Market Measure

THE INDUSTRY'S ANNUAL REPORT

Years from now, when our children and grandchildren are studying history, there will almost certainly be a chapter in their virtual textbooks that focuses on 2020. One might easily argue that 2020 will be remembered among the most influential years of the past two decades.

In this space, there is no need to revisit the myriad reasons 2020 has earned this dubious distinction. However, it is hard to separate the historical aspects of 2020 from the impact these events have had on the home improvement industry.

Before we dive into our industry analysis, we want to drive home a simple point that bears repeating. It always seems a bit callous to focus on the business aspect of the past 11 months without at least recognizing the real, brutal toll that comes along with the financial impact.

While the pandemic has brought a windfall in spending on home improvement, it has come at a cost that no one would want to diminish. We must at least acknowledge that, while it has been a record-setting growth year for home improvement, much of it has been fueled by the ripples from COVID-19, the subsequent lockdowns and the related lack of competition for disposable income.

It should also be noted that the sales increases experienced by home improvement retailers have been hard-fought during this period. Owners, managers and front-line employees, all considered essential to the economy, have worked long hours in indescribably difficult conditions to keep home improvement goods and services flowing to their communities.

While history books might not record the details of how home improvement retailers were impacted during this time, and how their employees and teams rose to the occasion, it is certainly worth noting here.

What We'll Cover

The information in this Market Measure report was gathered by Hardware Retailing *staff from a variety of resources that are attributed throughout the feature.*

Unprecedented

There is really no other word to represent what the home improvement retailing industry has seen during 2020 other than unprecedented. The growth the industry has experienced during this extremely short window is truly unlike anything we have seen in recent decades.

The year started out its first quarter posting modest gains over 2019. In early to mid March it looked like we were on pace to hit the 4.5 percent growth that we had predicted in this same space last year.

By the end of the second quarter however, it was a completely different story. Following the onset of the pandemic, subsequent lockdowns and the declaration that home improvement stores were essential to the economy, sales exploded.

Sure, there were huge increases in home improvement spending during the 1990s as the housing market roared into uncharted territory. This growth was more gradual and occurred over a period of years.

Throughout this more recent sudden increase in sales, NHPA kept in touch with retailers from across North America. Early on, the general sentiment was that we would see a three- or four-month increase in sales, a plateau and then a normalization around the end of Q3 and into the balance of the year.

As we go to press, the rocket ship has not lost any fuel and sales momentum continue to soar. In fact, sales were increasing at such a pace that actually keeping tabs on how fast they were increasing became difficult.

That being said, NHPA is estimating that overall sales for the industry in 2020 will increase by about 12.4 percent over 2019, bringing total sales in the industry to an estimated $457 billion.

Just tracking the U.S. Census Bureau reporting of sales in the NAICS 444- (home improvement retail) category (non-seasonally adjusted) puts the estimate just slightly lower at about 12.5 percent year over year.

Our friends at the Home Improvement Research Institute (HIRI) and IHS Global, as of the end of Q2, were predicting a more modest increase for the industry of about 8.7 percent (11 percent consumer and 3.5 percent pro). We understand that this is a relatively wide range of predictions, but there are several reasons for that.

The main factor driving these disparities is uncertainty in future performance. Most predictive analysis relies on lagging sales data to make future predictions. So far this year, we have all anticipated (and not yet seen) a drop-off from record performance, which somewhat skews typical predictive models.

When we are seeing large home improvement retailers such as Lowe's post sales increases of 35 percent in one quarter, there is a wider margin for interpretation. (As of this writing, we did not have Q3 results from major industry retailers.) Secondly, the housing market and professional product sales also factor into the overall industry, and the housing market hasn't exactly performed as predicted this year.

Then, when you figure in other non-industry related events (the election, potential stimulus, a resurgence of the virus) and it may at least be a bit more understandable why this year's predictions are a bit more "diverse."

Moving Forward

Ever since home improvement sales started surging at the end of the first quarter, the industry has been asking, "How long will this last?"

That question still persists. There are also less tangible factors that could impact home improvement sales in 2021, such as whether additional stimulus is offered or whether a vaccine opens up additional options for homeowners to spend their money on.

Lastly, and possibly most importantly, is that there will come a time when homeowners have worked through their project lists and we see at least a temporary fatigue in home repair and remodeling.

Considering all these factors, NHPA is predicting a slight decline in home improvement retail sales in 2021. We are anticipating a decline in industry sales of approximately -0.7 percent against 2020. We anticipate that Q1 should continue to see increases that will likely flatten out in Q2, and that while Q3 and Q4 will be robust when compared against 2019 or other average years, sales will dampen when compared to 2020 performance.

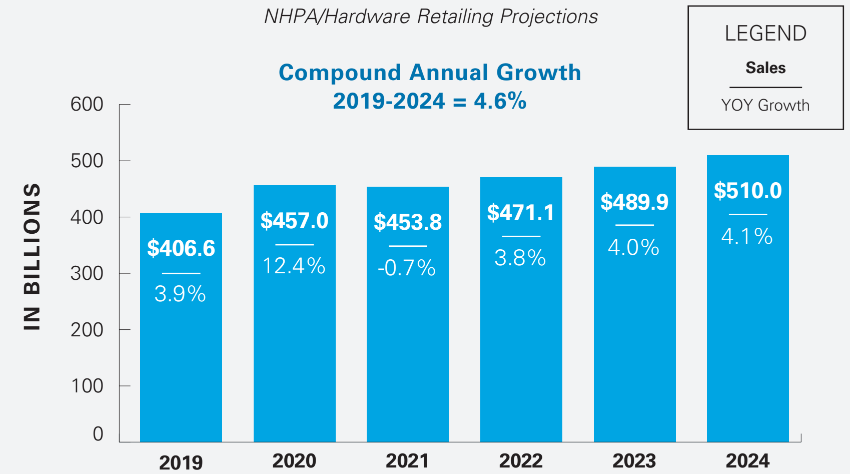
The team at the HIRI/IHS Markit is predicting sales to slow by about -0.1 percent on the consumer side in 2021 but for that to be buoyed by more robust spending from professionals (5.3 percent) translating to a 1.5 percent increase for the industry overall next year.

