THE PARLIMENT PAGES

April, 2008

HOW CAN THIS BE HAPPENING?

Over the past couple of months, you have seen a gradual run-up in pricing on rebar. We have heard countless complaints and have had blame placed on everything from the greedy steel companies, to government conspiracy, to sunspots. Well get ready, you ain't seen nothing yet. *Because right around the corner is yet another increase and this one is a whopper*.

Within the next few weeks you are going to see somewhere between a 25% to 30% increase in rebar, a greater increase in mesh, and further increases in everything that contains steel. This is a period of steel price increases that rivals what we saw in 2004. However, while the price increases are the same scale as 2004, the reasons behind it are totally different.

Most of you will recall that 2004 was a record-breaking year. Houses were being built as fast as nails could be driven. Demand for all products greatly exceeded supply. The results – a demand driven price increase.

Look around today. Subdivisions have been planned and not started. House after house is vacant and on the market. Contractor unemployment is at record levels. Clearly this product price increase cannot possibly be a demand driven event. It must be either price gouging by the steel mills or a government conspiracy. Not really, read on.

We have all been hearing that we now live in a global economy. For most of us, this was an abstract thought that really didn't matter to us. However, it does matter and it matters in a big way, because *these upcoming price increases are the results of several different global events*. Let's discuss each.

Even though construction is slow in the USA, it is booming elsewhere. Not only in China, which is an old story, but other parts of the world are also consuming vast quantities of construction materials. Fueled by oil price increases, the Middle East is constructing commercial and residential projects at a break neck pace. Right now, 47% of the world's tower cranes are at work in the Middle East. China continues its buildup towards the Olympics. Malaysia and Singapore are expanding at a breathtaking pace. And so on and so on. *The fact is that worldwide demand for construction materials is high.*

With the Fed's panic-driven rate decreases, *the already weak dollar, has come under extreme pressure and has continued to fall precipitously against all major currencies*. That means that imported steel has skyrocketed in price because a dollar just doesn't buy as much. Additionally, the weak dollar has caused the price disparity between foreign steel and domestic produced steel to be higher than it has ever been. This results in a one-two knockout punch. First, *quantities of imported steel that used to come here are off the domestic market and second, domestic producers are, for the first time, seeing opportunities to export steel, which results in taking huge quantities of their product also out of the domestic market.*

And if that is not enough, it is necessary to understand *that the production of steel products is an incredibly energy consumptive process.* Heating and fabrication are energy consumptive. And these high-consumptive operations are happening at a time when oil is selling at over $100 per barrel.

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And finally, raw material cost, primarily *scrap steel has continued its upward climb due in part to the tremendous demand.*

So, we are faced with:

1. Worldwide demand
2. Weak dollar
3. Lack of import
4. Threat of export
5. High production costs
6. High raw material costs

You will see in the next few months substantial price increases that will be evident in all steel based products from rebar to mesh to fasteners to Simpson products.

We have reviewed these upcoming price increases with our sales staff. Please listen carefully to their information because wise purchasing can lead you to some substantial profit opportunities.

MY ANNUAL WINTER COLD –

A couple of months ago, I came down with my annual winter cold. A trip to the drug store and $50 later, I walked out with my annual supply of cold remedies. I dutifully took them, coughed and hacked for 2 weeks and eventually got better. Did the medications do any good? Doctors tell us over and over that there is no cure for the common cold and yet we continue to spend billions of dollars on cold remedies. Doctors will say, "Let the cold run its course. You will eventually get better." And yet, despite hearing and knowing this, we continue to buy these products driven by desperation or for the psychological effect. Read on to see what this means to you.

INTEREST RATES –

You would have to be living under a rock to miss the dramatic drop in short-term interest rates by the Fed. *The predictions are that the Fed most certainly is not done yet and if the economy doesn't improve, will drop rates further.* It's not imaginable that we could soon be at a zero percent Fed discount rate. This is very reminiscent of Japan 12 years ago. For a 10-year period, Japan had a zero interest rate. And yet with that rate, their economy stagnated in one of the country's longest modern day recessions. Like Japan, *I don't think interest rate reduction alone is a strong enough fix for our current economic predicament.*

There is much debate on both sides of the issue as to whether these decreases will have a positive result. Just how much can the Fed really impact our economy? I am not so sure that these interest rate cuts are much more than my trip to the drug store. For the past 120 years, this country has gone through a recession every 7 years, give or take a month or two. Just like I can predict my annual winter cold, most economists can predict a recession. So the prudent central banker should accept the recession and plan around it. Instead, our central bankers have created a panicked and politically driven trip to the drug store, overspent on worthless remedies and in fact, they have weakened our immune systems.

What do I mean by all of this? Well*, the decreased Fed funds rates have very little impact on the economy.* Remember, these are short-term rates. The vast majority of borrowing in this country is long-term. Long-term rates already were at historic lows and have dropped very little as a result of the past Fed actions. In fact, long-term corporate borrowing rates recently began increasing at the same time that short-term rates are falling. So, *very little credit stimulus actually will result from these decreases.* Yes, there will be a short-term psychological impact. And that impact MAY be enough to generate a short-term resurgence in home buying. However, what will be the ultimate cost?

