

Market Outlook for Building Components – What's in Store for 2002??

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Outline

- **September 11th Impact**
- **Longer term economic outlook**
- **Lumber market outlook**
- **Demographic issues**
- **Componentization in housing**

September 11 Impact

Reading the Economy

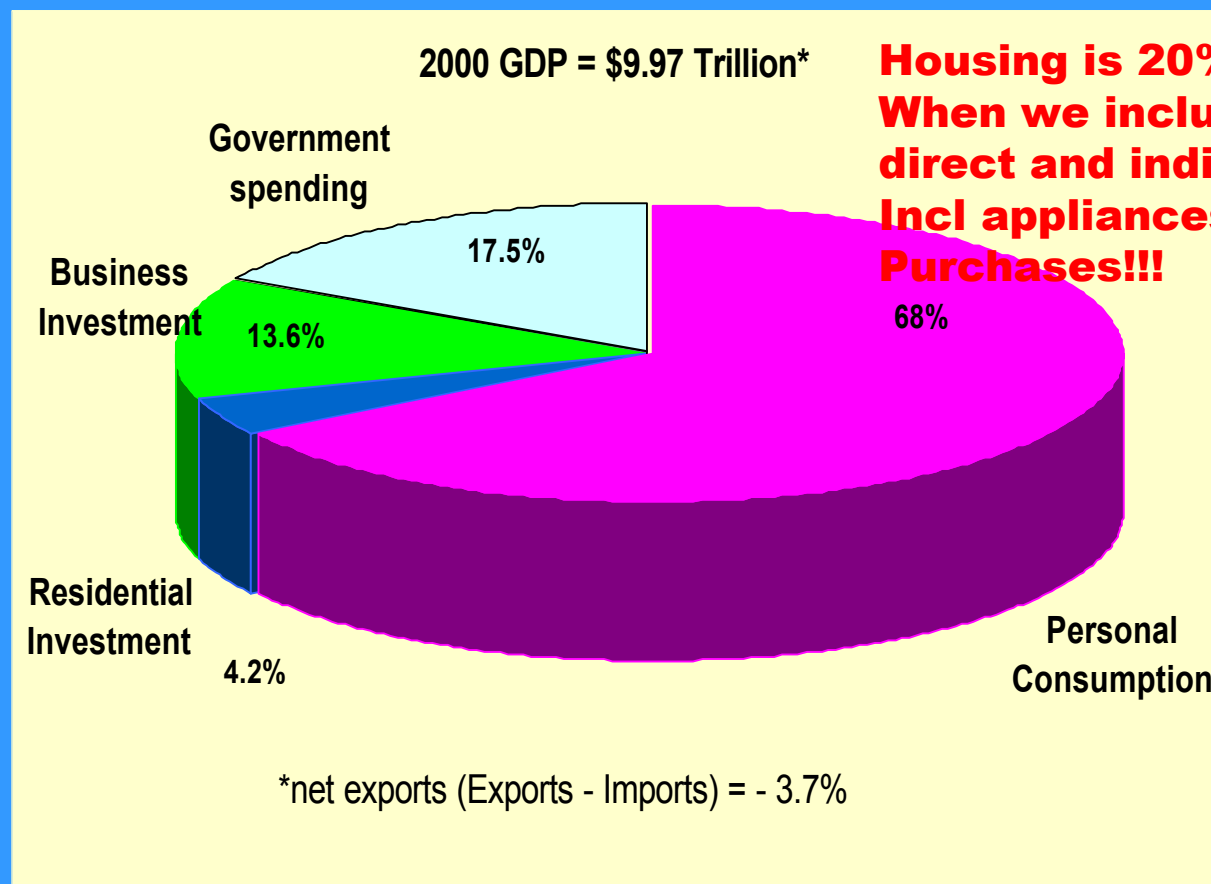
- **No simple answer, but there are easily accessible stats that provide valuable insight**
- **CNNMoney list a number of indicators grouped into four categories**
 - 1. Employment**
 - 2. Consumer spending**
 - 3. Industrial production**
 - 4. Inflation**

Consumer Spending – main engine fueling economic growth

- **Consumer confidence index**
- **Expectations index**
(www.conference-board.org/economics/index.cfm)
- **Advance retail sales**
(www.census.gov/svsd/www/advtable.html)
- **Income growth**
(www.bea.doc.gov/bea/rels.htm)

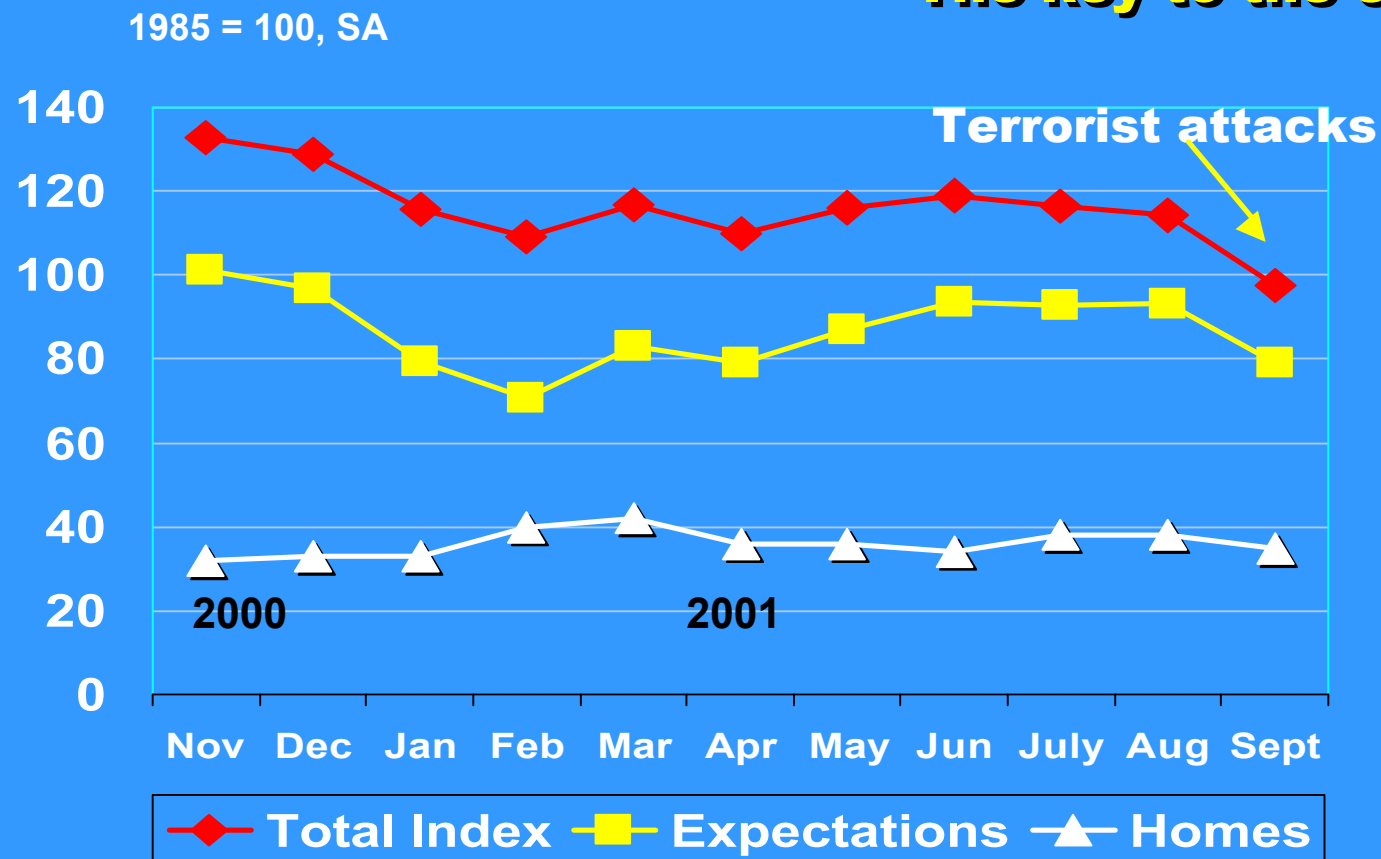
Consumer is 2/3rd's of U.S. Economy

GDP = Consumer Spending + Business Investment + Residential Investment + Govt. Spending + Net Exports



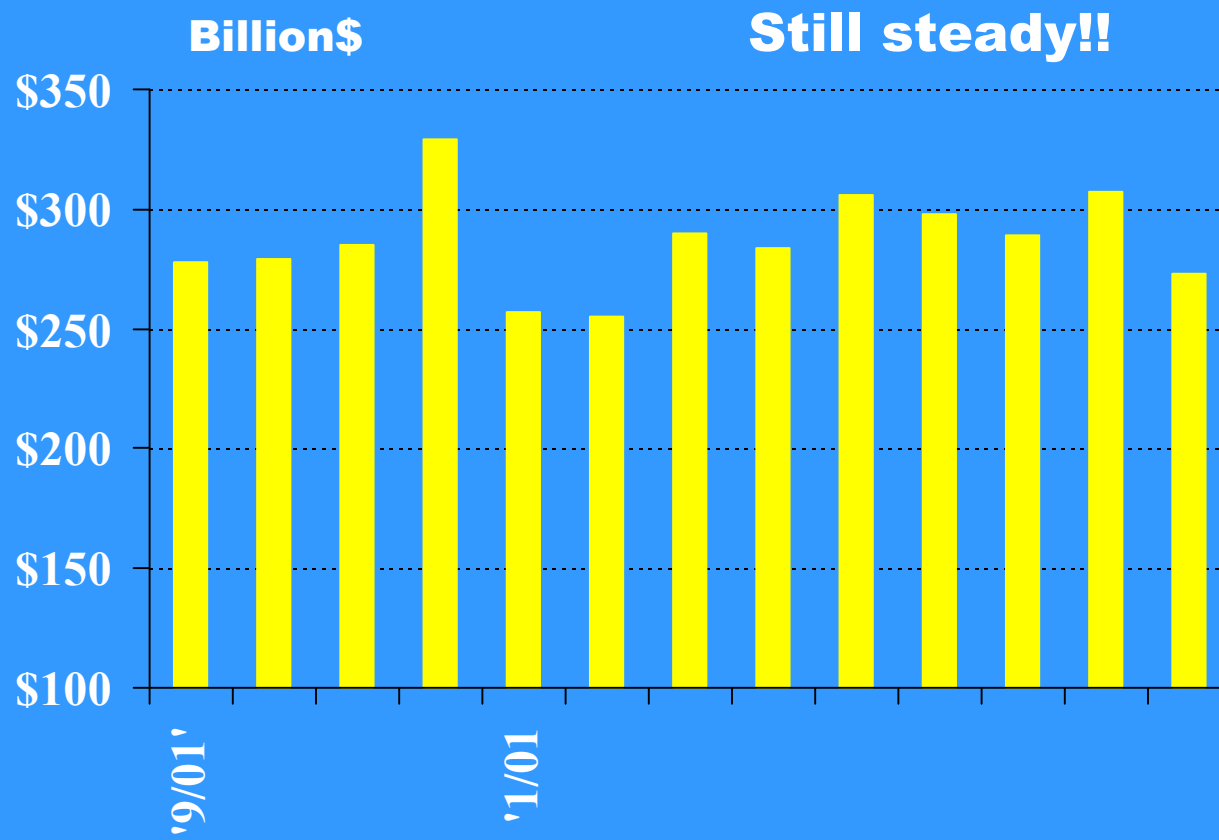
Consumer Confidence – Consumer Spending was 70% of GDP in 2000

The key to the economy!!!



