



# BUILDING INDUSTRY ADVISORS, LLC

MERGERS - ACQUISITIONS - EQUITY - DEBT

## BIA Executive Insights

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

December 2020

### Potential Buyers Are Watching What You'll Do with Dollars Earned and Lessons Learned in '20

*By Michael Collins, Managing Director, BIA*

I'm writing to you today on the winter solstice, a fitting near-conclusion to 2020's *annus horribilis*. But while this may be the Northern Hemisphere's shortest, darkest day of the year, it also is a day for optimism, and not just because the sunshine will return. Two Covid vaccines are being administered to first responders and the



most at-risk individuals, with millions more doses to come. At the same time, the LBM

industry is entering 2021 with an unexpectedly strong tailwind, as lots of signs point to continued robust demand for new homes and big remodeling projects. Given such prospects, it's no surprise that big private equity firms like **Bain Capital** and **American Securities LLC** are investing in construction supply.

We're hearing enough stories about robust sales volumes (leavened by sky-high lumber prices) to make us believe the vast majority of dealers will record a great year. So here's the next question: What will you do with that money?

You might be eyeing additional equipment, opening the checkbook for IT and computer gear, or spending money on structural improvements. Some of you already have given bonuses to employees, and others who aren't going the tax mitigation route might choose to put the money into a rainy-day fund.

Then there likely are some owners who remember going without a salary during the recession and thus will choose to pocket that cash rather than invest it. This particularly might be the case if they plan to exit their business soon and are thinking ahead to retirement needs. To that group we say: Please think again, because that strategy could end up reducing your facility's value in a sale.

This might happen because prospective buyers want an LBM operation that's on the upswing. Your willingness to invest, even if you're planning to leave eventually, signals to buyers that you intend for your company to remain strong for years to come. Passing that litmus test could help boost your company's valuation at sale beyond what you would have made if you had kept the money for your own purposes.

We're all tired after experiencing such a crazy year, but take heart: We're slowly coming out of the darkest days. It's time to position our companies for the future.



## Foundation Building Materials

Date	4/13/15	6/3/15	7/27/15	8/24/17	8/27/20
Buyer	<u>Builders FirstSource</u>	<u>Stock Building Supply</u>	<u>Beacon Roofing Supply</u>	<u>Beacon Roofing Supply</u>	<u>Builders FirstSource</u>
Target	<u>ProBuild Holdings</u>	<u>BMC</u>	<u>Roofing Supply Group</u>	<u>Allied Building Products</u>	<u>BMC Stock Holdings, Inc.</u>
TEV	<u>\$1,820</u>	<u>\$969</u>	<u>\$1,142</u>	<u>\$2,625</u>	<u>\$2,632</u>
Fannie Mae estimated forward 1-year growth in total housing starts at the time of transaction announcement	<u>10.8%</u>	<u>9.5%</u>	<u>15.1%</u>	<u>13.4%</u>	<u>3.4%</u>
Multiple	<u>9.6x</u>	<u>10.8x</u>	<u>14.5x</u>	<u>13.6x</u>	<u>9.3x</u>

### Lawsuit Prompts FBM to Provide More Details About Its Planned Sale to PE Firm

Faced with a lawsuit complaining it omitted information from an SEC filing detailing its plans to sell the company to a PE firm, **Foundation Building Materials** on Dec. 21 filed a [supplementary disclosure](#) with more details on the history, logic, and tactics behind the agreement. Some of the extra information concerns standstill and "don't ask, don't waive" provisions during the bidding process, while other sections spoke about the impact on the deal of having roughly \$90 million worth of TRA (tax receivable agreements) be part of the purchase price. That TRA was worth about 0.5x EBITDA for the last 12 and next 12 months.

The supplementary chart also included a table (shown above) analyzing the value and multiples from major LBM deals since 2015. The analysis was done by Evercore, which FBM had hired to help it forecast the financial consequences of various investment, organic growth, or sale plans.

