Modern
DISTRIBUTION MANAGEMENT®
Intelligence for Wholesale Distribution Professionals

VOL. 38, NO. 20
OCTOBER 25, 2008

Credit Crunch in the Channel

Growing concern over A/R, growth plans and deal-making

Credit has been virtually frozen since unprecedented turmoil hit Wall Street and major banks this month. Here's what it means for distributors, manufacturers and deal-making.

By Lindsay Young

The construction industry has been hit hard by the severe downturn in the housing market and the 160 member companies that make up the AMAROK Drywall Distributor Network are no exception. While a number of distributors are holding their own, others have seen business fall off so much that they have struggled to cover overhead.

Strike two: When builders started to file for bankruptcy and were unable to pay their subcontractors, the distributors' receivables fell off dramatically. Receivables have improved, but the distributors are now facing a third strike: the tightening of credit.

"We've seen distributors who have had their bank credit lines cut and some whose banks have quit lending altogether so they've had to find a new bank," says Jeff Jenkins, senior vice president of AMAROK. "Anyone who is not well-capitalized has to juggle things around to pay the bills on the reduced credit lines they have been given, and getting a credit line raised or finding a new bank is a daunting process today."

Rising Concern

What former Fed Chairman Alan Greenspan termed a "once-in-a-century credit tsunami" has distributors and manufacturers in every sector concerned with how turmoil in the financial markets could affect them.

In preliminary results of a recent MDM survey, about 77 percent of respondents said they are concerned with current credit markets "as it pertains to their day-to-day operations and growth plans."

"Lending standards are going to tighten," says Chris Coetzee, managing director at Robert W. Baird & Co. and head of the firm's Financial Sponsor Group. "Companies will find that scrutiny from banks will be higher, and that there will be an incredible focus by bankers on the end markets that these companies sell into."

Burt Schraga, CEO of Bell Electrical Supply, Santa Clara, CA, has seen this firsthand. He recently renegotiated his credit line at a local bank.

"We have a very close relationship with our bank," he says. "Our loan was renewed but they were very candid in saying that they were under a lot of scrutiny and not doing a lot of new loans. They also said they were being careful with loan renewals." He says that the company didn't see this in the early part of this decade when the industrial recession took hold. "Normally a loan renewal takes a week for due diligence," he says. "This time it took three or four weeks."

Many distributors and manufacturers are concerned tightened credit will hamper their ability to move into new markets or make acquisitions. But in many markets, "the operating environment has been good to strong in the last quarter," says Tom Lange, managing director and head of Baird's Distribution Group.

"The challenge in the coming year will be to maintain profitability in a declining business environment. CFOs have to evaluate debt covenants against various scenarios that could develop over the next 12 months. The focus should be to make sure liquidity remains available in an environment like this or in an economic downturn."

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INSIDE

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PERSPECTIVE ■ *Commentary by Thomas P. Gale*

Beware the Sound Bites

Alan Greenspan has gone from irrational exuberance in his description of the stock market boom of the 1990s to a "once-in-a-century" credit tsunami in 2008. The subject lines of my Wall Street Journal news alerts daily look increasingly like tabloid magazine headlines – "Dow Plunges!" But as we are seeing, wait a day and the news is reversed.

Sometimes a wake-up call is healthy; panic never is. Anyone who experienced the media's lack of understanding and coverage of the last recession at the beginning of this decade have a large and healthy degree of skepticism about what we see on TV and read in newspapers about the current crisis. But the reality gap is at its greatest right now. Fear and speculation are driving sound bites about how bad it might get.

As the lead article in this issue outlines, financial and credit market bubbles burst, and every distribution sector is starting to feel the impacts. This is an unprecedented situation. At the same time, our surveys and conversations with distributors and manufacturers offer some insight on how executives are responding to this challenge. And there are some sectors staying strong while others are flattening, not falling off a cliff. Here are a few common threads we are hearing and a few takeaways that may be useful.

This next year will push lean efforts – whether formal or not – to much deeper levels. It will push distributors and manufacturers to find ways to get even more efficient in how they conduct business in every way – demand visibility, marketing, inventory, logistics and financial.

The next 12-24 months will be about positioning, protecting and building market share. As the announcement (see the Industrial & Construction Markets Update in this issue) of Stock Building Supply's closure of 86 branches illustrates, there will be some major market shifts taking place. Some large distributors are shedding unprofitable branches; others are waiting for bargains as some smaller distributors run out of cash and deal with much more limited financing options.

Every business expects a tough year in 2009. What will separate successful from struggling for distributors will be close and careful management of assets – cash, inventory and accounts receivables. I'd also add human resources to the critical watch list. No business in this climate, regardless of size, can operate with less than peak efficiency and productivity from its team. Where sales traditionally could cover up flaws in service and performance, there won't be room for "adequate" when it comes to how customers view your company, and in turn how you set the bar for performance internally. ■

MODERN DISTRIBUTION MANAGEMENT

Founded in 1967 by J. Van Ness Philip

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Published twice monthly; $345/yr., $365 U.S. funds other countries; $169 each additional subscription to a company ($189 other countries). For group subscription rates and site licenses, please contact Tom Gale at 303-443-5060.

ISSN 0544-6538

Credit Crunch

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Customers

The largest concern in the MDM survey seemed to lie with the credit health of customers.

