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## DEALERS of the YEAR

**MANUFACTURER'S  
GUIDE TO IG  
CERTIFICATION**



By Andrew Bohutinsky

### How Investors See Industry in Current Climate

This summer, Lincoln International and Arthur D. Little co-hosted the 2008 Building and Construction M&A Conference in New York City. Attended by more than 250 financial and building industry participants, the conference offered a number of insights on how investors view the industry given the current climate in residential and nonresidential construction.

In a panel discussion featuring senior executives of building product companies, Peter Dachowski, CEO of CertainTeed Corp., suggested that there are four major trends shaping the industry today:

- The downturn of residential construction in the U.S.
- The financing crisis and the global tightening of credit;
- The rise of Asia and its impact on the price of commodities, especially energy;
- The collapse of the U.S. dollar.

These four trends have changed perspectives on where opportunities lie for the future, he noted. In particular, Dachowski said, “sourcing from overseas as a basic business strategy, which was a slam dunk some years ago, with the exchange rate movements and the rise of real wages,” has to be reconsidered.

Panelists pointed to multiple areas that now present exciting opportunities for the future. These include renewable technologies and green building products, building services and commercial construction.

#### CUSTOMER RELATIONSHIPS

Panelists also emphasized that businesses need to develop deep customer relationships to enhance value and be positioned for the future. “If you do not have a special relationship with your customer, where you can extract value and pass on your costs,” said Ted Hathaway, CEO of Oldcastle Glass, “the current inflationary environment

poses immense challenges.”

Both corporate leaders and private equity investors discussed the issue of customer concentration, which is particularly prevalent in the building and construction arena. Exposure to Home Depot and Lowe’s, which represent more than half of all home improvement sales nationally, was intensely debated.

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Dan Pansing, of Merit Capital Partners, commented that “when companies get involved with those customers...it’s distracting to the growth of the rest of their business.” High levels of customer concentration have a big impact in the evaluation of acquisition opportunities, causing some investors to reduce their valuations and others to not consider the transaction altogether.

#### MARKET OUTLOOK

Keynoting the event, Kermit Baker, chief economist at the American Institute of Architects and senior research fellow at Harvard University’s Joint Center for Housing Studies, noted that while the limited availability of mortgages and other credit conditions are currently having a negative effect, there are positives in the long-term outlook. Once excess housing inventory is absorbed, the industry can move towards a new round of production and continue with its long-

term growth trend because the longer term trend for household formations, a key driver for homebuilding needs, is very strong.

“We think we’re going to get back on track to produce between 14 million and 15 million new households this decade in the country,” he remarked. That prediction is up from

the 12.5 million in net new households formed over the last decade. This demographic trend provides a strong foundation for long-term demand in the housing industry, pointing to robust growth in the future. Once the economy is out of the woods, there is reason to hope for a quick recovery for residential construction, he suggested. “In previous cycles, there has been a sharp upturn in residential recovery, with production increasing 15 percent to 30 percent in the first quarter of a recovery, based on data from the last 50 years.”

Commercial construction has so far withstood the downturn in the residential sector and is forecast to grow by 2 percent until the end of 2008, but it is expected to decline by about 4 percent in 2009. Baker noted that most indicators point to a very mild nonresidential cycle by historical standards. One reason for this, he said, is that the institutional sector is expected to remain

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reasonably healthy throughout the period and post modest growth in 2009.

Overall, the conference highlighted that difficult times also tend to be times where great opportunities to build for the future present themselves to opportunistic industry participants. Companies that use these difficult times to reduce their cost structure, deepen relationships with their customers and suppliers and streamline their product structures can emerge as stronger competitors once the industry recovers. While the building and construction industry is facing a difficult market, a future

where more efficient construction practices, new technologies and environmentally friendly products transform the buildings of tomorrow can be seen in the horizon. ☐

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