**American Securities LLC** is buying FBM in an all-cash transaction valued at \$1.37 billion. FBM's adjusted EBITDA for the 12 months ended Oct. 31 totaled \$163.3 million, which suggests an EBITDA multiple of 8.4. That's lower than any of the deals cited above,

but the pandemic, the current stage of the cycle, and other factors can impact valuations. FBM's revenues for the 12 months ended Oct. 31 are down 5.1%, and it has been hurt by the pandemic-related decline in commercial and multifamily construction. Those parts of the construction industry are likely to feel pain for at least the next year.



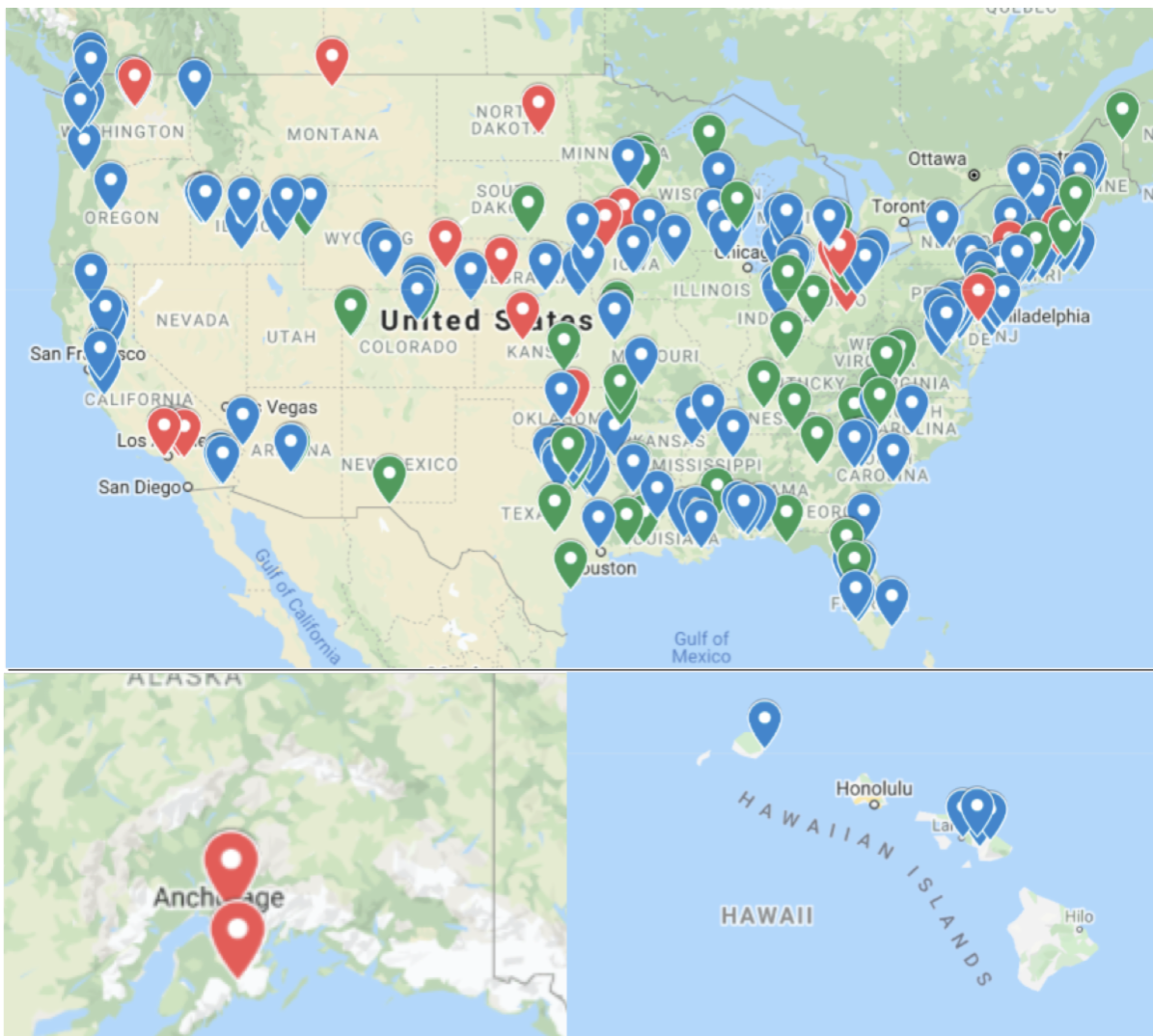
## **Coming Feb. 26: My PS100 M&A Session with Four of the Nation's Biggest LBM Execs**