At NHPA, we also feel that consumer spending will soften before professional projects early in 2021, but a potential bright spot for home improvement overall could be if interest rates remain low going into the spring and summer months.

Beyond that, both NHPA and HIRI/IHS see the industry returning to more consistent levels of growth. Through 2024, NHPA is predicting the industry to grow at a compound annual rate of approximately 3.9 percent, while HIRI/IHS has pegged that figure at 3.7 percent (at current prices).

U.S. Home Improvement Sales

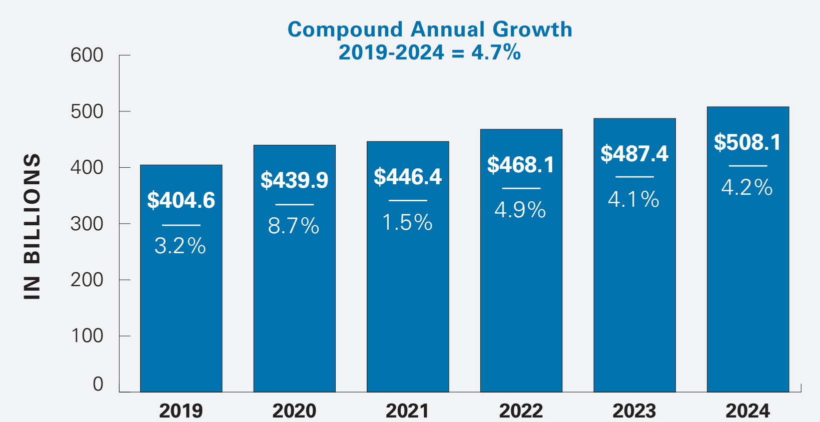
NHPA/Hardware Retailing Projections



Source: NHPA/Hardware Retailing

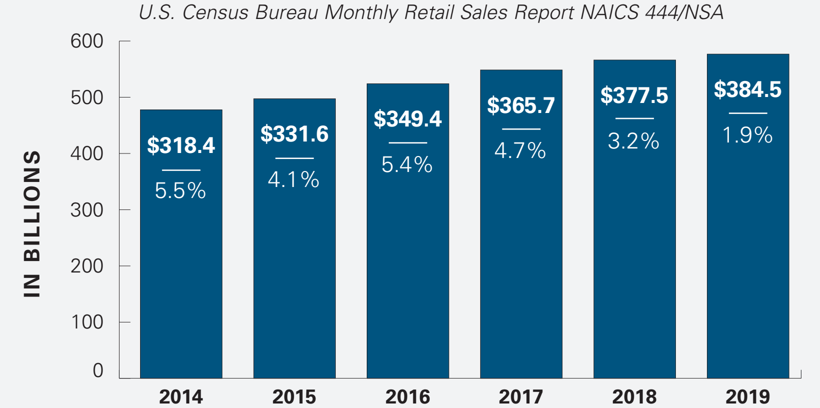
Home Improvement Product Sales Performance

Home Improvement Research Institute/IHS Projections at Current Prices



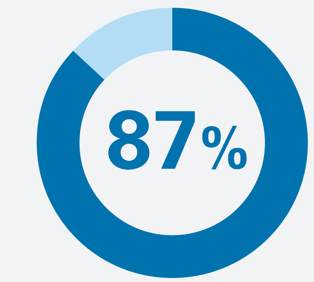
Home Improvement Retail Sales

U.S. Census Bureau Monthly Retail Sales Report NAICS 444/NSA



Sales in 2020

NHPA surveyed retailers about their sales early in the pandemic



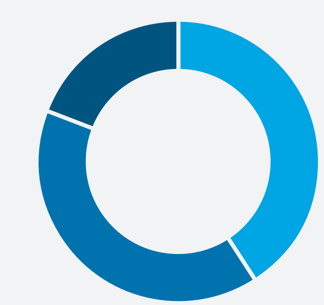
of surveyed independent retailers reported year-over-year same-store sales growth

19.4%

Average sales increases across all independent retailers in 2020

Budgeting for 2021

Most retailers are expecting sales to be down or flat in 2021



- **41.3%** Down from 2021
- **39.7%** Flat from 2021
- **19.0%** Up from 2021

Source: NHPA 2021 Retailer Budget Survey

2020

Home Improvement Sales by Month
(in billions)

January	$27.9
February	$27.2
March	$33.1
April	$36.8
May	$43.3
June	$43.2
July	$40.5
August (p)	$37.8
YTD	$328.0

Source: U.S. Department of Census/ Monthly Retail Sales Report NAICS 444/NSA

Sales Growth 2019 vs. 2020

January	1.1%
February	9.1%
March	7.1%
April	4.7%
May	12.8%
June	24.8%
July	16.6%
August (p)	13.0%
YTD	12.5%

Source: U.S. Department of Census/ Monthly Retail Sales Report NAICS 444/NSA (p) = preliminary estimate

2019-2024

Sales by Store Type
(in billions)

2019	Hardware Stores	$51.6
	Home Centers	$253.3
	Lumberyards	$101.7
	TOTAL	$406.6
2020	Hardware Stores	$61.8
	Home Centers	$297.9
	Lumberyards	$97.3
	TOTAL	$457.0
2021	Hardware Stores	$58.9
	Home Centers	$288.6
	Lumberyards	$106.3
	TOTAL	$453.8
2022	Hardware Stores	$60.3
	Home Centers	$294.8
	Lumberyards	$115.9
	TOTAL	$471.0
2023	Hardware Stores	$63.2
	Home Centers	$304.2
	Lumberyards	$122.5
	TOTAL	$489.9
2024	Hardware Stores	$64.8
	Home Centers	$317.2
	Lumberyards	$128.0
	TOTAL	$510.0
Compound Annual Growth Rate 2019-2024	Hardware Stores	4.7%
	Home Centers	4.6%
	Lumberyards	4.7%
	TOTAL	4.6%