Source: Conference Board (www.conference-board.org/economics)

Advance Retail Sales

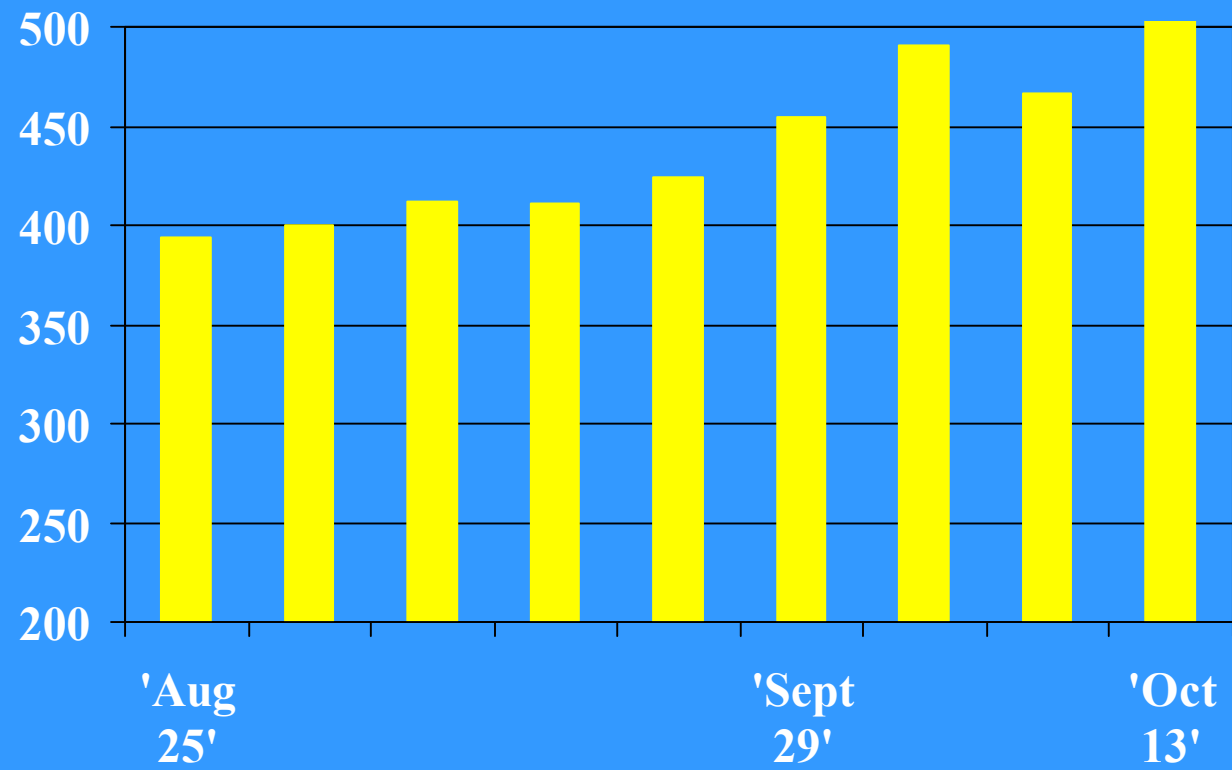


Employment

- **Unemployment rate – lagging**
- **New jobs created - forward**
(<http://stats.bls.gov/newsrelease/empsit>)
- **Help wanted index (Conference Board) - forward**
(www.conference-board.org/economics/index.cfm)

Unemployment – Initial Claims

Weekly Claims, 4 week moving average (000)

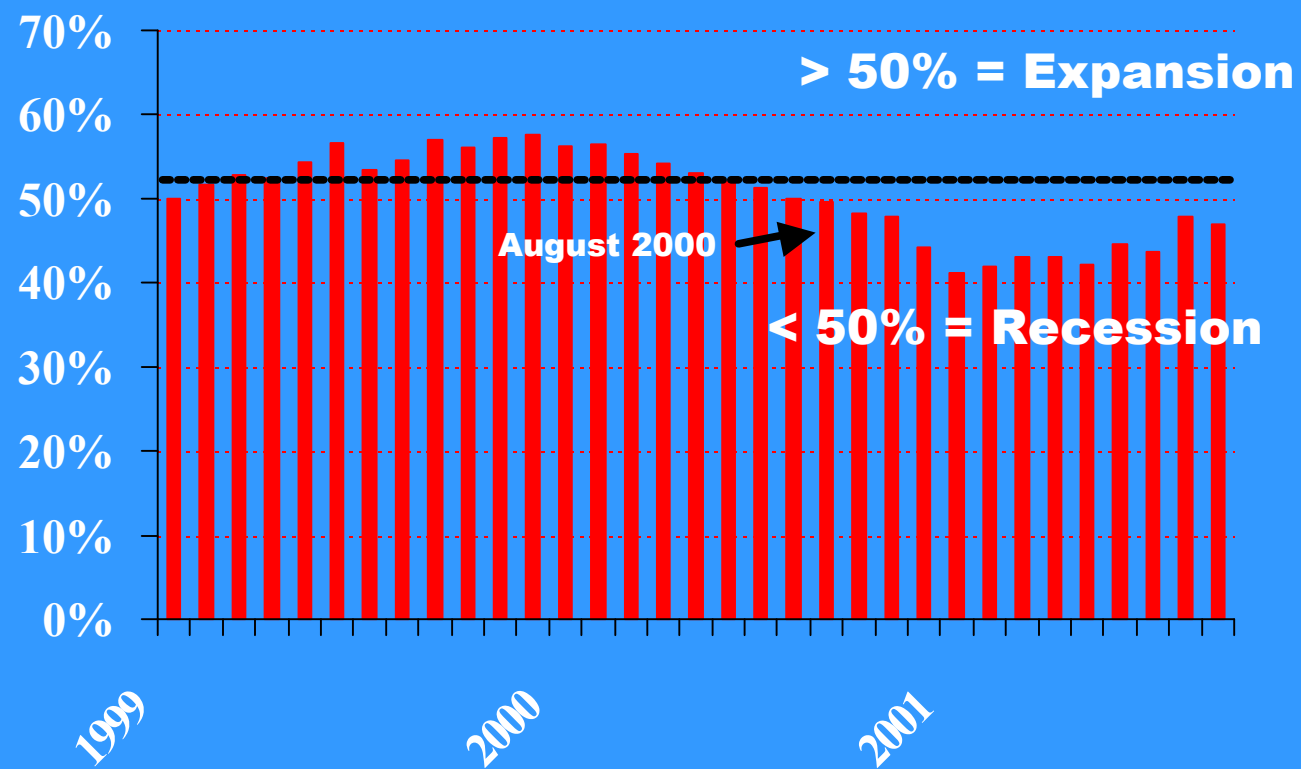


Industrial Production

- **Purchasing manager's index**
(www.napm.org/NAPMReport)
- **Industrial production index**
- **Capacity utilization index**
(www.federalreserve.gov/releases)

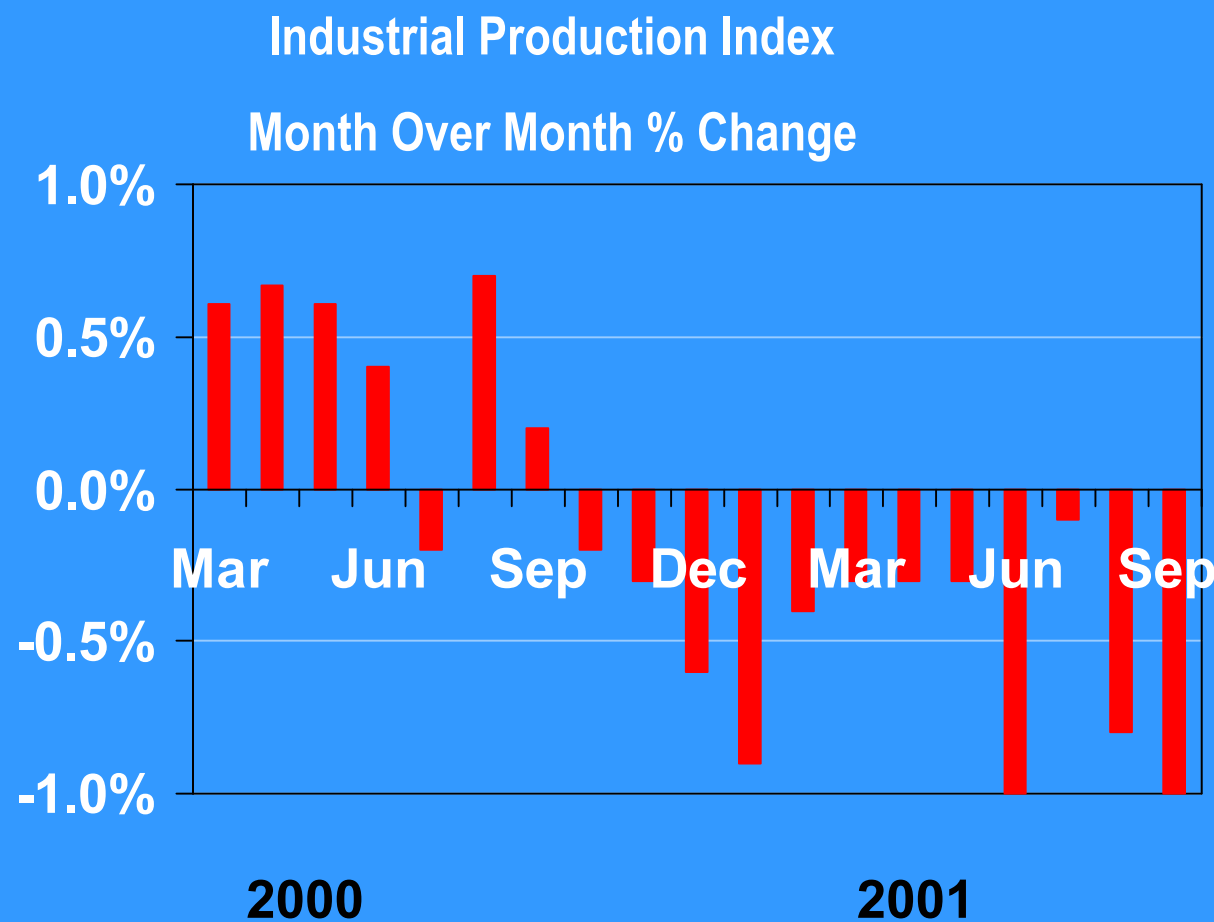
Purchasing Manager's Index

Manufacturing Recession Began in August 2000



Source: NAPM (www.napm.org/napmreport)

Manufacturing Recession



Big problem!