Here's a setback that's an opportunity: Because the [2021 ProSales 100 Conference](#) will be a virtual event, you now can watch my M&A panel discussion from anywhere ... and for free. It will take place from 12:30 to 1:30 pm ET on Feb. 26, 2021.

The 2021 panel features leaders from four of the biggest--and most acquisition-minded--companies in LBM. They are: Jim Drexinger, CEO, **American Construction Source** (upper left); Steve Swinney, CEO, **Kodiak Building Partners** (upper right); L.T. Gibson, president, and CEO, **US LBM** (lower left); and Ryan Nelson, SVP for corporate strategy, **SRS Distribution** (lower right).

As the moderator, I'm intent on making this more than just a discussion on to how to do deals. It also will be about lessons learned from recent combinations that you can use as you consider buying or selling in the future. How should you adjust your company's geographies to reflect market cycles? What is your business resiliency plan? Expect, too, for the panelists to share a teachable lesson from a particular acquisition.

This event and the rest of the ProSales 100 are free. [Register and get more info here](#),



# Bain's US LBM Buy, BFS-BMC Merger Assure 2020 Will Be a Record Year in M&A Dollar Terms

Billions of dollars changed hands in 2020 as we end what is shaping up to be a momentous year in LBM mergers and acquisitions. Through Dec. 20, there have been 208 yards that were part of deals, along with 53 greenfield openings and 25 closures. But those numbers don't count Dec. 21's announcement by **Beacon** that it was selling 81 yards to **American Securities LLC** and exiting the drywall/steel studs/internal products business. Also missing from that count are the roughly 150 **BMC** branches that soon will merge with Builders FirstSource and take the BFS name. Those 150 exclude the 10 facilities that BMC just acquired from **TW Perry**, which serves the Washington, DC, area.

There also has been a significant activity involving **US LBM**. That company announced Nov. 13 the signing of a definitive agreement in which **Bain Capital** would take a majority interest. US LBM has nearly 300 locations in 32 states and recorded \$3.5 billion in sales in 2019. Perhaps it was with knowledge that Bain was coming in that US LBM on Nov. 2 announced one of the year's biggest acquisitions, taking over **Zeeland (MI) Lumber**, No. 46 on the latest ProSales 100. And shortly after the Bain deal was announced, US LBM purchased **Tri-County Building Supplies**, a five-unit operation in southern New Jersey, and folded it into its **Universal Supply** division. US LBM also bought **Ridgefield (CT) Supply**.

Two days after US LBM revealed its plans, **Foundation Building Materials**, the second-biggest drywall specialty dealer, revealed that an affiliate of the private equity firm **American Securities LLC** had purchased it in an all-cash transaction. At \$19.25 per share, the deal was worth \$1.37 billion. FBM's stock price closed Nov. 13 at \$15.16 per share, so the purchase represents a 27% premium. Once the transaction is closed, FBM will stop being a publicly traded company. Meanwhile, with both the FBM and Beacon yards now in its portfolio, American Securities has become the major rival to **GMS** in the drywall business.

As usual, **SRS Distribution** has been among the most active companies this fall. In September, it announced the acquisition of **RSI Building Products**, a specialty dealer with five locations in Louisiana plus one in Dallas, and on the same day it revealed its purchase of **CB Wholesale Inc.** of Bellingham and Burlington, WA.