Source: NHPA/Hardware Retailing

2019-2024

Outlets

2019	Hardware Stores	19,100
	Home Centers	9,730
	Lumberyards	9,650
	TOTAL	38,480
2020	Hardware Stores	19,100
	Home Centers	9,725
	Lumberyards	9,640
	TOTAL	38,465
2021	Hardware Stores	19,085
	Home Centers	9,720
	Lumberyards	9,630
	TOTAL	38,435
2022	Hardware Stores	19,065
	Home Centers	9,715
	Lumberyards	9,615
	TOTAL	38,395
2023	Hardware Stores	19,020
	Home Centers	9,690
	Lumberyards	9,575
	TOTAL	38,285
2024	Hardware Stores	18,800
	Home Centers	9,645
	Lumberyards	9,535
	TOTAL	37,980
Percent Change 2019-2024	Hardware Stores	-1.6%
	Home Centers	-0.9%
	Lumberyards	-1.2%
	TOTAL	-1.3%

Source: NHPA/Hardware Retailing

Top Chains: Individual Performance

	2019 Sales (in billions)	Stores at End of 2019	Stores in 2020 (as of Nov. 1, 2020)
Home Depot Atlanta	$110.2	2,291	2,293‡
Lowe's Mooresville, North Carolina	$72.1	1,977	1,968‡
Menards Inc. Eau Claire, Wisconsin	$10.0*	325	335
Tractor Supply Brentwood, Tennessee	$8.4	1,814	1,904
84 Lumber Eighty Four, Pennsylvania	$3.8	250	252
Northern Tool + Equipment Burnsville, Minnesota	$1.6	114	119
Carter Lumber Kent, Ohio	$1.5	160	163
Sutherland Lumber Kansas City, Missouri	$0.9†	52	49

Sources: Company reports and Hardware Retailing *surveys*
The above represent home improvement retail chain stores that carry at least two core categories and have sales of approximately $1 billion or more.
‡Store counts include operations in the U.S., Canada, Mexico and all other locations.
**Source: Forbes, as of Dec. 17, 2019*
†Source: Hardware Retailing *estimates*

Market Share Profile

Top Chains: Industry Share			Top Chains: Combined Performance		
	Sales (as % of total industry)	No. of Stores (as % of total industry)		Net Sales (in billions)	No. of Stores
2015	49.7%	16.4%	2015	$154.8	5,885
2016	51.3%	17.4%	2016	$159.4	6,308
2017	51.9%	17.7%	2017	$168.6	6,447
2018	52.5%	18.0%	2018	$183.6	6,846
2019	51.3%	15.4%	2019	$208.5	6,983
2015-2019 Percentage Point Change	1.6%	-1.0%	2015-2019 Compound Annual Growth Rate	7.7%	4.4%

A Real-World Look at Retailers' Financials

The *2020 Cost of Doing Business Study* presents the North American Hardware and Paint Association's (NHPA) annual financial and operational profile of independent hardware stores, home centers, lumber and building materials (LBM) outlets and paint and decorating outlets. The study is the industry's only financial benchmarking tool and allows retailers to compare their operations to typical and high-profit independent home improvement businesses.

The study assesses the financial performance of home improvement retailers for fiscal year 2019. It presents composite income statements and balance sheets plus averages for key financial performance ratios. The data is segmented for hardware stores, home centers, LBM outlets and paint and decorating outlets. In this year's study, 1,051 independent home improvement stores participated, a 5.9 percent decrease over the prior year.

Methodology

The annual *Cost of Doing Business Study* is made possible through the cooperation of owners and managers of independent home improvement operations who provide detailed financial and operational information on their individual companies. Questionnaires were mailed to a sampling of outlets in the U.S. to collect detailed financial and operational information for 2019. Individual company responses are confidential.

NHPA then completes an analysis of the aggregate numbers in the final report after extensively reviewing retailers' financial data. Most figures in this report are medians, meaning 50 percent of businesses fall below that number and 50 percent are above it. The median represents a typical company's financial results, without extreme figures skewing the data.

To identify high-profit operations, NHPA ranks all participating companies in their category based on net profit before taxes. The high-profit companies are in the top 25 percent of their store type.

How to Use This Study

To get the most out of these selected results from the *2020 Cost of Doing Business Study*, follow these tips.

- **Compare numbers.** Determine your operating expenses as a percentage of sales and calculate your balance sheet as a percentage of total assets. Compare those numbers to the study results for typical and high-profit stores.
- **Look beyond the percentages.** Compare your real-dollar expenditures as well.
- **Consider the results.** If you find your store's individual data veers sharply from what's contained within the study, explore the cause behind the discrepancy and develop a plan to bring your numbers on par with high-profit stores.
- **Participation counts.** Overall figures can vary from year to year based on the group of participating operations. Year-to-year comparisons are helpful for illustrating general trends over time.

Figures to Know

- **Average transaction size** is the total sales over a period of time divided by the total number of transactions in that same period.

  Use It: *Measure your average transaction size weekly to spot shopping trends and establish a baseline for your business.*

- **Payroll** is the total cost of owner and employee salaries, insurance payments and benefit plans.

  Use It: *Compare your payroll expenses to typical and high-profit operations to find areas you could cut.*

	Hardware Stores	Home Centers	Lumberyards
Profit Margin	**4.0%** Profit before taxes in 2019 was 4.0% for typical hardware stores, the third-highest net profit level since 2016.	**2.1%** Profit margins at home centers for 2019 were the lowest they have been since 2016, falling 0.6 points over that year.	**2.5%** Typical lumberyards saw a 0.5 percentage point drop in profit margins from 2018, resulting in the lowest metric in the last five years.
Total Operating Expense	**38.9%** Total operating expense was up just over 2 points from 2018, which was the lowest in the last five years of data collection.	**32.4%** Total operating expenses at home centers have stayed steady over the last five years, up only 0.2 points from 2018.	**23.8%** Total operating expenses decreased 1.3 percentage points from 2018, and this year's metric is the median over the last five years.
Sales Per Square Foot	**$189** This metric was down almost 14% from 2018, but that year was the peak over the last five years at $219.	**$203** Sales per square foot fell over 35% from 2018, but total square footage was up more than 30%, which likely accounted for the shift.	**$1,702** This metric represents the highest sales per square foot for lumberyards over the last five years of data collection.
Gross Margin Per Employee	**$67,596** Gross margin per employee was down just over 3% from 2018 and is the lowest its been over the last five years.	**$71,788** This metric increased 3.7% over 2018. The average number of employees dropped by four in 2019.	**$91,866** Despite sales per square feet growing significantly, gross margin per employee last year fell by 32% over 2018.