Manufacturing is still contracting each month.

We're assuming that it's ready to turn around very soon.

Depends on continued consumer spending and increasing exports.

Source: Federal Reserve.
(www.federalreserve.gov/releases)

Inflation

- **CPI – retail inflation**

(<http://stats.bls.gov/news.release/cpi.toc.htm>)

- **PPI – wholesale inflation**

(<http://stats.bls.gov/news.release/ppi.toc.htm>)

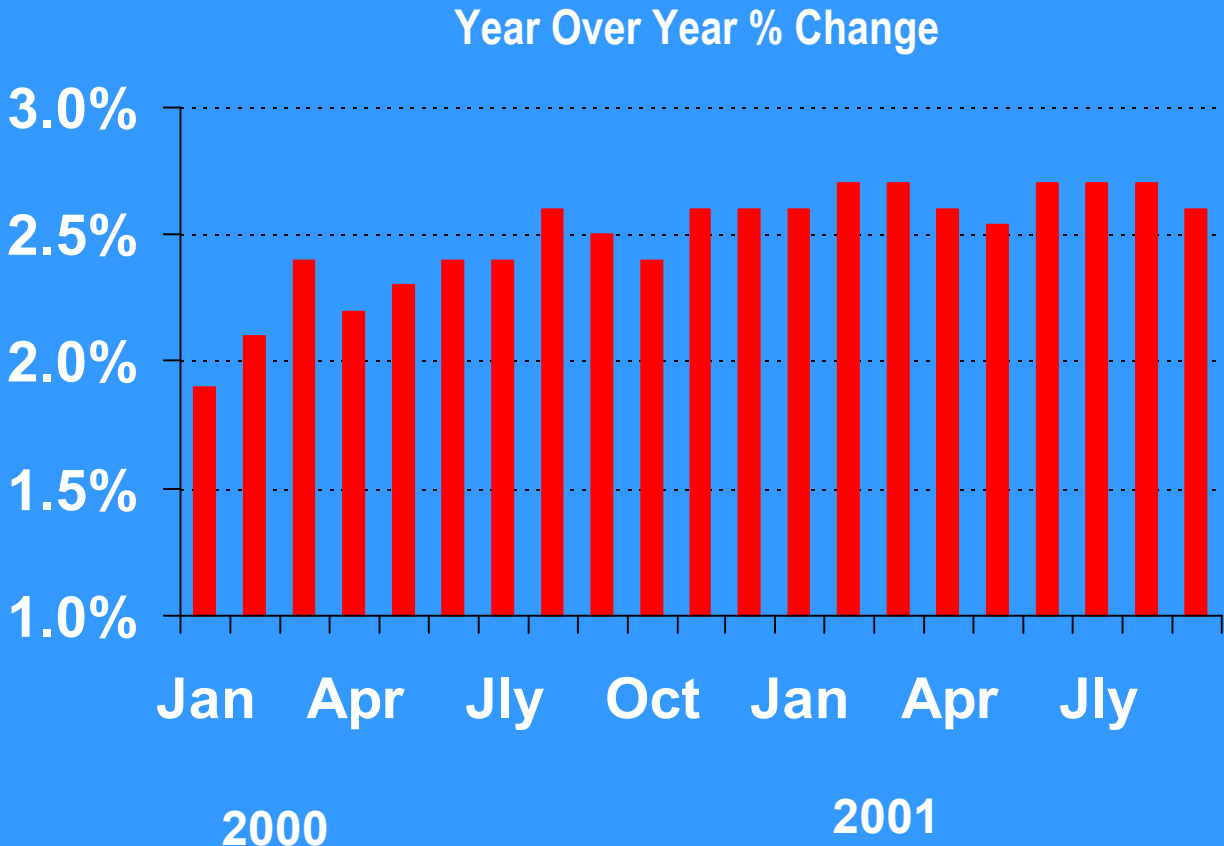
- **GDP deflator – broad measure**

(www.bea.doc.gov)

- **Employment cost index – wage inflation**

(<http://stats.bls.gov/news.release/pdf/eci.pdf>)

CPI- Core Inflation (Less Food & Energy)



Good news:
Core inflation is tame and interest rates can go even lower to stimulate business spending.
Gives Fed more “wobble room” to lower rates further

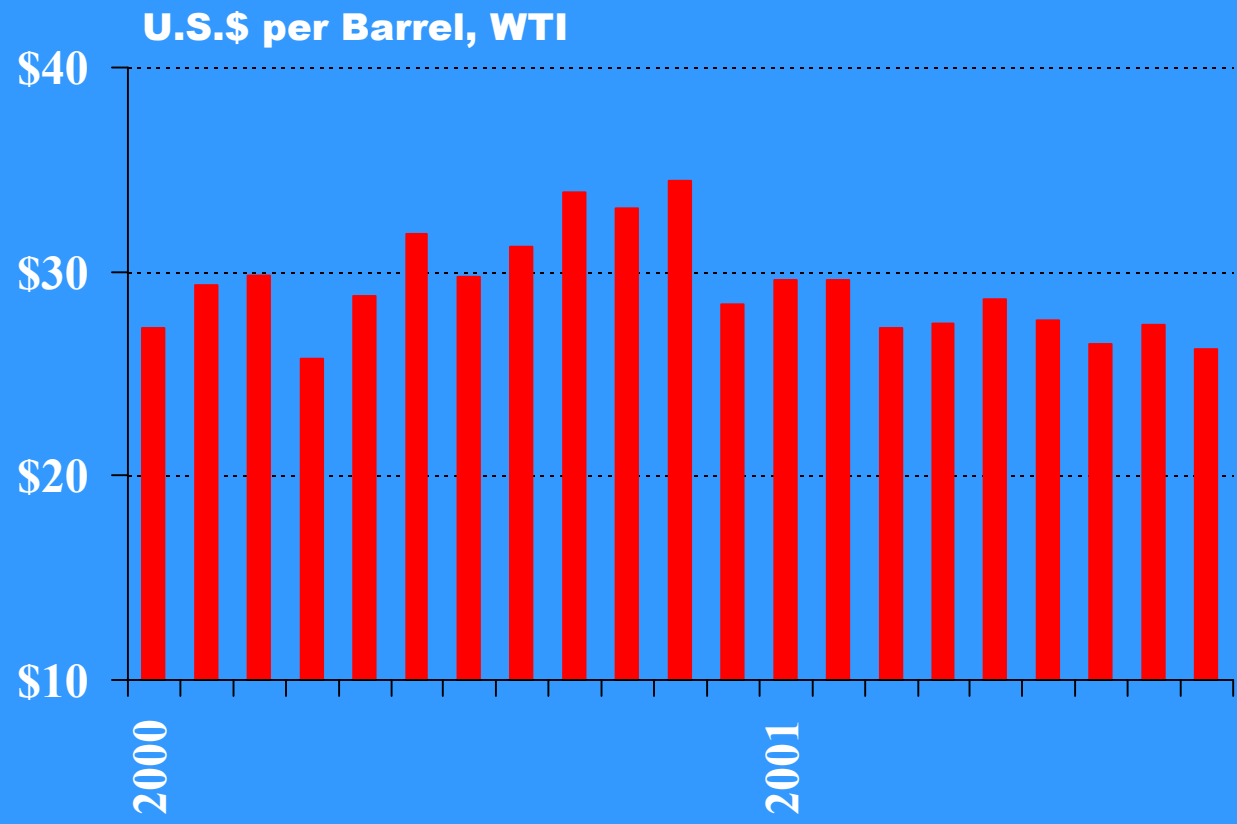
Source: US Census (<http://stats.bls.gov/newsrels.htm>)

U.S. Retail Gasoline Prices

**Can now buy gasoline
For under \$1/gal.(10/15/01)**

| | Price | Change Year ago |
|---------------------------|---------------|--------------------|
| Regular Gasoline - | \$1.35 | \$0.15 ↓ |
| Diesel | \$1.37 | \$0.24 ↓ |

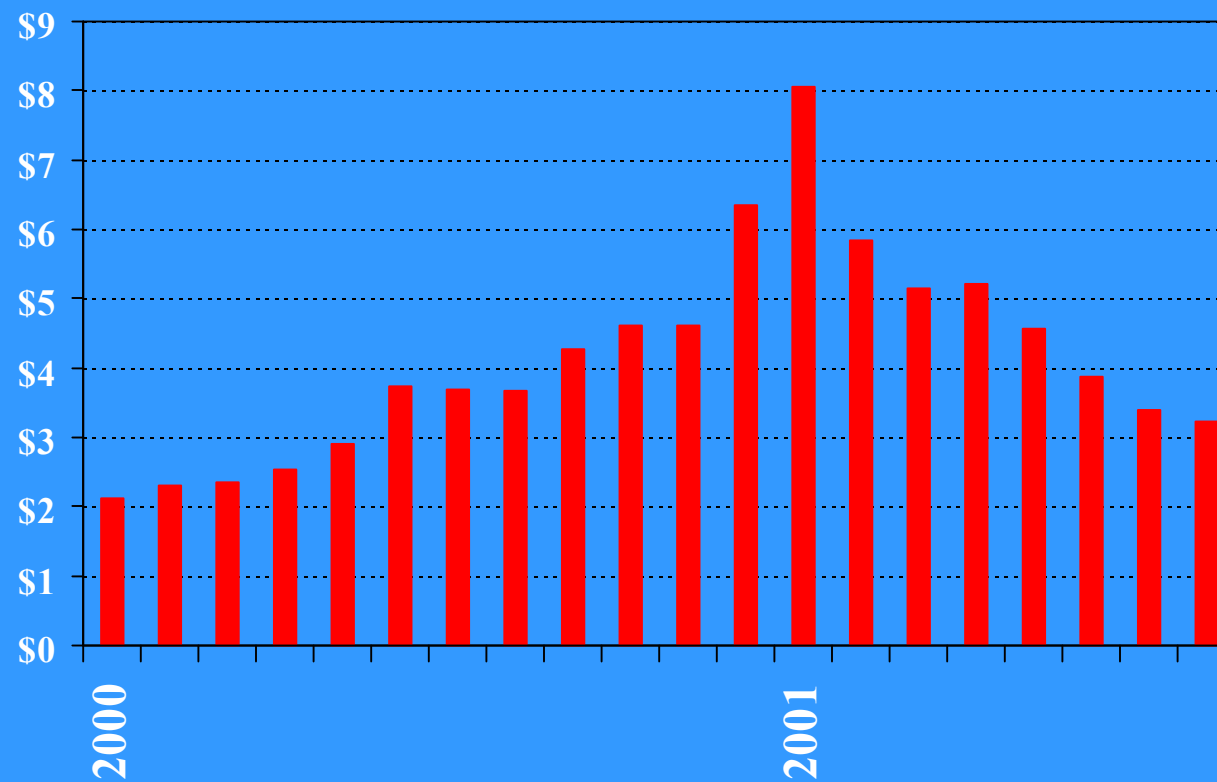
Oil Prices Down



Source: Energy Infor. Adm.

