

# Furnishings Digest Newsletter

April 2016

Reading Time

19 minutes



**Jerry Epperson**  
Managing Director

*Celebrating 45 Years of Proprietary Furniture Research*



## SPRING Home Furnishings Overview

Come See Us at these upcoming events:

- April 13<sup>th</sup>, Milan, Italy- The CSIL World Furniture Outlook, 11AM, C Saloni Fair, Congress Centre – presentation via video.
- April 18<sup>th</sup>, High Point, NC- 9:00AM, the N.A.H.F.A Retail Resource Center, first floor, Plaza Suites building.

My partner Howard Armistead ([wha@maeltd.com](mailto:wha@maeltd.com)) will be at the market as well. Please contact him to discuss valuations, mergers, acquisitions, or our other services.

## SOME PERSONAL NOTES, IF I MAY...

N.C. HB2 – The home furnishings industry probably has our country's best record for welcoming everyone. All religions, ethnicities and sexual orientations can be found within our vast industry. Our products and our retailers, by definition, have to meet the needs of our nation's mix of people. In fact, our industry has historically been a great place for minorities to be creative, express their talents and be recognized with success. In my opinion, if you are uncomfortable working with any of the various population subsets, you should probably go elsewhere.

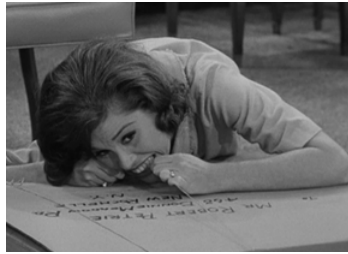
Internet Retailing – The world of home furnishings internet sales has taken hits recently, as a couple of the larger pure internet retailers' financial results have been revealed. Despite years of ramping up products, systems and brand development the losses continue to be staggering even on hundreds of millions in sales. Their private equity partners appear to be losing patience. For furniture, not accessories and décor, the best internet sites appear to be tied to traditional stores that give the websites credibility and provide comfort to consumers who may want to see or try the furniture in person and have a better option for returns. Returns continue to be the largest challenge for internet furniture retailers.



That said, internet sales will continue to grow because of the convenience of 24 hour shopping from home, an infinite variety of options, and constantly improving logistics. Amazon has said convenience and variety negates the need to have the lowest price so we will see how that plays out.

My personal experience with my recent move to a condo has been quite mixed despite shopping and ordering online from Grandinroad, Ballard's Designs, Home Depot, Lowes, Wayfair, Home Decorators Collection, and finding a couple things on eBay. In 30% of the items, the product was disappointing; not that it was misrepresented online but that some elements were not revealed beforehand. That never occurred in the furnishings bought in stores, even when it was ordered through the store.

**The Dick Van Dyke Show** – I am so old that I remember when Mary Tyler Moore as Laura Petrie opened a box that her husband, Rob, had ordered, curiosity getting the best of her. It was an inflatable boat that expanded explosively when the box was opened, getting larger and larger as she tried unsuccessfully to push it back into the box. This image comes to mind whenever I read about the current rage, the bed-in-a-box. I know how the manufacturers get it in the box but if they don't like it, how does the consumer get it back into the box? Yes, some consumers like wine in a boxes too but I don't think the bottled wine makers are so scared that everyone has to offer their version.



**Stores Opening and...** Our industry's leading retailers are aggressively opening stores, "making hay while the sun shines" as we used to say, but that is not true with everyone. Sadly, we continue to see where some of our smaller retailers are closing despite being solidly profitable with great reputations in their markets. Without heirs who want to run these stores, more often than not there is not a viable market to sell these good businesses. This is such a shame, at least to me. As a dear friend once told me "I never paid any of my employees enough that they can afford to buy my business." There is probably an opportunity here.

**The Strong U.S. dollar** is making European and Canadian furnishings more affordable in the U.S. Expect them to push to take advantage and offer some new and exciting furnishings.

- I. The home furnishings industry tends to blame the economy too heavily when business isn't strong. This year we can add the election, a strong dollar and a violent stock market.