Schraga says that he has already started to see customers pay more slowly. A portion of Schraga's business is commercial contractors. "It's not because they are bad guys, but because they are having a difficult time collecting money," he says. Many of his customers are seeing contracts for work canceled or delayed for six months.

Other distributors are seeing the same thing. Those serving the commercial construction markets are starting to see a slowdown as projects are put on hold because of difficulty in financing. One manufacturer in the survey worries that its customers might extend their normal payment terms – in essence using the supplier as a "bank."

As long as distributors pay manufacturers within their traditional terms, a tightening credit market should not affect day-to-day business, says Dave Thompson, former president of Kennedy Manufacturing Company, a manufacturer of industrial tool storage products and medical carts based in Van Wert, OH.

The challenge comes when a distributor does not get paid and that filters through the entire channel.

Manufacturers and distributors with a good relationship can be open about the challenges facing them, he says.

"It's a catch-22," Thompson says. "If a distributor's entire book of business is starting to slow down, a manufacturer with a relationship will try to work with that distributor, but they can't continue on as if there has been no change in the relationship. They are getting squeezed at the other end as well."

But just as manufacturers will be looking more closely at distributor paying patterns, distributors should examine their own customers' paying patterns.

Trust is important, Thompson says. "It can disrupt the flow in the industry when trading partners don't trust each other to get paid. It goes both ways," he says. "If you order from me you pay me. And I'm not ordering from you unless I expect to pay you."

Impact on Deal-Making

A top driver of mergers and acquisitions activity is the availability of credit. Over the past three months, "it's pretty amazing how much credit has tightened," Coetzee says.

"The last couple of weeks it's been a week-by-week evaluation of what can and cannot get done."

As a result, new deals have been put on hold until the credit markets thaw. One potential deal put on ice: Stock Building Supply apparently received a lot of interest when the UK-based Wolseley plc was looking at options for the struggling U.S. building materials unit. But the distributor said that in the end, a sale was not possible.

The credit crunch has a different flavor than fall 2007 when the markets began tightening. Up until a few months ago, it was more difficult to get funding for large deals than for mid-market or small deals.

But in the past three months that distinction has grown irrelevant. "No one is really immune," Coetzee says. The deals mostly like to secure financing right now are $50 million and below, he says.

In an environment where new buyout financing is not available, strategic buyers with access to capital and conservative leverage have an advantage.

Lange says that if a distributor has a growth strategy that includes M&A, and also has access to capital and experience with successful acquisitions, the current environment is a good one to make acquisitions.

"This could be a very good time to take market share and strengthen business long-term ahead of the next recovery," he says, adding that the environment is not ideal for a distributor's first acquisition.

It's hard to say when the credit markets may open up again, Coetzee says, but the market for buyout financing is likely shut down through the end of this year.

"You can only look at this short-term," he says. "We've never been through the events that have taken place. It's almost a week-by-week wait-and-see. Longer term, I have no crystal ball on how long this will take."

■ *State of the Distribution Software Industry, Part 3*

The Growing Role of the Internet

Industry experts: Build the Web into your overall business strategy

This is part of a series looking at the distribution software industry. This article examines the role the Internet is playing in driving change in the way distributors do business.

By Jenel Stelton-Holtmeier and Lindsay Young

In the last decade, the Internet has been one of the key drivers of technology development.

"The Internet is the backbone today for anybody that's in distribution, anybody in the supply chain and supply chain execution," Rod Winger, Epicor's director of product marketing. "You could not do what we do today without the Internet."

e-Commerce

The emphasis on having information available anytime from anywhere has been a driving force behind many companies' moving into the realm of e-commerce, doing business with suppliers and customers online.

"Doing business over the Web as part of a multichannel strategy is absolutely critical," says Mike Briglia, vice president for wholesale distribution/consumer packaged goods at IBM Corp. "Customers will be at the point if they're not there already where they will demand it and consider it a minimum requirement to do business with them, especially for routine inquiries such as product catalogs, order status and pricing."

Chief Technology Officer Ross Elliott of supply chain execution software provider Accellos agrees. "For society in general, the Internet has created a 'now' mentality," he says. "I want what I want – and I want it now. And if you don't have it, somebody else's Web site will."

Activant has seen an increased interest in its e-commerce platform offerings, says Vice President and General Manager Russ Mellott. For smaller distributors, e-commerce is more about providing an order platform for their customers. On the mid-sized and larger end of the spectrum, distributors see e-commerce as a customer service and CRM tool in addition to an ordering platform, Mellott says.

Creating an effective e-commerce site can be a challenge, especially on the smaller end of the market. "Every article I see says you've got to have an e-commerce site that's easy and customer friendly," says Charles Gray, owner of Machinery & Factory Industrial Supply, a $15 million distributor in Racine, WI. "We just haven't found one that's affordable for a company our size."

And having an e-commerce site does not automatically equal success. H&C Tool Supply and Hewes Fastener Division, a distributor in Rochester, NY, introduced online order placement around 2000. "It may have been ahead of its time or maybe we didn't sell it appropriately, but we found that it didn't catch on with our customer base," President Don Waltzer says.

For many distributors, the problem is that many products require a level of expertise and service that cannot be provided on a Web site, according to Steve Epner, founder of BSW Consulting Group, which advises distributors in technology decisions.

Waltzer agrees. "Primarily, we sell expertise having to do with a product. That's being delivered through a face-to-face meeting with a salesperson," he says. "E-commerce tends to be an alternative that delegates a lot of the effort onto the customer."