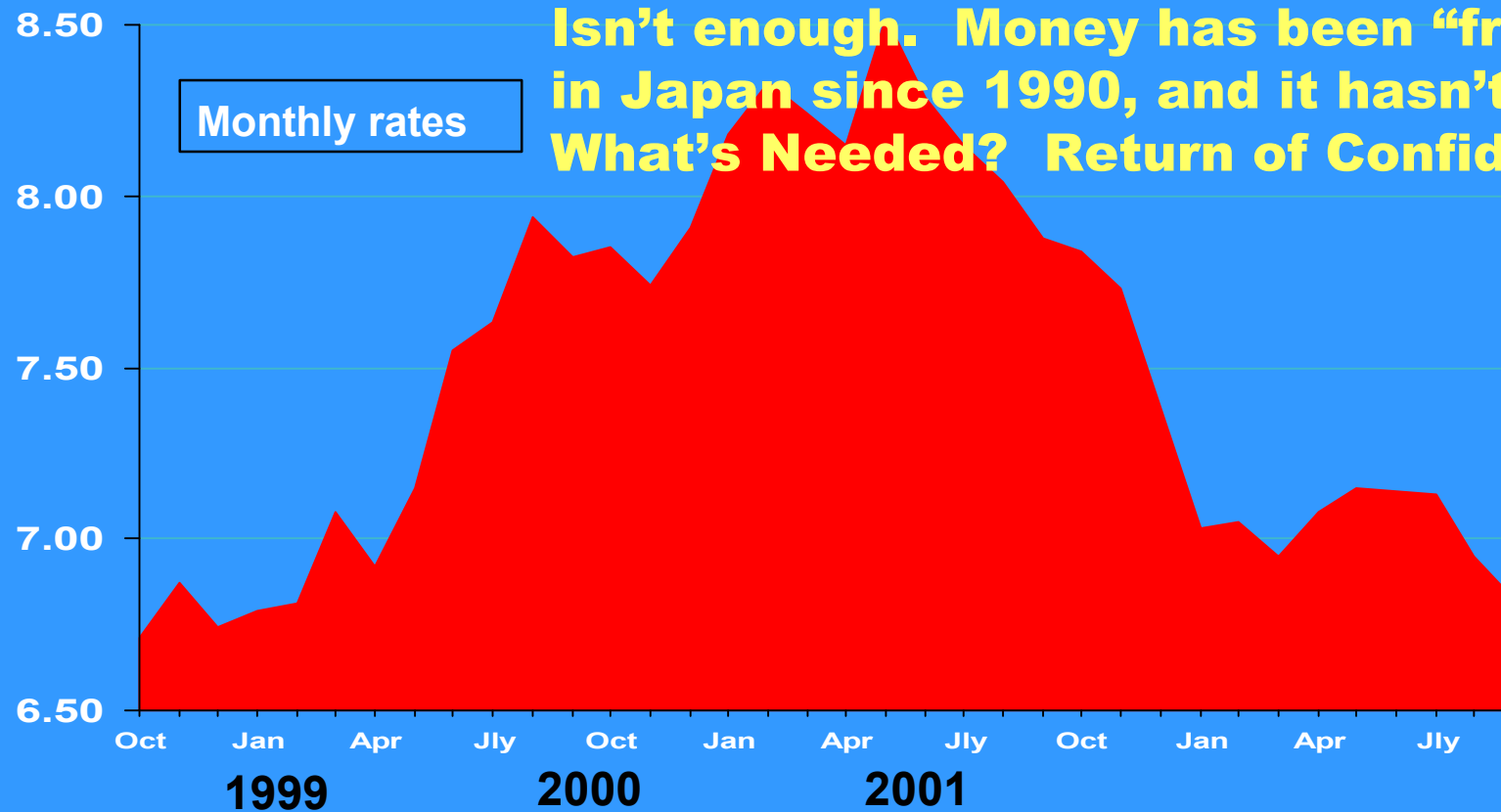
Natural Gas Prices Down

Wellhead price, U.S.\$ per thousand CF



Mortgage Rates - 30 Year: Low Rates are Nice, but Fiscal Stimulus Needed

Fed Funds, at 2.5%, means Money is “free”. But, “free money” Isn’t enough. Money has been “free” in Japan since 1990, and it hasn’t helped. What’s Needed? Return of Confidence!!!

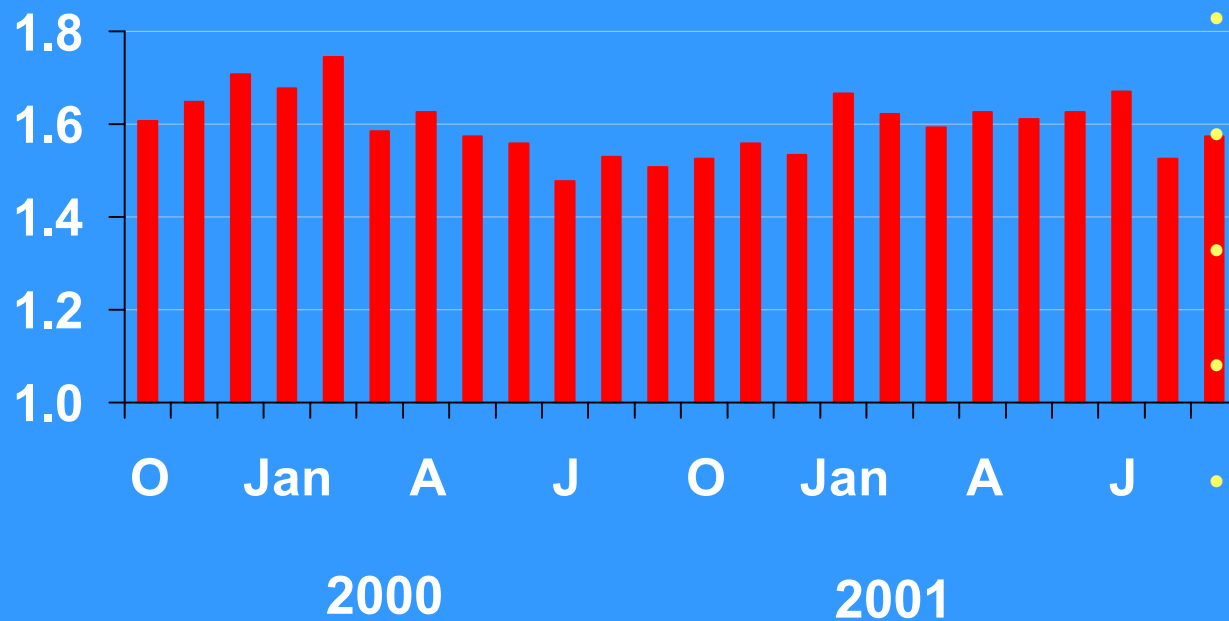


Source: freddiemac.com/pmms/, historical tables.

U.S. Housing Starts

September Annual Rate: 1.574 Million

Seasonally Adjusted
Annual Rate - Millions of Conventional Starts

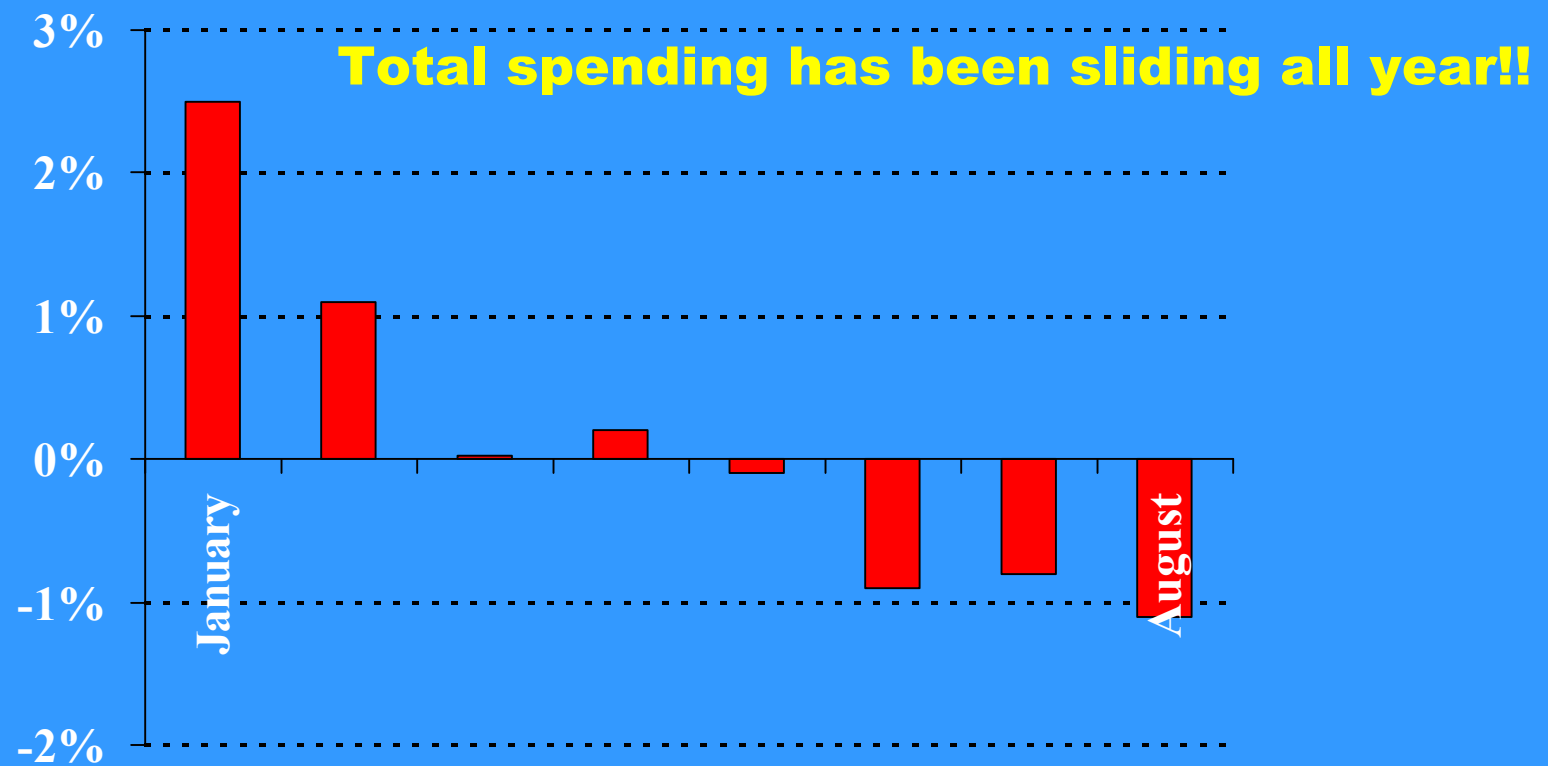


- Housing still healthy:
- Upward trend since mid-2000. 1.6 million rate this year.
- Total actual starts for the first nine months of 2001 were 1,234,300 units compared to 1,211,300 units last year, a 1.9% increase. Total single family starts were 3.3% higher.