Our economy had no housing momentum for six years but twenty-one months ago, housing turnover, consumer spending, employment, consumer confidence and the other important drivers of home furnishings sales turned favorable on a national basis and since mid-year 2014 our industry has enjoyed its best and most consistent sales.

Monthly Trends												Table 1.
% Change y/y	2016											
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Total consumption of furniture & bedding (a)	3.3%	3.9%										
Furniture stores sales (a)	1.1%	6.5%										
Mattress factory shipments (b)	N/A	N/A										
Furniture factory shipments (c)	(1.5%)	N/A										
% Change y/y	2015											
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Total consumption of furniture & bedding (a)	9.5%	4.2%	3.5%	3.4%	5.0%	5.9%	5.7%	5.3%	5.5%	5.3%	4.2%	3.0%
Furniture stores sales (a)	7.6%	3.1%	5.1%	4.9%	4.8%	6.5%	6.9%	3.3%	7.2%	6.9%	5.6%	5.6%
Mattress factory shipments (b)	12.0%	8.3%	3.2%	4.7%	5.0%	12.2%	6.0%	3.3%	13.6%	0.7%	6.5%	N/A
Furniture factory shipments (c)	10.0%	12.0%	3.3%	5.0%	5.4%	6.0%	7.4%	8.0%	3.2%	7.4%	4.5%	4.5%

Sources:

(a) U.S. Department of Commerce (data restated in 2013) (b) International Sleep Products Association (c) "Furniture Insights" a monthly publication by Smith Leonard

Our industry can get some credit from store upgrades and openings, updated and upgraded ad spending, better sales training and restored self-confidence. Vendors have helped greatly with lots of great new merchandise like we saw at the Las Vegas Market. During the recession, our furniture became dull and redundant with too many copying each other, especially at popular price points. Simply put, no one was willing to take any styling risk. Now we are adventurous – isn't it exciting?

With better business the challenges change to where should you reinvest – existing facilities, advertising, presentation, staff, technology, the back-end, additional stores or what? And while traffic in February and March leveled out, and growth has slowed, some of this is because of improving comps from 2015.

Of course, every company has its own answers, but make sure you know:

- We have not experienced this level of new store openings and expansion into new geographic territories since the early 1990's;
- Ad spending including the internet, social media and all other (TV, radio, print, etc.) is the highest seen since before the recession;
- Upgrades to retail displays have been dramatic since 2013, bringing consumers back into the stores. Vendors and great new merchandise have been a key;
- Home-related spending is growing faster than other credit-reliant consumer spending (travel, jewelry, electronics, vehicles, etc.) driven by higher levels of new household formations and Americans changing residences at a pace not seen since 2004; and
- More disposable income and greater employment opportunities have all helped improve our consumers' confidence for the coming years, and combined with ample credit availability, the ability to buy has greatly improved.

### Have You Noticed?

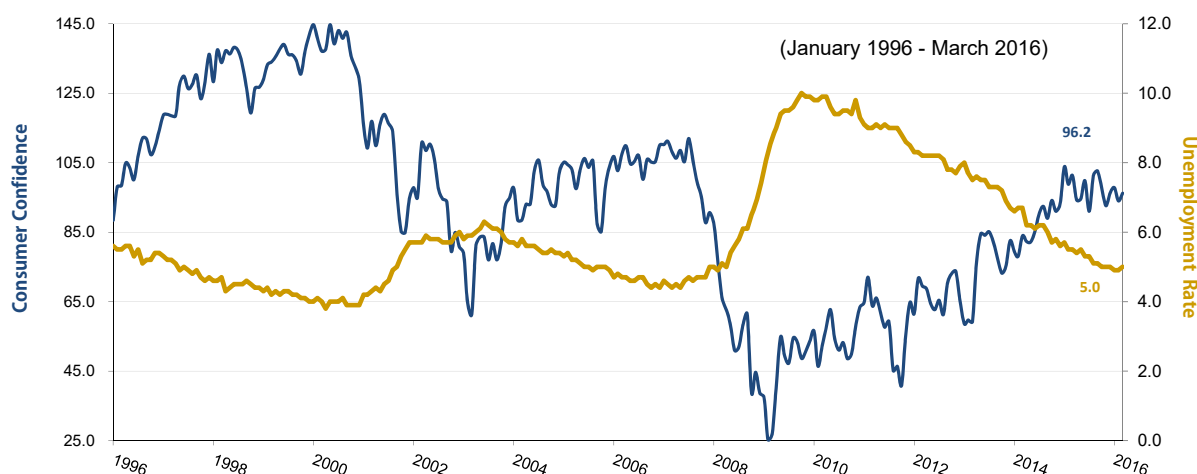
Higher employment	Household mobility is rising	Births are rising
More household formations	Inflation remains low	Home remodeling is increasing
Rising new home sales	Stores are opening	States and counties are improving
More existing home sales	Mortgage rates are great	"Boomerang" kids are leaving parents
Incomes are higher	Wealth is rebounding because:	Migration has resumed
Consumer debt is down	home prices are rising	Key segments of the pop. are growing
Credit is available	the stock market is up	More companies are profitable and expanding
Greater job availability	Consumer confidence is up	Wars are ending, troops returning