Companies considering e-commerce generally want to improve efficiencies and decrease customer representative time, said Gary Rippen, Infor's director of distribution industry marketing. "But I have yet to hear a distributor say that's going to replace their sales reps."

The Web can be successful with products that are considered commodities – products that differ little from supplier to supplier. And even with highly engineered products, e-commerce can play a vital role in replenishment and future fulfillment. Once they have identified a product that fits their needs, customers can go online and reorder.

"There is a new generation of users that are significantly more comfortable doing it that way," Epner says. The key is finding the proper balance between face-to-face service and online convenience.

E-commerce may also allow distributors to become direct-to-consumer sellers for certain items, says Scott Pugmire, senior vertical industry manager for Sage Software. Small ticket items or overstocks could be sold on the Internet either through a distributor's own site or through eBay stores or Amazon.

Other Roles

Though the focus of e-commerce is often placed on catalog accessibility and electronic ordering, the range of options with e-commerce is immense. Anytime a transaction involves the Web – from email quotes to selection of delivery options – that is considered e-commerce.

In fact, some specialized functions within e-commerce may be more readily available to smaller distributors that aren't ready or able to move to a fully functional and automated e-commerce site. BillTrust works with distributors and their customers to transition to electronic billing. "Not only is e-billing more green, but it can also save the distributor lots of money. A typical distributor can save 75 percent on sending a bill electronically versus sending it by paper," says Mitchell Rose, vice president of marketing.

By using BillTrust's electronic invoice presentment and payment (EIPP) system, contractors can view bills and payment history, or make payments. And distributors can decide which payments to make available to their customers. With credit card fees eating into profit margins, that option is important, Rose says.

Web portals can also allow better management of inventory, particularly for vendors who utilize delivery fleets, says Chris Jones, Descartes' executive vice president for solutions and services. "Mobile technology allows the warehouse to be able to track what's on each truck and better determine amounts when restocking," Jones said. "And, that's all possible because of the Internet."

Facilitating Globalization

In many ways, the Internet has helped make the farthest reaches of the earth accessible to businesses both large and small. The Web has transformed business into an anywhere-at-anytime institution. "Our customers want to be able to sell anywhere in the world. They want to be able to source from anywhere in the world," says Zach Nelson, president of NetSuite, a Software-as-a-Service ERP provider. "That's the promise of the Web."

But while technological advances may provide new opportunities in a global economy, doing business in a multinational environment creates its own set of challenges that software companies must understand to help their clients compete. Those in the industry say that software packages should include ways to translate information between different languages, be capable of multiple currency transactions and be adaptable to local regulations and customs to allow businesses to do business.

Sometimes the most effective way to meet those challenges is by utilizing niche software to adapt existing business operations to new needs. As part of its logistics offerings, Descartes can manage cross-border customs filings, something Descartes' Jones says is an aspect of multinational business that some companies may not think about enough.

Many bigger players are adapting their full-package ERP offerings to assist with the transition to international business operations. "One of the major reasons we acquired iScala (in 2004) was to roll out the global infrastructure it had into our other product lines," Epicor's Winger says. For example, the iScala platform includes capabilities for more than 40 languages.

SAP, which focuses more on organic growth, took many of its cues from businesses in Europe for how to adapt their offerings. "In the U.S., you don't really have to worry about the laws in Illinois being significantly different than the laws in Indiana. But in Europe, you do have to worry about the laws in Germany versus the laws in France," says Karen Lynch, SAP's vice president of global wholesale distribution.

As such, adoption rates of new technology and willingness to look to the Web for conducting business is higher in Europe than in North America. But, that will have to change if North American companies want to succeed in the global marketplace, Nelson says.

NetSuite recently rolled out its OneWorld product. "Functionality like OneWorld's going to be very important to distributors to be able to manage their subsidiaries as distinct units, but then, to consolidate the finances and the sales across those subsidiaries," Nelson says. The product is designed to manage, from one Web-based account, companies with multiple subsidiaries, business units and legal entities. Local users see the application in their own language and can make and track transactions in the local currency. "It's really made for the Internet age," Nelson says.

Improved Communication

Before the Web, doing business electronically was cumbersome. Manual data entry happened at many levels, and internal order approval could take days. The introduction of Electronic Data Interchange as an intermediary helped facilitate some of this.

"The old technology underlying EDI is so obsolete, it's laughable," says Tim Reynolds, president of Tribute Inc., a niche software provider to fluid power and hose distributors. He forecasts better efficiency will be developed in the near future. "I think overall data communication between supplier, distributor and customer is likely to be much more in real time."

With the introduction of e-mail, communication in the supply chain has already improved. In the past five years, e-mail has rapidly become the standard way of exchanging information that before had to be called in, faxed or hand-delivered.

"I've asked distributors at different demonstrations how many sent orders, received confirmations or received sales inquiries over e-mail five years ago," says Matt Hartman, president and CEO of MRH Technologies. "The answer then was about 5 percent to 10 percent. Today, it's a very high percentage."

An intermediary is no longer necessary for many companies. In the future, people may still refer to EDI, but what they will be describing is something completely different than what it has been, Reynolds says. Additionally, mobile technologies – such as smart phones and wireless Internet – are facilitating data transfer in real-time. "Tracking, mobile, wireless – we're seeing all those pieces come together in a single integrated solution," says Jones, of Descartes. "And what's driving it is the cost of mobile technology and data plans are coming down dramatically."