On Oct. 2, SRS' **Heritage Landscape Supply Group** acquired **Aquarius Supply**, a landscaping products specialist with four branches in New Jersey, two in Virginia, two in Pennsylvania, and one each in Delaware and Maryland. Heritage returned to the news on Oct. 30 with its purchase of **Irrigators Supply**, based in McKinney (SRS' headquarters city) and Denton, TX, and then again on Nov. 17 when it opened a branch in Wichita, KS, under the HLS Outdoor brand name. And that same day, SRS bought **C.C. Supply**, a roofing specialist with three facilities in Ohio.

Heritage returned to the news in December by taking over two companies in one day: **REAMS Sprinkler Supply**, based in Lincoln, NE, with a total of eight locations in that state, Iowa, and Missouri; and **Irrigation Station**, with locations in Houston and Oklahoma City. In addition, Heritage opened a new branch of its consumer-oriented **HLS Outdoor** stores in Wichita, KS. Add those to the totals and Heritage now has gone from zero to more than 100 branches in just 22 months.

In other action during the 4th Quarter:

- Hawaii's **Honsador**, a unit of **Canwel**, bought **Island Truss**, the only truss manufacturer on the island of Kauai.
- **Lumberly** opened in Cape Elizabeth, ME. This startup specializes in wood products from Maine.
- **Gillman Home Center** opened a new location in Gas City, IN.
- **Beacon Building Products** opened a branch in Denton, TX.
- **L&W Supply**, a unit of **ABC Supply**, purchased the assets of **Coastal Building Materials** in Cape Coral, FL, and opened its second facility in Nashville, TN.
- **TW Perry** acquired **Peoples Supply**, whose single location is in Hyattsville, MD, close to the District of Columbia line.
- **Builders FirstSource** bought **Kansas City Building Supply**, based in Overland Park, KS.
- **Pleasant River Lumber**, a timber mill, bought **Ware-Butler Lumber**, a dealer with three locations in Maine.
- **Nation's Best Holdings**, a Texas-based dealer that enjoys an equity investment from **Do it Best**, did two deals. In November, it bought **Connolly's Do it Best Hardware**, a five-store chain located in Do it Best's headquarters city of Fort Wayne, IN. And one month earlier, it acquired **Simms Lumber** of Weatherford, TX, and Simms' **MetroWest Transload** unit, based in Cresson, TX.
- **Nabor's Do it Best Home Center** purchased **C&D Lumber** of Amory, MS.
- Canada's **All-Fab Group** bought **Littfin Truss** of Winsted, MN.
- **US LBM's Universal Supply** division opened new stores in Manchester, CT, and Yeadon, PA, while its **Raymond Building Supply** division opened a store in Lakeland, FL.
- **ABC Supply** opened a new branch in Concord, NC.
- **Carter Lumber's Carter Kitchen + Bath** design center set up shop in Louisville, KY.
- **Bryan and Char Herrera**, who already own a Colorado business called the **Home Store**, bought the **Holyoke (CO) General Store** and will rename it as the **Home Store of Holyoke**.
- **New Castle (DE) Paint and Hardware** announced it plans to close by Dec. 31.

- **Sparr Building & Farm Supply** opened in Dunnellon, FL, after purchasing a site that became available when **Nichols Supply** closed.
- **Gordon Lumber** planned to close its yard in Port Clinton, OH.



## Government's Slow Pace Forgiving PPP Loans Prompts Need for Extra Language in Contracts

It's likely that tens of thousands of construction supply companies, home centers, and hardware stores received Paycheck Protection Program loans this year, mainly in exchange for promising to keep workers on their payrolls. Given the boom in contractor and DIY spending, the vast majority of firms were able to keep all their workers. So, in theory, there shouldn't be any question that their loans will be forgiven.

If only things were that simple.

October was supposed to be the month in which the federal government will start forgiving the loans, but as of mid-December there's no indications that any applications for forgiveness have been approved. As a result, we're starting to get questions about how to handle these loans when an M&A deal is under way.