Overall 2019 Business Performance

The following data from the *2020 Cost of Doing Business Study* is divided into three sections so retailers can compare their businesses' performance with home improvement operations similar to their own. NHPA divides the numbers by three types of retail outlets—hardware stores, home centers and lumberyards. The complete study, which also includes a paint store segment, is available for purchase at **YourNHPA.org/codb**.

Hardware Stores

Hardware stores saw numerous shifts in 2019. The data shows comparable stores saw sales increase by 4.1 percent in 2019 over 2018 figures, but customer count dropped 2.3 percent and sales per customer fell 0.6 percent. It's important to note that the same stores that reported increased sales for 2018 and 2019 only constitute a fragment of the study's overall respondents.

At high-profit hardware stores, sales were about $263,000 higher than at typical stores. High-profit stores reported higher customer counts, but their sales per customer were about 75 basis points lower than typical hardware stores. This difference suggests high-profit stores made up ground with their sheer volume of transactions.

While typical stores posted profits before taxes of 4.0 percent, high-profit stores saw this figure dip slightly in 2019 to reach 8.5 percent. Typical stores' gross margin after rebate hit 42.1 percent, the highest figure since 2016, while high-profit stores saw gross margin after rebate hit 43.6 percent.

Payroll as a percentage of sales hit one of its highest levels ever, coming in at 22.5 percent. High-profit stores managed to control payroll slightly better than the average operator; their rate was just 20.3 percent of total sales.

Home Centers

In 2019, the differences between typical home centers and high performers were stark. High-profit home centers saw more than 12,000 extra customers in 2019. Sales per customer were $69 and just $37 at typical home centers.

For high-profit stores, profit before taxes was 5.6 percent compared to 2.1 percent at typical home centers. The reason for this disparity can be seen when reviewing other factors like sales per square foot, where high-profit stores hit $433, up sharply from typical stores, which measured $203 in sales per square foot. In addition, gross margin per square foot at high-profit stores averaged $136, while typical home centers saw $68 for this metric, the lowest level recorded since 2013.

High-profit home centers did a better job at inventory management in 2019, achieving an inventory turnover rate of 3.3x versus 2.7x for typical home centers, which was the lowest level recorded since 2015.

Lumberyards

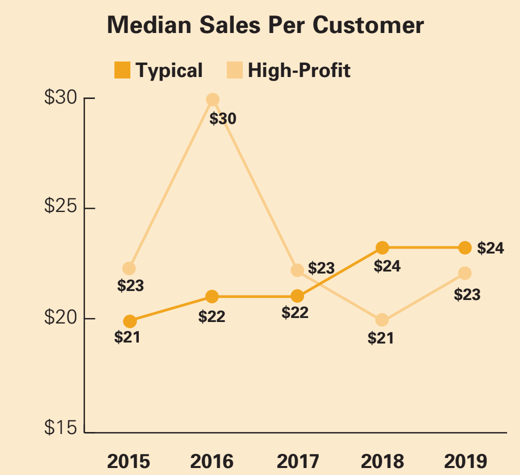
LBM outlets saw strong sales in 2018, so while sales fell slightly in 2019 for typical stores, average sales per location of $8.3 million represent the second-highest figure ever recorded in the study.

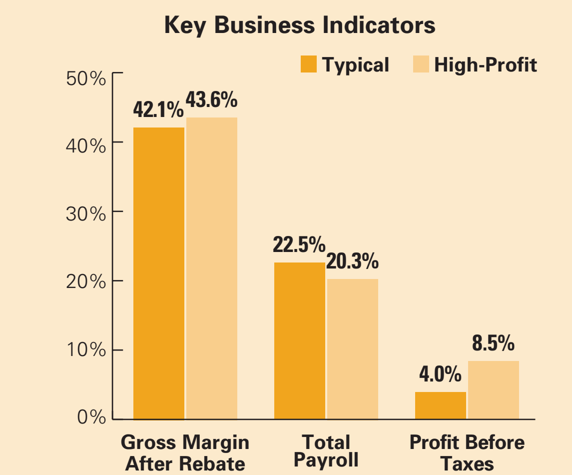
LBM outlets were not immune from an industrywide trend of declining customer counts, with typical stores reporting 26,517 customers in 2019, the lowest in a decade. High-profit LBM outlets were able to drive more traffic through their doors, recording 40,419 average visits. High-profit stores also achieved better deals than typical LBM outlets, reporting the cost of goods sold around 70 percent as opposed to 74 percent at typical operations. Similarly, gross margin after rebate for high-profit LBM outlets registered at 30.4 percent in 2019, compared to just 26.7 percent at typical stores in 2019.

It's important to note typical LBM outlets did a good job of controlling labor costs in 2019. Respondents saw total payroll drop by 160 basis points in 2019 to 14.6 percent of overall sales.

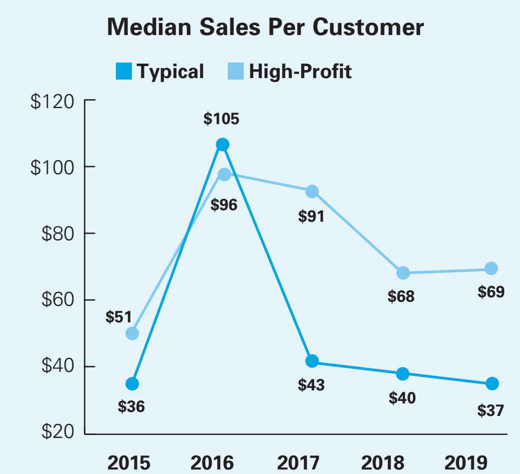
The typical LBM outlet recorded profits before taxes of 2.5 percent, while high-profit counterparts more than doubled this performance, posting an average of 6.0 percent.

