisal trends for lumber have generally been negative in the second half of 2023, as most appraisals are comparing to periods when prices were still relatively favorable. Mills have been negatively impacted by falling prices and demand, along with less volume and disruption from capital projects and labor shortages that have hurt efficiency and resulted in less absorption of overhead costs, negatively affecting gross margin and NOLVs. In addition, mills are flush with inventory as customers have stocked up significantly in months prior due to supply chain uncertainties last year, combined with cautious buying due to high interest rates and inflation. At the distributor level, while lower inventories compared to prior appraisals benefitted NOLVs due to lower weeks of supply on hand, excess inventory increased as a percentage of total inventory, negatively affecting NOLVs in the current period. In some cases, distributors were able to fend off some of the headwinds from falling market prices by locking in pricing to customers. However, this was offset by much lower inventory levels that deleveraged fixed liquidation expenses.

1 Softwood Lumber Futures - Price per MBF



At the time of the prior *Building Materials Monitor* in June 2023, softwood panel prices exhibited a downward trajectory; however, despite less-than-ideal economic conditions, panel prices have remained relatively buoyant and have even shown increases driven by fewer imports and a strong summer, limiting supply relative to demand. Composite prices have seen gains up to 10% compared to a year ago and the first half of 2023, illustrating a market where general cautiousness that would typically lead to downward price pressures can still be mitigated by the right deal.

Hardwood Lumber

Hardwood lumber is used in a number of manufacturing settings, including interior building products such as flooring, cabinets, panels, and doors, as well as furniture, boats, and other industrial applications. Although the market for hardwoods is tied to domestic housing demand and remodel activity, downstream applications in homebuilding, diverse uses in other industries, and export outlets have historically provided some additional protections against sharp changes in pricing, but recent market conditions have bucked that trend.

The unexpected uptick in housing start data from May 2023 proved to be just a blip in an otherwise sluggish year in U.S. residential construction. Housing start data from October came in at 1.372 million, which was 4.2% below October 2022. Residential building permits in October also came in 4.4% below October 2022. These numbers reflect the sentiment in the marketplace as demand for hardwood lumber and lumber products remains stifled. The widespread decline in production levels among hardwood mills since the end of 2022 has helped hardwood lumber prices creep back up after cratering in 2022, but prices generally remain depressed as demand continues to be soft both domestically and in foreign markets.

However, cautious purchasing has been exhibited throughout the market, as uncertainty surrounds domestic and global economies. Downstream industries for hardwood lumber products are feeling the impact of slowing investment in residential construction and remodel. Outside of a few species, there is ample inventory up and down the supply chain, keeping prices in check while limiting purchases to immediate needs. As we enter the winter months and residential construction activity slows even further, it is unlikely we will see any significant pickup in demand or pricing in the near future.

Repair and remodel activity remains at historically high levels, although it is widely expected final spending numbers for 2023 will

come in flat or slightly below 2022. In addition, after an extended period of projected increases, the Leading Indicator of Remodeling Activity published by the Joint Center for Housing Studies of Harvard University estimated a significant deceleration in activity for the last quarter of 2023, with 2024 projected to be another difficult year. The most recent LIRA chart forecasts a 7.7% decline in spending for the four quarters ended September 2024, which would directly impact hardwood markets such as flooring and cabinetry, as well as other interior and exterior lumber products.

Export activity remains a significant driver in North American hardwood log and lumber prices, and this sector remained sluggish in the second half of the year. Worldwide economic uncertainty is weighing heavily on spending and purchasing decisions. China's economic challenges continue to weigh on hardwood lumber imports. Through the third quarter, lumber exports to China remain down double digits from 2022 volumes. Beyond China, other major export partners like Vietnam and Europe also remain depressed. Mexico and Canada have shown the most promise in the export of hardwood lumber, with strong sales in recent months; however, the pace remains behind 2022 activity. Estimated overall year-to-date export volumes remain approximately 20% below those of 2022.