## II. The Economy: Back to Basics

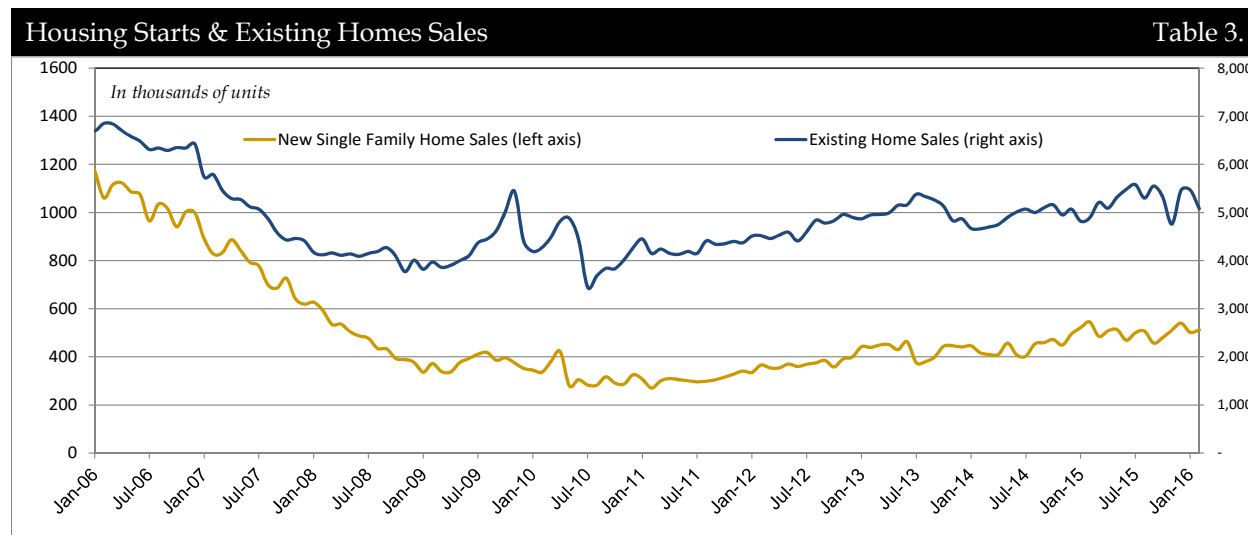
The U. S. economy is not good; it is growing at painfully slow rates. But the factors necessary for home furnishings to do well are all in our favor. Simply put, we need 1) a consumer who is confident and employed; 2) higher levels of household formations and improved housing sales; and 3) lending to be available to finance the consumers' purchases. This last point is looking especially promising since Americans have repaid so much debt since 2009, the banks and other lenders are flush with cash and there are many new financing options available to finance the home furnishings purchase.

National Consumer Confidence Index

Table 2.