Source: census.gov/pub/indicator/www/newconstruction

Construction Spending

Per cent change, Month to Month



Source: U.S. Census (C30); (www.census.gov/ftp/pub/const/www/c30index.html)

Economic Indicators

| <i>Indicator</i> | <i>What it's telling us</i> | <i>next update</i> |
|------------------------------|------------------------------------|---------------------------|
| Consumer confidence | weak growth | Nov 27 |
| Advance retail sales | Steady | Nov 14 |
| Purchasing Mgr. Index | weak growth | Nov 1 |
| Industrial production | weak growth | Nov 16 |
| Unemployment rate | weak growth | Nov 2 |
| New jobs created | weak growth | Nov 2 |
| CPI | low inflation | Nov 16 |

Economic Impact of Terrorist Attacks

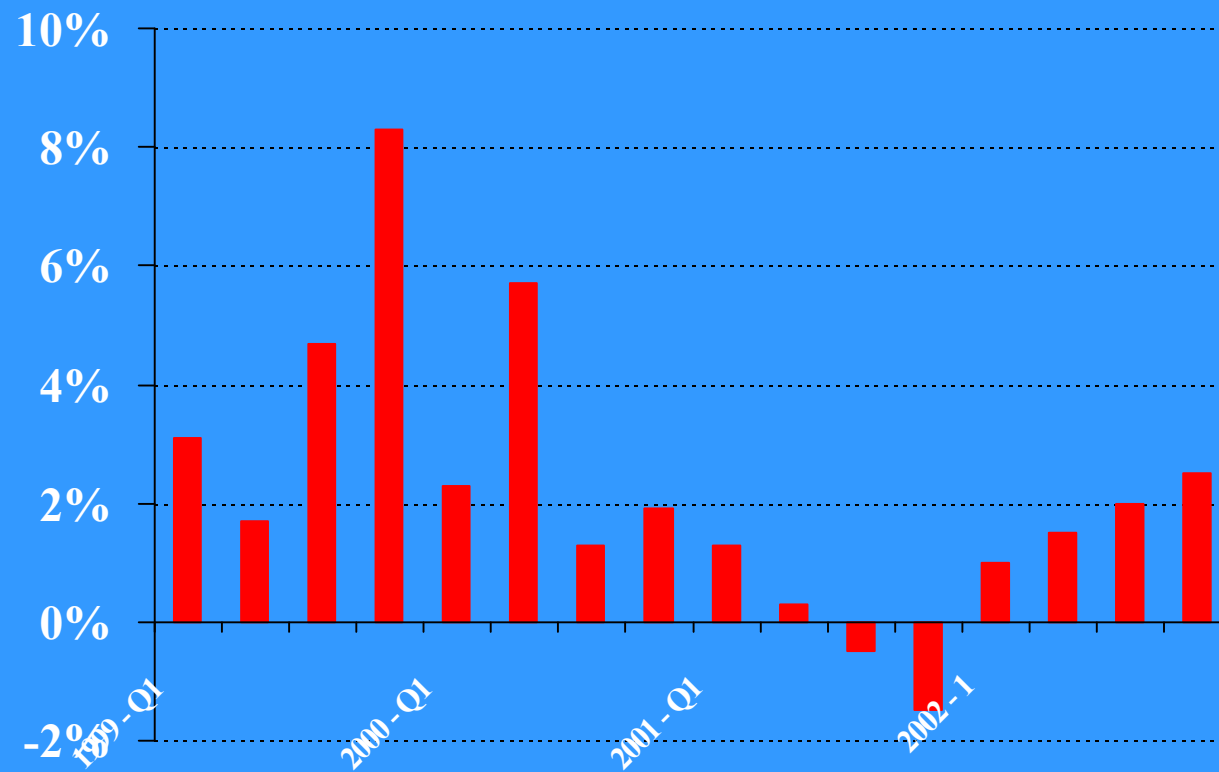
- **Manufacturing economy has been in recession since August 2000**
- **Rest of economy slipped into recession in Q3 – 01**
- **Terrorist attacks will delay recovery by at least 6 months***
 - *Two scenarios:**
 - A. one time event – no more major attacks for 2-3 years: economy will rebound by 2nd half 2002**
 - B. more attacks, spaced 3-4 months apart: big problems as U.S. (and world) is plunged into long term war time economy where each sector pulls back except the government.**
- **Conclusion – assume scenario “A”. GDP will return to trend growth (about 3%) by 2nd half 2002 as consumer and business confidence respond to 9 Fed rate cuts, \$100 billion+ stimulus package, better airline/travel security, and world progress toward containing terrorism.**

Impact , continued

- **Protracted fight against terrorism could make globalization slower and costlier**
 1. more costs and slower movement of goods
 2. immigration impacts – tighter rules
 - legal immigrants accounted for 34% of 1990's workforce growth
 - 25% of housing demand in past 3 years
 3. “The economic boom of the 90's probably would not have happened if not for immigration flows” - (Mark Zandi, Economy.com Inc.)
- **Bottom line – 4% plus growth of late 90's may not return**
- **Key challenge – restore confidence in safety of global economy**

Quarterly GDP*

Terrorist Attack Turns Weak Growth into Mild Recession: Qtr3 – 01 to Qtr4 – 01



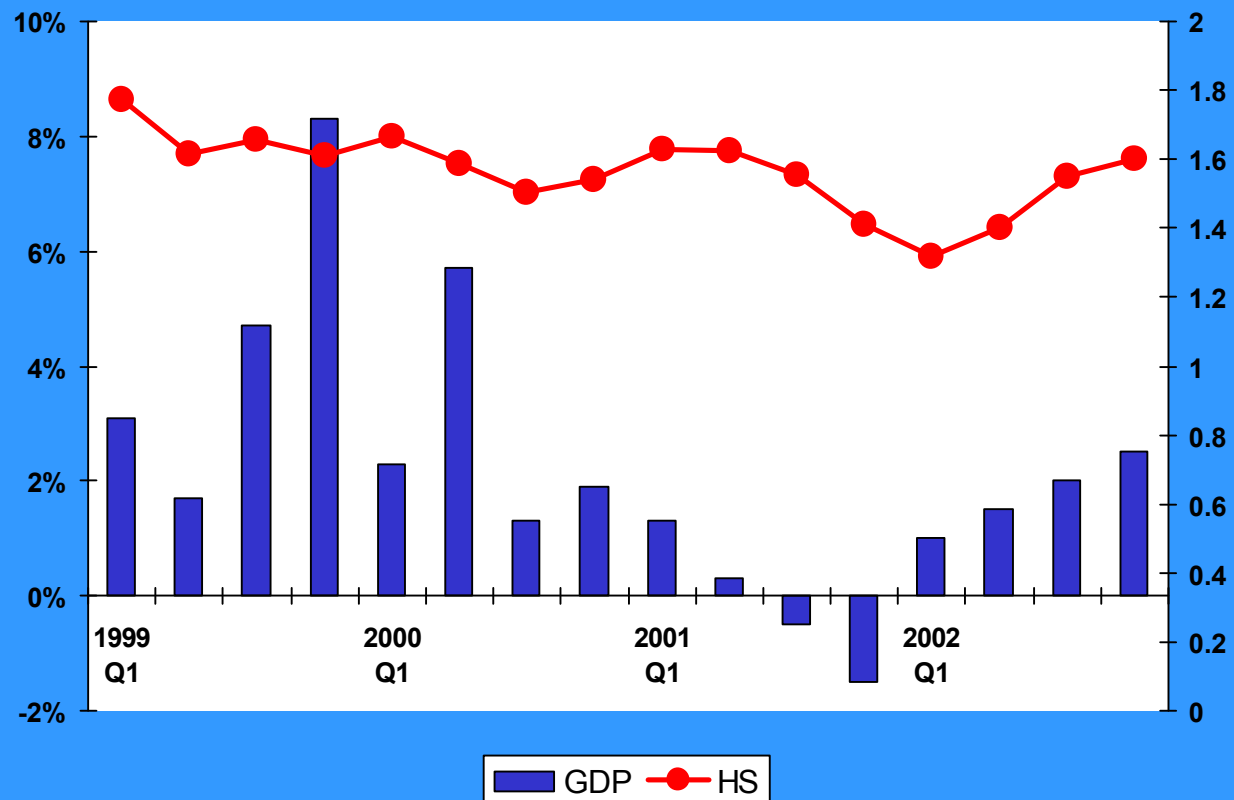
*Consensus (NAHB,NAR,NABE,Conference Board,WSJ, Morgan Stanley)

Quarterly GDP* and Housing Outlook**

Terrorist Attack Turns Weak Growth into Mild Recession: Qtr3 - 01 to Qtr4 - 01

Quarterly GDP growth, Qtr. To Qtr.