Appraisal values have remained stable to slightly down in 2023, with a market and pricing environment that has been stagnant for a prolonged period. With such short term uncertainty, it is difficult to forecast beyond a six-month period. As noted, many secondary wood product manufacturers and distributors are well inventoried, and purchasing activity continues to remain cautious. The negative indicators facing the hardwood industry in the second half of 2023, as well as lackluster predictions for the start of 2024, does not lead to expectations of improving NOLVs over the next six months. Hardwood producers' ability to manage inventory levels and maintain pricing to customers will dictate movement in appraisal recoveries.

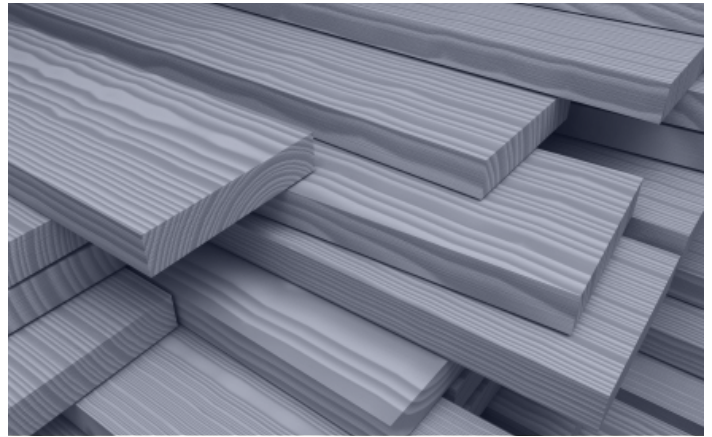
Lumber and Woodworking Equipment

The machinery and equipment involved in woodworking can be divided into two main categories: furniture manufacturing and lumber production. While both industries are tangentially related to both the residential and commercial construction industry, both categories respond differently regarding elasticities.

The sawmill and lumber production machinery industry has been relatively stable. There has been some easing in demand in recent months due to the slowdown in the lumber market, but the availability of good used equipment remains low. Lead times for new equipment remain long, bolstering used equipment pricing. Activity surrounding closures, consolidations, and restructurings amongst producers and wholesalers appears to be minimal at present, although several older mills are scheduled to be sold in 2024. Most of the closures have been single-location operations, which cannot operate with the economies of scale of larger operations and comprise the majority of industry participants. B. Riley continues to monitor liquidations in the sawmill and furniture manufacturing spaces.

B. Riley saw a reduction in mill auctions throughout 2020, a trend that began in 2019 but intensified due to the COVID-19 pandemic. In 2021, the increase in economic activity, combined with high lumber prices, caused demand for good quality used equipment to increase, but equipment availability remained flat. This has led to values for used equipment holding steady or in some cases increasing. Softwood mill equipment fared better than hardwood mill equipment due to its primary use in the building materials market.

In 2023, lumber prices declined back to more traditional levels. Higher mortgage rates have caused new home sales to slow, which has kept lumber inventories elevated and led to decreased prices. This, combined with the ever-increasing potential for an economic recession, has caused



uncertainty in the market. With limited amounts of good quality used equipment available, this has had a limited effect on pricing, but these factors must be closely monitored going forward into 2024.

The woodworking and furniture manufacturing industries enjoyed modest growth over the past several years due to sustained health in the housing market and an increase in disposable income. During this time, the furniture industry has seen increasing demand for customized furniture. Woodworking and furniture manufacturers are investing in automated smart woodworking machinery to respond to quick-changing customer demands, with shorter product changeovers while maintaining efficiencies. These equipment changes are also needed to remain competitive with foreign import products. Although new housing construction has slowed, the market for late model woodworking equipment has been strong through the end of 2023. While older equipment has been relatively flat for several years, recent trends show late model equipment, especially CNC machines, generating strong values. B. Riley has seen a reduction in the frequency of auction events, which limited the amount of used equipment available over the past several years, a trend that continued in 2023 but, as noted, could reverse in 2024. Lead times for new equipment are still long, in many cases up to a year, also helping to bolster values for used equipment.