Source: The Conference Board

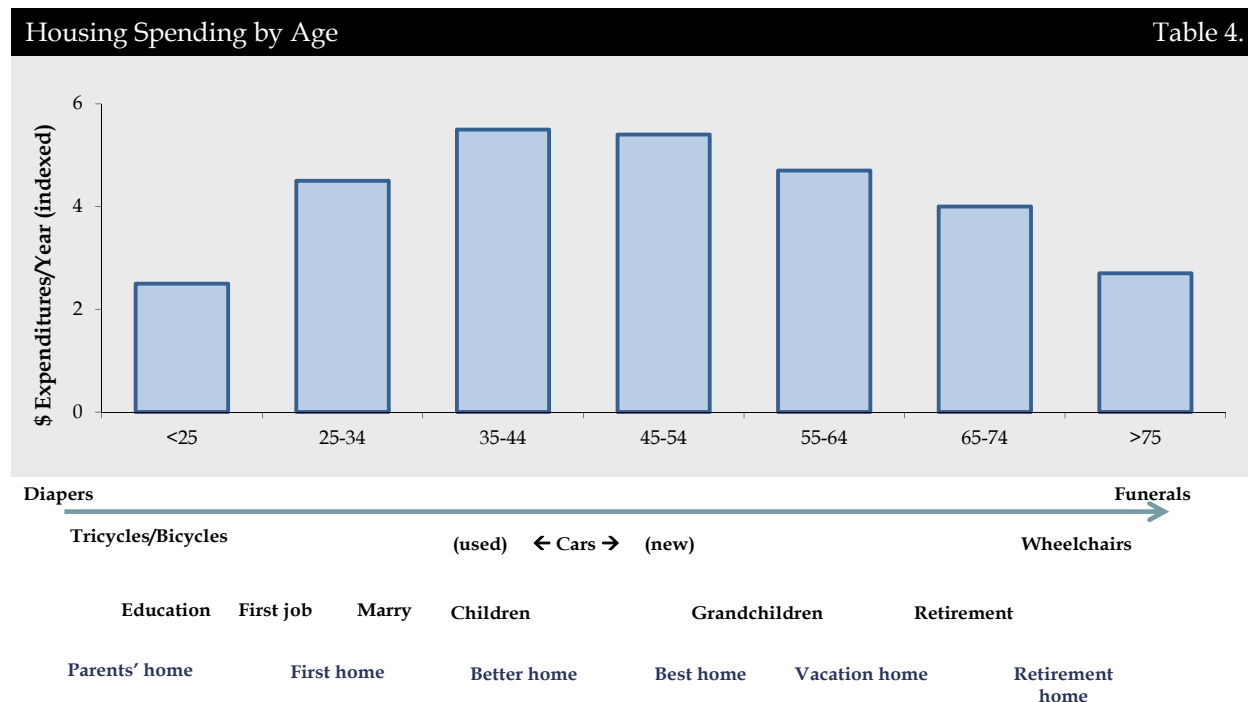


Source: U.S. Bureau of the Census

Benefits of the slow growth economy include low inflation and sustainability. Many of our post-war recessions have occurred because the economy overheated causing inflation and other strains on our economic capacity. This slow growth economy could last the remainder of this decade.