HS, Quarterly, SAAR



* Consensus (NAHB, NAR, NABE, Conference Board, WSJ, Morgan Stanley)

** Forecast: NAHB (Sept. 28, 2001)

Global GDP Growth(%) – Post 9/11

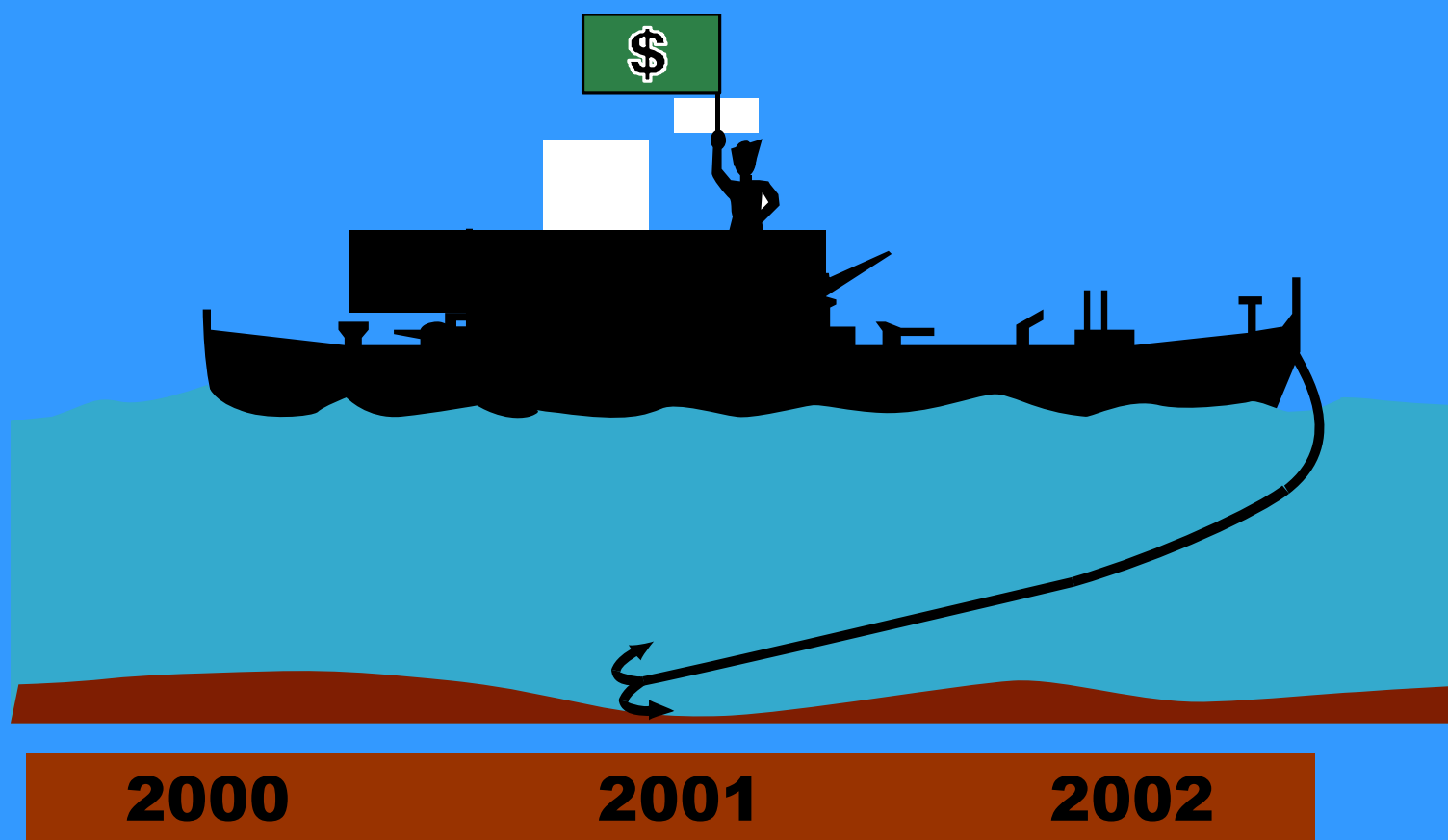
Globalization is the big loser if
fight against terrorism is protracted

| | USA | | Europe | | Japan | |
|------------|------|------|--------|------|-------|------|
| | 01 | 02 | 01 | 02 | 01 | 02 |
| Pre 9/11 | 1.3 | 2.7 | 1.8 | 2.5 | -0.8 | 0.2 |
| Post 9/11 | 0.9 | 1.0 | 1.6 | 1.5 | -0.9 | -1.0 |
| Difference | -0.4 | -1.6 | -0.2 | -1.0 | -0.1 | -0.8 |

Source: Business week 10/22

Longer Term Economic Impact

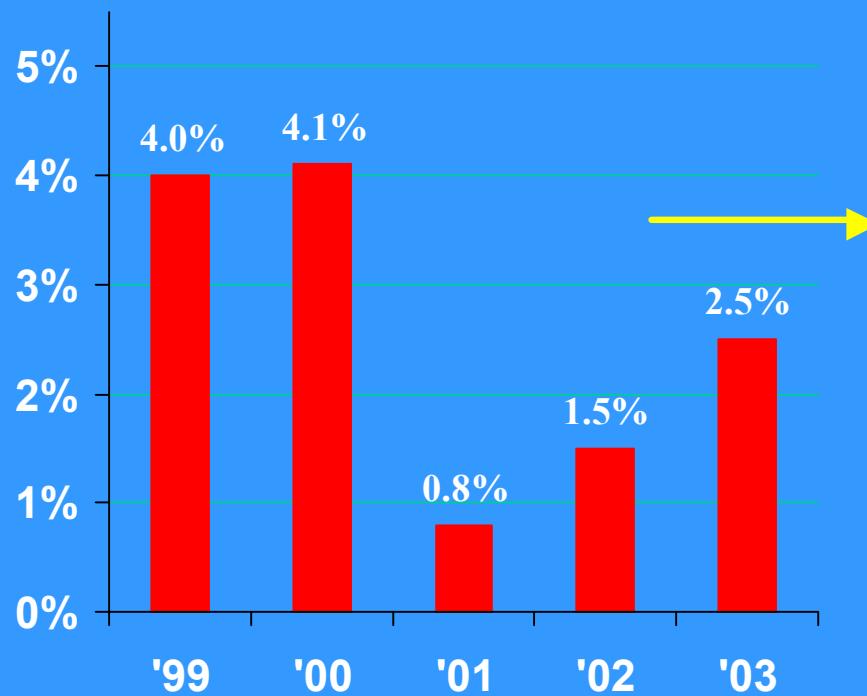
How long will we be dragging
bottom, Mr. Greenspan?



Source: APA, Craig Adair

Growth Will Return

U.S. GDP

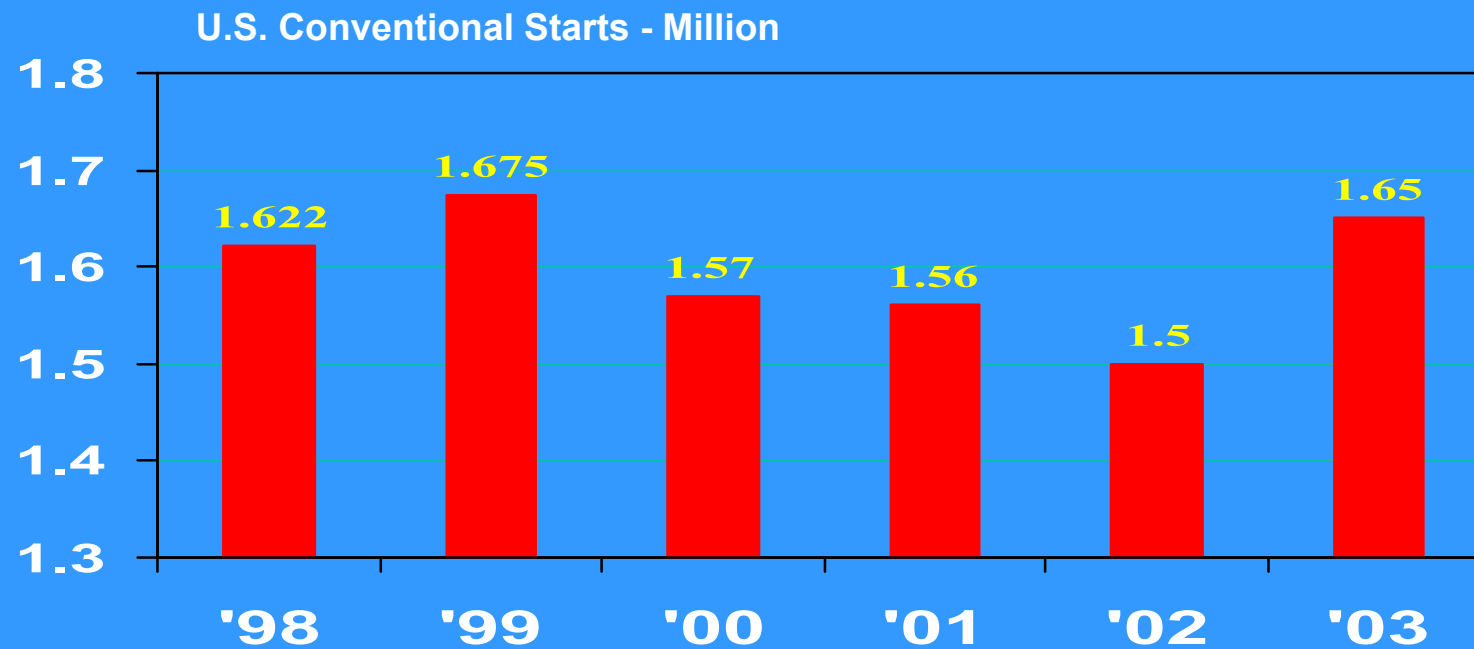


- **Outlook assumptions:**
- **Terrorist attacks “one time event”**
- **Lower mortgages = more refinancing.**
- **Manufacturing revives by 2nd half '02 with inventories back in balance.**
- **Europe’s rate cuts begin to take effect in '02.**
- **U.S./Canada experience short recession 2nd half '01**
- **The economy RETURNS TO A sustainable target growth of 3% by '03**

Source: Consensus (NAHB, NAHB, NAR, Conference Board, RISI)

Residential Market

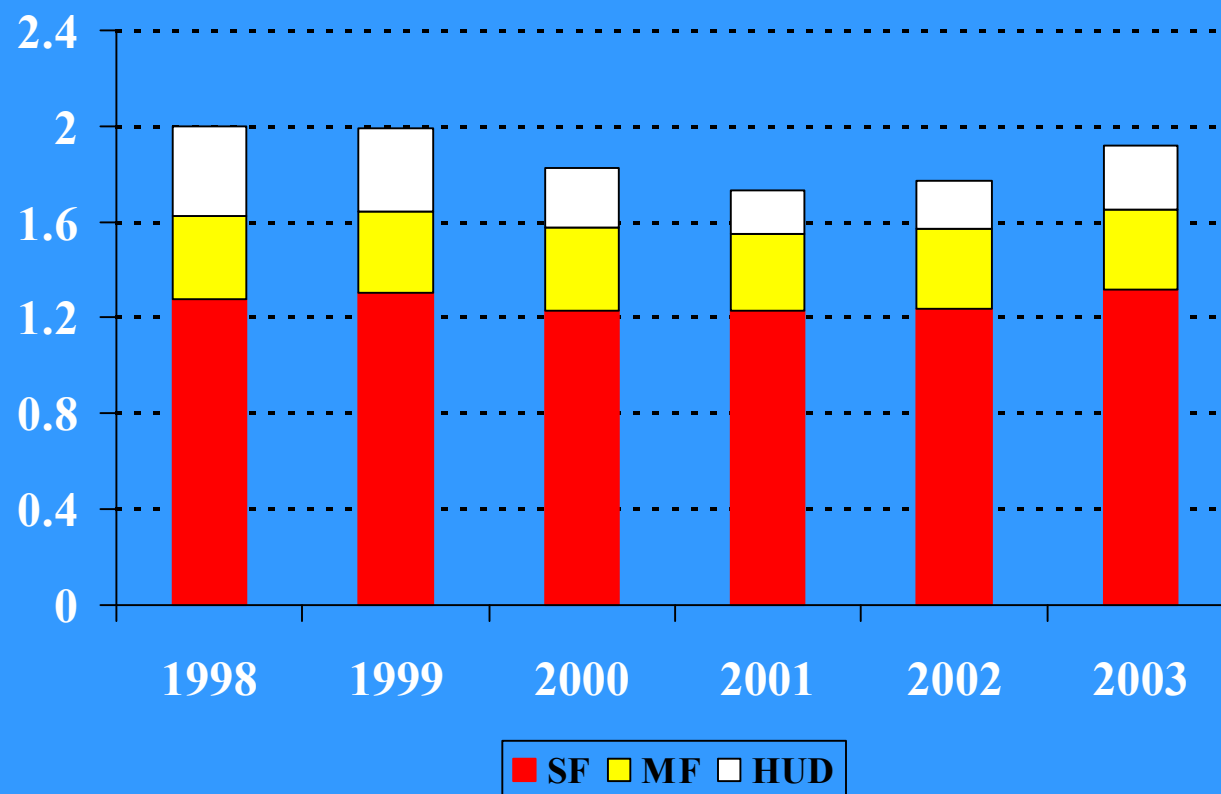
New demographic data shows more rapid population growth and the effect of immigration on household formations. Starts forecasts have been revised upward. 1.6 million is a sustainable level.