We believe that the high likelihood a PPP loan will be forgiven requires that PPP money be treated differently in the contract than are other debts. We suggest that language be inserted into the contract putting into escrow an amount equal to the PPP loan, from which the seller will get that money only after the PPP loan is forgiven.

We'll be happy to assist you with any questions about how to handle an outstanding PPP loan. In the meantime, we'll keep tracking developments. One of the most recent came when the Small Business Administration signaled that it wanted PPP recipients of \$2 million or more to complete loan necessity questionnaires. The National Lumber and Building Material Dealers Association wrote to SBA on Nov. 11 asking the SBA to withdraw that proposal or at least exempt businesses that had been designated as essential. There's been no word on the SBA's response.

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

## **My Favorite Charts and Discoveries from Meetings and Reports Season**

*By Craig Webb, President, Webb Analytics*

The fall normally is a busy time on the road for me as I speed from one conference to another, supplementing reports from those events with a flurry of fall reports. This year, my traveling was solely to my office computer for virtual conferences and lots of web surfing, but the nuggets of information I uncovered were just as valuable. Here are highlights.

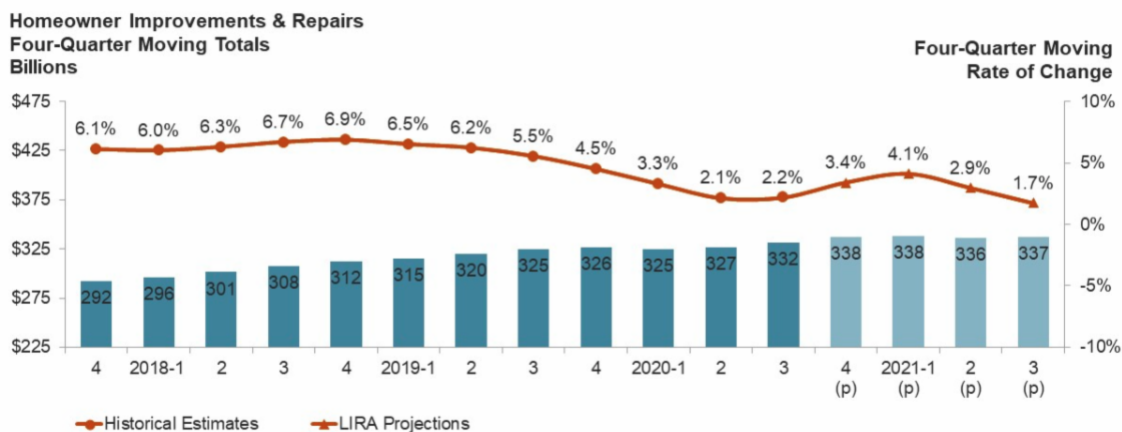
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BUILDER INTENT TO INCREASE USE IN FIVE YEARS COMPARED TO PAST YEAR	AUG 2019	SEP 2020
Roof Trusses	15%	23%
Factory-Built Open Wall Panels	9%	16%
Turn-Key Framing	7%	16%
Pre-Cut Framing Package	12%	16%
Panelized, Pre-Assembled Floors	7%	13%
Modular	7%	11%
Factory-Built Closed Wall Panels	9%	10%
Precast Concrete	7%	8%
Manufactured (HUD-Code)	1%	4%

The arrival of Covid—perhaps combined with an unexpected surge in demand for new homes—appears to be nudging builders toward being more open to embracing off-site construction materials. That’s one conclusion you can reach by comparing surveys of builders conducted in August 2019 and September 2020 by the [Home Innovation Research Labs](#). While the numbers are up, only 19% of September’s respondents said they now feel more favorably about off-site construction. The glacier is moving, but it’s not going very fast.