### III. Longer Term: THE NEW GOLDEN AGE OF FURNISHINGS Retailing

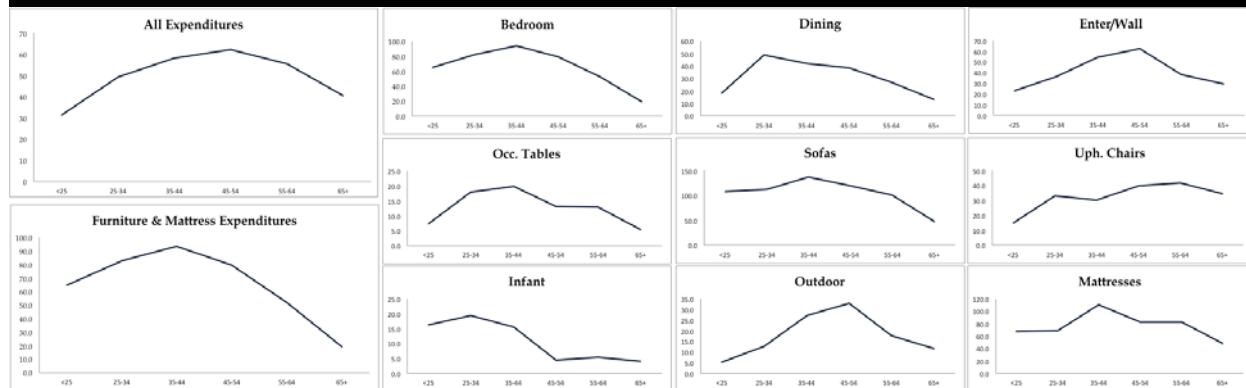
Before we, as an industry can look at our future, we needed a better economy and a return to profitability. That has occurred. In addition to the recession in 2008-2009, our industry has been under another burden, the smaller Generation X. These 57 million people could not support the retail base and economy that had been established to serve the massive 78 million post-war Baby Boomers. Overall household spending peaks in the 35-54 ages (Table 4) and in 2016, the Generation X'ers are 38-51.



Likewise, home furnishing spending peaks in these critical ages although it might differ somewhat by product category (Table 5).

Expenditures by Age per Consumer Group

Table 5.

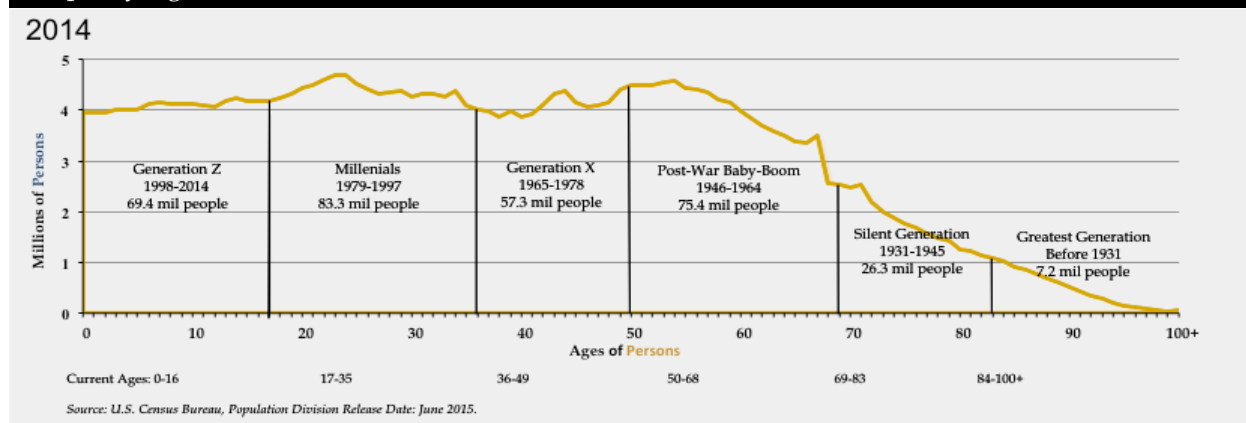


In addition to the lack of households in the key spending years, two additional critical elements developed:

1. The internet added significant additional retail capacity at a time we were over-stored in brick and mortar terms;
2. The massive Baby-Boom generation, once almost 78 million persons, began to reach retirement age or, in some cases, dying. This is the generation American retailers have been serving for the last forty years, and now their priorities are changing as are their incomes. Now 52 to 70, they are still spending but not like they were in the 1990's when they were mostly 35-55.

People by Age

Table 6.



Fortunately, the younger Baby Boomers were more numerous than the older ones, so the impact has not been as severe as it could have been. In addition, although their incomes began to slow overall, their accumulated wealth continued to grow also lessening the impact of them aging.

So what is going to change? The children of the Baby Boom generation will be emerging to have an even larger impact on retail and our economy than the original Boomers did in the 1970's to 1990's.