There are a variety of options that companies can consider – and likely will consider – for how to improve data exchanges, Reynolds says. "But, we all now are on a technical foundation to allow us to meet those needs over the next five years."

Internet and Growth

Many distributors are rethinking their e-commerce strategies, according to IBM's Briglia. "They all have their eyes on a bigger prize, once the basics are done well," he says. "They will be pretty aggressive evolving these strategies toward higher level services and more collaborative commerce both with their customers and their manufacturer suppliers."

This is where business intelligence initiatives can play a role, he says. Distributors can leverage order information to drive real-time promotions online. "It's a huge opportunity for wholesale distributors to create some real value in this space, as well as to redefine their value proposition with customers and manufacturers."

Distributors face the constant challenge of using technology smartly in their growth plans. "For technology providers, the rate of change is so high and so fast. The challenge is how do we continue to progress at that rate of change while at the same time taking care of your current customers?" says Richard Sides, senior vice president for Ramco Systems Corp. ERP OnDemand North America. As a Software as a Service product, Ramco's OnDemandERP enables companies to progress through the technology curve without having to manage it.

The Internet should become a key part of a distributor's strategy. Says Elliott: "What distribution companies have to do is to make the Internet a key component of their overall value proposition rather than a separate channel." There's no denying the Web will continue to play an even bigger role in how distributors do business, especially as younger people who are used to doing business electronically move into management.

"The winners 10 years from now are going to be guys who put the Web at the center of their business," Nelson says.

Pricing Software Grows in Distribution

Distributors consider better ways to maximize margins through technology

This article looks at the growing market for pricing software in distribution.

By Lindsay Young

For many distributors, managing inventory through software was a significant shift in how they viewed the strategic use of technology. Next up: Pricing.

Thanks to economic uncertainty and volatile costs, pricing is top of mind for many distributors right now as a strategy to preserve and expand gross margin.

"The way I think of it is this: In the old days, distributors learned how to manage their inventory using computer systems," says Tim Reynolds, president of Tribute Inc., a software provider to fluid power and hose distributors that also provides a pricing function. "If you have 20,000 SKUs, you can't do it in somebody's brain. You have to have a system. Now inventory management is really quite sophisticated, even in very small companies."

He says the same can happen with pricing. "To really do the market analysis and get the pricing correct for each item and customer – that's what strategic pricing is about."

Market Reach

Very few distributors have jumped feet first into software designed exclusively for pricing analysis. The cost and time required to set up complex enterprise pricing solutions is still prohibitive for many smaller and mid-sized distributors.

Instead, smaller and mid-sized distributors are starting small, using simpler, less comprehensive pricing software or add-ons to their current systems that analyze pricing on a surface level. Some distributors have built pricing systems in-house within their legacy systems.

"What we are seeing is increased competitive intensity as the economy tightens," says Brandt Hurd, director of sales engineering at Zilliant, an enterprise pricing software provider. "These guys want to grow their revenue and preserve bottom-line profitability."

Creating a standard off-the-shelf package is difficult in pricing, says Jon Ladle, president of on-demand pricing software provider Advanous, due to differences across distribution verticals. "But we are not a long time away from figuring that out."

"Some of the advanced algorithms and pricing optimization techniques for large distributors will be able to moved into a downstream-type model once distribution as a whole gets its arms around what a typical pricing package looks like," Ladle says.

Hurd says Zilliant is working to develop a more efficient solution that will go downscale. "I think there's still a cutoff today of $200 million or $300 million before the economics make sense," he says.

"But maybe just a year ago, the cutoff was $1 billion."

More and more, distributors with sales of $100 million and up are starting to show interest, Ladle says. "You see large distributors as early adopters, and hopefully it will trickle down from there, but we need to do more education on what is out there and what the software is capable of."

Simplifying the Process

The enterprise pricing software solutions use complex algorithms to help distributors determine the best price for a particular product to a particular customer. "What we do with the software is make sure that we can extend the insight from these algorithms to the front lines," Hurd says.

Systems will typically provide one market-aligned price or a series of prices, depending on the distributor's needs. The sales rep will start at a recommended point and will be told not to go below a floor-level price.

Despite the complexities that go into the calculations, the idea is to simplify the process at the distributor level – instead of providing analysis that a sales rep has to interpret. Sales reps often don't see anything different on their screen than before – except for the numbers. Some training is necessary though so that salespeople understand what is going into the prices they are seeing on their screens.

Future Growth

Hurd is optimistic for growth in the distribution industry. "Pricing is black and white, and the returns and gains in profitability are measurable," he says. "In tough economic times, this sector of the software space is rising above others because people are very pragmatic about where they spend their software dollar."

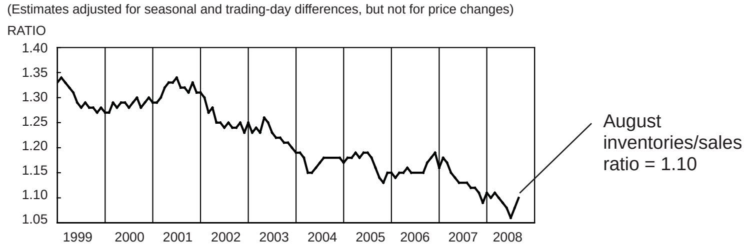
The key for distributors is ensuring they've chosen the right package for their current pricing needs. "Distributor margins are so thin that they have to be very certain when they go sign a contract to spend hundreds of thousands or even millions of dollars. They want to make sure the returns are there," Ladle says.