Source: Forecasts - NAHB

Residential Market

Strong Demographics Drive Total Demand toward 2 Million by 2003

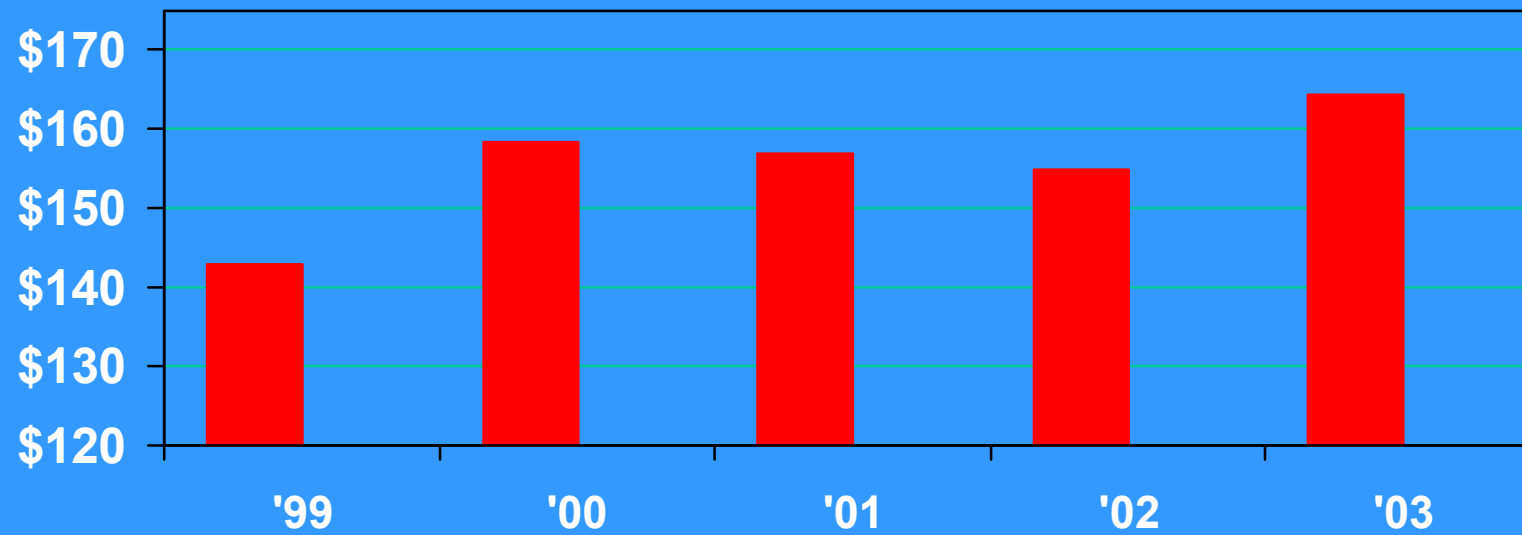


Remodeling Market

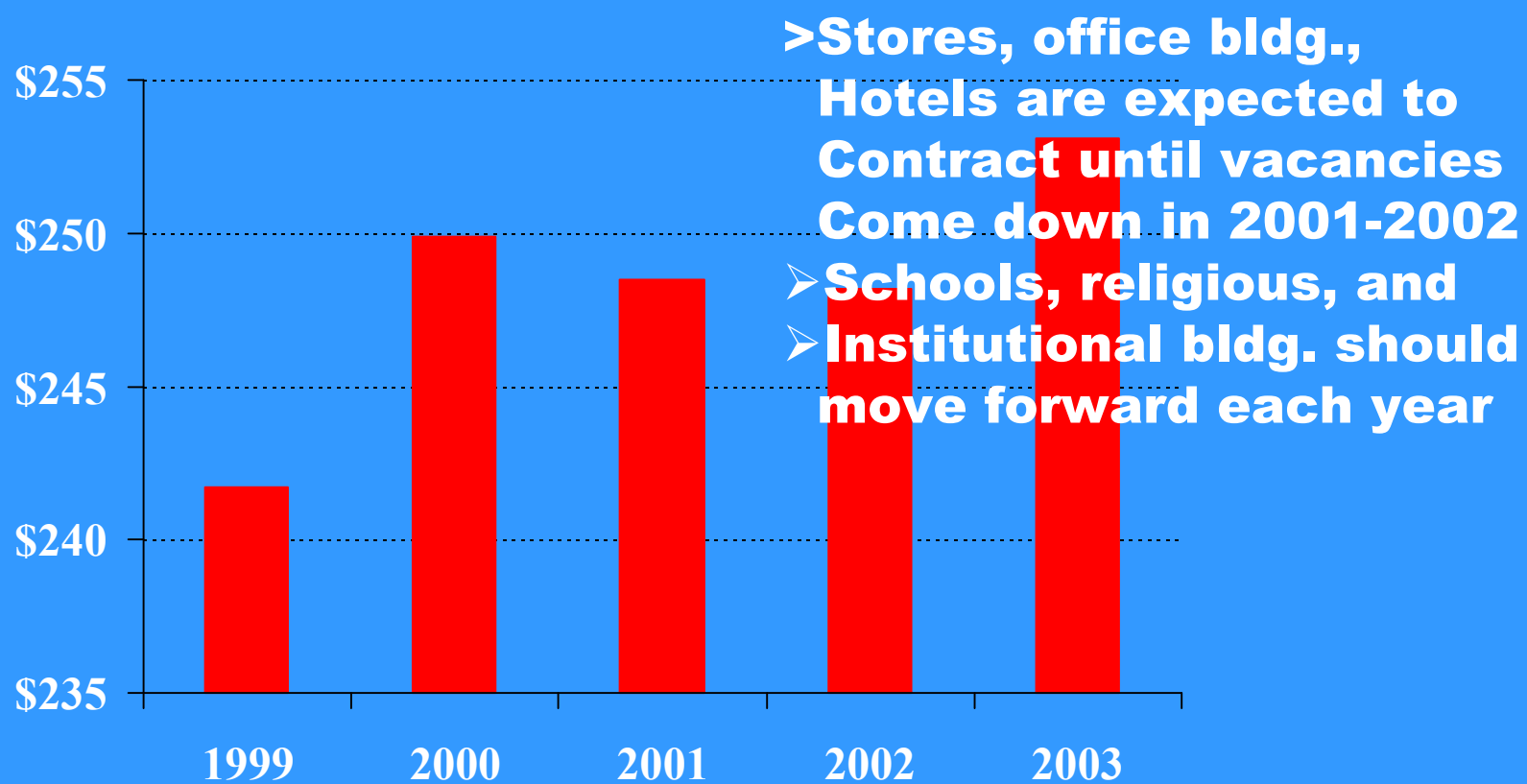
Remodeling expenditures could contract in 2001- 2002 before resuming growth. Wood products will benefit from the high turnover of existing homes which need remodeling.

Strong demographics will support Remodeling demand during next decade

U.S. Expenditures - Billion \$99



Non Residential Construction

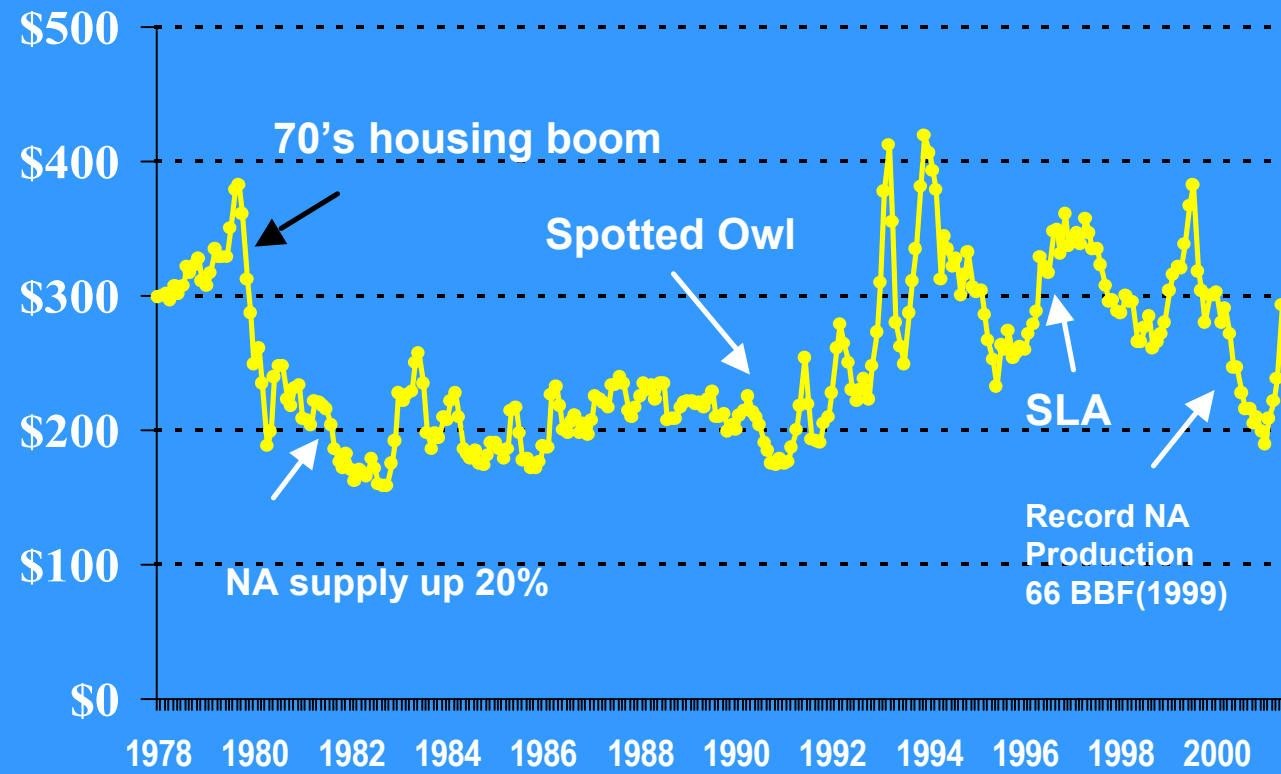


Source: forecast APA

NA Lumber Markets

Following a decade of adjustments, lumber prices appear to have reached a new equilibrium??