These Millennials, as they have been labeled, are now 19-37 and there are 83 million of them (Table 6). As they age into the key 35-54 age segment, they will have a growing impact on home furnishings sales, housing and almost everything else.

By 2032, they will be 35-53 and control our economy. But they have a lot going for them, not just size.

1. Having never known a home or classroom without a computer, they will be the most technologically savvy, productive, entrepreneurial and efficient generation ever.
2. The Millennials are the first generation where women and minorities have had, theoretically, the same educational and occupational opportunities as white males. The implications for household incomes and achievement are significant.

3. These are the children of the wealthiest generation, the Baby Boomers. The Boomers had opportunities like no prior generation to:
  - Buy homes when they were inexpensive,
  - Participate in a growing stock market that has been reaching new highs,
  - Be the first to have life and health insurance to protect their wealth,
  - Participate in various savings plans like 401K's, profit sharing plans, IRA's, etc. that have enhanced their wealth, and
  - Enjoy the highest levels of employment, success and income ever experienced.

In addition, some studies believe that the Baby Boomers, the first generation where 2 income households were the norm, feel guilty about not being home with their children, so they will be more generous to them earlier in life.

## SUMMARY

Our economy and retailing was dominated by the 78 million post-World War II Baby Boomers for forty years, 1970-2009. Today, our retailers have three large and very different consumer markets: the aging Boomers, the smaller Generation X and the emerging Millennials.

In each coming year, the Millennials will have a greater impact and create the communities that they desire. In my opinion, while the Millennials today are maturing, they prefer to live in more urban centers close to entertainment and services. What will change this is children and we experienced the first increase in births in 2014 in seven years. Having children made us all face quality of life and educational issues, and for the Millennials, we expect them to migrate to the suburbs to seek a safe, healthy environment plus good schools for their kids. And their "Baby Boom" parents will probably help their children and grandchildren along the way.

Public Furniture Company Latest Quarter				Table 7.			
	Q Ended	Sales	Net Income		Q Ended	Sales	Net Income
<b>Furniture Manufacturers</b>				<b>Bedding Companies</b>			
Bassett Furniture Industries	2016-02-27	3.2%	(45.7%)	Mattress Firm	2015-11-03	50.7%	52.9%
Culp	2016-01-31	(3.4%)	18.0%	Select Comfort	2016-01-02	(33.4%)	Loss
Ethan Allen Interiors	2015-12-31	5.3%	64.7%	Tempur Sealy International	2015-12-31	2.9%	17.9%
Flexsteel Industries	2015-12-31	9.6%	14.6%	<b>Foreign Companies</b>			
Hooker Furniture	2016-12-31	(6.7%)	(3.6%)	Ekornes	2015-12-31	7.1%	41.0%
La-Z-Boy	2016-01-23	7.3%	22.1%	HTL International Holdings	2015-12-31	(4.4%)	Profit
Stanley Furniture	2015-12-31	(13.9%)	Profit	Leon's Furniture	2015-12-31	1.5%	0.9%
<b>Furniture Retailers</b>				Natuzzi	2015-12-31	(5.0%)	(15.4%)
Aarons	2015-12-31	9.7%	(1.7%)	Kasen	2015-06-30	10.1%	Profit
Conns	2016-01-31	15.2%	(1.7%)	Man Wah	2015-09-30	15.1%	11.5%
Pier 1 Imports	2015-11-30	(2.5%)	(38.9%)	Samson Holding	2015-06-30	8.9%	35.0%
Restoration Hardware	2016-01-30	11.1%	(21.7%)				

### Notes:

"Profit" is shown without a % for companies that showed a net loss a year ago  
Chinlink, Kasen, Man Wah & Samson are compared on a 6 month basis

### Sources:

PitchBook as of April 10, 2016

Mann, Armistead & Epperson, Ltd.  
119 Shockoe Slip  
Richmond, VA 23219  
1-804-644-1200  
www.maeltd.com

Wallace "Jerry" W. Epperson, Jr., C.F.A.  
Managing Director

Jin S. Ko  
Financial Analyst

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