"Pricing in particular involves a lot of facets, so they have to feel committed to it and comfortable that they can get this implemented. Once they make that decision and make that commitment we believe that can be a game-changing event for them."

Monthly Wholesale Trade: Sales and Inventories for August 2008

August 2008 sales of merchant wholesalers, except manufacturers' sales branches and offices, after adjustment for seasonal variations and trading-day differences but not for price changes, were $404.9 billion, down 1.0 percent from July, but up 13.4 percent from August 2007, the U.S. Census Bureau reported. The July preliminary estimate was revised downward $1.7 billion or 0.4 percent. August sales of durable goods were down 1.5 percent from last month, but were up 5.5 percent from a year ago. Compared to last month, sales of hardware, and plumbing and heating equipment and supplies were down 6.5 percent and sales of lumber and other construction materials were down 5.2 percent. Sales of nondurable goods were down 0.6 percent from last month, but were up 20.7 percent from last year. Sales of petroleum and petroleum products were down 2.1 percent from last month.

Monthly Inventories/Sales Ratios
of Merchant Wholesalers: 1996-2006
(Estimates adjusted for seasonal and trading-day differences, but not for price changes)



Source: U.S. Census Bureau

Inventories. Total inventories of merchant wholesalers were $445.4 billion at the end of August, up 0.8 percent from the revised July level and were up 11.1 percent from a year ago. The July preliminary estimate was revised upward $0.6 billion or 0.1 percent. End-of-month inventories of durable goods were up 1.4 percent from last month and were up 10.0 percent from last August. Inventories of metals and minerals, except petroleum, were up 3.3 percent and inventories of computer and computer peripheral equipment and software were up 2.1 percent. End-of-month inventories of nondurable goods decreased 0.1 percent from July, but were up 13.0 percent compared to last August. Inventories of farm product raw materials were down 2.3 percent from last month, while inventories of grocery and related products were up 2.1 percent.

Inventories/Sales Ratio. The August inventories/sales ratio for merchant wholesalers was 1.10. The August 2007 ratio was 1.12.

Monthly wholesale trade: Sales and inventories August 2008

NAICS Code	Business Type	Sales $ millions	Inventories $ millions	Stock and Sales ratio	% Change in Sales 7/08-8/08	% Change in Sales 8/07-8/08	% Change Inventory 7/08-8/08	% Change Inventory 8/07-8/08
42	U.S. Total	404,862	445,394	1.10	-1.0	13.4	0.8	11.1
423	Durable	180,415	275,146	1.53	-1.5	5.5	1.4	9.9
4231	Automotive	24,145	42,644	1.77	-2.2	-11.5	1.2	12.6
4232	Furniture & Home Furnishings	5,526	8,115	1.47	-0.3	-1.7	-0.4	0.9
4233	Lumber & Other Construction Materials	9,506	14,959	1.57	-5.2	-8.9	0.4	3.3
4234	Prof. & Commercial Equip. & Supplies	30,712	32,844	1.07	-0.5	3.9	1.4	6.8
42343	Computer Equipment & Software	15,393	11,939	0.78	-0.2	1.8	2.1	9.3
4235	Metals & Minerals	16,172	28,589	1.77	2.2	19.0	3.3	22.1
4236	Electrical Goods	29,295	35,542	1.21	-2.9	9.0	1.9	9.9
4237	Hardware, Plumbing, & Heating Equipment	7,518	15,379	2.05	-6.5	-7.1	0.5	0.1
4238	Machinery, Equipment & Supplies	31,943	70,874	2.22	2.2	11.8	1.0	10.0
4239	Miscellaneous Durable	25,598	26,200	1.02	-4.1	21.5	1.9	11.3
424	Nondurable Goods	224,447	170,248	0.76	-0.6	20.7	-0.1	12.9
4241	Paper & Paper Products	8,483	7,172	0.85	0.7	9.2	-1.1	4.3
4242	Drugs	32,178	32,130	1.00	0.4	4.5	0.0	6.6
4243	Apparel, Piece Goods & Notions	11,436	16,270	1.42	-1.0	4.0	-1.5	-3.6
4244	Groceries &Related Products	45,066	27,728	0.62	0.7	5.8	2.0	7.3
4245	Farm-product Raw Materials	23,027	25,780	1.12	-1.8	37.7	-2.3	27.2
4246	Chemicals &Allied Products	10,098	10,082	1.00	1.8	24.2	-1.1	12.7
4247	Petroleum &Petroleum Products	64,243	17,088	0.27	-2.0	53.3	1.3	38.3
4248	Beer, Wine & Distilled Beverages	9,084	10,770	1.19	-0.9	4.0	0.0	7.4
4249	Miscellaneous Nondurable Goods	20,832	23,228	1.12	-0.3	13.4	0.2	19.8

U.S. Bureau of the Census, Current Business Reports, Monthly Wholesale Trade, Sales and Inventories Series: MDM compilation and analysis. Adjusted for seasonal and trading day differences. Figures for sales and inventories are preliminary adjusted estimates.

Source: Bureau of Labor Statistics

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Industrial & Construction Markets Update

VOL. 38, NO. 20 | OCTOBER 25, 2008

Wolseley to Shutter 86 Stock Building Supply Branches

Wolseley plc, UK-based distributor of plumbing and heating products and building materials, reported it would not sell Stock Building Supply but instead extensively restructure the U.S. building materials distributor.