Monitor Information

The *Building Materials Monitor* relates information covering most building projects, including industry trends, market pricing, and their relation to our valuation process. B. Riley Advisory Services internally tracks recovery ranges for specialty and exotic hardwoods and softwoods, building product retailers and wholesale distributors, and specialty building products, but we are mindful to adhere to your request for a simple reference document. Should you need any further information or wish to discuss recovery ranges for a particular segment, please feel free to contact your B. Riley Advisory Services Business Development Officer.

The information contained herein is based on a composite of B. Riley Advisory Services' industry expertise, contact with industry personnel, liquidation and appraisal experience, and data compiled from a variety of well-respected industry publications and sources believed to be reliable. B. Riley Advisory Services does not make any representation or warranty, expressed or implied, as to the accuracy or completeness of the information contained in this issue. Neither B. Riley Advisory Services nor any of its representatives shall be liable for use of any of the information in this issue or any errors therein or omissions therefrom.



Experience

LIQUIDATIONS

B. Riley Wholesale & Industrial Solutions has been involved in the liquidation of three National Home Centers building products locations, the liquidation of inventory and fixed assets across eight North Pacific Building Materials distribution centers, and the auctions of various woodworking companies, including Woodworking IVA, The Truss Company, Lux Cabinetry, LLC, and Graeber's Lumber & Millwork.

APPRAISALS

In addition, B. Riley Advisory Services has worked with and appraised numerous manufacturers and distributors within the building materials, lumber, and woodworking industries. While our clients remain confidential, they range in scale from smaller, more specialized regional businesses to major global and national industry leaders, and include the following sampling of companies:

- The nation's largest supplier of building materials for home building, as well as professional and contract builders.
- One of the largest roofing products distributors in the U.S., with locations throughout the country and sales exceeding \$2 billion annually.
- Global leaders in home fixtures and plumbing products, including faucets, sinks, toilets, and bath tubs, with presence in over 40 countries.
- Leading manufacturers of HVAC systems, serving residential, light commercial, and commercial applications, with annual sales exceeding \$1 billion.
- The largest publicly-traded roofing distributor in the U.S.
- One of the nation's largest producers of OSB, siding, and engineered wood products.
- The largest independent distributor of wallboard, acoustical, and other specialty building materials in the U.S.
- One of the world's leading manufacturers of windows and doors.

- Regional sawmills, log processors, and producers of green and kiln-dried lumber.
- Manufacturers and distributors of fasteners and bolts used in light and heavy construction.
- Suppliers of iron and wood building components utilized in stair construction.
- Specialty producers of custom interior wood doors for the education, commercial, health care, institutional, and hospitality industries.
- A leading distributor of roofing materials with 60 distribution facilities nationwide.
- A manufacturer and distributor of exterior residential building products, primarily servicing professional contractors.
- Distributors of exotic imported hardwoods utilized in high-end building projects.
- Independent building material and plumbing product retailers and wholesalers, each serving distinct regional customer bases.
- A diversified holding company operating in the building materials supply industry, with a focus on more specialized supply services.
- A manufacturer and distributor of metal roofing and accessories for residential, light commercial, and agricultural applications.
- Various companies' woodworking machinery and equipment, including producers of dimensional lumber, hardwood lumber, plywood, and fiberboard.

In addition to our vast liquidation and appraisal experience, B. Riley Advisory Services maintains contacts within the building materials and lumber and woodworking equipment industries that we utilize for insight and perspective on recovery values. B. Riley Advisory Services is a subsidiary of B. Riley Financial, Inc., whose affiliate B. Riley Securities, is nationally recognized for its highly ranked proprietary equity research.

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MONITOR BUILDING MATERIALS
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