Framing Lumber Composite Price(1982 US\$/MBF)

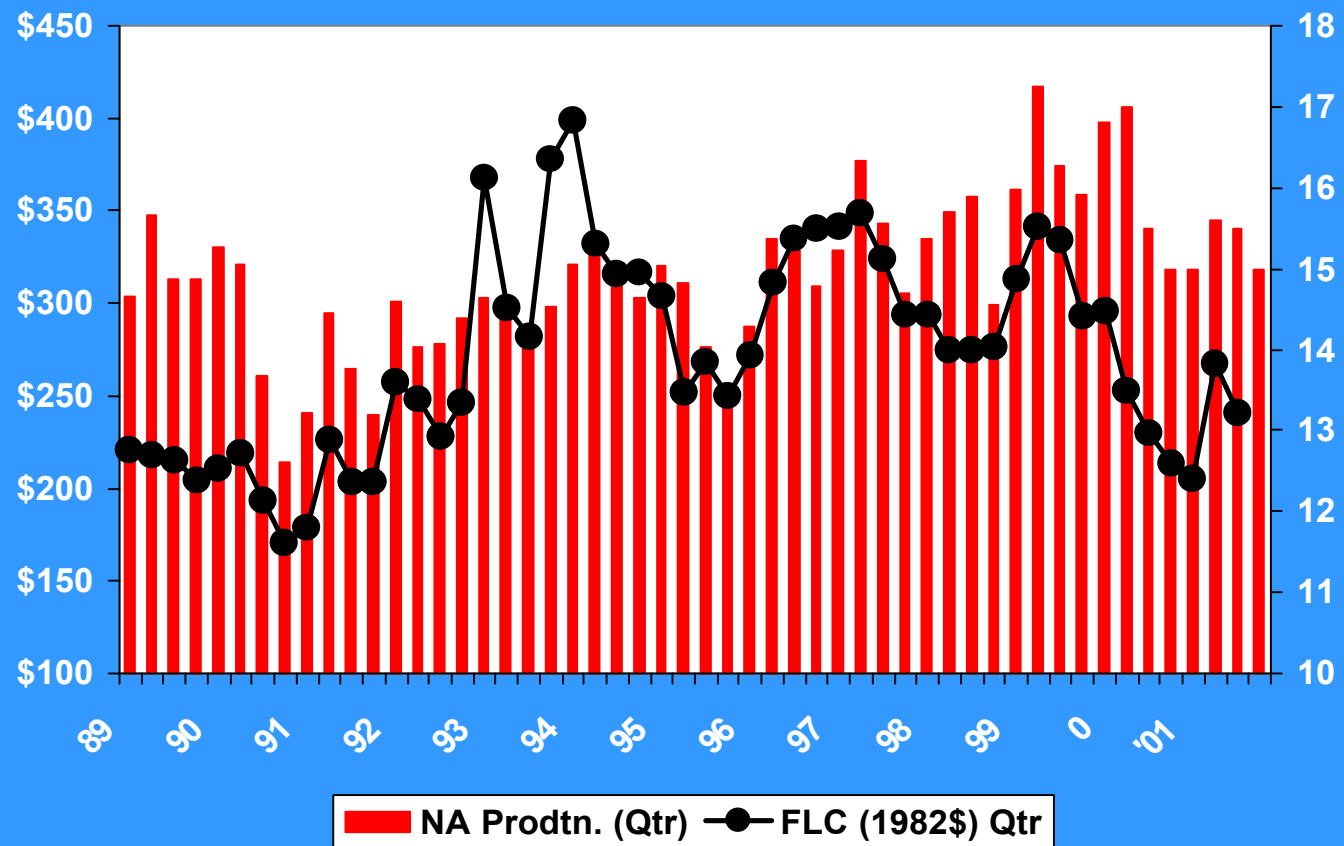


Source: Random Lengths

Volatile North American Lumber Markets

Framing Lumber Composite (FLC) (1982\$/Qtr.)

NA Production BBF/Qtr



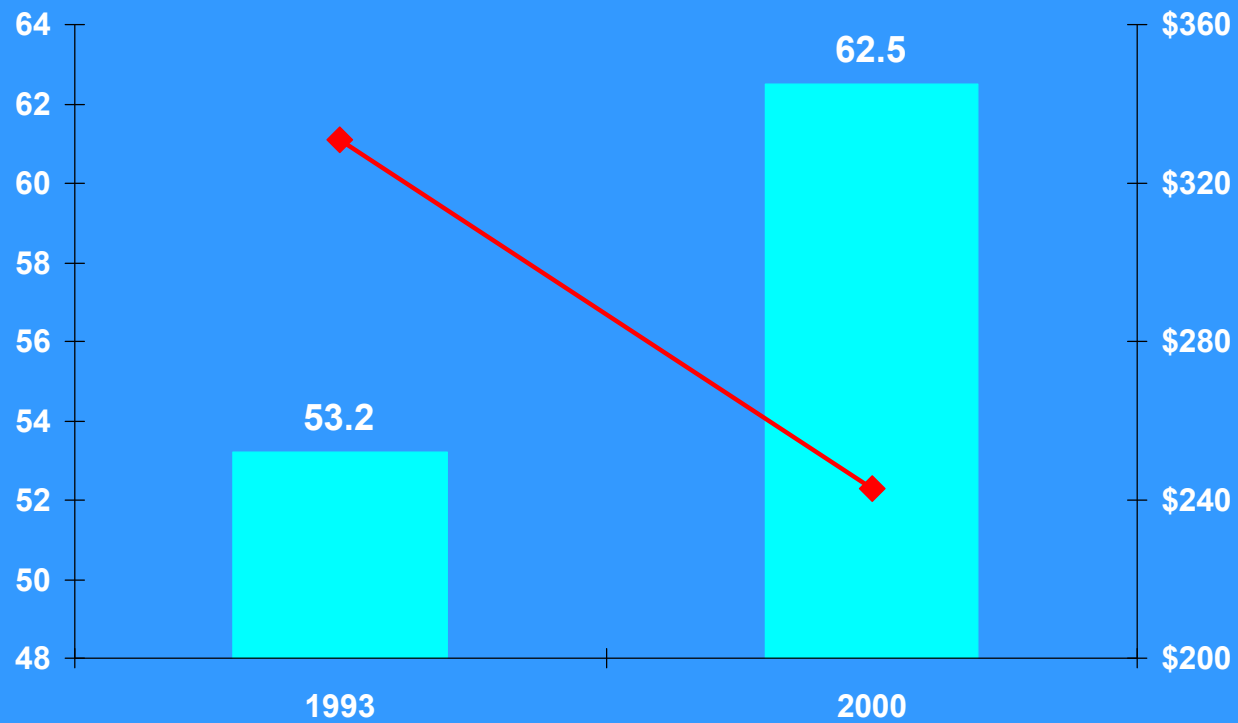
Too Much Lumber?

Between 1993 - 2000, North American Demand Increased 9.3 BBF(17%)
But Real Prices Fell 27%

Why? Supply Increased 20% more than demand

Demand, BBF

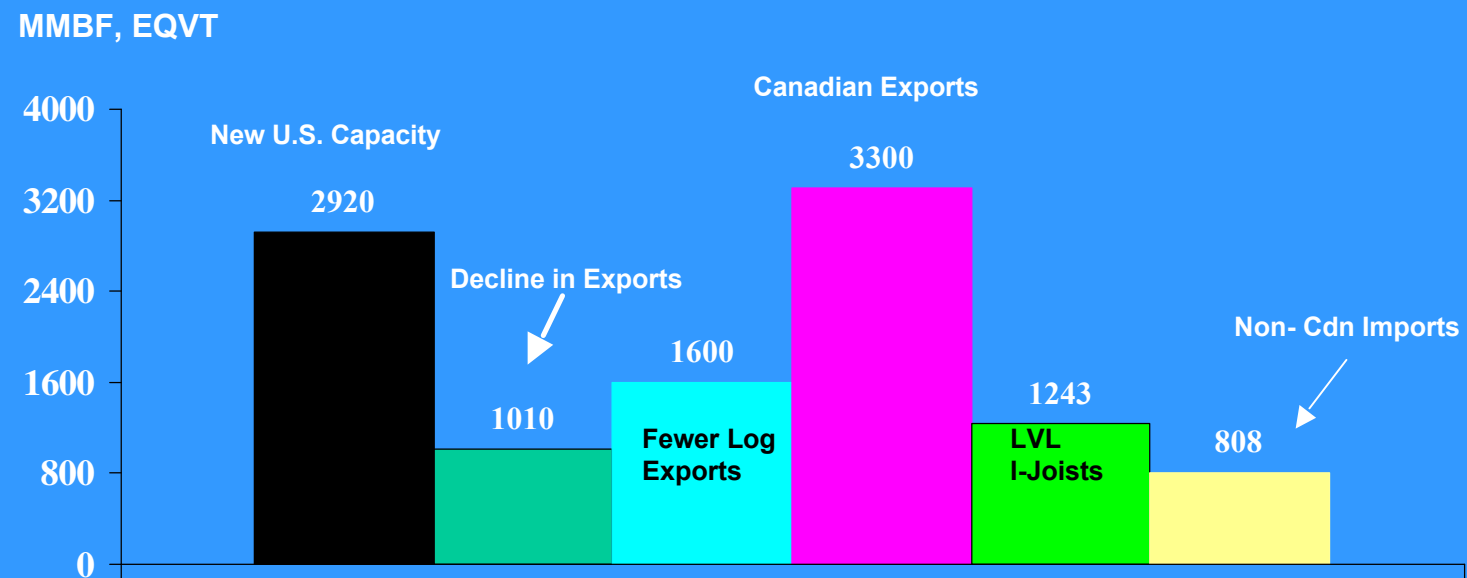
FL Composite Price (\$1982)



■ NA Demand ◆ Framing Lumber Composite (\$1982)

U.S. "Softwood Lumber Supply" Increased 11 BBF Between 1993 - 1999

New capacity, EWP's, fewer exports & more imports



Source: USFS