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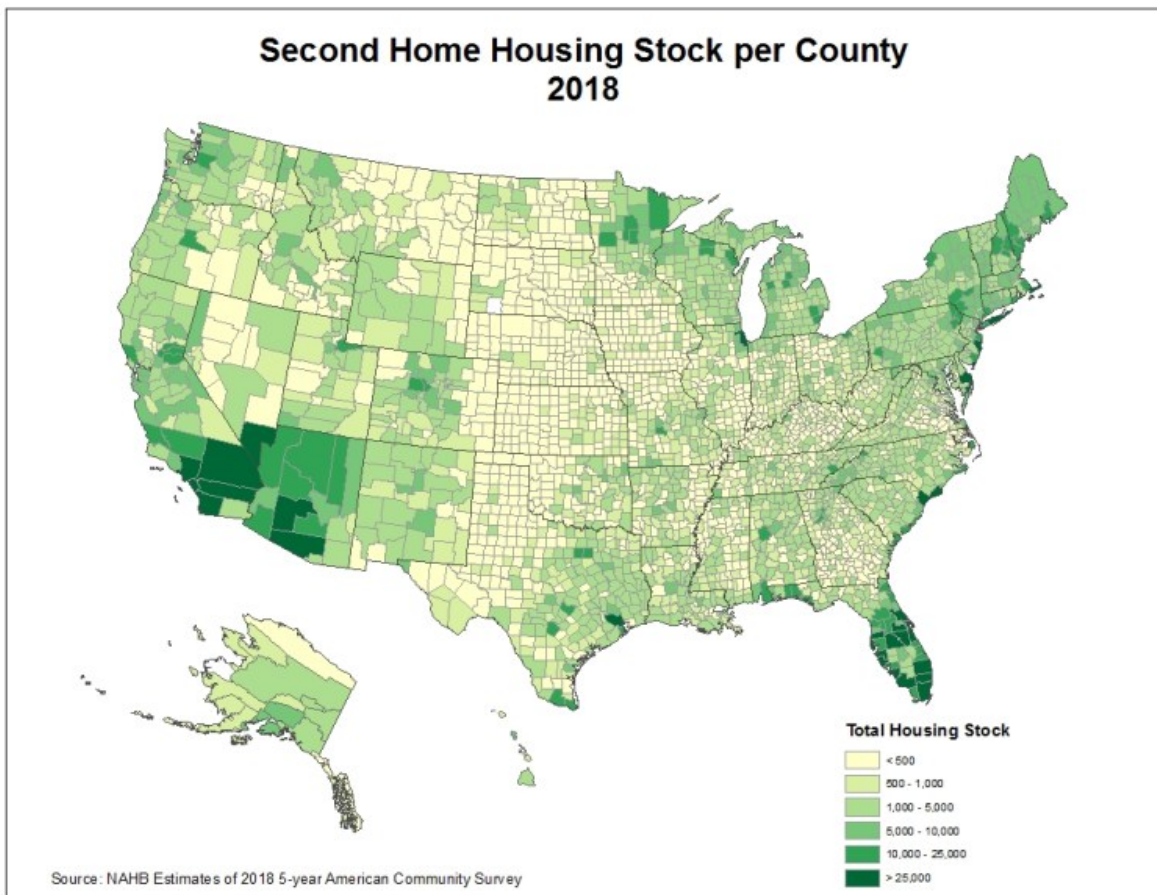
## Leading Indicator of Remodeling Activity – Third Quarter 2020



Note: Historical estimates since 2017 are produced using the LIRA model until American Housing Survey benchmark data become available.

Enjoy the DIY boomlet while it lasts, Harvard University's [Joint Center for Housing Studies](#) (JCHS) suggests. In fact, the center's latest Leading Indicator of Remodeling Activity (LIRA) predicts the annual growth rate in U.S. renovation and repair spending to rise to about 4.1% in the first quarter of 2021 but then soften to a 1.7% four-quarter growth rate by the July-September period. Why? First, because DIY historically has declined as a percentage of total homeowner improvement spending (see chart above). What's happening now is an exception, caused in part because the Covid shutdown took away many other non-DIY activities, like travel and eating out, that many homeowners would prefer to do. And second, the baby boomers are getting ever older. JCHS research has determined that owners 65 or older spend, on average, only 12% of their home improvement dollars on DIY projects.