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Immediately we are seeing a continued fall of the dollar resulting in cost increases from building products to gas at the pumps. Inflation will soon hit even harder at the grocery stores. We import far more than we export so it will not be long before we see price increases across the board and we will find ourselves in the inflationary spiral. *We do live in a global economy and what will inflation, a weak dollar, and poor credit ultimately do to our economy?*

Most of us are in this business for the long haul. I hate to see short-term remedies that cost us our future. Stay tuned for more. I don't think we have seen all of the impact of Bernake's Fed policy.

WHERE DOES ALL OF THIS LEAVE HOUSING –

You may remember that in our last issue we said that housing would not recover until it was no longer headlined in the papers or on the news. We also said that the increasing bitter political campaign just might do that. However, what we didn't count on was that the politicians were going to make housing an issue. So, even though the presidential candidates are filling the papers with their ridiculous antics, they are talking about the economy and housing enough that it is still prominent news. And *as long as people believe we have not hit the bottom or as long as they fear the economy, they will stay on the sidelines and will not be buying housing*.

With that said however, *we still see the gradual increases that we predicted at the beginning of the year.* We still believe that we will be about 12% over 2007. Granted, much of that increase will be happening in the last quarter because much of the building and unfilled demand will release once the political questions have been answered. *2008 will be a better year than 2007.*

WHAT IS THE LIKELY LONG-TERM SCENARIO –

It seems that we are finally getting some economic consensus and it is not particularly good news. *We may or may not be in a recession right now, however, even if we are, it will be of short duration and very mild*. However, as with my annual winter cold, the remedies may have mitigated the symptoms somewhat, but the cold is still there. *This economy is due a recession*. We may have delayed it somewhat, but eventually we will not disguise it through medication (aka: The Fed). *Therefore the prognosis is that we will recover from this mini-recession by the end of the year. We will feel pretty good for about 6 – 9 months and then will be hammered with a relapse sometime in late 2009.*

So we can expect a rebound in housing, as predicted, towards the end of 2008. But it will be of relatively short duration and will again hit the skids about a year later. How bad will the next downturn be? It looks like it will not be as bad for housing as the overall economy because we will still be catching up from some of the unfulfilled demand. It also looks like it will probably last only about 5 quarters and should be over by the beginning of 2011. *Beyond that, we should be in excellent shape for another 7-year cycle* assuming we control the worldwide effects of our present actions.

IS ANY OF THIS GOOD NEWS?

There is not doubt that there is a continual lack of good news. This endless downturn coupled with poor operating results has put us all in a funk. However, there is a silver lining to this downturn. Over the years, most of you have built your businesses by servicing the local homebuilder. He appreciated the service you gave him, didn't bust your chops on every penny, and was loyal as could be. Let me ask you? Does that sound like the national builder? Of course not. Well, *as is true in any downturn, we have a cleansing effect taking place*. Your weak competition is going out of business, the national homebuilders are retrenching, going out of business or leaving the area and the big box boys are focusing elsewhere and are beginning to stay out of our business.

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Believe me, when this recovery takes place, *we will all strategically be in a better place than we were a few years ago.*

ACCOUNTS RECEIVABLE –

One of the key indicators that we measure on a monthly basis is the average day's sales in accounts receivable. To calculate this number, we take our average daily sales for the last 2 months and divide that into our accounts receivable balance. Over the past 6 months we have seen that number increase by about 12 days. That means that our average account is paying us 12 days slower. What is the impact of this?

At any one time, we have several million dollars of accounts receivable. That 12 day slowdown on collections is costing us about $600,000 of working capital. That is $600,000 that we have to borrow just to cover this payment slowdown. That is a substantial cost to our business that we didn't have a couple of years ago.

We are talking with more and more of our customers who are also experiencing an increase in slow pays. This is critical to the health of your business. Not only do you incur working capital shortages, you also increase the likelihood of eventual bad debts.

We know that all of you do watch your collections because you can't be in this business without realizing the high cost of a write-off. But *what many miss is the high cost in working capital of a receivable list just slipping a few days.*

NEW PRODUCTS –

The lifeblood of our business, especially over the past couple of years, has been the addition of new products. These *new products have allowed us to capture market share, help our customers with additional profit opportunities, and keep our sales skills sharp.* How many new products have you added? Do your customers see the same ole same ole, day in and day out. Freshen your shelves and racks. Bring in some new stuff to generate some excitement. You will help your customers and you will give your sales staff something exciting to talk about.

Speaking of new products – *we continue to have great success with our PVC decking product*, Veka Deck. The closed cellular PVC formula gives it all of the advantages that the "filler" type composite products don't have. Additionally, *we have made some great inroads with the ArmorCast detectable warning panels.* It seems that people are finally becoming aware of the need of this product and ArmorCast is clearly the industry leader. If you haven't had a chance to see either of these products, ask your salesperson or call the office and ask for Kyle, our product specialist.

Our latest new product is called Jiffy Clip. Tying rebar has been referred to as spending all day reaching over and tying your shoes. *Rebar tying is labor intensive and causes considerable workman's comp claims.* Jiffy Clip is a labor saving system that secures the rebar. It comes complete with an installation tool and the clips. Any contractor concerned with labor cost should use this system. Not only will it save him considerable time tying bar, but it will also reduce his insurance claims and improve the morale of his workforce. We have samples of this new product and your salesperson will be presenting the benefits to you. Keep your eyes peeled.

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