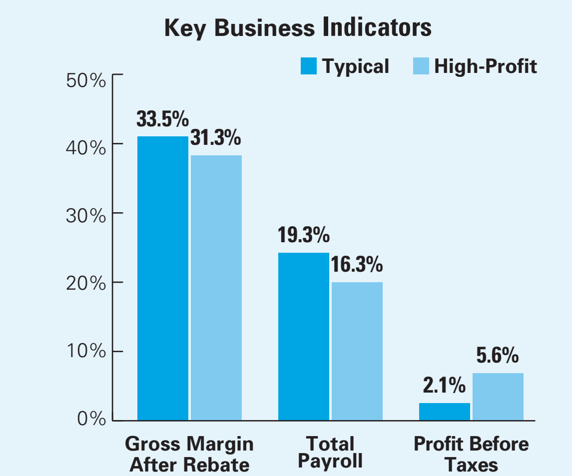
Hardware Stores



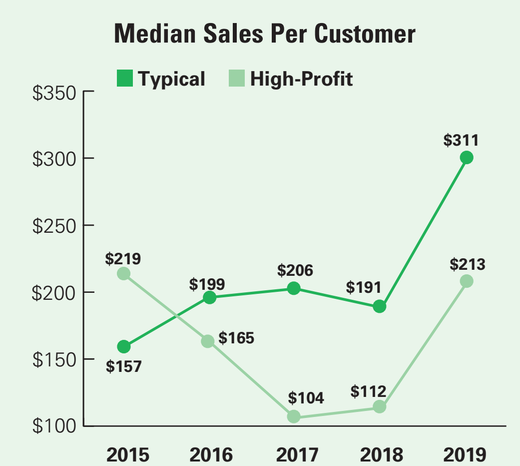


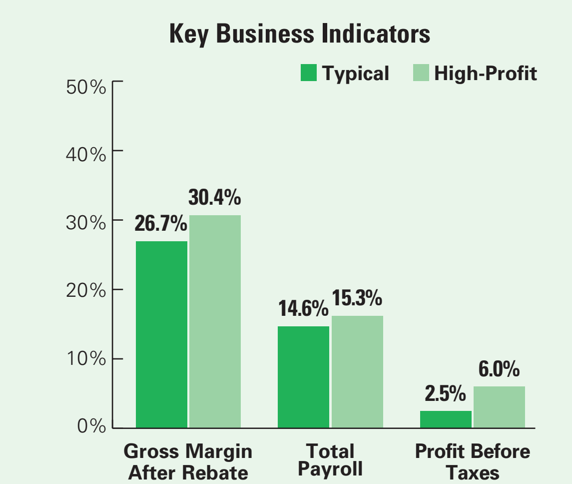
Home Centers





Lumberyards





Financial Profiles of Leading Publicly Held DIY Chains 2019

Operating and Productivity Profile	Home Depot	Lowe's Cos.
Number of Stores (at end of 2019)	2,291*	1,977*
Average Size of Selling Area (sq. ft.)	104,000	105,000
Total Sales	$110.2 billion	$72.1 billion
Total Asset Investment	$51.2 billion	$39.5 billion
Total Inventory	$14.5 billion	$13.2 billion
Sales Per Square Foot	$454.82	$346
Inventory Turnover	4.9x	3.7x
Net Sales to Inventory	7.6x	5.5x
Total Sales Per Employee	$329,743†	$225,313
Average Size of Transaction	$67.30	$78.36
Gross Margin Return on Inventory	258.6%	174.1%
Income Statement	Home Depot	Lowe's Cos.
Net Sales	100.0%	100.0%
Cost of Goods Sold	65.9%	68.2%
Gross Margin	34.1%	31.8%
Total Operating Expenses	19.7%	27.7%
Net Income (Before Taxes)	13.3%	7.8%
Balance Sheet	Home Depot	Lowe's Cos.
Total Current Assets	38.7%	38.8%
Cash	4.2%	1.8%
Receivables	4.1%	0.4%
Inventory	28.4%	33.4%
Other	2.0%	3.2%
Fixed Assets	61.3%	61.2%
Total Assets	100.0%	100.0%
Current Liabilities	35.9%	38.5%
Long-Term Liabilities	70.2%	56.5%
Net Worth	-6.1%	5.0%
Total Liabilities and Net Worth	100.0%	100.0%

Source: Home Depot and Lowe's annual reports
**Figure represents companies' total store count in the U.S. and other countries.*
†Hardware Retailing Estimates

Profile of Top 4 Distributors

	Ace Hardware Corp.	Do it Best Corp.*	Orgill Inc.	True Value Co.‡
Number of Distribution Centers	17	8	7	13
Current Number of Members	≈2,700	3,800	11,000 stores	N/A
Dollar Volume Most Recent Fiscal Year	$6.1 billion	$3.6 billion	$2.5 billion	N/A
% Sales Out of Warehouse	80.0%	34.0%	N/A	N/A
% Sales Out of Pool/Relay	0.0%	0.0%	N/A	N/A
% Sales Direct-Drop Ship	20.0%	66.0%	N/A	N/A
% Sales in LBM	0.0%	21.0%	N/A	N/A
Number of Employees	10,500	1,600	N/A	2,300
Avg. Number of SKUs in Warehouse	>80,000	67,000	N/A	80,000
Sales/Inventory Ratio for 2019	6.5	12.6	N/A	N/A
2019 Member Rebate Distributed	$182 million	$128 million	N/A	N/A
% Cash	39.0%	69.0%	N/A	N/A
% Stock	32.0%	31.0%	N/A	N/A
% Other	29.0%	0.0%	N/A	N/A

Sources: NHPA distributor surveys
**FY 2020 data; ended on June 27, 2020;*
‡True Value transitioned away from the co-op model in 2018 after it sold 70 percent of its ownership to a private investment firm. The company no longer shares certain data points.