The company will close 86 branches, bringing the number down to 209. It will be leaving 16 markets in six states, while leaving a presence in 27 states. And Stock will reduce headcount by 3,000. About 8,700 employees will remain. Stock has cut about 55 percent of its work force since 2006, its peak.

The 86 branches to be closed represent about 25 percent of Stock's revenue and 28 percent of its headcount.

The decision comes after a six-month review of the business.

Chip Hornsby, Group Chief Executive of Wolseley, said: "With the ongoing decline in U.S. new residential construction, significant over-capacity in the industry and the consequential negative impact that Stock is having on the Group's results, it is imperative that we take further action to restructure this business.

"The measures we are taking will move us back towards profitability, while still keeping a presence in key districts for when the market recovers."

Wolseley said in a statement that selling Stock to a third party "has not proved possible." In addition to restructuring, it also explored a joint venture with another party and closing the business altogether.

Wolseley said "there remains significant potential to create long-term value in the business."

The restructuring of Stock will focus on maintaining a presence in markets where it is a leading player, according to Wolseley, and where it will benefit most from market recovery.

For example, Stock will remain in its top states, namely North Carolina,

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McJunkin Red Man Corp. has acquired St. Louis, MO-based **LaBarge Pipe & Steel** Company. LaBarge Pipe & Steel distributes carbon steel pipe for use in the North American energy infrastructure market. It four sales offices in St. Louis, MO, Houston, TX, Birmingham, AL and Charlotte, NC and a manufacturing facility in Wagoner, OK.

Avnet, Inc., Phoenix, AZ, has offered to acquire U.K.-based **Abacus Group** PLC, a distributor of electronics components in 10 European countries, for £42.2 million ($73 million) in cash. In addition, Avnet would assume net debt from Abacus of £62.9 million ($108.8 million).

84 Lumber has announced 20 more store closings, according to news reports. The building materials distributors closed nine stores a few weeks ago. The company now has 335 stores, down from 400.

Cummins-Wagner Co., Inc., Annapolis Junction, MD, a distributor of industrial process equipment and HVAC equipment in the Mid-Atlantic region, has acquired Rochester, NY-based **Siewert Equipment** Co. and **Siewert Classic** Co. SECO is a distributor/manufacturers representative in the sales of fluid process equipment and provides assembly, aftermarket service and engineered solutions.

Henry M. Wood Co. and **Ritchie Industrial Marketing** have recently merged. The Cincinnati, OH-based companies sell industrial equipment, including pneumatic fluid power, pneumatic safety products, low-pressure fluid handling, leak test equipment and ergonomic manufacturing solutions. Ritchie will sell under its own name as a division of Wood.

Builders FirstSource, Inc., Dallas, TX, supplier and manufacturer of structural and related building products, has decided to leave the New Jersey market. The company operated a distribution center, a manufacturing facility and three showrooms there.

Moog Inc., East Aurora, NY, has acquired **Berkeley Process Control**, Inc., Richmond, CA, for $14 million. The acquisition expands Moog's product offering. Berkeley Process Control, Inc. holds several patents, among them its Autocalibration technology for improving the productivity and precision of equipment that processes semiconductor wafers.

Gates Corp., Denver, CO., a wholly-owned subsidiary of **Tomkins** plc, will invest in a new power transmission facility in the Izmir Free Trade Zone in Turkey. The new plant will support the growing demand for oil pumps and tensioners in Europe.

Saint-Gobain Performance Plastics, Aurora, OH, has acquired **The Green Glue Company** of West Fargo, ND, a manufacturer of visco-elastic soundproofing technology. Green Glue supplies products to global construction customers.

Zep Inc., Atlanta, GA, announced the launch of its new Zep Professional product line focused on the industrial distribution market, and new agree-

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ments with industrial distributors that serve targeted market segments. Zep has secured new agreements with **W.W. Grainger**, Inc., **Lab Safety Supply** Inc., **Graybar Electric Company**, Inc., **R3 Reliable Redistribution Resource**, a division of **Bunzl** North America, and **VWR International**, LLC.

Genuine Parts Company, Atlanta, GA, reported sales of $2.9 billion for the third quarter ended Sept. 30, 2008, an increase of 3 percent over third quarter 2007. Profit for the quarter was $131 million, an increase of 2 percent. For the first nine months, sales increased 3 percent to $8.5 billion. Profit was $387.6 million, an increase of 2 percent for the same period the prior year.

Anixter International Inc., Glenview, IL, distributor of communication products, electrical and electronic wire & cable, fasteners and other small parts, reported sales in the third quarter ended Sept. 26, 2008, were up 4 percent to $1.59 billion. Profit fell 5 percent to $61.7 million. Organic growth in the third quarter was 2 percent.

WESCO International, Inc., Pittsburgh, PA, distributor of electrical MRO products, construction materials and integrated supply services, reported sales in the third quarter 2008 were $1.62 billion, up 5.3 percent from the prior-year period. Profit was $66 million, down from $72 million.

MSC Industrial Direct Co., Melville, NY, distributor of metalworking and MRO supplies to industrial customers, reported sales in the fiscal year 2008 were $1.778 billion, up 7.5 percent from the prior year. Profit was $196.2 million, up from $173.9 million in fiscal 2007. For the fourth quarter, the distributor reported sales of $448.6 million, up by 5.8 percent from the prior-year period. Profit was $50.5 million compared with profit of $47.4 million in the fourth quarter of fiscal 2007.