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Two recent reports from the National Association of Home Builders' [Eye on Housing blog](#) dovetail in a way that can help investors spot what could be one of the next big growth opportunities: markets with lots of second homes. There are 932 counties in 49 states nationwide in which second homes accounted for at least 10% of the county's housing stock, NAHB says. That said, half of the roughly 7.5 million second homes are in just nine

states, particularly far south and far north on the continental map. People often are more emotionally attached to the area where their second home is located than in their main residence, so it stands to reason that if they could live their year-round, they might. That's where the second NAHB report comes in. Its survey found three in 10 people already were working from home part-time or full-time, and with Covid lingering, the work-from-home trend is sure to increase. Combine that with the desire to get away from the city and you could see a shift of people to those second homes. That certainly would be a boon for the area's builders, remodelers and LBM dealers.

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#### INSIGHTS



# 41.3%

say they are budgeting for sales to decrease in 2021 from 2020 actual.

39.7%=Flat 19.0%=Up

Source: NRHA/ 2020

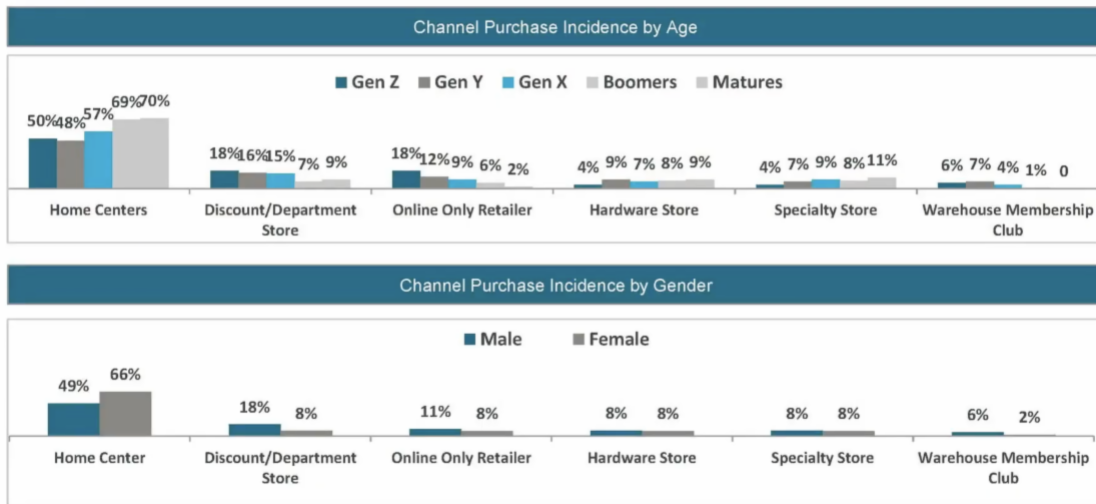


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We cited above some results from a recent survey by the [North American Hardware and Paint Association](#) (what used to be called the National Retail Hardware Association) in which the roughly 600 respondents suggested they did quite well in 2020. On the other hand, opinions were mixed about 2021. Only 19% predicted continuing sales growth next year, while 39.7% thought sales will be flat, and 41.3% were budgeting for a decrease.

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## Where DIYers made their last HI purchase – by Generation & Gender



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The Farnsworth Group is finding notable differences between generations and genders with regard to where and how they shop for home improvement products. In a presentation at the National Hardware Show, Jim Robisch of The Farnsworth Group pointed out that Generation Z (basically, people born after 1995) were half again as likely as millennials and three times more likely than baby boomers to shop online for home improvement products. Meanwhile, there was a 17-point gap between females and males on whether they went to a home center, while there was no difference with regard to shopping at hardware and specialty stores.

## 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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