Profile of Wholesaling Merchandising Groups

	PRO Group Inc.	Distribution America	Val-Test Group
Current Number of Wholesale Members	73	7	51
Number of Member-Operated Distribution Centers	150+	8	51
Dollar Volume for 2019 Fiscal Year	$6 billion	$1 billion	$650 million
Estimated Dollar Volume Calendar 2020	$6 billion	$1 billion	$650 million
Number of Retail Stores Served by Members	35,000	9,000	1,400
Number of Program Stores	800	N/A	90
Number of Employees	16	8	4

Sources: NHPA distributor surveys

What Housing Holds

A Q&A WITH ABBE WILL ABOUT THE HOUSING MARKET

Abbe Will is a research associate and associate project director of the Remodeling Futures Program for the Joint Center for Housing Studies of Harvard University. *Hardware Retailing* spoke to Will about what challenges and opportunities the housing market brought this year and what that could mean going into 2021.

***Hardware Retailing (HR)*: What kinds of shifts were there in the housing market this year because of the pandemic? How significant of an effect did the pandemic have?**

Abbe Will (AW): It's really been a roller coaster. Back in March and April, when the economy shut down, the market took a hit, and sales were down at a phenomenal rate. Housing starts were also down significantly at that point.

Then we saw a huge reversal in late spring and into the summer. I think part of that was households spending so much time at home in the spring and really not having a lot of other typical distractions. Because vacations and school events weren't happening, people were spending that time at home, focusing on what was and wasn't working for them in their homes. Especially given that people have been working from home, schooling from home, etc. They were figuring out how to live and do everything in one space.

And part of that, too, was not just doing what they wanted to improve in their current home, but thinking about whether they wanted to stay at all or whether moving was a better option. People who were already thinking about moving in the coming year, the pandemic increased that urgency to make that happen sooner rather than later.

Since then, home sales have rocketed back, and housing starts have rebounded, too. Homeowners are focused on home in a different way than they have been in a long time. The pandemic brought forward sales and remodeling activity that may have been happening anyway in the coming quarters or year, but we think this elevated level of activity will sustain.

HR: Where were people moving and what are the demographics of those populations?

AW: There is possibly a quickening of the trend of younger households moving from urban into more suburban locations because they wanted or needed to get out of denser urban areas at the onset of the pandemic.

Part of it is the millennial generation, as they have aged into their early to mid 30s, that's a prime homebuying age group. If they had been living in urban areas, starting families, that's been a typical trajectory for all generations. Once you're marrying and starting a family, you're typically looking for more room and going more suburban. But ultimately, when you talk about the urban to suburban migration, it is a small scale compared to all households that are moving.

We think there has also been a larger share of younger adults who, early in the pandemic, when their universities shut down or they lost their jobs, did the calculus of whether it would be safer to go home, where their parents or families are.

> Remodeling and housing are a brighter spot in the broader economy that could be helping to **lead the economy through recovery**.

HR: How much did the pandemic impact previous projections?

AW: We produce a quarterly short-term indicator of homeowner spending on home improvements and repairs, our Leading Indicator of Remodeling Activity (LIRA).

Last year, we were projecting slowing growth for the remodeling industry, but growth nonetheless. After several years of what we would call strong year-over-year growth—6 to 7 percent growth—we were projecting growth to return to a more sustainable pace around 5 percent annually. Last year's softness in new construction and existing home sales being the drivers in that expected spending slowdown.

This year has proven to be difficult time for projecting, even short term. In April, we were projecting a modest decline in spending for 2020, less than 0.5 percent.

Back in March and April, we were thinking the floor was really falling out from under us, that remodeling was going to take a severe hit. But then we started seeing change in demand and the level of retail spending at building materials outlets. That adjusted our projections for the most recent LIRA release for remodeling activity.

Now we have the market growing, not gangbusters, although we are projecting growth to increase over the coming two quarters. In our most recent projection from October, we project the home improvement and repair market to grow by 4.1 percent annually through Q1 of 2021 and then to slow again, and we're projecting 1.7 percent annual growth in Q3 next year.

Even though these projected annual growth rates are below the long-run historical acrage, remodeling and housing are a brighter spot in the broader economy that could be helping to lead the economy through recovery.

HR: Are home sales related to trends and upticks in DIY renovations?

AW: Home sales are one of our key inputs into our LIRA that shows home sales correlate well with home improvement spending nationally, but with quite a bit of lead time. Our model shows sales correlate to spending about five quarters out, so home sales today will influence remodeling sales in about a year.

Based on historical data, a lot of remodeling tends to happen around the time of sale. If a homeowner wants to get top dollar in normal market conditions, they will consider what improvements they need to do to their homes. You can often get bang for your buck with curb appeal, exterior projects like landscaping and doors and windows.

Typically, recent homebuyers, people who purchased in the last three years spend about 30 percent more on renovations than owners who have been in their homes longer than three years. Controlling for income and age, recent buyers still bend toward more renovation.

As home sales are a consistent driver for remodeling activity, the strong growth we've seen in home sales this summer and fall would suggest a pretty good boost in remodeling activity in the coming year or more.

HR: How has the pandemic impacted home prices? Will that continue in 2021?

AW: We didn't see a big shift in home prices this year until recently with price appreciation strengthening. They had been growing steadily about 5 to 6 percent over the last few years. In March and April, we were wondering if price appreciation would be impacted. With the steadying of the housing market and remodeling, we didn't see a hit. In fact, I think it appreciated even more in the last quarter or so. Part of that ultimately is increased demand in households wanting to purchase and take advantage of historically low mortgage interest rates, but there being a lower supply of homes available for sales. A lot of markets continue, to see tight inventory, which was a trend even before the pandemic.

Small Businesses Remain Optimistic

A Q&A WITH HOLLY WADE ABOUT THE ECONOMY

Holly Wade is the executive director of the NFIB Research Center, where she conducts original research and studies public policy effects on small businesses. She produces NFIB's monthly Small Business Economic Trends survey and surveys on topics related to small business operations. Wade is also a member of the board of directors of the National Association for Business Economics. *Hardware Retailing* spoke to Wade about the state of the economy and what is ahead in 2021.

***Hardware Retailing* (HR): What impact has the pandemic had on the overall economy compared to the independent sector specifically?**

Holly Wade (HW): The small firms we represent were impacted dramatically at the onset of the health crisis. The second quarter was decimated by COVID-19 due to shutdowns, and consumer spending slowed dramatically. Since then, we have had a sizable third quarter, GDP wise. The economy has started building back up again, as businesses were able to resume operations.