Reliance Steel & Aluminum Co., Los Angeles, CA, reported sales of $2.57 billion in the third quarter 2008, an increase of 42 percent from the year-ago period. Profit was $152.5 million, up 63 percent. For the nine months ended Sept. 30, 2008, profit was $416.5 million, up 27 percent, and sales were $6.58 billion, up 18 percent.

HVAC distributor **Watsco** Inc., Coconut Grove, FL, reported sales in the third quarter were $475 million, down 12 percent on a same-store basis. Profit was $23.3 million. Sales in the first nine months were $1.37 billion, down 9 percent on a same-store basis. Profit was $57 million.

The Fastenal Company, Winona, MN, reported sales for the quarter ended Sept. 30, 2008, were $625 million, an increase of 17.1 percent over the third quarter 2007. Profit increased to $72.9 million in the third quarter, an increase of 17.3 percent. Sales for the nine months ended Sept. 30, 2008, were $1.79 billion, an increase of 16.4 percent over the same period in 2007. Profit increased 23.1 percent to $217.1 million.

U.K.-based **Bunzl** plc, the international distribution and outsourcing group, reported sales for the third quarter ended Sept. 27, 2008, increased 15 percent compared to the same period a year ago.

Electronics distributor **Avnet**, Inc., Phoenix, AZ, reported sales of $4.49 billion for first quarter fiscal 2009 ended Sept. 27, 2008, an increase of 9.7 percent over the prior-year period. Organic growth was up 0.9 percent. Profit for first quarter fiscal 2009 was $92.8 million as compared with net income of $105.5 million for the first quarter last year.

Arrow Electronics Inc., Melville, NY, reported sales of $4.3 billion for the third quarter 2008, an increase of 7 percent over the same quarter 2007. Profit was $76.1 million, a decrease of 22.6 percent. For the first nine months, Arrow reported sales of $12.7 billion, an increase of 9.5 percent over the first nine months of 2007. Profit declined 12.1 percent to $258.2 million.

Diversified manufacturer **3M**, St. Paul, MN, reported sales for the third quarter 2008 of $6.6 billion, up 6.2 percent from third quarter 2007. Profit was $991 million, versus $960 million in the prior-year period. For the first nine months of 2008, sales increased 8.2 percent to $19.8 billion. Year-to-date earnings were up 10.6 percent over 2007.

Diversified industrial manufacturer **Eaton** Corp., Cleveland, OH, reported sales of $4.1 billion for the third quarter, an increase of 25 percent over the same period a year ago. Profit

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U.S. MARKET ANALYSIS: Bearings MRO

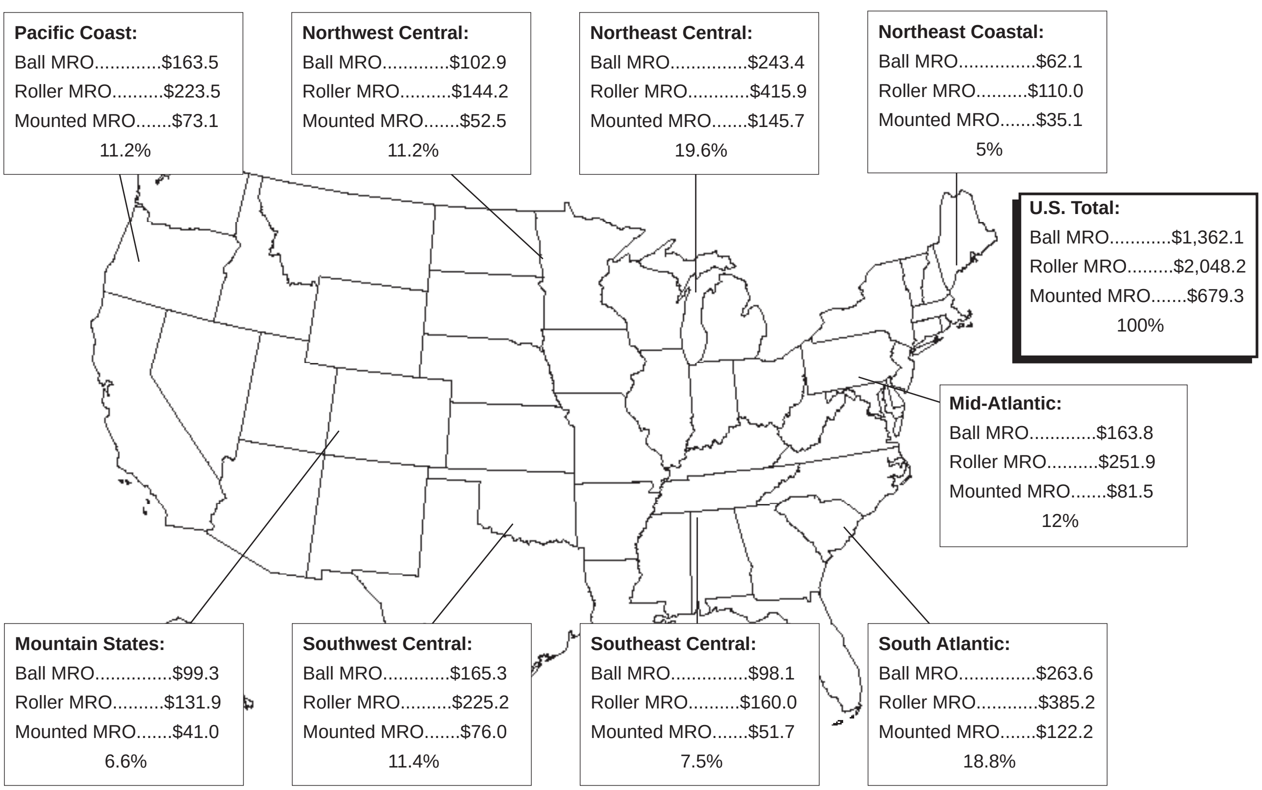
The industrial product group listed here - Bearings MRO - represented a market in 2007 of $4.1 billion, according to estimates by Industrial Market Information, Minneapolis.