However, it's diverged between those businesses that are able to operate more or less normally from where they were pre-pandemic and those businesses that are not. Either because of dramatic shifts in consumer spending or continued restrictions on activity. While there has certainly been a strong recovery, there are still many businesses that are continuing to struggle.

The Paycheck Protection Program that benefited most small employer businesses by providing financial assistance offered financial certainty through the first few months. Many businesses have largely recovered, but there is still a population of small businesses that continue and will continue to struggle until the crisis is resolved because they depend on more foot traffic of consumers coming into their stores, like bars or restaurants or travel and entertainment businesses.

HR: How does consumer confidence compare this year to other years?

HW: Consumer confidence plummeted in April, according to the University of Michigan consumer sentiment survey. Their measure was around 101 in February and plummeted to 71 in April. We're still a long way from pre-pandemic consumer sentiment.

Consumer confidence is still much lower than it was, but improving, and that's certainly a good sign. I don't know that we'll see major improvements until there is far more control over the health crisis. Small business sentiment and consumer sentiment were incredibly high over the last few years, right up until March. The health crisis was entirely responsible for the crash of both.

> Retailers should know that lead times and cycle times have lengthened, and that has to do with **ongoing capacity constraints and logistic challenges**.

We have a monthly survey of a random sampling of NFIB members, which measures small business optimism. It has been at record level highs over the last four years as the economy kept building and growing stronger, and then it crashed in March and April.

But the Paycheck Protection Program helped stabilize much of the small business sector, and the index started to improve. We are largely back to where we were before, but a lot of that is forward-looking sentiment. More small business owners are anticipating better conditions and more sales. They continue to remain optimistic of what things will look like going forward even as sales aren't where they want them to be.

The fundamentals of a strong economy are there, just waiting for a vaccine or better therapies to get the virus under control. Small business owners are certainly optimistic. In the same survey, we also constructed an uncertainty index, and the most recent was the second highest it's been in the survey's 46-year history. While they are optimistic, there is still a lot of anxiety. Many small business owners aren't able to determine whether things will get better or worse.

HR: Are there specific factors that contribute to that uncertainty in addition to the pandemic?

HW: The trend for online sales has increased year over year, and this year has just pushed that trend much further and faster than anticipated. Many businesses are having to adapt very quickly in creating an online presence to compete.

Many small businesses have had a limited online presence or didn't have one at all, and that has been one of the most important ways to find customers and allow customers to purchase and navigate products online.

Those are some adjustments that will be permanent going forward. Consumer spending shifts will probably moderate and readjust to where they were before, but the retail sector and how consumers shop is going to be notably different.

It is certainly a steep learning curve and very stressful to move up the timeline of adjusting to these trends more quickly than anticipated.

HR: What are some possible effects retailers may see regarding consumer spending if the pandemic continues as it is right now? Do you think this boost in home improvement spending is sustainable?

HW: Even those businesses that are seeing increased consumer demand, they're still having challenges in absorbing increased consumer spending in those areas.

Budgeting is a huge challenge, navigating what it looks like six to 12 months from now. Businesses that sell durable goods are looking at uncertainty in the near future because those are largely products you buy once every five to 10 years. So those operators are asking, "What does that look like as far as trying to navigate large fluctuations in sales?"

Because of the pandemic and the uncertainty of how it will be resolved, it's one of the biggest challenges small business operators have, trying to figure out what sales look like and how to budget for their business. We're still seeing low levels of capital spending. Business operators are still very hesitant about spending money, expanding their business or replacing equipment because of this enormous level of uncertainty going forward about how the pandemic will impact their business and shifts in consumer spending.

HR: The pandemic obviously upset so many projections economists were making at this time last year about what 2020 would hold. Are there any projections you can make about what the economic recovery will look like over the next six to 12 months? How will this period in history impact how economists make projections moving forward?

HW: This has put economic projections into a tailspin. In the best of times, forecasting is difficult. In the current situation, it's nearly impossible. There are so many variables coming up, the biggest one being weather related, how that impacts COVID-19 infection rates and decisions to further restrict business activities.

I think this health crisis is hopefully a one-off event where we can return to normal ways of looking at the economy, what will impact it going forward without so much uncertainty attached to it.

Canadian Retailers See Chaotic Rebound

PROVIDED BY MICHAEL MCLARNEY, PRESIDENT, HARDLINES INC., MANAGING DIRECTOR, NHPA CANADA

The Canadian retail hardware industry has weathered similar conditions to its southern neighbors through much of 2020. But before the pandemic, sales by the industry overall were facing negative growth at the end of 2019 for the first time since 2009. However, impacts varied from region to region and by store format.

Big-box retailers fared best during the uncertainty of 2019, growing in real terms and securing a larger portion of the entire market in Canada than ever before. Hardware stores showed great resilience, maintaining their role as an important part of the local communities they serve.

All these conditions set the stage for the industry's response to a world crisis in Q2. As people were forced to stay home, uncertainty was the overriding sentiment for retailers. Initial concerns about the health of the economy and the potential rise in unemployment gave way to a unique boom in home repairs and renovations. The result, much like in the rest of North America, was a huge surge in sales for retailers of all sizes.

While pandemic conditions certainly added to operational challenges, they did not diminish the overall buoyancy of the sector. The DIY boom started with paint and decorating projects, with retailers enjoying record increases—and vendors reporting empty warehouses. When people moved outdoors, they turned their sights and spending money to outdoor living products. People trying to adapt their homes to include office spaces, home schooling and recreation meant sales of everything from furniture and kitchenwares to swing sets and pools.

Retail Success Stories Abound

In Quebec, Canac now has 30 outlets, with more on the way. Its low-cost business model has been immensely popular with customers and the company is set to exceed $1 billion in sales. Canac has been supporting its tremendous growth—averaging a new store every year for the past five years—with investments in distribution for both hardware and building materials.

Peavey Industries, a chain of farm and ranch stores across Western Canada, has successfully absorbed its takeover of TSC Stores in Ontario, converting them all to the Peavey Mart banner. In addition, it took over the license in Canada for the Ace Hardware brand. About 90 stores in the country with the Ace banner will get their hardware supplied out of Peavey's distribution centres in Red Deer and in London, Ontario.