These charts show the top ten industries, by SIC code, consuming these products; and the 2007 end-user consumption of these groups sorted by the nine government market regions.

Top ten industries in $ volume, by SIC code consuming Bearings MRO (2007 estimates)

SIC CODE	Bearings Ball MRO	Bearings Roller MRO	Bearings Mounted MRO	Company Count	Total $ (Col. a+b+c)
2621 Paper Mills	43,956,112	253,954,380	74,195,230	2,307	372,105,722
1731 Electrical Work	110,716,710	156,827,751	45,809,771	112,113	313,354,233
1611 Highway & Street Const.	70,954,609	101,465,730	29,654,299	26,674	202,074,638
2631 Paperboard Mills	17,477,439	100,945,115	29,505,792	706	147,928,345
1771 Concrete Work	60,106,781	85,856,344	25,085,640	41,368	171,048,765
7694 Armature Rewinding	64,277,449	40,366,616	5,548,934	2,119	110,192,999
1629 Heavy Construction	36,075,220	51,473,934	15,047,145	17,125	102,596,299
1794 Excavation Work	35,644,145	50,771,075	14,832,149	40,946	101,247,368
1711 Plumbing, Heating, Air Cond.	36,103,989	46,591,047	13,592,449	168,664	96,287,486
1542 Nonresidential Construction	32,464,493	43,861,220	12,780,872	48,852	89,106,586

End-user consumption of Bearings MRO by region, millions of $ (2007 est.)



Source: INDUSTRIAL MARKET INFORMATION, INC. (763) 535-7432. Industrial Market Information has more than 200 industrial product profiles available at the county level. www.imidata.com

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Florida, Texas, California, Utah and South Carolina, but will exit Louisiana, where it does not have a significant presence.

The move is expected to reduce the annualized run rate of losses by about $100 million and result in losses of less than $200 million for Stock in the year ended July 31, 2009.

These numbers were based on average annual housing starts of 750,000 and lumber prices of $240 per thousand board feed.

Exceptional restructuring costs of around $225 million are expected to be incurred before Jan. 31, 2009. This cash impact is expected to be more than offset by cost savings and working capital reductions, in the six months ended Jan. 31, 2009.

In addition, there is likely to be a further impairment of more than $100 million in the carrying value of Stock's goodwill and acquired intangible assets.

Stock generates more than 70 percent of its revenues from new residential construction. Despite cutting headcount by around 40 percent and closing 70 branches since the market peak in January 2006, Stock reported a trading loss of $246 million in the year ended July 31, 2008, on revenues of $3,471 million.

The group announced in September it would conduct a fundamental review of the business.

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was $315 million compared to $258 million in 2007, an increase of 22 percent.

Danaher Corp., Washington, DC, reported profit from continuing operations for the quarter ended Sept. 26, 2008, were $372 million, an 11 percent increase from 2007. Sales from continuing operations were up 17.5 percent. Profit from continuing operations for the first nine months were $1.01 billion, an increase of 13 percent. Sales from continuing operations for the first nine months were up 20.5 percent.

Parker Hannifin, Cleveland, OH, reported fiscal 2009 first-quarter sales of $3.1 billion, an increase of 10 percent from the same period a year ago. Profit was up 9 percent to $250.2 million. Organic sales growth was 4 percent.

Kennametal Inc., Latrobe, PA, reported sales increased in the first quarter by 9 percent to $669 million. Organic sales growth was 3 percent. Profit was $35 million, flat from last year.

Sweden-based **Alfa Laval** AB, a manufacturer in heat transfer, centrifugal separation and fluid handling, reported sales of SEK 6.6 billion (US$843 million) for the third quarter ended Sept. 30, 2008, an increase of 4 percent over the same period 2007, excluding the impact of exchange rate variation. Profit increased 9 percent to SEK 1 billion (US$128 million).

Precision Castparts Corp., Portland, OR, reported sales in the second quarter fiscal 2009 were $1.82 billion from continuing operations, up 5.9 percent from a year ago. Profit from continuing operations was up 13.6 percent.

Canadian manufacturers sales in August decreased 3.7 percent to $52.0 billion, erasing most of the gains from the previous two months. The largest contributor to the decrease was the petroleum and coal products industry, where sales have fallen by nearly one billion dollars in two months. Constant dollar sales fell 3.7 percent in August to $46.3 billion.

The **Producer Price Index for Finished Goods** decreased 0.4 percent in September, seasonally adjusted, the Bureau of Labor Statistics of the Department of Labor reported. This decline followed a 0.9-percent drop in August and a 1.2-percent increase in July.

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ISSN 0544-6538

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