Home Hardware Stores Ltd., the country's largest co-op retail group, has more than 1,000 retailers. Over the past two years, Home Hardware has been undergoing considerable changes internally under President and CEO Kevin Macnab, the first company outsider to helm the company. The initiatives under his direction have been reshaping the company as a retail-oriented organization rather than one that considers itself a wholesaler. The ensuing changes have affected every part of the business, from store presentation at the retailer level to how products are bought by the merchandising teams.

Continued Retail Consolidation

Along with Home Depot Canada, Lowe's Canada, Home Hardware and Canadian Tire Retail comprise more than half of all sales by Canada's home improvement retailers.

Canadian Tire, a store format unique to Canada, sells hardware, sporting goods and automotive products. It is a key player in the retail home improvement industry, and with more than 500 stores coast to coast, it is a significant competitor for most traditional retailers. Canadian Tire has undergone a great deal of restructuring of its retail business and is focusing on acquisitions and brand expansion—especially of private labels. It is also focusing heavily on its online sales.

Surviving COVID-19

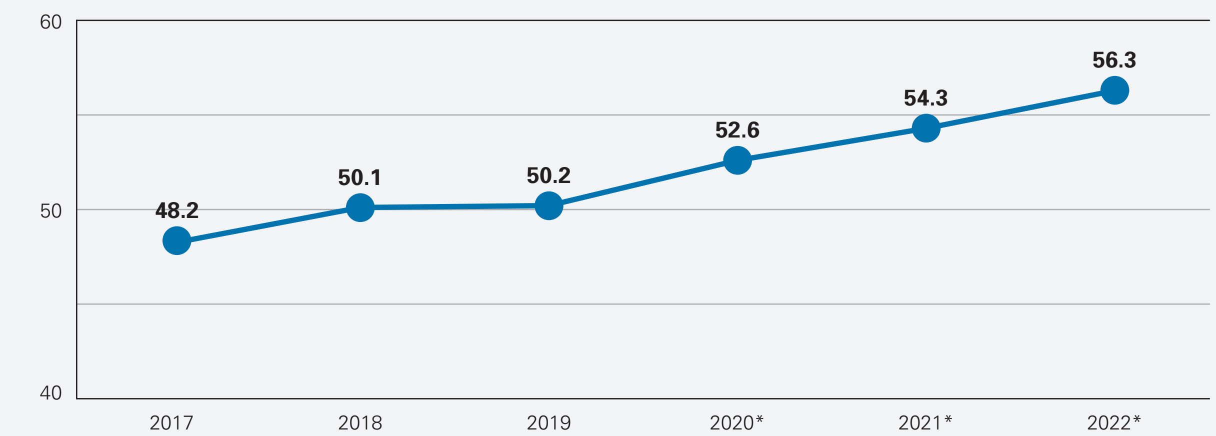
Big boxes have done exceptionally well in recent years, gaining a record amount of market share. But independents have managed to fare well during the pandemic. One reason for independents' successes during the pandemic has been their ability to pivot. As many provinces ordered retailers to move to curbside pickup, smaller local stores were often in the best position to execute that turnaround quickly.

On the other hand, forward-looking statements are a trickier proposition in the current climate. Retailers in every part of the country are concerned about just how long this boom can last. However, most retailers expected to come out of 2020 with positive sales gains, many of them in the double digits.

There are key trends to watch for guidance, such as an increased push by some major banners to woo pro customers, but plenty of uncertainty will continue before the Canadian market sees a new normal. In the meantime, a much-anticipated recovery is not expected to happen quickly, as retailers and vendors in Canada prepare for several more months of disruption. As a result, the industry is forecast to enjoy growth of 4 to 6 percent in 2020 and more moderate growth in the year ahead.

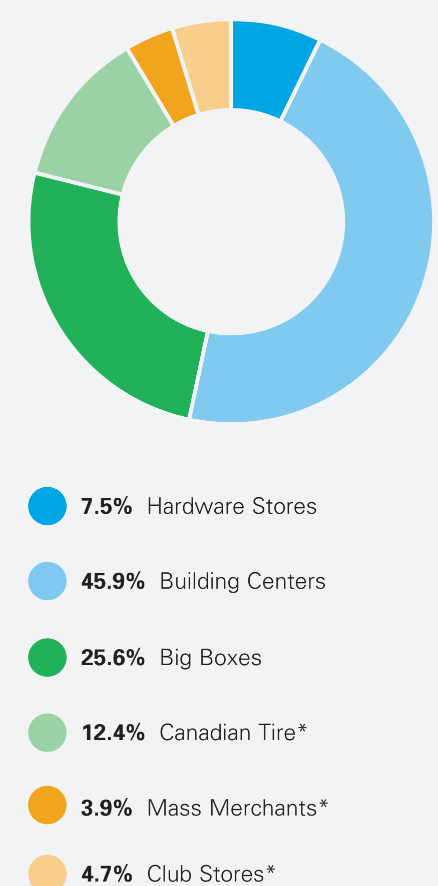
Home Improvement Industry Sales Growth

(IN $CD; IN BILLIONS)



*Forecasted numbers

Market Share by Store Format



*Related bulding materials sales only

Top 10 Home Improvement Retailers

Rank	Company	2018 Sales (in billions)	2019 Sales (in billions)	Percentage Change
1	Home Depot Canada	$8.5	$8.8	4.4%
2	Lowe's Canada	$7.4	$7.1	-4.3%
3	Home Hardware Stores	$6.6	$6.59	-0.8%
4	Canadian Tire Retail	$6.1	$6.2	2.3%
5	ILDC	$4.0	$4.1	1.7%
6	TIMBER MART	$3.2	$3.1	-4.6%
7	Sexton Group	$2.4	$2.2	-7.8%
8	Castle Building Centres	$2.2	$2.1	-5.0%
9	BMR Group	$1.3	$1.3	0.0%
10	Kent Building Materials	$0.93	$0.94	1.4%

Source: Hardlines 2020 Retail Report